

# The Relationship Between Informal Employment, Tax Revenue, and Economic Growth: A Cross-Country Analysis

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## ABSTRACT

This paper examines the relationship between tax collection, GDP growth, and the informal economy, addressing the question of how limiting informal activity and maximising tax collection can boost GDP growth in a country. The paper first reviews existing literature to point out established economic theories and recognise real-world examples that link informal activity, GDP growth and the efficiency of tax collection. Secondly, a quantitative analysis was performed using the variables of average tax revenue as a percentage of GDP, mean annual GDP per cent growth and average informal employment as a percentage of total employment. This relationship between variables is examined using a variate regression model and a correlation matrix, which aid in examining the exact measure of the relationship among the chosen variables. The results from the data analysis present a strong positive relationship between average tax revenue as a percentage of GDP and mean annual GDP per cent growth, additionally presenting a strong negative correlation between average tax revenue as a percentage of GDP and average informal employment as a percentage of total employment. These findings suggest that weak and inefficient tax collection can discourage formal economic participation and limit long-term growth. Based on the findings, policy changes that make the tax system simpler, proper and strong enforcement mechanisms and administrative capacity building are all recommended to potentially enable economic growth, maximise tax revenue while simultaneously suppressing the reliance on informal activity. This paper acknowledges limitations in the consistency and reliability of the data on informal activity, which may affect the robustness of the data.

**Keywords:** Informal economy; GDP; Laffer curve; Informal employment; Fiscal policy; Tax compliance; Tax revenue; Developing economies; Tax rates

## INTRODUCTION

A functioning and efficient tax system is crucial to the economic development of any country. One of the key

roles of the government is to choose and employ policies that allow for successful collections of tax revenue annually. To achieve this goal, most governments in the world have created policies, rules and regulations to allow for a system that aids in the collection of taxes. Most countries' tax systems typically consist of a mix of direct and indirect taxes that assist governments in increasing tax revenue and help with increasing the fiscal budget, as highlighted in Bird R. (1).

In most cases within mixed market economies, as outlined in Musgrave R.A. (2) the public expects

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governments to provide merit goods such as, but not limited to, schools and libraries for education, hospitals and parks for wellbeing and providing grants and aids to lower-income families to allow for economic progress. Furthermore, governments of countries often need to develop infrastructure and foster technological advancements to improve the quality of life for citizens and minimise externalities in the economy. The tax system that a country chooses to employ heavily influences the annual tax revenue that a government gathers from the economy, hence influencing the extent to which the government will be able to provide for its citizens. Tax revenue collected by the government is one of the primary financial factors that enable the government of a country to undertake these activities. (Another primary financial factor that must not be overlooked for government funding is debt, which also accounts for the fiscal budget.) While a tax system is vital for the fiscal budget of a government and encourages the government to reinvest more into the economy, there have been some cases where a country doesn't solely rely on income tax for revenue, such as the UAE, Monaco, Panama PwC. Worldwide tax summaries online (3). In these countries, they normally rely on other resources, like geographical advantages or natural resources that are available in abundance.

Although literature that has been published has examined taxation, informality and GDP growth individually, there seems to be a gap in these articles that fails to analyse the relationship between GDP growth, informality and taxation simultaneously across different countries. To add, there seems to be insufficient quantitative data analysis examining whether high tax collections and low informal activity lead to economic growth in the form of GDP. The objective of this paper is to get rid of the gap that exists in current literature and examine how the efficiency of tax collection and informal activity affect GDP growth. The study contributes to current literature by presenting data on tax revenue, GDP growth, and informal employment across countries to statistically analyse these relationships. Through data visualisation and analysis, this paper aims to provide factual, data-based insights into how governments can improve GDP growth and the efficiency of tax collection while discouraging informality.

## **LITERATURE REVIEW**

This section reviews articles that discuss similar topics to mine that have already been published in the

field. While prior research has delved into these topics from different perspectives, a comprehensive review seeks to identify gaps, inconsistencies, and contradictions among these studies.

