Supply-Side Economics of a Good Type: Supporting and Expanding South Africa's Informal Economy

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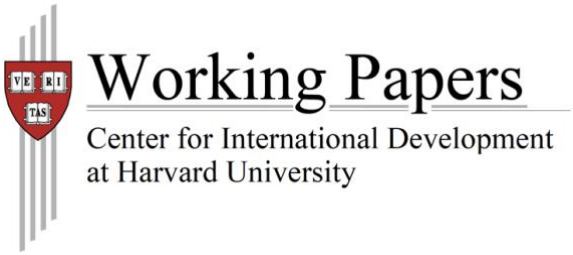
Working Paper No. 158

April 2024



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Acknowledgements: The authors wish to thank the CDE for funding this research and are grateful to David de Villers (DPRU-UCT) for his assistance with data work and additional research support. We also thank Ricardo Hausmann, Patricio Goldstein, Tim O'Brien, and the rest of the Growth Lab team at Harvard University for useful suggestions.

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1. Introduction

South Africa's inordinately high unemployment rates are now so well-known that they have almost become banal in the domestic policy discourse. Indeed, for an economy with one of the highest Gini coefficients in the world – let alone on all other inequality measures – the labour market looms large as one of the key drivers of this income inequality. Hence, the presence of some 30% of the labour force as zero earners in the national household income distribution yields to a Gini coefficient which has always exceeded 0.65 since the demise of apartheid (Leibbrandt et al, 2012; Leibbrandt et al, 2018).

Much of the descriptive and at least some of the early econometric work on the South African labour market, using standard Heckman selection-type econometric models, sought to describe the various individual determinants of unemployment in South Africa. The data persistently show that race, age, gender, location and education remain significant predictors of an individual's probability of not finding a job. Yet despite this rich literature, there remains a constant analytical exasperation at the disjuncture between the economy's relative normality on the one hand, in terms of its supply-side challenges (low investment levels, high energy prices, scarce skills, volatile exchange rates, and so on) – compared with its complete outlier unemployment rates on the other hand. One data point in this regard: Despite having very similar economic growth challenges to South Africa, Brazil's unemployment rate at 14.4% in 2021, remains close to 2.5 times less than that of South Africa's.

South Africa's persistently high unemployment could in part be explained by a level of informal sector activity that is abnormally low relative to its peers. As a share of the adult population South Africa's informality rate is 18% (Author's calculations using ILOSTAT, 2023 and World Bank, 2023a). Estimates suggest that the number of people participating in South Africa's informal economy number about 7.5 million, compared to 9.8 million in the formal economy. As we will see in the paper, South Africa has lower informality when compared with other comparator countries[1]. South Africa is shown to be an outlier and has an undersized informal sector; if South Africa had an informal sector that was similar in size to that in other developing countries, it would have an unemployment rate that would be much closer to those observed in other developing countries.

The informal economy has the potential to provide a point of first entry into the labour market for many unemployed South Africans and provide employment opportunities in the context of a formal economy that is not large enough and not growing fast enough to absorb the many South Africans in need of employment. This paper makes a case for an approach to the informal sector that is appreciative of the role it could play in providing employment opportunities in a constrained economy. Specifically, we provide an analytical synthesis of some of the reasons that could potentially explain South Africa's low informal sector activity in the face of such high levels of unemployment, and in turn, what policy options may be able to encourage informal sector activity in the country.

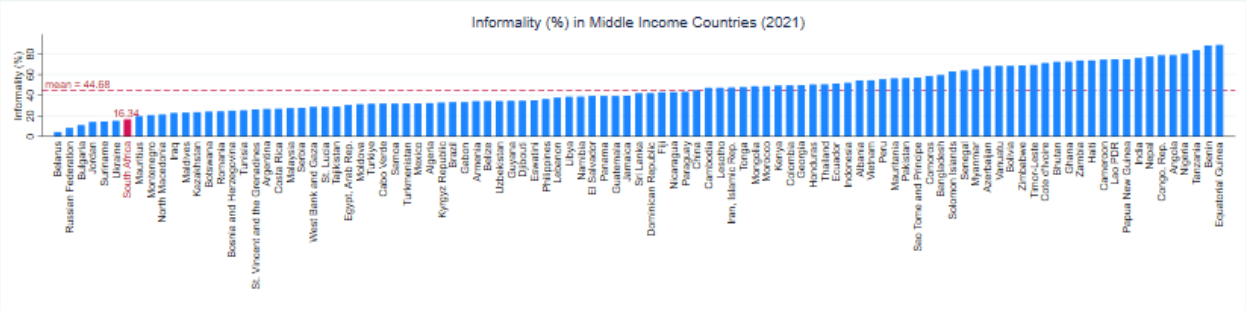
Section 2 of the report first presents an empirical profile of South Africa's informal sector, with an aim of understanding in empirical detail, why South Africa's informal sector employment remains relatively low in comparison to other developing countries. Section 3 presents an overview of exogenous constraints to informal activity in South Africa, accompanied by feedback from relevant national and local policy officials where appropriate. We received limited feedback from city officials – itself an indicator of how the informal sector is currently viewed within the country. We consider the limited feedback received within the context of existing data and findings in the literature concerning the informal sector of South Africa. Sections 2 and 3, Section 4 then provide a preliminary discussion on possible supply-side policy options for expanding the informal sector in South Africa and challenges that may be faced in this regard. Section 5 concludes.

[1] Peers with comparable levels of development such as Czechia (9%), Türkiye (13%), South Korea (15%), Argentina (17%), Brazil (22%), India (34%) and Mexico (34%).

2. The Informality Conundrum in South Africa: An Empirical Outline

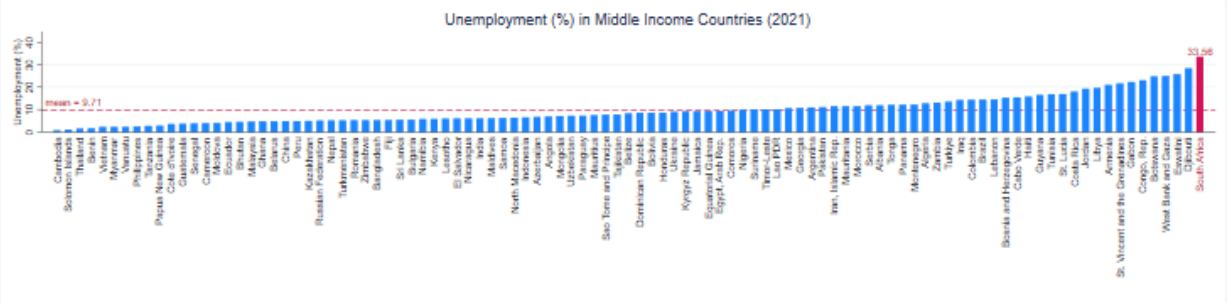
Figure 1 and Figure 2 below represent a sample of middle-income countries and plot the percentage share of workers in the informal sector as well as the unemployment rates of each country. The figures suggest that the mean global middle income country ratio of wage employed to informally employed to unemployed stands at 45:45:10 for every 100 individuals in the labour force. In contrast, for South Africa, this ratio is 50:16:34.

Figure 1: Percentage share of workers in the informal sector, middle-income country sample: 2021



Source: World Bank (2023a), own calculations.
Note: Informality measured as share of non-wage and non-salaried workers in country labour force.

Figure 2: Unemployment rates, middle-income country sample: 2021



Source: World Bank (2023a), own calculations.
Note: Unemployment based on official ILO definitions.

Put differently, these ratios suggest firstly that South Africa – relative to the mean middle-income country – in fact is an above-average generator of wage employment. In turn though, whilst most middle-income economies close their labour market through high levels of informal employment, at some 45 out of every 100 individuals in the labour force, South Africa is particularly poor in this respect. Hence, we find that only 16 out of every 100 individuals actively searching for a job in South Africa find their way into informal sector activities. Instead, this residual of workers unable to source wage employment in South Africa end up in unemployment. One is thus left with the intriguing and almost counter-intuitive conclusion that one of the key reasons for South Africa's high unemployment levels is in fact its very low levels of informality. That is, the South African economy does not close its labour market through high levels of low-barrier-to-entry informal employment – and thus results in the observed extraordinary levels of unemployment in the society.

This above empirical observation is the starting point for our inquiry into the informal sector in South Africa. Given the importance of this result, we provide a much more detailed analytical and empirical deep dive into this question through what follows below. Hence, in Section 2.1, we use employment-

output elasticities to show that the labour absorption of GDP growth does not seem to explain the reason why South Africa has such persistently high unemployment. This suggests that economies with much lower conversion rates from growth to employment have significantly lower unemployment rates than those of South Africa. We then illustrate the structural transformation of labour markets in the context of how the informal economy shrinks as countries grow richer in Section 2.2, and highlight how South Africa compares to other countries in this regard. In Section 2.3, the outlying nature of South Africa's labour market – with its high unemployment and low informality – is discussed.

2.1 Employment-Output Elasticities

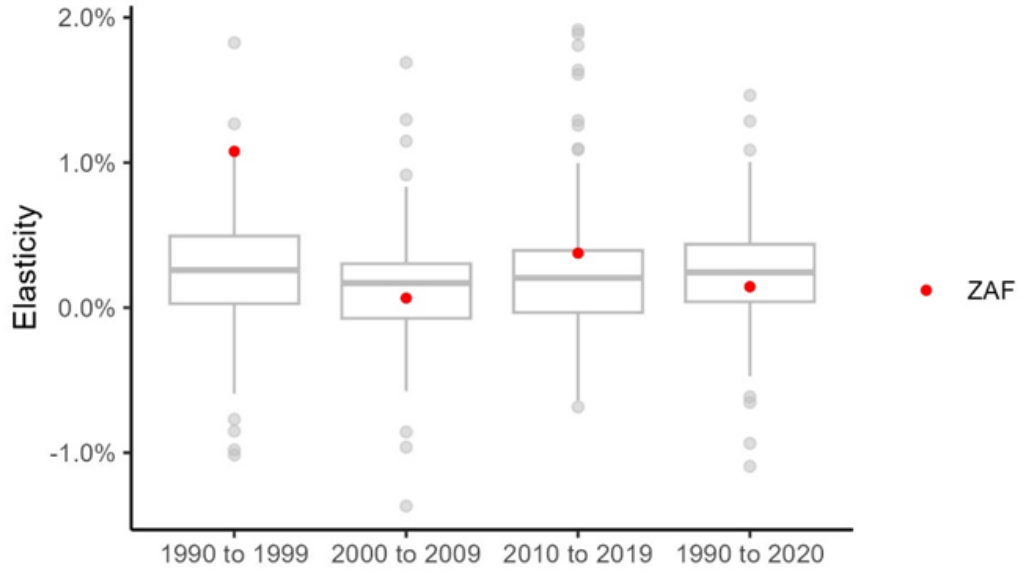
One might think that given South Africa's high unemployment rates, the employment elasticity of growth in South Africa is relatively low, and that this elasticity may explain the high levels of unemployment. Arguments about jobless growth and low growth notwithstanding, we can measure to what extent GDP growth has been helpful in increasing employment in South Africa relative to the experience of other countries. Following Kapsos (2006) we run the following regression to estimate the employment-output elasticities of South Africa and all other countries using the *point elasticity*. Specifically, we run:

$$\ln(E_{it}) = \beta_0 + \alpha D_i + \gamma_t + \beta_1 \ln(Y_{it}) + \beta_{2i} [\ln(Y_{it}) \times D_i] + \varepsilon_{it} \quad (1)$$

