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Informal Economy and Social Vulnerability in Kyrgyzstan and Tajikistan

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Introduction

Kyrgyzstan, like many CIS countries in the transition period, experienced almost complete collapse of state industries followed by the immediate increase in unemployment. Twenty years after the USSR break-down, the situation in our country has hardly improved. Corrupt privatization of state enterprises in the context of constantly changing bureaucracies led to a situation when new owners of the state factories and mines were selling expensive machinery for the price of metal and disassembling the factory buildings to sell as bricks for a short-term gain. As a result, half a century industrialization effort of the former Soviet regime was brought to nothing within few years after independence.

Both previous leaderships (of Akaev and Bakiev) did very little for recovering the industrial power of the country or for establishing new enterprises. Families of both presidents were blamed for stealing Kyrgyzstan's wealth and monopolizing the financial and service sectors. State policy through all these years was oriented towards exporting the labor force to Russia and Kazakhstan, as the easiest way out of hard economic crisis. Almost a million of Kyrgyz labor migrants were and are regularly sending money to provide a survival minimum for their families. Yet, the government did very little for setting up a proper climate for investing these remittances into small-scale businesses. High taxes, bureaucratic obstacles and corruption until today make it very hard to establish and legalize any kind of business in Kyrgyzstan.

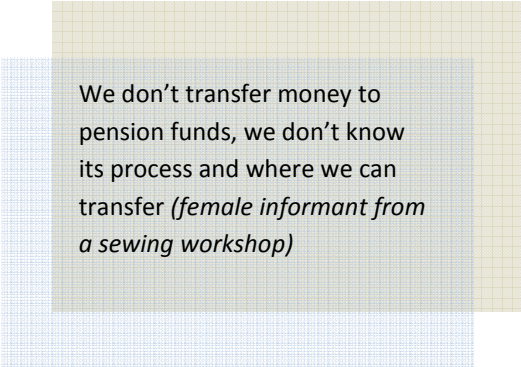
In such context, it was only understandable that informal and semi-formal economy

took the place of the former official employment in all traditional sectors: production, mining, transport, construction, services, trade and agriculture. People developed many ways of avoiding paying taxes and hiding their revenues and tax officers and other bureaucrats developed many ways of taking bribes for "closing their eyes" on what's going on. As a result, today in Kyrgyzstan, it is easy to propose that informal sector plays the major role in the country's economy and in the life of its residents.

The scale of informal economy

The research conducted by the UNDP¹ shows that informal economy in 2004 accounted for 53% of GDP. In such spheres of economy like trade and auto-repair services the share of informal work reaches 75.5%. On the level of the country, the share of undisclosed sales across sectors is 39.8% and undisclosed profits – 40.1%.

31.8% of all individual entrepreneurs and 28.4% of small businesses are not registered. Those businesses, which are officially registered have greater share of their work undisclosed – this part of their work contributes to 46.3% of the GDP! The share of illegal employment is 28.1% and for those who are legally employed 41.8% of their salary is undisclosed¹.



We don't transfer money to pension funds, we don't know its process and where we can transfer (*female informant from a sewing workshop*)

¹ *The Analysis of Nature and Scale of Shadow Economy in the Kyrgyz Republic*, report by UNDP and ОО «Инвестиционный круглый стол», published in Akipress, 2006, #2, under the "Сколько богатств спрятано в Кыргызстане?" title

Factors contributing to informal economy

Same report² shows that the degree of informality is not homogenous. It varies by a) the region (Issyk-kul and Bishkek have the highest figures); b) sector of economy (high for trade, restoration/auto-repair, real estate and construction); c) type of enterprise (the less public is the normative structure of the organization – the higher are the figures of undisclosed profits); and d) e size of organization (the smaller – the more informal).

Luneva³ suggests that it is the tax collectors who play the major role in the forcing the economy underground. For example, they ignore the Governmental decree about transferring sewing factories to the patent system, which would make life of entrepreneurs much easier. They insist on using traditional taxation system based on accounting, which when translated into local reality means giving bribes to them.

Yakishik⁴ in his study argues that “tax system is one large field which encourages increasing unregistered economic activities” (p.10). He also names following major obstacles on the way of legalization of informal economy: high taxes, ineffective social security system, frequent interventions of the government, bureaucratic permission and licensing policies, old administration body, high corruption, monopolistic economy, unreliable public economy, poor legal base

² *ibid*

³ Luneva, G. *He выйдем из подполья, не дают*, Слово Кыргызстана, 2006, №90, 25 авг

⁴ Yakishik, H., *Observation of unregistered economy in Kyrgyzstan and its effects*, Реформа, 2006, № 2

for controlling economic activities, insufficient capital for investment, inflexible labor market, and unfair business ethics.

The UNDP study placed the following actors as the main creators of problems for the informal businesses in the following order of significance: 1) tax collectors, 2) social fund, 3) sanitary-epidemic station, 3) fire-safety inspectors, 4) customs, 5) department of architecture and planning and 6) police. Bribery is a traditional and easiest way of solving the problem. For example, for tax collectors the average size of bribes is 7-15 thousand som. It is interesting to note that the size of bribes for unregistered enterprises is half as big as that of the registered. This is one of the

important findings that prove the main conclusion of the UNDP study: informal economy is an important mechanism of survival for businesses because it creates better conditions for development than the existing official legal business environment⁵.

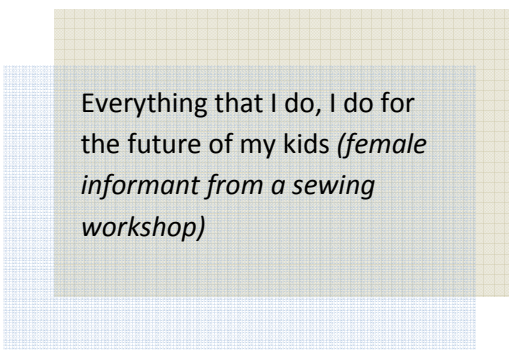
Internal migration is also a reason of the growth of the informal sector, especially in the capital Bishkek, where the number of migrants makes more than a quarter of all city population⁶. Hardly any of the new comers to the city register there and therefore legally they cannot be employed. Yet the majority comes for that purpose and the majority does work. Like in many regions around the world – the rural-urban migration creates cheap labor supply and feeds the informal sector of economy.