One of the articles most closely related to this paper is Ulyseas (4). This paper provides a detailed analysis of how the informal economy in developing Asian economies affects and changes tax systems and policies. It highlights the idea that the role of governments and policymakers is to ensure that tax systems and policies in countries are clear and understandable for citizens, in addition to ensuring they are properly enforced and followed to raise tax revenue. Ulyseas explores the idea that the 2 main types of businesses that conduct informal activity are low-productivity businesses that are simply surviving by conducting informal activity, and firms that are highly productive but choose to stay informal as a means of tax evasion, which can aid in maximising profits. This observation is vital as it proves that sometimes informal activity does not directly correspond with changes in tax policies.

Similarly, authors İlgün et al. (5) estimate a panel threshold analysis on BRICS-T countries. The article talks broadly about 9 "BRICS" countries and examines Turkey as well. The study examines the depth of the relationship between tax burden and informality and addresses how the relationship between tax burden and informality is a threshold effect rather than a straightforward linear relationship. This means that the relationship between tax burden and informality is only triggered at a certain point. The article also suggests that the informal economy/shadow economy induces a positive effect on tax revenue for governments until a certain point, after which it becomes negative. This can also be represented using a Laffer curve (6), which is a nonlinear relationship tax revenue and tax rates showing that increasing tax rates initially incur a positive effect on tax revenue until a certain point, after which the revenue starts declining. (The Laffer curve is a theory developed by Arthur Laffer in 1974 that analyses the relationship between tax rates and tax revenue for governments. The Laffer curve will not be used in this study as it requires nonlinear modeling and this study focuses more on the maximisation of GDP and economic growth through achieving a balance between informal activity and the collection of tax revenue through building trust and enforcing regulations properly. This article suggests that while moderate taxation may lead to an increased fiscal budget and higher tax collection, extreme tax rates incentivise firms to undergo informal activity, ultimately

reducing tax revenue. This is important because it highlights an inconsistency, proving it is not necessarily true that increased tax rates lead to higher tax revenue for governments and, in turn, can lead to higher informal activity instead.

Rogan (7) views the reason behind informal activity differently. This paper presents taxation as one of the key reasons why there is an increasing number of self-employed workers/ individuals in the informal economy. On the other hand, the paper examines the reasons for governments to tax individuals and firms and takes real-world examples through the form of case studies to inspect how types of taxation are affecting the shadow economy. Rogan suggests that governments should bring informal activity into the tax net to provide additional revenue through the form of tax for governments. The paper highlights that efficient tax systems must have low administrative costs and high enforcement for the formalisation of informal activity, aligning with Ulyssea (2021)'s findings, suggesting that for informal activity to stay minimal while improving tax revenue, high enforcement and low administrative costs must be employed.

The final article in this review is Akitoby (IMF). The article reviews 5 real country examples of successful tax policies and suggests practical solutions for current governments. The study suggests that sustained increases in tax collection are supported by improvements in infrastructure, simplified tax policies and heavy enforcement, which aligns with the ideas of Ulyssea (4) and Rogan (7).

These real-world examples provide real proof that long-term economic growth stems from public trust rather than constant increases in tax rates, further supporting the claim that proper enforcement of laws is key to reducing informal activity and boosting economic growth.

