

Informal Economy and Employment in Albania

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Abstract It's clearly to say that, informal economy is one of the most subjects that have impact in the growth of the country's economy. Discussing about the informal economy, can say that this is a current issue not only for Albania, but also for all those countries in transition. In this paper is intended to analyze: What is the size of informal economy and informal employment (black labor) by sectors, gender, ages and regions in Albania? What is the impact of informal economy in Albanian's growth? Nowadays an important subject is the black labor. The method of regression analysis is used to shed further light on this informal sector's data. The study of this paper is realized on the basis of analysis the impact of informality on the GDP growth. From this analysis can draw conclusions about the sector with the highest level of informality, and it cause a negative impact on the development of economy. Appropriate measurement is therefore of high importance to analyze and design of appropriate strategies to reduce informality. Answering the questions, results a clearly picture about the economic environment of Albania and the things that must to do in order to resolve some of the economic problems.

Key words: informal economy, informal employment, Albanian growth

1. Introduction

Different scholars use different terms to determine informal activity but having substantially the same content, the black work, invisible, hidden. Another definition is "A set of activities that we conducted legally and that principle should be subject to taxation but was not declared as legal and commercial activities that are not included in the value of national income or that partially included in GDP" (ftp://ftp.econ.puc-rio.br/gfranco/Schneider_informal_economy.pdf, accessed 8 November 2011). The informal sector as defined by governments, scholars, banks, etc. is the part of an economy that is not taxed, monitored by any form of government, or included in any Gross National Product (GNP), unlike the formal economy. The most obvious effect of the informal economy is tax evasion, because as has been emphasized the informal sector is the sector that pays no taxes, this reaction leads to reduction of government revenues, causing the vicious circle of informal economy. According to the World Factbook informal economy during 2007, 2008, 2009 it has been calculated that Albania informal economy approximately is close to 50% of the official GDP. (http://ue-varna.bg/uploads/bibl/tom1/Sb_%20tom%201_RB_GD_BM.pdf, accessed 9 November 2011).

2. Literature review

According to the paper by Schneider (2002) Albania is ranked as one of the countries with high level of informality. According to the paper by Olters (2003) in Albanian's case, it is not high tax rates but, to a large extent, the ineffectual and discretionary application of tax laws and governmental regulations that has created the conditions under which the shadow economy is growing. According to the paper by Bode *et al* (2009) arrive to the conclusion that one of the main factors that brought about the development of the informal economy in Albania was the widespread corruption, a legal and sublegal framework that was arbitrary and inconsistent, bureaucracies in the administration, higher level of taxes, lack of information on how they could be formalized.

According to the paper by Gerxhani (2006) were mentioned some suggestions like (<http://ferrer.iae-csic.org/Ferrer-i-Carbonell&Gerxhani.pdf>, accessed 20 November 2011):

- The reduction of entry barriers in the legal labor market for registration of a private enterprise.
- A reform and renovation of the managerial structure of bureaucracies is needed
- International assistance must be directed at creating and reinforcing legal institutions
- Government has to include in its programs measures to strengthen and protect property rights.

According to the paper by Velu (2008) is mention that the experience shows that there is not a magic formula or a solution for transforming the informal economy to formal economy. Reviewing the report prepared by the OECD for Albania (2004), the informal economy with its consequences in terms of tax evasion, labor market distortions and unfair competition, is a major issue in Albania, as well as many other transition economies.

According to the paper by Osmani (2007) arrives to the conclusion that the private sector is destined primarily by the low ratios of taxpayers and public services.

3. Informal Economy and Black Labor in Albania

What cause informality or informal employment? Firstly, all over the world, the share of informal employment, that is jobs performed outside the formal structures that govern taxes, workplace regulations and social protection schemes, is very high. Secondly, informal employment is not withering away. Thirdly, the reasons for informality vary considerably among countries, occupational categories and types of enterprise within a country. For most, informal employment is the only available option and functions as a last resort for people excluded from the formal labor market. Informal workers in developing countries have few social rights, with no social security, severance pay or standards for working conditions.

