

## Employment Status and Subjective Well-Being: Evidence from Indonesia

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“Without work, all life goes rotten. But when work is soulless, life stifles and dies.” -- Albert Camus

“...I was looking for a job and then I found a job, and heaven knows I'm miserable now...” -- Steven Morrissey and Johnny Marr

### Extended Abstract

#### Motivation

In the development literature, the informal sector is often viewed as an unregulated sector where workers have less attractive terms of employment relative to their counterparts in the formal sector. Researchers are divided, however, as to whether “informality” is just another characteristic of employment or reflects a barrier to entry into formal jobs.<sup>1</sup> If informal sector employment provides flexibility not found in the formal sector, for example, then informal workers may be no worse off than those employed in from formal sector. By contrast, a “constraint” view suggests that institutional failures prevent a large portion of the population from having better jobs (De Soto 1989, Loayza 1994). Employment in the informal sector as a result of excessive taxes and regulations that prevent workers from registering or accessing formal jobs, and workers who would otherwise prefer the benefits of formal jobs are excluded in a segmented market. A “voluntary choice” view of informality, on the other hand, considers that informal jobs reflect workers’ choice given their human capital, preferences, cost and benefits of formality, and the availability of other means of social protection (Perry et al 2007). Self-employment can bring independence and flexibility (Maloney, 2004), and may be preferred if social security is provided irrespectively of whether one contributes to its financing (Levy 2008).

In Indonesia, differences in earnings and access to health and pension benefits across informal sectors, as defined by the Central Bureau of Statistics, suggests that formal sector jobs are preferable (World Bank, 2010). Examination of summary statistics , however, does not provide definitive evidence against the the possibility that some workers may nonetheless prefer the flexibility of informal sector work. This paper focuses on a non-pecuniary outcome of informality, the subjective well-being of the workers, to assess whether informal sector workers are indeed worse off.

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<sup>1</sup>For a review of findings on informality, see Maloney (2004), La Porta and Schleifer (2008), and World Bank (2007).

According to the “constraints” view, workers face barriers to entry into formal jobs, and thus formal sector workers should report higher levels of job and life satisfaction. The “choice” view implies that after controlling for individual and job characteristics, informal workers may be as well off those in the formal sector. In Indonesia, roughly two thirds of employment is informal (World Bank, 2010). If the constraints view is correct, then one third of the labor force enjoys utility rents at the expense of the rest. This paper looks into the use of subjective well-being data (SWB) to study the existence of “happiness rents” in Indonesia’s labor market. It responds to the question: are self-employed informal sector workers more or less happy than workers earning a wage? Transitions into the informal sector may provide a buffer against unemployment when there is an aggregate shock lowering demand in the formal sector.<sup>2</sup> If that is the case, then self-employed informal sector workers may have less job and life satisfaction and show lower levels of subjective well-being.<sup>3</sup>

We document the association between informality and subjective well-being of individuals. We first document whether informality is associated with lower job and life satisfaction, and examine whether there are significant differences by gender in differential job and life satisfaction and subjective well-being between formal and informal sector employment. Next, the paper exploits county-level shocks to wage employment to examine the extent to which involuntary employment in Indonesia’s informal sector affects dimensions of well-being.

### **Methodological Approach**

The main data sources for this paper are the 2000 and 2007 waves of the Indonesia Family Life Survey (IFLS). The IFLS provides exhaustive information on households, individuals and community characteristics. It asks respondents question on life and job satisfaction, as well as mental health questions that will be used to build an index of SWB widely used in the literature, the Center for Epidemiologic Studies Short Depression Scale (CES-D10). The design of the data is particularly suited to answer the questions presented in the literature. The IFLS allows us to examine the evolution of SWB and job satisfaction. While most of the literature uses cross sectional data, the panel allows controlling for unobserved individual characteristics that might drive the results in other studies. Furthermore, we next describe the effect of transitions between employment states on changes in SWB. Finally, we use employment shocks from district level employment data aggregated from SAKERNAS surveys to identify the effects of constrained informal sector employment on measures of well-being.

*The Indonesia Family Life Survey (IFLS).* The IFLS contains exhaustive information on individuals and household characteristics. As noted in our discussion above, a module on mental health allows one to construct alternative measures of SWB that are consistent across the two waves. An employment module contains the questions on job characteristics, including the availability of benefits such as health insurance, pension, and other benefits, and detailed questions on job requirements such as physical effort, stress or social interactions. Since questions about the current job tenure were also asked, we also construct measures of exposure to different job characteristics. In addition, in the latest round of IFLS,

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<sup>2</sup> Extensive evidence from both Latin America and Indonesia suggests that informal work expands during down turns. Loayza and Rigolini (2006); Gutierrez *et al* (2010); Thomas *et al* (2000).

<sup>3</sup> Pages *et al* (2008) test this view using data from three Central American countries. They find that job satisfaction is not significantly different in the informal sector, especially for low-skill workers.

individuals are also asked rate their job satisfaction. The paper uses indicators of job characteristics for two purposes: First, they will provide descriptive statistics on how formal and informal jobs differ in their characteristics. Second, we control for these features in alternative regression models examining the relationship between SWB and informal sector employment.

*SAKERNAS*. The *SAKERNAS* is a repeated cross-section survey with a sample size of roughly 200,000 individuals from approximately 65,000 households. The nationally representative survey collects information on activities of individuals over 15 in sampled households. Information collected includes education attainment, labor market participation, job seeking characteristics, and for those who are working, the industry of employment and other job characteristics. We match the *SAKERNAS* to the IFLS panel in order to calculate changes in local labor market conditions over time.