

The Informal Economy in Cambodia

An Overview

While formal sectors could not generate adequate employment, attention should be paid to the informal economy where the vast majority of people are working and operating their business

In Cambodia, there are three principal formal sectors, garment, tourism and public administration. However, the informal economy takes a huge proportion of the remaining economy and is extremely beneficial to employment generation as well as economic growth. This informal economy benefits the vast majority of the people, particularly the poor, while the formal economy is not large enough to absorb the increasing labour force of the country.

Nonetheless, not enough attention has been paid to the informal economy, which deserves a considerably broad treatment. In the informal economy, enterprises have been plagued with an extensive array of constraints, burdensome and inappropriate regulations, which place limits on opportunities for better productivity and growth. Informal participants further encounter a variety of social issues such as exposure to very poor working conditions, child labour, AIDS/HIV, lack of democracy, gender inequality and so on. These predicaments are massive threats to the welfare of people and major obstacles to the fight against poverty nationally and internationally.

The majority of the poor are working and doing business in the informal economy. So if this economy is effectively assisted and impediments are eliminated, it will grow and eventually benefit the poor and the very poor in society. Cambodia seeks to alleviate poverty and thus needs to address the various problems found in the informal economy.

What is the Informal Economy?

In the 1970s, instead of using informal economy, the term informal sector was widely used to signify

activities which were not recognised, recorded, protected or regulated by the public authorities. The term informal sector has been developed and redefined to a better refined definition. Later on, the International Labour Organisation (ILO) coined a new term, informal economy by broadening informal sector to encompass the expanding and increasingly diverse group of workers and enterprises in both rural and urban areas operating informally.

In Cambodia, informal sector has been also used to denote these

unprotected and unregulated activities in the economy. Cambodia characterises the term informal sector as (1) activities which do not have a firm, identifiable postal address, (2) where workers are self-employed such as road side vendors where census data is usually not available, (3) where operations are labour intensive and where there are quick turnovers, (4) where the use of energy inputs are from human or animal sources and take place in non-structured premises where there are no regulations, licenses, insurance and taxes are not paid.

Box 1: ILO Program in Cambodia

The concept of promoting the informal economy was developed in the 1999 report of the ILO Director General through a vision of the Decent Work for all workers regardless of where they work. The benchmark of the decent work was measured by four defined factors: employment deficit, rights deficit, social protection deficit and representational deficit.

In Cambodia, the ILO promotion of decent work in the informal economy was introduced through a regional project, the so called Informal Economy, Poverty and Employment (IEPE) implemented in three different countries in the region: Cambodia, Mongolia and Thailand. The project aims to raise awareness of the dilemma in the informal economy; provide enabling environments, build capacity for informal participants; organise workers and enhance social dialogue; improve productivity and market access; promote social protection such as insurance, occupational safety and health and AIDS/HIV issues; and share knowledge and lessons learned.

Thus far, the IEPE has accomplished a range of activities for the support of the informal economy. These activities include (1) the publication of a handbook on commune council and civil society partnership, (2) support for a rapid assessment study on the five informal economy target groups conducted by the Cambodian Association for Informal Economy Development (CAID), (3) another study on legal requirements for business registration and handicraft export procedures conducted by the Artisan Association of Cambodia (AAC) and (4) provision of various training of trainers courses to home-based workers.

This ILO project is also assisting informal workers with the promotion of market access and capacity building. For instance, it backs the HURREDO organisation, which works to promote the production of vegetable products and their markets. Assistance has been offered to the *Groupe de Recherche et d'Echanges Technologiques* (GRET) to expand their health insurance plans to a larger number of informal workers. In terms of promoting awareness of the problems in the informal economy, the ILO project has commissioned the Economic Institute of Cambodia to conduct a literature review on the informal economy and produce a handbook in addition to another study on the extension of labour protection to the informal economy.