Where E_{it} is total employment for country *i* at time *t*, D_i is a country dummy, αD_i is a country fixed effect, γ_t is a year fixed effect, Y_{it} is total real GDP in local currency and ε_{it} is an error term clustered at the country level. β_0, β_1, β_{2i} are parameters to be estimated and the point elasticity for country *i* during the period of analysis is given by the sum $\beta_1 + \beta_{2i}$ (Kapsos, 2006). We run this regression for four time periods: 1990 to 1999, 2000 to 2009, 2010 to 2019, and then for all years available between 1990 to 2020 – which then also picks up some of the initial years of the COVID-19 pandemic. This allows us to calculate the output-employment elasticities for every country for each of these time periods. Figure 3 shows the distribution of estimates for output-employment elasticities for all countries with South Africa highlighted in red.

Aside from the period of 1990 to 1999, where the employment output elasticity was much higher than average, South Africa's employment-output elasticities are not large outliers. Between 1990 and 1999, South Africa saw an employment output elasticity of 1.07% well above the median value. The reason for such a high elasticity is two-fold. First, GDP growth during this period was relatively volatile, while there was a well-documented large increase in the labour supply due to a combination of demographics and the increase in women's (especially black women's) participation in the workforce following the end of apartheid (Banerjee et al., 2008). Previous estimates by Kaspos (2006) showed that there was heterogeneity during this period with a negative elasticity between 1990 to 1994 and 1999 to 2003, while the elasticity between 1995 and 1998 was 1.94%. During the 2000 to 2009 period, the employment-output elasticity was a more modest 0.06% (slightly below the median of the world) as in South Africa the beginning and end of this period were marked by economic struggle, even as the mid-2000s was a period of high growth, if low absorption of the labour force. The 2010 to 2019 period saw an elasticity of about 0.38% which was close to the 75th percentile of all countries. However, this period was one of positive but low and declining GDP growth caused by the shocks of collapses in network industries – especially electricity – (Hausmann et al., 2022), meaning that overall employment growth was low. Looking at the period between 1990 and 2020, overall output employment elasticities were about 0.14%, which was only slightly below the median value of all countries in the period.

Figure 3: Employment-Output Elasticity of South Africa and the Rest of the World



Source: World Bank (2023a), own calculations.

The results suggest that while current low growth may be a driver of some labour market challenges in South Africa, the labour absorption of GDP growth does not seem to explain the reason why South Africa has such high unemployment. South Africa's employment-output elasticities are not very low relative to other countries, and overall are only slightly below median with some periods much higher and other periods lower, meaning that South Africa's ability to increase employment as a result of GDP growth is more-or-less on par with other countries. This suggests that the absorptive capacity of South Africa's growth experience does not seem to explain South Africa's persistently high rates of unemployment. However, increasing growth from the current low-growth regime is important from a perspective of reviving growth in employment.

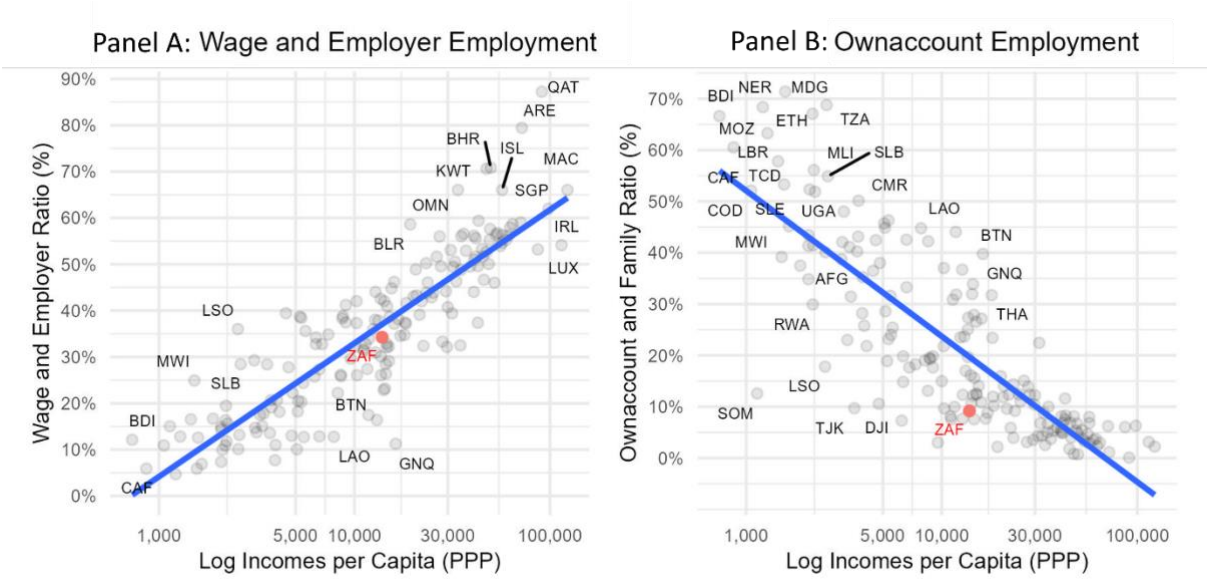
2.2 Informality, Unemployment and Income Levels

As countries develop, grow, and become richer, there is a clear pattern of transformation in their labour markets. Specifically, as documented by several researchers (for example, La Porta & Schleifer (2014) and Poschke (2019)) poorer countries will tend to have many people employed as own-account, self-employed workers. We can see this in Figure 4 where on the x-axis we have the natural log of real GDP per capita in 2017 PPP dollars, and the y-axis has the share of the working-age population that is engaged in wage employment (left-hand side) or who are own account workers (right-hand side). Own account workers are those who are self-employed and who do not hire other workers outside of their immediate family. Indeed, the poorest of countries can have more than 70% of their working age population employed as own account workers.

But as countries get richer, a smaller and smaller share of workers are own account workers. Instead, many more people are engaged in regular wage employment either as employees or as employers hiring workers. As the figure below shows, there is a strong relationship between the share of the working age population that is employed in wage employment in firms and a country's income level. Economic growth, the increase in wage employment, and the decline of own account employment, go

hand in hand. Thus, the process of structural transformation and growth also sees with it a transformation of the labour market: Where most people are islands unto themselves in own account work, to one where most people are working with others in more complex ways earning a wage.

Figure 4: Wage and Own Account Employment as % of Working Age Population and GDP Per Capita PPP

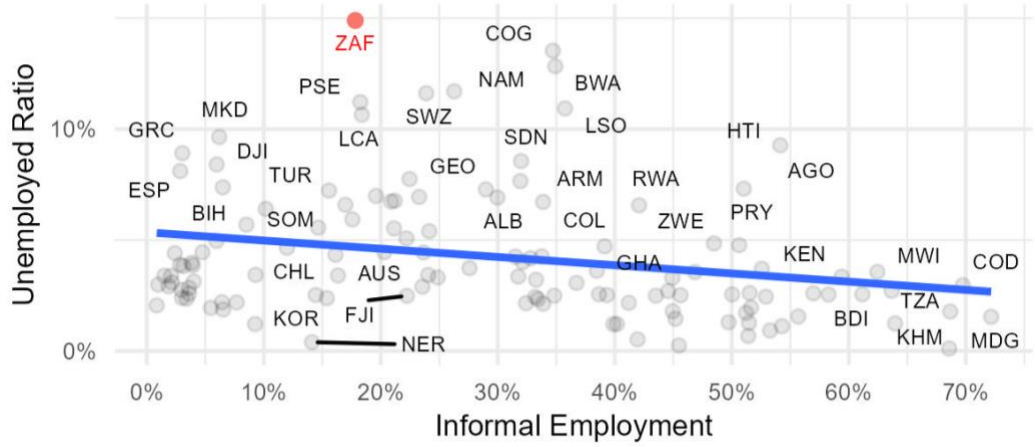


Source: World Bank (2023a), own calculations.

What is clear though in Figure 4, is a confirmation of the labour market ratios alluded to above. Hence, we find that in terms of Figure 4 (left-hand-side graphic- Panel A) South Africa's share of wage employment is consistent with its income per capita in PPP terms relative to other countries in the sample. However, Panel B makes it plain that given its income per capita levels, South Africa in fact has a share of own-account and family workers that is below the expected estimate – at about 10% relative to at least 20% in this cross-sectional sample of countries.

Figure 5 below arguably crystalises the highly unusual nature of South Africa's labour market. The figure plots the share of the unemployed against the informally employed in a country's labour force. It is clear that South Africa is an outlier: The economy for its given level of informality has very high levels of joblessness. In fact, South Africa is one of the few countries in this sample where the unemployed ratio is close to the informality ratio.

Figure 5: Informal Employment Ratio versus Unemployed Ratio



Source: World Bank (2023a), ILOSTAT (2023), own calculations.

Thus, what makes South Africa's labour market unique, is that it has a combination of high unemployment with low levels of informality – and crucially in an environment where wage employment is in fact slightly above the middle-income country average. As a result, in South Africa, those that are not in formal work are relatively more likely to be unemployed rather than in informal work.

This small size of the South African informal sector has been noted by several other researchers. There are a number of studies that have explored the small size of South Africa's informal sector (see Kingdon & Knight (2001), Fourie (2018) and Shah (2022)). Some studies have also looked at various explanations for this unique feature of the South African labour market from centralized bargaining (Magruder, 2012) to crime (Grabrucker & Grimm, 2018). An analysis by Shah (2022), found that many of the usual explanations for South Africa's high unemployment rates (like social grants or minimum wages) were not satisfactory explanations that could account for high unemployment and low informality.

