RESEARCH

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Options to Support the Incomes of Informal Workers During COVID-19

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In Emerging Markets and Developing Economies, high informality and weak administrative capacity make it challenging for governments to deliver direct income support necessary to tide workers over the crisis in the presence of social distancing. This note reviews these challenges, existing systems and recent crisis responses, and provides a rough quantification of the costs of expanding transfers to informal workers. A transfer to cover the basic food and energy needs of all informal workers for two months could cost over 2 and 5 percentage points of annual GDP in the median emerging market and low-income economies, respectively. As an illustration, the note quantifies potential fiscal gains from two among several possible funding options.

I. CONTEXT

Emerging Markets and Developing Economies (EMDEs) face unprecedented output drops and job losses following the COVID-19 outbreak. Collapsing external demand, capital outflows, falling commodity prices, and, increasingly, domestic health crises and the associated mitigation measures curtail economic activity. The informal sector, often a buffer in past recessions, has been hit hard. Many informal workers are daily wage earners and self-employed in urban areas, in jobs vulnerable to social distancing, and cannot rely on sufficient personal savings to weather a long-lasting crisis. This also means that mitigation measures are unlikely to succeed in the absence of sufficient government support to induce people to stay at home.

High informality and the low coverage of social protection schemes imply very weak automatic social stabilizers. This strengthens the case for discretionary support to affected workers. Informal workers account for about 50% and 80% of the workforce in EMs and LIDCs, respectively (Figure 1).[1] They have no insurance against the risk of income loss, and only a fraction of them—typically the poorest—receive anti-poverty cash transfers (see below). Therefore, supporting informal workers is warranted for economic, humanitarian and social cohesion motives. Even in the formal sector, unemployment insurance is under-developed—less than half of EMs, and 10%

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[1] The note uses the World Bank's definition of informality. However, there are multiple ways of measuring informality that can yield fairly different estimates—for instance, the national accounts, currency demand or multiple indicators multiple causes (MIMIC) approaches. See Medina and Schneider (2018) for a review.

Figure 1: Share of Informal Workers in Total Employment in EMDEs, by Region (%)
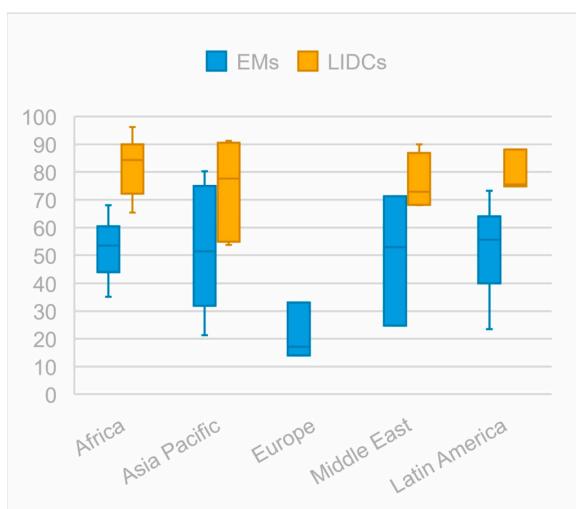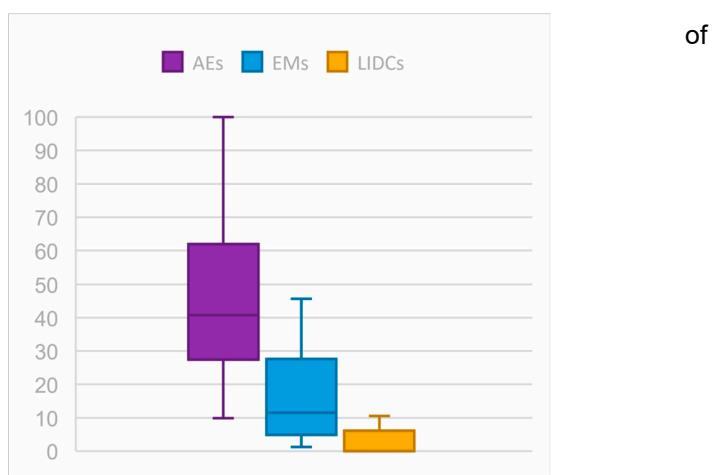
Figure 2: Share of Registered Unemployed Receiving Unemployment Benefits (%)

Source: World Bank and ILO, 2018, or latest year available. *Notes:* dashes indicate the median, boxes plot the interquartile range, and the upper and lower whiskers plot the max-min range; Figure 2 excludes 4 outliers for graphical clarity.

LIDCs, have an unemployment insurance system. As a result, less than 20% of registered unemployed in EMs, and less than 10% in LIDCs, receive some form of unemployment benefit (Figure 2).

Limited fiscal space in most EMDEs adds to these challenges. In the formal sector, the policy tools used in advanced economies—subsidized working-time reductions, unemployment insurance, wage subsidies[2]—can apply, and are also being deployed in a few EMDEs, but this requires fiscal space. So do the policy options available for governments to support informal workers' incomes, which are the focus of this note. Against this background, the note also attempts to provide ballpark estimates of potential costs, and compares them to the potential fiscal gains from illustrative domestic funding options—temporary cuts in public wage bills and taxes on higher incomes, leaving aside the fiscal space that can be built through external debt relief.

