Discussion of "Informal Labor Markets in Times of Pandemic: Evidence for Latin America and Policy Options" by Gustavo Leyva and Carlos Urrutia

11th BIS Consultative Council of the Americas Research Conference "The Economics of the Covid-19 Pandemic"

Discussant: Alan Finkelstein Shapiro

Background

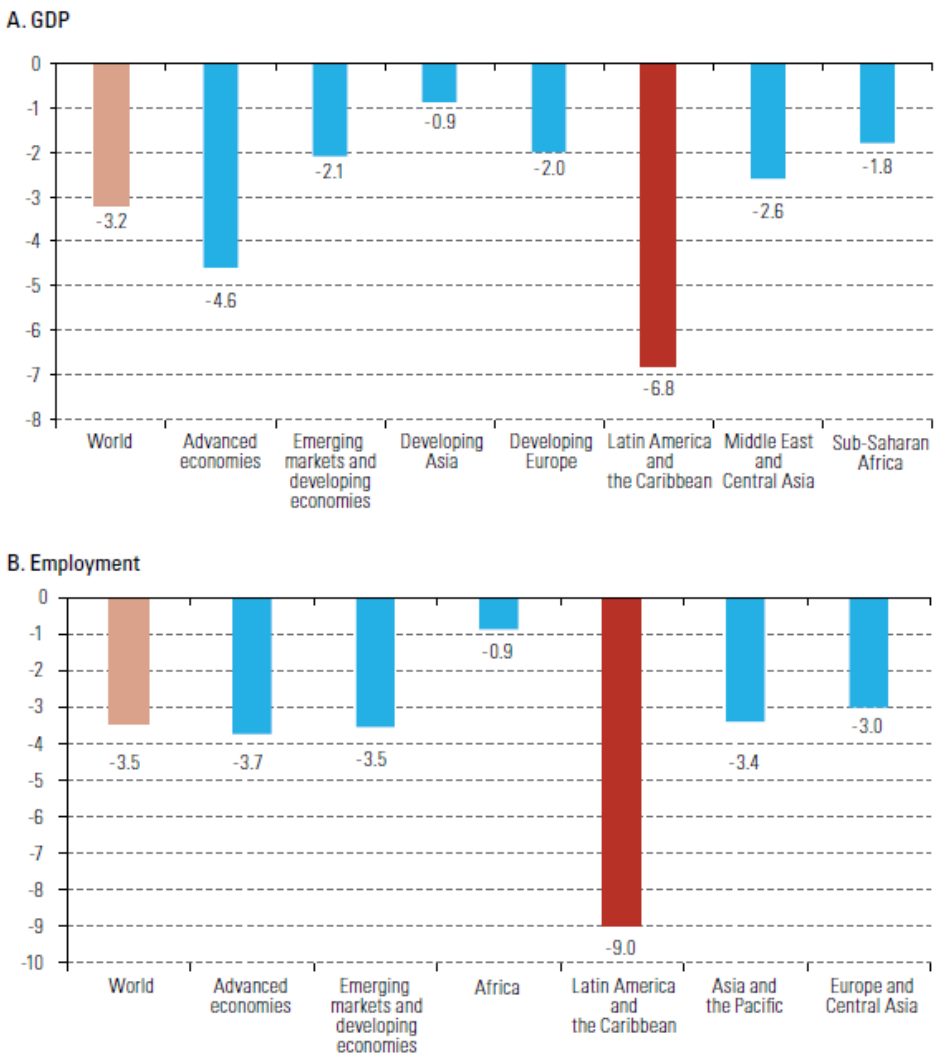


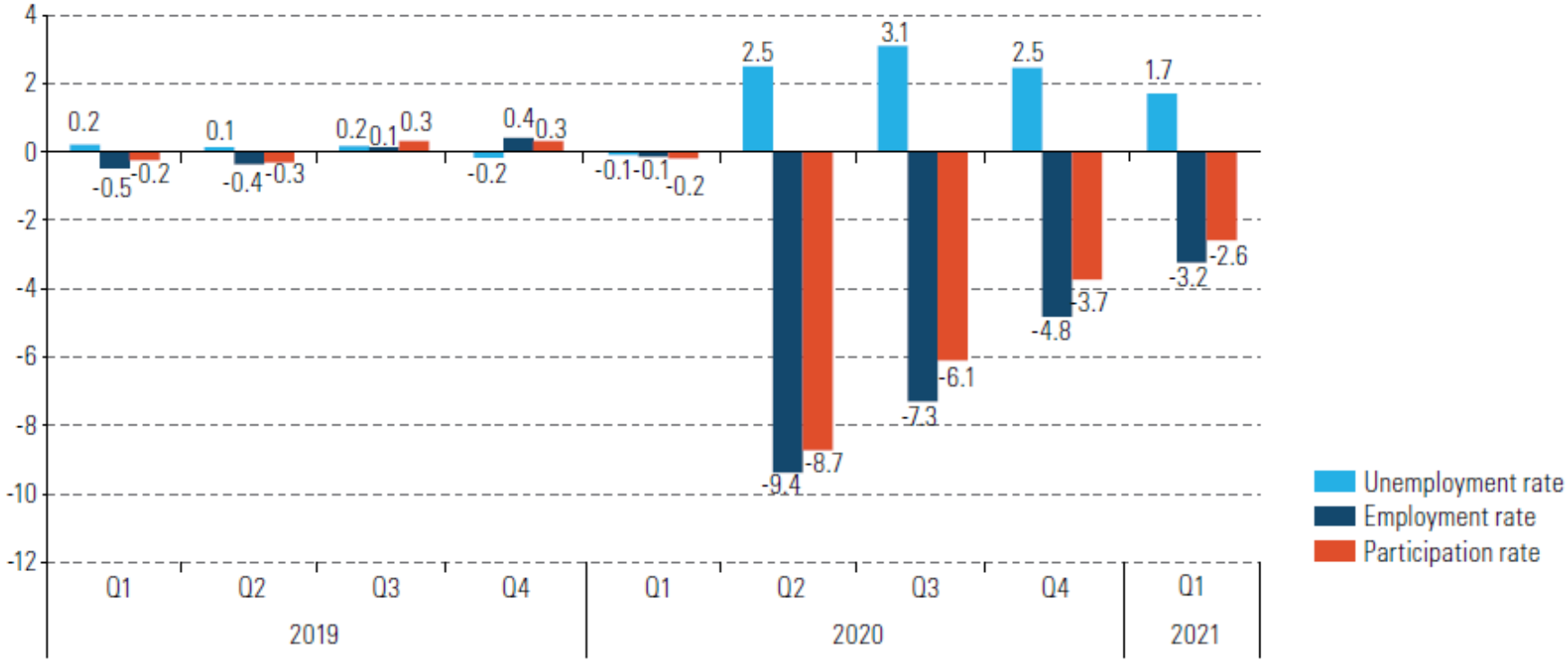
Figure II.1
World and selected regions: changes in GDP and numbers employed, 2020
(Percentages)

Source: International Monetary Fund (IMF), *World Economic Outlook Update*, July 2021 [online] https://www.imf.org/-/media/Files/Publications/WEO/2021/Update/July/English/text.ashx; International Labour Organization (ILO), *World Employment and Social Outlook: Trends 2021*, Geneva, 2021; and Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

Notes: Copied from ECLAC (2021).

Background

Figure I.32
Latin America and the Caribbean (14 countries):[a] year-on-year variation in the employment, participation and unemployment rates, 2019–first quarter of 2021
(Percentage points)