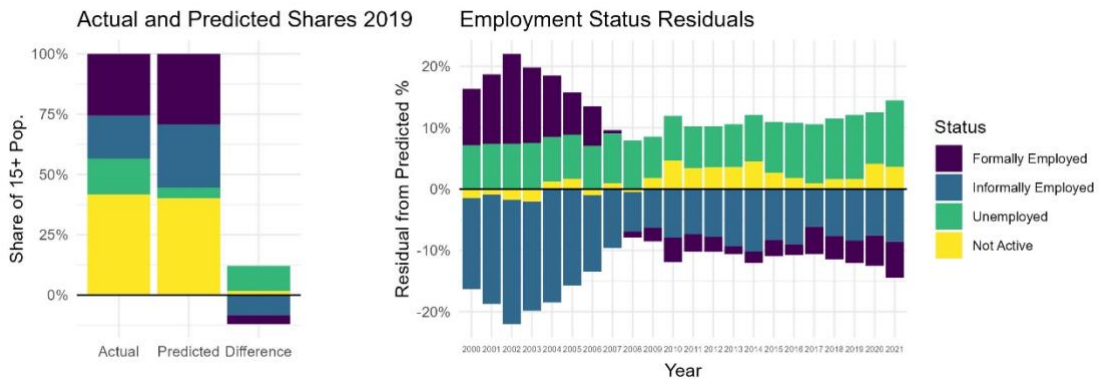
Despite the puzzle, explaining South Africa's uniqueness of high unemployment and low informality has received less attention in the public debate. This is unfortunate because qualitatively, if South Africa's informal sector were as large as its income per capita would predict, its unemployment rate would also be much lower. We test this question – namely what South Africa's predicted unemployment would be – through running the following regression:

$$E_{it} = \beta_0 + \alpha D_i + \gamma_t + \beta_1 \ln(y_{it}) + \varepsilon_{it} \quad (2)$$

where:E_{it} is the rate of formal, informal, unemployed, or inactive as a share of LF for country *i* at time *t*; αD_i is a country specific fixed effect; γ_t is the year fixed effect; y_{it} is GDP per capita in 2017 PPP dollars; ε_{it} is error term clustered at country level; β_0 and β_1 are parameters.

Running the regressions in equation (2) for each year separately, we can calculate both the predicted values of South Africa's formal, informal, unemployed, and inactive adult populations given South Africa's level of income. In addition, we can measure the residual value of how far off South Africa's actual values for these metrics are relative to the prediction. Figure 6 thus shows the results of this exercise, where the left-hand panel shows the actual, predicted, and residual for 2019, while the right-hand panel shows the residual and its decomposition by employment status for the years 2000 to 2021.

Figure 6: Actual, Predicted, and Residual Employment Status for South Africa



Source: World Bank (2023a), ILOSTAT (2023), own calculations.

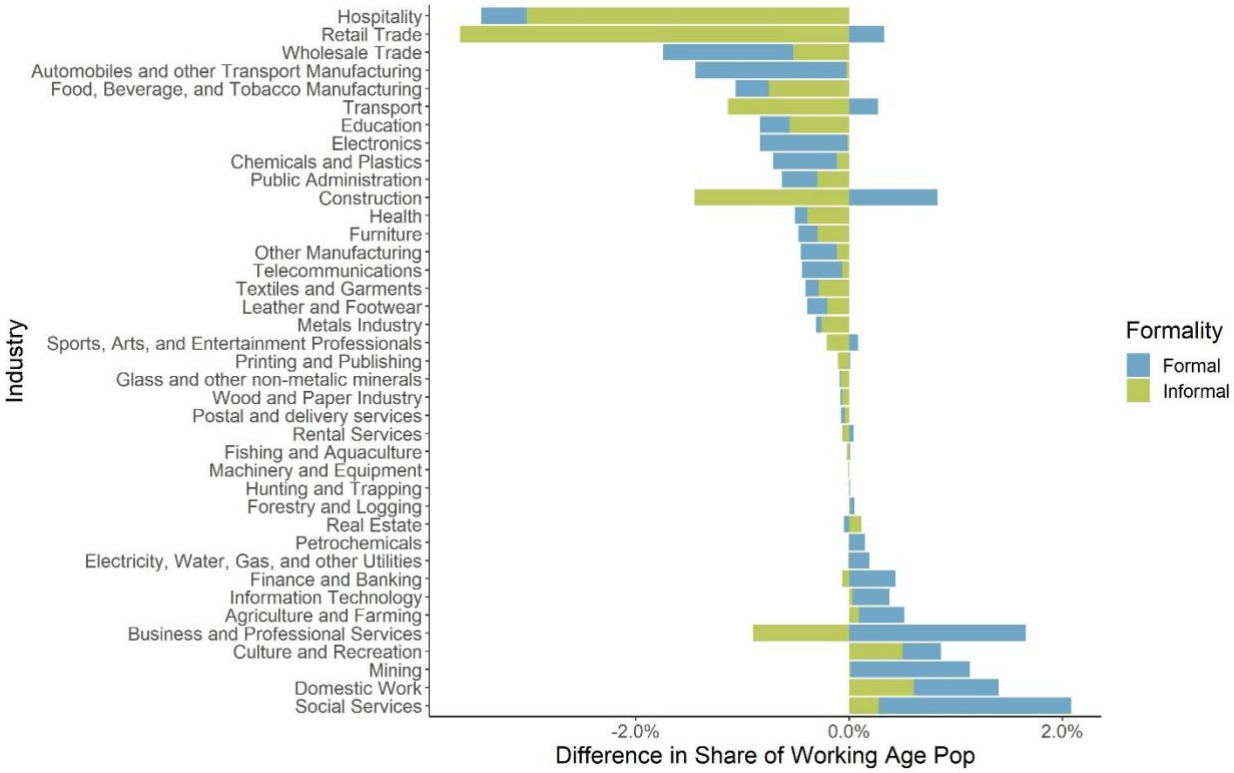
For 2019, we can see that almost the entire difference between South Africa and its predicted values arises from having more unemployment and less informality. Another way of interpreting this result is that if South Africa's labour market looked like that of the average country with its level of income, then its formal, wage employment rate and inactive rate would be little changed, while its rate of informality would be much higher, and its level of unemployment would be much lower. In fact, if South Africa had informality rates closer to that predicted by its level of income (i.e., moving from 18% of the adult population to 26% of the adult population), the implied unemployment rate for 2019 would change from the actual value of about 26% of the labour force (or 15% of the total adult population), to instead about 7% of the labour force (or only 4% of the total adult population). With a higher informal workforce, South Africa would look much more "normal" in terms of unemployment from a global perspective.

Looking at the above composite result over time, the persistence of South Africa's high unemployment rate seems to be explained by structurally higher unemployment and lower informality rates. The right-hand panel of Figure 6 thus shows that South Africa's anomalously high unemployment and low informality relative to other countries at similar levels of income has been a persistent feature of its labour market since at least 2000. In this graph, we do see some differences across time periods. In the pre-2008 period, some of South Africa's low informality was accompanied by higher-than-expected formal employment, and in the post 2008 period, South Africa's formal sector employment has been underperforming more and more, with a rise in higher-than-expected levels of inactivity and unemployment. This later trend likely reflects the low growth and macro challenges that South Africa has been facing over the last more than decade, brought on by the breakdowns in the electricity and other utilities sectors as well as the COVID-19 shock. But for most time periods the majority of the difference between South Africa's labour market and the labour market for the average country of its income level lies in its high unemployment and low informality.

When we compare South Africa's labour market to that of other middle-income countries, we can see that South Africa seems to be "missing" much employment in informal hospitality and retail. South Africa and Mexico in 2018 had similar levels of GDP per capita. Both are middle-income countries. When we compare the labour markets of these two countries, we see a pattern very similar to the graph in

the left-hand panel of Figure 6, where the two countries have similar levels of formal, wage employment and inactive populations. The big difference is that South Africa has high unemployment and low informality, while Mexico has relatively low unemployment and high levels of informality (i.e., Mexico looks much more like the typical country of its level of income). Figure 7: Difference in Employment Shares of Working Age Population Between Urban South Africa and Mexico (2018)Figure 7 digs deeper into the differences between these two countries using micro labour market data. It shows the differences in employment shares of the working age populations (i.e., age 15-64) of the two countries by broad industry category, and then decomposes those differences by informality.

Figure 7: Difference in Employment Shares of Working Age Population Between Urban South Africa and Mexico (2018)



Source: Reproduced from Shah (2022).

Positive values imply that the industry has a relatively higher share of the working age population in South Africa compared to Mexico. Negative values imply that the industry has a higher share in Mexico than in South Africa. If we were to include the unemployed and inactive as additional "industries" then the differences in shares would sum up to 0 by construction. Thus, the graph shows that South Africa has a higher share of its population employed in formal social services, domestic work, mining, culture and recreation, and business services. Mexico in line with its comparative advantage in manufacturing has relatively more formal employment in various manufacturing sectors but in particular, vehicles as well as food and beverages. However, the largest and most striking difference between the urban employment rates of the two countries is that Mexico has much more of its working age population in informal services like hospitality, retail trade, transport, and construction. Informal hospitality will include food hawkers and stalls, while informal retail trade will include street vendors, both of whom

are ubiquitous and visible across cities in Mexico. These are also the most common sectors for informal work in South Africa, but the overall informal sector is small in the country.

The comparison raises a number of questions about the high level of unemployment, and low levels of informal employment, in South Africa. More tangibly, why do we not see the large numbers of food hawkers and street vendors and other informal self-employed workers that are ubiquitous in other countries? Further, why do South African workers continue to report searching for work rather than engaging in one of these activities? Are there barriers that prevent South Africans from engaging in informal work, and if so, how might those barriers be alleviated? The following sections of this paper discuss some of those barriers (especially at the city level) and consider some policy experiments and interventions that may be appropriate for addressing those barriers.

