

## The informal sector in Algeria

(Trends, Implications and Strategy for Transformation to the formal economy)

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### ملخص:

تعتبر هذه الدراسة بمثابة مساهمة في النقاش الدائر في الوقت الراهن حول ظاهرة القطاع غير الرسمي، والتي أصبحت تشكل ظاهرة عالمية مست كل دول العالم دون استثناء، غير أنها استفحلت بشكل كبير في الدول النامية ووصلت إلى معدلات أقل مما يقال عنها أنها خطيرة.

وتركز الدراسة على حالة الجزائر من خلال الوقوف على حجم القطاع غير الرسمي فيها والتعرض لأهم العوامل التي أدت إلى نموه والآثار التي يخلفها على الاقتصاد الوطني ومن ثم استراتيجية احتواءه والانتقال إلى الاقتصاد الرسمي .  
**كلمات مفتاحية:** القطاع غير الرسمي، العمالة غير الرسمية، الجزائر، القطاع الرسمي، البطالة

### Abstract :

This study is a contribution to the current debate on the phenomenon of the informal sector, which has become a global phenomenon in all countries of the world, but it has greatly increased in developing countries and reached serious rates.

The study focuses on the situation of Algeria by identifying the size of the informal sector and the exposure to the main factors that led to its growth and its effects on the national economy, then the strategy of containing it and moving to the formal economy.

**Keywords:** Informal sector ,Informal employment , Algeria, formal economy, unemployment.

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## 1.Introduction:

Nowadays, diverse studies and researches revolve around the issue of informal economy, This phenomenon that has different labels: hidden economy, non observed economy, non organized economy, parallel economy, Shadow economy, etc.

According to the international labor organization report, the informal economy recruits 61% workers worldwide, 93% are deprived of their legal rights and social protection-worse than that, half the workers have informal jobs if we discard agriculture. 85% of jobs in Africa are informal, 68% in Asia and pacific, 68,6% Arab countries and 25% in Europe and Asia Minor.

In Algeria, the growth of the informal sector coincided with the transition period of the national economy and the reforms accompanying the policy of economic openness and the direction of the market economy and the resulting high unemployment rates and low incomes of individuals and low standard of living.

The contribution of the informal sector to non-agricultural GDP has been estimated at 45 percent for algeria in 2012 and it has 45.6% of the total labor force outside the agricultural sector.

This research paper tries to project the causes of informal sector growth and its repercussion on Algerian economy and the ways to incorporate it in formal economy, through a study of the following points :

- Definition of the informal economy;
- Measuring the informal sector;
- The reasons for the growth of the informal economy;
- The extent and trend of the informal economy in Algeria;

- The effects of the development of informal economy on the Algerian economy;
- Strategy of transforming to the formal economy.

## **2. Definition of the informal economy**

In 1970s, the first who coined the term “informal sector” is Keith Hart, an anthropologist, to describe the scope of unregistered economic activity operating in Accra, Ghana (Keith Hart,1973, p 61-89), He noticed marginal urban productive activities of self-employed to satisfy their own needs. At that time, these kinds of activities were ignored by politicians and economic researchers and in national economic accounts, which require their introduction in the development strategy.

Thus, the ILO (International Labor Organization) Kenya report on employment aimed to formulate this concept, in 1972, where the term “informal sector” is used to describe the activities of poor workers who worked very hard to survive and meet their own needs but who were not recorded or regulated by the state authorities, This report is based on the dualistic view of the link between the formal and informal economy and that the informal economy has positive effects on the official one (labor market and distribution of incomes) .

Hence, this concept became a crucial part of the economy, and attracted the attention of politicians and economic researchers.

Furthermore, basing on the report of Kenya, the ILO undertook several studies on the informal sector (1993, 2002, 2003), where it brought new developments to this field each time, Meanwhile, all the definitions of the informal sector

included poverty, marginality and underemployment (Soumia Bouanani ,2013,p10).

