

Low-Tier Informal Workers over the Medium Term: Evidence from Indonesia

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Informal work = inferior work?

- Lower and more volatile income (Gunther & Launov, 2012)
- Workers fully exposed to risks: no contracts, no insurance
- Informal work is safety net (Loayza & Rigolini, 2011)
- Formalization is occupational upgrading (McCaig & Pavcnik, 2015)
- As an economy grows, workers move out of informal sector (Gindling & Newhouse, 2012)

Not quite

- Informal sector is heterogeneous
 - Entrepreneurs (incorporated) vs unincorporated (Levine & Rubinstein, 2015)
 - Entrepreneurs earn more than similarly observable employees
 - Low-tier vs high-tier informal
- Some workers may be better off and prefer to be in informal work
 - 55% of informal workers are voluntary (Gunther & Launov, 2012)
- Some evidence of constraints?
 - 30% of unsuccessful entrepreneurs have the same characteristics like successful entrepreneurs (Gindling & Newhouse, 2012)

Research questions

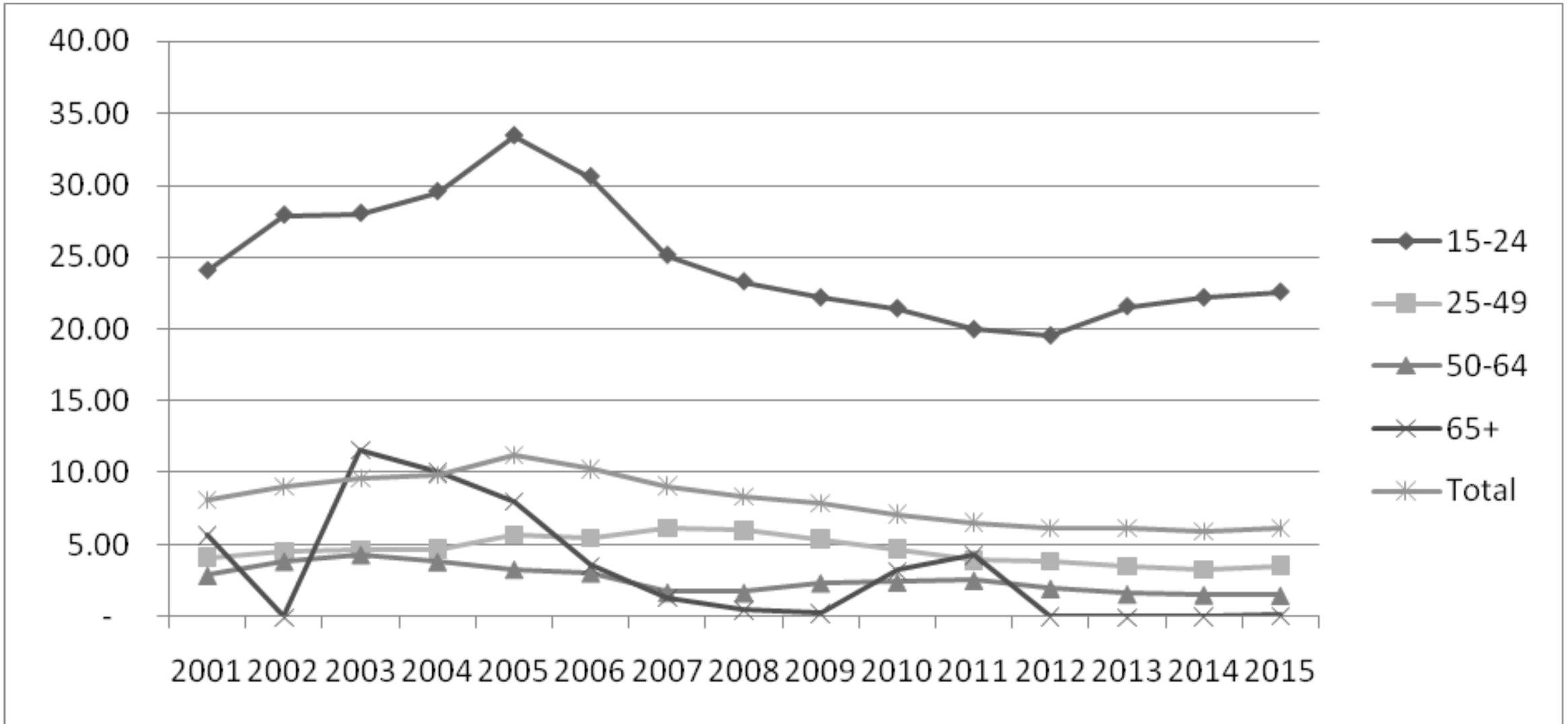
1. What is the proportion of individuals whose first job is low-tier informal? Does it change as Indonesia becomes a middle-income country?
2. What are the characteristics of individuals whose first job is low-tier informal? How do they compare with high-tier informal and formal?
3. Among those whose first job is informal, what proportion switched to other sectors? Who switched?