3. Exogenous Constraints to Informal Sector Expansion

This section on exogenous constraints begins to consider what some of the higher-level environmental factors are that may be limiting economic activity in the informal sector in South Africa. In Section 3.1 we provide an overview of how regulations may play a role in constraining activity in the informal sector. We emphasise that a shift in thinking at the policy level is necessary for expanding the informal sector in South Africa. We then discuss spatial barriers to expanding the informal sector in South Africa in Section 3.2. In Section 3.3, crime and security are introduced as additional constraints to informal sector activity. Finally, Section 3.4 considers how challenges related to the provision of urban infrastructure create barriers to entry and growth in the informal sector. Much of this section is also informed and shaped by interviews of city and local government association officials. Hence, to gain a better understanding of the opinions of officials on informal trading, we compiled and sent a questionnaire to the City of Cape Town (CoCT) and asked that it be completed by officials working with the informal sector. We received feedback from a small number of (five) CoCT officials working within the Enterprise and Investment to Economic Analysis, Policy and Strategy departments. In addition, we conducted a verbal interview with an official working directly with the Informal Trading Permitting System, in order to better understand the workings of the system. See Appendix A for the questionnaire sent to officials. We also engaged a number of South African Local Government Organization (SALGA) officials and note some of their views on the regulation of informal sector activity in the report where appropriate.[2]

3.1 Regulations as a Constraint to Informality

Excessive regulations can interfere with market forces and distort the decision-making processes of economic agents. Across various departments and tiers of government there is a general lack of coordination for bodies that work with the informal sector (Masuku & Nzewi, 2021). Because of the hierarchical structure of legislation governing the informal sector, it leads to increasing regulatory red tape and in turn coordination failures (Christensen, Hegazy & van Zyl, 2016). Red tape in general has compliance costs for small businesses, and it slows the rate of establishment of new business activity. The SALGA officials we spoke to agreed that reducing regulatory red tape can improve access to trade. Regulatory red tape obstructs dynamic adaption, innovative power, and entrepreneurial activity, and

[2] SALGA is an autonomous association and partner of all local governments in South Africa. In SALGA's the role of supporting local government intelligence, they contribute common policy positions and provide solutions to various challenges experienced by local governments (SALGA, 2024).

in turn limits sales turnover growth and hampers market competition performance (De Jong & Van Witteloostuijn, 2014).

3.1.1 Legislative Constraints

While the rights of informal sector workers are protected by relevant provisions of the Constitution (Republic of South Africa, 1996a), in practice there are a number of laws and regulations which constrain the ability of individuals to participate in the informal economy. The Businesses Act 72 of 1991 regulated informal trade (Republic of South Africa, 1991) and initially removed restrictive laws concerning business licencing, premises and hours for both formal and informal businesses, meaning that traders were in fact allowed to trade freely with this piece of legislation. However the Businesses Act did also regulate and make provisions for (i) the issuing of trading permits and licences[3], (ii) the right to have written notice of why a licence was denied or repealed and the reasons for this, (iii) the opportunities to appeal the decisions associated with (ii), (iv) fines and criminal offences associated with non-compliance, (v) regulations, and (vi) the power of local authorities regarding informal traders (Republic of South Africa, 1991).

Given the new freedoms associated with the Businesses Act, municipalities were unable to cope with the amount of trading taking place in public spaces. This in turn led to the Businesses Amendment Act 186 of 1993 (Republic of South Africa, 1993). The Businesses Amendment Act enables municipalities to make by-laws around the supervision and control of informal traders. Moreover, these by-laws are evidently near mirror images of one another (Skinner, 2018).[4] In all the major metropoles, for example, the sanction of violation is criminal – either a fine or imprisonment, demonstrating a punitive approach to street-trader management (ibid., 2018). For instance, the City of Cape Town (2021a) provides details of common offences/non-compliance to by-laws, such as having more than two people working at your bay at one time, or cooking on open fires without permission from the city. Ultimately, the Businesses Amendment Act 186 of 1993 rolled back any gains to trading access underpinned by the original act. Put simply, cities and urban centres were now able to regulation away any freedoms to trade by the informal sector.

Several other pieces of national legislation relating to health and safety are also relevant in shaping informal sector activity. The National Building Regulations and Building Standards Act 103 of 1977 (Republic of South Africa, 1977b) sets about norms and standards related to fire safety, ventilation, and building structures. However, informal businesses may not have the means to adopt premises that conform to these norms and standards. Legislation also outlines where traders may carry out business, to ensure the safety of both the public and the traders. The National Road Traffic Act 93 of 1996 for example outlines where traders may trade on public roads (Republic of South Africa, 1996b). Informal trading is prohibited along public roads outside an urban area. By-laws can allow trading at intersections but restrict vendors from obstructing sidewalks and creating traffic hazards. Finally, the Health Act 63 of 1977 allows authorities to issue food traders with a 'Certificate of acceptability' (Republic of South Africa, 1977a), and the Meat Safety Act 40 of 2000 ensures meat safety standards are maintained (Republic of South Africa, 2000). Together, these ensure that food is safe for consumption. However, these standards can often be unaffordable to informal businesses. For example, the activities of slaughtering in outside areas and preparing meals on open fires, which is common in township neighbourhoods, is in fact prohibited by many municipal by-laws.

[3] Particularly those related to the selling of meals and perishable food.

[4] See City of Johannesburg (2022), City of Cape Town (2013), and Ekurhuleni Metropolitan Municipality (2012).

Municipalities acknowledge the challenges related to regulating informal trade and struggle to successfully put policies in place (Ekurhuleni Metropolitan Municipality, 2012: 5). Informal trade legislation appears to lean more towards urban management than small business development – with informal traders facing the highly unusual environment (as economic agents in a developing country context) of regulations that are more akin to those found in an industrialised economy. Indeed, it is precisely this regulatory 'iron wall' that may serve as one of the key initial contributors to discouraging the expansion and operation of the informal sector in South Africa.

3.1.2 Zonal Laws and Licencing

Such an overarching regulatory environment is in turn shaped and reinforced through the micro-management of the areas where informal traders are indeed even allowed to operate. Hence, for South African urban centres, zoning maps are developed at a local government level, and land-use zoning generally considers multiple factors including resource allocation, economic development, environmental protection, public health, and social and community development. However, these inevitably restrict business operations, as standard zoning approaches are often unsuitable in informal contexts (Charman & Peterson, 2018). Specifically, these zoning regulations create limited spaces where informal traders can carry out their business, and in so doing circumscribe both the position of trade as well as effectively the number of traders.

In their feedback, officials stated that informal economic activity in the City of Cape Town is largely limited to main streets and commercial areas. The City provides 5500 informal trading bays around the city; the locations of which are informed by trading plans. However, a large proportion of informal economic activity occurs in residential areas outside of the city, and officials estimate this activity to be approximately 8000 informal traders trading outside the demarcated spaces.

The city officials' awareness of the share of informal workers working outside of demarcated areas, and the fact that these individuals are mostly active in townships, is very important. First, these are typically home-based workers, often involved in informal trade and take-aways or providing services. These home-based entrepreneurs often have limited financial capital, frequently relying on low-cost building materials, such as corrugated iron or zinc sheets, old shipping containers, and simple stalls (Scheba & Turok, 2020). These building materials and structures do not comply with official building and zoning regulations. Second, this home-based portion of the informal sector in townships has been growing. Charman and Pietersen (2017) indicated that microenterprise activity in Delft had doubled between 2010 and 2015. In addition, spaza and house shops ranked in the top 5 informal businesses in Delft in 2015, and street traders increased from 2% of all informal enterprise in Delft to almost one-tenth (8.2%).

Ultimately then, restrictive zoning in urban centres has possibly displaced trading to outlying township communities where the potential market is both smaller and certainly less wealthy. In turn, the upper limit placed on the number of traders – a highly unusual practice for any developing country city – has the effect of acting as a clear barrier to entry into economic activity for informal sector operators.

Zonal laws however also go hand-in-glove in urban centres with licence issuance for informal traders. Again, this remains a highly unusual practice in a developing country context in relation to informal trade. Information from one city – Cape Town – reinforces the restrictive and over-regulated form of management of the informal sector. Hence, in the case of Cape Town, an online e-services system exists. The fact that such a system exists – whilst on its own restrictive – is further reinforced by the fact of an assumption of access to online facilities by the applicant. In addition, the system has a number of inter-linked steps prior to permission being granted for the individual to be allowed to operate and

trade in what is probably one of the wealthiest cities in the continent. These steps include firstly the individual needing to register online. Secondly, the individual would need to gather the required documents needed for the application. These are proof of address, a copy of their identity document or work permit, an affidavit stating that they are unemployed, and a photograph of themselves. Thirdly, the individual will need to find a suitable trading bay that is being advertised, apply for that specific trading bay and submit the required documents via the online system. If the applicant receives the highest score according to an AI-generated automated system of selection, they will be asked to attend an in-person screening interview. After successfully completing the interview, the applicant will then receive confirmation of the allocation of the trading bay and be requested to pay the informal trading permit fee. However, before the permit can be issued, each applicant needs to undergo an induction course on the rules and trading conditions in the city. Both the steps in the licencing process and indeed, the very existence of a licencing process – embedded in most cities in South Africa – is highly unusual for a developing country.

Given the above, it should be clear that this micro-regulation arising out of the broader Businesses Amendment Act 186 of 1993 has arguably engendered an ultimately highly aggressive and restrictive regulatory approach to the informal sector in South Africa. If one adds to this legislative environment – a clear policy of city officials to criminalise any actual or perceived transgression by informal traders in cities through physical harassment, confiscation of goods and jailing (Skinner, 2018; Mkhize, Dube, & Skinner, 2013:1, 22) – then it is amply clear that South Africa's regulatory environment and its enforcement thereof is designed to control the number of informal traders and to regulate their trade. This regulatory over-reach in informal sector management, rather than the default in almost all developing country cities of no management at all, possibly remains one of the key reasons for the inordinately low number of informal sector operators in the South African economy.

