

TRADE REFORMS, INFORMAL SECTOR ACTIVITY AND EMPLOYMENT

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□ ***Outline of Presentation***

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□ ***Introduction***

➤ As an aftermath of political independence developing countries embarked on strategies towards achieving economic independence

- Adoption of inward-oriented development strategy in the wake of independence in the early 1960s

- Tariff barriers

- Non Tariff barriers

Result – lack of growth and slow pace of development (Krueger, 1978; Krueger and Tuncer, 1982; Bhagwati, 1988; Dollar, 1992).

□ ***Introduction***

- **Policy response to the findings above included:**
 - Shift from protectionism to openness trade liberalization, and outward looking development strategy.
 - Emergence of bilateral and multilateral trade agreements aimed at promoting intra-regional trade, as well as north-south trade (Olofin et al. 2008)

□ ***Nature of sub-Saharan economies***

Rural – Urban Dichotomy

- The rural areas are characterized by lack of basic socio-economic infrastructure.
- Urban centres are characterized by concentration of socio-economic infrastructure and industries.

■ **Co-existence of the formal and informal sector**

- The formal sector consists of public sector and private sector firms and industries whose operations and activities comply with existing factor and product markets' regulations

- The informal sector is characterized by small scale and medium scale firms that don't comply fully or at all with existing markets' regulations (see Scherer, 1980; Ajakaiye and Akerele, 1996; Goldberg and Pavcnik, 2003; Folawewo, 2004; Olofin and Folawewo, 2006).
- The slow pace of development has enhanced the expansion of the informal sector over the years.

We therefore hypothesize that there is still a missing link in all these efforts without which the story in sub-Saharan Africa is likely not to witness any significant change except it is given the attention it deserves.

□ ***Filling the Analytical Gap***

- ▶ Trying to fill this important analytical gap has been the primary focus of our on-going research effort, albeit currently limited in scope to the Nigerian economy due to resource constraints.
- ▶ Our empirical investigations are aimed at understanding the nature and structure of the informal sector with particular focus among others on the following, (Olofin & Folawewo, 2005, 2006):

□ ***Filling the Analytical Gap***

- ▶ an empirical examination of the determinants of labour demand,
- ▶ the nature of workers' skills in the urban informal sector,
- ▶ The nature of firm-specific factors, such as, year of establishment, ownership structure, investment and profit levels as important factors affecting the demand for labour in the informal sector,
- ▶ The role of wages in the determination of labour demand.

- ▶ Measurement of workers' productivity (measured by educational level) and experience as an important explanatory factor in determining level of employees' earnings in this sector.
- ▶ We do expect some degree of similarity to exist in the nature, structure and workings of the informal sector across most African countries.

- ▶ However we do expect to find some country specific features that may make sweeping generalisations based on our findings on Nigeria quite difficult.
- ▶ Our intention therefore is to extend the scope of our coverage in a panel data study that would allow us have a more representative picture cutting across several African countries by selecting representative countries in the various sub-regional zones.

- In the Doha Round majority of sub-Saharan African countries are classified as LDCs, with the exception of a few.
 - they are under the trade assistance programme Integrated Framework (IF) and the Enhanced Integrated Framework (EIF).
 - Consequently, the extent of formal trade among these countries is low; while informal trade is high.
- ***Thus, a re-assessment of the current global trade architecture would be incomplete without focusing on the challenges of trade and employment in the informal sector in these economies.***

Suggestions for Likely Research Focus and Emphasis

- **Research focus should aim at evaluation of the impact of trade liberalisation on informal sector employment activities at the micro level before embarking on global analysis of impact at the broad aggregative macro level as is often the case in most formal sector studies.**
- **More specifically, analysis of trade and informal sector activities may focus on the following:**
 - **Examining the structure and diversity of informal sector activities;**

□ **Suggestions for Likely Research Focus and Emphasis (Contd.)**

- Evaluating the impact of 'aid for trade' programmes on informal sector activities;
- The extent to which trade assistance programmes have enabled the LDCs in the region to grow to trade?
- If yes, quantifying the magnitude of such impact first on the informal sector, and on the economy as a whole and the corresponding aggregation problems.

❑ ***Justifying the Re-Focusing of Emphasis***

- **The need to recognise the significance of the informal sector in the development process and with particular reference to these economies.**
- **The informal sector bears the brunt of any negative fall outs from badly formulated and/or badly implemented macro economic policies designed primarily for the formal sector.**



Justifying the Re-Focusing of Emphasis (contd.)