3.1 Informality and informal employment share by sector, ages and gender

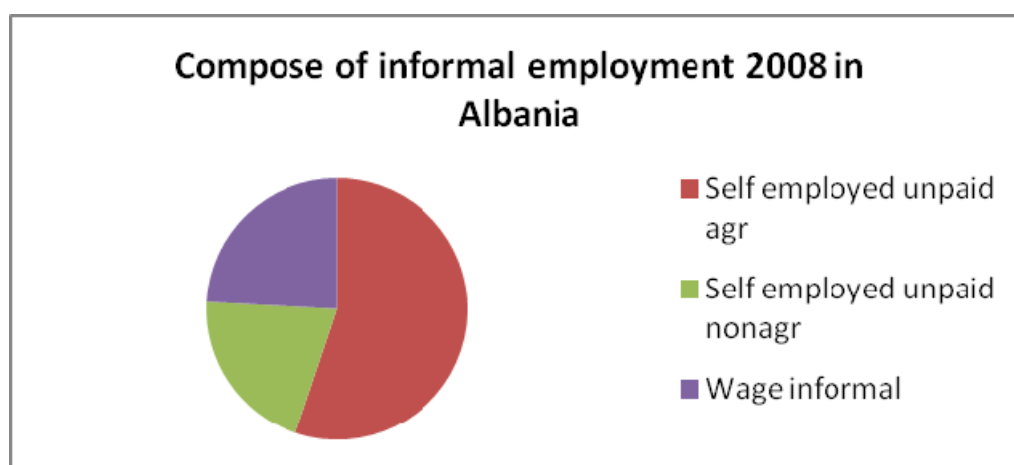
Informal employment can be classified according to major characteristics such as wage employment or self-employment, urban or rural employment, and in informal or formal enterprises, by sectors, gender, ages etc. A set of main employment categories of informal workers can be identified to take into account differences in employment relationships:

- Employer-owners of informal firms,
- Own-account workers,
- Informal employees (of formal and informal firms),
- Sub-contracted workers (domestic workers),
- Casual day workers or unpaid contributing family members,

In non-agricultural sector, 55 % of employment classified as informal. Less educated people, the poor and young people are also those who are overrepresented in the informal employment sector.

Employment of women in the formal sector remains low, compared with male employment. It can be discern a strong correlation between age and informal employment, young people in particular are highly represented, because of a lack of alternatives in the formal labor market. Statistics supplied by the OECD, the OSCE, the EU and the Council of Europe show that the level of informal employment is higher in Albania than in its neighbouring countries. Within the country, no definition on informal employment is agreed upon.

Graph 1. The compose of informal employment in Albania (2008)



Source: World Bank

The informal labor in some sectors mostly in construction, in confection sector, in hotels and restaurants etc continue to be very high. In the construction sector, this indicator is higher. If there are added to this situation the black activity of the informal enterprises not registered in the fiscal administration, the percentage of the black market will be higher. The high level of informal sector, the high level of migration of Albanian people from 1991, the high rate of hidden unemployment in

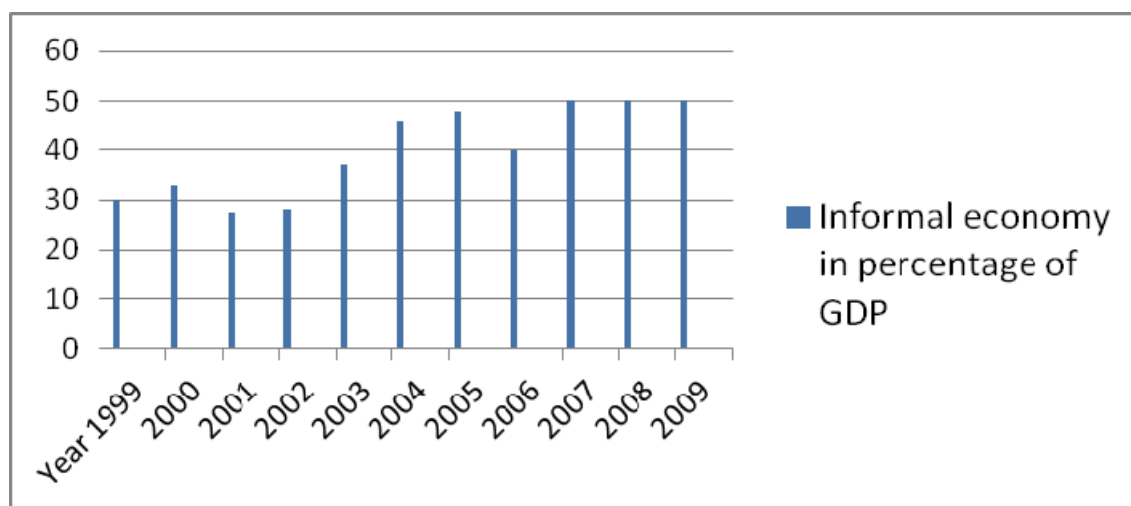
agriculture sector, and the high number of unemployed that are not registered in the public employment service, constitute some of the factors that makes difficult the real evaluation of the unemployment in the country.

