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## Informal Employment in SCO Countries: Realities and Prospects

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**Abstract:**

*Based on the inter-country analysis, the article proves that informal employment in countries that are members of SCO is the adaptation of the population to social and economic, and institutional conditions formed in the region. Russia has the greatest losses from a wide spread of informal labor practices as a result of considerable losses of centralized funds, monetary funds, decrease in the professional qualification of employees, and understatement of salary rates.*

*The latter is the consequence of the mass inflow of labor migrants from Central Asia to the sectors with a wide involvement of employees under informal employment conditions. The authors have determined that for the excess labor resources of the Central Asian region, Russia and SCO as a whole were tools of regulating the labor market and internal political situation. In China the wide spread of informal labor relations is stipulated by the increase in the availability of already cheap multi-million labor resources that for several decades have been making up the main factor of the economic growth of the country.*

*According to the forecasts of the article authors, in the medium term the PRC's government is not going to solve the problem on informal employment in spite of the arising problems related to ageing of the population and the lack of the citizens' pension provision system.*

**Keywords:** *informal employment, Shanghai Cooperation Organization (SCO), labor migration*

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## **Introduction**

“The Shanghai process” has started since 1960s due to the essentially changing international relations, the need to solve the issue about the Soviet and Chinese boundary and the allocation of spheres of influence in the Central Asian region. Many years’ cooperation in this area resulted in the foundation in 2001 of the regional international organization with six permanent members – Russia, China, Kazakhstan, Kirgizia, Tadjhikistan and Uzbekistan. This agreement was called the Shanghai Cooperation Organization (SCO). Now its importance and sphere of influence in the Asian region is expanding. It resulted in India and Pakistan entering the organization in the middle of 2015.

In spite of the fact that this grouping is considered mainly as a political union, nevertheless, each of its members pursues its own trading and economic interests from cooperating within the SCO. Russia and China try not to allow the USA to enter the region under consideration in order to preserve the Central Asia within their influence, both political and economic. In their turn, Central Asian republics that considerably lag behind their partners are interested in obtaining trading and economic privileges, financial and technological assistance. However, all together the SCO countries make up an economically colossal grouping that has a lot of promising investment and innovational areas of developing (Maytdinova, 2013).

## **Method and Methodology**

Works of foreign and national researchers on issues related to the international economic integration, specialists on integration of Russia, Central Asian countries and China, and documents and decisions taken in the SCO made up the theoretical and methodological basis of the research. The methodological basis of the research is the dialectic method, comparative and functional, and system approaches to considering integration processes in the SCO, country analysis of the trading and economic cooperation of the organization countries. When writing the work, the information was collected and processed statistically and economically. The tasks set in the work were solved based on applying general research methods within the structural and functional, and comparative analysis, as well as analysis and synthesis, analogous and comparison, and method of economic and statistical groupings.

## **Results**

Russia and China are the countries that have considerable reserves of almost all known mineral resources. Large reserves of fuel and energy raw materials are concentrated in Kazakhstan and Uzbekistan. A lot of labor resources are found in all SCO countries excluding Russia. China has a developed chain of supplies in many areas of the processing industry. Russia is characterized by a strategically advantageous geopolitical location. Subject to all above advantages in this region,

there are a number of factors that restrain the development within the SCO. One of them is an informal sector of economy that is considerable by its volumes and continues growing (Loayza, 2011; Medvedeva, Komarova and Kozenko, 2015).

The inter-country analysis of the share of informal sector of economy from the GDP shows that it has been developed most of all in China, then in Tadzhikistan. In Kazakhstan, Kirgizia and Uzbekistan informal economy is almost on the same level, within 42%. In Russia the situation is better as compared to other SCO members. However, the 30% value of this indicator is extremely high according to the global community (Zhusupova, 2013). In its turn a wide spread of informal economy causes the countrywide use of informal labor practices and contributes to informal employment in the region (Davydenko, 2005).