Source: International Labor Organisation (ILO)

Significance of the Informal Economy Key Issues

In Cambodia, the components of the formal economy exist primarily in three sectors: garment, tourism and public administration. These sectors are not able to generate sufficient numbers of jobs and absorb a continuously growing and unskilled workforce. For instance, the registered investments with the Council for the Development of Cambodia (CDC) in 2003 were at around US\$ 86 million, expected to create about 33,000 jobs; this number of jobs is not commensurate with the number of new entrants in the labour markets of approximately 200,000 persons annually. The informal economy therefore plays a great role in providing employment to people and contributes much to the economy. Its contribution to GDP has declined, given the potential growth of tourism and garment industries in recent years.

Within the framework of the informal economy, the non-agricultural workforce increased over years whilst the figure of workforce agricultural activities shows the opposite. This may be explained by the recent economic boom in tourism and the garment sector, which absorb a large range of informal activities in urban areas such as those activities serving both tourism and garment sectors: transportation, food, services of accommodation for workers...etc. These informal employments have encouraged people living in rural areas to migrate to urban areas.

There have been a variety of studies, policies and initiatives focusing on the formal economy which has been considered as an essential engine for employment generation and economic growth of the country. The informal economy has been, however, left in the cold in spite of its magnitude. This practice is in tune with the traditional view that the government does not need to intervene in the informal economy as the informal economy will, in any case, decline with economic growth.

Activities in the informal economy are not well regulated and protected. When they are regulated, the regulations are very multifaceted. As a result, informal workers are left outside the legal framework and thus face extortion and harassment by public authorities. This is frequently found in the daily lives of street vendors and micro-vendors at various public markets. Ambiguity or absence of market regulations and municipal regulations on the use of public spaces and sidewalks leave room for public authorities to solicit bribes. The vendors need to pay bribes to the public authorities in exchange for authorisation to sell and display their products, just to survive.

Legal and Regulatory Framework in the Informal Economy

In Cambodia, state regulations cause even more burdens such as corruption, bureaucracy and excessive costs of doing business compared to other countries. To formalise a business, operators need to register with various line ministries: the Ministry of Commerce for business registration, the Ministry of Economy and Finance for securing patent tax and/or value added tax identification

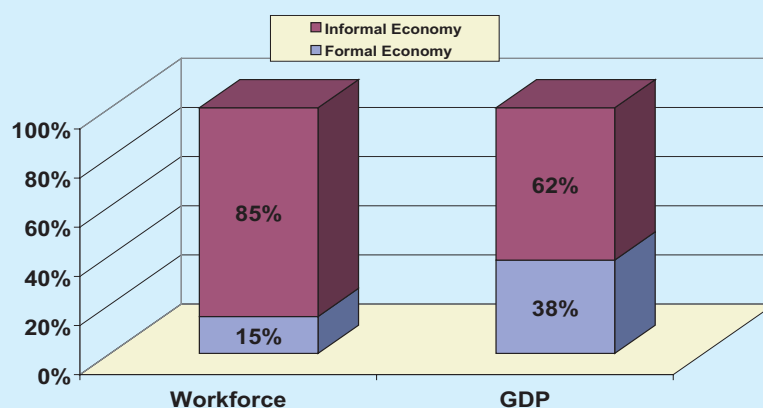
numbers, the Ministry of Labour for approval for internal rules and other relevant ministries if the business activity relates to other specific areas. Several enterprises have thus opted to remain informal and operate their business without permits and registration to avoid those burdensome, complicated regulations and the high costs of registration. Tax evasion and a lack of trust in government transparency of its tax management are other prevailing arguments for informality.

The vulnerability of people in the informal economy is twofold. On one hand, they have low and irregular income so they cannot afford to comply with burdensome regulations. On the other hand, in the informal economy, they are often plagued with a range of harassment and extortion such as unofficial visits from public authorities for bribes and repression.

Social Related Issues in the Informal Economy

Informal workers are entitled to neither legal nor social protection under the current labour legislation. They work in the informal economy where working conditions are worse than in the formal economy. Also, exposure to hazards in Cambodia such as AIDS/HIV is another threat to

Figure 1: Structure of the Cambodia's Economy



Source: Economic Institute of Cambodia (EIC)

their welfare, in addition to the absence of social protection.

