



There is growing concern over the impact of COVID-19 on the shadow/informal economy. Questions about how lockdown is affecting informal traders, what form of assistance/relief is available for the informal sector, is the shadow economy expected to increase or decrease, and will the informal traders be able to bounce back into business when the economy opens up again are some of the critical questions that need to be interrogated in order for Eswatini to be able to take action to protect all people in their various sectors of the economy.

For the purposes of this piece, the shadow/informal economy is any unregulated part of economic activity that is not part of the official total production of goods and services known as gross domestic product (GDP). The shadow economic activities do not include illegal activities such as growing and selling of marijuana, among other banned activities.

Why should the shadow economy be part of COVID-19 economic recovery dialogues?

The spread of COVID-19 has caused many governments, including the Government of Eswatini (GoE), to close shops, factories, and borders. What we know for certain is that the COVID-19 Regulations

are restricting the movement of people and goods thus negatively affecting the extent to which both formal and informal traders are able to engage business to generate income. Every sector of the economy has been affected in one way or the other by COVID-19 and the economic losses that have followed in the wake of locking down the economy have been likened to the Great Depression. What is uniquely different, and a source of added vulnerability for the informal sector, is that it is not part of the registered/official economy closely monitored by government. Formal businesses benefit from their ability to lobby government for comprehensive relief packages/financial assistance to address the market failures that have been caused by the COVID-19 pandemic.

All around the world, governments are working tirelessly to design COVID-19 economic strategies that can cushion individuals' incomes, rescue or bail out businesses in distress, and are injecting money into the different sectors of the economy to stimulate productive economic activities with hopes to patch the social and economic dent that has been created by the health crisis. By being outside of government's register of official economic activities, the informal sector tends to miss out on these critical economic bailouts and stimulus packages that are meant to prevent massive shutdown or collapse of private sector businesses.



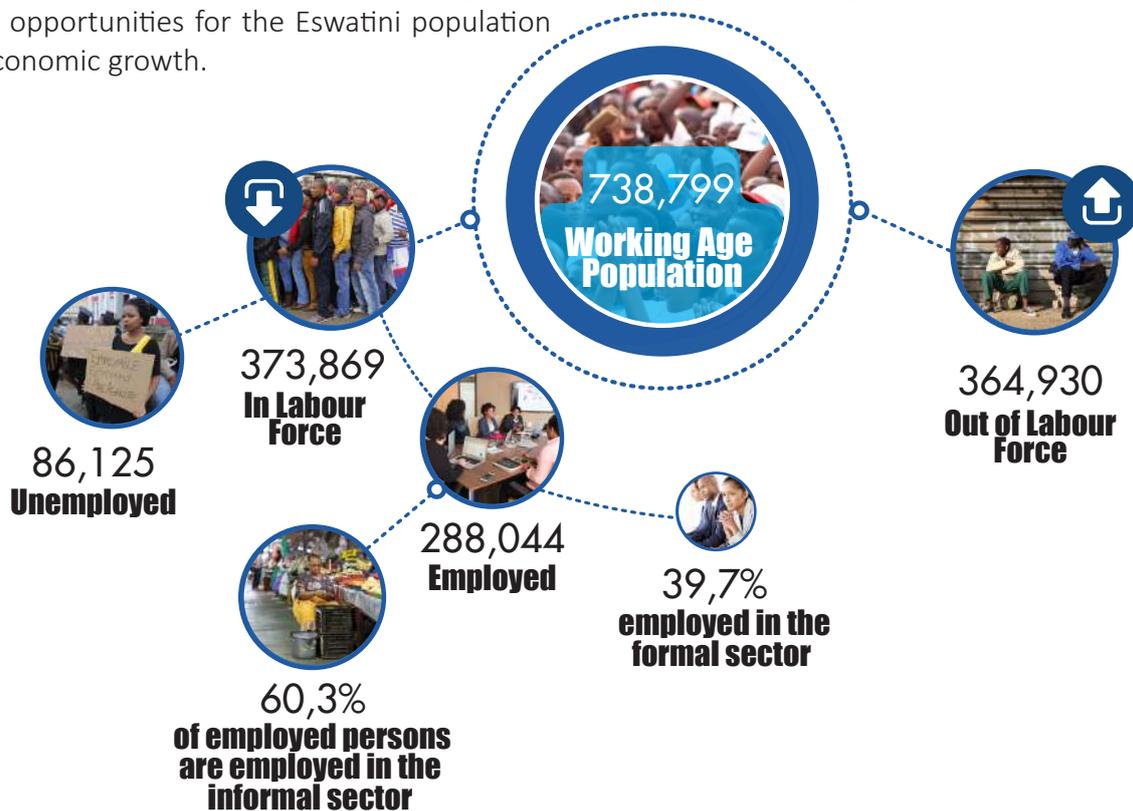
What do we know about the informal economy?

