



# Formal but Less Equal. Gender Wage Gaps in Formal and Informal Jobs in Urban Brazil



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## ARTICLE INFO

### Article history:

Accepted 28 August 2017

### Key words:

gender wage gaps  
informality  
selection into work statuses  
Latin America  
Brazil

## SUMMARY

In developing countries, a large share of employees work informally and are not covered by employment protection legislation. I study how gender inequality differs across formal and informal wage-earners in urban Brazil. The raw gender wage gap is about the same on average in informal jobs (5%) as in formal jobs (7%), but I show that this difference is the result of different male and female selection processes. First, female employees have better observable characteristics than male employees, for example in terms of educational attainment. After controlling for observable characteristics, the adjusted gender wage gap is on average about 24% among formal employees and about 20% among informal employees. Second, men and women entering formal and informal jobs have different unobservable characteristics. Controlling for endogenous selection into formal vs. informal jobs, I find that the gender gap in wage offers is high and increases with education in formal jobs. In informal jobs, however, estimated wage offers are the same for men and women. I discuss the potential implications of these findings regarding the effect of labor market regulation on gender wage gaps.

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## 1. Introduction

A striking characteristic of labor markets in developing countries is the existence of a large informal sector where labor regulations are non-existent. Labor regulations protect workers against several risks, for example unexpected job loss, by defining the conditions under which firms are allowed to lay off employees. Men and women do not depend in equal measure on these labor regulations since, for example, only women need to stop working around childbirth. Employees are entitled to parental leave and benefits, and job protection during leave as long as their contract has been officially registered; parental leave and benefits are almost exclusively used by women. This asymmetry affects how men and women value formal salaried jobs. It also influences the incidence of statistical discrimination against women.<sup>1</sup> While

informal jobs have lower labor protection and labor costs, they may offer other benefits to workers such as greater flexibility. Those aspects are likely to influence female and male wages in different ways. It is thus important to understand how men and women sort across different types of jobs and to analyze how the gender wage gaps in formal and informal jobs differ. Moreover, it is useful for policymakers to understand the gender wage differences in formal and informal jobs separately since it sheds some light on how employment regulation affects women's prospects compared to men's in the labor market.

This paper focuses on employees in urban areas of Brazil and aims at examining whether significant gender gaps in earnings exist among both formal and informal wage-earners and whether the gender wage gap differs across these two groups. There are several reasons motivating the choice to focus on employees. First, it is important to analyze employees separately from other groups, such as self-employed workers, because certain determinants of gender differences in earnings apply only to employees such as employer discrimination for example. Second, there are different ways of defining informality and the criteria vary across employment statuses (Henley, Arabsheibani, & Carneiro, 2009). Looking at employees, I am able to adopt one concept of informality that depends on employers' compliance with the legislation. The formal and informal workers that I compare are similar in the sense that

<sup>1</sup> Discrimination implies that two individuals who are equally productive are treated unequally because they belong to different groups, defined by gender. Statistical discrimination suggests that employers have imperfect information on the behavior of their employees regarding, for example, labor market attachment as defined by the probability of quitting or duration of leave. If employment discontinuity and job protection generate higher labor costs for the firm through the reorganization of personnel as well as vacancy and replacement costs, employers have incentive to reduce expected wage offers because women take on average more or longer periods of leave.

they all have an employer and receive a wage. Third, focusing on employees makes it possible to compare the findings to others found in the literature, which concentrates heavily on the gender wage gaps. Lastly, employees account for the biggest share of employment. To complement the main analysis on formal and informal employees, I also provide estimates and a discussion of the gender earning gap among the self-employed.

In this paper, I do not attempt to estimate the causal effect of labor market legislation on employers' discrimination against women, but I do show that the gender gap in potential wage offers is much higher in formal salaried jobs and discuss scenarios that are consistent with this finding. To recover the gender gaps in potential wage offers I control for both observable characteristics of workers and non-random selection into formal and informal salaried jobs.<sup>2</sup> Failing to deal with non-random selection into formal and informal jobs is a major concern as it would lead to misleading estimates of gender wage gaps. Using the estimated gap in wage offers, I am then able to show what share of the total gender wage gap truly cannot be explained by workers' productive characteristics. To do so, I first use a multinomial logit model and study the sorting of men and women into different employment statuses: informal employment, formal employment, and not in paid employment. I then investigate how selection into work status affects the estimation of the gender wage gaps using the control function approach. Wage equations are estimated for formal employees and informal employees separately. In the last step, I use the Oaxaca-Blinder-Ransom decomposition to compute the gender wage gaps in both types of jobs.

