



WORLD BANK GROUP

Addressing Informality

Workshop on Informality in the Latin America and the Caribbean Region
June 2023

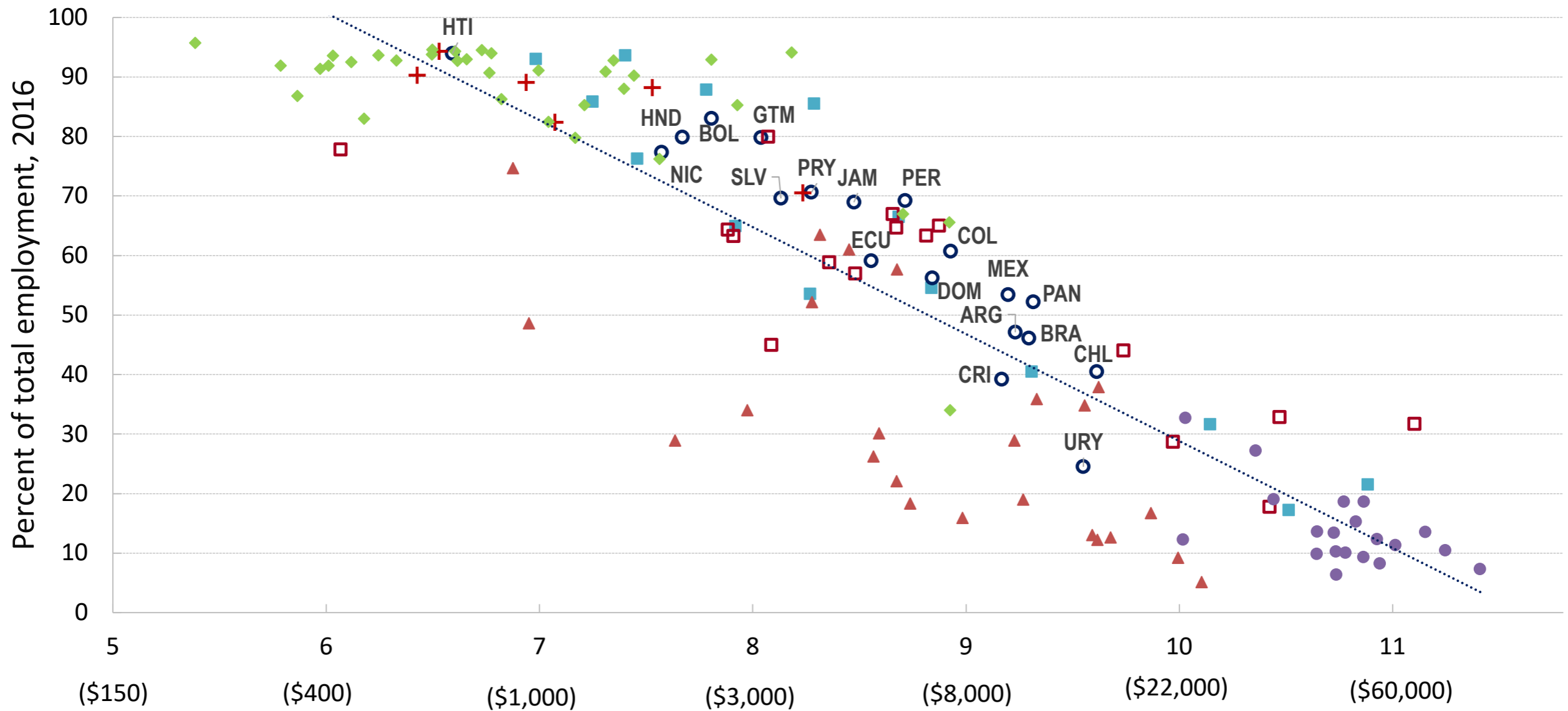
Norman Loayza
Director

Development Economics Global Indicators Group

Is there anything to address?

- **WDR 2013 *Jobs***: “Informal is normal”

Informal labor vs. GDP per capita



Is there anything to address?