Upon examining these four articles, we can draw some conclusions, make comparisons, and formulate general assumptions. Firstly, all four articles suggested that countries would benefit more from simplifying tax policies rather than tampering with tax rates. Additionally, all four articles suggest that for the informal economy to decrease and for tax revenue in countries to be maximised, these tax policies must be enforced rigorously and the government must go the extra mile to enforce them. In Rogan's (7) case, he suggests that informal activity as a whole should be taxed by the government. In developing countries, minimising the informal economy is a huge factor that contributes

to the fiscal policies and budgets of a country. While minimising informal activity is important to the growth and development of a country, it is also important to acknowledge that informal activity is a huge contributor to lower-income households and can serve as a leeway against underdevelopment in lower-income households, as suggested in Deléchat C, Medina L. (9). Maximising tax revenue isn't only about minimising costs but also about making sure that citizens comply with tax regulations through setting fair rates and simple policies. Minimising the informal economy isn't only about lowering tax rates and setting tax policies, but also about the enforcement and complexity of these tax policies; the less the complexity, the better. However, there is limited analytical research that simultaneously examines the relationships between tax revenue, GDP growth, and informal employment across different countries globally. Many existing studies focus only on specific regions or qualitative analysis, leaving specifics out across countries.

This paper contributes to the literature by addressing the exact relationship globally through a multi-country global quantitative data analysis of tax revenue, GDP growth, and informal employment, through the use of a variate regression model, thereby extending existing research on taxation and informality to broader macroeconomic outcomes.

## **METHODS AND MATERIALS**

In this section of the paper, the mean data of all 3 variables is gathered, and the relationships between all 3 of my variables are analysed. This is shown through presenting tables and graphs. For this section of the paper, the 3 variables used are: GDP growth over time, tax revenue as a percentage of GDP and informal employment as a percentage of total employment, differing between genders. This data will be for countries worldwide. For this study, I have chosen to select 3 variables and the data for them accordingly. GDP growth (%): International Monetary Fund (IMF), World Economic Outlook database (11). For this variable, I collected data from the IMF between 1980 and 2025 and used it to calculate the mean, standard deviation, and interquartile range. The second variable is tax revenue as a % of GDP: IMF Government Finance Statistics (12), where I have counted the number of observations by country, interquartile range, mean and standard deviation. The last variable is informal employment as % of total employment: ILOSTAT database (10), which is presented

as a graph and not a table. It is important to note that the number of observations differs across countries because of the lack of data availability. Similarly, some countries like Russia only have data available from 1993 rather than 1980, like the rest of the countries. To add, the use of 2025 values is a prediction rather than an actual value since, at the time this paper was written, it was still 2025. This was to maintain consistency across the dataset, but it must be recognised.

After presenting all 3 graphs, observations can be made. A few similarities observed from the graphs above were that in countries with extremely high or low GDP growth, the informal sector of the economy is likely to

be higher than in a country with stable GDP growth. For example, a country like Mexico or India experiences high rates of informal employment as seen in Figure 3 while it experiences high volatility of GDP growth, as seen in Figure 1, in comparison to Germany, which experiences a low rate of informal employment and has relatively stable GDP growth. Another similarity that was noticed in all 3 graphs was that in countries with high tax revenue collection, informal employment tends to be lower with respect to countries with low tax collection (eg, Germany with high tax revenue and Mexico with lower tax revenue).

**Table 1.** Summary statistics of GDP growth by country (1980-2025).

| Country   | First Date | Last Date | Average | Standard Dev. | Interquartile range |
|-----------|------------|-----------|---------|---------------|---------------------|
| Mexico    | 1980       | 2025      | 2.25%   | 3.66          | 8.4                 |
| USA       | 1980       | 2025      | 2.64%   | 1.92          | 1.77                |
| UK        | 1980       | 2025      | 1.98%   | 2.84          | 1.75                |
| Germany   | 1980       | 2025      | 1.55%   | 2.06          | 1.83                |
| India     | 1980       | 2025      | 6.02%   | 2.64          | 3.08                |
| Japan     | 1980       | 2025      | 1.69%   | 2.34          | 2.89                |
| Singapore | 1980       | 2025      | 6.01%   | 4.13          | 5.29                |
| Russia    | 1993       | 2025      | 1.82%   | 5.41          | 6.97                |
| UAE       | 1980       | 2025      | 3.54%   | 6.51          | 5.52                |
| Romania   | 1980       | 2025      | 1.86%   | 5             | 5.32                |