⁵ *The Analysis of Nature and Scale of Shadow Economy in the Kyrgyz Republic*, report by UNDP and ОО «Инвестиционный круглый стол», published in Akipress, 2006, #2, under the “Сколько богатств спрятано в Кыргызстане?” title

⁶ Nasritdinov, E., *Discrimination of internal migrants in Bishkek*, SRC AUCA, 2008

Positive and negative effects of informal economy

Besides being the survival mechanism for almost half of the population, informal economy keeps the economy floating. For example, Biyalinov⁷ suggests that it is the dollar cash circling in the informal sector that prevents inflation and keeps Kyrgyz som stable in spite of the very weak economy and incredibly low official income figures. The situation is such that the National Bank must even buy “extra” dollars to avoid overusing the som. Only in 2007 it bought \$8 mln. Where does this money come from? It is money generated in the informal sector and money that comes as remittances from the Kyrgyz labor migrants. The government of Kyrgyzstan is very proud of “its” achievements and takes all the credits for keeping economy stable, while in reality all credit must go to the informal sector, and it is the government who should take responsibility for corruption and for creating obstacles for proper economic development of our country.



Everything that I do, I do for the future of my kids (*female informant from a sewing workshop*)

But from whatever angle one looks at it, at the end of the day, large informal economy has more negative effects. National budget does not receive taxes to be used for public expenditures, such as schools, hospitals, infrastructure, etc. Informal economy breeds further corruption on all layers of governmental bureaucracy. It results in the exploitation of workers employed in the informal sector, who have to work daily 12-hour shifts for a minimal pay, without proper working conditions and any social security benefits. It makes the overall climate unfavorable to investments. Informal economy reduces the efficiency of

⁷ Biyalinov, A., *Тень на плетень*, Вечерний Бишкек, 2007, №66, 9 апр

production and possibility of applying latest technologies. The government loses its trust on behalf of its citizens and as a result, the political stability of the country is threatened because it involves both corrupted governmental and criminal structures on all levels: from large industrial enterprises to small firms and individual entrepreneurs forming the main “army” of informal sector. Yakishik⁸ and other authors even propose that one of the main reasons of the March revolution in 2005 was the particular situation in the informal sector, where, on one hand, the “family” of Akaev tried to monopolize all economic activities in the country, while on the other hand, the number of people involved in the informal sector and their unhappiness with the existing system of exploitation reached critical mass and levels. Similarly, we could speculate that the same reasons were present in the April revolution of 2010. Criminal structures supported by Bakiev’s family were “cutting off the oxygen” for so many businesses by imposing their own “taxes” on entrepreneurship.

Attempts at dealing with informal economy

Considering all the negativity associated with informal economy, was there any attempt on behalf of the Kyrgyz Government to deal with the issues of informal economy? Unfortunately, after almost twenty years of independence, the attempts were insignificant and unfruitful.

Soltoeva⁹ refers the first shot at measuring the informal sector to the study made by

⁸ Yakishik, H., *Observation of unregistered economy in Kyrgyzstan and its effects*, Реформа, 2006, № 2

⁹ Soltoeva, A., *В тени +40*, Слово Кыргызстанаб 2003, 3 апр.

the National Statistics Committee only in 1999 – eight years after independence. The next attempt was made by the Interdepartmental Committee organized by the Ministry of Finances of the Kyrgyz Republic. The committee studied nearly a hundred research projects done in the West and came to conclusion that the first main reason of growing informal economy is high taxes. It was pointed that increasing taxes only for 1% in the developed countries leads to the growth of the informal sector for 1.4%. (This point is argued against by Orozbekov¹⁰). Committee proposed two recommendations: 1) to introduce the unified social security tax which works on regressive scale (the more salary is paid, the smaller are taxes) and 2) to reduce/cancel the main turnover taxes. The second main reason was seen in the highly bureaucratic and complex procedure of permitting and licensing. The recommendation was made to simplify it. Some other recommendations included simplifying the mechanisms regulating labor contracts, making legal system work, creating freedom for private business initiatives and guaranteeing property rights.

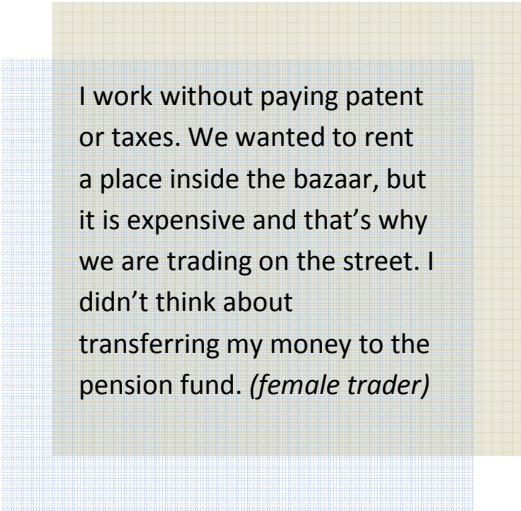
These recommendations were not really taken on board until 2007 when the Prime Minister Almazbek Atambaev signed the governmental decree introducing the *Program of legalization of shadow economy in Kyrgyz Republic for 2007-2010*¹¹. The program was designed by the Ministry of Finances on the basis of the recommendations from other ministries

¹⁰ Orozbekov, S., *Налого ли причина экономического кризиса*, Akipress, 2006, #2

¹¹ *Program of legalization of shadow economy in Kyrgyz Republic for 2007-2010*, Банковский Вестник Кыргызской Республики, 2007, №8

and governmental bodies and of the previously mentioned UNDP report. A special Committee was established to oversee the implementation of this program. In addition, special expert groups were to be engaged in the design of specific recommendations and legal acts to be reviewed by the committee.