3.2 Spatial Inequality

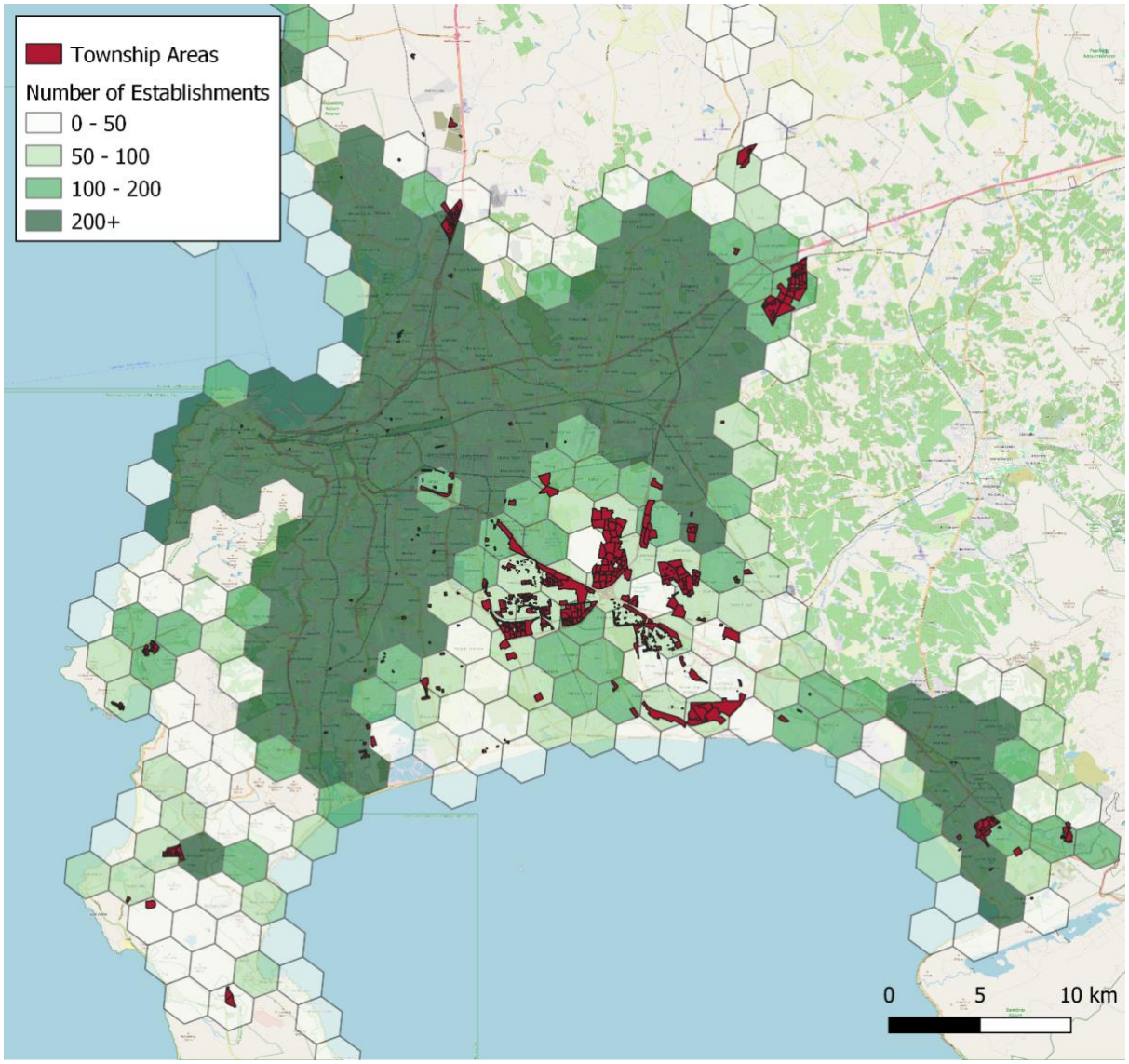
The spatial legacies of the apartheid government have resulted in present-day spatial dispersion and systemic issues in relation to how people and jobs are distributed in South Africa. This spatial segregation has in turn disproportionately affected the poor and economically marginalised. Post-1994, many people migrated from rural areas and settled on the outskirts of the cities. Individuals in former homelands are of course worse off than people outside these borders, as homeland areas tend to be insufficiently dense and poorly connected, resulting in low economic activity (Lochmann, 2022). Those that migrated internally within South Africa, from rural to urban areas, have a higher probability of employment, and a higher real wage income (Lochmann, 2022).

These spatial issues affect those living on the outskirts of the city – and their ability to participate in the informal sector – on multiple levels. On the one hand, these people are further away from nodes of economic activity. As there is a lack of efficient and affordable transport infrastructure in South Africa, individuals need incur high transport costs and long commute times to reach economic hubs where there are more opportunities On the other hand, for those located outside of the main economic hubs and trading spaces, who are trying to participate in the informal economy in that location, opportunities can be limited. Lower purchasing power of potential customers and low foot traffic due to low built-up density, can limit demand to engage with informal businesses. (see Hausmann et al., 2023). Informal businesses therefore have two options to choose from: 1) Pay high transport costs to travel to communities with a larger economically active population, 2) remain operating within the current location and be limited by the informal economy in that area.

Figure 8 presents the locations of townships versus the number of formal enterprises (establishments) in each area. The hexagon shades represent the number of formal establishments within that area, with

darker green representing a higher number of establishments. Areas with a higher number of formal enterprises represent areas where more activity and potential employment and customers are located.

Figure 8: Township vs formalized economic hubs in Cape Town (Based on number of Establishments per hexagon)



Source: Authors, using City of Cape Town (2022) and Nell & Visagie (2023).

Without a functioning transport infrastructure service available to use, this adds to the difficulties experienced by both individuals in wage employment and informal economy participants when trying to access markets. From the figure, we can see that townships typically fall outside or along the outskirts of the areas where higher economic activity takes place. This illustrates the need for informal sector workers to travel into the economic hubs where they would be more successful in growing their businesses. The need to travel to economic hubs is influenced by both transport infrastructure and the availability of trading spaces in economic hubs.

Furthermore, transport infrastructure is not only a necessity for informal sector operators trying to trade in the economic hubs, but also vital for accessing suppliers. Despite many informal sector workers being township and home-based, this does not mean that they are home-bound, and may still require access to an efficient transport system (Chen, 2014).

In South Africa, commute times from homes to jobs have increased. Between 1993 and 2013, all modes of transport can be characterised by increasing mean travel time to work (Kerr, 2017:328). Moreover, these times are higher for African individuals, and those in lower income quintiles. Transit times for informal workers also tend to be longer than formal sector workers – a manifestation of their vulnerability. This exacerbates the circumstances of informal workers who are situated far from opportunities in the first place. City of Cape Town officials have indicated that informal traders travel between 2 and 4 hours to get to trading locations. In Gauteng, township dwellers have a longer average commute time than all other neighbourhood types, and spatial policy reform instruments (such as mixed-use developments and mega-housing projects) have not influenced commute times (Moselakgomo, Mokonyama & Okonta, 2017).

These rising commute times mean higher monetary transport costs. In Mexico City, high commuting costs have been shown to induce workers to choose informal sector work over formalised work (Zárate, 2019). Using the National Income Dynamics Survey (Wave 2) and National Household Travel Survey for 2020, Shah and Sturzenegger (2022) find that transport costs are significantly correlated with employment status in South Africa (see Table 1).

Table 1: Transport Costs and Employment Status

	Dependent variable			
	Log Share of Working Age Population			
	Wage	Own Acc.	Unem. Broad	Inactive
	(1)	(2)	(3)	(4)
Log Total Transport Cost (Adj.)	-0.206***	0.323**	0.089	0.182***
	(0.050)	(0.157)	(0.132)	(0.057)
Constant	0.128	-5.192***	-2.375***	-1.969***
	(0.221)	(0.696)	(0.586)	(0.252)
Observations	52	52	52	52
R^2	0.256	0.078	0.009	0.171
Adjusted R^2	0.241	0.060	-0.011	0.155
Residual Std. Error (df=50)	0.271	0.853	0.717	0.308
F Statistic (df=1; 50)	17.189***	4.235**	0.454	10.329***

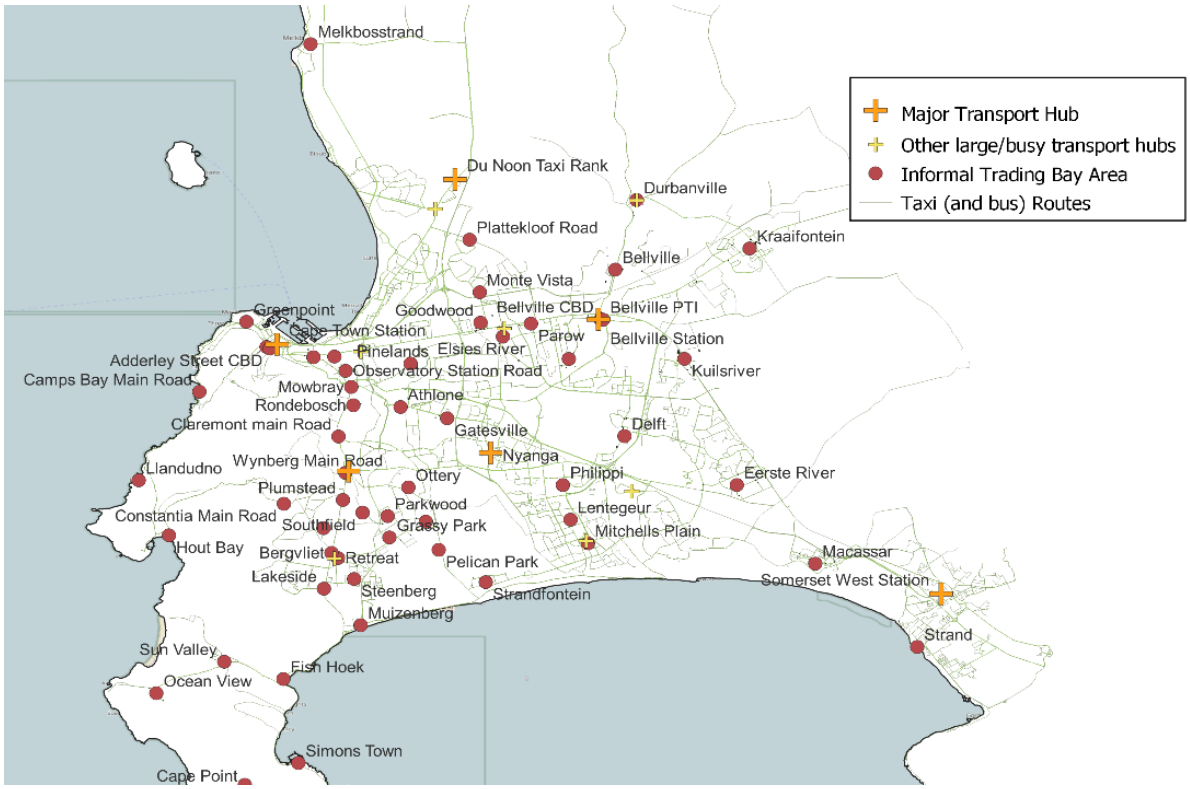
Note: *p<0.1; **p<0.05; ***p<0.01.
Source: Shah and Sturzenegger (2022).

In Shah and Sturzenegger's (2022) study, a 10% increase in average transport costs was associated with a 2% decline in wage employment, a 3.2% increase in own account employment and a 1.8% increase in those listed as inactive[5].

Evidence from city officials through the various interviews also confirm that transport hubs and informal trading opportunities are highly correlated. Officials for example indicated that the busiest transport hubs in the Cape Town metro are Cape Town CBD, Bellville, Nyanga, Somerset West, Wynberg and Du Noon. Figure 9 illustrates the high correlation between locations of trading bays and these transport hub locations. We see that although not all trading bay locations are at a transport hub, typically the major transport hubs will have informal trading bay spaces located at or nearby the stations.

[5] Not in wage employment, own account employment or broad unemployment.