The lowest number of informally employed citizens is in Kazakhstan (32.8%), and (in the ascending order of this indicator) in Uzbekistan (40%), Russia (42%), and Tadzhikistan (47.5%). In China (67%) and Kirgizia (76%) the share of informally employed people considerably surpasses half of all economically active population of the country (Sayakvaev and Mokrousova, 2014; Hushkadamova, 2013; Faizova, Kozhevnikova, Kashipova, Zinurova and Egorova, 2015).

At first sight such tendency says about the system of employment in the region. It causes

- 1) High taxation loading for the registered labor power and firms because of tight taxation base;
- 2) Increasing risk of destabilizing the law order and state management;
- 3) Growth of financial losses of the state;
- 4) Irrational use of resources, preserving out-of-date technologies which causes low labor efficiency and functioning of mainly uncompetitive, inefficient productions;
- 5) Even if the informal sector contains productive firms, they do not have prospects because they face the limited access to the capital which causes the lack of opportunity to expand and develop (Bobkov, 2014; Günther, 1990; 1993).

Summarizing the above, it is possible to resume that developing countries have to pay about 1-2 percent points of the annual GDP growth for the informal sector as stated in the work by Tsepliaeva and Sonina (2013).

## **Discussion**

However, the research of reasons and peculiarities of informal employment in countries that are SCO members makes these conclusions far from ambiguous. To stipulate this provision, it is necessary to separately analyze informal labor relations in every SCO member country.

### ***I. Russia and Informal Employment***

For our country informal employment has a double meaning. On the one hand, it is a survival strategy for millions of Russian citizens. For twenty years of moving from socialism to capitalism in Russia, tens of thousands of large industrial, agricultural, construction, transport, household, communal and other organizations have been liquidated. In 2011 the volume of industrial products made up 85% as to the level of 1990, including the production of machines and equipment – 47.9%, means of transport – 55.5%. The position is even worse in the clothing industry – 22.6%, leather and footwear industry – 28.5%. At the present time in Russia, with a half of its land area being located near forests, the wood processing and production is only 43.3% as to 1990.

Over the recent five years, the agriculture that mainly became a family business has produced less than 85% of the 1985-1990 products (Rudnev, 2013). Statistical data say about the decrease in the working places in the formal sector of economy. Their deficit is compensated by informal labor relations. On the other hand, informal employment contributes to the decrease in the level of the population's life, and defines a low level of the already decreased salary rates (Anikin and Tihonova, 2014).

If we try to compare all sectors of the Russian economy using two criteria such as the tempos of the value added growth and the changing of the level of salary sectors can be classified into four groups.

The third group is of special interest. In spite of the advanced tempo of the sector growth, here the arrearage on the level of the labor payment is observed as compared to the average value in economy. Such situation is explained by vast involvement of employees in this sector under informal employment conditions. The possibility to employ workers with informal contracts allows to restrain the salary growth in quickly growing sectors, and simultaneously to provide them with competitive advantages for the further development.

Along with this, it is necessary to note that the external labor migration has a considerable impact on restraining the labor payment in Russia, including under the conditions of informal employment. Two reasons explain this fact.

Firstly, in Russia numerous generations born in the 1950s become economically inactive. It is replaced by the numerically insignificant generation of the 1990s. The decrease in the number of economically active population in our country surpasses the reduction of workplaces in the formal sector of economy. However, no deficit of labor resources in Russia is observed because this is the migration that is a factor smoothing the acuteness of the problem related to the lack of labor resources. Russia is a center attracting labor migrants, mainly from the CIS countries. However, some

of them (for example, Ukraine) faced the same precedent that has no analogues in the world history (Maleva 2016; Kovalenko, Yakimova, Avtaykina and Zaytseva, 2016).

Secondly, the majority of migrants agree to get a low labor payment in the Russian informal sector because in the immigration countries the level of salaries is many times lower, and employment chances are minimal. In addition to decreasing the citizens' welfare, informal employment causes great financial losses of the state. As a whole, if to consider the problem of informal labor relations in Russia, today's situation looks as follows. In the Russian Federation 33.7 mln persons are "deadheads". Only 48 mln persons out of 86 mln of employable population work in the legitimate sector, 4.3 mln persons are officially registered as unemployed, and the remaining part (39%) is invisible for the country's economy (Golodets, 2013).