The empirical analysis uses the Brazilian household survey, the Pesquisa Nacional por Amostra de Domicílios (PNAD), for the year 2015. In Brazil, all employees of the private sector have a labor card (*carteira de trabalho*) which is a booklet in which their employment biography is recorded. By signing this document, both the employer and the employee commit to abide by labor regulations and employees are entitled not only to labor rights but also to social security benefits. The PNAD provides information on whether the worker's labor card is signed by the employer so I am able to adopt a definition of informality based on employers' compliance with labor market regulations. Public sector employees are considered as formal employees.

Looking at the raw data, I find that the total gender wage gap is on average the same among formal and informal employees and increases with education in both types of jobs. Controlling for observable characteristics, I find again no significant difference between the gender wage gap among formal employees and the gender wage gap among informal employees on average.

Controlling for selection into work status, I find that the gender gap in potential wage offers is no longer significant among informal employees but remains significantly positive and high among formal employees. The gender gap in potential wage offers is the highest among highly educated people in formal salaried jobs but it remains insignificant across all educational levels in informal salaried jobs. These findings are consistent with a greater incidence of statistical discrimination against women and a glass ceiling effect in formal jobs. A positive gender wage gap in formal jobs is also consistent with compensating wage differentials for job protection and social security benefits when protection and benefits are more valued by women.

This paper contributes to a small strand of the literature that studies labor market outcomes for men and women when a large share of employment is informal. [Pagán and Ullibarri \(2000\)](#) find

that in Mexico the adjusted gender wage gap is larger in unregistered firms compared to registered firms. Using data for Turkey in 1994, [Tansel \(2001\)](#) finds that the adjusted gender wage gap is strong and positive among workers with social security coverage but not significant among uncovered workers. [Deininger, Jin, and Nagarajan \(2013\)](#) focus on casual workers in India and find that the gender wage gap is particularly important for casual workers in the agricultural sector but not in non-agricultural sectors. I depart from these papers in two ways. First, in my definition of informality I focus on employers' compliance with labor regulations rather than on social security coverage or temporary work. Having information on the worker's contract rather than on firm registration enables me to consider informal wage-earners working in both registered and unregistered firms. Second, in the empirical methodology, I compare two approaches for dealing with non-random selection into multiple employment outcomes and estimate the wage function and selection bias for different education groups.

This paper is also related to the vast literature on the segmentation of the labor market and the formal wage premium. Several authors question the dualistic view of the labor market and find that some workers are actually better off choosing informal jobs ([Gunther & Launov, 2012](#); [Magnac, 1991](#) among others). Interview data for Brazil reported in [Maloney \(2004\)](#) suggest that about 30% of both male and female informal employees are voluntarily working informally. However, the motives behind this choice differ for men and women. Out of the 30% of women who preferred informal employment, about 13% cited competing household chores as the reason for this preference. Almost no men chose to work informally to balance paid employment and household responsibilities. More than 10% of men said that they did not want a formal job because they earn more in their current informal job, a statement less than 4% of women agreed with. This suggests that there might be different selection rules into informal vs. formal jobs for men and women. I attempt to uncover these selection rules for female and male employees and to present estimates of the gender wage gaps adjusted for the selection biases.

Finally, this paper contributes to the literature on gender wage gaps and the role of selection into employment for the assessment of gender wage gaps by adding the informality dimension (see [Arabsheibani, Carneiro, & Henley, 2003](#); [Albrecht, Bjorklund, & Vroman, 2003](#); [Blau & Kahn, 2006](#); [de la Rica, Dolado, & Llorens, 2008](#); [Madalozzo, 2010](#); [Olivetti & Petrongolo, 2008](#) among many others). I show that women are more positively selected than men in formal jobs but not in informal jobs. Accounting for selection has a different effect on the gender gap in wage offers in formal and informal jobs.

The remainder of the paper is organized as follows. I start by discussing the impact of informality on gender employment and wage inequality while reviewing the related literature. Section 3 sets up the empirical model. In Section 4 I first describe the data and provide descriptive statistics on gender inequality among wage-earners in the urban labor markets of Brazil. I then discuss the results, looking at the selection into potential work-statuses before moving on to the comparison of the gender earnings gaps in formal salaried jobs, informal salaried jobs, and self-employment. The last section concludes.

## 2. Why should informality matter?

Before considering the empirical evidence, I first ask why the gender wage gap should differ across formal and informal jobs.

*Individual characteristics across different types of jobs.* According to the dualistic view of the labor market, the informal sector is characterized by lower wages. Empirical evidence confirms that

<sup>2</sup> Non-random selection into jobs means that, even after controlling for observable characteristics, formal employees are systematically different from informal employees in a way that affects their wages. This is also referred to as "selection based on unobservables".

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