Figure 9: Locations of Informal Trading Bays and Select Transport Hubs, Cape Town



Source: Authors, using City of Cape Town (2022).

However, the potential gain from placing trading bays close to transport hubs is limited by two factors. First, those who have more disposable income typically do not make use of public transport in South Africa, meaning that those with more disposable income are less likely to come across traders in these areas. Second, the deterioration of rail infrastructure in South Africa has further reduced foot traffic at transport interchanges.

Ultimately, South Africa's history of spatial segregation which has remained entrenched in the post-apartheid period, has served to also mitigate against the growth of informal trading in the country. Data from the city of Cape Town thus makes it clear that whilst attempts have been made to offer trading bays linked to transport hubs, this remains both inadequate but also serves as an instrument for ensuring that vulnerable workers only have access to consumers who are least equally vulnerable. Access to richer consumers remains in large part beyond the average informal trader given both licencing and zonal laws as noted above – but also effectively ensured through an historical distance to market metric which mitigates against the expansion of informal trade into the richer more densely populated CBDs of South African cities.

3.3 Crime and Security

Issues related to security and crime influence the environment in which informal traders operate. Criminals target informal businesses who typically do not have adequate security measures, nor full protection from the police. In their response to our questionnaire, City of Cape Town Officials indicated that crime is the most relevant constraining factor for informal businesses. This perception is shared by potential and current informal sector workers (Cichello et al. (2011), Willemse (2011), and Statistics

South Africa (2019)). Willemse (2015) surveyed migrant business owners in Johannesburg concerning factors influencing day-to-day business operations, and found that police and crime were mentioned by 70% and 63% of respondents, respectively. Moreover, 29% of respondents found that private security have a positive influence on their business.

Informal sector firms generally have little or no insurance. The World Bank (2023b) notes that more than 10% of South African informal businesses are exposed to economic crime annually, while only 1% of informal businesses reported spending on security. With a lack of capital and limited insurance, this means that the loss of inventory due to confiscation or theft, (and/or in turn the inability to offer services) can be catastrophic for informal sector entrepreneurs. Larger firms are typically able to spend more on security systems that are effective at detecting and deterring crime (Moyo, 2011: 15). Thus, smaller and informal firms are more vulnerable to crime.

Bhorat and Naidoo (2017) studied the perceptions and incidence of crime in an urban township setting, using the 2012 World Bank Diepsloot Enterprise Survey. According to the data, the perception among survey respondents was that crime was the most serious hindrance to successfully operating and growing of enterprises. Furthermore, the study found a strong relationship between older and wealthier informal firms and the incidence of crime. These are firms that that may be closer to moving into the formal economy. The implication of this is that these firms may be limited by crime when trying to move from the informal sector into the formal economy, and there is scope for affordable security measures for smaller firms.

However, Shah (2022) argues that although crime is perceived to play a substantial role in deterring participation in the informal economy, the impact is not large enough to explain why South Africa's informal economy is relatively small compared to other developing economies with similar crime rates. It may be the case that the opportunities for crime are exacerbated by other constraints that relate to where these informal sector entrepreneurs are located.

Using the City of Cape Town as an example, because most informal traders live and trade outside of or on the periphery of the city, the factors constraining them may be related to where they are located. Areas on the periphery of the city are more impacted by the lack of efficient and safe transport infrastructure or limited access to asset protection. These additional challenges might be exacerbating opportunities for crime, and addressing them could potentially alleviate the issue of criminal activity targeting these traders.

3.4 Urban Infrastructure

In a survey of informal traders by the City of Cape Town (2021b), the main infrastructure/ services informal traders highlighted for improving their trading circumstances were (1) lockable storage, (2) other (with shelter, permanent, structure, roof, permit being the dominant response), (3) water, (4) public toilets, (5) electricity, (6) waste and garbage removal, (7) law enforcement, (8) health (inspection) services, and (9) lighting at night.

Many informal businesses also do not have shelter or access to storage; this means that informal business may be more affected by the weather than common infrastructure needs. Moreover, goods and services are therefore vulnerable to becoming damaged, spoilt or stolen. Municipalities however say they are not responsible for storing goods for businesses (Daniels, 2023). Without storage facilities, goods are even more vulnerable to crime, with the cost of this also considered substantial to informal traders (ibid., 2023). Occupational hazards, such as lack of shelter and storage space affects not just the health but also the productivity of workers. The challenges are related to other common issues

experienced by those in the informal economy such as lack of rubbish removal, no toilets, and blocked drains, which all ultimately lead to a loss of customers because they are not acceptably hospitable.

Moreover, many vendors in the informal economy do not have access to essential infrastructure at their trading bays, such as running water, a toilet, or electricity (Guven & Karlen, 2020). This has repercussions regarding hygiene and the health and well-being of vendors and patrons. This is a particular concern for people preparing food for public consumption. Lack of running water and toilets further discourages customers, since amenities enable customers to spend more time engaging with informal businesses.

Asmal, et al (2024), using data from the SESE (2017), find a notable correlation between access to amenities (piped water, electricity, and sanitation) and the average employment growth over a 12-month period (Table 2). In particular, they show that amenities can increase firm employment growth by 21% over a 12-month period. This suggests that urban businesses that have access to amenities are more likely to stay operational and maintain or expand employment over a sample period of 12 months. These findings highlight the important role that urban infrastructure plays in fostering growth, and emphasises the need for strategic urban planning that ensures access to amenities for informal businesses.

Table 2: Probit regression - Dependent Variable: Firms which have increased or maintained employment levels over the past 12 months[6]

Variables	**Marginal effects**
Dependent variable: 12 Month firm employment growth >=0	
Operational	
Urban	0.0570* (0.0323)
Amenities	***0.0825** (0.0397)***
Financial literacy	-0.0191 (0.0539)
Advice	0.0620** (0.0314)
Financial records	-0.0921*** (0.0347)
Debt	-0.1033 (0.0959)
Insurance	0.1910 (0.1216)
Location	
Owners dwelling w/o own space	0.0266 (0.0413)
Structure attached to owners dwelling	0.0252 (0.0648)
Another person's dwelling	0.0228 (0.0746)
Non-residential building	0.1185* (0.0640)
Taxi rank/bus station/train station	0.2570*** (0.036)
Footpath, street or open space	0.0649 (0.0463)
Open market with a permanent kiosk	-0.0393 (0.1709)
Mobile (no fixed location)	0.0620 (0.0405)
Customer's homes or offices	-0.0435 (0.0812)
Other	-0.1303 (0.1124)
Number of observations	**1534**
Wald chi²(33)	**214.94**
Prob > chi²	**0.0000**

Source: Asmal, de Villiers, Monnakgotla, and Rooney (forthcoming).

[6] Firms surveyed for the SESE are asked the number of employees they currently employ as well as the number of employees the firm employed at the same time a year ago. From this we have deduced whether firms have increased and maintained their employment over the past year. Firms which increased or maintained their level of employment were coded as 1, otherwise 0.

*Notes: Additional Controls Included: Age, Gender, Race, Marriage, Educational Attainment, Industry. Robust standard errors in parentheses; '***' denotes p-value < 0.01 ; '**' denotes p-values < 0.05; '*' denotes p-value < 0.10.*

Another important consideration is that a large share of those involved in the informal sector are home-based workers. Proper shelter or storage space, sanitation, electricity, water, and access to the internet are important for home-based business growth. Furthermore, clear and usable roads are needed for general access to the community. This is important not only for allowing business to function, by allowing deliveries or improving access to customers, but also allowing services such as waste disposal and security to reach these areas (Yu, 2002).

Ultimately though, within an environment that is simultaneously far away from markets, unsafe, and in turn subject to overly stringent regulation, informal sector operators – should they overcome all these barriers to entry – are then in turn offered very little by way of an enabling infrastructure. Such infrastructure – many of which are common for formal enterprises – includes storage facilities, waste removal, water and sanitation, and electricity. This basic infrastructure, which is essential for sustenance of the sector – a sector so critical as an alternative to unemployment – is almost completely absent in all of South Africa's major urban centres.

4. Supply-side Economics of a Good Type: An Overview

The discussion above makes clear that there a number of challenges that individuals face in accessing economic opportunities in the informal sector. These exogenous constraints listed above impose costs on individuals and businesses, whether they be in the form of transport costs, security costs, regulatory costs, or infrastructure costs. By mitigating these costs that are faced by individuals and businesses through appropriate measures, entry into the informal sector and expansion of informal sector businesses can be incentivized. This is ultimately embedded in the notion of 'supply-side economics of a good type'. Importantly however, the constraints (or costs) that require addressing for incentivization of informal sector businesses vary in accordance with the type and size of business. Section 4.1 highlights the constraints (and corresponding costs) on individuals across a spectrum of businesses of different sizes, with different likelihoods of operating within the informal and formal sectors.

4.1 A Firm Support Package Matrix: A Primer

Based on the challenges noted above, we can think of a number of different ways in which businesses in the informal sector can be supported to overcome the costs imposed on them by exogenous constraints.

The constraints businesses face, and costs imposed on them, differ depending on whether they are located in the formal and informal sector, and the size of their operations. They will therefore require alternative mixes of policy to address the costs that they face in order to incentivize their operation and growth. For example, an informal one-person survivalist enterprise may be urgently in need of storage facilities, while a formal medium-sized enterprise may require subsidized finance to grow their business. Small and medium businesses, in both the formal and informal sectors, can be offered support that addresses their most pertinent constraints and blockages by lowering the costs of those constraints on those businesses.

The table below shows that businesses of different sizes face different challenges according to their size and stage of growth.[7] As firms increase in size and turnover, the nature of the constraints they face, and the type of support they require, evolves. The logic of the matrix is that firms of different sizes will require different policy support within each of the broad areas. Further, firms of different sizes have different likelihoods of being located in formal and informal sectors, and this may require alternative types of support.[8] Indeed, it is entirely possible that such broad support will differ in emphasis and tenor by sector and across different time periods. As a static picture and as a framework for supply-side interventions, the central thrust of the policy matrix is to ensure that policy makers in South Africa – when thinking about infrastructure support for example – are considering not only the recapitalisation of ports for exports, but also ensuring that storage facilities are provided for informal sector firms at the city level. The same may be true for example if we consider the regulatory constraints for large firms (which may for example involve phytosanitary standards on exports) relative to informal sector operators, who face local government regulations which actively limit the number of firms which can operate in the CBD.