In 2017, the Eswatini Economic Policy Analysis and Research Centre (ESEPARC) with support from the United Nations Development Programme (UNDP) conducted a study on size and drivers of the shadow economy in Eswatini. The study found that the shadow economy in Eswatini was 37.4% of the formal economy or equivalent to 37.4% of Eswatini's GDP in 2016. Put differently, this means an estimated E20.5 billion worth of transactions/trade occurred in the shadow economy in 2016, which was unaccounted for in formal calculations of total production of goods and services in the country.

The motivation for the study was based on the observation that unemployment according to the 2014 Integrated Labour Force Survey (ILFS) was too high. Unemployment in 2014 was estimated at 28.1% with 38% of the formally employed population still dependent on the shadow economy for extra income. Employment figures that followed in the 2016 Labour Force Survey (LFS) indicated an even bigger problem: the formal economy could not provide enough employment opportunities for the Eswatini population to spur economic growth.

In fact, the working age population based on the current LFS consists of 738,799 people of which almost half (49.4% or 364,930 people) are out of the labour force. That is the first problem. Adding to this problem is the fact that in 2016 only 288,044 people (77%) out of the 373,869 that made up the labour force were employed. That means 23% of the people actively looking for work were unemployed. This is the second problem: there is high unemployment yet the labour force is relatively small compared to the total working age population, that should be engaged in productive economic activities.

The third problem is about the informality factor. The problem about the formal economy in Eswatini is that a high number (60.3%) of employed persons are employed in the informal sector compared to just 39.7% employed in the registered/formal economy. Simply put, the informal economy is supporting many more livelihoods because people who would otherwise be unproductive, are able to engage in productive economic activities to generate income.





The power of the informal economy is not to be underestimated. Apart from being a source of livelihoods for both rural and urban unemployed people, it also plays a significant role in stimulating the growth of the micro small and medium enterprises (MSME) sector. Informal economic activities have strong linkages with the MSME sector as a large number of these small businesses directly or indirectly depend on informal value chains for supply of skills and input raw materials. To explain, the FinScope MSME Survey in 2017 reports that out of the 68,536 MSMEs in Eswatini, only 25% are registered in the formal economy. That means a majority (75%) of MSMEs in Eswatini operate in the informal economy. Nevertheless, the MSME sector provides employment to a significant 92,643 people while generating a monthly turnover well over E2.8 billion. It is therefore not surprising that an equivalent of more than a third of Eswatini's economy circulates in the informal sector.

A deeper analysis of the FinScope Survey results reveals that out of the 59,283 people that own MSMEs in the country, 74.7% are individual entrepreneurs (or 25.3% of MSME owners have employees excluding the owner). Furthermore, 74% of the individual entrepreneurs running these MSMEs are women and the majority of the businesses are located in rural areas. In the Eswatini context, an independent entrepreneur is the smallest sized MSME, defined by zero employees except the owner, assets value of less than E50,000 and turnover of less than E60,000 per year. This implies that a good performing independent MSME on average make sales worth E5,000 per month.

In reality, the motivation to start an informal business is mainly driven by unemployment and the need to take care of one's family. Without the informal sector in which the bulk of the MSMEs originate and operate, many people in Eswatini would be jobless, vulnerable, and looking up to government or external aid to make ends meet. Every day that people working in the informal economy are unable to work, they are unable to earn an income to feed their families and take care of other basic livelihood needs. It's a struggle between staying at home to face starvation or going out to sell/trade at the risk of catching COVID-19.

