



INFORMAL EMPLOYMENT: SYSTEMATIC ANALYSIS OF ECONOMIC, SOCIAL AND LEGAL NEGATIVE CONSEQUENCES.

Mamatkulova Mushtariy

Doctoral student at the Scientific Research Center
“Scientific foundations and problems of
economic development of Uzbekistan” under TSUE
mushtariymamatqulova@gmail.com
ORCID: 0009-0000-8092-0365

Abstract. *This study provides a comprehensive analysis of informal employment and its multifaceted negative impacts on economic, social, and legal systems. Through systematic examination of global trends and specific focus on Uzbekistan's context, this research identifies the critical challenges posed by informal labor relations and proposes strategic solutions for policy implementation. The study employs quantitative analysis of ILO data and national statistics to demonstrate that informal employment affects over 50% of Uzbekistan's workforce, creating significant fiscal losses and social inequalities.*

Key words: *informal employment, shadow economy, labor market, social protection, economic development, Uzbekistan*

Абстрактный. *В данном исследовании представлен всесторонний анализ неформальной занятости и ее многогранного негативного воздействия на экономическую, социальную и правовую системы. Благодаря систематическому изучению глобальных тенденций и уделению особого внимания условиям Узбекистана, в данном исследовании выявлены серьезные проблемы, связанные с неформальными трудовыми отношениями, и предложены стратегические решения для реализации политики. В исследовании используется количественный анализ данных МОТ и национальной статистики, чтобы продемонстрировать, что неформальная занятость затрагивает более 50% рабочей силы Узбекистана, создавая значительные финансовые потери и социальное неравенство.*

Ключевые слова: неформальная занятость, теневая экономика, рынок труда, социальная защита, экономическое развитие, Узбекистан

Introduction.

Worldwide — and especially in many developing countries — informal employment has come to form a large and persistent part of everyday economic life. The International Labor Organization (ILO) defines informal employment as work arrangements that lack formal contracts, social security coverage, or legal protection (ILO, 2018). That definition captures more than an absence of paperwork: it describes a whole set of relationships and institutional gaps that shape people's livelihoods, their vulnerability to shocks, and the way states collect revenue and deliver services.

Informal work takes many shapes. It includes subsistence farming and unpaid family labor on small plots; street vending and small-scale retail without registration; casual construction and day-labor with no written contracts; domestic work paid in cash; and, increasingly, gig-economy tasks mediated through apps but outside formal protections. In many countries, entire microenterprises operate without registration, bookkeeping or access to formal finance — effectively blurring the line between self-employment and concealed wage work.

Drivers of informality are structural and practical. On the supply side are limited formal job opportunities, low wages in the formal sector, insufficient skills, and urgent household needs that make flexible, short-term work attractive. On the demand side are regulatory complexity, high registration or compliance costs, weak enforcement, and tax burdens that make formality unattractive for small operators. Together these factors produce a segmented labor market where movement from informal to formal work is difficult and risky.

For many households, informal work is a rational survival strategy: it provides immediate income, flexible hours, and low entry barriers. Especially in regions with

scarce formal employment, informality enables people to feed their families and bridge economic shocks. But that short-term gain comes at a long-term price: lack of social protection, unstable incomes, no pension accumulation, and limited access to credit or training — conditions that constrain lifetime earnings and socio-economic mobility.

Addressing informal employment is not achieved by enforcement alone. Because informality reflects both institutional barriers and household choices, effective strategies combine: simplifying registration and compliance, designing affordable and flexible social protections, expanding access to finance and training, and building trust in public institutions. Only such an integrated policy mix can convert the short-term lifeline that informal work provides into sustainable, protected pathways into formal employment.

Literature Review.