The next section (II) goes through available options to reach the informal sector, discussing existing schemes that were already in place before the crisis in EMDEs, recent crisis responses, and delivery issues. Section III provides ballpark estimates of the potential costs of supporting informal workers in EMDEs under alternative transfer levels. To fix ideas, Section IV compares those costs to the potential fiscal gains from temporarily lower public sector wages and higher taxation on higher incomes.

II. OPTIONS TO REACH THE INFORMAL SECTOR

In general, reaching the informal sector is best achieved by reaching its informal workers. By definition, informal firms are hidden from the authorities and, in fact, many of them are non-incorporated self-employed (informal) workers or family firms. Consequently, to support both informal workers and firms, the most straightforward approach is to expand the coverage of existing social assistance programs (e.g. by relaxing eligibility criteria), increasing benefit levels or setting up new transfer schemes.[3]

The need for speedy and contactless delivery of income support puts a premium on cash transfers, especially if delivered digitally, but these may not be feasible at scale and other options need to be

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[2] These options are covered in detail in the IMF Note "Options to Support Incomes and Formal Employment During COVID-19". Further, both types of support are not independent from each other—supporting formal employment can have positive effects on informal workers, directly through family ties and indirectly by curbing competition from displaced formal workers who may otherwise transition to the informal economy.

[3] Not all informal workers work in informal firms. In a country like Mexico, for example, almost one fifth of the workforce consists of informal workers working in formal firms. Supporting formal firms can help this category of informal workers. See also IMF Note on "Managing the Impact on Households: Assessing Universal Transfers."

considered. Mitigation measures suppress the income of most informal workers and need to be accompanied by support for their livelihoods. Urgency calls for prioritizing existing schemes over new ones that may take time to set up. Further, such support should be aligned with the need for social distancing and therefore minimize human contact, particularly given the need to support workers in urban areas. Consequently, expanding current programs, ideally contact-less ones like digital cash transfers, dominate alternative options such as cash transfers delivered through more traditional means, and even more so in-kind transfers. Where the former options are not feasible or not enough, the latter ones have to be pursued. With this in mind, this section reviews the systems already in place and those recently set up in response to the outbreak. It then discusses potential alternative delivery options.

Programs Already in Place Before COVID-19

Because of pervasive informality, social protection in EMDEs comes mostly in the form of social assistance programs. Social assistance programs encompass cash transfers (conditional and unconditional), in-kind transfers, fee waivers (for health insurance, education, housing and utilities), school feeding, public work, social pensions, and other programs such as scholarships. Social insurance programs, instead, provide insurance against various income loss risks. They include contributory, publicly provided or mandated insurance schemes that cover old age, disability, maternity leave, sickness and death (of the main household provider). Finally, labor market programs refer to all passive (e.g. unemployment insurance) and active (e.g. public works or training programs, wage subsidies) labor market policies. Overall coverage in EMDEs tends to be incomplete. Social assistance programs cover 20% of the population in Africa and 40% in Latin America. And the coverage of social insurance and labor market policies is above 30% only in European EMDEs and in the Middle East (Figure 3).
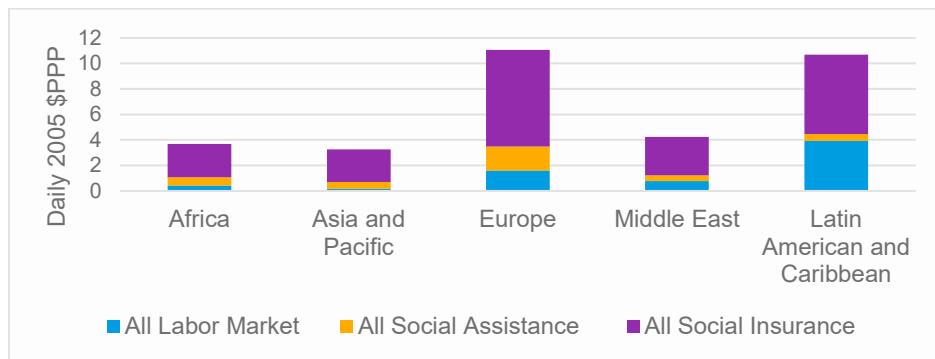
Figure 3: Share of Population Covered by the All Programs
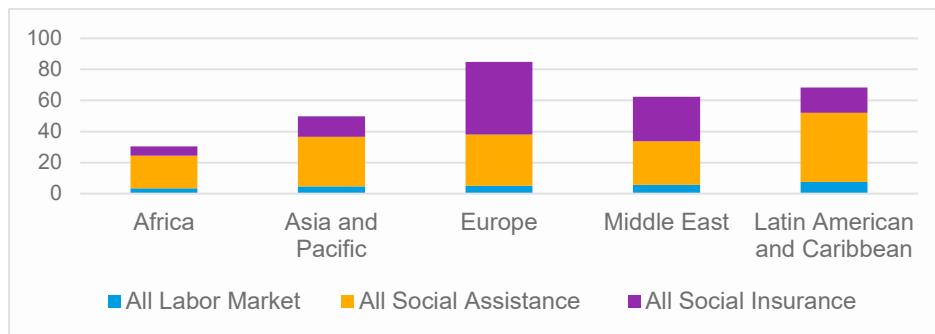
Source: Aspire – The Atlas of Social Protection. Note: Regional values are computed using the most recent available year for each country over 2008-2016. Coverage includes direct and indirect beneficiaries.

