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URBANIZATION AND LABOR MARKET INFORMALITY IN DEVELOPING COUNTRIES

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Abstract

Rapid and uncontrolled migration created by the population moving from rural to urban areas causes serious problems from the viewpoint of labor markets. Increases in rural-urban migration flows is contributing to a larger urban labor supply. This increasing labor supply has produced an increasing urban unemployment rate and a deterioration in the quality of employment, as it is evident from the increased informal employment rates. One of the most distinctive features of the economies in developing countries is the fact that more than half of workers are employed in the urban informal sector. Urbanization and informal sector are joint and rising trends in these countries. The informal sector represents a significant part of the economy, and certainly of the labor market in developing economies, and plays a major role in employment creation, production and income generation.

Keywords: urbanization, informal labor market, urban labor market, rural- urban migration, developing countries

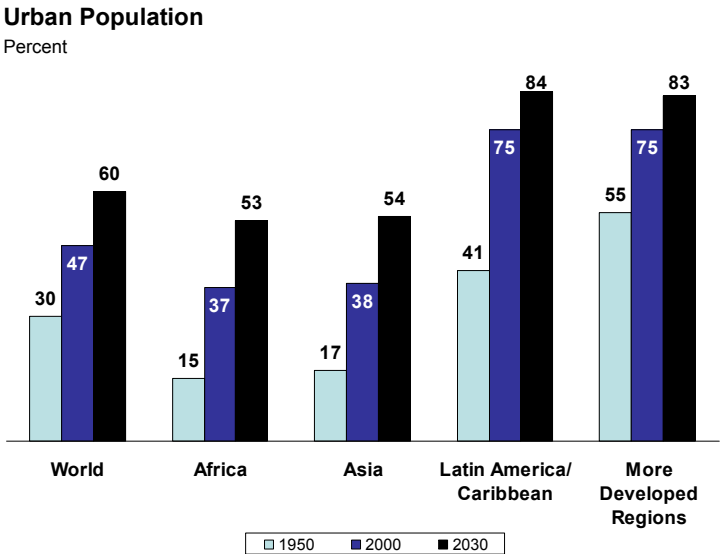
URBANIZATION IN DEVELOPING COUNTRIES

The twentieth century witnessed the rapid urbanization of the world's population. The global proportion of urban population increased from a mere 13 percent in 1900 to 29 percent in 1950 and reached 49 percent in 2005 (UN, 2005). By 2030, almost 60 percent of the population of the developing world will be living in urban areas. (UN, 2002).

There are enormous differences in the pattern of urbanization between regions and even greater variation in the level and speed with which individual countries or indeed individual cities within regions are growing. Latin America, for example, is far more urbanized than Africa or Asia. The level of urbanization in Latin America-around 75 percent-already matches that of North America as well as many European countries. Consequently,

the rate of urbanization in Latin America is quite slow. Argentina, Brazil, Uruguay, Venezuela, and Chile, for example, are all well over 80 percent urban while levels of urbanization are somewhat lower in most of Central America and the Caribbean. At the other end of the spectrum, Asia and Africa, still both heavily dependent on agriculture, are predominantly rural in character although both have around 38 percent of their populations living in urban areas in 2000. By being less urbanized, these two regions are expected to experience relatively faster rates of urbanization over the next 30 years (Cohen, 2006).

Trends in Urbanization, by Region



Source: United Nations, *World Urbanization Prospects: The 2001 Revision* (medium scenario), 2002.

LABOR MARKET INFORMALITY IN DEVELOPING COUNTRIES

Concept of Informality

Since the release of the report of a comprehensive employment mission to Kenya undertaken by the ILO in 1972, the term “informal sector” has gained acceptance in international official documents. Initially the informal sector was considered to be mainly composed of the urban “working poor” migrated from rural areas in search of work. Later it was recognised as an important employment-generating sector and an important source of production and income (Husmanns and Mehran 1989).