A majority of the women and men working in the informal economy do so not out of choice to deliberately dodge regulation but rather out of necessity to feed their families. For most of them, their informal business is the only source of income and financial independence for their families. In another study with support from the UNDP, ESEPARC profiled 391 women working in the informal sector with an affiliation to the Eswatini Women Economic Empowerment Trust (SWEET). The study found that 94.3% of informal trader women were self-employed with 52.3% operating businesses that were retail oriented such as vending and hawking.

The study also revealed that agro-processing was the most profitable type of business in the informal economy yielding a monthly profit of E1,933.33 on average. The study further determined that 39% of the income generated from informal activities was spent on consumption, while the women also spent 17% of their incomes on their children's education. Moreover, 72.5% of informal traders indicated that they were saving on a monthly basis, supporting that the informal sector contributes to the economic empowerment of the women and their families. Generally, the informal economy is an integral part of the livelihoods of underprivileged women in Eswatini. It plays a significant role in employment creation and income generation for a large proportion of women residing in rural Eswatini and urban surroundings.

While the total money circulating in the informal economy (E20.5 billion) may appear lucrative because of its potential aggregate contribution to GDP, at the individual level for the majority of the people working in this sector, the money is about making ends meet through small incomes that can only sustain marginal rates of savings and investment, and negligible capital accumulation. This makes informal traders particularly vulnerable to economic shocks. If informal traders are overlooked/ignored in COVID-19 crisis-related short-term financial assistance programmes for businesses, it will mean decapitating livelihoods for a significant portion of Eswatini's population.



The informal sector is not completely informal

Just like formal businesses, there is a case to be made for rescuing the informal sector from the worst impacts imposed by the COVID-19 pandemic. Street vendors and market traders involved in the sale of fruits and vegetables as well as clothing are a crucial link to food security and access to basic household necessities in Eswatini's households. They are particularly important for low income households or the poorest segments of the country's population that cannot always afford to buy their household goods from the formal supermarkets and hardware stores. Moreover, the informal economy also supports livelihoods derived in the formal economy. For example, domestic workers are on the frontlines helping to maintain hygiene at home while also providing care for Eswatini's segment of the population that earns decent and stable salaries out of the formal economy.

Over and above being a support system for the middle and high-income groups of the society, informal traders also contribute to the formal value chains within the different sectors of the formal economy. The reason for this is that the informal economy does not occur in a vacuum totally detached from the formal economy.



When people earn an income through informal trade, they still buy food in formal supermarkets, they buy some of their clothes and household goods from the formal retail shops, they too connect to the formal utilities such as water and electricity, and they use formal financial services such as Mobile Money/eMali to receive, send, or save money. The money spent in the informal economy will, one way or the other, make it to the formal economy to circulate and create value.



It is true that if all business activities were to be registered and monitored by government, the value of goods and services produced within the Eswatini economy would be greater than current GDP estimates. Eswatini would be richer. At the same time, there would be a larger tax base from which government could generate national revenue for social and economic development. The motivation for complete registration and monitoring of business activities is not just a one directional benefit only for government: it also benefits entrepreneurs and businesses. With more businesses operating in the open under the same set of government regulations, it creates more opportunities for private sector growth where both individuals and businesses can compete and seize opportunities in a fair footing for income generation and wealth creation.



What is the conversation that needs to be had?

There tends to be mixed views on the contribution of the shadow economy on the overall national economy. Those against it view the shadow economy as a hindrance to the mainstream economy because it encourages tax evasion, which leads to a reduction in the country's tax base. When the shadow economy grows much faster than the formal economy, it imposes serious penalties on government's ability to generate income to drive development and can be a significant contributing factor to the country's deficits and slow economic growth.

On the other hand, advocates of the shadow economy argue that it is the cornerstone of the MSME sector as it promotes entrepreneurship and income generation. They see the shadow economy as an enabling engine for employment creation. In this view, the shadow economy is an alternative economic pathway to support basic livelihoods, especially among the poor and marginalised. At a national policy level, Eswatini adopted the 2030 Agenda for Sustainable Development Goals (SDGs) in 2015, which committed the country to create opportunities for all emaswati to access decent work in order to end hunger and poverty as well as ensure that all emaswati enjoy a good standard of living.

