The Unofficial Economy and the Business Cycle: A Test for Theories

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The shadow economy is an extensive phenomenon worldwide. It poses several questions, the consequences of fluctuations in economic activity being among the major ones. Based on official data, this paper establishes a set of cyclical properties of macroeconomic aggregates and studies how these vary across countries with the size of the unofficial sector. Through comparisons with the existing literature on business cycles in economies featuring underground activities, the obtained ‘stylized facts’ are used to test the relevance of theoretical predictions on the influence of the shadow economy. Using this procedure allows us to confirm that the evidence is not entirely of the sort suggested in business cycle models. In particular, some important macro aggregates and cyclical properties have been neglected in the analysis altogether, while others have been paid too much attention for no apparent empirical reason. Some possible avenues for future research can be drawn from this exercise.