According to the fifteenth international conference of labour statisticians: (Economic Commission for Africa,2007,p3)

- The informal sector may be broadly characterized as consisting of units engaged in the production of goods or services with the primary objective of generating employment and incomes to the persons concerned, these units typically operate at a low level of organization, with little or no division between labour and capital as factors of production.
- Production units of the informal sector have the characteristic features of household enterprises, the fixed and other assets used do not belong to the production units as such but to their owners Expenditure for production is often indistinguishable from household expenditure Similarly, capital goods such as buildings or vehicles may be used indistinguishably for business and household purposes.
- Activities performed by production units of the informal sector are not necessarily performed with the deliberate intention of evading the payment of taxes or social security contributions, or infringing labour or other legislations or administrative provisions. Accordingly, the concept of informal sector activities should be distinguished from the concept of activities of the hidden or underground economy.

The conceptual framework endorsed by the 17th ICLS relates the enterprise-based concept of employment in the informal sector in a coherent and consistent manner with a broader, job-based concept of informal employment.

A person can simultaneously have two or more formal and/or informal jobs, Due to the existence of such multiple

jobholding, jobs rather than employed persons were taken as the observation units for employment. Employed persons hold jobs that can be described by various job-related characteristics, and these jobs are undertaken in production units (enterprises) that can be described by various enterprise-related characteristics (Ralf Hussmanns,2004,p4).

The 17th ICLS defined informal employment as the total number of informal jobs, whether carried out in formal sector enterprises, informal sector enterprises, or households, during a given reference period, Included are: (Economic Commission for Africa,2007,p8)

- Own-account workers (self-employed with no employees) in their own informal sector enterprises ;
- Employers (self-employed with employees) in their own informal sector enterprises;
- Contributing family workers, irrespective of type of enterprise;
- Members of informal producers' cooperatives (not established as legal entities);
- Employees holding informal jobs as defined according to the employment relationship (in law or in practice, jobs not subject to national labour legislation, income taxation, social protection or entitlement to certain employment benefits (paid annual or sick leave, etc.) ;
- Own-account workers engaged in production of goods exclusively for own final use by their household.

To sum up, there are three related official statistical terms and definitions which are often used imprecisely and interchangeably: the informal sector refers to the production and employment that takes place in unincorporated small or unregistered enterprises, informal employment refers to employment without legal and social protection—both inside

and outside the informal sector ,and the informal economy refers to all units, activities, and workers so defined and the output from them. Together, they form the broad base of the workforce and economy, both nationally and globally(Martha Alter Chen,2012,p8).

### **3. Measuring the informal sector**

There are two broad methods for measuring the informal sector direct and indirect, Direct measurement requires the conduct of a survey while indirect measurement entails the use of other data sources and statistical models.

#### **3.1. Direct method of measuring the informal sector**

For the direct method, the collection of data on the informal sector can take many approaches special surveys on the informal sector, through regular surveys with expanded coverage such as the labor force or other household surveys or the establishment/enterprise surveys and censuses and the mixed household–enterprise surveys.

Many academic researchers have based their observations on establishment surveys, Their utility cannot be disputed especially in the absence of alternative sources, However, it is particularly difficult to find a reliable survey frame for sampling.

This difficulty could be overcome if there is a strong and well-organized union association governing the trade, However, this may prove insufficient for the location of the observation (or survey) unit, notably in the case of workers with no fixed location (with movable stalls).

Sampling and the establishment of a survey frame using household surveys are both facilitated. However, it should be borne in mind that the standard approach is designed to measure an activity that is widespread among the population, but it is not necessarily effective in capturing certain activities, the household survey itself may be skewed because poor households are more inclined to cooperate than their rich counterparts.

### **3.2. Indirect measurement methods**

There are different indirect methods for measuring the informal sector, including: (Economic Commission for Africa,2007,p40)

- The differential method, which simply allocates the difference between expenditure and income to the informal sector. It is based on the comparison of aggregates and account balances (by analysing the supply and use table);
- The flow of goods method, which is based on the same principle but at a disaggregated level;
- The labour input approach, which is based on the labour input matrix and assumes a stable relationship between the potential working population (based on age) not incorporated in the informal sector and production by the informal sector;
- The different monetary approaches that assume stable relationships between economic activity and a few monetary variables.

A few remarks should be made with respect to these methods. In many countries that use them, preliminary studies have established conditions on the structure of national accounts, thereby establishing relationships governing the

indirect methods. Given the need to make national accounts available, these relationships have to be reviewed.

The assumptions used in the indirect methods must be explained clearly at any time and incorporated into the methodology and the publications, because they form the basis of economic policies. For example, for the employment-based method, the assumption used is that per capita production in the informal sector is constant in real terms.

