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Contribution to the 2015 United Nations Economic and Social Council (ECOSOC) Integration Segment

Harnessing the potential of the Informal Sector for inclusive growth in Africa

ECA Contribution to the ECOSOC Integration Segment

In recent years, African countries have experienced remarkable economic growth, but this has not generated sufficient decent jobs for the millions of young persons who enter the labour market each year. While it is estimated that there are 122 million new entrants annually, African countries created only 37 million jobs over the last decade, out of which only 28 percent were in wage-paying formal jobs (Mckinsey 2012). This jobless growth process has been attributed to the slow pace of structural transformation accompanied by the shift towards more productive, labour-intensive jobs in manufacturing and high-end services (ECA 2014).

The informal sector remains the major source of employment across Africa, accounting for 70 per cent of employment in Sub-Saharan Africa and 62 per cent in North Africa (AfD2013). The dynamism of the informal sector in creating employment and value addition is particularly strong, representing about 80 per cent of the total labour force, and contributing about 55 per cent of sub-Saharan Africa's GDP. In addition, 9 in 10 informal workers are women and youth, but the lack of social protection, skills' upgrading and productive income often trap these groups into poverty and exclusion from economic growth and development, with only about 10 percent of operators benefiting from social protection schemes (AU 2011).

But the nature and size of the informal economy varies greatly across countries and regions. In Senegal, the share of the informal sector in value addition in agriculture and forestry is close to 100 percent, demonstrating the close links that could exist between sustainable green growth and the informal sector (Benjamin et al., 2012). Female informal cross-border retail trade, which is generally small and self-employed, amounted to 64 per cent of the added value of national trade in Benin, 46 per cent in Mali and 41 per cent in Chad in 2012 **(UN 2011)**. In addition, the diversity of informal employment across countries is captured by a set of characteristics related to the type and location of activities, access and use of technology, access to credit, productivity levels, and contribution to social security.

In most countries, informal jobs mostly emanate from the services and agriculture sectors. While the share of services in GDP value added has consistently exceeded other sectors, reaching 50 per cent of total value added between 2000 and 2013 (ECA 2015). The services sector is largely composed of informal, but also modern services (including ICT and financial services) which reflect a successful shift into higher productive and more formal jobs. Mauritius is country which has successfully formalized and created productive employment through policy interventions, including fiscal incentives to the private sector complemented by human capital development programmes.

Drivers of informality

Country specificities exist in informal employment, although some common traits can be observed. On the supply side, the low quality of numeracy and literacy attained in educational systems, and inadequate skills development, are among the main factors leading to informality on the continent. The lack of technical and vocational training, limited investments in infrastructure, technology and innovation, as well as poor alignment of educational curricula to labour market demand, constitute other major hindrances for job seekers to enter the formal market. At the same time, large cities with little or no industrial bases exacerbate informal employment as a coping mechanism, particularly by young people.

On the demand side, an employment focused growth trajectory that shifts production processes to labour intensive sectors through backward and forward linkages to the local economy is a critical component.

The transition from informal to formal employment becomes easier when on-the-job training, through technical and vocational training (TVET), apprenticeships and other non-formal training, is combined with formal education. Thus studies have shown that workers in major urban cities in West Africa have seen higher marginal returns from these programmes than from general secondary education alone (Kuépié et al., 2009).

The prevalence of informal activities is also related to weaknesses in two institutional areas, namely taxation and regulation. While the introduction of indirect taxes and value added tax enables informal sector operators to contribute to government fiscal revenues, the potential gains from direct tax of the informal employees and businesses could be as high as 55 percent and 74 percent of GDP in Burkina Faso and Benin respectively (Benjamin et al., 2012). However existing regulatory procedures on eligibility for formal registration require a certain threshold of revenue which often acts as a disincentive, pushing firms into informality.

Towards inclusiveness and higher productivity in the Informal Sector

Some good practices have emerged in different countries to enhance conditions in the informal sector and increase the productivity of operators. In Kenya, the development of a fledging innovation ecosystem, *iLab Africa*, links universities and entrepreneurship, providing business solutions for informal firms through mobile technology, thus improving access to ICTs and overall productivity. This is forward-integrated with venture capital firms to create formal employment opportunities for youth (Blohm 2008). In Botswana the forward linkages in raw diamond production created 21 firms in cutting and polishing and 3,000 jobs (Grynberg 2013).

Accelerated by Rio+20, developed, developing and emerging economies are launching national and regional green economy plans and policies to ensure the transition and inclusion of informal workers in green-based initiatives. For instance, the active participation of informal food vendors in Accra, Ghana with local government and waste management firms ensured improved sanitary conditions in the exchange of goods and healthier food production and trade. This in turn improved the overall health conditions of the low-income groups as the highest proportion of consumers from these vendors. Similarly in Kenya, the government took appropriate steps to enable informal dairy producers and traders to be accepted into the licensed milk trade, and risk analysis of milk borne hazards was the basis of a capacity building programme for informal traders to obtain official trading certification (Benson 2014).

The large contribution to growth and employment by the informal sector is a critical aspect in the transition to the SDGs, while country specific data is needed to calibrate interventions. In particular, a systemic policy package for the informal sector is necessary to contribute to a transformational and green industrialization process. Adequate resources and curricula redevelopment aligned to an industrialization process and more broadly to an inclusive sustainable growth path are required for education and skills upgrading for informal sector, coupled with access to credit, public utilities, and ICTs, at the same time as the macro-economic framework becomes more employment focused, with backward and forward linkages to local economies.

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