THE INFORMAL ECONOMY: CONCEPTUAL BACKGROUND AND THEORETICAL FRAMEWORK

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Abstract: The concept of informal economy first appeared in 1973 in a report by the International Labour Office (ILO), defined as an economic activity, which takes place within the informal sector and it is unregulated by law but governed by custom or personal ties. As a scientific research theme is quite young in economic and sociological spheres, but in the last four decades a vast literature has gathered on this subject, although there are missing the studies which synthesize the conceptual approaches and theoretical visions. The purpose of the present paper is to give a large scale synthesis through a literature review about main theories, models and research methods analysis and synthesis on the informal economy, taking into consideration that it has been a controversial subject worldwide in the last decades.

Keywords: informal economy, formal economy, theory of informal economy, definition of informal economy, precarious economy.

Introduction

This paper’s main objective is to offer a general conceptual and theoretical background of the informal economy and a short contextualization of this concept from Romania point of view. The structure of the study follows the above mentioned objective: a conceptual description, presentation of the main theories and a Romanian contextualization.

Informal versus formal: a conceptual background

In the special literature about informal economy (Hart, 1973; Portes, 1994; Centeno & Portes, 2003; Harding–Jenkins, 1981; Sassen, 1992, 1994; Busse, 2001; Offe & Heinze, 1992; Sik, 1996; Adler-Lomnitz & Scheinbaum, 2004) the variety of definitions and approaches is
characteristic. In the most of the definitions, the informal economy sphere covers all illegal economical activities along the formal-informal duality. Beyond that, the authors shade the definitions, which results usually overlap. Anyhow is not clear the limitation: the household economy appears as black economy, the contraband activity appears as non defined informal work. It is also problematic, not evident the definition of gray economy. But the sets of those economical activities, which results along the interests of employers, employees and clients, get the underground, illegal or informal economy label (Portes, 1994:426-427).

The concept appeared first in the context of the Third World. Keith Hart mentioned it (Portes, 1994:426-427; Harding–Jenkins, 1989:7-14) and gave a dual model of incomes on the urban labour market: the wage/salary and income of self-employed status. The informal attribute belongs to the latter mentioned, and is characterized by intense dynamism and diversity. The concept became later institutionalized, lost its dynamic character, and as a result of redefinition the informal attribute became the synonym of poverty and unemployment, so the informal economy belonged only to a specific urban way of life (Portes, 1994; Harding & Jenkins, 1989).

The representation of informal phenomena in negative light leads to its redefinition. The researcher recognized, the Third World context is false, because the phenomenon of informal economy is present in the economical system of developed industrial societies. But to the scientific investigation the relevant system of clear definitions is required. The conceptualizations’ most important representatives in the international panels are Edgar L. Feige (1990), Saskia Sassen (1992), Jonathan Gersuny (in Spéder, 1993; in Harding-Jenkins, 1989), Manuel Castells (1992), Alejandro Portes (2003), Claus Offe and Rolf G. Heinze (1992), Philip Harding and Richard Jenkins (1989) etc.

According to Feige (1990) all economical activities, which are not controlled by the state, are going together with informal sphere. She gives a useful taxonomy of the phenomena and specifies those social grounds, where these types of activities happen. The starting point of the classification is the underground economy as an umbrella concept. The different informal activities are labeled under the aegis of this umbrella concept. The first group covers the notion of the illegal economy, which includes the distribution of illicit and indictable goods and

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1 This concept appears by Saskia Sassen (1992, 1994) also.
services. The *unreported economy’s* components are those activities, which avoid the rules of code. The *unrecorded economy* more or less corresponds to the previous, but approximates from the side of institutions, including e.g. the false statistics of administration. The *informal economy* covers those activities, which avoid the rules and therefore they are excluded from the protection of administration and the system of contracts, credits and social security (Portes, 1994:428-429; Harding & Jenkins, 1989:84).

