

7 Informalization of Labour Markets Is Formalization the Answer?

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INTRODUCTION

The overarching theme of this volume is gendered differences in the impact of economic liberalization on livelihoods, employment opportunities and labour markets. As the chapters in this volume have illustrated, this requires an understanding of, first, overall impact and, then, gendered differences in impact. It is now widely understood that the impact of trade and market liberalization on livelihoods and employment is diverse. Indeed, the way that women and men workers experience market and trade liberalization is determined not only by their sex but also by the sector and type of unit in which they work; by their employment status; by their race, ethnicity, age and class; by where they live and work; and by the complex interplay of all these factors.

In general, policies that increase access to export markets, facilitate imports of scarce inputs and encourage investment in domestic production are thought to have positive effects on livelihood and employment opportunities (Heintz 2006). And policies that facilitate imports of consumer goods, over imports of scarce inputs, and/or do not encourage investment in domestic production are likely to have negative effects on livelihood and employment opportunities. In brief, the relative size of exports compared to imports—not the total volume of trade—appears to determine the impact of trade openness on employment (Heintz 2006). However, market and trade liberalization are often associated with the informalization of labour markets. So it is important to assess the impact of liberalization on the *quality* as well as the *quantity* of livelihood and employment opportunities.

Further, the employment impacts of trade openness tend to be gender specific and may change over time. In the first phase of trade openness, women tend to disproportionately gain from the jobs created from export growth and men are disproportionately impacted by the job losses associated with import penetration (Heintz 2006). However, in the second phase of trade openness, when export-oriented activities often become more profitable and mechanized, men may take over from women: as happened in the export assembly and processing sector in Mexico (Polaski 2004; UNIFEM 2000; White et al. 2003).

In addition to exports and imports, the third main pathway by which trade liberalization affects livelihoods and employment is through labour migration and related migration policies. But there are barriers to labour mobility, especially across borders, and to the flow of remittances, which undermine the ability of migrant workers to earn decent incomes and develop skills in host countries and reduce the potential benefit of their remittances on employment creation back home (Heintz 2006).

As other chapters in this volume have illustrated, it is also now widely understood that trade and market liberalization create risks as well as opportunities. But the contradictory impacts on employment and livelihoods are not well understood. First, it is still widely assumed that trade liberalization leads to employment creation. But this is not always the case. Countries—or sectors within countries—can experience so-called “jobless growth”, when economic output expands but formal employment stagnates or declines. At the sector level, jobless growth is often due to choice of technology or, more specifically, to mechanization. But at an aggregate country level, jobless growth is also often due to the privatization of public enterprises, downsizing of the public bureaucracy and competition from cheap imports. Second, it is still widely assumed that the jobs that are created are “good jobs”. But this too is often not the case. In fact, trade liberalization is associated with a global production system that favours subcontracting production of low value-added labour-intensive activities to producers, suppliers and workers in developing countries. Near the bottom of the global supply chains are the unprotected workers in export processing zone factories or small export-oriented production units. At the very bottom are the industrial outworkers—or home-workers—who produce for a piece-rate for suppliers (or their intermediaries) and have to bear most of the costs of production other than wages and raw materials.

Finally, it is still widely assumed that informal employment results from underdevelopment or poor economic performance. But trade liberalization and economic growth are, in some contexts, associated with the informalization of labour markets. When not enough jobs are created to meet the demand, people turn to self-employment in the informal economy. When the self-employed cannot compete with cheap imports, they often shift into low-skilled and low-paid wage jobs. When people can no longer afford public services once they are privatized, they may be forced to supplement their existing earnings with self-employment in the informal economy. When the new employment opportunities are linked to the global production system or labour migration, they are often “bad jobs”.

This chapter considers what can and should be done about labour market informalization. The chapter opens with a brief overview of informal labour markets in developing countries and labour market informalization in (mainly) developed countries, including gendered patterns and trends. It then considers whether “formalization” is the answer to informalization, by considering what formalization should consist of for both the self-em-

ployed in informal enterprises and wage workers in informal jobs. Finally it outlines a broad approach to informal labour markets that goes beyond formalization per se, including reorienting economic policies, reforming the formal regulatory environment and empowering informal workers.

INFORMALIZATION OF LABOUR MARKETS

Broadly defined, the informalization of the labour market represents a situation in which the ratio of the informal labour force to the formal labour force—or the share of the informal labour force in the total labour force—increases over time. However, the term is often used, more narrowly and specifically, to refer to the informalization of once-formal jobs in (mainly) developed countries. In this chapter, the term is used in the broad sense to refer to informalization of work over time in both developing and developed countries. But a distinction is drawn between informal employment in developing countries and nonstandard work in developed countries.

In developing countries, labour statisticians have used the term “informal sector” to refer to employment in informal enterprises (that is, unregulated and small enterprises). Recently, they have adopted the term “informal employment” to refer, more broadly, to all forms of informal employment (that is, unregulated and unprotected employment) both inside and outside informal enterprises. Increasingly, labour economists and other observers are also drawing the distinction between the “informal sector” and the broader concept of “informal employment”.

Broadly defined, the informal labour force includes the *self-employed in informal enterprises* (that is, small and unregulated) as well as the *wage labourers employed in informal jobs* (that is, unregulated and unprotected) in both urban and rural areas (Chen et al. 2005; ILO 2002). So defined, informal labour markets encompass *rural self-employment*, both agricultural and non-agricultural; *urban self-employment* in manufacturing, trade and services; and various forms of *informal wage employment* (including casual day-labourers in construction and agriculture, industrial outworkers, and more).

In developed countries, relatively few labour statisticians, economists or other observers use the concepts of informal sector or informal employment. Rather, the more common concept and term for forms of work that have been flexibilized or informalized is “nonstandard work”. Nonstandard work refers to forms of work that do not—or no longer—conform to regular, year-round, full-time employment with a single employer. The most commonly cited categories of nonstandard work in developed countries, for which official data are readily available, are self-employment, part-time work and temporary work. It is important to note that, in addition to self-employment, two categories of nonstandard work—day labour and domes-

tic work—that are often informal (that is, unprotected) are fairly common in developed countries. Also, some part-time and temporary workers in some developed countries are not covered by legal or social protections and could, therefore, be considered as informally employed.

