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# Trade, Informal Employment and Labor Adjustment Costs<sup>1</sup>

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## Abstract

Informal employment is ubiquitous in developing countries, but no existing studies have estimated workers' switching costs between informal and formal employment. This paper builds on the empirical literature grounded in discrete choice models to estimate these costs for workers in Brazil and Mexico. The results suggest that inter-industry labor mobility costs are large, but entry costs into informal employment are significantly lower than the costs of entry into formal employment. Simulations of labor-market adjustments caused by a trade-related fall in manufacturing goods prices indicate that the share of informally employed workers rises after liberalization, but this is due to entry into the labor market by previously idle labor, a mechanism that has been seldom analyzed in the existing literature.

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Keywords: Informal Economy, Trade Policy, Trade and Labor Market Interactions.

JEL Classification: F16, F13, E26.

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