The sociologists recognized that the legal and criminal categories, just like normal and abnormal, must be redefined. An analogy can be identified: while illegal economy means the production of illicit goods and services, informal economy concerns the production of permitted goods and services. Castells and Portes (1989 in Portes, 1994) give a clear delimitation and definition: the basic difference between formal and informal resides in the *mode* how the goods and services were produced *not in the nature* of final products. They suggest a triple distinction of economical activities: *formal, informal* and *illegal*. The explicit delimitation allows the systematical exploration of differences and correlation of reciprocal economical relations. So the typical economical spheres, the modes of production and redistribution and the final products are characterized along the dimensions of *permitted* and *not permitted*. The above mentioned activities are characterized with the following parameters: in the formal economy both, the final product and the mode of production are licit; while in the informal economy the final product is licit or permitted, the mode of production is illicit; the final products and the mode of production are illicit, not permitted in the illegal/criminal economy.

This description gives us a functional approach of the phenomena, allocates goals for the different types of economical activities. These kinds of activities – informal and illegal- actually can serve the individuals’ or households’ survival in the process of production and marketing of goods and services (Portes & Castells & Benton, 1989 in Portes, 1994). In practice, the distinction is not so clear; this is an ideal-typical approach, as the same job representing survival for the informal worker is illegal activity for his employee etc.

Sassen’s conception (1992:79-88) is analogous, interprets the phenomena in the context of post-industrial societies (excludes the exclusivity of the Third World), emphasizes the entity of formal and informal categories. Without institutional/formal frame informal sphere does not exist, emphasizing the importance of rethinking the existing economical theories. In Hungarian
literature among others Spéder Zsolt (1993) reveals this idea. The underground economy as umbrella concept is also used by Sassen as a category of uncontrolled economical activities; who, similarly to Castells and Portes describes it with three components: illegal/criminal activities, different forms of tax evasion and informal economy. Sassen raises the issue: if the criminal economical activities are labeled as underground economy, will the informal be part of the formal? The question is: based on the described logic why is informal economy not part of formal economy? (Castells & Mollenkopf, 1992:79-88; Sassen, 1991) As we can see, Sassens’ approach also shows the doubtfulness of the definitions. In reality, in most of the situations the underground as a label is entitled to those economical activities that are out of state control. This umbrella concept guarantees the distinction of non formal activities, which differ in the nature and mode of activities and final products.

**The theories of informal economy**

As we described above in the conceptual background, „officially”, the informal economy concept had been developed for the first time by Hart (1973:61-89) within his report to ILO, describing the urban sub-proletariat, proving that the majority are not included by the employees on labour market. After this edition, the informal sector had been described in an optimist vision and it was recommended to support it, but once the concept had been institutionalized, its positive and dynamic presentation became a bureaucratic one. Within the ILO publishing works, labour employment in the informal economy sphere was constantly identified as an under-employment, and it was suggested that this fact is affecting the workers, which are not able to benefit from the modern economy. But this featuring and quasi-negative presentation of the informal sector within the poverty context was contested by other researchers, militating for an alternative attitude for this phenomenon, underlying that he informal activities are manifest signs of the entrepreneurship dynamism. This re-defining trend had as result a new conception. It was recognized the fact that the informal issues and characteristics from the under-developing world are also present within the modern, developed countries’ economy. But it is necessary to systematize the already used definitions. For example, the representatives of this thinking are: Feige (1990), Sassen (1992), Castells and Portes (1989, 1992, 2003), Offe and Heinze (1992),
Harding and Jenkins (1989) and many others. Within the ample informal economy redefining process, Castells and Portes (1989) are stating the difference between formal and informal: according to them, the primordial difference consists not in the final product nature (which may be formal or informal), but in the manner it had been manufactured, or it had been the object of an economic trade (see Castells & Portes, 1989; Portes, 1994; Portes & Haller, 2005:405). They propose a triple differentiation as in this way, the concepts of formal, informal and illegal allow to reveal the differences within their close relationship. During the last decade all over the world, the interest for the informal economy renewed due to the fact that first of all the informal economy not only increased, but also appeared in new developments located in different/unexpected places emerged; secondly, despite the debate on its defining features, supporting the informal enterprises and the improvement of working conditions at the informal jobs are more and more viewed as growth promotion and poverty decreasing ways. This thinking involves a more expanded defining way by admitting the structural segmentation and assumptions reviewing on the defining characteristics of the informal economy (Chen M. A., 2006). By this study we are joining to the idea, which is underlining the fact that the informal economy is a constitutive part of the economical development, it is not a phenomenon on the way of disappearance, more over it knows a continuous growing; it cannot be ignored by the decision makers, governments, specialists, activists. According to Chen M. A. (2006) a very well grounded and informed political approach has to became aware that the informal economy is very diversified, covering a wide range of activities (starting the surviving strategies toward the dynamic enterprises), is caused by many factors, may contribute to the poverty decreasing and is also affected by the public policies and legislation in force, but is differently affected as the formal economy. Further to the theories presentation we review the views (and also the critics) of the dualist school, structural school (the dynamic links between formal and informal) and institutional prospective, role of trust, of social capital and informal social networks.