Hence, total production is obtained by multiplying this coefficient by the number of persons employed by branch. This assumption may be considered strong to the extent that:

- It reflects a possibility of continuous expansion of a branch (possibility of always finding work, even if this means taking away employees from other sectors);
- It does not take into account the constraints of branches, such as availability of farmland.

In regard to the differential method based on accounts, account balances are often derived from experts' estimates, under the system of national accounts, while the validity of the process can be guaranteed, it lacks scientific scrutiny because it is not predicated on a statistical process.

In other words, the accuracy of the method is debatable, in the absence of direct statistical information on the informal sector.

#### **4. The reasons for the growth of the informal economy**



The reasons for the growth of the informal economy often interrelated and to some extent overlapping, are the following:

- Limited absorption of surplus labour : The limited capacity of agriculture and the formal economy to absorb surplus labour, together with increasing numbers of job seekers, has boosted the size of the informal economy, In countries with high rates of population growth or urbanisation, the informal economy tends to absorb most of the growing labour force in the urban areas when the manufacturing industry and off-farm activities in general do not grow at the same pace;
- Barriers of entry into the formal economy: Excessive costs and government regulations as well as corruption in areas such as business start-up, granting of business permits and land titles, have forced people to remain informal;
- The weak capability of formal institutions to provide education, training and infrastructure as well as other incentives for structural reforms has contributed to the growth of the informal economy;
- Structural adjustment programmes during the eighties and nineties have fuelled the growth of the informal economy in developing countries, the disappearance of public sector jobs and the closure of uncompetitive businesses have forced many laid-off workers to find other ways to survive;
- Capital is favoured over labour: Global integration privileges companies who can move easily and quickly across borders to the disadvantage of workers;
- The globalization of the world economy as well as global trade and investment patterns thus tends to privilege capital and disadvantage labour, especially lower-skilled workers that cannot migrate easily or at all (ILO,2002);
- Demand for low-cost goods and services : The informal economy has been boosted by rural to urban migration in

- conjunction with the demand for low-cost goods and services from those employed in the formal and informal economies;
- Uncommitted or unaware governments: Many governments are unaware of the economic contributions of the informal economy and the problems found in it and have therefore found it unnecessary to intervene because of the belief that the informal economy would die out, The informal economy has often been left unattended and has thus had few obstacles for its growth;
  - Economic hardship and poverty;
  - There are growing numbers of women that enter the labour markets outside of agriculture. However, although many women own or run micro enterprises, only a small number of women entrepreneurs actually enter the formal economy (Kristina flodman Becker,2004,p10).

## **5. The extent and trend of the informal economy in Algeria**

The crises in Algeria and its negative effects on the economic, social and political levels led to the intensification of the informal economy, which increased to 19.5% of the gross national product at the end of the 1980's to reach 42% of the GNP in 2003, And reached 50% of the GDP in 2010 and 45% of the GDP in 2012.

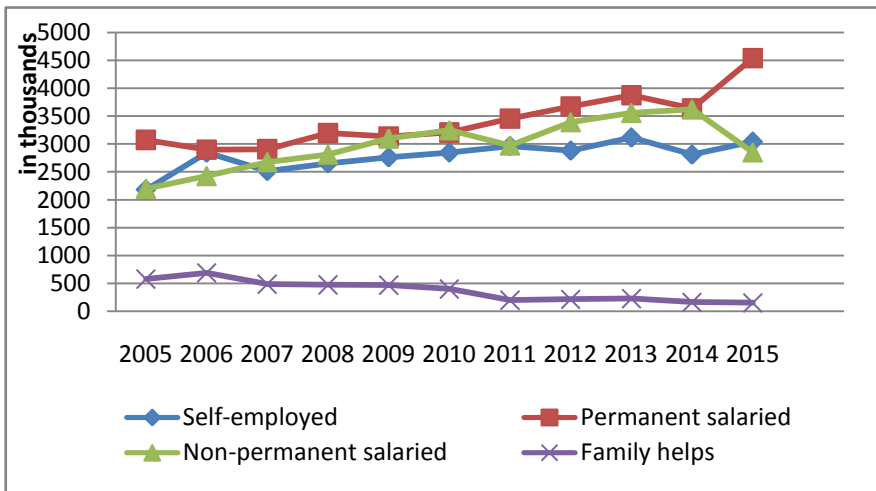
According to an investigation conducted by the national bureau of statistics, Excluding agriculture, informal employment represents occupied 3.9 million workers in 2012, or 45.6 % of total non-agricultural employment; distributed in the sectors of trade and services (45.3%) and construction, public works (37%) and industrial activities (17.7%).