- **WDR 2013 *Jobs*:** “Informal is normal”
- But “being normal” does not imply that it is fine:



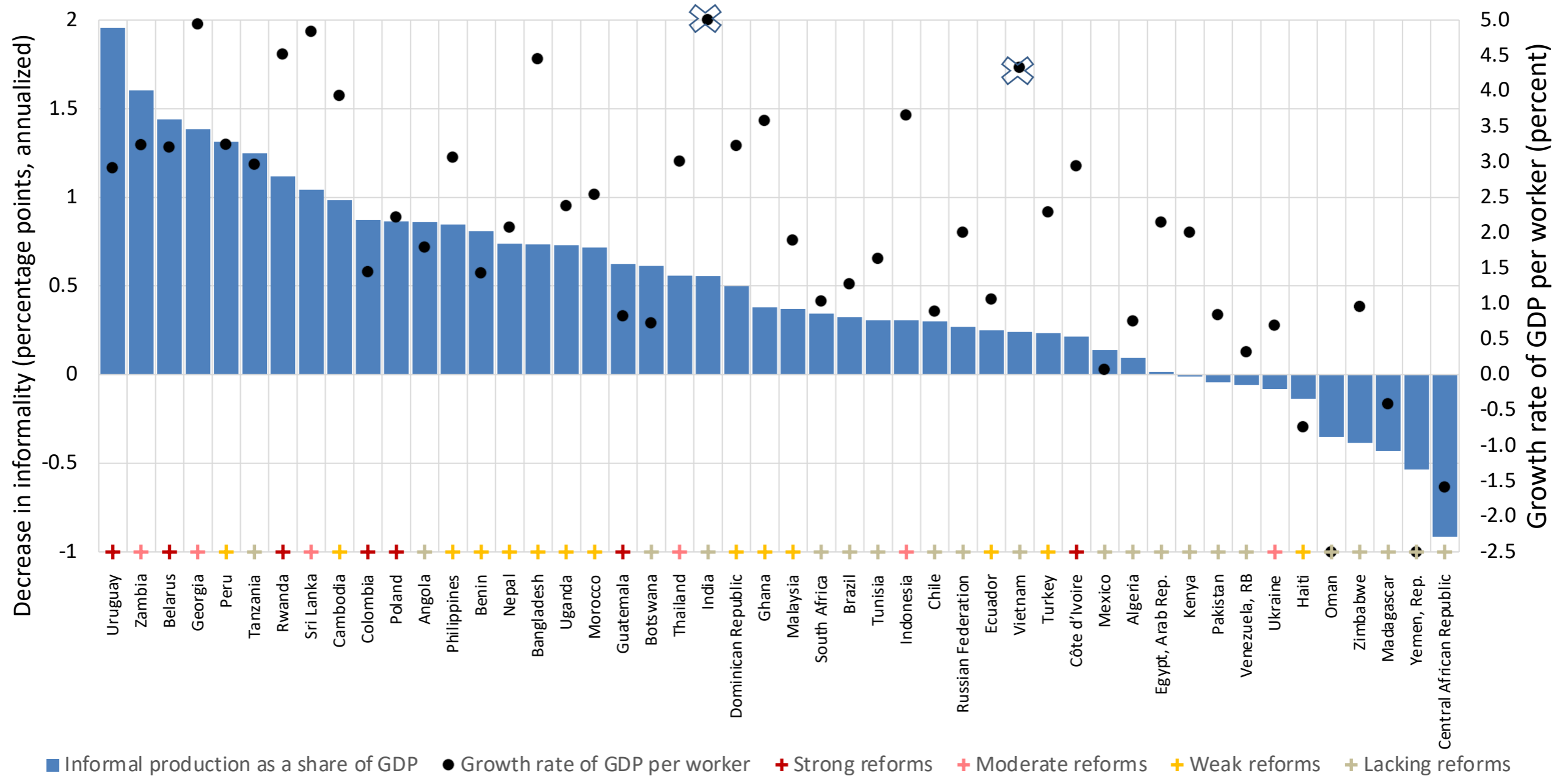
- **Why should it be addressed?**
 - 1. Insiders:** Informality implies that businesses and people do not benefit from appropriate technologies, economies of scale, and access to public services and social protection
 - 2. Outsiders:** Informality is a social burden because it represents unfair competition to formal firms, contributes little in taxes, and promotes a culture of lack of respect for law and order