Table 3: A Firm Support Package Matrix to Address Exogenous Constraints on Businesses

Intervention Area/Firm Size	Own Account	Micro (1-4)	Small (5-9)	Medium (10-49)	Large (50+)
Constraints					
Regulation	Zoning Regulations	Zoning Regulations	Business Licensing; Extension To Non-Parties; Red Tape; State Procurement	Tax, Customs&Trade Regs; Extension To Non-Parties; Comp. Policy; Tax Exemptions; State Procurement	Tax, Customs And Trade Regulations; Stronger BEE; Legislation
Spatial	Distance from market; Lack of economic opportunities where individuals are located	Distance from market; Lack of economic opportunities where individuals are located	Distance from market; Lack of consumers where businesses are located	Distance from Workers; distance to market	Distance from Workers; distance to market
Infrastructure & Security	Internet Access &Cost; Storage Space To Operate; Transport; Access To Land; Security	Internet Access& Cost; Storage Space To Operate; Transport; Access To Land; Security	Internet Access& Cost; Electricity Cost; Improved Security; Transportation	Internet Access& Cost; Electricity Cost; Improved Security; Transportation	Regular, Quality Supply Of Energy, Water, Transport Infrastructure
Fiscal and Regulatory Support					
Supply-side Incentives to Lower Costs Imposed by Exogenous Constraints	Revise by-laws; crime prevention interv. ; infrastructure; Zero-Rate Licences;	Revise by-laws; crime prevention interv. ; infrastructure; Zero-Rate Licences; Wage	improve ease of formalization ETI– Increase Wage To SMEs; Subsidized Credit; Tax	Reduce red tape; ETI – Increase Pc Wage To SMEs; Subsidized Credit; Tax	Reduce red tape; SOE Regulation; EPZs; Stronger Legislation; SME-BEE

[7] The table only shows exogenous constraints that we have discussed in this report that are broadly outside the control of business owners, and for which government can either improve the environment in which businesses operate, or provide support to compensate for the constraints imposed on business owners in these areas. Firms also have firm resource and skill constraints (not having the resources or knowledge or skills to operate a business). These constraints are not the focus of this report.

[8] The matrix notes that businesses on the smaller end of the spectrum are more likely to be informal than businesses on the larger side. The matrix, however, is not intended as a blueprint as to how businesses should transition from informal to formal.

	Wage Subsidy; Transport subsidy	Subsidy; Capital Grants; Transport subsidy	Exemptions; Capital Grants	Exemptions; Capital Grants	Supply Chains; Target Specific Labour-Intensive Sectors With Incentives
Number of Firms	1 281 678	482 336	121 561	132 708	19 461

Hence, the table provides a menu of possible constraints specific to firm size and organized according to the composite constraint. Here we have identified these composite constraints as being in the areas of regulation; space and infrastructure; and security. Indeed, other constraints could be added including financial services access and skills for example. The key though is that each constraint 'block' will differ in detail by firm size. A micro-enterprise will have storage facility as a key infrastructure constraint, whilst a large firm's infrastructure constraint will be poor functioning rail and ports. In turn though the table also directs one to the regulatory and fiscal response that may be required to respond to the identified composite constraint – again organized by firm size. Hence, infrastructure improvement in the South African large firm context is currently focused on improving the functioning of SOEs. In the informal trading context, as we showed above, providing adequate basic infrastructure such as storage facilities to these traders would be a critical constraint to overcome. The list of regulatory changes and fiscal support are also of course not exhaustive, and in some cases may be too simplistic. What this firm policy matrix offers however, is the organizing framework for policymakers to think about what the detailed constraints are for each segment of the firm size distribution, and then to design detailed policy responses – organized by regulation and fiscal incentives we would argue – for each of these firm-size cells.

4.2 Towards Policy Guidance for the Informal Sector: Early Thoughts

It remains true however, that in the case of the informal sector in South Africa, arguably too little emphasis has been placed on policy intervention and policy change in order to ultimately give more economic oxygen to this part of the economy. And indeed, global evidence suggests that there is a positive economic return to such policy change. For example, evidence from a field experiment study by Blattman et al. (2014) in Uganda, found that grants increased business assets by 57%, work hours by 17%, and earnings by 38%. It was also found that many of the candidates were able to formalise their businesses and ended up hiring more labour. A long-term RCT aimed at supporting women and youth entrepreneurship in rural Bangladesh was found to enable severely disadvantaged women to move out of agricultural employment and start their own microenterprise (Bandiera et al., 2013). It focused on both asset and skills transfers to eligible women. These women were offered various business opportunities, such as livestock rearing to retail trade, coupled with training specific to their chosen business. In a broader policy approach it may also be worthwhile exploring a similar approach such as that taken by the World Bank in respect of 'Economic Inclusion (EI)' packages. These EI packages are not targeted to informal sector firms in particular (and are not purely focused on exogenous constraints faced by individual) – but present a way to think about the types of support that can aid individuals to improve their livelihoods. Support offered through these packages have ranged from food security and social inclusion to enhanced market access and financial inclusion. Economic inclusion packages have been shown to create productive safety nets; promote better jobs and livelihoods through asset transfers, loans/access to credit/ financial education, and training; and promote financial inclusion (World Bank, 2019:10-12).

Given the positive global examples with supply-side interventions for survivalist enterprises, it may be worth providing a set of early thoughts which could be utilised to energise the policy debate around encouraging the expansion of informal sector activities in South Africa. Based on our evidence above, we settle on two possible short-term targeted options to incentivize individuals to operate businesses

in the informal sector in South Africa: These would be firstly to lower, remove or indeed change the conditions of licensing and registrations costs of, and stipulations to, informal trading. Secondly, post-registration for a trader, we consider the possibility of infrastructure and transport subsidies to overcome both capital and spatial constraints for informal sector operators.

A critical caveat to these proposed short-term options: Clearly the most important policy shift would be to entirely deregulate the management and oversight of the informal sector. Hence, this would in specific terms require the dismantling of the entire edifice of the business trading and urban management regulatory architecture for local governments and cities in South Africa. At the core of the latter lies the Businesses Amendment Act 186 of 1993 (Republic of South Africa, 1993) as illustrated above – but many more pieces of legislation would need to be altered to effectively deregulate the informal sector. Such a freeing up of informal sector access to markets however requires a long and detailed – and possibly contested – amendments process, which many city governments will either oppose or be unable to see the benefit of. In turn there is of course a real likelihood of a rapid 'race to the bottom', as was the case in the early 1990s when the backlash from city governments effectively rolled back the freeing up of markets to the informal economy enshrined in the original Businesses Act 72 of 1991 (Republic of South Africa, 1991). In this regard then, a slow, gradual process of supporting and nurturing expanded access of opportunities to the informal sector, through carefully considered supply-side measures, may serve as precisely the demonstration effect required to phase in more all-encompassing regulatory change. We turn then to the two examples of this demonstration effect.

4.2.1 Licensing Fees and Conditions

When considering licence fees in the current city informal trading environment, it is clear that a business license/s and being allocated a trading bay, solves the constraints associated with security of tenure for many traders. In turn however, the drawbacks of trading bay-license rigidity is that informal traders may struggle to respond to a changing economic environment – which may require moving to a different, more lucrative location based on altering market and economic conditions and dynamics. Think here of a new mall being opened, or a new large formal employer moves into the city. Perhaps one solution for municipalities that have been overly rigid, is to introduce some leeway or flexibility in the spatial boundary of the trading licence. Hence, such flexibility could allow for a much more expansive interpretation of where within a spatial boundary informal traders are permitted to trade. Thought could also be given to removing constraints on the type of trade which can be undertaken.

In terms of the licencing process, the strong consensus amongst government officials interviewed was that online applications for permits were superior to paper-based systems. This is because paper-based systems remain onerous, time-consuming, wasteful, more prone to human error, and more susceptible to corruption. On the one hand there are efficiency gains from using an online system. On the other hand, the online application process itself represents a barrier since it relies on having a device and access to the internet. One possible solution would be to utilise technology solutions that do allow for the vulnerable to have access to the online licencing system, together with a closer link to other state services – such as grants disbursement – where access to a much larger pool of vulnerable individuals is possible.

Apart from changing the conditions of licencing one must recall that licence fees are due for every successful trading application. We present below the detailed estimates of licensing fee costs for the City of Cape Town for 2023. It is clear firstly that licence fees are dependent on the type of product or service being offered, with the key distinction being between food and non-food trading, and whether such trading is happening through a designated formal granted bay. The key here is the cost of the fee – which must be viewed as a cost of doing business for informal sector workers in Cape Town – that stands on average at 147% of the value of the Social Relief of Distress Grant (SRD) offered to all unemployed South Africans. At the median licence fees are some 136% higher than the SRD.

Table 4: Mean and Median Licencing Costs by Type of Informal Trading, City of Cape Town Sell non-foodstuffs

Activity	Mean (R)	Share of SRD	Median (R)	Share of SRD
Sell non-foodstuffs from bay	272.32	0.78	209.3	0.60
Sell meals from bay	935.32	2.67	872.3	2.49
Hawk* non-foodstuffs	107.2	0.31	107.2	0.31
Hawk meals	745.2	2.13	745.2	2.13
Total	515.01	1.47	477.25	1.36

*Notes: * - pedestrian trader. SRD of R350. Business licence of R10 for hawking, else R25. Certificate of acceptability R638. Trading bay fee is unweighted mean. Source: City of Cape Town (2023, 2024a, 2024b).*

Ultimately, the state in this instance has imposed a barrier to entry to would-be agents willing to engage in economic activity – that is higher than the unconditional grant offered to unemployed South Africans. The policy dissonance between discouraging work and incentivising grant collection is very clear. Given this additional, and arguably unnecessary, supply-side cost for starting and running a business for informal traders, a zero-rated licence is proposed as a clear and simple solution to boosting informal sector activity. Currently many municipalities charge breakeven fees for the associated administration system for managing informal traders. Yet by all accounts, relative to other municipal costs, these administrative licencing costs are fairly benign for most city governments. Indeed, one could view this proposed zero-rating of licence fees as a clear subsidy to encourage or lower the barriers to entry for informal traders.

4.2.2 Transport cum Infrastructure Subsidies

Once the individual informal sector operator has been registered and is granted a licence through a process that is possibly more open and low-cost to vulnerable individuals and households, it is clear that constraints to market access and market production remain. Principal amongst these in the South African context, would be distance to market and also the capital costs of setting up a business. Distance to market is represented by the spatial vestiges of apartheid which have been noted above. Guzman and Oviedo (2018) found that public transport subsidies have reduced accessibility gaps (between rich and poor) to income-generating opportunities in Bogotá.