Social assistance programs aimed at reducing poverty provide much lower transfers than social insurance schemes aimed at protecting formal workers from income losses. The total amount of daily transfers per capita from all social protection programs ranges from a bit more than $3 per day in South Asia to more than $10 in European EMDEs and Latin America (Figure 4). Out of this total, social assistance programs only provide at most $1 per day in Africa, and even less in other regions, except for Europe, where it amounts to $2 on average. These are low numbers even considering the sizeable share of the population living with less than $3 a day in each region, notably 74% in Africa, suggesting that if these programs are to serve as vehicles of income support during the crisis they will need to be beefed up.
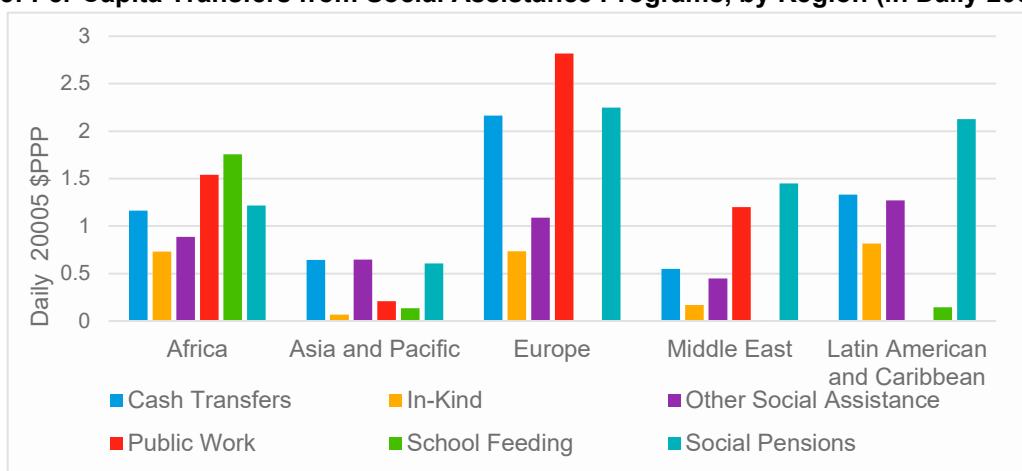
Figure 4: Average Per Capita Transfer Among Beneficiaries in Daily 2005 $PPP for All Social Protection Programs
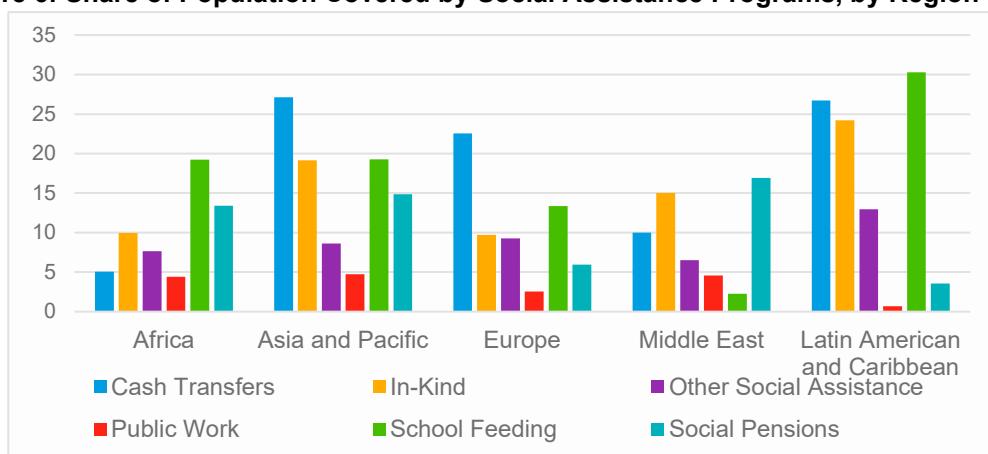
While cash transfers (and non-contributory old-age pensions) make the bulk of social assistance transfers, in-kind transfers and school feeding programs play an important role, notably in Africa (Figure 5). These programs, which may be hard to square with COVID-19 containment measures, have the largest population coverage (Figure 6). This underlines the challenge of not only raising transfer levels but also making delivery more efficient and contactless.

Figure 5: Per Capita Transfers from Social Assistance Programs, by Region (in Daily 2005 $PPP)

Figure 6: Share of Population Covered by Social Assistance Programs, by Region (%)

New Measures Taken in Response to COVID-19

Most countries have introduced new measures in response to the COVID-19 crisis. Most fall into the social assistance category and take the form of cash transfers. As of April 17th, according to World Bank estimates, 133 countries had planned, introduced or adapted 564 social protection measures in response to COVID-19, 60% of which belong to the social assistance category (Figure 7). The total number of beneficiaries from these new social assistance measures were about 622 million individuals (for public work programs) and households (for cash transfers). Cash transfers are the most common tool, accounting for about half of these newly introduced social assistance measures. Social insurance measures for formal workers include paid sick leave, unemployment benefits and wage subsidies, but these are predominantly in advanced economies.