Six main directions of work were identified in the decree: 1) national information campaign, 2) simplification of tax procedures and reducing the tax burden, 3) improvements in business environment and in the system of registration and licensing, 4) optimization of labor contracts, 5) review of the patent taxation system, and 6) reduction of smuggling and fight with corruption.



I work without paying patent or taxes. We wanted to rent a place inside the bazaar, but it is expensive and that's why we are trading on the street. I didn't think about transferring my money to the pension fund. (*female trader*)

Three years have passed since the decree was introduced. What has been achieved and how successful it was? Luneva¹² is very critical. She refers to Gani Abdrasilova, adviser to the Minister of economic development, who says that the main targets were not achieved due to

some objective and subjective reasons, which include poor discipline in the ministries, lack of priority given to the Program, frequent changes in the executive administration, unprofessionalism, and short period for implementation. Both governmental offices and representatives of the private sector can be blamed.

Yet she refers to several good initiatives, which were implemented. These include passing several important legislative acts, opening of consulting centers, introducing patent taxation system for sewing factories, etc.

¹² Luneva, G., *Вышли не все из подполья*, Слово Кыргызстана, 2008, №11

Obviously, with only one (in two decades) poorly implemented program for dealing with issues of informal economy we cannot expect these problems to be solved and therefore the situation with the informal sector today is just as difficult as it was ten years ago. As it has been discussed above, the problems are many, but there is one specific issue, which is of the most important interest to this research – it is the question of future social security of people working in the informal sector.

Research aim and focus

This study intends to analyze the effect of informal economy on the pension fund of people involved in the informal sector. Retirement pensions of Kyrgyzstan citizens today depend on their employment period and on taxes they paid towards their pension fund. Only those who are officially employed make these payments, while those who are in the informal sector do not. This puts at risk their future retirement age. While at the moment, it still might be not too noticeable because people working in this sector are still young - ten, twenty and thirty years from now this will become a serious problem for Kyrgyzstan when large share of its elderly citizens will be left with minimal retirement pensions.

This research aims to establish the longevity of work in informal sector and analyze what factors are associated with being informal, not paying taxes and not making payments towards pension.

Research Methodology

From the introduction we have developed some sense of what informal economy involves. However before proceeding with research methods and results we need to clarify what this term means for this research.

Defining the informal economy

The definitions of 'informal' economy are quite many. Carson¹³ associates it with such words like "cash, black, unofficial, informal, irregular, unrecorded, moonlight, twilight, gray, subterranean, marginal, dual, second, parallel and illegal." Kuznetsova¹⁴ defines it as "the economic activity which is not regulated by statistics". She defines three types of informal economy: 1) concealed or underestimated legal activity, 2) unofficial but legal activity (family gathering to do some work) and 3) legal activity where people are engaged illegally (for example without license).

Similarly, Glinkina¹⁵ defines three approaches to informal economy: juridical (legal versus illegal), economic (paying/not paying taxes) and statistical (registered/not registered).

I came to Bishkek in 2000 and I still have no home. I haven't registered anywhere. Here at the market, I pay only for the place, but not taxes. As for the pension, we have the proverb: "In 50 years, even the land will be different". I don't think we have a stable system, I don't believe in our government, because the laws can be changed anytime. We have no choice.
(female trader)

¹³ Carson, C. *The Underground Economy: An Introduction, Survey of Current Business*, 1984, May p. 21

¹⁴ Kuznetsova, T. *The non-formal economy in Russia*, Social Sciences, 07-01-98, last assessed at <http://dlib.eastview.com/browse/doc/2197458> 11.09.10

¹⁵ Glinkina, S., *The Shadow Economy: Myths and Reality*

Light¹⁶ emphasizes the institutional and political context: “People without regular jobs and outside legitimate businesses develop an “informal economy”, constrained by a restrictive institutional environment, forged by those in power”. Kyrgyzstan is a perfect example of the role that the state and its politics played in the growth of informal sector through all kinds of bureaucratic obstacles, high taxes and lack of incentives. Light also defines as informal the activities which help “to get something more from the mainstream system, like the widespread use of informal payments or favors in poorly run or poorly funded health care systems”. According to Light, informal actors are people, who bend, manipulate, ignore or violate the laws.

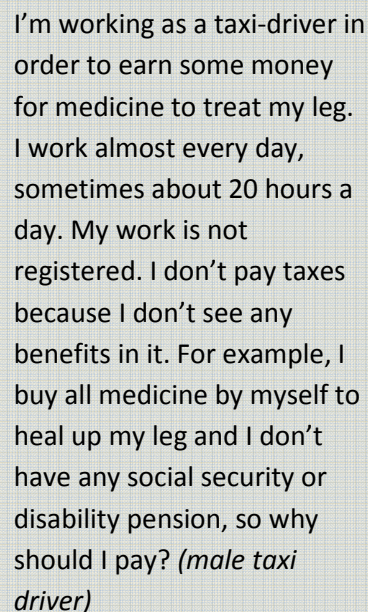
Many authors find the Post-Soviet transitional economies as perfect environments for the growth of informal sector. Light¹⁷ considers collapse and reconstitution of formal socialist economies as main causes of *informalization*. Latov and Kovalev¹⁸ suggest that informal economy multiplies in the “border zones” between centralized and decentralized economies, when the old systems of control are weak.

For this research, we identify informal economy as all activities aimed at generating some kind of income, which are either 1) not registered at all, 2) registered,

but do not pay taxes or pay reduced amounts through hiding some of the profit, 3) registered, but downsize the salaries for their employees.