The need for a capital grant, or indeed an infrastructure grant, relates to the high set-up costs required of an informal trader to operate within an urban and semi-urban setting. One can think of this relating to for example, movable structures and the necessary equipment required to trade ranging from food equipment through to point-of-sale devices. Key to this policy proposal for both the transport voucher and the infrastructure subsidy, however, is that the capital grant is conditional on being offered a trading licence and in turn can be subject to a means-test for individual traders. Currently no local governments in South Africa, as far as can be assessed, offer these supply-side grants to informal traders.

Early design principles for each of these subsidies could include for example an endogenous transport subsidy where the subsidy value is proportionate to the distance to market for the individual trader, with a maximum payable subsidy value. The transport subsidy could also potentially be conditional on proof of regular trading. In terms of the capital grant, again conditional on a licence being issued – the specific form of trading (street vending, food, clothing, manufacturing, arts & crafts) could elicit a particular infrastructure grant value – with maximum value again. One extension of the infrastructure grant – particularly for example in the case of food trading – would be for the local government to

provide the actual infrastructure to ensure adherence to existing health and safety legislative provisions. In direct relation to the infrastructure grant however, would also be a provision for city officials to provide adequate and easily accessible storage for infrastructure used by informal traders as well – where it is known that such complementary infrastructure is critical for successful street trading. The latter infrastructure includes for example ablutions facilities, access to water and sanitation and electricity provisioning. Currently these are not codified in legislation, and could indeed form part of a legislative amendment process from the national government.

Ultimately then, the notion that licencing is altered to both reduce the costs, widen the access and also deregulate the provisions of trading – are a critical first step to increasing access to informal sector operators. Secondly however, once this licencing and registration process is reformed it is essential that the costs of operation – either spatial or infrastructure related – are indeed ameliorated in a structured manner by local governments. The notion of a transport as well as a product-specific infrastructure grant must then feature as a policy support package to informal traders in South African urban centres.

5. Conclusion

In this paper, we have argued that South Africa's unemployment problem is, in one aspect, a consequence, obtusely, of a suppressed rate of informality. If South Africa's unemployment rate was consistent with what is observed in countries with similar levels of national income, its unemployment rate would have been 7% in 2019 instead of 26%. It is clear thar one of the key reasons then for South Africa's extraordinary rates of joblessness lies in the high barriers to entry to informal employment. These barriers, we note, would not seem to be evident in other middle-income countries, given that on average these economies record 45 out of every 100 individuals to be in informal employment, compared to South Africa's estimate of 16 out of every 100 members of the labour force.

We show then that a series of exogenous factors – including onerous and unnecessary regulation, spatial segregation, crime and the lack of urban infrastructure – are just three of the core reasons mitigating against the growth of informal sector activities in South Africa. Focusing on these factors, it is clear that the current approach to regulation of the informal sector, which is done through a lens of urban management rather than economic inclusion, is a major constraint on the expansion of the informal sector in South Africa. Regulation serves as a key barrier to market access for firms operating in the informal sector. Related to this – but more difficult to overcome in the medium-term – the presence of spatial apartheid makes it very difficult for individuals living and operating businesses in less developed parts of the economy to access key markets. We also argue that challenges related to the lack of supporting urban infrastructure, and the impact of crime on businesses and individuals, also act as key constraints in growing the informal sector.

In turning to an initial discussion on policy solutions, we utilize the notion of a firm size-based policy matrix which we argue can direct policymakers in terms of thinking about policy packages in relation to firms categorized by size. Regulation-, infrastructure- and spatial-related policy packages are the ones identified here, through which policy solutions ranging from deregulation, to fixing SoEs and providing fiscal incentives across the size continuum, can thus be identified. Using this matrix, we show then how deregulation is the key manner in which to creatively destroy South Africa's inordinately high barriers to entry for the informal sector. Short of this unlikely outcome – which does require longer term policy engagement – we propose a few shorter-term policy interventions. These policy changes, in the domain of licensing costs and conditions, transport vouchers and infrastructure provisioning, could in our view all serve as a starting point for ensuring a more responsive and incentivized policy environment, to fully realising the potential of the informal sector in South Africa, and in its significant ability to generate materially improved income generation opportunities for unemployed South Africans.

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Appendix A: Questionnaire

A. Overview

1. What types of economic activity take place within the informal sector in your municipality?	
• Trading	
• Services	
• Construction	
• Manufacturing	
• Other	

2. To what extent do informal businesses in your municipality fall into the following categories?	
• Survivalist micro-enterprises	
• Enterprises employing 2 to 4 people	
• Enterprises employing more than 4 people	

3. Approximately how many businesses are operating in the informal economy in your municipality?	

4. Approximately how many people work in the informal economy in your municipality?	

5. Based on your knowledge, what are the most common reasons for entering the informal sector:		
• Retrenchment		
• Poverty		
• Unemployment		
• Flexibility		
• Having a comparative advantage		
• Other, please specify		

B. Understanding the Constraints to Informal Sector Growth and Employment

1. There is a lot of research related to informal trading. However, how are other informal economic activities regulated? (Such as Informal construction; informal services). Are there similar regulations for other informal economic activities?	
• Yes	
• No	
• Please provide more detail:	

C. Demand and supply of trading bays

1. How many licences/spaces are available?	

2. How is it decided how many spaces are made available at each informal trading area?	

3. How is it decided where informal trading areas should be placed?	

4. On a scale of 1 to 5 (1 being least important and 5 being most important), how important are the proximity of the following neighbourhood features when deciding where informal trading areas and bays are located?	
• Police station	
• Transport interchange	
• Taxi rank	
• Shopping mall	
• Lack of a shopping mall	
• Urban density	
• Wealth of neighbourhood	
• Number of tourists	
• Unemployment	

5. What are the busiest transport hubs in the city?	
6. How many informal traders work at these hubs?	
7. How correlated are transport hubs with informal trading opportunities?	

8. What is the average travel time for informal traders?	

9. Should trading bays be placed specifically in high unemployment neighbourhoods?	

10. What criteria excludes someone from obtaining an informal trading permit?	

D. The Application Process and Permits

1. How long is the trading permit valid for?	

2. Are there designated trading bays/spots available, or is finding a spot (compliant with by-laws) the duty of the trader?	

3. Once a bay (location) is assigned to a trader, would they be able to switch to a different space or do they have to re-apply for a new space?	

4. Are these the correct steps in the application process to obtain an informal trading permit?	Yes / No
1) Register for e-services	
2) Gather required documents	
3) Apply for a specific trading bay that is being advertised	
4) Screening interview process	
5) Confirmation and allocation of trading bay	
6) Pay informal trading permit fee	

5. How would you rate the ease of the application process as a whole for the informal trader? (mark with an X)									
Very easy		Easy		Neutral		Difficult		Very Difficult	

6. How would you rate the ease of each step in the process of obtaining a trading licence for the informal trader? (1 - Very easy, 2 – Easy, 3 – Neutral, 4 – Difficult, 5 - Very Difficult)	
1) Register for e-services:	
2) Gather documents:	
3) Apply for trading bay:	
4) Screening interview process:	
5) Confirmation and allocation of trading bay:	
6) Pay informal trading permit fee:	

7. How long does the application process generally take in its entirety from application to approval (upon payment of fee)?	

8. What factors determine the score that the algorithm calculates for allocation of bays/permits?	

9. Does place of residence influence permit issuance?	

10. How many applications are received annually?	
11. What percentage of applications are approved?	
12. What are the most common reasons for rejections?	

13. How many people can trade/operate under a single permit?	

One result of a study on the Cape Town Informal Economy Development Spatial study conducted in 2015 was that multiple traders could operate on one spot throughout the day (morning, lunch and evening), which would be more efficient, but does not appear to currently be allowed according to regulations.		
14. Do you agree that this should be allowed?	Yes / No	
15. Why is this currently not being done?		

16. How are permit fees determined?	

17. How do permit fees compare to other jurisdictions?	

18. What are the alternative permit options? For example, the city offers a 'beach trading permit'.	

19. How do traders apply for a permit to be mobile traders/for mobile food trucks?	

E. Support for informal trading from the City

1. With respect to infrastructure and services, which of these does the city provide to informal traders/trading bays? (mark with an X)									
Electricity		Water		Internet Access		Security		Storage facilities	

2. If the city does provide these, are there associated costs for traders? If so, what costs do traders bear in respect of each of these?	
Electricity	R_____
Water	R_____
Internet Access	R_____
Security	R_____
Storage facilities	R_____

3. If the city is not providing any of these, do you believe that they should, to support informal sector businesses? If YES, indicate which of these should be provided.	

4. Does the City offer support programmes to entrepreneurs in the informal economy? If so, what types of support is offered?	
5. Are these city-led programmes related to financial skills?	
6. Are you aware of any other skills and financial training being offered by any other stakeholders to informal sector workers or those wishing to enter the informal sector? If YES, please provide details:	

F. Views/Opinions and Policy Options

1. On a scale of 1-5, how relevant do you think each of the following factors are for constraining informal sector operation, growth and creating employment? (1 – Irrelevant, 2 – Somewhat irrelevant, 3 – Not sure, 4 – Relevant, 5 – Very Relevant)	
1) Regulations	
2) Infrastructure	
3) Education and skills (human capital)	
4) Access to financial assistance	
5) Competition	
6) Crime and corruption	

2. How often does the city perform checks on informal traders?		
1) Weekly		
2) Monthly		
3) Quarterly		
4) Bi-annually		
5) Annually		
6) Other, please specify:		

3. Are there any other factors you believe are relevant constraints on informal sector operation, growth and job creation? Please provide a reason for your answer.	Yes / No

4. Do you believe police/law enforcement restricts informal sector activity in any way?	
If yes, please provide more detail:	

5. Do you agree that the current informal sector regulations sufficiently promote activity and participation in the informal economy?	
If yes, please provide more detail:	
If no, do you have any suggested regulations/policy changes that may improve/promote informal activity?	

6. Do you agree that a wage subsidy for survivalist firms is an efficient way of incentivising informal sector activity? Please provide a reason for your answer.	Yes / No
7. Please highlight any challenges that you believe may be faced with respect to the implementation of such a policy.	

8. Do you agree that a transport subsidy is an efficient way of incentivising informal sector activity? Please provide a reason for your answer.	Yes / No
9. Please highlight any challenges that you believe may be faced with respect to the implementation of such a policy.	

10. For which of these is the lack of each of these items inhibiting operations and growth of informal businesses?		
1) Electricity		
2) Water		
3) Internet access		
4) Security		
5) Storage facilities		
6) Other, please specify:		

11. Do you agree that a zero-rated hawker's licence is an efficient way of incentivising informal sector activity? Please provide a reason for your answer.	Yes / No
12. Please highlight any challenges that you believe may be faced with respect to the implementation of such a policy.	

Thank you.