Effects of informality on Albania’s labor market

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Abstract. With the growing interest on the size of informal economy in Albania, an important concern remains the best ways to reduce its dimension. According to scholars of the field, informality in Albania may be as large as 50 percent of its official GDP, or even higher. A reflection of informality in economy is also displayed by informality in the labor market. The socio-economic changes of the late last century, along with other changes, brought about a high rate of unemployment. The effects of unemployment in Albania’s informal economy will be discussed, and one of the methods used for its measure, as well as pinpoint to important lessons drawn when employers and employees are faced with one another. The aim of this paper is to focus on the reduction of informal economy, as seen through labor market lens, as an anti-crisis factor.

Keywords: informality, non-official economy, economic crises, labor market

JEL Codes: E26, J21

1. Introduction
The world has experienced an array of crises, of different shapes and forms, during its lifetime. However, the crisis of the beginning of this century impacted the economies of developed and developing nations. A debate has arisen on ways and tools to reduce its effects in countries directly or indirectly impacted by it. Tangible effects of the crisis were translated into job losses, stricter physical policies adopted by impacted countries, etc. Various countries used bespoken measures that lessened to a certain degree the consequences of the global crisis. In this paper the authors present their views on the size of informal economy in Albania and the growing concern to reduce its dimension, in the light of the crisis.

2. Materials and Methodology
Renowned researchers such as Cohen, Kindleberger, etc, have conducted studies on the field, including Albania’s experience in the limelight of the current crisis which can be used as key reference materials. In compiling this study various official data gathered through various means were used, as well as public data which are available in Albania. The objective of this paper is to highlight the informal sector in the Albanian economy, and especially in the labor market.

3. Research Results

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The world has faced hundreds of financial crises in the last four hundred years. What is most critical in a crisis is not just what happens in the unfolding of the event, but its aftermath. Scholars indicate that there are several common denominators of a crisis, to include the increase of money available in the market, which bring about development before the collapse. It is inevitable that crisis should be related to economic decline in the countries it occurs.

This late November, Albania will celebrate its centennial anniversary of independence. During this period the country has experienced various stages of development, including a centralized state-owned economy during communism moving onto a market economy after its collapse as early as 1991. The economic development of Albania in the last decades has faced various bumps along the road, despite that it has marked rapid development. Noteworthy enough, neighboring Greece has been faced with a severe crisis in the last couple of years. The recent economic crisis can affect Albania’s development. As in any crisis, countries could be categorized either as directly affected by the crisis, or suffering from its consequences. Albania falls in the later. An important role in Albania’s economy is played by its agricultural sector, which provides almost one quarter of its Gross Domestic Product; given that half of its population lives in the rural areas. Latest data indicate that rural population in Albania carries its activities through 368,997 agricultural economic units, also known as farms. Each unit area ranges between 0.52 to 1.13 hectares. Understandably farm sizing is considered small. Although farms are small, the agricultural sector plays an important role in the economy of the country. Given the limited developments of these areas, they are considered as survival economies.

In their study, Schneider and Este (2000) considered this type of economic activity as the first level of informal businesses. As of 1990 the economic activity or land owned by the farms has not been taxed. Presently only 320 farmers have paid their obligations and taxes. The government allowed that farmers bypass their tax payment obligation, as an opportunity for farmers to fulfill their survival needs. Therefore collecting information on informal economy is hard, given that those involved in it have not identified themselves or have avoided doing it. In order for policy makers to make effective decisions it is important to possess accurate data on the allocation of Albania’s resources in the informal economy. Therefore it is imperative to know who is engaged in it, how often they engage, and what kind of activities fall under it.

In the last five years the CIA Fact book reports that Albania’s informal, and unreported, sector may be as large as 50% of the official GDP. The country develops its economic ties with Greece and Italy, whose informal sector reaches 20 percent, and in turn this also influences the high level of informality in Albania. It is important to note that the informal economy also affects the economic efficiency of the country.

Due to the fact that a part of Albania’s economy is held informally, fewer revenues are collected by tax offices. Less collected taxes means that the government is forced to seek other financial means, such as Treasury bond issue. Thus, the presence of informal economy can in term impact the effectiveness of macro policies. Also, high levels of informality directly impact official economic data and due to their lack, statisticians and policy makers in turn lack important information on unemployment level and revenues. Informal labor creates a layer in the society that is not protected by the labor legislation. Occupational accidents, professional diseases contracted while working, unpaid contribution in the interest of the workers are some of the effects of informality at the workplace. A direct effect of informality is that these types of entrepreneurs that informally hire workers are not properly controlled by the line institutions or the Labor Ministry, and the fact that these people work under such conditions, displays their tendency to observe the state norms or employees’ rights. A snapshot of informality in the labor sector would display that treatment some of the employees go through, especially those that have experienced occupational accidents, such as injury, death, paralysis, poisoning, in the mining and construction industries, and in the clothes industry, resemble the condition of the employees in the first stages of capitalism. Those working in the informal sector put in long workdays, face difficult working conditions, and receive small salaries, even if they are enrolled in the official social and health insurance scheme. Employees face threats of various forms from their employers, including dismissal.