We use a medium-term perspective. No study from emerging economy has been able to follow individuals over reasonably long period of time.

Brief Indonesia context

- Economic crisis in 1997, over by 2000
 - Since early 2000s, stable economic growth of 5-6% per year
- Labor Law passed in 2003 – one of the most rigid labor market regulations in the world (Manning & Pratomo)
 - Only 30% of workers entitled to severance pay received it (Brusentsev et al., 2012)
- Pre-2015, legislated minimum wages had followed tri-partite negotiations, involving provincial government
 - Proportion of employees earning below the minimum wages increased from 28% in 2002 to 60% in 2015 (Purnagunawan et al., 2017)
- From 2016, legislated minimum wages follow a formula of national growth rate + national inflation rate

Unemployment Rate (%), 2001-2015



Source: Purnagunawan et al. (2017)

Data

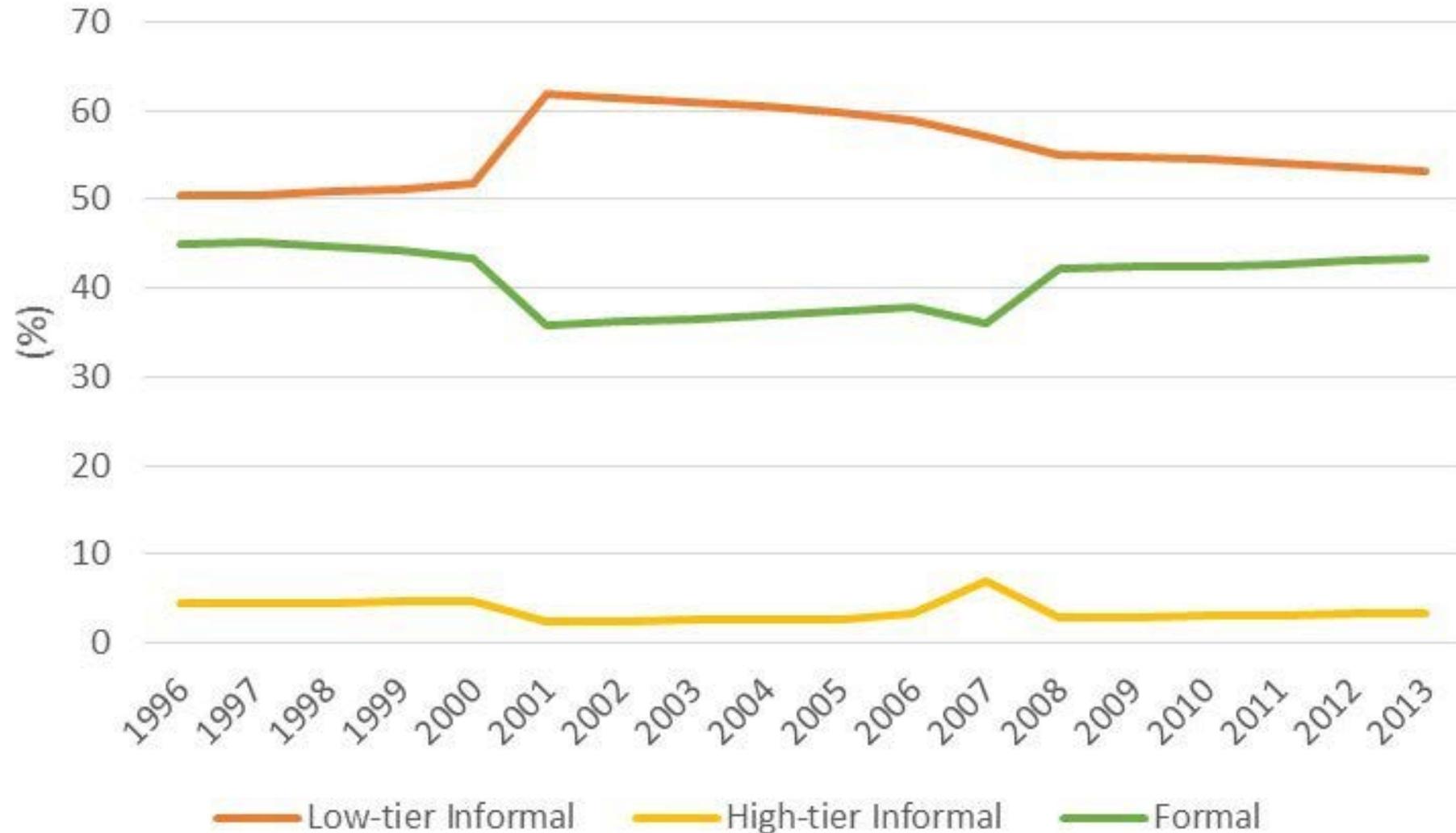
- Focus on males in non-agriculture sector
- Indonesia Family Life Survey
 - 1993, 1997, 2000, 2007, 2014
 - Representative of 83% of Indonesian population
- Individual-level employment status
 - 1996 – 2013: Perhaps the longest in developing country.
 - Focus on those starting work in 1996-2000 (IFLS 3) & 2001-2007 (IFLS 4).
 - We observe their annual employment status until 2013.
- Cognitive & math skills, height, schooling
- Parental education