**Table 2.** Summary statistics of tax revenue as a percentage of GDP by country, including the number of observations, mean, standard deviation, and interquartile range.

| Country   | No. of Observations | Interquartile Range | Mean values | Standard Dev. |
|-----------|---------------------|---------------------|-------------|---------------|
| Mexico    | 35                  | 5.84                | 20.80       | 3.09          |
| USA       | 24                  | 1.57                | 30.50       | 1.20          |
| UK        | 45                  | 2.35                | 35.45       | 1.92          |
| Germany   | 34                  | 1.46                | 45.30       | 1.16          |
| India     | 37                  | 1.95                | 18.98       | 1.29          |
| Japan     | 45                  | 2.6                 | 30.66       | 2.81          |
| Singapore | 35                  | 2.26                | 17.76       | 1.65          |
| Russia    | 27                  | 2.19                | 34.33       | 1.68          |
| UAE       | 35                  | 5.0                 | 29.93       | 5.28          |
| Romania   | 35                  | 2.1                 | 31.27       | 2.86          |



Figure 1. Annual GDP growth rate (%) by country from 1980 to 2025. Each line represents one of ten countries in the sample.

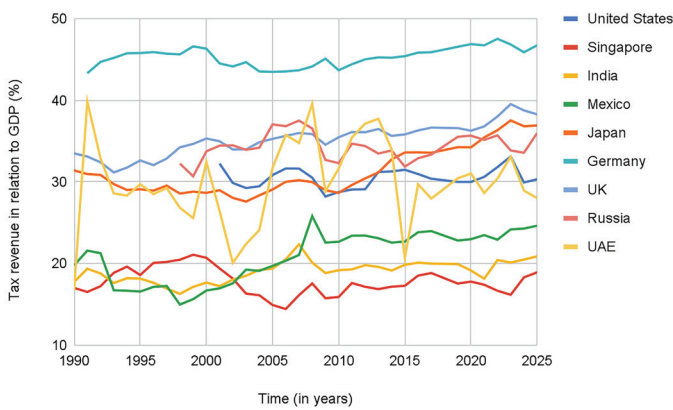


Figure 2. Tax revenue as a percentage of GDP by country from 1990 to 2025. Each line represents one country in the sample.

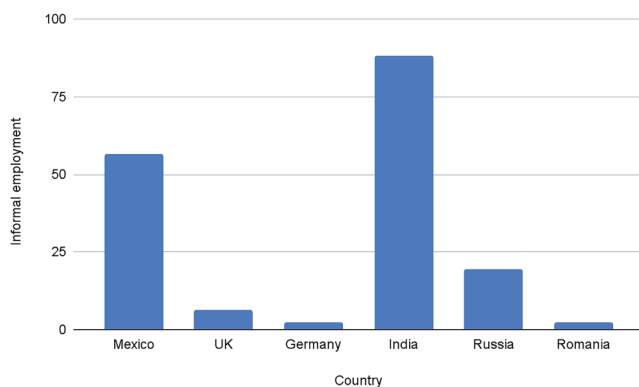


Figure 3. Informal employment as a percentage of total employment by country. Data coverage varies by country due to limited availability in the ILOSTAT database (2025). Countries with no available data are excluded.

Table 3. Cross-country comparison of mean annual GDP growth (%), mean tax revenue as a percentage of GDP, and mean informal employment as a percentage of total employment. Countries with missing informal employment data are excluded from that column.

| Country   | Mean annual. GDP growth | Mean tax revenue as a % of GDP | Mean rate of Informal employment |
|-----------|-------------------------|--------------------------------|----------------------------------|
| USA       | 2.64%                   | 30.5                           |                                  |
| UK        | 1.98%                   | 35.45                          | 6.512                            |
| Germany   | 1.55%                   | 45.3                           | 2.49                             |
| India     | 6.02%                   | 18.98                          | 88.364                           |
| Japan     | 1.69%                   | 30.66                          |                                  |
| Singapore | 6.01%                   | 17.76                          |                                  |
| Russia    | 1.82%                   | 34.33                          | 19.327                           |
| UAE       | 3.54%                   | 29.93                          |                                  |
| Romania   | 1.86%                   | 31.27                          | 2.206                            |