According to national employment surveys, the trends of the labour market in Algeria display strong growth in self-

employment and non-permanent salaried, which essentially make informal employment (Philippe Adair ,Youghourta Bellache,2015,p4)

Non-permanent salaried has grown dramatically: Which increased from 2203 thousand in 2005 to 3623 thousand in 2014, surpassing the number of permanent salaried for the first time in 2010, And almost equal in 2014, Then declined by 2015 to 2855 thousand.

**Figure 1. Trends and structure of the employed population (2005-2015)**

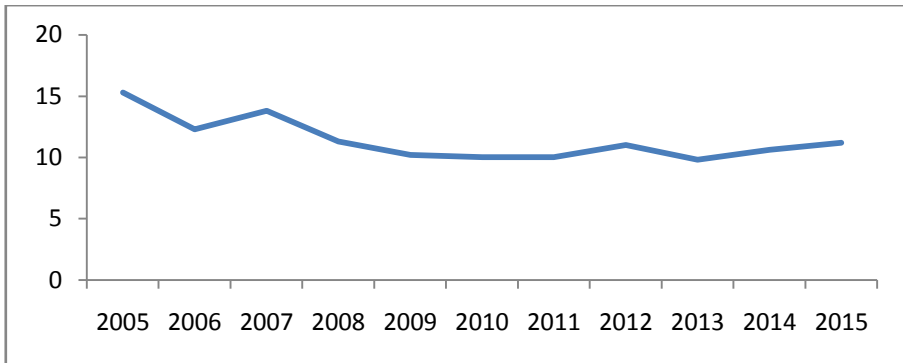


Source :ONS, 2015, P12.

In 2006, 54.1 % of the total employed population do not register with social security and constitute the informal employment according to the ILO definition, But this rate fell to 38.5% in 2015(ONS,2015,p12)

The increase in non-permanent salaried in this period coincided with a decline in the unemployment rate, which fell from 15.5% in 2005 to 9.8% in 2013 and 11.2% in 2015.

**Figure .2. Development of unemployment rates in Algeria (2005-2015)**



Source :ONS, 2015, P12.

## **6. The effects of the development of informal economy on the Algerian economy**

The rising size of the informal economy has many on the effects official one, Although the analysis of those implications is difficult, most of economic researches focused on the impact of the informal economy on allocation of resources and the loss of revenues for the state, and ignored the crucial role of official institutions, norms and rules. However, we will stress some effects of the informal economy on the official economy, as follows:

- The increase of informal economy leads to the deficiency of stability in economy. Where the existence of this economy can lead to overestimation of the economic and monetary indicators, such as unemployment rate, inflation rate and growth rate, etc.
- The loss of an important part of the revenues on the State Treasury: The Algerian public treasury loses as a result of

the spread of the informal sector equivalent to 7% of income tax revenues, while social security loses 20% of its revenues, which is equivalent to 585 million dollars for income tax revenues, and 1.7 billion dollars for income Social Security Fund, which is sufficient to meet the annual deficit of the social security system, and the estimated tax losses, especially the value-added tax of 300 million dollars .

- This sector poses a danger to the official sector through the latter's exposure to the large competition with smuggled foreign products and counterfeit goods, which are sold without any financial obligation, in addition to the negative impact these products have on consumer health, China, the United Arab Emirates, Taiwan, Hong Kong, India and Turkey are among the biggest exporters of counterfeit goods to Algeria (Direction générale des douanes,2006,p20), because in these countries, there is a difficult control over their industrial products. In addition, these countries are known with tradition, This is in addition to the spread of the phenomenon of counterfeiting the invoices of imported imitation materials, which included almost all products, including: textile, leather, spare parts, electronic products, electric appliances, household appliances,, perfumes, food industries, medicines, cigarettes, The marketing of counterfeit products that do not have an origin indicates absence or lack of control over various levels, such as the Ministry of Commerce, which is legally competent to monitor commercial operations, the Ministry of Health and Population which is no longer able to protect public health, the Ministry of Labor and Social Protection and its role on protect workers from violations in the field of social protection.
- The workers in the informal sector are working under bad condition which lead to diseases-also, they are violated from

any kind of protection-neither medical care nor Social one, they are working for long hours with less salaries comparing with the available condition in the formal economy.

