Work/Jobs

Employment in the formal and informal sectors

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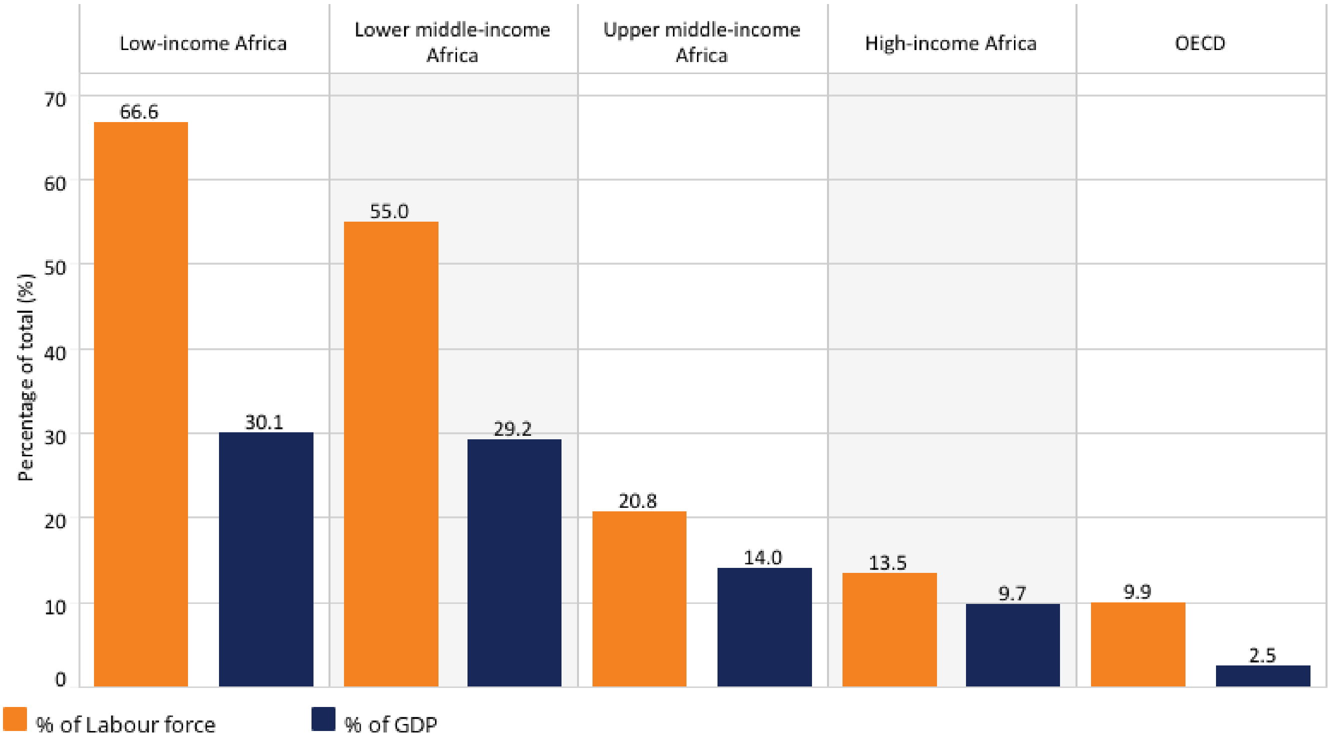
Whereas the informal sector accounts for only around 3% of the GDP of the 38 members of the Organisation of Economic Co-operation and Development (OECD) and informal labour accounts for a mere 10% of the labour force, the ratio for Africa's country income groups is much higher (Chart 1). The informal sector in developed countries is often of an illicit nature compared with its survivalist character in poor countries.

Chart 1: Size of the informal sector in Africa by country income group: contribution to GDP and portion of labour



Source: IFs 7.63 initialising from International Labour Organization and International Monetary Fund data
The Organisation for Economic Co-operation and Development (OECD) is an international organisation that consists of 38 members from North and South America, Europe and Asia-Pacific.

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Employment also differs by age. Underemployment among younger adults (aged 15–24) is higher than among adults (25 years) and is higher in rural areas than in urban areas.

Prior to the COVID-19 pandemic, the ILO estimated that the adult unemployment rate (15 years or older) in Southern Africa was 26%, making it the region with the highest unemployment rate globally. An important reason is that the informal sector is smaller in Southern Africa than elsewhere in Africa and so serves as less of a cushion to unemployment than elsewhere. With low levels of employment, inequality is generally high. Generally labour market participation rates only recovered from the pandemic in 2023, reflecting the damage it caused.

The reason is rooted in historically extractive policies based on cheap labour and minerals in much of Southern Africa – a region that achieved the transition to majority rule quite recently and with ruling parties heavily infused with ideological models from several decades ago, most prominently the former Union of Soviet Socialist Republic. In addition to the skewed economic structures inherited at the time of transition to majority rule, all are stuck in a mindset of economic centralism and top–down control that offers little room for self-help. As a result, economic emancipation has not yet taken place. Governments promise to provide for their citizens but rarely do.

In South Africa, the most recent country in the region to transition to majority rule, the previous system of mining, education and business was premised on the extraction of maximum profits and burdened the country with huge inequalities. With poor-quality education and limited entrepreneurship, employment is particularly low and inequality is exceptionally high. In fact, on both these counts South Africa fares worst globally. In the IFs forecast to 2043, South Africa is also set to buck the informality trend. Whereas the size of the informal sector is set to decline slowly elsewhere (both its contribution to GDP and as a portion of the total labour force), it is likely to increase in South Africa, largely as a result of tardy economic growth and, at only 19% of the labour force, it coming off a much lower base than elsewhere on the continent (the average for Africa is 58%).

At low levels of development, the informal sector is generally much less productive than the formal sector, but the gap typically reduces as countries move up the income ladder. At higher levels of development, a large informal sector may often reflect a determined effort to avoid regulation, because informality is often more nefarious at higher levels of income compared with being survival oriented at low levels of development. In high-income countries, productivity in the informal sector could, in select examples, be similar to that in the formal sector, as the primary orientation is often not survival but regulatory avoidance. Therefore, productivity in the informal sector in a country such as Italy or Greece, where the illicit economy is large, is not likely to differ from that in the formal sector. These characteristics are reflected in the modelling in IFs.

Irrespective of the level of development, a large informal sector is costly for society and constrains sustainable development. Workers active in the informal sector do not contribute to direct taxes (as they are not registered to pay personal or company tax) but the informal sector still requires infrastructure and services. A large informal sector therefore puts an additional burden on service delivery and congests public infrastructure without contributing to either, except through indirect taxes such as value-added and service taxes. However, this drag is balanced by the extent to which it absorbs people who would otherwise not have any employment or opportunity.

The ILO data on unemployment in Africa described earlier is therefore quite misleading without appropriate context, as poignantly revealed by 40% of respondents in a 2018 Afrobarometer survey saying that unemployment is the most important issue for governments to address, significantly more than concerns about healthcare or poor infrastructure.

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About the authors

Dr Jakkie Cilliers is the ISS's founder and former executive director of the ISS. He currently serves as chair of the ISS Board of Trustees and head of the African Futures and Innovation (AFI) programme at the Pretoria oce of the ISS. His 2017 best-seller Fate of the Nation addresses South Africa's futures from political, economic and social perspectives. His three most recent books, Africa First! Igniting a Growth Revolution (March 2020), The Future of Africa: Challenges and Opportunities (April 2021), and Africa Tomorrow: Pathways to Prosperity (June 2022) take a rigorous look at the continent as a whole.

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