Table 1. Classification of Low-Tier Informal Workers, High-Tier Informal Workers, and Formal Workers

		Work Status					
		Self-employed	Self-employed with family members	Employer	Government employee	Private sector employee	Unpaid family worker
Work Type	Professional	HI	HI	HI	F	F	LI
	Director or manager	HI	HI	HI	F	F	LI
	Official or administrative	HI	HI	HI	F	F	LI
	Sales	LI	LI	HI	F	F	LI
	Labor	LI	LI	HI	F	F	LI
	Production	LI	LI	HI	F	F	LI
	Transportation	LI	LI	HI	F	F	LI
	Unskilled	LI	LI	HI	F	F	LI

- Low-tier informal to high-tier informal: notion of ‘leveling up’
- Low-tier informal to formal: not as clear

Proportion of all workers by informality 1996-2013



Proportion of workers starting out as low-tier informal

	IFLS 2000				IFLS 2007				IFLS 2014			
	Informal Low-tier	Informal High-tier	Formal	Total	Informal Low-tier	Informal High-tier	Formal	Total	Informal Low-tier	Informal High-tier	Formal	Total
Proportion	17.1%	1.7%	81.2%	100%	35.5%	1.7%	62.8%	100%	27.4%	0.8%	71.8%	100%
Change from previous IFLS wave					0.184	0.000	-0.187		-0.081	-0.009	0.090	
<i>p</i> -value of change					***	No	***		***	*	***	
Age	22.4	26.6	22.5	22.6	22.1	26.3	22.7	22.5	20.3	22.5	22.3	21.8
Years of schooling	8.9	13.2	9.5	9.5	9.3	10.8	10.8	10.3	9.0	12.4	10.7	10.2
Cognitive score	5.4	7.6	5.6	5.6	9.9	10.0	10.1	10.1	9.1	10.6	9.6	9.5
Mathematics score	1.8	3.3	1.8	1.8	3.0	3.8	3.2	3.1	2.7	3.0	2.9	2.8
Height (in cm)	162.6	169.0	162.6	162.7	162.4	166.1	162.7	162.6	163.5	164.2	164.7	164.3

- Workers starting out as high-tier informal are clearly different from the other two groups in 2000. The differences narrowed in 2007 and 2014.

Do low-tier informal workers switch job types?

- Among those starting out as low-tier informal:
 - 46% remained through the next 13-18 years.
 - 7% became high-tier informal for at least one year.
 - 47% became formal for at least one year.
- Among the 54% who switched:
 - Average years as high-tier informal: 0.4 years
 - Average years as formal: 3.9 years
 - Short, compared to 13-18-year careers that we observe
- Average job spell for those who switched:
 - 0.2 years as high-tier informal, 1.7 years as formal, 3.8 years as low-tier informal

What are the correlates of switching out?

	Probability of Switching (Yes = 1)	
	(1)	(2)
Age	-0.051*** (0.009)	-0.051*** (0.009)
Height (standardized)	-0.027 (0.051)	-0.026 (0.053)
Years of schooling	0.013 (0.009)	0.014 (0.009)
Father has more than six years of education (Yes = 1)	0.185** (0.074)	0.186** (0.076)
Urban (Yes = 1)	-0.015 (0.077)	-0.013 (0.080)
Number of years employed (total over 1996-2013)	0.059*** (0.007)	0.059*** (0.007)
Mathematics score (standardized)		-0.031 (0.020)
Cognitive score (standardized)		0.007 (0.042)
Observations	218	218
R-squared	0.273	0.276

Conclusion and next steps

- Between 2000 and 2007, first job formal fell from 80% to just 60%. But picked up in 2014. But rigid labor laws could play a role
- The characteristics of first job low-tier informal and formal are very similar, except the latter is slightly more educated (but not more skilled)
- The first job high-tier informal are different from the other groups
- Switch from low-tier informal mainly go to formal.
 - Very little switch to high-tier informal. In other words, ‘levelling up’ doesn’t seem to happen.
- But switchers still spend most of their career (that we observe) as low-tier informal
- The strongest correlate of switching is father education. Proxy for network / aspiration / opportunity?
- Next step: estimate the wage returns of different job types