

# The Informal Workforce and Public Policy

Este País Website<sup>1</sup> | Luis Videgaray Caso | 267 | 01.07.2013 |

The phenomenon of the informal workforce is widespread. It finds its roots in different fields — education, demographics, politics, etcetera— and it has impacts on all of those. How does the federal government view this problem and what can it do to deal with it? What solutions do the current reforms propose? *Este País* invited the Secretary of Finance to discuss this topic.

## Introduction: Relevance of the Informal Workforce

The relevance of the phenomenon of the informal workforce is closely related to many aspects that are very important in terms of economic performance and the welfare of the population.

The informal workforce reduces productivity and thereby diminishes economic growth. Moreover, it impedes full social protection of the population, reduces the quality of life and creates increased vulnerability to adverse events such as unemployment, sickness and accidents. In addition, the informal workforce diminishes the revenues of the State, thereby limiting its ability to provide the necessities of life for the population. The existence of the informal workforce produces inequities in the contributions of workers and sharing the tax load. It also undermines the building of a state where the laws are respected.

Because of the strong connection between the informal workforce and economic development and the welfare of the population—and also the complexity of the phenomenon— it is clear that all existing public policy tools must be used to deal with the problem in an overall manner. Any other approach would make it impossible to significantly reduce the informal workforce, with corresponding effects on the quality of life for all Mexicans.



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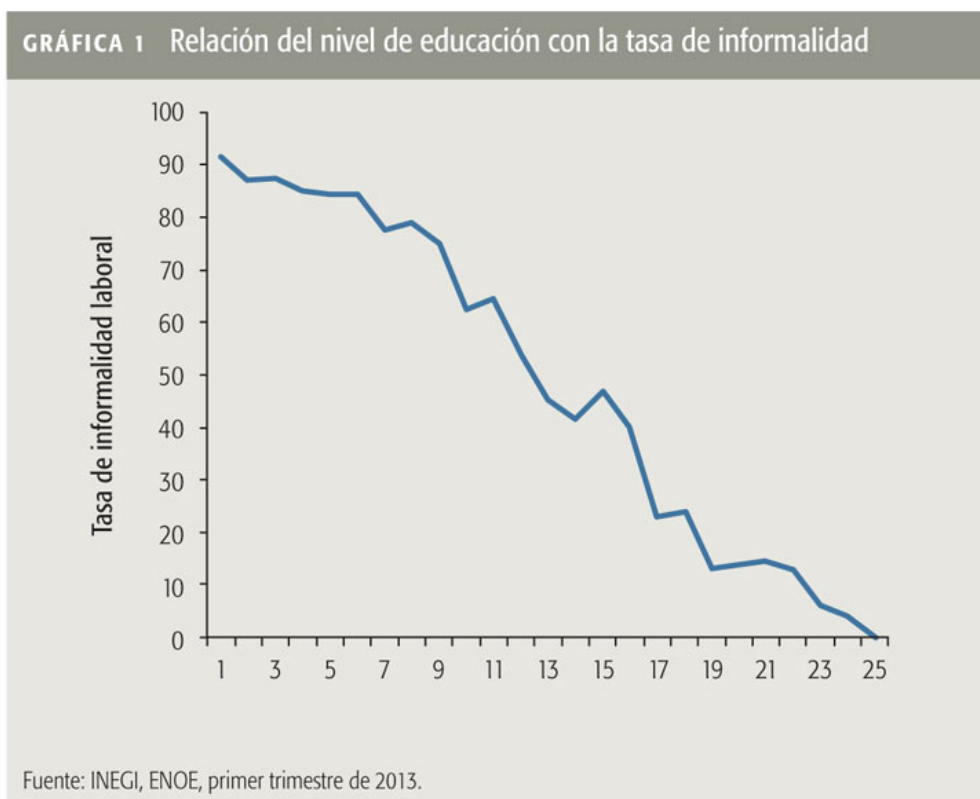
<sup>1</sup> This is an English translation of an article originally published in Spanish, “[El fenómeno del la informalidad y la política pública](#),” *Revista Este País*, No. 267. [Trabajo Informal](#), July, 2013. Mexico. Translation by Women in Informal Employment: Globalizing and Organizing (WIEGO) with permission of the publisher