Methods

The research was conducted in two countries: Kyrgyzstan and Tajikistan with the equal distribution of survey sample. One important point has to be made here: as readers might have noticed, all previous discussion was based mostly around the situation with informal economy in Kyrgyzstan, not in Tajikistan. This is because the authors live and therefore are well familiar with the situation in this country. Access to the information in Tajikistan was more complicated. However, there was a chance to request our colleagues from Tajikistan to conduct the survey in Dushanbe and Khujant for the purpose of comparison. Therefore, Kyrgyzstan remains the main focus of this research, while Tajikistan is used only in the analysis and comparison of the survey results.



I'm working as a taxi-driver in order to earn some money for medicine to treat my leg. I work almost every day, sometimes about 20 hours a day. My work is not registered. I don't pay taxes because I don't see any benefits in it. For example, I buy all medicine by myself to heal up my leg and I don't have any social security or disability pension, so why should I pay? (*male taxi driver*)

To achieve these aims the researchers employed mostly quantitative methods with a questionnaire survey as the major research instrument. The survey sample consisted of 600 people in two cities in Kyrgyzstan: 150 in Bishkek in the North and 150 in Osh in the South and in two cities in Tajikistan: 150 in Dushanbe and 150 in Khujant. Sample was assembled evenly across five major sectors of economy: trade, construction, transport, services and

¹⁶ Light, D., *From Migrant Enclaves to Mainstream: Reconceptualizing Informal Economic Behavior*, Theory and Society, Vol. 33, No. 6 (Dec., 2004), pp. 705-737

¹⁷ *Ibid.*

¹⁸ Latov and Kovalev, Теневая Экономика

industry. SPSS software was used to code and analyze the results of the survey.

Researchers also had a qualitative component in the form of 20 life stories from respondents from different sectors. The purpose of collecting stories was to establish a more insightful perspective on the research questions.

We believe that research results would be essential in the formulation of policies and programs at national level taking into account behavior of citizens, their motivations and their everyday social reality.

The SPSS analysis was done in four main steps summarized in the following chapters of the report: life stories; identifying the scale and nature of the problem; descriptive analysis of the overall sample of respondents and revealing factors contributing to the informality and social vulnerability; and comparison of data from two countries and four cities. But before we listen to what numbers have to say to us, let's listen to some real voices of people who shared with researchers their life stories. These stories often provide many more insights on the essence of informal sector than abstract figures.

Living informally

Gul'barchyn, 27 years old, divorced, 2 children, works at the sewing factory

I am from Jalal-Abad. I got married when I was 19, but after the birth of our second child we got divorced. In order to not to be a burden on my parents I came to Bishkek six years ago looking for a job. Now, I work in the sewing workshop, I earn 2500-3000 som in a week, but it is not enough. For example, I paid 2000 som for my son's school, he is in the first grade, and sometimes I have to borrow money to live. My younger daughter lives with my parents in Jalal-Abad. She is four years old and she has problems with her stomach. It is a very bad decease, so I send money to them.

We cannot live on my 3000 som pension. A bag of flour costs 1500 som, benzene is expensive. Except for this I'm satisfied with my life. My son studies at the university; my daughter is in Russia; my youngest daughter studies at school. I think, that I'll be working as a taxi-driver for a long period of time, because there are not many opportunities when you are 45, are there? *(male taxi driver)*

Once I heard about the work record book (трудова́я книжка) and I would love to pay taxes. But I found out that it would cost me 700-800 per month. Everything that I do, I do for the future of my kids. My parents have 9 children and my mother is going to be a pensioner soon. In the future I would like to work in the sewing sphere for 5-6 years, and later open a small shop or something like this. I am trying to get a residential registry here in Bishkek, and in the future I want

to live here. I am even planning to open a bank account. I have already learned that I need 5000 som for that and after that I will get the interest or add more.

Aikygul', 50 years old, married, 5 children, works as a trader in the market

I am from Issyk-Kul and I came to Bishkek looking for a job. I have worked as a nurse in a hospital for 7-8 years. Also I have worked as a tailor. But after the 1990s I started working in the market. Here we pay

170 som for the place every day. We pay this amount even if we do not work that day.

At the hospital without paying taxes we have no benefits. So I have paid a lot of money for the public hospital. The private ones are not the solution because they require even more money. We have no health benefits in public hospitals, not even for pensioners. We don't pay any taxes as our activity is counted as private. I went to local administration to get information on our situation as we would like to get pension when the time comes. But I didn't get a satisfactory answer. I agree to pay any part of my income for pension. I don't know whom we are paying, because we pay money for the place, but I have no idea where this money goes. Right now the main purpose in my life is to provide my children with a better future, to educate them, so that they have a more decent life, not like ours.

Kairinisa, 42 years old, married, 5 children, works as a trader

I was born in 1968 in Suluktu; I studied at the school #3 named after Makarenko and then I graduated from the pedagogic institute. After graduation I have worked in the kindergarten for 5 years for 180 rubles. In 1991s our kolkhoz collapsed and our kindergarten stopped working. I started selling tobacco. Since then I am working as a seller. My husband worked as a driver, but now he has no job. Life is hard, we think only about our children. I think we have lived enough, but they should live a better life. I would like to change my work place, but where will I go? Plants and factories do not work; even if they worked, my health conditions wouldn't allow me work there. School? Who will accept me? I don't know how many years I will work here. But anyways, I have no faith in our government. I am even afraid of giving this kind of interview. We pay taxes for our land for

four people, but I don't believe that this money goes to the right place. I don't know what is going to happen with my pension fund and our future is ambiguous.

Saparbek, 37 years old, married, three children, works as a taxi driver

I came from Kara-Kul. I rent a flat in Bishkek. Previously, I worked at the Toktogul hydropower station as a welder for about nine years. I've got specialized secondary education. At the beginning of the perestroika we didn't have enough money and that's why I quit my job and left to Russia, where I also worked as a welder for 3 years. My family was here in Bishkek and children were going to school, that's why I came back to Kyrgyzstan. We couldn't live and work in Kara-Kul anymore, because the town is not developing; it stays the same. After arriving I bought a car and started working as a taxi-driver. I have been working for four years now. I buy patent, when I can afford it. I buy patents seasonally, mainly in august and in New Year. In other periods I don't buy it because I don't have money. Right now I've got a patent and I can show it to you.