Developing Countries

To date, relatively few developing countries have measured informal employment broadly defined and fewer still have measured trends in informal employment over time. This is because the expanded concept of “informal employment” was ratified only in 2003. However, an indirect measure of informal employment can be—and has been—used to estimate the size of informal labour markets and the informalization of labour markets over time: namely, estimating informal employment as the difference between *total* employment (estimated by labour force surveys or population censuses) and *formal* employment (estimated by enterprise surveys or economic censuses).

What follows is a summary of findings regarding the size of the informal economy in 25 developing countries (ILO 2002) and changes in informal employment over time in 20 of these countries (Heintz and Pollin 2003): Official national data were used to estimate informal employment in each of the countries using the indirect measure noted earlier.¹ Findings on labour force segmentation and average earnings are based on two recent reviews of available data (Chen et al. 2004, 2005).

Informal Labour Markets

Informal employment broadly defined comprises one-half to three-quarters of *non-agricultural* employment in developing countries: specifically, 47 per cent in the Middle East and North Africa; 51 per cent in Latin America; 71 per cent in Asia; and 72 per cent in sub-Saharan Africa. If South Africa is excluded, the share of informal employment in non-agricultural employment rises to 78 per cent in sub-Saharan Africa; and if comparable data were available for countries other than India in South Asia, the regional average for Asia would likely be much higher.

Some countries include informal employment in *agriculture* in their estimates. This significantly increases the proportion of informal employment: from 83 per cent of *non-agricultural* employment to 93 per cent of *total* employment in India; from 55 to 62 per cent in Mexico; and from 28 to 34 per cent in South Africa.

The main segments of informal employment, classified by employment status, are as follows:

Self-Employed:

- *employers:* owner operators of informal enterprises who hire others;

- *own-account workers*: owner operators in single-person units or family businesses/farms who do not hire others;
- *unpaid contributing family workers*: family workers who work in family businesses or farms without pay.

Wage Workers:

- *informal employees*: unprotected employees with a known employer: either an informal enterprise, a formal enterprise, a contracting agency or a household;
- *casual wage workers*: wage workers with no fixed employer who sell their labour on a daily or seasonal basis;
- *industrial outworkers*: subcontracted workers who produce for a piece-rate from their homes or small workshops.

While average earnings are higher in formal jobs than in informal employment, there is also a hierarchy of earnings within informal employment. In Tunisia, for example, informal employers earn four times the minimum wage and over two times (2.2) the formal wage. Their employees earn roughly the minimum wage, while industrial outworkers—mostly women home-workers—earn less than one-third (30 per cent) of the minimum wage. In Columbia and India, informal employers earn four to five times the minimum wage, while own-account operators earn only 1.5 times the minimum wage (analysis of national data by Jacques Charmes, cited in Chen et al. 2004).

In brief, within informal labour markets, there is a marked segmentation in terms of average earnings across the different employment statuses outlined earlier. Research findings suggest that it is difficult to move up these segments due to structural barriers (state, market and social) and/or cumulative disadvantage. Many workers, especially women, remain trapped in the lower earning and more risky segments. To statistically test whether there are structural barriers to mobility across the different segments will require better data on key variables—such as education or assets—across these different segments.

Informalization of Labour Markets

As noted earlier, there is a widespread assumption that the informal economy is countercyclical: that is, it expands during economic downturns and contracts during periods of economic growth. However, recent analyses of data over time from different developing countries suggest a more complex and dynamic picture, with substantial variation in patterns of informalization across countries. As might be expected, sharp economic downturns are associated with a rise in informal employment. But in some countries, steady rates of economic growth are associated

with an increase in informal employment. This is because certain forms of informal employment expand during downturns in the economy, such as survival activities and subcontracted and outsourced activities linked to formal firms trying to cope with recession. While certain other forms of informal employment expand during upturns in the economy, such as the more entrepreneurial small firms as well as sub-contracted and outsourced activities linked to the global production system.

Consider the findings from 20 countries in Asia, Africa and Latin America at two points in time—generally in the 1980s and the 1990s. For each of the countries, the rate of change in informalization is compared to the rate of growth in average per capita gross domestic product over the same time period (Heintz and Pollin 2003, cited in Heintz 2006). Most of the countries (14 out of 20) experienced growth in informalization; four experienced a decline; and two experienced little, if any, change. What is interesting to note, and which goes against the common assumption, informalization increased in three countries with respectable per capita growth rates (>2 per cent) and declined in two countries with poor per capita growth rates (<1 per cent). “These patterns suggest that informal employment has been increasing faster than formal employment, even in countries with strong rates of growth” (Heintz 2006:17). But the authors conclude that “[h]igher rates of growth are generally associated with smaller increases in the rate of informalization. At very high levels of growth, informalization may decline” (Heintz 2006:18; Heintz and Pollin 2003). But they also note that such cross-country comparisons do not include all types of informal employment: this is because the available data often exclude own-account production and informal wage employment, especially industrial outwork. High levels of growth driven by export production may be associated with increases in certain types of informal employment: notably, industrial outwork for global supply chains (see evidence from Tunisia in the following section).

In sum, cyclical patterns cannot fully explain the rate of informalization: Structural factors also play a role. When it comes to informal self-employment, there is a widespread notion that excessive bureaucracy and costly regulations are what drives informality. But economic liberalization is associated with fewer regulations, not more. So what contributes to *structural* informal self-employment? First, the markets in which the smallest informal enterprises compete are often not deregulated in at least the first generation of economic reforms: they often remain either outside the reach or control of government (for example, traditional street-trading in many countries around the world) or under the control of government (for example, minor forest products in India). Second, as noted earlier, people turn to self-employment in the informal economy when they lose a job (which happens under conditions of economic growth as well as economic decline or stagnation) or when they need to supplement their earnings. When it comes to informal wage employment, certain forms of subcontracted and outsourced jobs are associated with the global production system and trade liberalization.

Developed Countries

Few labour statisticians, economists and other observers in developed countries use the concepts of informal sector or informal employment: The more common concept is that of “nonstandard” work. And the most common categories of nonstandard work for which official data are available are: self-employment, part-time work and temporary work. Although not all part-time workers and temporary workers are informally employed, in the sense of being unprotected, many receive few (if any) employment-based benefits or protection.² Comparable data on other categories of employment that are even more likely to be informal in nature—namely, contract work, industrial outwork and casual day labour—are not readily available in developed countries.