## Towards an Understanding of the Informal Workforce

Of course, an essential condition for dealing properly with the problem is a clear understanding of the informal workforce, its characteristics and how large the informal workforce is in México. INEGI, the National Institute for Statistics and Geography, publishes statistics on the rate of informal employment, which includes all those workers who have no social security protection, either because they are working in informal businesses or they have no access to social security even though they are formally employed. According to that definition, 59% of the working population in Mexico is informal. (1)

Closer examination of the informal workforce reveals some of its main characteristics. Informal workers are not as well educated as formal workers. In terms of average years of schooling, the difference is 50%. The connection between schooling and the informal workforce is strikingly dramatic: more than 80% of working people with six or less years of schooling are in the informal workforce. For those who have 20 or more years of schooling, the number in the informal workforce is less than 15% (See Graph 1).

**GRAPH 1 Relation between Level of Education and the Informal Workforce**



Source: INEGI, ENOE, First quarter of 2013 (Lefthand column: Rate of Inclusion in the Informal Workforce)

Another characteristic of the informal workforce is its concentration in the rural areas of the country and in the activities of the agriculture and fishing sector. Some 60% of informal workers live in communities with less than 100,000 residents. This is in sharp contrast to workers in the formal workforce. Two-thirds of them live in communities with more than 100,000 residents, where there is a greater presence of large, formally established businesses. (*See chart below*).

**CHART Contrast between Informal Workforce and the Formal Sector  
Characteristics of the Informal Workforce, 2013.**

Variable	Formal sector	Informal sector (1)	Difference (2)	
	(average)	(average)	Absolute	% Informal
Years of schooling	11.7	7.9	-3.9	-49.1
Degree of urbanization				
More than 100,000 residents %	66.5	40.1	-26.4	-65.9
Less than 99, 999 residents %	33.5	59.9	26.4	44.1
<b>Employment sector</b>				
Primary	3.2	20.8	17.6	84.8
Secondary	27.7	21.2	-6.5	-30.7
Tertiary	69.1	58.0	-11.1	-19.1
<b>Size of enterprise</b>				
Single person	5.0	31.8	26.8	84.3
Two to 5 people	12.0	49.3	37.3	75.7
Six to 10 people	8.0	7.4	-0.6	-8.4
11 to 50 people	25.7	7.3	-18.4	-250.5
51 or more people	49.3	4.2	-45.2	-1082.6
<b>Average hourly pay (In Pesos)</b>	28.2	18.2	-10.0	-55.0
(1) Rate of informal workers				
(2) Difference between informal and formal sectors				