The loss the state incurs from informal economy and especially by the informal labor sector is huge, and at various levels. When the institutions fail to collect contributions and taxes from income revenues, this
would automatically lead to less revenue ending in the state budget. A social responsibility bill accompanies and weakens any government performance, and this is particularly noticeable in the pension and wages level, including public services. From different perspective the well-being of the population is not solely an objective of interest for the government, but also of any entrepreneur, as this would mean higher purchasing power, thus greater revenues for all. A protective measure that could occur is organizing workers under trade unions. Several attempts have been made to organize a trade union in the private sector, where informal economy dominates, but great difficulties have been noticed along the road, especially from employers. Those employees that undertook this responsibility were faced with pressure of all kinds, including dismissal.

The largest number of informal workers has been evidenced in most developed towns of the country, where there is greater concentration of economic activity. Data show that the largest numbers of individuals exercising an illegal activity or whose license has expired are located in these cities: Shkoder, Tirane, Fier, Elbasan, and Vlore. The highest density of unlicensed workers was evidenced in the suburbs around the afore-mentioned towns or rural areas which are out of control, and where the economic development rhythm is lower than in the city center.

Some objective and subjective reasons of informal labor market include: uncontrolled demographic movement of population toward larger inhabited centers, of greater economic level, and due to higher density of businesses, need for employment in these businesses which has generated the possibility of informal employment; dishonest competition and large movement influx of workforce according to market demand, especially in the construction business, hampers control and legality of the informal labor market; lack of total mobility control and currency circulation are additional reasons that favor informality; the lack of logistical structure can be counted as one of the objective reasons of this phenomenon; while one of the subjective reasons for informal labor market existence can include unemployment level, and employment is seen as one of the ways to flatten it; inter-institutional cooperation among executive bodies, such as the Tax Department, the Labor State Inspectorate, and the Institute of Social Insurance is still at memorandum of understanding level, and cohesion of joint actions in not a legal obligation yet.

Another factor that supports an increase in the informal sector is an increase in regulations. Legislative bodies entrusted with law-making authority should place greater importance not simply to increasing the number of regulations, but to their enforcement. It seems like the larger the number of regulations, the larger informal economy gets.

4. Conclusions

Informal economy plays a vital role for job openings, generation of incomes, and reduction of poverty in many countries, especially in developing countries. Capturing informal economy is important as it makes visible the works employed by this sector, and their actual economic contribution to the society. However, when economies operate in the informal sector, this operation is tied to operational costs. If informal businesses or employees are caught, they need to pay penalties for not operating in the official market.

Informality in Albania is supported by widespread corruption, the existence of a legal framework which varies at times and whose implementation is arbitrary, yet again for corruption reasons, entangled bureaucratic procedures, lack of information on formalization of businesses, and existence of family businesses – 90% of small businesses in the country.

As Albania transitioned from state-owned economy to market economy, the demography of the country changed. Inner migration was one of the factors that helped the establishment of approximately 800 informal zones. The country is undergoing a process legalization of these zones, where some 150 thousand illegal settlements were established in the last two decades. The Agency for Legalization, Urbanization, and Integration of the Informal Zones/Buildings was mandated to carry this responsibility, and it aims to complete this daunting task by the end of 2013.

Informal economy in the country is showcased in various shapes and forms, such as in the form of rural families that conduct their daily economic activities, family businesses which almost never register
officially; SMEs operating informally using two types of accounts, where officially they report either smaller number of employees or lower wages paid to them, thus evading payment of due taxes; various forms of criminal and illegal activities such as trafficking of narcotics, smuggling, money laundering, whereas they cover their businesses doings as legal businesses, etc.

The system of social contribution in Albania is unstable. It has been calculated that nearly 30 percent of employees in officially registered companies are insured and pay social contributions (UNDP, 2007.) Those that pay contributions reportedly pay minimum pay contributions, thus what the system collects is very minimal, even if contributors pay. Polls show that businesses pay minimum required as they are able to be more competitive, and because everyone acts like this. Another reason is lack of trust in the ability of the state to ensure health needs and retirement pensions for workers in the future. The revenues the Albanian Social Insurance Institute collect would increase if inspectors were incentivized, and thus improve performance.

Labor force polls of 2009 showed that nearly 55.8 percent of general employment in Albania was in the informal economy. This figure includes a number of employees working for family businesses and who are not paid, those working but who do not pay social contributions, all those self-employed and who hire less than five workers. Those employees whose contributions were not paid represented 27 percent. Those at younger age are more exposed to informality, and data showed that mostly men than female are more prone to work informally.

The rate of informality in a country is a pivotal indicator in the study of its economic development. The analysis of informal labor or informality in general helps explain the present condition of the country, especially consolidation of state institutions, level of implementation of legislation, corruption level, to name just a few.

5. References