In North American, European Union (EU), and other Organisation for Economic Co-operation and Development (OECD) countries, available evidence suggests that the workforce has become flexibilized or informalized. In these regions, statisticians and researchers use the concept “nonstandard” work for the forms of work that are flexible or informalized. The term “nonstandard work” as commonly used includes: (i) jobs that entail an employment arrangement that diverges from regular, year-round, full-time employment with a single employer without secure contract; and (ii) self-employment with or without employees (Carré and Herranz 2002). The common categories of nonstandard wage work are temporary work, fixed-term work and part-time work. Increasingly, interfirm subcontracted work in the service sector (such as janitorial services and home care) and in the manufacturing sector (such as garment-making and electronic assembly) are also included. However, data on the following categories of “nonstandard work”, which are very likely to be informal (that is, unprotected), are not readily available in developed countries: informal wage work for informal enterprises (employees of the self-employed), for households (domestic workers) or for no fixed employer (casual day-labourers).

What follows is a brief summary of trends in three categories of nonstandard work—part-time work, temporary work and self-employment—in Europe (Carré 2006; Carré and Herranz 2002).

Part-Time Work

Since the early 1970s, there has been a marked growth in the proportion of part-time workers in total employment. By 1998, part-time workers accounted for 16 per cent of total employment in EU countries and 14 per cent of total employment in OECD countries.

Temporary Employment

For the EU as a whole, and in a majority of EU nations, the share of workers in temporary employment, including both direct hire and agency hire,

increased from the mid-1980s to the late 1990s. By 1998, temporary employment accounted for around 10 per cent of total employment in EU countries.

Self-Employment

Self-employment, including both employers and own-account workers, has increased in many OECD countries over the past 25 years.³ Indeed, outside of agriculture, self-employment has grown at a faster rate than total employment in 14 (out of 24) OECD countries where data were available. Also, as self-employment has been growing, so has the share of own-account self-employment within total self-employment. As a result, in OECD countries today, more self-employed persons are own-account workers than employers.

Gendered Patterns

Informalization of Labour Markets by Sex

The last two decades have seen a marked increase in women's labour force participation: most significantly in the Americas and Western Europe, and more modestly in sub-Saharan Africa, Southeast Asia and East Asia (Heintz 2005; UNRISD 2005). Only in two regions—Eastern Europe and South Asia—has women's labour force participation rate actually fallen. The marked increase in women's labour force participation worldwide has given rise to the notion of the "feminization of the labour force". But this notion has been defined and used in two distinct ways. First, to refer to the situation in which the ratio of women's labour force participation rate to men's labour force participation rate increases over time. Second, to refer to a situation in which the structure of the labour force itself is "feminized": that is, when jobs take on features associated with women's work such as low pay, drudgery, uncertainty and precariousness (Heintz 2005; Standing 1989, 1999).

Whether or not there is a causal link between the increase in women's labour force participation and the growing precariousness or informality of work is not clear—and has been hotly debated. Are the expansion of women's labour force participation and the informalization of labour markets over the past two decades linked in some way, or do they represent parallel but distinct processes? The pervasive segmentation of labour markets by gender, which we will discuss later, suggests that women's labour did not simply substitute for men's labour. Rather, that there has been some parallel process at work creating low-paid and poor quality informal employment opportunities for (primarily) women (Heintz 2005; Standing 1989, 1999).

Estimates of changes over time in the degree of informalization within the female and male labour force are not available. However, a recent analysis of trends in the Tunisian labour market, with a special focus on informal

employment, suggests the kind of analysis required and the trends that might be found elsewhere.

Between 1975 and 1997, informal employment in Tunisia grew at a very fast rate. During the economic slump of the 1980s, the share of informal employment increased, accounting for almost 40 per cent of non-agricultural employment by 1989. This trend confirmed the conventional notion that the informal economy is countercyclical, expanding during economic downturns and shrinking during economic growth. However, during the rapid economic growth and trade liberalization of the 1990s, the share of informal employment grew even faster, accounting for over 47 per cent of non-agricultural employment by 1997. In brief, while informal employment grew at an annual rate of over 5 per cent in the late 1970s and 1980s, it grew at an annual rate of 7.5 per cent between 1989 and 1997 (Charmes and Lakehal 2006).

How can this apparent contradiction be explained? The authors make the case, with supporting data, that the distinction between informal employment *inside* the informal sector (that is, small non-registered enterprises) and informal employment *outside* the informal sector is behind this seeming contradiction. During the late 1970s and 1980s, it was largely informal employment *inside* the informal sector that grew. During the economic growth of the 1990s it was largely informal employment *outside* the informal sector that grew: notably, informalized and subcontracted labour for larger enterprises, most of it undeclared. By 1997, less than half of the informal workforce (46 per cent) was employed in small informal enterprises (that is, the informal sector), while over half (54 per cent) was employed as *undeclared informal workers* for both formal and informal enterprises, most of whom are women outworkers for export-oriented firms. In brief, the evidence from Tunisia suggests that, while employment inside the informal sector may be countercyclical, informal employment outside the informal sector may be procyclical (Charmes and Lakehal 2006).

The Tunisian example confirms what the cross-country analysis, summarized earlier, suggests: namely, that certain forms of informal employment—notably, subcontracted work linked to the global production system—expand during periods of economic growth, especially when growth is driven by trade and financial liberalization. What is important to note is that women workers tend to be overrepresented in global production systems, at least in the early stages of industrialization and trade liberalization, when a premium is placed on export-oriented light manufacturing and low-skilled (and low-paid) workers (Chen et al. 2005).

Informal Employment in Developing Countries by Sex

Informal employment is generally a larger source of employment for women than for men in the developing world. Other than in the Middle East and North Africa, where 42 per cent of women workers (and 48 per cent of

male workers) are in informal employment, 60 per cent or more of women non-agricultural workers in the developing world are informally employed. Among non-agricultural workers in sub-Saharan Africa, 84 per cent of women workers are informally employed, compared to 63 per cent of men workers; in Latin America, 58 per cent of women workers, compared to 48 per cent of men; and in Asia, 73 per cent of women workers, compared to 70 per cent of men workers (ILO 2002).