Figure 7: Policy Responses to COVID-19 as of April 17th 2020 (AEs, EMDEs and LIDCs)
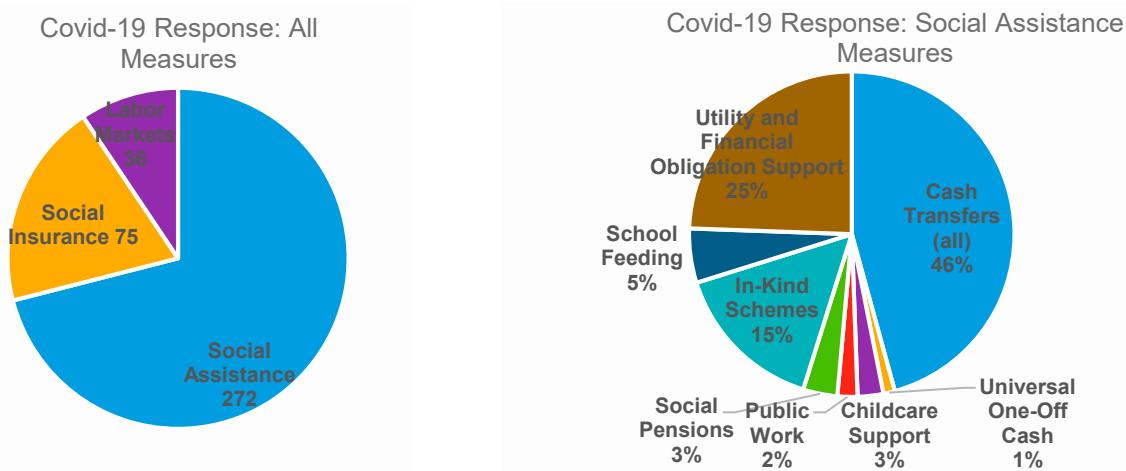
Source: "Social Protection and Jobs Responses to COVID-19: A Real-Time Review of Country Measures", by Ugo Gentilini (WB), Mohamed Almenfi (WB), Ian Orton (ILO), and Pamela Dale (UNICEF).

Delivery Methods for Policy Implementation

A key challenge is to gather enough information on informal workers' characteristics and set up a reliable delivery system to promptly reach the targeted beneficiaries. In general, this puts a premium on scaling-up existing social assistance programs, for example by broadening eligibility criteria and making them unconditional (e.g. on participation in education or health programs). In many cases, however, existing databases may be too narrow to enable this, putting informal workers at risk of being covered neither by (formal) social insurance systems nor by extended social assistance programs—the "missing middle." This should push governments to explore alternative information databases and methods that can ensure speedy delivery while keeping transfers reasonably well-targeted.

The ideal integrated system entails: (i) a universal ID system; (ii) ID-specific links to socioeconomic data on households and individuals; and (iii) an effective mode of benefit delivery.[4] However, only very few EMDEs meet these criteria, reflecting the incomplete coverage of, and insufficient integration between, various information sources. There is wide dispersion in the coverage of a National ID system across countries,

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[4] See also the IMF note "Reaching Households in Emerging and Developing Economies: Citizen ID, Socioeconomic Data, and Digital Delivery".

especially in Africa and in the Asia Pacific region (Figure 8). Likewise, social registries, which often link IDs to relevant individual socio-economic indicators, have quite uneven coverage across countries (Figure 9), with Pakistan's covering 87% of the population relative to Mali's 3%. In the future, investing in the expansion of the coverage of the Integrated Social Registries will be critical as they can used as gateways to multiple programs. For instance, Mexico, Montenegro, Brazil, Chile, and Colombia run around two dozen programs with their Social Registry.[5]

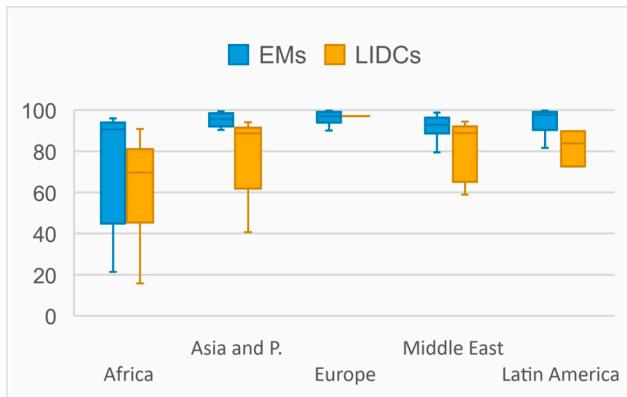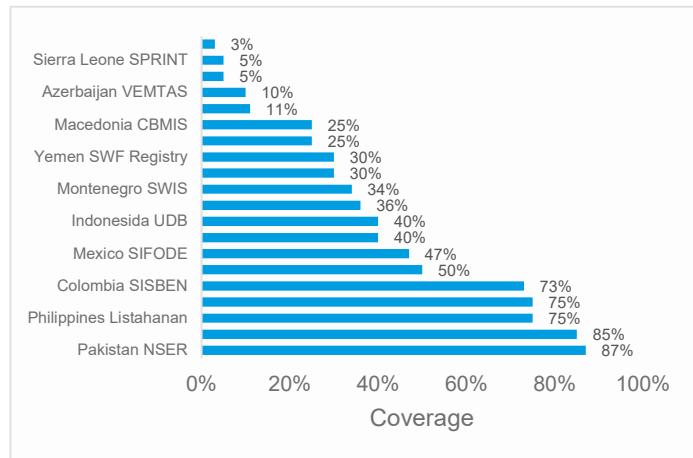**Figure 8: Share of Population with a National ID (%)**