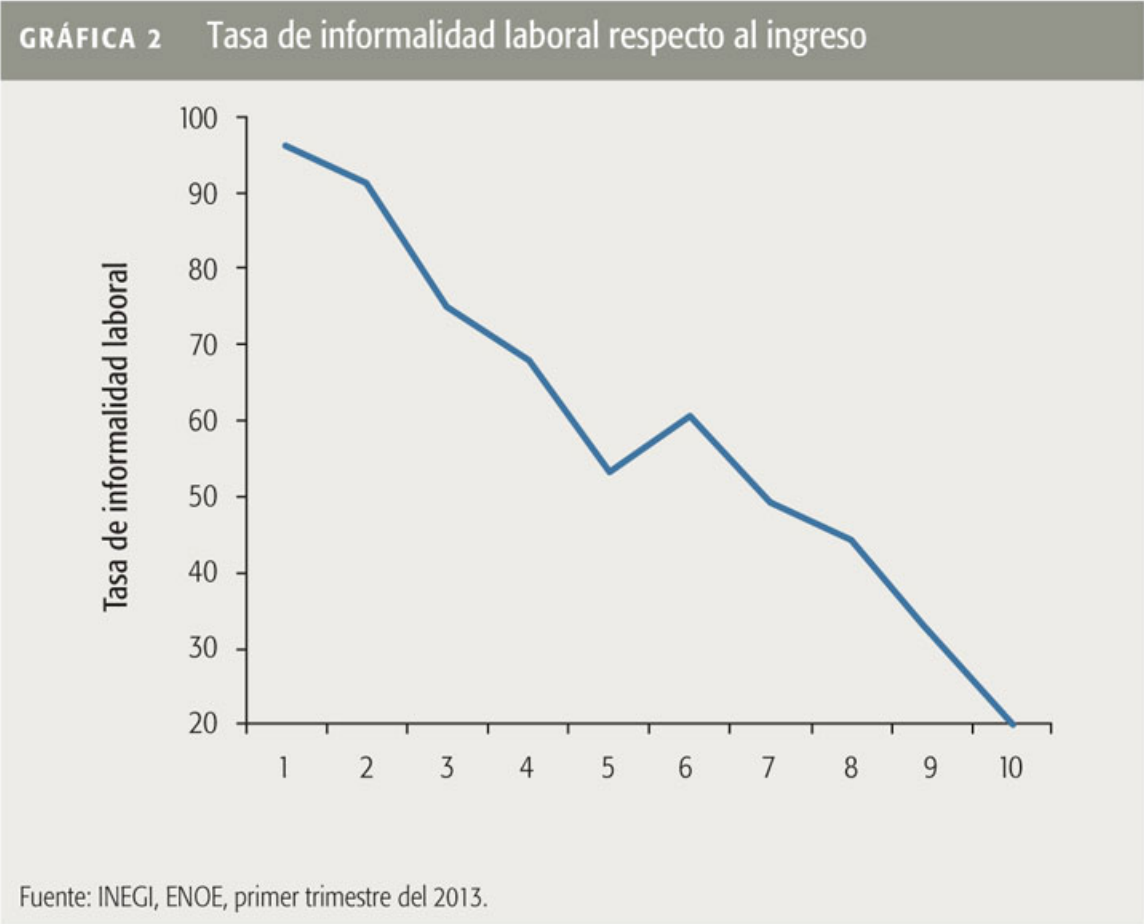
Source: INEGI, ENOE, First quarter of 2013.

In terms of employment sector, one of every five informal workers is employed in the agriculture and fishing sector, while only one of 40 formal workers is employed in that sector. Given the lower levels of physical and human capital per worker in the agriculture and fishing sector, which translates into lower levels of worker productivity, this difference is reflected in the lower incomes of informal workers.

Informal workers are also employed by small-scale businesses. That is another factor that reduces productivity and incomes because smaller companies find it difficult to achieve economies of scale in their operations. Some 81% of informal workers are employed by companies with five workers or less. This is in sharp contrast with the situation of formal workers, where 75% of those workers are in companies with at least 10 employees.

For the reasons described, there exists a wide discrepancy between the incomes of informal workers and formal workers (See Graph 2). On average, formal workers earn hourly incomes that are 55% higher than those of informal workers. Informal workers are generally in the lowest deciles and rarely in the higher deciles of income.

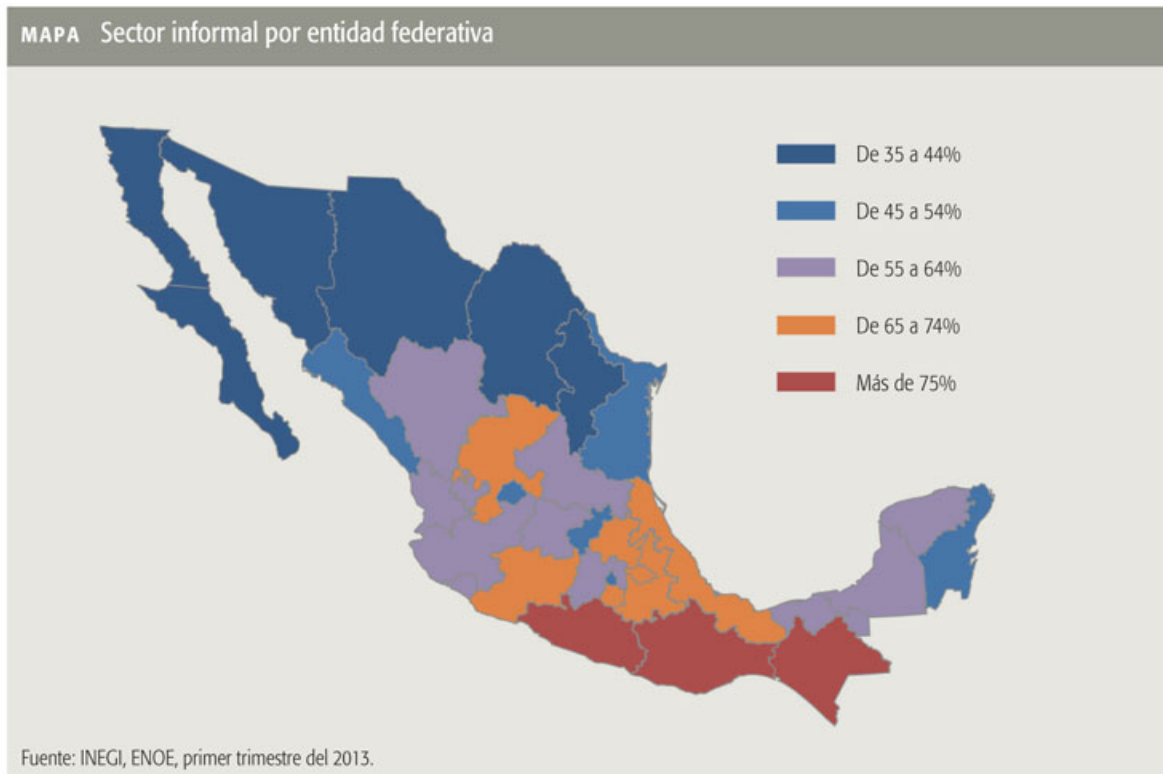
**GRAPH 2 Rate of Informal Workers Income**