My wife works at a sewing workshop. She also works without a patent. We pay for patents but our work record books are at home. Then what do we need a patent for? If we work we need to pay taxes to the government so that we can receive pensions, otherwise we won't get anything. I think that when I am old I will just go back to live in Kara-Kul, buy some cattle and work as a shepherd.

Sergei, 49 years old, married, one son, works in construction

I have secondary education. After school I lived with my parents. It was the time of the Soviet Union. I began my carrier as a construction worker then. Many of my

friends were constructors so I started helping them. While helping, I learnt and practiced a lot. That was my work and certainly, part of my salary was transferred to the pension fund. After the break-up of the USSR I just continued working in construction, but now informally. Since then I work illegally. I don't transfer money to the pension fund. It is more convenient as I don't have to give away my money for taxes and registration. I work alone. I have many clients now in Bishkek who call me for a work and for me there is simply no need to be registered. I don't worry about my future pension because I already worked enough during the times of the USSR and I also rely on my growing son to help me and my wife in the old age. On the whole, there is not much for me to worry about.

Each of these stories is unique and at the same time there are so many things which are common. Perhaps, one common thing is pessimism and lack of trust to the government and strong degree of uncertainty in the future. At the same time, there is a will and energy and almost universal striving to create a better life for the new generation of children. Will it be possible? Well, let's see what numbers have to say about the situation in the informal sector.

Identifying the scale and nature of the problem

First of all – what is the problem? To begin, the research tried to establish the degrees of formality/informality and future social vulnerability. Three factors were chosen as indicators: 1) registration of work, 2) payment of taxes, and 3) payments towards the social fund.

Registration

In regards to the first question - registration: the number of those who

registered their work was equal to those who did not – 47% (6% were not sure). 76% of those registered did this at the Taxation Department and 17% (traders) in the market. As we can see from the Figure 1 the main reasons for not registering are economical: not seeing benefit in it (lack of economic motivation) and not having money to do it (lack of economic means).

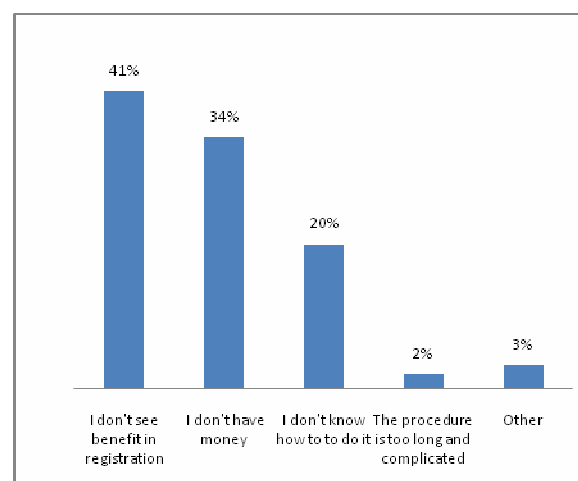


Figure 1 Reasons for not registering

Other reasons could be found in answers like: “I am just a student”; “If there is work we work, if there is no work we don't”; “We don't have a place, why should we register?”; or “I work seasonally”.

At the same time, among those who register the main motivator was “because it is required” (for 59%). 10% register to avoid problems, 11% to have social benefits, 6% are forced by tax inspectors, and 7% have some personal motivations, like “In order to be respected”.

The most frequent mode of registration was through the patent system (58%), which required buying patent every month (59%).

Payment of taxes

The second question (Do you pay taxes?) reveals very similar situation: half of respondents (50%) pay and half (50%) don't. Figure 2 shows that the most common

reasons for not paying taxes are attitudinal and economic. Other reasons include statements like: “The government doesn’t give us anything, why should we?”; “There are no proper conditions for work, why should we pay?”; “I am a refugee”; “What for? I can live without it”, or “There is not enough work”.

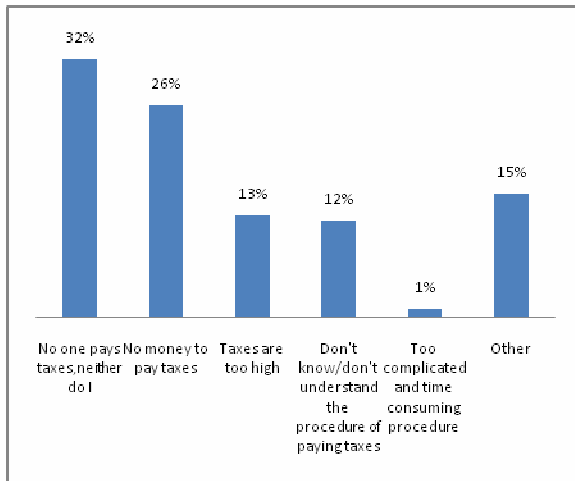


Figure 2 Reasons for not paying taxes

The majority uses the patent system (see above). For those who pay income tax the average percent of declared income is only 30%. This confirms findings of the UNDP study.

Payments to the Social Fund

Finally, the third question was about making payments to the Social Fund. This is money, which currently is transferred towards the future pensions of workers. The overall figure is very far from optimistic – 69% of respondents do not make these payments. Considering that almost a half of all who work in the country are engaged in the informal sector, this figure is quite alarming – it tells that nearly 35% of working population (and this does not include housewives and elderly, who do not work) will be left with minimal pensions when they retire unless there are radical changes in the legislation. Another negative outcome is that with such a large share of population not making payments to the

Social Fund – the budget of this Ministry is in a strong shortage today, which means that the position of today’s pensioners and all other people receiving social benefits is affected.