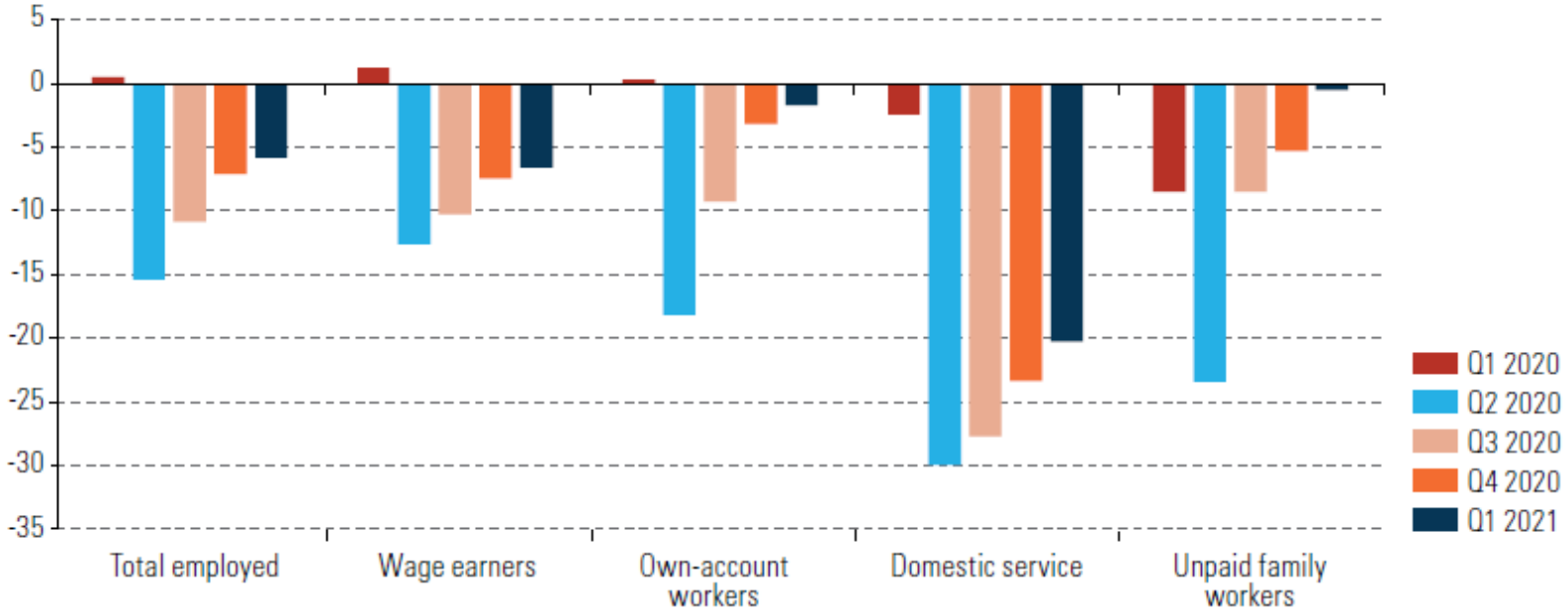


Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.
[a] Argentina, Brazil, Chile, Colombia, Costa Rica, Dominican Republic, Ecuador, Mexico, Nicaragua, Jamaica, Paraguay, Peru, the Plurinational State of Bolivia and Uruguay.

Notes: Copied from ECLAC (2021).

Background

Figure I.35
Latin America (11 countries):[a] year-on-year variation in employment by occupational category, 2020–first quarter of 2021
(Percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.
[a] Simple average of the following countries: Argentina, Brazil, Chile, Colombia, Costa Rica, Dominican Republic, Ecuador, Mexico, Paraguay, Peru and the Plurinational State of Bolivia.

Notes: Copied from ECLAC (2021).

What This Paper Does

- Analyze labor market dynamics in LA-5 (Brazil, Chile, Colombia, Mexico, Peru) amid COVID-19
  - Characterize responses of employment (total, formal, informal), inactivity, and unemployment
  - Characterize responses of empl. by industry, age, gender
  - Informal employment and inactivity: central to understanding labor market dynamics
  - Collapse of informality rate and inactivity: unique features of pandemic
- Using data for Brazil and Mexico, characterize labor market flows in past recessions and during COVID
  - Job creation, destruction by formality status + temporary layoffs, absent employees, telework
  - Bulk of drop in job creation, destruction comes from informal employment dynamics

What This Paper Does (Continued)

- Build a SOE model with unemployment, inactivity, formal jobs, and self-employment
  - Consider shocks that rationalize labor market response to pandemic
  - Shocks to informal sector productivity + labor supply $\Rightarrow$ essential for capturing labor market response

- Analyze three labor market policies: formal wage subsidies, formal vacancy-creation subsidies, informal-income transfers
  - Formal vacancy-creation subsidies are most effective
  - Informal income transfers: boost employment, but hurt recovery via lower productivity

Main Comments: Empirics

Labor Flows, Temporary Layoffs, and Absent Employees

- Limited data to characterize labor market flows in EMEs: Brazil and Mexico are two exceptions

- Paper highlights the dynamics of job creation and destruction during the pandemic and vs. past recessions in Brazil and Mexico
  - Behavior of overall job creation, destruction driven by informal job creation, destruction
  - Informality was central to labor market dynamics during COVID
  - Important contribution for understanding labor markets in LA, as well as what recovery may look like

- Facts on temporary layoffs and absent employees
  - These are, to my knowledge, completely new and very interesting facts!
  - Temporary layoffs in advanced economies received a lot of attention during COVID, but little work/evidence on this for EMEs
  - I would highlight these facts more!

Services/Retail, Female Employment, and Young Workers

- Section 3.2: pandemic had asymmetric effects on services + retail/wholesale trade, women, and young workers
- Leyva and Urrutia (JIE, 2020): informal sector leads recovery process after recessions in Mexico
- Useful to have brief discussion on what asymmetric impact during pandemic implies for likely recovery of LA economies
  - Relevant given recent work (on U.S.) on strength of recoveries and composition of demand (durables vs. non-durables, services) by Beraja and Wolf (2021)

Wage Empl. and Self-Employment During Recovery

- Unique feature of COVID recession vs. other recessions: reduction in informality

- ECLAC (2021): dynamics of wage employment and own-account work (or self-employment) at the onset of COVID and as economies have slowly reopened are different
  - Contraction in own-account work was larger but its recovery swifter (noted by the authors as well)

- May be informative to separate wage employment from self-employment in analysis in Section 2
  - Focus on self-employment as proxy of informal employment may be more transparent when documenting behavior of informal employment, and for understanding the effects of policy