The dual labor market theory, first introduced by Doeringer and Piore (1971), provides an important starting point for understanding the nature of informal employment. According to this framework, labor markets are segmented into two distinct spheres: the primary sector, which offers stable jobs, higher wages, and social benefits, and the secondary sector, characterized by instability, lower wages, and lack of protections. The theory also emphasizes that workers often find it difficult to move from the informal (secondary) sector into the formal (primary) sector due to structural barriers, rather than individual choice.

Building on this idea, Schneider and Enste (2013) expanded the discussion by focusing on the relationship between informality and the underground economy. Their research highlights how widespread informality weakens fiscal systems by reducing tax revenues and undermines governance structures by eroding compliance with state regulations. This perspective shifts the focus from labor market segmentation alone to broader institutional consequences of informality.

Keith Hart (1973) was the first scholar to use the term “informal sector” in his pioneering study of Ghana’s urban economy. He observed that many people engaged in informal activities not because they preferred such work, but because formal employment opportunities were scarce or inaccessible. This interpretation underlined the necessity-driven character of informal work in many developing economies. Later, Hernando de Soto (1989) added another dimension by arguing that excessive bureaucracy, rigid regulations, and costly licensing systems pushed entrepreneurs into informality. In his view, informality often represents a rational response to restrictive institutional environments rather than a cultural or personal preference.

More recent scholarship has challenged overly optimistic views of informal entrepreneurship. La Porta and Shleifer (2014), for example, demonstrate that informal firms are typically smaller, less productive, and have limited potential for growth. They also tend to provide poorer working conditions compared to their formal counterparts. Similarly, Perry et al. (2007) found that workers in informal arrangements face significant disadvantages, including weak job security, irregular income flows, and very limited opportunities for career advancement. This body of research suggests that informality is not merely a safety net or entrepreneurial stepping-stone, but a trap that reinforces poverty and vulnerability.

The fiscal implications of informality are also well documented. Williams and Schneider (2016) provide a comprehensive analysis showing that shadow economies reduce government revenues by an estimated 15–20% in developing countries. This loss of revenue not only undermines fiscal stability but also weakens the ability of states to provide essential public services. Earlier work by Torgler and Schneider (2009) supports these findings, showing a strong link between the prevalence of informal employment, declining tax morale, and reduced state capacity. These insights confirm that informality is not simply a labor market phenomenon but a

systemic issue that affects the economic, social, and political foundations of development.

Research Methodology.

In this study, we decided not to rely on just one type of data, but to combine numbers with real human experiences. That is why a mixed-methods approach was chosen, bringing together statistics and personal stories to build a fuller picture of informal employment in Uzbekistan. On the one hand, we turned to large existing datasets – from the International Labour Organization, the World Bank’s surveys of Uzbek firms, national labor statistics, and UNDP reports – to see the broad patterns. On the other hand, we carried out our own survey across all 14 regions of Uzbekistan, interviewing 2,400 people, of whom the majority were informal workers, but also included formal employees and entrepreneurs. Thanks to face-to-face interviews and the use of digital tools, the response rate was very high, which gave us reliable insights.

Numbers alone, however, cannot tell the whole story. For this reason, we also spoke directly to people. We conducted 45 in-depth interviews with government officials, business leaders, and representatives of trade unions and NGOs. In addition, eight focus group discussions were organized with workers from different backgrounds – farmers, builders, street vendors, and domestic workers. These conversations helped us see the everyday realities behind the statistics: why people choose informal work, what challenges they face, and how they think about formalization. When it came to analysis, we started with simple descriptive statistics to show where informal employment is most common and who is affected by it. We then moved on to look at the relationships between informality and broader factors like economic growth, education, or regional development. More advanced regression models allowed us to identify what really drives people into the informal sector. We also compared Uzbekistan’s situation with neighboring Central Asian

countries, countries at similar income levels, and places that are often mentioned as examples of best practice.