Why do people not make these payments? Figure 3 shows that in addition to the economic reason many people simply do not know how to do it. The legislation has been changing so frequently and the whole system is radically different from what used to be during the Soviet times. Many people simply do not know how it all works. That suggests the need for at least a proper information campaign.

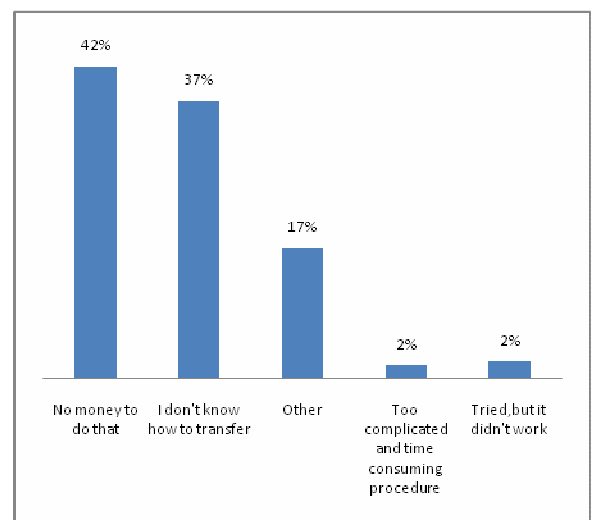


Figure 3 Reasons for not making payments towards pension

To understand the seriousness of the problem we also need to establish the longevity of work in the informal sector and plans for future. First of all, on daily level the informal work is quite difficult. Respondents work in average 9.25 hours every day and 6.25 days a week and for 96% of respondents this job is their main source of income. Analysis shows that the quarter of respondents worked for more than 10 years and another quarter 5-10 years. When asked about their future plans 55% were not sure, but one quarter was going to continue their work for longer than 10 years. These figures are all strong indicators of the stability of informal sector. They also

tell about the long-term effects on and potential threats to the social vulnerability. To understand what factors cause informality and vulnerability will be the task of the next section.

The informality/vulnerability portrait

An important question of this research is what contributes to the informality and social vulnerability of workers. The analysis revealed seven factors. These are: gender, ethnicity, education, residential status, work experience, employment status and sector of work. It is important for the research to analyze how these factors are related to the formality of work and social vulnerability of workers.

Gender

Almost universally across both countries and four cities there were more men engaged in informal work than women (65% versus 35%). Gender was strongly correlated with the sectors: construction and transport were dominated by men, while sewing industry and trade by women. Only Services were more or less gender neutral (Figure 4).

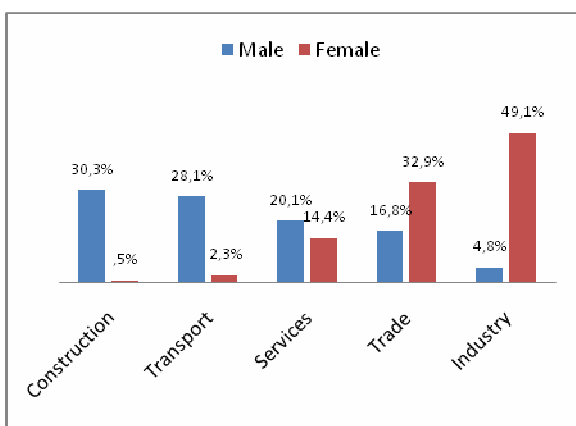


Figure 4 Sectors by gender

When we run correlation between gender and formality of work we see that for two

countries taken together women are more formal: they are better registered and more of them pay taxes. However, they are more vulnerable because they make smaller payments towards their pension fund. But when we make a break-down by countries and cities, we can see that Kyrgyz women in Bishkek are not only more vulnerable, but also less formal.

Ethnicity

There were four main ethnic groups of respondents Tajiks (47%), Kyrgyz (29%), Uzbeks (17%) and Russians (8%). Ethnically, the respondents' sample in Kyrgyzstan was significantly more diverse than in Tajikistan, where it was almost completely homogeneously Tajik. When we compare the formality of work by ethnicity we reveal that Uzbeks are the most formal, while Kyrgyz are the least formal (Figure 5).

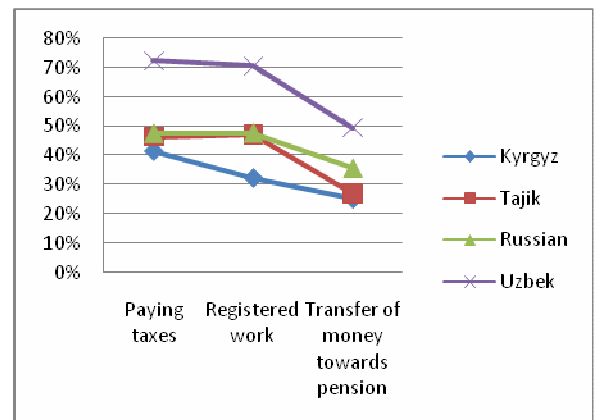


Figure 5 Formality and vulnerability of work by ethnicity

The majority of respondents were married (69%) and living with family (70%), parents (17%) or relatives (5%). One of the early research hypotheses was about the importance of family and relative networks in the life of informal workers. These figures support it.

Education

Contrary to many other regional contexts, the educational levels of people working in the informal sector in the CIS countries are quite high. For example this study shows that 21% had higher education, 14% specialized secondary and 50% completed secondary education. High educational standards were left to Kyrgyzstan and Tajikistan as a valuable Soviet heritage, which unfortunately is not used in its full potential. Education seems to be a very important factor that contributes to the formality of work and social protection of workers. Figure 6 shows this strong correlation.