Segmentation of Informal Employment in Developing Countries by Sex

Available evidence from several developing countries suggests that, as a general rule, relatively high shares of informal employers are men and relatively high shares of industrial outworkers are women. In India, for example, 6 per cent of informal employers, 19 per cent of own-account operators, 16 per cent of informal wage workers and 59 per cent of industrial outworkers are women.⁴

In brief, men tend to be overrepresented in the top segments of the informal economy; women tend to be overrepresented in the bottom segment; and the relative shares of men and women in the intermediate segments vary across sectors and countries. Available evidence also suggests that there are significant gaps in earnings within the informal economy: informal employers have the highest earnings on average; followed by their employees and informal employees of formal firms; then own-account operators, casual wage workers and industrial outworkers. These two stylized facts are depicted graphically in figure 7.1.

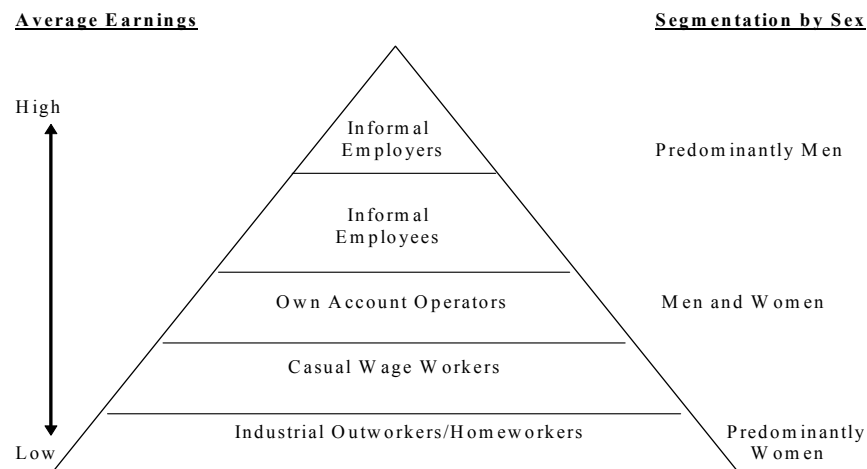


Figure 7.1 Segmentation of informal employment, by average earnings and sex.

The available data on poverty risk—that is, the likelihood that a worker from a given segment of the labour force is from a poor household—indicate a similar hierarchy. Workers in the formal economy, particularly in public sector formal jobs, are less likely than workers in the informal economy to be from a poor household. Within the informal economy, informal employees are more likely than their employers to be from poor households, own-account operators are more likely than informal employees to be from poor households and so forth down the segmentation pyramid illustrated earlier (Chen et al. 2005). However, analysing the poverty risk of workers, as opposed to their average earnings, is complicated by whether or not a worker is the sole earner, the primary breadwinner or a supplemental earner in her household. For example, because their earnings are so low, women industrial outworkers are likely to be supplemental earners in households with male earners. Whether or not an industrial outworker is from a poor household depends on whether the earnings of the whole household, including her earnings, fall below or above the poverty threshold. However, if she is the sole or primary breadwinner, the household of a women industrial outworker is very likely to be poor (Chen et al. 2005).

An additional fact, not captured in figure 7.1, is that there is gender segmentation and earning gaps *within* these broad employment status categories. Women tend to work in different types of activities, associated with different levels of earning, than men—with the result that they typically earn less even within specific segments of the informal economy. Some of this difference can be explained by the fact that men tend to embody *more human capital* due to educational discrimination against girls, especially in certain societies (for example, in North India and Pakistan). This difference can also be explained by the fact that men tend to have *better tools* of the trade, operate from *better worksites/spaces* and have *greater access to productive assets and financial capital*. In addition, or as a result, men often *produce or sell a higher volume or a different range* of goods and services. For instance, among street vendors in many countries, men are more likely to sell non-perishables while women are more likely to sell perishable goods (such as fruits and vegetables). In addition, men are more likely to sell from pushcarts or bicycles, while women are more likely to sell from baskets, or simply from a cloth spread on the ground.

In sum, there is a significant range of average earnings and poverty risk within the informal economy by employment status with a small entrepreneurial class (comprised of most informal employers and a few own account operators) and a large working class (comprised of most informal employees, most own-account operators, all casual workers and all industrial outworkers). There is also gender segmentation within informal labour markets, resulting in a gender gap in average earnings with women overrepresented in the lowest paid segments and earning less on average than men in most segments.⁵

Nonstandard Work in Developed Countries by Sex

Part-Time Work

In virtually all EU and OECD countries, the incidence of part-time work is much higher among women than men: in some countries it is twice as high. By 1998, women represented 82 per cent of all part-time workers in EU countries. Further, rates of part-time work are high for women, but not men, in their prime working years.

Temporary Employment

Temporary employment, like part-time work, is primarily a female phenomenon, although there is wide variation among EU countries. In all countries except Austria, the incidence of temporary employment among female workers is higher than among all workers. And, like part-time work, temporary employment is concentrated in the service-producing industries. Interestingly, in regard to temporary agency employment, women account for the majority of agency temps in countries where such employment concentrates in services, while men account for the majority of agency temps in countries where such employment concentrates in manufacturing and construction: that is, “the gender composition of employment mirrors that of the sectors in which temporary agency assignments take place” (Carré 2006:13).

Self-Employment

In 1997, women comprised one in three self-employed persons in OECD countries and this proportion is growing. For EU countries as a whole, the incidence of own-account work is greater for men (11 per cent) than for women (7 per cent). But, in some countries, a higher proportion of women than men are own-account work. Age is a factor in own-account work, with workers aged 45 and above more likely than younger workers to be own-account workers (Carré 2006).

IS FORMALIZATION THE ANSWER?

The Formalization Debate

Over the years, the debate on the informal economy has crystallized into four dominant schools of thought regarding the causes, composition and nature of the informal economy, and what should be done about it. The *dualist* school, popularized by the International Labour Organization (ILO) in the 1970s, sees the informal sector as comprised of marginal and survivalist activities—distinct from and not related to the

formal sector—that provide income for the poor and a safety net in times of crisis (ILO 1972; Sethuraman 1976; Tokman 1978). According to this school, the persistence of informal activities—and, thus, a dualistic labour market—is due largely to the fact that not enough modern employment opportunities have been created to absorb surplus labour in developing countries, due to slow rates of economic growth and/or faster rates of population growth.