The Fifteenth International Conference of Labor Statisticians (ICLS), held in January 1993, eventually adopted a resolution concerning statistics of employment in the informal sector that provides an international statistical standard definition of informal sector. The ICLS describes the informal sector as consisting of production units that: "*typically operate at*

a low level of organization, with little or no division between labor and capital... and on a small scale.... Labor relations - where they exist - are based mostly on casual employment, kinship or personal and social relations rather than contractual arrangements with formal guarantees" (ILO, 2003).

There are two “informal” concepts that affect employment: ***employment in the informal sector, informal employment***. They are both useful for analytical purposes and complement each other. Employment in the informal sector and informal employment are concepts, which refer to different aspects of the ‘informalisation’ of employment and to different targets for policy-making. Statistics users and others often tend to confuse the two concepts because they are unaware of the different observation units involved: enterprises on the one hand, and jobs on the other (UNECE, 2003).

Employment in the informal sector: ‘all persons who, during a given reference period, were employed in at least one of the informal sector enterprise, irrespective of their status in employment and whether it was their main or a secondary job’.

Informal Employment: Persons employed in the informal sector + persons employed in “informal jobs”.

Informal jobs: non-standard, atypical, irregular, precarious, unprotected, not covered by existing regulations (social protection, benefits).

(The first criterion is based on the production unit, the second criterion on the type of job)

The ICLS issued the Guidelines on a Statistical Definition of Informal Employment in 2003 and defined informal employment to include the following types of jobs:

- Own-account workers employed in their own informal sector enterprises;
- Employers employed in their own informal sector enterprises;
- Contributing family workers, irrespective of whether they work in formal or informal sector enterprises;
- Members of informal producers’ cooperatives;
- Employees holding informal jobs, whether employed by formal sector enterprises, informal sector enterprises, or as domestic workers employed by households; and
- Own-account workers engaged in the production of goods exclusively for own final use by their household (such as subsistence farming or do-it-yourself construction of own dwellings).

There are currently two opposing views of informal labor markets. On one view, the informal sector is a ‘residual sponge’ which absorbs that part of the growing labor force that cannot be employed in the more productive and remunerative formal sector: its growth is a sign of economic failure, and policies are needed to reduce poverty within it. This view further perceives the informal sector as a state between formal employment with social protection and open unemployment. A form of market failure prevents individuals from moving from the informal to the formal sector. This is based on an ‘insider-outsider’ model where those in formal employment are insiders and those in the informal sector and the unemployed are outsiders. In the presence of such labor market segmentation, wages in the two sectors of the economy will differ for two employees of equal potential productivity. On the other view, the informal sector is a dynamic sector, containing much budding entrepreneurship: its growth is a sign of economic success, and policies are needed for its encouragement. On the former view, informal employment is likely to be involuntarily imposed, and on the latter view it is likely to be voluntarily chosen. In fact, both views can be correct: they might apply in different countries, and in the same country in different proportions (Ruffer, 2007).

In developing countries, the term “informal sector” has broadly been associated with unregistered and unregulated small-scale activities that generate income and employment for the urban poor. With increasing urbanization, the informal economy tends to absorb most of the growing labor force. Informal sector employment is a necessary survival strategy in developing countries that lack social safety nets such as unemployment insurance. But the creation of employment through informal sector has generated poor working conditions such as; low wages, insecure jobs. Some of the main labor market problems generated by rapid and uncontrolled urbanization process in developing countries are; informality, urban unemployment, working poverty, decreasing work quality.

Size of Informality

Today, there is no universally accepted definition of labor informality because it is not easy to define and measure informality in a comparable manner across countries. Conventional metrics focus on “enterprise size”, “individuals’ labor-market status” and “social security coverage of the labor force”. Some countries include informal employment in agriculture in their estimates of informal employment. In these countries the inclusion of informal employment in agriculture increases significantly the proportion of informal employment.

The share of informal employment is highest in the poorest developing regions, particularly in South Asia and sub-Saharan Africa. In India, for example, the share of informal employment was 76 per cent in urban areas in 2000. According to Barbara Harris-White, it accounts for 60% of the GDP. The share of informal workers by sector and continent is shown in the table below (Deshingkars, 2004). The bulk of new employment generated in recent years in developing countries has been in the informal economy. Over the past decade, informal work is estimated to have created over 90 per cent of new jobs in Africa, and a major portion of jobs in South Asia.