To make sure the findings are trustworthy, we used several checks for reliability and validity. The survey was carefully tested, the data was cross-checked against official statistics, and independent experts reviewed the instruments. Throughout the process, we followed strict ethical standards: participants gave their informed consent, all responses were kept anonymous, and data was stored securely. Of course, no study is without its limits. People often have different ideas of what counts as informal work, and some are reluctant to report their real income. It was also difficult to reach highly mobile workers, and seasonal changes in jobs could not be fully captured. Finally, because the research was based on a snapshot in time, it cannot prove cause-and-effect relationships, and the fast pace of policy reforms in Uzbekistan means some findings may change over time.

Analysis and discussion of results.

The findings of this study show that informal employment in Uzbekistan, as in many other developing countries, has wide-ranging effects on the economy, society, and institutions. From an economic perspective, informality directly reduces state revenues. Since many workers and firms operate outside official registration, the government loses a large share of potential taxes that could support schools, healthcare, and infrastructure. Estimates suggest that in Uzbekistan this loss is equivalent to about 8–12% of GDP. At the same time, informal businesses compete with formal ones on unequal terms. By avoiding taxes and regulatory requirements, they gain an unfair advantage, which puts pressure on honest entrepreneurs and sometimes forces them into informality as well. This cycle not only damages fair competition but also weakens the foundations of a healthy market economy. In addition, informal enterprises usually have lower productivity because they lack access to finance, technology, and training. Studies show that their efficiency can be up to half that of formal firms, which slows down overall economic growth.

The social consequences are equally significant. Informal workers often do not have pensions, health insurance, or legal protection. As a result, they remain vulnerable to poverty if they lose their job or fall ill. ILO statistics confirm that around 60% of informal workers worldwide lack any form of social protection. In Uzbekistan, women are particularly overrepresented in informal work, such as home-based activities and small-scale trading, which limits their economic empowerment. Young people and migrants are also at higher risk, often accepting low-paid and insecure jobs because they lack alternatives. Informality also limits opportunities for skill development, as most informal jobs do not provide training or career advancement. This in turn reduces human capital and keeps workers trapped in low-income activities.

On the legal and institutional side, informality erodes the rule of law. When a large part of the economy operates outside regulations, trust in institutions weakens and respect for the law declines. This environment often fosters corruption and reduces the effectiveness of governance. Moreover, because informal work arrangements are not protected by legal contracts, disputes cannot be properly resolved. Workers therefore have little bargaining power, and businesses are less likely to make long-term investments in their workforce.

Another important legal consequence of widespread informality in Uzbekistan is linked to the complexity of business registration procedures. When entrepreneurs face long, costly, and bureaucratic steps to establish a business, many of them choose to remain outside the formal legal framework. This weakens the rule of law, reduces

Stage	Current Process	Time Required	Proposed Process	Time Required	Cost Reduction
1	Name reservation	3-5 days	Digital name check	1 hour	90%
2	Charter preparation	5-7 days	Template-based online	2 hours	85%
3	Notarization	1-2 days	Digital signature	Instant	100%
4	Tax registration	7-10 days	Automatic integration	Same day	80%
5	Statistical registration	3-5 days	Automatic integration	Same day	100%
6	Social fund registration	5-7 days	Automatic integration	Same day	100%
7	Bank account opening	2-3 days	Simplified procedures	1 day	70%
Total	26-39 days	\$350-500	3-4 days	\$75-100	80%

trust in state institutions, and fuels the expansion of the shadow economy.

As shown in Table 1, the current registration process requires multiple stages and may take up to 26–39 days with costs ranging from \$350 to \$500. Such procedures create unnecessary legal and administrative burdens for small businesses and start-ups. In contrast, the proposed simplified process—through digitalization, automatic integration of databases, and streamlined procedures—would reduce registration to just 3–4 days and cut costs by nearly 80 percent.

This comparison illustrates how legal and bureaucratic barriers contribute directly to informality. Unless such processes are simplified, many economic actors will continue to avoid formal registration, which undermines contract enforcement, transparency, and the overall credibility of legal institutions. Therefore, regulatory

reform and simplification should be seen not only as an economic necessity but also as a legal measure to strengthen the rule of law and reduce informality.