Figure 9: Coverage of National Social Registries (%)

Source: Global Findex. *Notes:* dashes indicate the median, boxes plot the interquartile range, and the upper and lower whiskers plot the max-min range.

Source: Leite, P., George, T., Sun, C., Jones, T. and K. Lindert (2020); "Social Registries for Social Assistance and Beyond: A Guidance Note & Assessment Tool."

Digital delivery methods are the most appropriate. Specifically, automatic transfers on people's bank accounts or phone applications should be prioritized where bank and/or phone coverage is broad enough—with the latter being also particularly useful to scale-up the coverage of existing Official Registries (as in Azerbaijan, Chile and Turkey). Successful examples of digital delivery include Togo, which introduced a new cashless transfer program (Novissi) targeting adult informal workers, and Thailand, with the digital payment platform PromptPay. However, where bank and mobile phone coverage is low alternative approaches are needed. Coverage is very heterogeneous across countries, averaging below 40% across all LIDCs (Figure 10, Panels A and B). In some cases, as a last-resort option, alternative approaches such as utility subsidies may be useful if the share of population paying utility bills online is significantly broader (see Figure 10, Panels C).[6] To avoid generating losses and eventually utility supply disruptions, the cost of such subsidies should be covered by the government through on-budget transfers to utility providers—SOEs, in a number of cases—and such subsidies should have a clear sunset clause to ensure they are removed during the recovery.

Delivery of in-kind support should be left as residual option whenever it cannot be done via mail. This type of support is less efficient since it restricts recipients' choices, and it involves physical interactions that can fuel the contagion.[7] Alternatively, governments should consider mailing pre-paid cards covering essential purchases.

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[5] See Leite, P., George, T., Sun, C., Jones, T. and K. Lindert, 2020, "Social Registries for Social Assistance and Beyond :A Guidance Note & Assessment Tool"
[6] A main drawback to relying on utility bill subsidies, however, is the common practice to steal electricity in many EMDEs, so that access to electricity (virtually 100% in many EMs, see Figure 10 Panel D) is not necessarily informative of the potential coverage of a utility subsidy.

[7] However, governments may well need to take other, separate measures to protect food supply chains and thereby ensure that recipients can spend their cash transfers on adequate food supplies.

Figure 10: Population Coverage of Potential Delivery Means (%)

Panel A

Mobile and/or Bank Account %

Panel B

Mobile Account %

Panel C

Paid Utility Bills Online %

Panel D

Access to Electricity %

Source: Global Findex. *Notes:* dashes indicate the median, boxes plot the interquartile range, and the upper and lower whiskers plot the max-min range.

III. HOW MUCH WOULD IT COST TO SUPPORT INFORMAL WORKERS?

Most EMDEs have binding fiscal constraints. It is then critical to provide the potential magnitude of the cost of supporting informal workers during this crisis. As base metric, and leaving aside delivery issues, a two-month cash transfer is considered, focused on poverty alleviation. This transfer is assumed to reach the fraction of the population not covered by existing social insurance or social assistance programs (as a proxy for the so-called "missing middle"), and to cover average consumption of food, utilities and electricity for a two-month period (the potential duration of the containment measures).[8] Such a transfer would mitigate poverty but would not replace informal workers' incomes—and as such may not be large enough to keep them at home. The latter option would be costlier, particularly in the more advanced EMDEs where informal workers' income can significantly exceed the cost of a basic consumption basket.

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[8] The basic basket considered excludes shelter costs as these may be alleviated in the short term through executive orders to delay rent payments. As a benchmark, in the average country in our sample, close to 60% of expenditures are accounted by food, utilities, and energy while around 10% goes to housing.

The theoretical two-month transfer could cost about 2.2 and 5.7 percent of annual GDP in the median EM and LIDC, respectively; more if the transfer were to include also social assistance recipients. Figure 11 plots, for each region and country income group, the distribution of the costs of a targeted transfer for basic consumption goods.[9] While the calculation is certainly coarse, using mean values and ignoring consumption disparities, it still provides useful insights. Most importantly, it shows that such transfers are more affordable for the more advanced EMDEs because the fraction of income spent on food, utility, and electricity is lower, and the fraction of population already covered by social assistance and insurance is higher. If the transfer were extended to all those that do not have social insurance—including those that already receive social assistance— the total cost for the median EM and LIDC would increase by some 3 and 1.2 percentage points, respectively.[10] For comparison, the cost of current social assistance programs ranges between 0.5 and 1.5 percent of GDP in the typical EMDE.