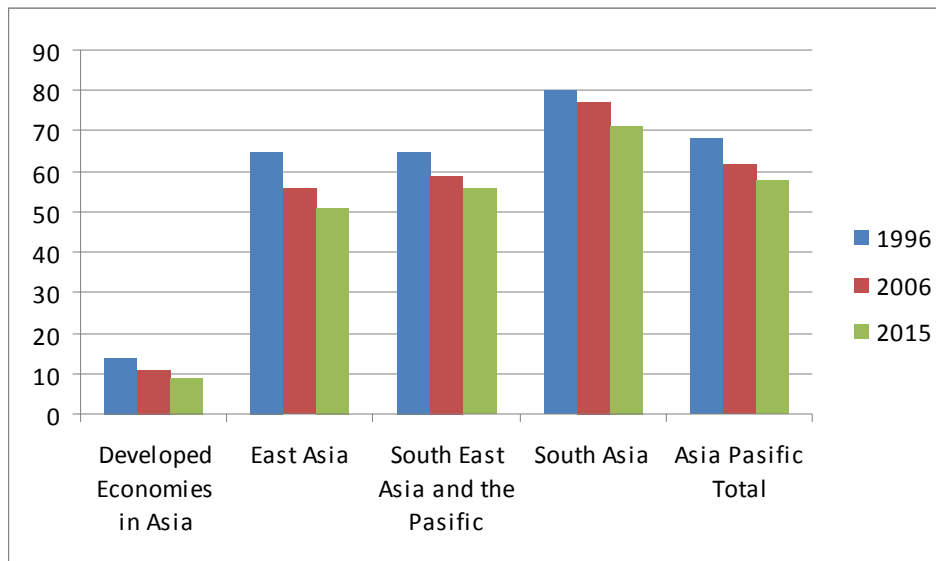
Table 1- Size of the informal sector

Informal Workforce as a Share of	Africa	Latin America and Caribbean	Asia
Non-agricultural employment	78%	57%	45–85%
Urban Employment	61%	40%	40–60%
New jobs	93%	83%	NA

Source: K. F. Becker (2004) “**Fact Finding Study: The Informal Economy**”, Swedish International Development Agency.

Widespread informality have become structural characteristics of the developing countries. If recent trends continue, Asia’s informal economy will remain vast. Although the number of contributing family workers is projected to decline by around 86 million – a reflection of declining agricultural employment – the number of own-account workers is expected to increase by 128 million. Based on this, their combined share in total employment would decline moderately from 61.9 per cent in 2006 to 57.3 per cent in 2015. At the same time, wage and salary employment is expected to increase by 176 million, although part of this increase will be in small and micro-enterprises operating in the informal economy. As a result, the informal economy is expected to account for around 60 per cent of the region’s total employment in 2015. The largest share of informal economy workers in total employment is expected to be in South Asia (more than 70 per cent), followed by South-East Asia and the Pacific (about 55 per cent) and East Asia (approximately 50 per cent) (ILO, 2007a).

Figure 2- Estimated share of informal employment in total (%), 1996, 2006, 2015



Source: ILO (2007), **Global Employment Trends Model** .

WHAT IS THE RELATIONSHIP BETWEEN URBANIZATION AND INFORMALITY IN DEVELOPING COUNTRIES

One striking feature of the urbanization in developing countries is the presence of a large informal sector. Between 30% to 70 % of urban labor force works in the informal sector. There are multiple factors underlying informality in developing countries (ILO, 2007):

- Poverty and the livelihood opportunities and jobs for the working poor,
- The inability of the industrial sector to absorb labor in more productive jobs,
- The increasing flexibility of work in the formal economy, with work arrangements lacking security and proper social protection,
- Weak governance,
- ***The rapid pace of rural-urban migration.***

Several studies indicate that there is a close relation between migration from rural to urban and the informal sector (Banerjee, 1983; Sethuraman, 1992). In this migration process, the growth of the informal sector in developing labor markets is inevitable because the informal sector is the primary job generator. In these countries, many of new jobs is created by micro-enterprises, own-account workers and domestic services. Therefore, urban informal employment absorbs the urban labor force.