A Policy Approach

I. Trust economic growth: it will reduce informality... eventually

- **Growth drivers:** improvements in total factor productivity, investments in physical and human capital, and better provision of public infrastructure:
 - will make emerging, medium, and large enterprises (with higher labor productivity) more prevalent
 - drawing resources –workers and activities– from the informal sector
- **Informality will decrease gradually:** roughly 1 pp reduction of informal labor (over total labor) for each pp of economic growth

Growth decreases informality (2005-2015)



Source: Loayza (2018)

II. Improve the business environment

- How? Only a **holistic** approach can work

When *obstacles to formality* come, they come not single spies, but in battalions



Rigid labor market

Cumbersome entry and exit

Inexistent or confusing land rights

Formalization

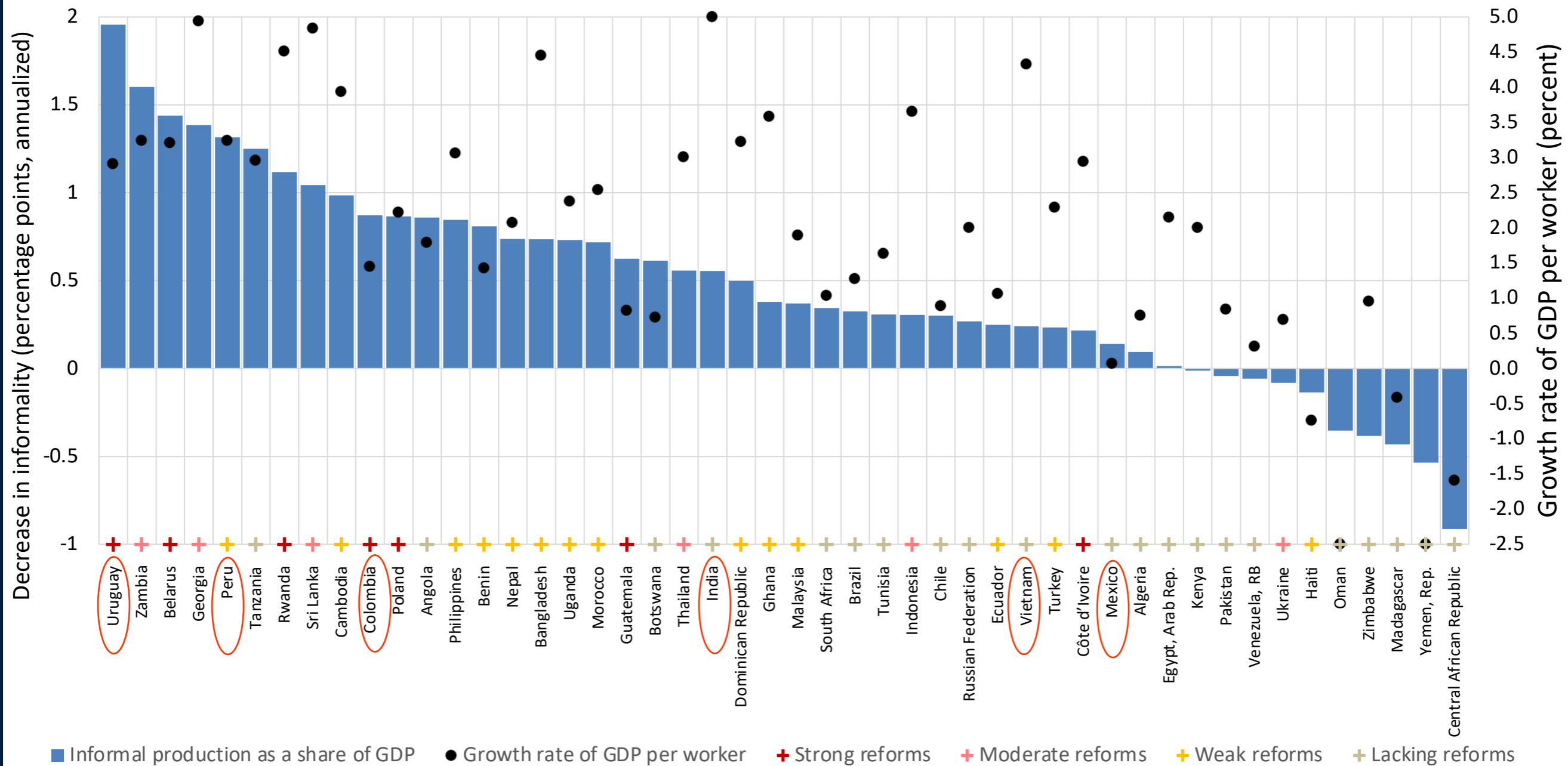
Financial and credit constraints

Excessive and complicated taxes

II. Improve the business environment

- How? Only a holistic approach can work
 1. Streamline and improve the quality regulations (e.g., do not make workers too expensive)
 2. Provide public services that complement regulations (e.g., provide social protection funded through general revenues, not labor taxes)
 3. (Do not obsess with formalizing micro and small firms)