Figure 11: Fiscal Cost of a 2-month Targeted Transfer for Food and Energy Consumption
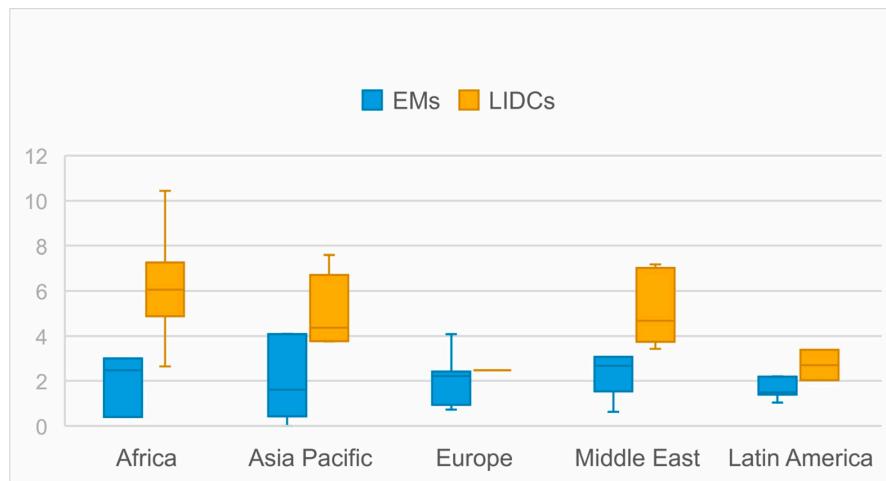
Source: World Bank Global Consumption Database; IMF World Economic Outlook, and authors' calculations. *Notes:* dashes indicate the median, boxes plot the interquartile range, and the upper and lower whiskers plot the max-min range.

IV. FINANCING THE FISCAL COST OF TRANSFERS

EMDEs where transfers are more needed are also those where costs would be higher and delivery more challenging, and where public finances tend to be stretched. Countries with high informality tend to have lower social programs' coverage and weaker fiscal positions (Figure 12).

Multiple funding measures might be considered to build the necessary fiscal space. These may include, for example, broadening the base of existing taxes, postponing non-essential public investments, temporary reductions in the public wage bill or extraordinary income measures (such as solidarity levies). Further fiscal space may be built through external support in the form of debt payment deferrals, debt relief, and other multilateral and bilateral transfers that go beyond the scope of this note. For illustrative purposes, the analysis

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[9] The cost of targeted transfer for basic consumption goods is calculated as: (Private Consumption Expenditure as % of GDP)*(Fraction of Consumption Expenditure Spent on Food, Utility, and Electricity for an average household)*(1-(fraction of population receiving social assistance and/or insurance program)), at the country level. Data on private consumption expenditures are retrieved from World Economic Outlook. Fraction of consumption expenditure spent on food, utility and electricity is retrieved from World Bank Global Consumption Database. Lastly, data on the fraction of population receiving social assistance or insurance program is retrieved from The Atlas of Social Protection Indicators of Resilience and Equity (ASPIRE) by World Bank. If the transfers were instead focused only on food, the average cost would decline by around 10 percent in EMs and by almost 15 percent in LIDCs, reflecting the higher share of food in the latter's consumption basket.

[10] The additional cost would be higher for EMs due to a higher coverage of population under social assistance.

below provides rough estimates of the potential gains from two domestic measures that governments might be tempted to consider, and some of them are actively contemplating or implementing: temporary cuts in public wage bills and increases in the taxation of higher incomes. As with the transfer cost estimates above, these simple calculations aim to provide rough estimates of potential fiscal gains and abstract from important practical issues—such as some countries' limited ability to collect income taxes.