Whether one is against or a fervent supporter of the shadow economy, and noting that it is impossible to completely get rid of it, Eswatini has to formulate its own policy direction to channel shadow economic activities into the formal economy. However, the idea of a completely formal economy where all business activities/transactions are registered is a utopian and impractical dream. There simply isn't enough government time and resources to monitor all economic activities. Nevertheless, the country has to invest resources to understand the dynamics of the shadow economy and its contribution to the formal economy. Research on the shadow economy can generate new knowledge on how to nurture and grow MSMEs out of the shadow economy. The goal is to assist govern-

ment in creating a conducive business environment that incentivises a larger share of businesses to operate in the formal economy.

The Sustainable Development Goals are about creating social and economic opportunities for all people to make sure that no-one is left behind. The ideas discussed in this piece are not meant to create an argument for or against the shadow economy. The point is, the country has to position itself to effectively deal with this unprecedented health and economic crisis that is affecting all spheres of our lives. Hence, Eswatini needs to make sure that it addresses the issue in a holistic and inclusive manner in order to protect and empower all emaswati in their different corners of the economy.

Still, COVID-19 has some key lessons to teach. The country needs everyone to engage in productive economic activities under the control of the GoE so that Eswatini's tax base can increase to finance the necessary development programmes as outlined in the National Development Strategy (NDS). By fast-tracking the implementation of the NDS, Eswatini would also be fast-tracking the implementation of the SDGs. Everyone has a role to play to achieve these development milestones. When a crisis like COVID-19 hits, Government is expected to provide assistance to all people and businesses, regardless of their level of participation in the formal economy.





The Key Message

Inevitably, people trading in the informal sector will be one of the hardest hit groups due to COVID-19. Given that businesses in the informal sector tend to be unregistered, many of them do not pay tax and so are generally not eligible for structured economic rescue packages/bail-outs. Despite the fact that informal sector traders operate in the “shadows”, a substantial number of these businesses have affiliations to registered and well-governed associations (for example Coalition of Informal Economy Associations of Eswatini, Eswatini Women Economic Empowerment Trust, just to name a few) under different product lines, such as domestic workers, garment workers, street vendors, waste pickers, amongst others.

Policy makers need to ensure that they make operating in the formal economy an attractive business strategy for every entrepreneur. This will ensure that even though some businesses may continue to start in the informal sector, they will in turn deliberately endeavour to grow out of it and graduate into the formal economy to expand the country’s private sector.

Ignoring the informal economy would not be a wise economic policy option for the Kingdom of Eswatini. The informal sector acts as a crucial component of the formal economy, providing income for farmers, food for low-income earners, and cheaper resources for urban dwellers. In fact, ignoring the informal sector will simply grow it even bigger particularly now during and after the COVID-19 pandemic when many people would have lost their jobs or had their livelihoods severed because of the slowdown in economic activities.



Eswatini can leverage the COVID-19 pandemic to entice the informal sector to register all of its activities with formal structures/institutions in the economy so that it can be developed further until a larger share of the activities can be absorbed into the formal economy. Moving towards formality calls for a change in the administration and delivery of services within the country, making access to services more pronounced, and easing the burden on businesses to operate in the formal economy. A more digital environment should provide low cost mobile services and platforms that informal traders may use to effectively participate in the formal economy.

Overall, moving towards formality calls for Government to reduce the over-regulation of some services, reduce inefficiencies/delayed decision making, and bureaucratic processes. Establishing MSME friendly regulations and simple government processes that improve the ease of doing business can be a good start to induce a mass business migration from the informal to the formal sector. It is true that not everyone will see benefit in being formal. The key in addressing this issue is an appreciation that formalisation does not have to be a one-size-fits-all approach: formalisation means different things to different groups. For instance, to street vendors, formalisation involves secure access to public space, licenses to sell, and infrastructure.

To the least, Eswatini needs to understand the informal sector and create the incentives for people to register their informal sector activities so that they get the required support to grow into fully-fledged formal businesses. There is a case for providing COVID-19 economic assistance to the informal sector and priority should be given to people who want to resuscitate their businesses and just need seed capital to do so. These traders should be able to prove to some reasonable level that they were engaged in business before COVID-19 and demonstrate the losses incurred due to the slowdown in the economy and restrictions imposed by the COVID-19 Regulations. Creating an economy with a higher proportion of formal enterprises and jobs is important to long-term social and economic welfare, which in turn can accelerate the implementation of the SDGs and win the fight against poverty.