The *structuralist* school, popularized by Caroline Moser, Alexandro Portes and others in the late 1970s and 1980s, sees informal enterprises and informal wage workers as subordinated to the interests of large capitalist firms, supplying cheap goods and services. In the structuralist model, in marked contrast to the dualist one, formal and informal modes of production are seen to be inextricably connected and interdependent (Moser 1978; Portes et al. 1989). According to this school, the nature of capitalist development (rather than a lack of growth) accounts for the persistence and growth of the informal economy.

The *legalist* school, popularized by Hernando de Soto in the 1980s and 1990s, sees the informal sector as comprised of “plucky” microentrepreneurs who choose to operate informally in order to avoid the costs, time and effort involved in formal registration (de Soto 1989).⁶ According to de Soto, cumbersome government rules and procedures create barriers to formalization and thus stifle the productive potential of informal entrepreneurs (de Soto 1989).

The *voluntarism* school, popularized by neoclassical and neoliberal economists across the decades, sees informal entrepreneurs as deliberately seeking to avoid regulations and taxation. According to this school of thought, informal entrepreneurs choose to operate illegally—or even criminally—in order to enjoy the benefits of avoiding taxation, commercial regulations, electricity and rental fees and other costs of operating formally (Maloney 2004). Some voluntarists see the informal economy as dealing with illegal, even criminal, goods and services and, therefore, refer to it as the underground or black economy.

Since these schools of thought focus on different segments of the informal economy—from survivalists to subcontracted producers and workers to independent entrepreneurs—they see different linkages between economic liberalization and informalization. The dualists argue that the informal sector is countercyclical, the structuralists highlight how informal workers and units are subordinated to the global production system, and the legalists and volunteerists focus on regulation and taxation. Each of the schools of thought has distinct notions of what formalization of the informal economy should entail, as follows.

- The *dualists* argue that governments should provide credit and business development services to informal operators as well as basic infrastructure and social services to their families.

- The *structuralists* argue that governments should address the unequal relationship between “big business” and subordinated producers and workers by regulating both commercial and employment relationships.
- The *legalists* argue that governments should introduce simplified bureaucratic procedures to encourage informal enterprises to register and extend legal property rights for the assets held by informal operators in order to unleash their productive potential and convert their assets into real capital (de Soto 1989, 2000).
- The *voluntarists* focus on bringing informal enterprises under the formal regulatory environment in order to increase the tax base and reduce unfair competition by informal enterprises.

Given the heterogeneity of the informal economy, there is merit to each of these perspectives as each school reflects one or another “slice of the (informal) pie”. But the informal economy, as a whole, is more heterogeneous and complex than the sum of these perspectives would suggest. Therefore, the common policy prescription of “formalizing the informal economy” needs to be reexamined to reflect all forms of informality.

Rethinking Formalization

To begin with, it is important to recognize that formalization has different meanings for different segments of the informal economy. To date, the formalization debate has focused primarily on the self-employed in informal enterprises; and often, more specifically, on microentrepreneurs who hire others. At a minimum, the formalization debate needs to distinguish between wage workers in informal jobs and self-employed in informal enterprises. Ideally, it should further distinguish between different segments of the self-employed and wage employed in the informal economy as each segment has its particular needs and constraints.

Second, it is important to ensure that formalization offers the benefits and protections that come with *being* formal and does not simply impose the costs of *becoming* formal. For the self-employed, formalization should not mean just obtaining a license, registering their accounts and paying taxes: these represent, to them, the costs of entry into the formal economy. What they would like is to receive the benefits of operating formally in return for paying these costs, including: enforceable commercial contracts; legal ownership of their place of business and means of production; tax breaks and incentive packages to increase their competitiveness; access to government procurement bids; membership in trade associations; protection against creditors and clear bankruptcy rules; and government contribution to the social protection of

themselves and their employees. What about informal wage workers? For them, formalization would involve paying taxes and making some kind of regular social security contribution. In return, formalization would mean obtaining a formal wage job—or converting their current job into a formal job—with a secure contract, worker benefits, membership in a formal trade union and government and employer contributions to their social protection (Chen 2006).

What is required is an approach to formalization of the informal economy that seeks to promote good or appropriate regulations—not deregulation or reregulation—and is comprehensive in design but context-specific in practice. A comprehensive design for formalizing the informal economy should include the elements listed in box 7.1.

Box 7.1 Formalization of the informal economy: A comprehensive approach

1. *Formalization of informal enterprises*

- Registration and taxation:
 - simplified registration procedures
 - progressive registration fees
- Legally-recognized property rights
- Benefits of operating formally:
 - access to finance and market information
 - access to public infrastructure and services
 - enforceable commercial contracts
 - limited liability
 - clear bankruptcy and default rules
 - access to government subsidies and incentives, including procurement bids and export promotion packages
 - membership in formal business associations
 - access to formal system of social security

2. *Formalization of informal jobs*

- Legal recognition and protection as workers
- Rights and benefits of being formally employed:
 - freedom from discrimination
 - minimum wage
 - occupational health and safety measures
 - employer contributions to health and pensions
 - right to organize and bargain collectively
 - membership in formal trade unions
 - access to formal system of social security

In formalizing specific groups of informal workers, policymakers and practitioners should choose appropriate elements from this framework and tailor interventions to meet local circumstances. Consider, for example, the specific conditions of several informal occupations in which large numbers of working poor women tend to be concentrated.

Street Vendors

The common problems faced by street vendors around the world include:

- insecure place of work, due to competition for urban space;
- capital on unfair terms, due to dependence on wholesale traders;
- uncertain quantity, quality and price of goods, due to dependence on wholesale traders;
- lack of infrastructure: shelter, water, sanitation;
- ambiguous legal status, leading to harassment, evictions and bribes;
- negative public image.

What do street vendors want in exchange for registering their businesses and paying taxes? They want:

- secure vending sites;
- access to capital on fair terms: a loan product tailored to their daily need for working capital;
- bargaining power with wholesale traders;
- infrastructure services at vending sites: shelter, water, sanitation;
- license to sell and identity cards;
- freedom from harassment, evictions and bribes;
- positive public image.