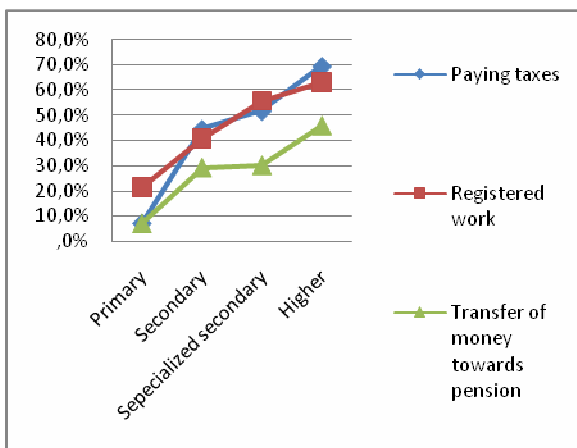


Figure 6 Formality and vulnerability of work by education

Residential status

Like many classical urban studies show, rural-urban migration becomes a continuous source of new labor force in the cities. Kyrgyzstan and Tajikistan, traditionally being the two poorest CIS republics, both experienced high rates of internal migration, especially to the capitals Bishkek and Dushanbe because of high rates of poverty in their rural areas and in the small former industrial towns. Millions of Kyrgyz and Tajiks then decide to migrate in the search of better income opportunities. In Kyrgyzstan, from those who migrate, about a half leaves the country, while another half migrates internally. The ineffectiveness of the old residential registration system, which is still

significantly based on the Soviet notion of *propiska* becomes the reason of why only 0.5% of those who come to Bishkek for work, register their presence in the city¹⁹. This system of registration contradicts many aspects of constitutional freedoms of Kyrgyzstan and among them – the freedom to work. Currently, a person cannot get officially employed in Bishkek if he/she doesn't have residential registration. Only this simple fact suggests that almost all migrants (by our estimates – 300-400,000) who come to the city get engaged in the informal sector. This research confirms this hypothesis: Figure 7 shows a strong correlation between the residential status and formality of work and social vulnerability.

The situation of migrants is vulnerable not only in their future, but also in the present. Without registry in the city migrants also have limited access to medical treatment, education for their children and other basic social services.

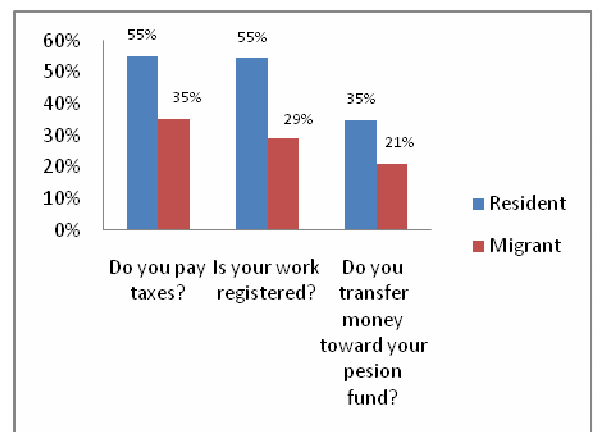


Figure 7 Formality and vulnerability by residential status

¹⁹ This figure comes from two sources: the Bishkek City Mayor's Office figure of 220,000 migrants living in the city in 2009 and Ministry of Internal Affairs' figure of 2,000 migrants who registered their presence in the same year. Considering that registration is valid for only half a year, we come with a figure of less than 0.5%.

Sectors

Similarly to the UNDP study this research reveals different levels of formality for different sectors of informal economy. However, the comparison of two studies is contradictory. In the UNDP report, trade and services were the least formal, while in our study they are the most formal (Figure 8). This perhaps can be explained by either strong formalization processes that took place since 2004 in the trade and services sectors or by the differences in methodologies. The least formal are construction and transport (taxi).

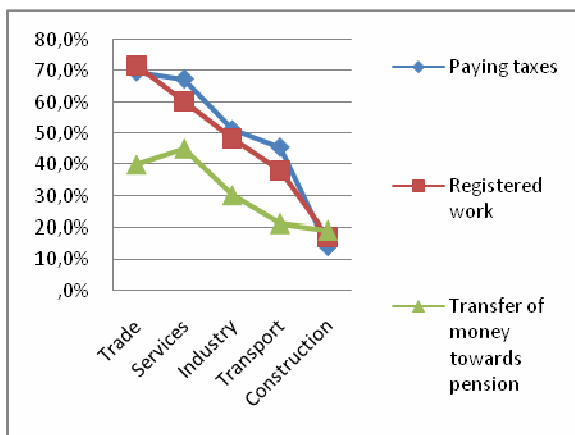


Figure 8 Formality and vulnerability by sectors

Employment status

One other very significant correlation is between the employment status and formality of work. In the Figure 9 we can see the 2-3 times difference between the formality of employers and employees while the self-employed are in the middle. This figure partly explains how things often work here in the informal sector. Those who employ others have higher visibility and must register their businesses and pay taxes, but they don't make contracts with their employees. Explanations can be following: the minimum wage of 6,000 som is too high, the work contracts are too rigid and complicated, employees do not have residential registry (therefore cannot get officially employed) and finally, employees

themselves do not want to pay taxes from their salaries, which are already too small.

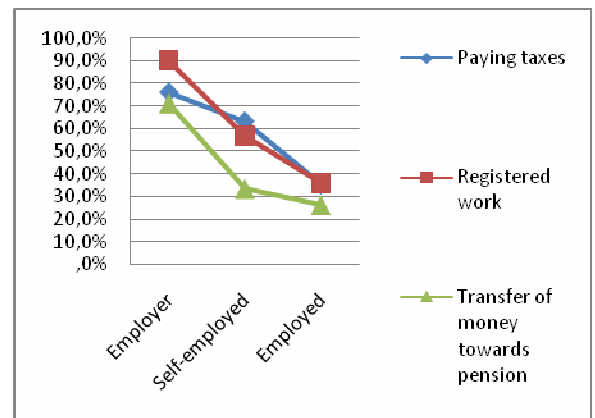


Figure 9 Formality by employment status

Work experience

Finally, last factor that contributes to the informality of work is the work experience itself. Research shows that the longer people work, the less informal they become (Figure 10).