**Figure 12: Social assistance/insurance coverage, Informality and Strength of fiscal positions in EMDEs**
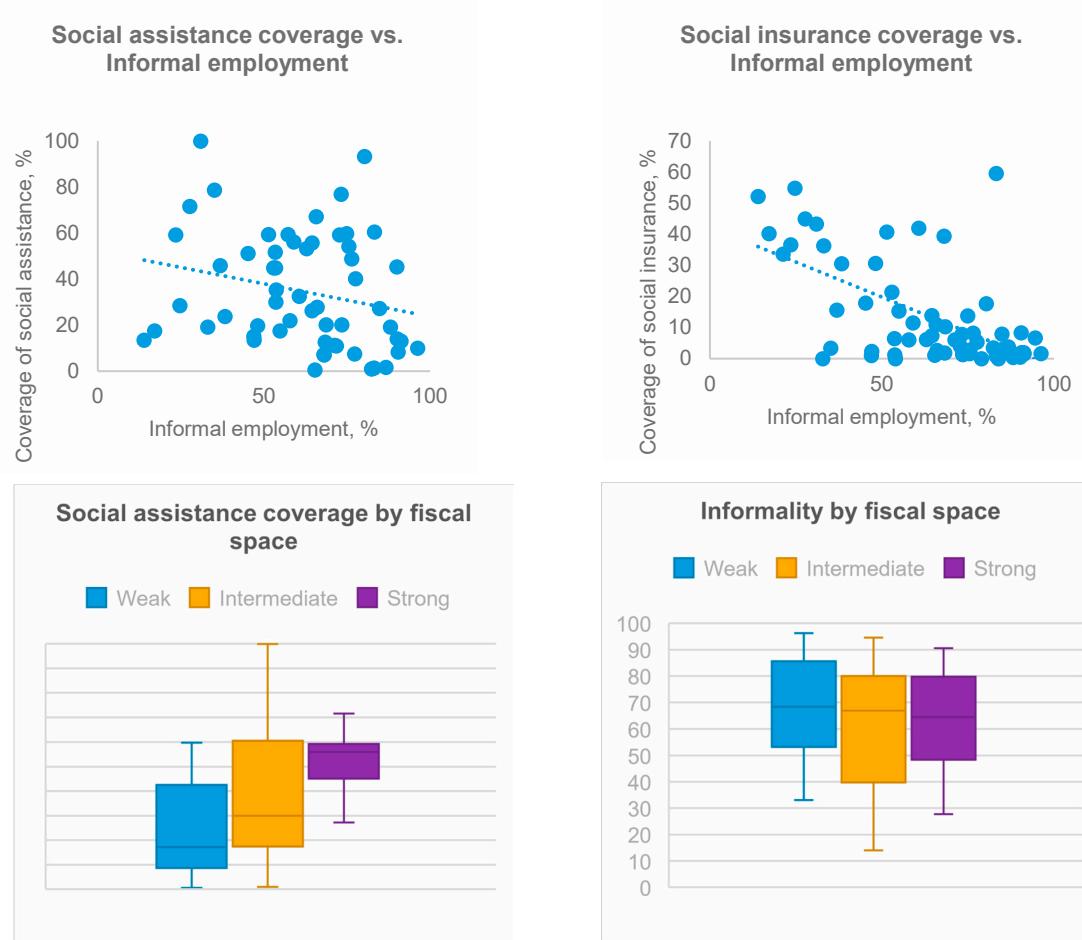
Source: IMF, World Bank Aspire, and ILO, 2018 or latest year available. *Note:* Strength of fiscal space is measured based on public sector liabilities. Coverage of social assistance and social insurance programs is denoted in percent of population, informal employment is denoted in percent of non-agriculture employment. Dashes indicate the median, boxes plot the interquartile range, and the upper and lower whiskers plot the max-min range.

A temporary public wage bill cut for one year could provide some of the funding for expanded social transfers, but it would still leave a sizeable financing gap.[11] Governments might be tempted to consider this option on three grounds: (i) public sector workers are less affected than others by the crisis, since they typically keep their jobs and incomes; (ii) they enjoy a wage premium over private sector workers (of over 10 percent on average across EMDEs, albeit with significant variation across countries, see IMF 2016: "Managing Government Compensation and Employment- Institutions, and Reform Challenges"); (iii) unlike many other options such as increased income taxation, it would immediately strengthen the government's cash position and thereby free up

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[11] Examples of countries considering cuts to public wages including Albania, Brazil, Colombia, Rwanda, and Uruguay. See IMF Note "Issues When Cutting Government Pay to Help Reshuffle Spending in a Crisis" for a detailed discussion on this topic.

cash for urgent spending. It could also be designed to meet some progressivity objectives. At the same time, (i) a large fraction of public sector workers are essential workers in education or health, who should arguably be exempt from any public wage cuts, considerably reducing the potential fiscal gains; (ii) the public sector wage premium is bigger among lower-skilled workers, reducing the progressivity of the measure all else equal; (iii) public wages support extended families and aggregate demand in many EMDEs; and, (iv) such a pay cut could be potentially challenged from a legal standpoint in some jurisdictions, and might also be politically difficult to implement.[12] All of these important issues should be factored in when contemplating any public wage bill reduction. Bearing these concerns in mind, Figure 13 plots the estimated fiscal savings from an illustrative, broad-based, temporary 15% public wage cut for one year.[13] Such a cut would go some way toward funding expanded transfers but would still leave a sizeable financing gap, especially in LIDCs.[14] In EMs, this would cover around 57 percent of the total cost of targeted transfers as roughly estimated (in Figure 11) above. In LIDCs, the corresponding number would be about 16 percent, reflecting the higher fiscal cost of the transfer and, to a lesser extent, the smaller share of the public wage bill in GDP (9.4 and 7.4 percent of GDP in the average EM and LIDC, respectively; IMF 2016).