3.2 The share and size of informality in the economy

It would be important to note that the changer of demographic map of Albania has created approximately 800 informal zones, with some 150,000 illegal settlements, and which is calculated to have cost between \$3 to \$4 billion. Officially it is reported that about 15 percent of taxes are not paid, but the Albanian reality shows that some 30 percent of taxes are not paid. Quite a few working people may actively choose informality to avoid paying taxes and complying with regulations, and also to put out of social insurance schemes and other public services that they consider low quality. Labor informality is largely a consequence of labor laws and regulations whose very aim is to provide workers with protections and benefits. Some of the most typical forms that informal economy in Albania is displayed are:

- The economic activity of rural families.
- Micro individual or family business, usually temporary and almost always unofficial.
- SME or large businesses that operate at various levels of informality.
- Criminal and illegal activities which are covered up as legal business.
- Companies with foreign capital, independently of their size.
- Informal activities in Albania are two-fold: those generating small revenues or larger profits.

Graph 2. The value of informal economy in years



Source:

- For year 1999-2004, OECD December 2004, (<http://www.oecd.org/dataoecd/27/6/43280298.pdf> , accessed 10 December 2011).
- For year 2005-2006, (www.worldbank.org/PGLP/Resources/AlbaniaPolicyNotes.doc, accessed 9 November 2011).
- For year 2007-2009, (http://ue-varna.bg/uploads/bibl/tom1/Sb_%20tom%201_RB_GD_BM.pdf , accessed 9 November 2011).

3.3 The impact of informal economy on GDP growth

The informal economy brings about a decrease in the economic growth and consequently less trustworthy statistics. The decrease of the informal rates influences economic growth because there is an income increase due to the tax collection and rise in the public expenses. Opposite, the informal economy may be more efficient in terms of competitiveness with the formal sector. High rates of informal economy are result on huge sums of uncollected taxes and this is reflected on the reduction of the state budget income, on the decline of the social and health insurance income; it encourages illegal jobs, makes the quality of goods and services worse, especially when it reaches a considerable size. (http://www.bcentral.cl/estudios/banca-central/pdf/v6/001_010soto_loayza.pdf, accessed 28 December 2011). As mentioned, current GDP estimates incorporate an assessment of informal activity at about one-third of total output.

4. Database, Methodology and Analysis

This paper uses the regression analysis model in order to analyze the relationship between the size of informal economy (ALL) and nominal GDP (ALL) (www.instat.gov.al), and the contribution of it's to the macroeconomic growth. Informal economy (ALL) is supposed: Informal economy (ALL) = Informal economy (on percentage of GDP) x nominal GDP (ALL). For intermediate values of informal economy are used average value. The linear regression equation is as follows:

$$Y = \alpha + \beta X + \varepsilon$$

Where:

(Y) The dependent variable = growth in GDP at current prices (ALL) ; (X) The independent variable = size of informal economy (ALL) ; (β) The coefficient of the independent variable ;

(α) Intercept parameter and (ε) the standard error

Table 1. Data base for regression analysis

Year	Informal economy (% of GDP)	Informal economy (ALL)	Growth in GDP at current prices (ALL)
1999	30	141,527.40	471,758
2000	33.4	174,696.36	523,043
2001	22.7	132,424.76	583,369
2002	23.4	145,714.37	622,711
2003	37.5	260,286.75	694,098
2004	46.5	349,225.23	751,022
2005	48	391,102.56	814,797
2006	38	335,239.42	882,209
2007	50	483,835.00	967,670
2008	50	544,066.00	1,088,132
2009	50	571,805.00	1,143,610

Source: Growth in GDP at current prices (ALL) generated from (INSTAT, <http://www.instat.gov.al/graphics/doc/tabelat/Trequesit%20Ekonomik/Llogarite%20Kombetare/LLK2011/tab2.xls>, accessed 10 December 2011).