The Dualist School: it treats the informal economy within the undeveloped countries, and subscribes to the idea that the informal sector is composed by marginal activities – different from the formal economy - assuring incomes for poor people and a safety network in crisis times. According to this school thinking, the informal economy represents a stage in a country development, is mostly due to the lack of modern working opportunities giving the ability to
engross the labour excess caused by the slow rhythm of economic growth and the rapid rhythm of population growing. According to the dualist thinking, the informal sector acts as a reserve, safety solution, absorbing or integrating the labour force excluded from the labour market by restricting the formal sector and offering a reserve labour during the expansion periods of the formal sector. Simultaneously the informal sector offers affordable goods and services for the marginalized people, contributing to their social integration (Chelcea & Mateescu, 2004:8-9). As a consequence, the informal sector is identified as a sector which is decreasing simultaneously with the formal sector increasing; it is a parallel developed sector to the formal one, what is not formally integrated, becomes informal (Bhattacharya, 2007).

One of the Dualist School critics is Sethuraman (1981). Having in view the prospective formal – informal discord, the dualist thinking identifies the urban economy as a continuum, where the enterprises and activities part of the two sub-systems are differentiated according to certain features, as: the way of developing the production, the organization way and operations proportions. According to Sethuramans’ view, it is requested a more precise definition, because the „delimitation” features for the two sub-sectors suggest the fact that the informal enterprises are emerging in spite of the lack of requested financial capital and professional qualification too, or that these entities are not even real enterprises according to a conventional meaning of the word, rather some production units evolving during an evolution process.

At the end of the theoreticians optimism this time less normative as the dualist thinking, has been directed toward the real possibilities concerning the research questions and the phenomenon issuing. One of the greatest names of these debates is Hernando de Soto (1989) with his book „The other path”. His book was born from the doubt he had in front of the following three theorems: clandestinity means only poverty and marginalization, the Peru culture is incompatible with the enterprising spirit and the economic systems of the most developed countries in the world, all bad things from the Latin America are due to the foreign forces and not to the domestic errors.