According to the Harris-Todaro's theory of rural to urban migration: rural to urban migration causes overcrowding and unemployment in cities as migration rates exceed urban job creation rates, with many people ending up in unproductive employment in the informal

sector. However, even though this migration creates unemployment and induces informal sector growth, this behavior is economically rational and utility-maximizing in the context of the Harris-Todaro model. As long as the migrating economic agents have complete and accurate information concerning rural and urban wage rates and probabilities of obtaining employment, they will make an expected income-maximizing decision (Harris-Todaro, 1970).

Therefore, migration from rural to urban areas will increase if:

- Urban wages increase, increasing the expected urban income.
- Urban unemployment decreases, increasing the expected urban income.
- Urban job creation increases the number of available jobs in the urban sector, increasing the expected urban income.
- Agricultural productivity decreases, lowering marginal productivity and wages in the agricultural sector, decreasing the expected rural income.

Gary Fields extended the Harris-Todaro model in several directions, most relevantly by incorporating an urban informal sector. Employment in urban informal sector is characterized as "underemployment", an alternative to open unemployment for rural migrants unable to find work in the urban formal sector (Fields, 1975). Developed countries generally have stronger unemployment insurance systems, and thus open unemployment can more readily provide an alternative to informal employment in the face of job loss.

Fields built on such observations as well as his own research in urban Costa Rica and Malaysia, developing the idea of dualism within urban informal employment characterized by "easy-entry" and "upper-tier" informal employment. He found that many upper-tier informal workers had previously worked in formal employment, where they had gained the skills and savings to set up their own informal enterprises. Though Fields emphasizes that upper-tier informal employment is "voluntary", he also refers to its "constrained voluntary nature", elaborating that "given the constrained choices available to them, a great many of informal sector workers are in that sector voluntarily" (Fields, 1990).

WHO ARE THE WORKERS IN THE URBAN INFORMAL ECONOMY?

In general, new entrants to the city often enter the labor market through the informal sector. Informal jobs are in family rather than formal enterprises, are small scale, often lack a fixed location, involve small investments, have no fixed earnings, involve no formal training. Most informal economy employment is self-employment. Informal employment is normally unstable and insecure – consisting of very long hours and high pressure periods to finish contract orders within short deadlines, followed by “inactive” periods waiting for orders.

There is a link – although not a perfect correlation – between working in the informal economy and being poor. This stems from the lack of labor legislation and social protection covering workers in the informal economy, and from the fact that informal economy workers earn, on average, less than workers in the formal economy (ILO, 2004). In urban areas, the working poor include street vendors, waste pickers, informal transport providers, construction workers, and people who work in sweatshops or from their homes. In rural areas, the working poor in the informal economy include very small farmers, agricultural day laborers, artisans, people who rear livestock or poultry, fisher folk, and forest gatherers (Chen, 2007).

Informal workers are vulnerable, as they are unprotected by labor laws. Most lack basic social protection and hold unproductive jobs with low earnings. They have few social rights, with no social security, severance pay, minimum wage, or standards for working conditions. Who are these workers?

- ***Children and Young People:*** Rapid rural to urban migration is the cause for the increasing rate of child labor in urban areas of developing countries. Tens of millions of children in developing world are employed mostly in the informal labor market under unhealthy working conditions, without any social security. Even though children are paid less than adults, they are important contributors to the family income.

Young people make up the most vulnerable segment of the labor market. The vast majority of the world's young people work in the informal economy. While employment in the informal sector is growing rapidly, and the young unemployed are increasingly forced to find work in small unregistered companies, for family businesses or in home working or self-employment (ICFTU, 2005). Young informal workers frequently work long hours with low wages, under poor and precarious working conditions, without access to social protection, freedom of association and collective bargaining (ILO, 2005).