Informal economy (% of GDP):

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-For year 2005-2006, (www.worldbank.org/PGLP/Resources/AlbaniaPolicyNotes.doc, accessed 9 November 2011).

-For year 2007-2009, (http://ue-varna.bg/uploads/bibl/tom1/Sb_%20tom%201_RB_GD_BM.pdf, accessed 9 November 2011).

According to the regression result:

X Variable coefficient = 1.3262808 ; Intercept coefficient = 350977.27179 ; R Square = 0.932960 Standart Error = 0.118507 ; t statistics = 11.19151

So, estimated regression equation is as follows:

$$Y_i = 350977.27179 + 1.3262808 \cdot X_i$$

t statistic is the significance test for an estimated parameter in regression using the *t distribution*. The higher this calculated t ratio is, the more confident . In that case, $y = 350977.271 + 1.326 \cdot x$; **t statistic (11.19)** ; **F statistic (125.24)**

It can be estimated GDP growth by using predicted regression equation as in the following table:

Table 2. Predicted GDP growth

Year	Informal economy (ALL)	Growth in GDP at current prices (ALL)	Predicted Y
1999	141,527.40	471,758	538,642.60
2000	174,696.36	523,043	582,624.65
2001	132,424.76	583,369	526,572.51
2002	145,714.37	622,711	544,194.53
2003	260,286.75	694,098	696,117.50
2004	349,225.23	751,022	814,049.92
2005	391,102.56	814,797	869,579.26
2006	335,239.42	882,209	795,504.74
2007	483,835.00	967,670	992,542.48
2008	544,066.00	1,088,132	1,072,408.79
2009	571,805.00	1,143,610	1,109,190.70

It must be compared the calculated t ratio to the critical value of the t distribution with $n-k=11-2=9$ df given by Table of t distribution. This t test of the statistical significance of the estimated coefficient is performed at the 5 percent level of significance. Thus, at 0.05 level of significance in Table of t distribution and at 9 df, it is founded that critical value of $t=2.26$ for this two-tailed t test.

In that case, calculated value of $t=11.19$ exceeds the tabular value of $t=2.26$ for the 5 percent level of significance with 9 df, the null hypothesis is rejected that there is no relationship between X (value of informal economy in ALL) and Y (growth in GDP at current prices ALL) and the alternative hypothesis is accepted that there is in fact a significant relationship between X and Y . The analysis of variance uses the value of the F statistic, or F ratio. Using the values of $R^2 = 0.932961$, $n=11$, and $k=2$ for that case, it is obtained $F=125.24$. It is compared the calculated or regression value of the F statistic with a critical value from the table of F distribution. To determine the critical value of F that it is founded in the table for the 5 percent level of significance is 5.12. Since the calculated value of the F statistic of 125.24 exceeds the critical value of 5.12 for the F distribution with 1 and 9 df, the null hypothesis is rejected that there is no relationship between X (value of informal economy in ALL) and Y (growth in GDP at current prices ALL) and the alternative hypothesis is accepted that there is in fact a significant relationship between X and Y .

Conclusion

According to the regression result, it can clearly say that there is a strong relationship between Albanian GDP growth and informal economy growth or size. The coefficient of determination explains important and significant relation between macroeconomic performance and informal economy growth. As a result, Albanian informal economy maintains the sustainable important role and key determinant in determination of macroeconomic performance or economic growth in the long run.

Annex:

SUMMARY OUTPUT

Regression Statistics	
Multiple R	0.965899
R Square	0.932961
Adjusted R Square	0.925512
Standard Error	61427.43

Observations	11
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ANOVA					
	<i>df</i>	<i>SS</i>	<i>MS</i>	<i>F</i>	<i>Significance F</i>
Regression	1	4.73E+11	4.73E+11	125.2499	1.39E-06
Residual	9	3.4E+10	3.77E+09		
Total	10	5.07E+11			

	<i>Coefficients</i>	<i>Standard Error</i>	<i>t Stat</i>	<i>P-value</i>	<i>Lower 95%</i>	<i>Upper 95%</i>	<i>Lower 95.0%</i>
Intercept	350977.3	42299.69	8.297396	1.65E-05	255288.7	446665.8	255288.7
X Variable 1	1.326281	0.118508	11.19151	1.39E-06	1.058198	1.594364	1.058198

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