The Structural School, promoted by Castells and Porters (1989) is subscribing to the idea that the informal sector is consisting in subordinated units (micro-firms) and workers, accomplishing costs decreasing, so being part of the big capitalist firms’ competitive growth. Within the structural model, contrasting with the double nature model, the production forms and
modalities are not considered just as co-existent, but also closely related and interdependent. According to this view, the capitalist development nature (and not the lack of economic development) is explaining the informal production relationships development persistence and growth. While the previous approaches defined the informal sector according to its characteristics, as economic activity type, company size, social status of the workers, or the invested capital amount, this approach champions (Portes & Sassen-Koob, 1987; Castells & Portes, 1989; Benton, 1989; Fernández-Kelly & Garcia, 1989; Sassen-Koob, 1989; Sassen, 1992) are making a distinction concerning the informal economy by production and trading processes. So, the informal economy includes all income generating activities which are effectively regulated by the state within the social environments where similar activities are settled (Castells & Portes, 1989). Based on this definition, the sociological structural approach states the fact that the informal economy is not strictly associated with the underdevelopment of the third world countries, contrary persisting even within the modern, post-modern or post-industrial sectors of the economy. Portes and Sassen-Koob (1978) are assessing the informal economy relationship within the industrial development theories context, the activities character and dynamic and their development. They consider as informal, the above mentioned working situations where the work and capital are not clearly separated, the contractual relationship among them is missing, there is a paid labour, and also the working and payment conditions are missing. So definite or identified, the informal sector of economic activity is heterogeneous considering a structural point of view, and involves activities as: subsistence, small scale production and commerce, subcontracting to quasi-clandestine companies and home workers.

Logically, the institutional prospective was supposed to be included also as a critical view by the informal economy dualist assessment. The issue was separately treated while within the institutional approach other newer theoretical issues concerning the informal economy have been also introduced, as the role of trust, of social capital and networks in the informal economy. Sindzingre (2006:58-74) emphases the idea that instead of formal – informal discord, phenomena considered as informal may be explained by other features as: the credibility and feasibility of institutions and contracts, either formal or informal ones. The social capital and social networks role represents an important concept in studying the informal economy. Within the new contemporary regulations and globalization context, the informal economic organization forms
became quite popular, profoundly inter-connecting with the official economies, consequently the „old” notion of informal sector and informal economy raised questions. Both in the industrialized societies and the developing ones the informal economic arrangements based on links among relatives, kinships, friendship, community connections interfered within the contemporary economies as subcontracting, illegal work, transnational migration etc. as result of state involving diminishing in the population welfare and labour employment. Within this context researchers as Portes (1994) reached to the conclusion that the formal – informal distinction overcame the utility. Using the social networks theory the ability of social forces assuring a settlement framework flexible integrated within the fellowship and confidence is assessed. So, the social networks are considered more a social capital source, able to strength the efficiency and independent state economic development. Better to represent the economical informality in the regulation absence terms, the social networks is developing the portrait of informal economy as an alternative form of settlement, operating beyond the settlement frame offered by the state.

**Informal economy in Romania: social-economic context**

Based on didactic reasons three stages are concerned: the informal economy before 1989, the informal economy during the transitory period just after 1989 and the informal economy during the present times – new faces of informalisation. The scientific contribution of this chapter consists entirely in the autochthonous scientific literature synthetizing, the presentation of studies and researches developed in Romania, the inventory of great authors dedicated to this theme research from different expectations. The base studies, articles and books we took as milestones represent the autochthonous professional literature in the field (Chelcea & Mateescu, 2004; Dobrescu, Rughiniş, & Zamfir, 2000; Hunya, Réti, R. Süle, & Tóth, 1990; Neef, Stânculescu, & Adair, 2007; Sik, 1996a, 1996b, 2006; Stânculescu, 2004; Stânculescu & Ilie, 2001; Mungiu-Pippidi, Ioniţă, & Mândruţă, 2000; Verdery, 1996; Êkes, 1993).

We may not talk about sociology research of this phenomenon in Romania before 1989, while officially there was no secondary or informal economy. Concerning this period of time there are no available scientific tools for researches synthesizing, our work was restricted to informal activities inventories and especially to develop their context within the social-economic
environment before 1989, what is an important issue, since the past of the communist economy is reflected also in nowadays. Anyway, the discourse concerning the communist informal economy is not denied by the secondary economy concept, which although it was not present in the communist economy, stroke roots within the public discourse. In the Romanian communist context we may agree to the conclusion of Girasek and Sik (2006:75), according to which the informal economy before 1989 functioned as an inventive response to the rigidity of the planned and controlled economic system, a tool for increasing the incomes – not necessary in currency.