### Calculating correlation between 2 variables

To examine the relationship between all 3 variables, the Pearson correlation coefficient was calculated in Google Sheets using our data. The purpose of this tool is to quantify the extent of the linear relationship between variables. The formula can be represented as:

$$\text{Correlation} = \text{Covariance}(X,Y) / \text{STDEV}(X) \text{STDEV}(Y)$$

In this formula, the covariance between two variables represents how changes in one variable are associated with changes in the other variable. The standard deviation represents the variation of the variables in that particular dataset. A correlation coefficient close to -1 identifies a strong negative relationship between variables, meaning that if one variable increases, the other variable is likely to decrease and vice versa. A correlation coefficient close to 1 indicates a strong positive relationship between variables, meaning that if one variable increases, the other variable is likely to increase as well.

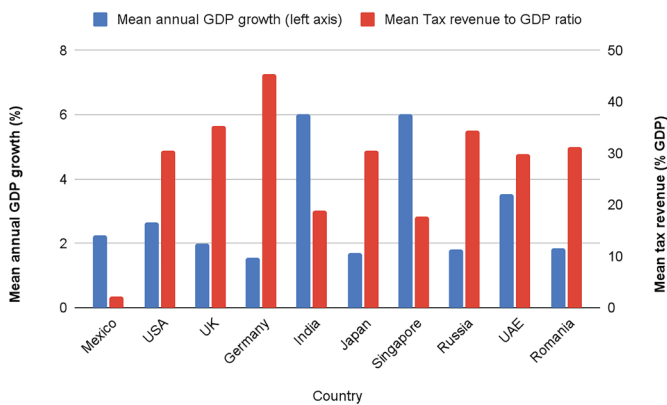
Below are graphs representing the relationship between variables taken as an average.

### UNIVARIATE REGRESSION MODEL

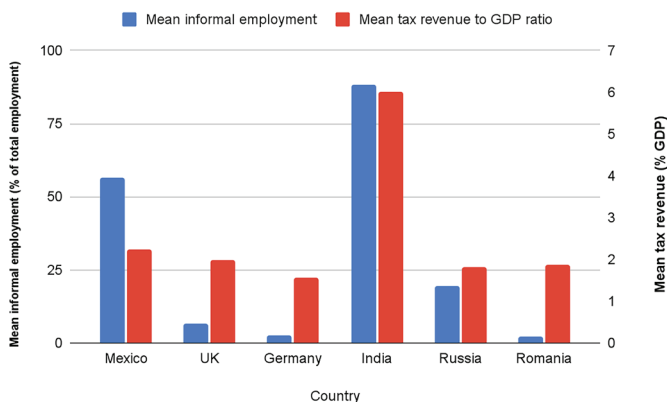
To examine the relationship between informality, tax revenue and GDP growth, this paper employs a univariate linear regression model. GDP growth is

**Table 4.** Correlation matrix showing pairwise linear associations between mean annual GDP growth, mean tax revenue as a percentage of GDP, and mean informal employment as a percentage of total employment across the ten-country sample. Values range from -1 (perfect negative correlation) to +1 (perfect positive correlation).