Except in societies where gender norms restrict women's mobility, women account for a major share of street vendors. However, with a few notable exceptions in mainly African countries, women traders are more likely than men traders to have the more risky work situations, by: operating from the street rather than a cart or stall; operating from an insecure or illegal space; trading in perishable goods; generating a lower volume of trade; working as commission agents or employees of other vendors; and not employing others to work for them (Cohen et al. 2000). Consequently, women vendors also tend to earn less than men vendors (Cohen et al. 2000).

Waste-Collectors

It is estimated that 2 per cent of the world's urban population lives off collecting and recycling waste (Medina 2007). Waste-collectors commonly suffer:

- very low average earnings;
- fluctuations in quantity, quality and price of waste;
- harsh working conditions and related occupational hazards;
- negative public image.

In many waste-collection communities, women and children often collect and sort the waste—thus adding to their exposure to the waste and associated health risks—while the men sell the waste. Since they have to move around different neighbourhoods to collect waste, women and girls face teasing, touching and other forms of sexual harassment (Paula Kantor, personal communication, 2005).

Given these conditions, many waste-collectors would like to find alternative employment opportunities. This can be done within the waste-recycling sector by training them in waste-recycling skills or by organizing them into cooperatives and negotiating contracts for these cooperatives to provide cleaning services to, or collect waste from, government and private offices or institutions.

What would formalization mean for those who continue to work as waste-collectors? It would mean:

- legal recognition and positive public image as waste-collectors (who contribute to the upkeep and cleanliness of the cities they work in);
- identity cards to protect them;
- bargaining mechanisms to negotiate with: (i) those to whom they sell the waste they collect, and (ii) municipal officials and police;
- organization and bargaining power;
- appropriate implements and protective gear (gloves and aprons) to help them avoid dangerous and toxic waste.

Industrial Outworkers

Around the world, women represent the vast majority (80 per cent in some countries) of industrial outworkers who work from their home (ILO 2002). Industrial outworkers, whether in the garment, shoe or electronic sectors, face a number of common problems:

- low piece-rates and earnings;
- irregularity of work;
- irregular and (often) delayed payments;
- costs of providing/maintaining workspace, utilities and equipment.

In addition, some endure harsh or dangerous working conditions: for example, shoemakers are exposed to toxic glues. Many also suffer sore backs and deteriorating eyesight from working in badly equipped and poorly lit workplaces (often their own homes).

What would formalization mean for industrial outworkers? It would mean:

- regular, secure and enforceable work orders;
- regular and timely payments;
- piece-rates that are equivalent to minimum wages;
- occupational health and safety measures;
- capital to improve their workspace (often their home) and upgrade their equipment.

In today's global economy, there is probably no greater difference in terms of market power and wealth than between the chief executive officer of a multinational corporation that sells garments, footballs or electronic goods, and the woman industrial outworker who stitches or assembles these goods for that firm in her home.

Construction Workers

In many developing countries, where the industry has not been mechanized, the construction workforce is comprised largely of casual day-labourers, often migrants. Many such construction workers are unskilled and engaged in lifting and carrying loads of cement, bricks and concrete. Except in societies where gender norms restrict women's mobility, women represent a significant share of the unskilled construction workforce.

What are the common problems of unskilled construction workers? They include:

- irregular days of work;
- low and erratic earnings;
- arduous and hazardous work: frequent accidents and occasional deaths;
- lack of occupational health and safety measures;
- lack of accident or disability insurance.

What would formalization mean to construction workers? It would mean:

- more regular work;
- higher wages;
- skills training: masonry, carpentry and other construction skills;
- safety regulations;
- accident insurance and workers' compensation;
- identity cards;
- registers or other proof of days of work.

Horticulture Export Workers

In Latin America and (less so) Africa, there has been a notable increase in women agricultural workers in the non-traditional agro-export sectors: specifically, in the production and packaging of fresh flowers, fruit and vegetables (see chapters by Deere and Whitehead in this volume; see also Barrientos and Barrientos 2002; Barrientos et al. 2004).

What are the common problems of women workers in these agro-export sectors? They include:

- temporary contracts;
- uncertain days and hours of work, associated with “flexible” contracts;
- piece-rate payments and low wages;
- occupational segregation by gender (especially in packing houses).

What kind of formalization would these agricultural workers want? They would want:

- permanent contracts;
- regular days and hours of work;
- wage payments and higher wages;
- opportunities to shift to better paid work within occupation.

Challenges to Formalization

Admittedly, implementing a comprehensive yet context-specific approach to formalization will not be easy or straightforward. Among the key policy challenges facing such an approach are what to do about informal employers. Many informal wage workers work for informal firms. The policy challenge is whether and how to make informal employers comply with labour regulations and offer their employees formal benefits and protections. This is what the ILO has referred to as “the dilemma of the informal sector” (ILO 1991). It is genuinely difficult for many informal employers to offer legal benefits and protection to their employees at their present level of operations and profits. This suggests that formalization may need to be sequenced as follows: by first providing incentives and benefits to informal enterprises that register and then progressively enforcing compliance with taxation and labour regulations (ILO 1991).⁷ But available evidence suggests that many informal employers are not poor (Chen et al. 2004, 2005). For this more entrepreneurial class of informal operators, the issue is less whether they are *able* to comply with commercial and employment regulations than whether they are *willing* to comply.

Another related challenge is what to do about *formal* employers who hire workers under informal employment relations or subcontract production to a chain of suppliers. Faced with global competition, formal firms or employers often prefer to hire workers under flexible contracts or to outsource or subcontract production. In today's global production system, suppliers are often small informal enterprises who, in turn, hire workers under informal contracts or subcontracts. Hence, for producers of labour-intensive products, such as garments, who operate in global markets where demand is sensitive to price, there needs to be simultaneous change in all countries, otherwise they will be squeezed out of the market if they are the only ones to have to increase their prices as a result of meeting higher labour costs.

In sum, both formal firms and larger informal firms need a special package of incentives and sanctions to encourage them to provide benefits and protection to their workers. Admittedly, there is the risk of offering unnecessary incentives for them to extend benefits/protection to their workers or creating perverse incentives for them to continue to deny benefits/protection to their workers. But, this risk notwithstanding, appropriate labour standards and social protection can, and should, be developed for informal wage workers through tripartite negotiations, including employers (formal or informal), the government and informal workers. The Self-Employed Women's Association (SEWA), the well-known trade union of women informal workers in India, has effectively negotiated with the government and employers/contractors to obtain wage increases, annual bonuses, health benefits and/or pension contributions for a wide range of informal workers, including: day-labourers in construction and agriculture and industrial outworkers who produce garments, embroidered goods, incense sticks and *bidis* (cigarettes) at home.

