



INSTITUTE FOR ECONOMIC RESEARCH ON INNOVATION
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The Informal Economy in Developing Nations: Hidden Engine of Innovation ?

- New economic insights and policies –

**Project implementing WIPO
Development Agenda Recommendation 34**

prepared Jacques Charmes and by the WIPO Secretariat

The Informal Economy in Developing Nations: Hidden Engine of Innovation ?

- Despite the importance of the IE, little is known about how new processes, products, and other innovations are generated and monetized in the IE.

- Three core questions
 1. How does innovation occur in the IE, how is it diffused, who are its actors and what are innovation impacts?
 2. How do inventors in the IE reap the benefits of their innovations? What forms of appropriation are in use?
 3. What are suggested policy recommendations to improve innovation impacts in the informal economy?

Contributions of this CDIP project

Opening a window to an important facet of innovation which has not been explored before

- the first set of cross-country comprehensive studies into the informal sector
- bringing hitherto separated experts of the informal economy, innovation and IP together

Supporting the innovation measurement agenda

- groundwork for future empirical work
- 2nd African Innovation Outlook

Contributing to a new stream of policy-making – innovation policies to cater to IE

- UN 2013 Annual Ministerial Review of the Economic and Social Council 14 March 2013

1. What is the informal economy and how large is it?

- Since its invention in the early 1970s In Ghana and Kenya, many tentative definitions have been given
- However the statistical concepts that allow an homogeneous and harmonised measurement of the phenomenon have been established under the auspices of ILO

International definitions

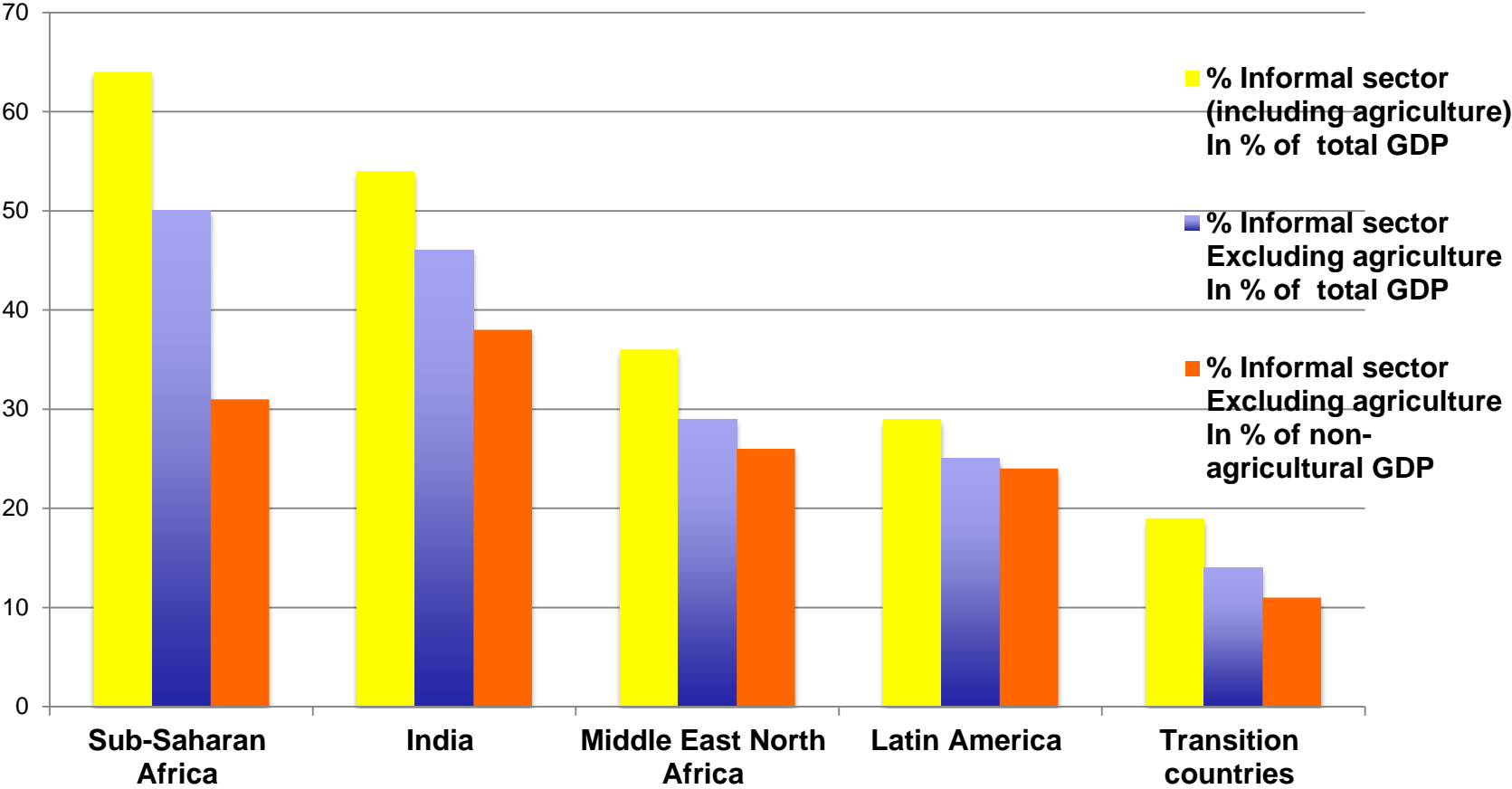
The informal sector defined by the 15th ICLS in 1993 is an establishment- or enterprise-based definition: *all unincorporated economic units not registered and/or not registering their employees, and/or under a size threshold of 5 permanent paid employees*