According to the analytical research of Sberbank of Russia, the formalization of the informal labor relations existing in our country would enable the Pension Fund to annually earn additional deductions in the amount of USD 22.76 bln., and to increase the earnings of regional budget by USD 13.46 bln.

## ***II. Chinese Model of "Cheap Labor"***

For China informal employment is the price of the economic growth that has been 10% per annum on average over two decades. The Chinese "economic wonder" resulted not in achievements in the area of innovational technologies, increase in the area of education, growth of markets and enterprises efficiency, but in a great supply of cheap labor force. Besides, it is necessary to note that this competitive advantage has not run its course. It is only in 2015 when the number of Chinese employable population will achieve its peak amounting 923.5 mln of persons (Will cheap labor force disappear, 2010). This tendency will keep on till 2050.

In China, like in Russia, the number of workers informally employed through the formal sector of economy is high, i.e. it goes mainly about the undeclared rather than unregistered employment (Note 1). About 2/3 of the aggregate employment is consisting as informal employment which makes the Chinese labor resources more accessible.

Comparing the expenses of the employer when hiring a worker under the conditions of formal and informal employment, it is obvious that the main difference is related to the expenses for the labor payment. One more peculiarity is the essentially specific attitude to residents and migrants involved in the informal sector of economy. Subject to a longer working week, the labor payment of the latter is 11% lower. While in China working migrants are in the knowingly losing position, and do not have a considerable impact on changes of the local workers' welfare, in Russia, as stated above, the situation is entirely different.

It is necessary to note that under the modern organization of the Chinese pension system, this country does not suffer much losses from the lack of pension deductions as a result of the wide spread of informal labor practices. In the CPR the pension is paid to a small number of citizens from the total number of employed population. These are mainly public employees who work in the formal sector of economy with the total labor experience of not less than 15 years (Jinjun Xue, 2014; Günther and Launov, 2012). As a whole, the Chinese system of pension provision is being reformed. That is why according to the traditions existing in the society; old people are supported by their children. However, the current demographic policy related to limiting the birth rate makes the implementation of these obligations by the youth difficult to fulfill. In the nearest future it will cause social tension in the society and make the problem related to informal employment especially urgent.

### ***III. Informal Labor Relations in Central Asian Countries***

Analyzing the peculiarities of informal employment of Central Asian republics that are members of the Shanghai Cooperation Organization, it is possible to single out two basic reasons of its wide spread:

- 1) The fall of the Soviet Union, whose economy was a highly integrated complex with tightly related mutual elements, caused a catastrophic fall of GDP of the former union republics and liquidation of the industrial production. The number of workplaces in the formal sector of economy decreased. It affected the economic activity of the population and employment level. The period of stagnation has continued for more than twenty years. However, no positive shifts on changing the current situation are predicted in the nearest future.
- 2) In the countries under consideration it is possible to observe the natural growth of the population due to the birth growth. That is why the main component of their labor resources is the population of employable age.

As a result, on the labor market of this region, a stable tendency of surpassing of the labor force supply over demand was formed. The position is worsened by the citizens' lack of opportunities to make investments in accumulating the human capital. It causes the situation when the only possibility to adapt to the existing social and economic realities is informal employment.

However, it is necessary to note that the greatest part of the population of these countries, excluding the Kazakh citizens, prefers external migration, mainly to Russia, to informal labor practices. As stated above, it is explained by higher salary rates in the Russian Federation as compared to countries of the Central Asian region. The level of salary of Russia and Central Asian countries has decreased by 2014. In our country this indicator was 3.2 times higher than that in Uzbekistan, 7.9 times higher than that in Tadzhikistan, 4 times surpassed the analogous indicator

in Kirgizia, and it was only 1.4 times higher than in Kazakhstan (The Average Salary..., 2014). The effect of this factor stipulated the “female face” of informal employment because men prefer to go for earnings to the regions with a higher labor payment (Komleva, 2012; Stroeva, Lyapina, Konobeeva and Konobeeva, 2015).