- Most economic units in the informal economy do not enjoy secure property rights, which deprives them of access to both capital and credit, They have difficulty accessing the legal and judicial system to enforce contracts, and have limited or no access to public infrastructure and public markets, Informality may also inhibit investment in bigger businesses and impede trade because informal firms often lack the necessary size to exploit economies of scale fully. Company size, productivity growth and export opportunities are closely linked. Not only can large firms benefit from economies of scale, they also have easier access to high-skilled labour and banking credit(ILO,2014 ,p9)

Although the negative effects of the informal economy, it is considered as a substitutional sector in economic crisis and a source of income for the poor people. Let us shade alight on some positive aspects of the informal economy:

- It is a solution to the problem of Unemployment and it provides working opportunities and reduces poverty. If the unemployment leaves the absence of income, poverty, diseases, social problems, the informal work reduces such problems because it is considered as a substitutional source for the incomes, The official statistics shows decrease of unemployment in Algeria because of the increase of informal sector, this is what we have pointed out in the previous section.
- it is considered the most dynamic and flexible sector because of its ease to join it, there is no bureaucracy in this sector

and because it Provides the services and products that the society need in its daily life.

## **7. Strategy of transforming to the formal economy**

The transition from informal to formal sector activities, in principle, is an encouraging sign of economic development. The formal sector is typically more productive than the informal. It is also subject to government taxation and social security contribution, thereby making the overall economy more conducive to sustainable growth

Changing the face of informal enterprises is a complex multidimensional process, where policymakers will have to understand the nature of eclectic categories of informal workers, their constraints as well as their potential to contribute to overall GDP.

- For the self-employed or employees in informal enterprises, formalization generally means registering their business followed by obtaining a license and ultimately regularly paying taxes. However, these workers will only be willing to bear this cost if they perceive benefits from operating formally. These benefits include enforceable commercial contracts, tax breaks and incentive packages to raise their competitiveness, membership with trade union associations, access to government subsidies and incentives, employer contribution to pensions, and rights to organize and bargain collectively.

- Informal work is often undertaken because of barriers to entry to formal work, These barriers include the absence of requisite educational qualifications and the lack of corporate networks, The formal sector can bridge this gap by employing people from low-income households, investing in them through on-the-job training

along with on-field exposure to working systems, A few firms engage in such processes through corporate social responsibility (CSR) objectives, However, mainstreaming this process by setting targets for hiring people who are found to be worthy of training would make the formal sector more inclusive ( Monami Dasgupta, 2016)

- In 2014, the ILO developed a comprehensive framework based on seven key avenues towards formalization (see the figure below) which emphasizes the importance of vertical integration and coherence across the range of policies to curb informality, while the horizontal dimension focuses on intensifying action in each policy area. These policy areas are: quality employment generation and growth strategies, the regulatory environment, social dialogue, organization and representation, promoting equality and addressing discrimination, measures to support entrepreneurship, skills and finance; the extension of social protection; and local development strategies (ILO,2014,p13)

**Figure.3. Strategy of transforming to the formal economy**



Source :ILO,2014,p13



## **8. Conclusion**

The informal economy currently accounts for more than one-third of the national product and employs about half of the total labor outside agriculture, The growth of this sector results in the loss of a large part of the revenues of the public treasury, It also poses a danger to the official sector, Which requires the need to treat and try to contain and take steps to ensure the development of productivity and organization with the provision of legislative and social protection to ensure the protection of the worker and contribute to the maintenance of a decent life away from the conflict of laws and regulations, and reducing the cost of the establishment, operation and liquidation of projects and facilitate financial and commercial administrative procedures, and to fight all forms of corruption.

Finally, we emphasize that the effectiveness of the measures to combat or contain this phenomenon is related mainly to knowledge of all its causes, dimensions and characteristics, which requires the preparation of studies and statistics in-depth and comprehensive on the informal economy in Algeria.

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