The informal employment defined by the 17th ICLS in 2003 is an individual-/job-based definition: *all occupied persons not affiliated to social security or without written contract*

The Informal Economy is important contributor to employment in Africa and elsewhere

- At end of 2010s, employment in the informal economy accounts for on average 70% of non-agricultural employment in Sub-Saharan Africa and also in Southern and South-Eastern Asia 53% in Northern Africa and 57% in Latin America
- The IE has an important social dimension: for many people, and especially the poor, it is the only means for earning a living

Contribution of informal sector to GDP



2) What innovation is taking place in the IE and how?

- Large amounts of constraint-based innovations take place under conditions of scarcity and constraints.
- Innovation is rarely driven by R&D but is often driven by knowledge gained through adopting, adapting and improving to solve problems.
- overcome shortcomings of the formal economy and/or to adapt foreign products to local conditions.

2) What innovation is taking place in the IE and how? C'ed

- Firms in the IE tend to operate in clusters
- Low capital intensity, limitations to technical upgrading and limited skills.
- Supply and demand interactions play an important role in IE
- Skills are acquired through early formal education, learning-by-doing through work experience, and learning-by-training through apprenticeships in the informal or formal sector.
- Information diffuses freely - The copying of ideas is rapid.

Barriers to Innovation in the IE

Location and infrastructure constraints	Lack of space and infrastructure to expand operations paired with inconsistent energy supply and other factors
Financial constraints	Capital market imperfections, risk and uncertainty coupled with risk aversion, pressure to achieve immediate return, and lack of demand for informal sector products
Skill constraints	Lack of competencies and skills, including entrepreneurial ambition
Information constraints	Imperfect functioning of the information market about new machines
Social constraints	Relating to the need of entrepreneurs to share their profits with a family or extended network or to invest in informal collective social insurance schemes (discouraging them from developing their business in the first place) or to employ family members such as sharing obligations with the extended family
Institutional constraints	Such as ill-managed government regulations and exposure to corruption and the lack of insurance

3) Which mechanisms are used in the IE to appropriate innovation?

Actors in the IE
either

- pay less attention to appropriating their innovation, or
- (b) rely on semi-formal or informal rather than formal appropriation mechanisms.

Distinct approaches
to passing on and
keeping knowledge
confidential, most
often relying on

- secrecy
- particular codes to transmit knowledge or oral transmission of techniques and skills,
- tacit knowledge systems.

4) What are policy implications and future work strands?

- No uniformly agreed policy framework targeted at the IE.
- Existing IE policies were aimed at suppressing informality.
- Policy ambitions are shifting in part from suppressing the IE to creating an enabling environment for the IE.
- Proposal of a new policy framework

SECOND PART

Preliminary policy framework for IE innovation

1) Providing a functioning property rights system and functioning economic institutions

2) Improving the infrastructure and providing urban spaces

3) Facilitating access to markets and participation in the formal economy

4) Providing access to finance

5) Improving education and skills, including entrepreneurship capacity

Preliminary policy framework for IE innovation

6) Fostering the innovation system and improving the capacity to innovate

- Assess or quantify the contribution of IE innovations
- Facilitating start-ups
- Stimulating linkages between formal and informal actors
- Facilitating the assimilation of innovations created elsewhere
- Implementing demand-side measures
- Improving IE actor organization

7) Intellectual property policies

- Needs assessment – Establishing the relevance of IP system (unique inventor, novelty, etc.)
- Overcoming the hurdles in accessing the IP system
 - Dealing with access barriers: Awareness-raising, costs, processes and training on IP
 - Technological information and advisory services +++ Financial assistance
 - Assistance in IP exploitation and technology transfer
- Redesigning certain features of the IP system

Outlook on next steps of the project

- **MORE SECTORS OR COUNTRIES:** systematically assess the structural forces as play that make informal innovation and appropriation more/less effective.
- **DOCUMENTING AND SEEKING TO UNDERSTAND THE INFORMAL IP-LIKE MECHANISMS THAT HAVE EMERGED IN THESE SECTORS**
- **ADVANCING THE POLICY SUGGESTIONS AGAINST THE ANALYTICAL FINDINGS.**