

Impact of informal economy indicators on unemployment rate and economic growth in the Republic of Kosovo and the Western Balkans

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Abstract

The informal economy is a very important phenomenon which is present not only in developing countries but also in developed ones, thus attracting the attention not only of researchers and economists, but also of policy-makers. Moreover, the impact of the informal economy on the unemployment rate is indisputable, however what remains debatable is the extent and level of such an impact in developing countries.

The main purpose of this paper is to determine the impact of the informal economy on the unemployment rate and economic growth in the Republic of Kosovo and the Western Balkans for the period 2000 - 2018.

The methodology used in this paper is the indirect approach: MIMIC method (type of SEM). Causal variables include the business freedom index, economic freedom index, tax burden, unemployment rate and government size, while as indicative variables we have the currency (M0 / M1) which is defined according to the limitation of the MIMIC method as the indicator which is set to be fixed at the preliminary value, the labor force participation rate and the GDP growth rate per capita.

The results suggest that the informal economy has a significant positive impact on the unemployment rate and the GDP growth rate per capita. Regarding the correlation between the informal economy and other variables, the findings show that there is a positive correlation with the index of economic freedom and tax burden, while a significant negative correlation can be observed between the size of government in the Western Balkans for the period 2000 – 2018.

Keywords: informal economy, unemployment rate, economic growth, MIMIC method.

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