The post-communist period has its own special characteristics. Within the economic transition context, the informal economy may be considered as the previous regime heritage. The practice, as the economic elite saved their economic connections reviving them within the market economy, is relevant also for the informal surviving strategies. This means that people involved in the invisible economy during the communism are using their practice, connections and information sources in order to assure their surviving within the structural change in Romania (Péter, 2003). Coming back to Girasek and Sik (2006:75): during the post-communist transition period, unlike the period before 1989, the informal economic strategies „invented” within the new economic context have the role of a defense mechanism – facilitating the advantages in the social-economic situation after 1989.

In spite of the fact that here is no clear demarcation line between the post-communist period and the period after the post-communist period, from didactic reasons and not only, it was treated separately having in view the informal economy, sketching the social-economic profile of the post-modern informalisation within the Romanian paradox. But many times, when characterizing the Romanian society, we fall into trap of the communism/post-communism/political-economic transition when motivating certain social phenomena, not taking into consideration the world wide economic-social trends strongly influencing the structure and evolution of social processes in Romania.

An OECD report on informal employment signed by Parlevliet and Xenogiani (2008) shows that informal employment persists in Romania. The authors identify two main groups involved in informal employment: there are people working informally because they have no real alternative and informal work is a survival strategy and there are people who deliberately avoid taxes and social security contributions. The first group includes some forms of informal
employment in agriculture and unpaid family workers. The second group includes unregistered companies or those companies that do not declare their workers they hire without employment contract, or declares a minimum income, the real value of wages paying in pocket - payment in the envelope, so the second group comprises general indirect employers and employees who accept these informalised working conditions for various reasons. The authors identify several factors contributing to the continued persistence of informal employment: post-transition socio-economic evolutions (economic restructuring, privatization of state enterprises, low economic growth, unemployment, poverty, social inequalities); emigration (many emigrants returning to Romania for temporary short periods of time and engage in informal work); there are institutional factors that affect the informalisation of the labour market (labour market regulations, the structure of tax systems, social security, bureaucracy, public administration, corruption); informal employment is also determined by social/behavioral factors (culture, lack of trust in public institutions, the negative perception of the role of the state, partial understanding or underestimation of the benefits derived from social security).

Regarding informal employment trends we are focusing only on certain aspects of the informal economy after 2000, since the nature of informal employment has changed due to economic growth. Although the importance of agriculture has declined, yet agriculture remains an important activity in the portfolio of income generating strategies. Most informal activities are concentrated in retail trade, transport, construction, repair and maintenance, agriculture, hotels and restaurants, health and education (see also Neef, Stănculescu & Adair, 2007; Stănculescu & Elias, 2001; Stănculescu, 2004).

Finally, based on Parleviet and Xenogiani (2008) we can conclude that there isn’t one single policy that would reduce informal employment required for formalizing the status of the labour market. They propose a mix of policies which address the needs of at least the following informally employed groups of people: the poor and vulnerable people who are informally employed because they have no other options; those who are informally employed (voluntary or non-voluntary), but they have the potential to occupy formal; those who are working in the informal sector by own choice. In the process of implementing policies informality has to be differential treated according to the specific needs of the various vulnerable groups.
Conclusion

Although the phenomenon of informal economy was "recently" discovered for science, until now has been accumulated an extensive literature produced by academic sphere and international, national, governmental and non-governmental organizations as well; constituting a frequent topic on the agenda of public policies. With this study the main objective was to offer an overview of the specific literature, as part of a large theoretical and conceptual review of the phenomenon. This work was not intended to make a resolution on the benefits or negative effects on society of the informal economy. As a main conclusion in Romanian context is, that analyzing the informal sector, we have to take into consideration the country-specific aspects (space and time). The informal economy in Romania does not function as an instrument of income support such worked before 1989, nor as a defense mechanism - facilitator of advantages in the context of transition after 1989, but as a defense mechanism of disadvantaged groups on dual labour market often promoted by the formal sphere (labour market), using different methods.

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