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Social capital as a substitute for formality:
Evidence from Bolivia

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Abstract

The paper studies the role of social capital in the urban informal sector in Bolivia. It shows that a formal firm has about 6.4 times the sales of an informal firm with no social capital, but informal firms use their social capital to compensate for the lack of formal productivity benefits. By being formal, firms obtain permanent visibility because they can operate a shop or a visible production location and they can produce in locations with better public infrastructure. Informal firms, in contrast, sell in one place – typically in street markets in front of formal shops – and produce in another – typically in the outskirts. Social capital increases accessibility of informal firms and provides them with security benefits at their production location.

JEL classifications: O17; D22; H26

Keywords: Social capital; Formal and informal institutions; Informal sector; Small firms; Bolivia

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