Those who run single-person or family businesses present a different kind of challenge. To begin with, they do not hire workers. Second, they often earn so little that they fall into the lowest tax brackets. What *are* burdensome to these operators are the bureaucratic regulations and fees related to registering their businesses. For them, formalization requirements need to be made simpler and less costly through, for instance, a single-window registry system and differentiated registration fees (that is, depending on the size, output or location of their enterprises). For them, formalization should be seen as an incremental process that begins by introducing appropriate incentives and benefits of formality and then progressively enforces compliance with the costs and regulations associated with operating formally. This would create the conditions under which the working poor in the informal economy would be entitled to the benefits of formality while, at the same time, being enabled to comply with the duties of formality.

Limits to formalization

As outlined in this chapter, formalization of the informal economy can, and should, take different forms, including: creating incentives for the informal

self-employed to register their enterprises and benefits for them once they do; and creating a mix of incentives and sanctions for employers, both formal and informal, to extend benefits to their informal workers.

However, the limits to formalization need to be understood. First, it should be recognized that formalization is *not* a one-time process involving a specified set of steps. Rather, formalization should be seen as a gradual ongoing process involving incremental steps and different dimensions leading towards varying degrees and types of formality. Second, it should be recognized that formalization will *not* proceed quickly or automatically for all those who choose to formalize. The bureaucratic procedures and incentives for registered informal businesses need to be retooled and streamlined. Labour standards and benefits for informal workers need to be carefully negotiated by employers, workers and government. Third, it should be recognized that formalization will *not* be feasible or desirable for all informal enterprises or all informal wage workers. Rather, it should be assumed that many informal enterprises and informal wage workers will remain informal or semi-formal for the foreseeable future. In other words, informality—in varying degrees and forms—is here to stay.

Other fundamental challenges, then, are to create more formal employment opportunities and to decrease the costs and increase the benefits of those who continue to operate informally or semi-formally.

BEYOND FORMALIZATION

Reorienting Economic Policies

Clearly, there are limits to thinking of formalization in narrow “one size fits all” or “magic bullet” ways. While streamlining registration procedures for informal enterprises and extending property rights to informal operators are critically important, they are hardly sufficient. The informal economy is simply too big, too heterogeneous and too segmented for simple solutions. The global development community needs to recognize that to reduce poverty and inequality, including gender inequality, it has to deal with the informal economy in a comprehensive way that goes beyond formalization *per se*. Too many people—especially the working poor and women in particular—earn their living in the informal economy for it to be treated as a legal problem requiring formalization or a social problem that can be redressed by social policies alone. The challenge is to reorient development strategies—and development economics—to deal front and centre with the informal economy.

To deal effectively with the informal economy—and those who earn their livelihoods in it—will require a comprehensive economic strategy with three interrelated components: (i) creating more employment opportunities through employment-intensive growth; (ii) formalizing informal enterprises and informal jobs through a context-specific mix of incentives

and regulations; (iii) improving conditions and increasing returns of those who continue to work informally.

Component (i) requires putting employment creation back at the centre of macroeconomic policies, ensuring that employment is labour-intensive and targeting investments at low-income communities and under-developed areas. Component (ii) requires implementing context-specific elements of the comprehensive approach to formalization outlined earlier. Component (iii) requires a complimentary set of policies to help those who continue to operate informally improve their working conditions and get higher returns to their labour by increasing assets and competitiveness, assuring better terms and conditions of work, securing appropriate legal frameworks and addressing risk and uncertainty.⁸

Reforming the Regulatory Environment

An essential dimension of this reorientation of economic policies is the reform of existing laws, regulations and institutions. This does not mean deregulation but *appropriate regulations*. As the evidence presented in this volume has highlighted, work is increasingly informal in today's global economy, rendering obsolete many of the features of existing legislation, regulations and institutions modelled on the modern industrial era job. To legitimize and protect all types of workers today will require, in the end, reforming the laws, regulations and institutions that govern both commercial and employment relations. Laws, regulations and institutions governing commercial relations need to reflect the reality that most economic units are very small with few hired workers and that many working poor operate on their own account. Similarly, laws, regulations and institutions governing employment relations need to reflect the reality that most wage workers are not formal employees. Also, biases in existing laws, regulations and institutions that favour large enterprises over small enterprises, formal workers over informal workers and men over women in both categories need to be addressed. In the absence of new more appropriate laws, regulations and institutions, most of the working poor in the informal economy will remain unprotected, insecure and vulnerable.

Changing the existing regulatory regime should not be seen simply in "either-or" terms—regulation versus deregulation. The goal is, rather, appropriate regulations. Changing the existing regulatory regime in appropriate ways should not be seen as a pipe dream. Proposals have been made and measures have been taken to deal with the growing numbers of nonstandard wage workers in developed countries. To address the new employment relationship in the United States, which renders obsolete many features of the existing labour law regime, several types of legal reforms have been proposed and/or tested: benefit portability and broader safety nets; new anti-discrimination strategies; the legal right to organize across employer units; broader notions of bargaining units; and labour organizations that operate across industries and across firms in local or regional geographic areas (Stone 2004).

The EU has issued directives on part-time work (1997) and fixed-term employment (1999) to uphold the principle of “non-discrimination” between such workers and workers in formal contracts. The extent to which workers in part-time and fixed-term jobs are protected by these directives depends on the degree to which these directives are implemented in member states as well as pre-existing national regulations or collective bargaining agreements in those states. In particular, eligibility criteria such as mandated thresholds of employment continuity, work hours and years of experience need to be adjusted to ensure part-time and fixed-term workers are eligible for social protection measures such as unemployment insurance and pensions (Carré 2006).

Some EU countries have extended the right to representation in collective bargaining arrangements to nonstandard workers. In some EU countries, depending often on their length of experience, fixed-term workers have the right to attend meetings of workplace representative bodies as well as to vote and present their candidacy in elections. Temporary agency workers tend to participate in representation structures, if any, within the temporary agency itself, rather than in that of the user firm. In several countries, union membership is not a precondition for coverage under collective bargaining agreements. For the self-employed, the main option is belonging to, or building, an association of similar workers. But there are a few examples of trade unions reaching out to and incorporating the self-employed (Carré 2006).