Source: INEGI, ENOE, First quarter of 2013. (Lefthand column: Level of informal workforce income)

As might be expected, considering the main characteristics of informal employment, this condition produces a clear regional pattern (See map below). Rates of informal employment are particularly high in regions of the country where the population is widely dispersed, education levels are lower, a greater number of people are engaged in the agriculture and fishing sector and there are major gaps in infrastructure.

## MAP Informal Work Sector in Different Areas of Mexico



Source: INEGI, ENOE, First quarter of 2013

### The Role of Public Policy

The informal workforce is a complex phenomenon, related to many factors, some of which are structural in nature. As a result, any real solution to the problem must necessarily deal with all of the elements that contribute to the informal workforce.

Among structural factors that must be overcome initially is the need to increase the human capital of the country's workforce. This will require increased levels of education and improvements in the health of all population groups to develop more productive workers, which will lead to higher levels of public well-being. The recently approved education reforms should make an important contribution to that objective.

Considering the geographical patterns of the informal workforce, improved infrastructure is indispensable in those regions that have been marginalized. This will stimulate economic integration with the rest of the country and create conditions for establishing larger-scale businesses. At the same time, we need to change those policies that inhibit the growth of urban areas. This implies, for example, ensuring that our housing policies guarantee access to well located housing at reasonable cost. To achieve that, we have been conducting a full review of existing housing policies.

An examination of its principal features shows that the informal workforce is a complex phenomenon, related to many factors, some of which are structural in nature. As a result, any real solution to the problem must necessarily deal with all of the elements of the informal workforce.

Another distinctive feature of the informal workforce is its concentration in small businesses. We must find ways of making it easier for these businesses to grow. This includes action to promote easier access to funding for businesses of all sizes, which is one of the goals of the financial reforms recently introduced in the Congress of the Union. The objective is to help small businesses increase their scale of operation and to become more efficient.

In addition to measures aimed at the structural elements of the informal workforce, any solution to the problem must include an effort to facilitate compliance with all the requirements related to bringing businesses and workers into the formal economy. Our financial policy must include a taxation level that promotes the participation of all population groups in the formal economy.

The financial reforms to be presented in the second half of this year represent an opportunity to achieve that. We have a responsibility to establish taxation policy in our country that encourages participation in the formal economy and public spending policy that provides incentives for doing that.

The various reforms I have mentioned provide an opportunity to promote the participation of all population groups in the formal economy. If we succeed in taking advantage of that opportunity, we will have made significant steps toward improving social protection for all our citizens and increasing productivity in a full and inclusive way. That would be a decisive step to improving the welfare of all Mexicans.

*(1) All the data mentioned in this article refer to the first quarter of 2013 and are found on the Web page of INEGI, the National Institute for Statistics and Geography, or were calculated using the national survey of occupations and employment published by INEGI.*

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