Analyzing the data of the Bank of Russia on unilateral money transfers from our country in 2013, it is possible to state that economies of Tadzhikistan, Kirgizia, and Uzbekistan are the most dependent on them. In spite of the fact that in absolute figures the majority of all transfers are made to Uzbekistan (this is only 7% of its GDP), money transfers of labor migrants from Russia to Tadzhikistan made up  $\frac{1}{5}$  of this country's GDP (20.5%), and in Kirgizia this indicator is almost 15% of its GDP.

In 2014 there was a tendency related to decreasing the volumes of private unilateral transfers from Russia to Central Asian countries. It is explained by the sudden devaluation of the RUB rate as to USD. As a result, the average salary in our country decreased by 51.6% (from USD 950 to USD 490) and provoked the simultaneous decrease in labor income of migrants from the Central Asian region (Raevskiy, 2016).

However, it is in 2015 when the situation starts essentially changing. A high share of mutual goods turnover between Russia and Central Asian countries, as well as a great volume of mutual settlements on export and import transactions made in RUB caused the devaluation of currencies in Central Asian counties on the background of the devaluation of our national currency. Firstly, it caused the outflow, and then the recovery of the previous share of foreign workers on the Russian market of labor force.

#### ***IV. Informal Employment in India***

Over the recent years the Indian economy has shown 8-9% growth which is compared to the Chinese growth tempos. In terms of establishing new workplaces, India outran other BRICS countries (Bhaumick, 2013). The country has the lowest level of unemployment among the BRICS countries. Thus, in 2014 the level of unemployment in India was 8.6%. However, the share of employed in the total number of the population was the lowest – only 50.5%. This difference says about a considerable number of hidden unemployed citizens. It is especially great in some rural areas of India where 70% of the country's population live. The excesses of labor resources in the rural area of India can surpass 150 mln of persons (Mokhanti, 2015).

Consequently, this fact confirms the wide spread of informal employment in the region under consideration. The employment in the informal sector of economy is about 93% from 470 million of employed citizens in India where the official employment is only 7% (Bhaumick, 2013).

The use of unstable forms of employment in large companies based on the Indian Territory has grown enormously. Outsourced workers are not directly hired by those companies where they work. Officially they are workers of contracting companies on supplying the labor force that are appointed by these companies. Such employees work together with permanent employees of the company performing the same work, but they are paid only one third (or less) from the permanent employee's salary. That is why the situation when permanent employees make up only 30% of the total number of the company's employees, and all other employees are "hired" from the third party has become habitual. This is the way the majority of Indian automobile companies are functioning today. The companies' management also uses services of contractors on supplying personnel when it goes about the security service or even engineering and technical personnel. The salary in the Indian informal sector of economy is not regulated, either, and remains on a very low level (Bhaumick, 2013).

## **Conclusion**

When forming the social life, this is not the fact of informal employment that is important. Neither is its scale. Firstly, the attitude of the authorities to the informal employment is extremely important for the further development of the country. During such periods it was traditional for Eastern power structures to support informal employment that removes a part of responsibility for the population's fate. This tendency that has various forms is observed today, too. At the same time in Russia informal employment is perceived by the authorities with irritation, and on the everyday level it is a breeding ground for small-scaled corruption which does not contribute to achieving the consensus in the society and growth of the trust to the power.

Secondly, it is very important how the state will decrease the informal employment as it pursues goals of the reforms and stabilizes the social and economic situation. The tools selected by the state can have a serious impact on the society development. In this aspect, it is expected that focusing on the growth of its internal market; China will avoid tough regulation and do its best to maintain a considerable segment of the aggregate demand in the long-term period. Positions of Central Asian countries are more vulnerable because their own economy cannot assimilate the excessive number of the manpower, and a considerable economic growth lacks a number of factors. For these countries the SCO is a serious tool to regulate the labor market, and even the internal political situation. In its turn, Russia has the unique possibility to choose the future policy related to informal employment. What is more, this policy will have not only social and economic but also external political importance.



## Notes

**Note 1.** The authors classify informal employment into two types: unregistered and undeclared. *Unregistered employment* is a type of informal employment when the employee and the employer enter labor relations under conditions of the oral agreement (without concluding a labor contract). *Undeclared employment* is a type of informal employment when the actual conditions of employment differ from the conditions specified by the employment contract.

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