Figure 13. Fiscal Savings from 15% Public Wage Cut for One Year (% of Annual GDP)
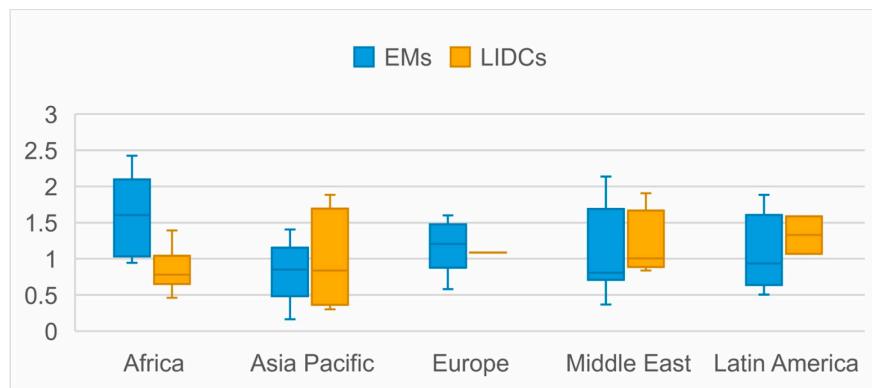
Source: IMF World Economic Outlook, and authors' calculations.

A temporary tax on the top 10% income earners could provide complementary financing, especially in the more advanced EMDEs. An important advantage of income taxes is that they can be designed to achieve progressivity and income redistribution. However, because of widespread informality, tax exemptions and expenditures, and tax collection issues, the share of households that actually pay income tax is relatively small in many EMDEs. In addition, some high-income earners, such as owners of small-and-medium-sized enterprises, are severely affected by the crisis. To illustrate the potential fiscal gains from a temporary (one-year) tax hike on higher incomes, and abstracting from behavioral responses and tax collection issues—both of which imply lower gains than estimated here, Figure 14 shows the tax rate that would have to be levied on the top 10% of households to cover the cost of expanded transfers as discussed above (using information from the World Inequality Database to infer how much income the top 10 percent of households hold as a share of GDP in each country). The required increase in taxation appears to vary immensely across countries, partly because the cost of transfers is much larger (as a share of GDP) in lower-income countries and, to a lesser extent,

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[12] An alternative option might be a public wage deferral via bond issuances, but at the cost of raising fiscal debt burden over the medium term. For instance, governments could issue a one-year bond and replace a fraction of public sector wage payments with bonds and pay back one year later.

[13] This calculates the percent of the total cost of targeted transfer program that can be covered by 15% of public sector wages. The data on public sector wages are for 2018, retrieved from the IMF World Economic Outlook database.

[14] Those countries without access to financial markets would also face a liquidity issue, since the wage cuts would save on expenditures gradually (every month over a year) while the expansion of cash transfers would have to take place upfront (over two months, under the illustrative assumption retained here).

because the income share of the top 10 percent also varies. In many advanced EMDEs, a 3 percent tax rate hike would be sufficient to cover two months of transfers for those that do not benefit from the current welfare system, while in LIDCS is the required tax rate hike would have to be 4 times larger on average.

Figure 14. Temporary Tax Rate on Higher Incomes Required to Cover Targeted Transfer (%)
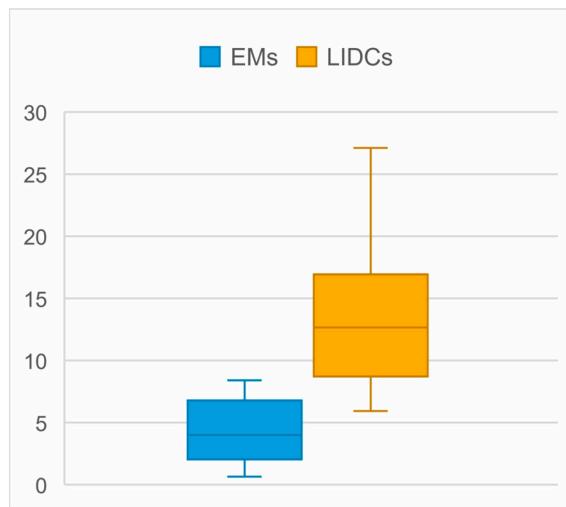
Source: IMF World Economic Outlook, World Inequality Database, and authors' calculations. *Notes:* Dashes indicate the median, boxes plot the interquartile range, and the upper and lower whiskers plot the max-min range.

V. CONCLUDING REMARKS

The COVID-19 crisis presents unique challenges for Emerging Markets and Developing Economies (EMDEs) as high informality and weak administrative capacity make it hard for governments to deliver the direct income support necessary to tide workers over the crisis in the presence of social distancing measures. This note provides a rough quantification of the costs of expanding transfers to informal workers and reaches the following conclusions: 1) Supporting informal workers' basic food and energy needs for two months would cost between 2.2% and 5.4% of GDP for the median EM and LIDC, respectively, with great heterogeneity across countries. 2) EMDEs where transfers would be more helpful tend to be those where costs would be higher, delivery more challenging, and public finances more stretched. This calls for domestic funding measures, in addition to external debt payment deferrals and relief that might be negotiated on the international arena. As an illustration, simple calculations point to significant potential fiscal gains from temporarily higher taxation of high incomes and lower public wage bills—two among several measures some EMDE governments have been considering. 3) Logistically, digital cash transfers, the preferred option (fast and contact-less), cannot be easily ramped up in countries without an existing appropriate infrastructure. Governments need to explore alternative databases and delivery options, including more unconventional ones.