



The State of the Informal Economy

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This policy brief addresses problems related to economic and labour market policies, specifically those that affect the poor and marginalised. A key problem is the appropriateness of viewing the economy as a dual economy, made up of a 'first' and 'second' economy. This perspective is problematic as renders elements of the 'second' economy invisible, and therefore outside the mainstream of economic and social debate. One of the concrete expressions of this is the lack of government support for the informal economy.

Policy focus

The conceptualisation of the 'first' and 'second' economy tacitly acknowledges the failure of trickle down economic growth policies and informs much of government's more recent emphasis on poverty alleviation. This dualism allows the government to argue that its economic policies for the first economy have been successful and enable it to address issues of poverty and unemployment in the second economy now that the first economy is stabilised. There is a general agreement on the need for economic intervention, particularly to boost incomes at the lower levels, but perceptions of the economy and the relationship between the first and second economies

influence policy interventions and outcomes.

In November 2003 President Mbeki stated that 'The second economy (or the marginalised economy) is characterised by underdevelopment, contributes little to the GDP, contains a big percentage of our population, incorporates the poorest of our rural and urban poor, is structurally disconnected from both the first and the global economy and is incapable of self generated growth and development' (Address to National Council of Provinces). Our research on the informal economy shows that this is not all necessarily the case.

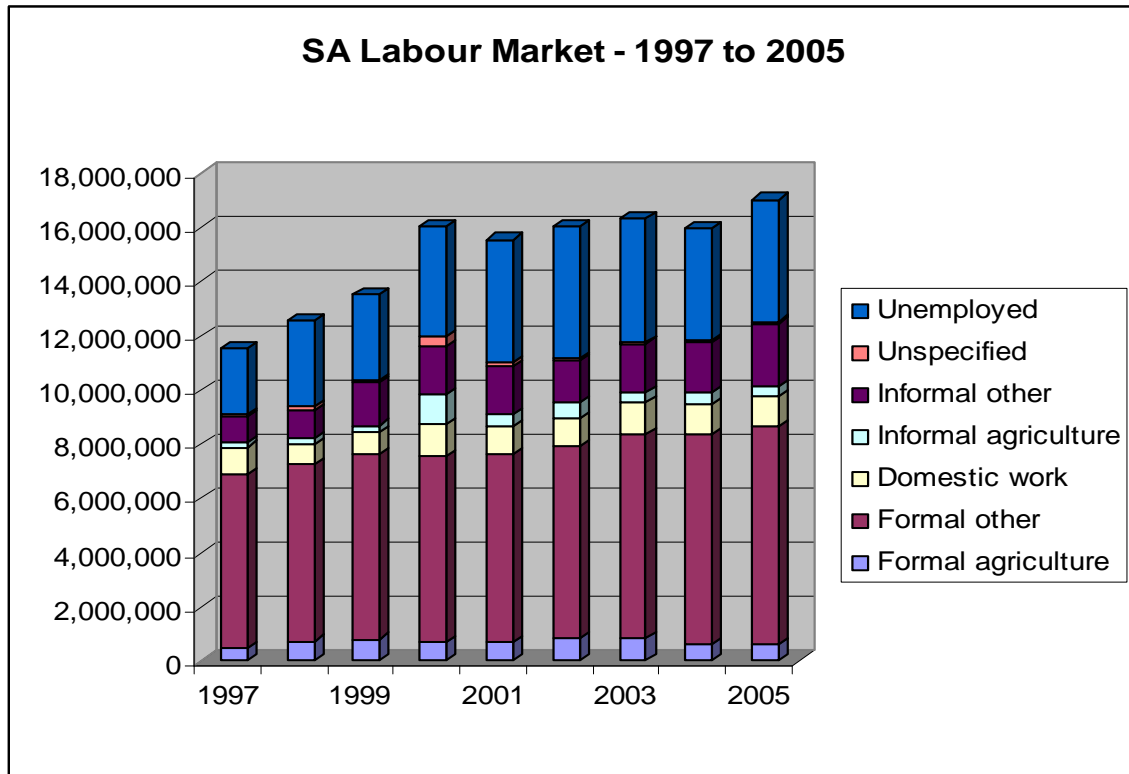
What constitutes the informal economy, and what is its contribution?

1. Informal activities encompass many different types of economic activity, different employment relations and activities with different economic potential – features that are not adequately captured by the term informal sector.

2. The informal sector is expanding. Calculations based on the October Household Survey (1997-1999) and the Labour Force Surveys (2000-2005) shows that employment in the informal economy increased from 965,000 in October 1997 to just over 2.3million in September 2005 (figure 1.)



Figure 1: Trends in the South African Labour Market, 1997-2005



Source: Adapted from Devey *et al.* (2006) and Skinner and Valodia (2006)

3. It is concentrated in trade with just under half of all informal workers located in this sector. There are significant numbers in construction, manufacturing and services. The majority are poor and black, with women represented in the less remunerative tasks.

4. Contrary to popular belief, figures from various studies show that the informal economy contributes somewhere between seven and twelve percent of GDP.

5. The 'second economy' is far from being structurally disconnected from the

mainstream of the economy. Instead, multiple forward and backward linkages exist between formal and informal activities. Data from the Labour Force Survey shows that there is a surprising level of churning within the labour market, with the status of more than half the workers having changed at least once in the period under analysis (February 2002 to March 2004). Another study suggests that capital moves between the two sectors because households that have some form of regular income are most often also involved in self-employment. Much of the 'formal economy' is becoming informalised.



What are the implications for policy?

Policy should take the needs of survivalist workers and the informal economy into account more than it has done up to now. Research shows that government policy for the 'second economy' is either absent, or where it does exist, is either piecemeal or ineffective. Analysis of DTI funding allocations for the period 1994-2003 shows these tended to favour established Small and Medium Enterprises rather than 'survivalist enterprise, women entrepreneurs and rural SMEs. Research undertaken in Johannesburg and Durban shows that there is little or no training support for workers in the informal economy.

Policy analysis and intervention: changing the framework to include the poor.

Internationally there is a trend towards applying the commodity chain or value chain approach to growing the informal economy. This view necessitates seeing the informal economy as an integral part of the economy and identifying those working in the informal economy at each stage of production. Use of a sectoral/commodity chain approach allows the identification of key policy level and

project interventions, in order to expand the sector and enhance the incomes of those working within it. Sectoral analysis of this kind has already been applied to the traditional medicine sector in KwaZulu-Natal. Similar sectoral analyses should be conducted in the segments of the informal economy that both contribute to economic growth and which employ large numbers of people, such as clothing, crafts, fruit and vegetable distribution and waste collection.

This policy brief draws on Devey, R., Skinner, C. and Valodia, I. (2006). *The State of the Informal Economy*. In: Buhlungu, S. et al (eds) *State of the Nation: South Africa 2005-2006*.

Further Reading:

Devey, R., Skinner, C. and Valodia, I. (2006). Definitions, data and the informal economy in South Africa: a critical analysis. In: Padayachee, V. (ed.) *The Development decade: Economic and social change in South Africa 1994-2004*, Cape Town: HSRC Press, p.302-323.

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