Growth and a better business environment reduce informality (2005-2015)



Source: Loayza (2018)

II. Improve the business environment

- How? The only approach that works is holistic
 1. Streamline and improve the quality regulations
 2. Provide public services that facilitate compliance
 3. (Do not obsess with formalizing micro and small firms)

- How again? Be specific!



**BUSINESS
READY**



DEC

Global
Indicators
Group



**WOMEN, BUSINESS
AND THE LAW**



**ENTERPRISE
SURVEYS**



**BUSINESS
READY**
SUBNATIONAL



WORLD BANK GROUP

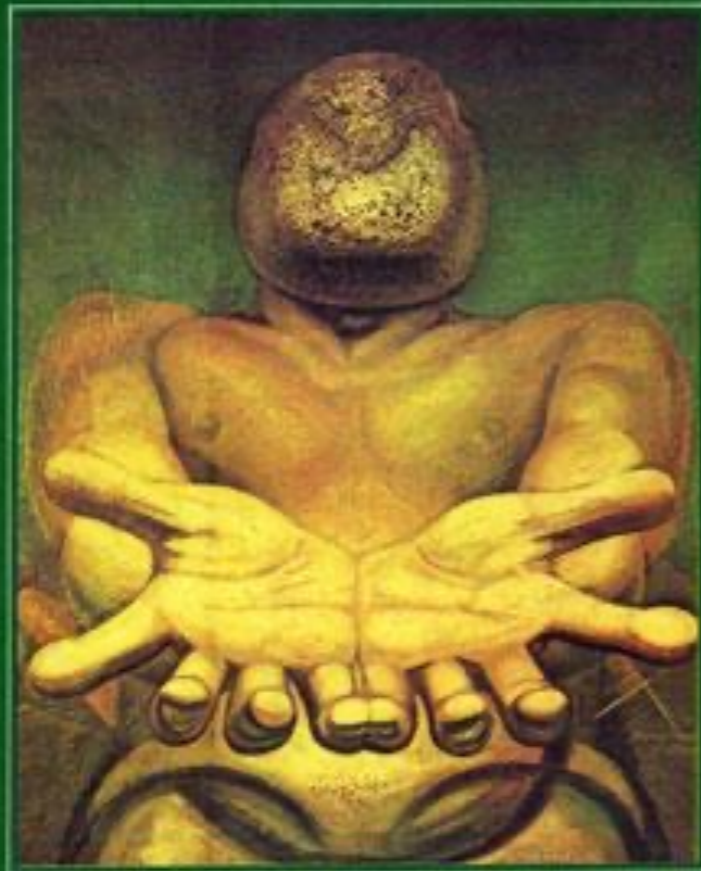
III. Don't punish informality: carrots are better than sticks

- Will **severe enforcement** reduce informality? Maybe a little
- Most likely, it will force it **deeper in the underground economy**
- with much **worse consequences**: without informality as a safety net and job provider,
 - unemployment
 - drug or alcohol addiction
 - crime
 - insurrection
- **“Jobs are the ultimate solution”** – Ajay Banga, June 8, 2023

HERNANDO DE SOTO

en colaboración con E. Gherzi y M. Ghibellini

EL OTRO SENDERO



Editorial Sudamericana

THE INVISIBLE REVOLUTION
IN THE THIRD WORLD

THE OTHER PATH



HERNANDO DE SOTO
FOREWORD BY
MARIO VARGAS LLOSA

I.B.TAURIS & Co Ltd

In summary

- 1. Trust growth... and promote it**
- 2. B-READY: improve the business environment**
- 3. Be gentle: make formality attractive rather than punish informality**



WORLD BANK GROUP

Thank you

Development Economics Global Indicators Group