- ***Women:*** Informal employment is generally a larger source of employment for women than for men in the developing world. Other than in North Africa, where 43 per cent of women workers are in informal employment, 60 per cent or more of women non-agricultural workers in the developing world are informally employed. In sub-Saharan Africa, 84 per cent of women non-agricultural workers are informally employed

compared to 63 per cent of men; and in Latin America the figures are 58 per cent of women in comparison to 48 per cent of men. In Asia, the proportion is 65 per cent for both women and men (Chen, 2007).

The increasing employment of women in the informal sector can be put down to various reasons. First of all, with the increase in unemployment, women are tending to lose ground in the formal sectors of the economy. Secondly, given the rapid process of urbanisation, women, because of their low level of skills, cultural conditioning and traditional family responsibilities, stay out of the formal labor market in favour of the informal one. Thirdly, stagnating and falling household incomes due to the poor performance of the economy also leads to the increased entry of women into the informal labor market. Fourthly, export-oriented industries, in the search for cheap labor, favour women's employment. These factors are leading to the increasing informalisation of the female labor force. This informalisation takes place broadly in one way: work is being pushed out of factories and formal work situations into small workshops, homes and informal situations (Ozdemir, 2004; Unni, 1999).

- The Self Employed

The informal sector is characterized by a large number of small-scale production and service activities that are individually or family owned and use labor-intensive and simple technology. Because of this, the main component of informal sector employment is self employed people. Unlike the formal sector, workers in the informal sector are mostly in self-employment rather than wage employment. The self employed, most of whom are own account and unpaid family workers, constitute the major part of the urban informal sector in developing countries. The majority of the self-employed in the urban informal sector are low-skilled or unskilled. Formal education levels tend to be lower than in the formal sector.

Home-based workers and street vendors are two of the largest sub-groups of the informal workforce: with home-based workers the more numerous but street vendors the more visible of the two. Together they represent 10-25 per cent of the non-agricultural workforce in developing countries and over 5 per cent of the total workforce in developed countries (Wiego, 2009).

CONCLUSION

In this paper, we have looked at the labor market informality as a result of rapid and uncontrolled migration from rural to urban areas in developing countries. At the root of the problem of the informal economy is the inability of economies to create sufficient numbers of decent jobs to absorb the growing labor force. With increasing urbanization in developing countries, the informal economy tends to absorb most of the growing labor force. But the creation of employment through informal sector has generated poor working conditions. In summary, the main characteristics of the urban informal sector jobs are:

- low skill and productivity
- small scale measured in terms of sales, assets, employment etc.
- large degree of self-employment,
- extremely low incomes,
- no protection or little protection under labor laws,
- favored by recent migrants
- ease of entry.

What can be done about urban labor market informality?

- First of all, struggling the labor market informality requires making employment a central concern of economic and social policies. This entails promoting employment-friendly macroeconomic frameworks and policies.
- A powerful instrument for reducing labor informality is to improve the skills of the labor force. Improving the skills of informal labor is key to their ability to access decent jobs, improve productivity and income. This can be done through the education system.
- Unemployment insurance is one of the most important components of formalization of labor market. Many of developing countries either have no unemployment insurance or have limited. Whereas providing decent income support to unemployed jobseekers may decrease underemployment and informality. So, unemployment insurance programs must be adapted to suit the needs of developing countries.
- Policies of rural development are crucial. Many scholars agree on the central importance of rural development to solution of the urban informality problem. As Todaro said, “a more appropriate balance between rural and urban economic and noneconomic opportunities appears to be indispensable to ameliorating urban and rural unemployment problems and to slowing the pace of rural–urban migration” (Todaro, 1997).

- Policy initiatives should promote decent work through growth strategies and quality employment generation. Urban places should be areas where high-quality jobs are created. An urbanization attained through the informal sector cannot constitute a valid response to this vital need. Developing countries have to find better ways of development (Bulutay, 2004).

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