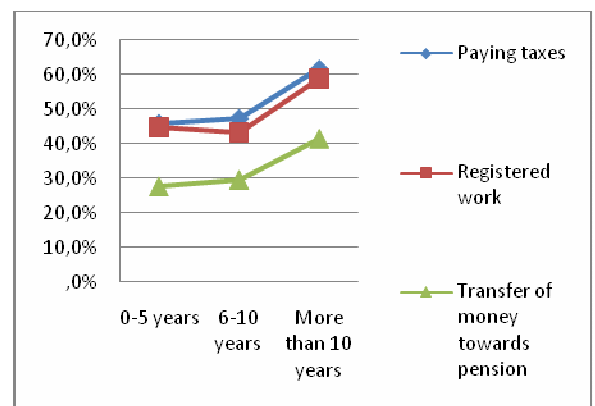


Figure 10 Formality and vulnerability by work experience

Seven correlations analyzed in this section allow us to draw the social portrait of the least formal and most socially vulnerable informal worker. This would be a Kyrgyz woman with primary or secondary education who came to Bishkek and who does not have residential registry in the city and works as an employee in a sewing factory for the less than 5 years. In a fairly similar position would be Kyrgyz and Tajik men

with similar characteristics who work in construction or transport.

Regional peculiarities

In the last section of this report it is interesting to make some comparisons between two countries and four cities.

Differences between Kyrgyzstan and Tajikistan

Kyrgyzstan and Tajikistan are two countries, which are similar in many economic, cultural and geographic characteristics. These were two poorest republics during the days of the Soviet Union and industries in both countries were heavily subsidized by the center in Moscow. These subsidies stopped immediately after the break-up of the Soviet Union. Mountains in both of the countries leave very little land for agriculture. Both are landlocked and far away from any ports and both had quite limited oil, coal and gas resources. In both countries levels of formal official employment are low, while informal economy and external labor migration are high.

This study shows that rates of work registration are very similar too: Kyrgyzstan – 48% and Tajikistan 47%. Payment of taxes is slightly higher in Kyrgyzstan – 54% than in Tajikistan – 46%. As for the payments towards pension fund Kyrgyzstan is also higher – 35% versus 27% in Tajikistan.

Some other differences include higher shares of respondents who were self-employed in Tajikistan – 54% versus 37% in Kyrgyzstan. The number of migrants in the informal sector is higher in Kyrgyzstan – 35% versus only 20% in Tajikistan. One other very interesting difference is between the formality/vulnerability factors by gender in two countries: women in Tajikistan

seem to be much more formal: 70% have registered their work there versus 44% of women in Kyrgyzstan; 69% pay taxes (in Kyrgyzstan – 51%); twice as many women in Tajikistan (35%) make payments towards pension fund than in Kyrgyzstan (17%). Finally, there is more team work in Kyrgyzstan (61%) than in Tajikistan (44%).

Differences between cities

In Kyrgyzstan – Bishkek and Osh are two major cities. They are situated in two economically and culturally different regions: North and South and there is a big difference in ethnic composition: there are more Uzbeks in Osh and there are more Russians in Bishkek. The results of analysis can be said to reflect some of these geographical, cultural and economic differences in the ways they are imprinted in the structure and functioning of the informal economy.

Bishkek is the capital and it is much more active economically. Therefore, there are many more migrants here than in Osh (45% vs. 25%). Ethnically, the respondents' sample in Osh consisted of Uzbeks for 62%. Perhaps, because of the combination of these two factors (having residential registry and Uzbek ethnicity) the case of Osh is significantly more formal and less vulnerable. For example, 62% of respondents in Osh registered their work versus only 34% in Bishkek; similarly 62% pay taxes in Osh versus 45% in Bishkek; and finally, 43% make transfers towards pension in Osh versus 27% in Bishkek.

Very similar differences are found in two cities in Tajikistan: Dushanbe and Khujand. In Dushanbe, the capital, the economy is less formal: work registration is 40% vs. 53% in Khujand; payment of taxes is 39% vs. 52% in Khujand; and payment towards pension is 24% vs. 30% in Khujand. One aspect that contributes to this formality is the work experience – in Khujand (like in Osh) work experience is longer: 32% work longer than 10 years vs. 23% in Dushanbe. Also, twice as many people in

Khujand think that they will be working in their informal sphere for longer than 10 years (33% vs. 15% in Dushanbe).

From this comparison we can propose that there is more informality and vulnerability in the capitals/larger cities than in smaller ones.

Conclusions and recommendations

Perhaps, the most important conclusion is that informal sector is very prominent in Kyrgyzstan and Tajikistan and it has strong links with the current and future social security of people who are engaged in it. The involvement is long-term and at the moment, there is no sign of change on the horizon. The government in Kyrgyzstan has only started addressing the issue, but the latest political turmoil has probably took everything back to where it all started. The current system of registration and taxation bred on complex bureaucracy and corruption will not be easy to change. That is why people are quite pessimistic; they don't have trust in the government, in the system and they prefer to rely completely on themselves. This is another reason why informal economy is flourishing.

However, it doesn't mean that the civil society should also sit and wait. It is exactly because the situation is so difficult that there is a need for strong advocacy campaign both for improving the business environment to bring the informal economy to legalization and to address the issues of those who are most affected now and whose future social security is so vulnerable. The study revealed several major factors that contribute to the informality and social vulnerability. It recommends that these factors have to be taken into consideration in designing the solutions.

One other consideration is important. The comparison of informal sectors in two countries and in four cities has shown that informal economy is both typical and unique at the same time. Therefore, even if there are some

common – country-wide programs and strategies – they have to be adapted to specific local geographic, economic, cultural and political contexts.

Sharing the degree of pessimism with many respondents, but also learning from their eagerness to take matters into their own hands and do something about their lives, authors of the study propose active engagement with all involved parties in attempt to improve the situation.