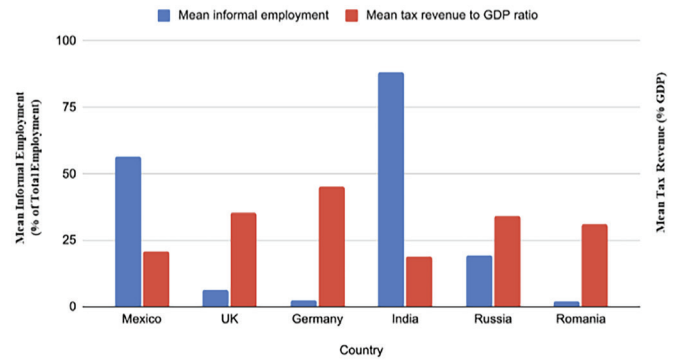
|                                  | Mean annual. GDP growth | Mean tax revenue as a % of GDP | Mean rate of Informal employment |
|----------------------------------|-------------------------|--------------------------------|----------------------------------|
| Mean annual. GDP growth          | 1.000                   | -0.758                         | 0.870                            |
| Mean tax revenue as a % of GDP   | -0.758                  | 1.000                          | -0.866                           |
| Mean rate of Informal employment | 0.870                   | -0.866                         | 1.000                            |



**Figure 4.** Mean annual GDP growth (%) against mean tax revenue as a percentage of GDP for ten countries.



**Figure 5.** Mean informal employment (% of total employment) against mean annual GDP growth (%) for countries with available informal employment data.



**Figure 6.** Mean informal employment (% of total employment) against mean tax revenue as a percentage of GDP for countries with available informal employment data.

treated as the dependent variable in this case (Y), while 2 separate independent variables (Informal employment and tax revenue) are put into different models with the dependent variable. Hence, 2 separate regressions are estimated, each affecting GDP growth differently, therefore providing separate data. The equation for the univariate regression model can be represented as:

$$Y = \beta_0 + \beta_1 X$$

Where Y denotes GDP growth, X represents the 2 separate independent variables,  $\beta_1$  is the slope coefficient and  $\beta_0$  is the intercept. The slope coefficient can be expressed using the equation:  $\beta_1 = \text{Covariance}(X, Y) / \text{Variance}(X)$  and the intercept can be expressed using the equation:  $\beta_0 = \bar{Y} - \beta_1 \bar{X}$  where  $\bar{V}$  denotes the mean value of the variable V. The slope coefficient measures the average change in GDP growth per one unit change in the independent variable. A positive slope value indicates a positive relationship between variables, and a negative slope value indicates a negative relationship between variables.

Additionally, the regression produces a P-value and a  $R^2$  value. In this case, the P-value tests the null hypothesis that  $\beta_1 = 0$ , which doesn't indicate a relationship between variables at all. A smaller P-value suggests that the observed relationship is statistically strong and unlikely to have occurred at random. The  $R^2$  value (also referred to as the coefficient of determination) represents how well the regression explains the variation in GDP growth using tax revenue and informal employment. The closer the  $R^2$  value is to 1, the better, since it explains how much of GDP growth can be explained by the X variables.

**Table 5.** Univariate linear regression results for two models estimating mean annual GDP growth (%) as a function of (1) mean informal employment and (2) mean tax revenue as a percentage of GDP. Reported values include the intercept ( $\beta_0$ ), slope coefficient ( $\beta_1$ ), p-value, and coefficient of determination ( $R^2$ ).

| Model                | $\beta_0$ | $\beta_1$ | P-value | $R^2$ |
|----------------------|-----------|-----------|---------|-------|
| X=Informalemployment | 1.36      | 0.04      | 0.02    | 0.76  |
| X=Tax revenue        | 7.51      | -0.16     | 0.01    | 0.58  |

## RESULTS AND DISCUSSION

After computing the correlation through a correlation matrix and after computing the univariate regression model, the findings of the data are discussed. Firstly, I computed the correlation between variables to assess the relationship between them. After computing the correlation between different variables, I found out that the variables with the highest correlation with each other were Informal employment and GDP growth. The correlation is a positive one of 0.87 between GDP growth and informal employment. This is a powerful correlation and suggests that the higher the GDP grows in a country, the higher the informal employment in that country becomes. Real-world examples to justify this data can be used. In Figure 5, the countries with high GDP growth tend to have higher informal employment. An example of this is India, where the mean annual GDP growth is approximately 6%, being the highest out of any other country by far; however, it comes with the unfortunate drawback of having the highest informal employment rate out of any other country in the sample, being around 88%.