Women in the informal economy take a huge proportion of unpaid work while men dominate the position of self-operator, which is the category that earns income for their families. Also, men are more numerous than women in other paid work categories. On economic terms, women have limited opportunity to generate income. They depend on men for their daily lives. Women in the informal economy are thus excluded from access to medical care, school and other social, cultural and political activities because of lack money.

Informal participants are rarely organised. If they are organised, their associations are often weak, lacking in focus or capacity on servicing members, and with no clear channels for their voices. Informal participants have difficulty in organising themselves because they comprise so many different occupations and activities that the people involved might have trouble recognising their common interests. And they lack time and opportunity to organise. So they have little to say in society. As a result, their interests and rights are not subject to discussion by policymakers.

Why Informal Enterprises do not Prosper?

In Cambodia, there are a large number of complaints about barriers to private sector business. Informal enterprises, especially micro-enterprises, face impediments similar to formal enterprises. Yet, obstacles to informal enterprises seem to be more diverse and they are more vulnerable. These obstacles are: poor infrastructure such as poor road conditions, high road taxes, high cost of water and electricity, limited access to training and formal education, lack of access to capital, lack of information about markets and raw materials, lack

of market access, excessive government regulation, a high cost of doing business, limited access to land and property rights, lack of skills and technology, no access to social security, competition from imports and poor product quality.

How to Promote Informal Enterprises?

If the above impediments are removed, these informal enterprises may gradually grow up and therefore secure the employment for new entrants into the growing labour force. The removal of constraints and the growth of informal enterprises are intertwined. In Cambodia, the government, donors and some NGOs take part in assisting informal enterprises with education, capacity building and microfinance. Despite concerted efforts of these institutions, the skill improvements and microfinance for these people are still very limited. Skills of workers and entrepreneurs need to be improved. Many people are still unable to access formal financial services.

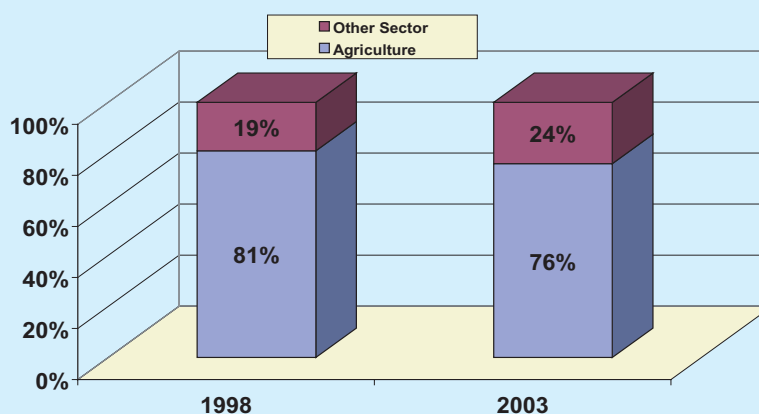
The capacity of lending institutions is limited. Microfinance institutions have been often criticised for mismanagement and high interest rates. Some microfinance schemes are not successful and merely further the debts of poor people. This is due

to lack of good practice in providing loans, inappropriate identification of clients and the dire business environment. In Cambodia, law enforcement and legal systems are not effective and efficient. Land and real estate have been frequently used as loan collateral. In that sense, securing property rights of informal enterprises is another aspect of enhancing better opportunity for them to access finance.

The microfinance system in Cambodia still faces many constraints. Real properties of clients have been often assessed at low values due to high risks in enforcing loan collections because of ineffective legal systems. As a result, clients could only access a limited amount of credit. Guaranteed Funds, which secures loans, needs to be established to widen opportunities of microfinance clients to access better terms on their loans.

All these seem to be different from the understanding among international and national communities, organisations and governments that microfinance and microcredit are means of alleviating poverty through the creation of self-employment and income generation, as enshrined in the resolution 53/197 of the General Assembly of the United Nations, which recognises the year 2005 as the International Year of Microcredit.

