



STEG-PEDL Virtual Course on 'Private Enterprises, Productivity and Economic Growth'

Session 4: Friday 27th February 2026

[Gabriel Ulyssea](#)

[Lecture Slides](#)

[Video](#)

Q: Why was there no data on Nigeria on the map?

A: Probably lack of appropriate data from labor force surveys. Not all countries ask questions about this.

It could also be a lack of comparable data. They may collect something but not comparable to other countries.

Q: Reality shows that even if $V_f > V_i$ firms remain in the informal sector - any thoughts on that?

A: One reason might be that there are costs or returns that are not easily observed... So the calculations that you are thinking about might be missing some important dimensions of costs and returns.

Q: If the policy implications are this obvious, why still we observe this much informality?

A: There are positives to informality as well, especially in places where there is limited social insurance. He just said that the costs of enforcement exceed the benefits to tax revenues.

I think Gabriel will be addressing this later.

Q: Does this model match with self-reported reasons for remaining formal, when we speak to small firms? Like, do we think that all informal firms are seeking to maximize profits from that firm alone (e.g. versus diversification of income streams across multiple livelihoods)?

A: I think the cost of formalisation is a big deterrent, and there is some literature that suggests reducing costs to nearly nothing does increase registration.

This is a great question, especially (I think) when you start looking at self-employed people and very small household enterprises -- as distinct from the slightly larger firms that are more specialized. There is an old literature from the agricultural development literature, on the "agricultural household model," which assumes that households have potentially many different activities and face missing markets for inputs and outputs. In that case, the household decision gets divorced from profit maximization, and firms are understood as embedded in a more complicated utility maximization problem.

See: <https://documents.worldbank.org/en/publication/documents-reports/documentdetail/621291468739297175>. A classic reference.

Q: Is informality always inappropriate, or does it depend on the context?

A: it's "inappropriate" or not, it's definitely a feature of reality, and so it's worth understanding what are the drivers and forces that affect it... And what are the implications of having high informality in economies.

I think Gabriel will touch on this.

Q: How do we observe informality in the data? Informality seems to be not well recorded in even census data, right?

A: Some countries like Brazil and Mexico collect these data quite well. The key is to make sure that people trust that the data collection efforts are not linked to enforcement.

But that means that a lot of the work on informality is done in these countries.

Q: Descriptively, do we know how often firms directly incorporate into being formal firms, versus operating as informal firms for a while and then formalizing?

A1: John Sutton did a lot of work on this about fifteen years ago, looking at formal firms in three (?) countries in Africa. Pretty sure this was Ethiopia, Tanzania, and maybe Uganda. He did "enterprise maps" in which he essentially collected qualitative data from all of the large firms in those countries: <https://www.theigc.org/collections/enterprise-map-series>. (There were countably few of them.) I think a recurring finding in those economies -- though probably not transferable to Latin America -- was that all of these firms had essentially come into being as large firms. None had started as small informal firms and then grew. A recurring theme was that these were trading companies that then branched out into other activities. My hunch is that this will differ a lot across countries, but I do think this will be true for a lot of African contexts.

A2: There is mixed evidence on this. For large formal firms, they almost always start formal (see LaPorta and Shleifer (2014)). But in a formalisation policy change in Mexico, Kaplan et al (2011 JPubE) finds one thing and Miriam Bruhn uses different data to find another. (And now I can't remember which of them says that the formal firms come from informal and which says they are new entrants!)

Q: How is this pre-entry signal measured in the data?

A1: It's not; but the fact that there is an overlap in the productivity distributions of formal and informal firms can be explained in this way.

A2: I doubt that it is measured in the data. The idea that people have some sense of their productivity is used to explain why more productive firms tend to be formal. The idea people don't perfectly know their own productivity is used to get overlapping distribution.

Q: Does that mean extensive > intensive margin?

A: Both margins turn out to be important!

Q: In response to trade openness: conceptually, it could also be that formal firms decrease informal workers because of stronger legal enforcement linked to increased trade (eg the importer sets standards for the exporting country), is this something that is observed?

A: Really interesting question. Certainly we know that participation in some of these value chains requires formalization and compliance with some set of regulations. So that wouldn't be surprising.

Q: Bolivia has an 85% informality rate, which rises to 91% if public sector employment is excluded. Are there other factors that should be considered in these cases, such as network externalities?

A: I think Gabriel is making the point that the focus on formality may be taking us down a slightly unhelpful path, as opposed to focusing on firm productivity. The prevalence of informality may be a symptom of an economic environment where many firms are optimally very small, and where small firms find little benefit in formalizing. So maybe we ought to be asking why it's so many firms find it desirable to operate at such small scale...

Q: The recent market labor legislation reform in Argentina focuses on hiring/firing costs reduction for firms, to increase formal employment. The creation of an "unemployment insurance" and the elimination of current rigidities are key points. What could be possible effects on the extensive/intensive margins?

A: I think these are the kinds of policies that can be well modeled in the kind of framework that Gabriel is presenting. There are likely effects on both extensive and intensive margins. But I think the broader point is that the overall high prevalence of informality may be pretty sticky, as Gabriel is explaining.

Q: But don't we care about a few high potential firms growing a lot? If that creates employment and lower cost goods?

A: I think the point is that most of the high potential firms enter as formal firms. (They may still have informal workers at the intensive margin.)

Q: If you have a question for Gabriel for the Q&A, please respond to this comment. Let's collect some. (Editor's note: see video for answers).

Q1: Gabriel said that the elasticity of interventions to formality have to be too high to justify expenditures in interventions (if I understood correctly). Has this been studied in a general equilibrium setting? I can think about social benefits from formalization coming from different channels than tax collection.

Q2: Also, Brazil was the Latin American country that advanced the most in terms of formality in Latin America in the 21st century. What lessons can other developing countries learn from the Brazilian experience?

Q3: Bolivia has an 85% informality rate, which rises to 91% if public sector employment is excluded. Are there other factors that should be considered in these cases, such as network externalities?

Q4: In the Peruvian case, I have the impression that informality may be sustained as a stable equilibrium linked to weak state capacity. Firms might be responding optimally to low returns to formal status because public goods provision and enforcement are limited. Is there a structural literature that explicitly models informality as an institutional equilibrium of that kind, rather than purely as a distortion driven by taxes or regulation?

Q5: If public procurement expands but formalization does not respond (as in our data), does that suggest that informality is not primarily constrained by demand-side returns, but by deeper institutional features such as weak enforcement or limited state capacity? Is there structural work that models procurement or state demand as part of the equilibrium determination of informality, rather than as a simple formalization incentive?

Q6: A lot of literature assumes that formal jobs are "good jobs" because they come with benefits. But if the state offers good social safety net protections for the elderly, sick, etc., then presumably this takes away some of the reasons why formal jobs are supposed to be good. Does the literature look at this connection?

Q7: Because climate shocks (droughts/floods/hurricanes...) may destroy capital and disrupt economic activity, I can imagine ambiguous effects of those shocks on informality: (1) reduction in the extensive margin because of capital destruction, and maybe other channels (?) (2) increase in the intensive margin because the labor force

may become overall more precarious and seek any kind of employment that provides flexibility. What do you think about this, and do you know of research that looks at the effect of climate change on informality (other than Imbert & Ulyssea 2026 :))

Q8: If I understood: It is argued that informality may constrain long-term economic growth and undermine fiscal revenue mobilization. However, in contexts where many African governments focus primarily on tax collection without delivering visible public goods and services in return, a central question emerges. How can formalization processes be effectively designed and implemented in such settings?