Alternatively, in Figure 5, one can see that countries with stable GDP growth, such as Romania, tend to have a low informal employment rate. This is a strong positive correlation between variables. Additionally, the variables that were collected after performing the univariate regression model can be assessed. In this case, the  $\beta_1$  value is equal to 0.04, indicating that a one percentage point increase in GDP growth is associated with an average increase of 0.04 percentage points in informal employment. It is important to note that this reflects a statistical association rather than a causal relationship. Additionally, the  $R^2$  value for this equation is 0.76, meaning that 76% of the variation in GDP growth within the model is statistically associated

with variation in informal employment. This does not suggest that informal employment explains GDP growth in a real-world sense, but rather that the model captures a significant share of the variation in the dependent variable. The remaining variation may be due to other macroeconomic factors, such as inflation, or unobserved infrastructural differences. The P-value of these 2 variables supports the claim that their relationship can be explained by one another, since the P-value is 0.02, which is quite close to 0, meaning that there is only a 2% chance that the relationship formed between informal employment and GDP growth is random. This aligns with our correlation matrix, showing that there is a very strong positive correlation between informal employment and GDP growth. In developing countries around the world, labour is in very high quantities due to the overall consumption and demand for goods increasing when the GDP rises. Furthermore, in developing economies, due to time lags in enforcement, the government might not be able to implement educational training programs in time for workers to adapt to the boom in economic activity. This means that workers are often not skilled enough due to the lack of education, often having to take low-skilled jobs for a regular income, which are often unrecorded and unmonitored. The informal sector also supports sudden rises in economic growth better than formal jobs in economies, leading to increased job opportunities for those who are unemployed and unskilled.

Through the data collected and presented, one can also find that GDP growth and tax revenue have a negative correlation with each other, which can be visualised in Figure 4, which shows that in general, countries with high tax revenue tend to have lower GDP growth rates. The correlation matrix can be used to identify that the correlation between tax revenue and GDP growth is -0.758. In other words, this is a relatively strong inverse relationship, meaning that if one variable increases, the other is likely to decrease as well. As seen in Figure 4, we can observe that in countries with high GDP growth, like Singapore, mean tax revenue tends to be lower as a percent of the overall GDP, sitting at around 17.8%. On the other hand, in countries with high tax revenue as a percentage of the GDP, like the UK, the GDP growth tends to be relatively low. From the univariate regression model, the claim that there is an inverse relationship between tax revenue and GDP growth is supported by the /slope being -0.16. The model suggests that a one per cent increase in the tax revenue to GDP ratio leads to a fall in GDP growth by

around 0.16 per cent. The  $R^2$  value of the regression ends up being 0.58, which is quite decent. This means that 58% of the variation in GDP growth can be explained by tax revenue. The P-value of the regression is 0.01, suggesting that only 1% of the relationship between GDP growth and tax revenue is random. From an economic standpoint, the cause behind this might be the fact that when tax revenue increases, incentives for consumption and investment in the economy may potentially decrease due to consumers having lower disposable incomes if they are taxed more, especially if they are taxed more as a proportion of their income. Due to this, aggregate demand falls, and therefore, GDP falls too. On the other hand, countries with low GDP growth rates may increase taxes to help collect tax revenue, which can help fund government infrastructure projects, fund public goods and overall, if used properly, help citizens' overall quality of life through fiscal spending.