In developing countries, there have also been efforts to extend existing labour and social protection regimes to cover informal workers. In Ghana, the Ghana Trade Union Congress (GTUC) carried out a review of national labour laws and found that the laws were outdated, fragmented and did not match either the work realities or the Ghanaian constitution. The GTUC resolved to push for reforms of existing laws to extend protection enjoyed by formal workers to informal workers. The resulting New Labour Act (2003) was negotiated through a tripartite process involving the government, trade unions and employers. The act allows temporary and casual workers to benefit from provisions of collective agreements on equal pay for work of equal value, access to the same medical provisions available to permanent workers and a full minimum wage for all days in attendance and public holidays. In addition, the act mandates that a temporary worker employed by the same employer for a continuous period of six months or more must be treated as a permanent worker (Kofi Asamoah, personal communication, 2004, cited in Chen et al. 2005; Owusu 2003).

In India, a national policy on street vendors was officially adopted in early 2004. Jointly drafted by the Government of India and the National Association of Street Vendors of India (NASVI), this policy includes provisions mandating legal status, special hawking and vending spaces, fee-based licenses, organization and representation and social security

and financial services for street vendors. Other bills which would provide social protection to, and guarantee minimum working conditions for, all informal workers were being debated in the Indian parliament in late 2007.

Empowering Informal Workers

To promote and sustain this major reorientation of economic policies and regulations, two preconditions are essential. First, increased *visibility* of informal workers—especially working poor women and men—in labour force statistics and other official data used in formulating policies. Second, the *representative voice* of informal workers—especially working poor women and men—in the processes and institutions that determine economic policies and the formal regulatory environment. Arguably, official visibility and representative voice are the two most *essential* and *enabling* dimensions of formalization for the working poor in the informal economy. Being visible in official statistics and to policymakers, and having representative voice in policy-making institutions and processes is what will ensure that the working poor can demand and ensure that both formalization per se and the broader economic strategy outlined earlier meet their needs and suit their circumstances.

Again, increasing the voice and visibility of informal workers should not be seen as a pipe dream. Over the past two decades, organizations of informal workers have been coming together to form a growing international movement of informal workers. There is now a global alliance of street vendor organizations (called StreetNet) as well as national and regional networks of organizations of home-based workers (called HomeNets) (see chapter 6 in Chen et al. 2005). And, over the past decade, concerted efforts have been made by the ILO, the International Expert Group on Informal Sector Statistics and the Women in Informal Employment: Globalizing and Organizing (WIEGO) network to improve statistics on informal employment, and to make these accessible to informal workers and their organizations (see chapter 4 in ILO 2002).

Engendering the process

Further, it is important to recognize that both informal and formal markets are gendered institutions: that there is gender segmentation and a gender gap in earnings/pay within both informal and formal labour markets. In the informal economy, women are concentrated in the segments of the informal economy associated with the lowest earnings and highest risks. But even when women and men do similar kinds of informal work, there is often a gender gap in earnings.

In part, this gender gap in earnings reflects differences in the amount of time that women and men are able to spend in paid work. Most societies

around the world share a common gender division of labour whereby women are associated with reproduction (unpaid care work) and men with production (paid market work). As a result, many women are forced, or conditioned, to engage in paid employment that is home-based. Formalization should include the provision of childcare services to allow women the choice of whether to engage in paid work outside their homes. In addition to the greater demands on their time, women's access to property is typically less than that of men and often mediated through their relationship to men; women's access to education, finances and other resources are typically less than that of men; and women often face greater social constraints on their physical mobility than men. Formalization could address these constraints as well.

BEYOND FORMALITY AND INFORMALITY

In closing, it is important to consider that informality may not be the problem, and that formalization may not be the answer. After all, in developing countries, the majority of all workers and the vast majority of the working poor, especially women and other disadvantaged groups, work in the informal economy. And in developed countries, nonstandard work is expanding. After all, many of the existing formal economic institutions are now obsolete, modelled in the mid-twentieth century on mass production, large factories, firms and so-called "modern" jobs in industrialized countries. Given the persistence and growth of informal employment in developing countries—and the informalization of once modern jobs in developed countries—much of economic reality in the new millennium does not fit the twentieth-century industrial model. Imposing the existing narrow set of formal economic institutions on the large diverse set of informal economic activities may be neither desirable nor feasible. What is needed are twenty-first century institutional arrangements—a creative mix of formal and informal—for twenty-first century economic realities.

NOTES

1. This summary is based on recent analyses of available national data, as indicated, as well as earlier summaries of these analyses in Chen and others (2004, 2005). The authors of ILO (2002), as well as Heintz and Pollin (2003), analysed a common set of official national data collected and compiled by Jacques Charmes.
2. It should be noted that part-time work is often not informal (that is, unprotected). In the Nordic countries, part-time work is often long-term with social protection. In the United States, however, part-time workers are offered very few benefits: In the mid-1990s, less than 20 per cent of regular part-time workers had employer-sponsored health insurance or pensions (Hudson 1999).
3. Statisticians distinguish three main subcategories of self-employment: (i) "employers", the self-employed who hire others; (ii) "own-account workers", who do not hire others; and (iii) "unpaid contributing family workers".

However, many statistical analyses, such as those by the OECD reported by Carré (2006), exclude unpaid family members because they are considered “assistants”, not “entrepreneurs”. Since the majority of unpaid family workers in most contexts are women, this exclusion understates the real level of women’s labour force participation and entrepreneurship (Carré 2006).

4. These figures were computed by Jeemol Unni, using the individual records of the Employment and Unemployment Survey, 1999–2000, 55th Round of the National Sample Survey Organization, New Delhi.
5. For a detailed analysis of available statistics on the gender segmentation of the informal economy and the linkages between working in the informal economy, being a woman or man and being poor, see Chen and others (2004, 2005).
6. In a similar vein, neoclassical and neoliberal economists argue that labour market regulations (for example, dealing with minimum wage or hiring/firing) encourage employers to shed workers or to hire workers under informal contracts, thus justifying the deregulation of labour markets.
7. For a similar argument, including the need for government industrial policies, see Tandler (2004).
8. For a detailed elaboration with good practice examples of the comprehensive yet context-specific response to informal employment, see Chen and others (2005).

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