Main Comments: Model and Quantitative Results

Frictionless SE and Model-Data Mapping

- Fig. 3 in paper: informal job creation and destruction behind bulk of response of overall job creation and destruction
  - This separates paper from other analyses of LA labor markets amid pandemic (IMF, 2020; ECLAC, 2021)
- Model assumes frictionless self-employment: no notion of informal "job" creation or destruction
  - Disconnect between important aspect of data and model!
  - Introducing entry/exit into self-employment does not have to be difficult, and can enrich model at minimal cost

Frictionless SE and Model-Data Mapping

- Simplest way of doing this: assume that evolution of SE is given by

$$L_t^s = (1 - \rho_{s,t}) L_{t-1}^s + \phi X_t \tag{1}$$

where $0 < \phi =$ efficiency of SE search effort (X_t), $\rho_{s,t} =$ separation probability SE (can be time-varying)

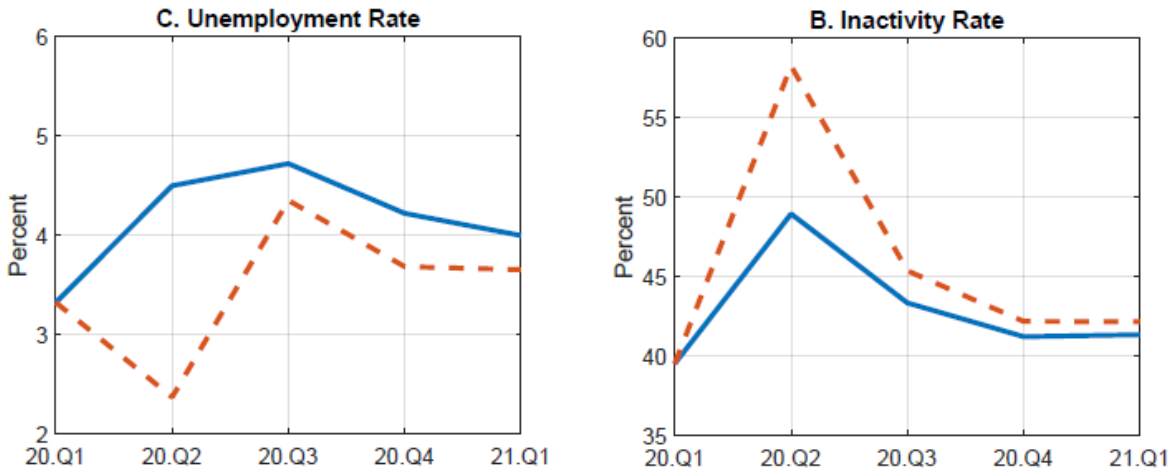
- Household chooses L_t^s and X_t subject to budget constraint and to (1)

- Several advantages:
  - Can calibrate process for $\rho_{s,t}$ to capture rise in informal (and overall) job destruction at onset of COVID
  - Can assess extent to which entry into SE (informal "job" creation) contributes to behavior of total employment along recovery path
  - Can analyze whether labor supply shock is partly capturing destruction of informal employment

Unemployment at Onset of Pandemic

- Following last comment, informality contributes to job creation/destruction patterns in data

- Having entry/exit of SE may help generate rise in unemployment (+smaller fall in inactivity) in the data



Notes: Copied from Fig. 7 in Leyva and Urrutia (2021). Blue line: Mexican data. Orange dashed line: model calibrated to Mexico.

- Sidenote: experiment comparing contributions of shocks in 2008-2009 versus 2020 is excellent!

Aggregate vs. Sectoral Capital Stock

- Does single-capital-stock assumption matter for quantitative results (especially for recovery)? (calibrated capital share = 0.23)
- Bulk of capital stock in LA economies is in formal firms (Busso et al., 2012)
- If assume sectoral capital stocks, capital shares may differ by sector, which can change quantitative effectiveness of policies
- Sectoral capital stock shapes value added by sector, which matters for effectiveness of labor market policies in EMEs
  - Policies supporting formal job creation can be very effective; policies supporting SE can bolster employment but slow down recovery (Epstein and Finkelstein Shapiro, JDE 2017)
  - Having sectoral capital stocks can allow you to make stronger quantitative case for subsidies to formal vacancy costs

Broader Model Validity: Brazil and Mexico

- Model performs well in capturing cyclical dynamics in Mexico, despite behavior of unemployment at onset of COVID
- Can model perform similarly well using Brazilian data? Would give broader validity to model
- In addition, can then use model to study how widely different policy responses in two countries may have shaped labor market dynamics during COVID
  - Mexico's fiscal response was widely different compared to Brazil's
  - Larger fall in informality in Mexico vs. Brazil could be explained by Brazil's transfers to low-income households: model can speak to this