Taken together, these results highlight that informal employment is not just a labor market issue. It undermines fiscal stability, deepens social inequality, and weakens state institutions. Addressing it requires integrated policies that improve tax systems, expand social protection, and strengthen governance, while also creating fair opportunities for workers and businesses to operate within the formal economy.

Conclusion and Recommendations

The analysis shows that informal employment in Uzbekistan, while providing short-term income opportunities, creates deep economic, social, and legal challenges. Economically, it leads to substantial fiscal losses, market distortions, and low productivity. Socially, it deprives workers of protection, reinforces inequality, and limits skill development. Legally and institutionally, widespread informality weakens the rule of law, reduces trust in governance, and undermines the effectiveness of state institutions.

At the same time, the research confirms that informality is not only the result of individual choices but is strongly shaped by structural and regulatory conditions. Complicated business registration, excessive bureaucracy, and weak enforcement of legal frameworks continue to push many workers and enterprises outside the formal system. Unless these issues are addressed, informal employment will remain a barrier to sustainable development in Uzbekistan.

Based on the findings, the following recommendations are proposed:

- Regulatory reform and simplification – Streamline business registration procedures through digitalization and automatic integration, reducing time and cost burdens that currently encourage informality.

- Strengthening social protection – Expand access to pensions, healthcare, and labor rights for informal workers, with special focus on vulnerable groups such as women, youth, and migrants.
- Fiscal incentives for formalization – Introduce tax benefits, simplified reporting, and temporary exemptions for small businesses that transition from informal to formal status.
- Capacity-building and training – Develop programs for skills development and professional training to improve productivity and competitiveness of workers.
- Institutional strengthening – Enhance transparency, fight corruption, and improve governance quality to build trust between the state and economic actors.
- Awareness and education – Conduct information campaigns to raise awareness among workers and entrepreneurs about the benefits of formal employment and available state support mechanisms.

By implementing these measures, Uzbekistan can gradually reduce the scale of informality, strengthen its fiscal base, and promote inclusive economic growth. Most importantly, formalization will improve the quality of life for millions of workers and ensure a fairer and more sustainable labor market.

References

1. Adams, A. V., De Silva, S. J., & Razmara, S. (2013). Improving skills development in the informal sector: Strategies for Sub-Saharan Africa. World Bank Publications.
2. Benjamin, N., & Mbaye, A. A. (2012). The informal sector in francophone Africa: Firm size, productivity, and institutions. World Bank Publications.
3. Chen, M. A. (2012). The informal economy: Definitions, theories and policies. WIEGO Working Paper, 1, 1-26.
4. De Soto, H. (1989). The other path: The invisible revolution in the Third World. Harper & Row.

5. Djankov, S., La Porta, R., Lopez-de-Silanes, F., & Shleifer, A. (2003). Courts. *The Quarterly Journal of Economics*, 118(2), 453-517.
6. Doeringer, P. B., & Piore, M. J. (1971). *Internal labor markets and manpower analysis*. Heath Lexington Books.
7. Elgin, C., Kose, M. A., Ohnsorge, F., & Yu, S. (2021). Understanding informality. CEPR Discussion Paper No. DP16497.
8. Farrell, D. (2004). The hidden dangers of the informal economy. *McKinsey Quarterly*, 3, 26-37.
9. Hart, K. (1973). Informal income opportunities and urban employment in Ghana. *The Journal of Modern African Studies*, 11(1), 61-89.
10. International Labour Organization. (2018). *Women and men in the informal economy: A statistical picture* (3rd ed.). ILO Publications.
11. International Labour Organization. (2020). *Global employment trends for youth 2020: Technology and the future of jobs*. ILO Publications.
12. International Labour Organization. (2023). *World employment and social outlook: Trends 2023*. ILO Publications.