Figure 2: Workforce in the Informal Economy



Source: Economic Institute of Cambodia (EIC)

Poverty Reduction and the Informal Economy

In Cambodia, the fight against poverty through economic development is problematic. In spite of the relatively strong economic growth of about 6 percent per annum (1994-2003), the poverty rate has risen from 36% to a higher rate ranging from 40 to 45%. Little benefit has trickled down to the rural areas where the vast majority of the population live. This is one of the consequences resulting from the uneven distribution of resources and incomes.

People in the informal economy have worked hard but are still vulnerable, marginalised and poor. This workforce is large and has made significant contributions to the economy. Thus there is a need for appropriate regulations, laws and policies to guide the informal economy. Indeed, the constitutional value of rights of informal participants indicates that they should enjoy an equitable distribution of incomes, assets and resources and benefit from the economic development of the country in the same manner as the rest of people do without any discrimination whatsoever.

Assisting the informal economy may improve income and productivity and the conditions of work for all people, especially the poor and therefore help alleviate poverty in the country through economic development and eventually fulfil the aspirations of alleviating poverty prescribed in the Poverty Reduction Strategy Paper as well as the UN's Millennium Development Goals.

In summary, there is no reason that major stakeholders should disregard the main component of the economy where the majority of the population, particularly the poorest and the most vulnerable groups of people, are working and doing business.

The bottom line is hence to identify an extensive range of those

appropriate policies and initiatives which may benefit and reach those working poor and marginalised groups. The response to this situation is to initiate a diversity of policies aiming to remove all barriers to development of the three essential players in the informal economy – informal enterprises, self-employed and informal workers. These barriers are weak institutions, lack of good governance, poor working conditions, lack of education, lack of health protection and poor organisation.

Concluding Remarks

Considering the critical contribution of the informal economy to GDP and employment, the informal economy needs to be assisted. The growth of informal enterprises leads to employment and income generation and ultimately to economic development. To assist the informal economy, there is a need for appropriate regulations to guide it. For instance, costs and burdensome registration procedures need to be reduced. In addition to legal or regulation constraints, informal participants encounter a variety of social constraints that hinder their developments. Assistance to the informal economy should focus on the removal

of these social problems.

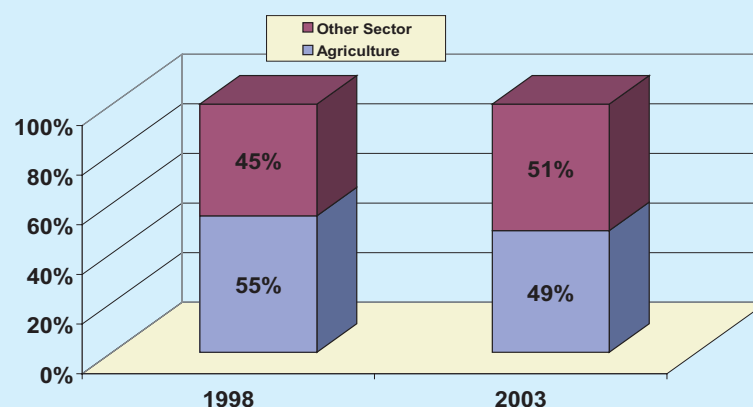
The policies should focus on the removal of impediments of informal participants, which is of vital importance for the informal economy to prosper. In general, informal enterprises need a conducive and enabling policy, legal surroundings that provide a low cost of registration, simplified registration and licensing procedures, incentives for registration, appropriate regulations, better public infrastructures such as roads, water and electricity as well as opportunities to access finance, skills, technology and markets.

There is patchy and uneven distribution of income and resources which indicates that poverty is unlikely to be reduced despite economic growth. Resolute strategies to eradicate poverty are doomed to failure without addressing the problems in the informal economy. The advantage of assisting the informal economy is not only to drive economic growth but also to equitably and impartially distribute resources and incomes to the poor and the very poor.

Nuth Monyrath

This article is compiled from a study report on Literature Review on the Decent Work in the Informal Economy, commissioned by the International Labour Organisation (ILO).

Figure 3: Nominal GDP in the Informal Economy



Source: Economic Institute of Cambodia (EIC)