- **Few existing studies on trade, informal sector and employment have been concentrated on Asia, Latin American and Caribbean countries (Goldberg and Pavcnik, 2003; Soares, 2005; Marjit and Kar , 2007), with the exception of Currie and Harrison (1997).**
- **Finally, results from analyses of trade-employment relationship in the informal sector remain inconclusive as findings from such studies have sometimes been contested on methodological grounds.**

❑ ***Some Theoretical Propositions Awaiting Further Empirical Verification***

- **There are several theoretical propositions regarding possible outcomes of the relationship between trade and employment. Some of these for which additional studies would yield greater insights include:**
 - that trade liberalisation could have both positive and negative effects on employment in terms of job creation and job destruction;
 - that in the long run trade is expected to increase inequality between skilled and unskilled labour in developed countries, while the gap is expected to narrow in developing countries;

□ **Some Theoretical Propositions Awaiting Further Empirical Verification (Contd.)**

- the effect of trade on employment in the short run depends on country specific factors, however, in the long run the efficiency gains caused by trade liberalisation are expected to lead to positive employment effects, either in terms of quantity or quality of job creation or a combination of both;
- exporting sectors of an economy are expected to expand and demand for more labour, while importing sectors would contract and lay-off workers;
- trade policy can have effect on employment if an economy is not characterised by full employment before the reform, or if some domestic policies and labour market characteristics hamper the adjustment process (Brecher, 1974);

❑ **Some Theoretical Propositions Awaiting Further Empirical Verification (Contd.)**

- effects of trade on employment to a large extent depend on the link between export – import firms, low-productivity and high productivity firms among others (Bernard and Jensen, 1999; Bernard et al, 2007); and
 - trade reforms are expected to depress informal wage by contracting the formal sector and driving labour into its informal counterparts (Marjit and Kar, 2007).
- **Empirical evidences have emerged in respect of some of the foregoing propositions, but hardly can such evidence be taken as sufficiently conclusive as to warrant the exclusion of need for further research.**

❑ ***Some Major Empirical Findings Deserving of Further Evidence***

- **Some major empirical findings deserving further evidence particularly from the context of developing countries such as sub-Saharan African economies include the following:**
 - there have been some positive effects of trade on manufacturing sector employment (Papageorgiou et al, 1990; WTO-ILO, 2007);
 - the effect of trade on employment depends on the prevailing job search behaviour and the nature of the labour market in an economy (Rama, 2003);
 - trade liberalisation has led to a rise in real wage and real fixed assets in the informal manufacturing sector of India (Marjit and Kar, 2007);

□ **Some Major Empirical Findings Deserving of Further Evidence (Contd.)**

- post-comprehensive trade liberalisation led to a rise in firms' hiring of more temporary workers in Morocco (Currie and Harrison, 1997);
- trade reforms has led to resource reallocation from the formal to informal sector in some Latin American and Caribbean countries (Stallings and Peres, 2000),
- there is no empirical evidence showing that trade liberalisation contributed to increases in informal sector employment in Brazil and Colombia (Goldberg and Pavcnik, 2003).

❑ ***SOME METHODOLOGICAL AND DATA ISSUES***

- ▶ It is important to note that in addition to theoretical issues and inconclusive empirical results awaiting further evidence, there is also the problem of the complexity of outcomes resulting from yet to be resolved methodological issues and challenges, (see: Greenaway, 1993; Collier, 1993; Gaston and Trefler, 1997; Trefler, 2001).

- ▶ Some of these methodological issues also need to be addressed with specific reference to informal sector activities, (see: Dollar and Collier, 2001, WTO–ILO 2007).
- ▶ Generally, given the nature of the complexity of the informal sector, an eclectic investigative approach may be more promising than a doctrinaire conventional approach to modelling, (see: Shapiro and Stiglitz (1984); Bulow and Summers (1986),;Saint–Paul (1996) and Goldger and Pavcnik (2003); Olofin & Folawewo, 2005).

❏ **CONCLUSION**

- ▶ In conclusion an understanding of the nature and workings of the informal sector is critical to the transformation of African economies given its potentials for trade and employment generation. It therefore deserves greater attention of researchers than it is given at the moment relative to the formal sector.
- ▶ Unlike it is with formal sector studies where easy access to published secondary data reduces the burden on the researcher, the collection of primary data remains a challenging task.

- ▶ It is no doubt a highly challenging task, but nonetheless not an insurmountable one.
- ▶ As the sector receives the research attention it deserves, data gathering authorities are likely to appreciate the need to extend the coverage of their data collecting activities to informal sector activities.

- ▶ We also see collaborative research effort between institutions in Africa and other developing countries in Asia and Latin America with informal sector challenges helping to resolve some of the data and methodological challenges confronting informal sector research in Africa