

Background

An informal economy is an economic activity that is neither taxed nor monitored by a government and is not included in the government's GNP, or Gross National Product. In 1971, Keith Hart created the term "informal economy" while studying in Accra, Ghana. While there, he noticed that despite external constraints, most migrants still engaged in informal activities that still generated them money. Hart described the informal economy as two categories, the "legitimate employment" and the "illegitimate employment." The legitimate activities include those that make a small contribution toward economic growth such as home-based production, manual labor, or personal services. "Illegitimate employment", on the contrary, includes that were questionable value to national development and were often criminal, such as begging, pickpocketing, scavenging, and streetwalking. Since Hart's observations, the informal economy has been constantly debated over. It undergoes many different names such as the Unobserved economy, the Unorganized Sector, the Unprotected Sector, the Uncounted, or just the poor and marginalized. One agreement, though, is that in order for the informal economy to become formal, they must have registrants, possible subjection to health and security inspections, legality with payment of formal taxes and tariffs, and compatibility with official guidelines of working hours, social security contributions, and fringe benefits. Some people believe that the informal economy is problematic and that the workers are deliberately trying to avoid regulation and taxation while others believe that is the source of livelihood for the working poor. The informal economy is most often associated with the poor and marginalized and people who are unable to find work. In response to their unemployment and need for money, they must create their own revenue or employment. The informal economy is found in most developing countries where people are unable to find work. For example, the informal economy comprises 27 percent of North Africa, 41 percent of Sub-Saharan Africa, 29 percent for Latin America, and 31 percent for Asia.

Although the informal economy provides many poverty-stricken communities with jobs, it has some negative impacts on the economy. For example, it makes macroeconomic variables such as GDP and inflation unreliable which consequently makes the leaders of the countries unable to make accurate decisions about their country. The informal economy also creates unfair competition for the formal economy. Because the informal economy does not have to pay taxes, they can sell things for cheaper, therefor undercutting the formal economy. Having a large informal economy also creates ongoing budget deficits for the country. The informal economy is not paying taxes, therefor, the government is not collecting the money which leads to financial crises and eventually causes the country to borrow heavy amounts of money from other countries. Plus, the informal economy causes a negative financial structure in the social security system. By not paying taxes, the informal economy diminishes revenues of social security organizations which consequently weakens their provided services. Lastly, the informal economy has negative impacts on public reconciliation.

The informal economy also results in many deficits for the employees. For example, the status of labor may be undocumented which results in people working below minimum wage, lacking social benefits, or employment under illegal terms. Plus, the conditions of work are also unregulated which leads to ignorance in health and hygiene and other safety departments.

UN Involvement

After Hart's work in Africa, the International Labor Organization or the ILO used his work as the groundwork to distinguish between formal and informal employment. Since then, the ILO has done much to help the Informal Economy. In 2002, they introduced the ILC Resolution and Conclusion on Decent Work and Informal Economy which addressed the poor working conditions in the informal economy. Through this, the ILO hoped to create better employment and income opportunities by promoting social protection and dialogue. Then in

2015, building upon this resolution, they released the R204 resolution. This resolution included a recommendation for the Transition from the Informal to the Formal Economy. It included a three-part objective, first, to facilitate in the transition of workers and economic units from the informal economy to the formal economy while keeping the workers' rights and allowing for secure incomes, security, and livelihoods. Second, the resolution tried to promote the creation of sustainable enterprises with decent jobs in the formal economy and consistency of macroeconomic, employment, social protection, and other social policies. Lastly, the resolution included the prevention of the informalization of formal economy. Plus, the Informal Economy Unit directly works with the transition process from informal to a formal economy.

Country Policies and Solutions

The informal economy is very prevalent throughout Pakistan. The people have limited access to labor and welfare services. The informal economy comprises 73.3 percent of the employment in main jobs outside agriculture, mostly in rural areas. The biggest revenues in the informal economy include wholesale and retail trade, manufacturing, community or social personal services, and construction and transport. Although the informal economy is continuing to grow, the country of Pakistan is trying to redirect it to the formal economy. In 2010, Pakistan introduced a new labor policy which addresses the issue of workers in the informal economy. Under this policy, the government is aiming to provide benefits to these workers, which includes home workers and domestic workers, and helps to improve safety and health arrangements, provides access to social security arrangements and payment of minimum wages. Overall, this helps to make the informal economy more like the formal economy.

Pakistan proposes a series of solutions to help solve the issue of the informal economy. The first solution is to create a universal definition for the informal economy. This would clear up confusion and debate about the informal economy due to the many different interpretations of what is included. Creating a universal definition would help quantify the size of the informal economy, and in turn, define the tax potential. This would help prioritize the efforts for conversion of the informal economy. Pakistan proposes that an informal economy is the economy that is excluded from taxes, social security, and traditional trade unionism and is not included in the country's GDP estimates.

Adding to this universal definition, Pakistan further proposes to create a universal set of terms-of-registration for a company or individuals to enter into the formal economy. These terms would include an agreement to pay fees and revenue-based taxes and in return the company would be eligible to be a supplier or contractor for government sponsored contracts and research efforts. Sub-contractors would also be required to be registered. The employees will be offered social security and will be protected by employment laws and health safety standards.

The second solution that Pakistan proposes is to slowly transition the informal economy into the formal economy. To accomplish this, Pakistan proposes a two-step plan. The first step is to implement a minimum wage and health safety incentives for the informal employees. To do this Pakistan plans to incentivize the employers to include these benefits in their work. These incentives would include giving the companies access to markets, entrepreneurship, skills, finance, and management, plus access to government projects. The second step is to implement social security into the informal economy. This would protect the workers, provide stability to the work force, and add a supplementary boost to the economy. By slowly integrating parts of the informal economy into the formal economy, Pakistan hopes reduce the size and impact of the informal economy while not losing the businesses and allowing people to keep their jobs.

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