### **FURTHER LIMITATIONS**

Despite encouraging initial results, the present analysis still has some limitations, which are highlighted in this section. These limitations should motivate further research into findings from informal employment across different countries and sectors. Although this data appears to be coherent and relevant, it is a must to acknowledge that there are some limitations and areas where further research is warranted. For starters, though the univariate regression model provides insight into the nature of the relationship between variables, it is important to consider the data's statistical inaccuracies. In addition to reporting P-values, confidence intervals should ideally be calculated to provide a range of plausible values for the estimated regression coefficients. Moreover, in the graphs in the materials and methods section of the paper Figures 4-6 are based on small sample sizes that may affect the validity of the relationship. Additionally, this study is missing confidence intervals. Confidence intervals would calculate the precision of the slope line and would be useful to determine the validity of the data. Furthermore, the sample size of only 10 countries comes with some missing data points (e.g., Russia's GDP growth data only beginning in 1993), which limits the reliability of the data findings. Lastly, it is important to acknowledge that for some countries, data for the informal economy wasn't available due to insufficient findings. This affects the validity of the univariate regression models and can introduce bias to the data because of the missing countries.

### **CONCLUSIONS**

This study examined the relationship between tax revenue, GDP growth and informal employment to determine how fluctuations in tax revenue as a percentage of GDP growth and informal employment as a percentage of total employment affect GDP growth and overall economic growth. The findings suggest that higher tax revenue as a percentage of GDP is not consistently associated with higher economic growth, particularly in developing economies, due to reduced incentives, lower purchasing power and potentially an increase in savings.

Looking at the relationship between tax revenue and GDP growth, one can conclude that tax revenue is not always necessary for developing countries to develop their economy. High tax rates discourage spending and investment back into the economy and can potentially lead to tax evasion or avoidance, which can lead to the government losing out on money altogether. Through data and previous studies already published in the field, one can conclude that rather than increasing tax rates, governments and policymakers should focus on making tax policies easy to understand for the general public and ensuring that policies are enforced so that economic growth isn't suppressed. Additionally, looking at the relationship between tax revenue and informal employment, it is reasonable to come to the conclusion that governments honing in on building tax compliance through public trust and secure enforcement can broaden the taxable base by lowering the rate of informal employment. Which allows governments to invest more in infrastructure through the extra source of revenue gained by broadening the taxable base. Although widening the taxable base in an economy may allow the government to obtain funds for projects, it is also important to acknowledge that, according to our findings in the univariate regression model, an increase in tax revenue can lead to a decrease in aggregate demand and, therefore, GDP. This happens because higher tax revenues discourage consumption in the economy by lowering households' disposable income, meaning that they would be spending a greater proportion of their income on goods and services in the economy, with higher tax rates potentially leading them to spend less. To add, higher corporate tax rates and business taxes disincentivise firms to reinvest back into the economy in forms such as the development of technology, machinery or simply, the firm itself. This can lead to investment in the economy falling as fewer firms are investing in

the economy because of price constraints affecting the investment variable of GDP. Adding on to the first point, if tax rates do rise as a result of higher tax revenue, then it is likely that groups with a higher marginal propensity to consume will cause a negative multiplier effect, leading to lower economic activity, aggregate demand and therefore, lower GDP. Lastly, higher tax rates may reduce incentives to work harder and longer, take risks and start businesses and overall, decrease morale for those in the labour force. These reasons can also be used to suggest why governments should rely on trust and enforcement of tax policies rather than just looking at tax rates to attribute the success of a tax system.

In conclusion, in the short term, informal employment can enhance GDP growth by providing a boost of economic activity and can drive growth by creating easy and accessible jobs for workers; however, in the long run, informality can limit tax revenue for governments, prevent workers from gaining skills for the future and slow productivity which is bad for overall economic growth sustainability. It is important that governments recognise the importance of limiting the informal economy for sustainable development and economic growth, and focus on limiting the informal economy through understandable, accessible and easy tax policies rather than simply increasing tax rates so that they can broaden their taxable base, increasing government tax revenue, which can be used for investing back into the economy in meaningful ways. Governments should make tax policy changes that align with the best needs of the country and that can help increase efficiency through public trust, rather than focusing solely on the tax rates.

### CONFLICT OF INTEREST

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