

Land of Smiles and Shadows

Thailand's shadow economy – the non-regulated, non-taxed part of its national economy – is among the largest in the world. Accounting for roughly half of Thailand's official GDP over the last two decades, and largely responsible for the country's remarkably low unemployment rate, the shadow economy appears to be not so much a concern for Thailand as it does a necessity

By **Jennifer Khoo**



Thailand's ubiquitous tuk tuks

All photos courtesy of Pixabay

Roadside noodle stalls littered with fold-out tables and low plastic stools. Street vendors selling packets of fresh cut fruit. Pushy tuk-tuk drivers; thronging night markets; mobile cocktail carts that disappear when the sun rises. From women touting massage services on the beach, to more aggressive propositions amid smoky nightclubs; the list goes on.

Anyone who has visited Bangkok – or anywhere else in Thailand for that matter – will be familiar with many of the scenes just described. What is less often acknowledged, is that these same scenes which give the Land of Smiles its personality, are just some of which comprise the beating heart of its shadow economy.

Dark phenomenon

Shadow economies, also known as underground, black, or informal economies, are broadly defined by scholars as “those economic activities and the income derived from them that circumvent or otherwise avoid government regulation, taxation, or observation.” They refer to, in other words, the legal and illegal activities that bring in revenue “off the books.”

While this phenomenon appears in every country to varying degrees, it is hugely apparent in Thailand. Shadow market activities – both legitimate and illegitimate – provide a steady source of employment and income for many Thais.

This largely explains the country’s unusual and consistently low unemployment rate of less than one percent – even lower than wealthy neighboring Singapore – despite the estimated ten percent of its population who live below the poverty line. In Thailand, street vendors, tuk-tuk drivers and other informal workers of that nature are largely counted as employed under government statistics.

So great is the impact of shadow activity on Thailand’s economy that it accounts for over half of the nation’s GDP. According to research published by Friedrich Schneider, economics professor at the Johannes Kepler University in Linz, Austria, income from Thailand’s shadow economy has accounted for as much as between 40 and 70 percent of the country’s overall GDP over the last two decades.

The topic is a sensitive one in Thailand; deeply pervasive and yet rarely discussed. But the following questions persist:

What are some of the driving forces and enablers behind Thailand’s shadow economy? What are the implications for the country and the wider business community?

Labor economics

According to a 2012 report by Bangkok-based firm,

Noviscape Consulting Group (NCG), the business landscape in Thailand is dominated by small- and medium-sized enterprises (SMEs), which – generally speaking – don’t generate enough high-income employment opportunities to attract sufficient legal workers to the formal sector.

The Thai government responded in 2013 by implementing a daily minimum wage policy of 300 Baht



Street food markets coming alive at night

(approximately US\$9), which unsurprisingly didn’t have the intended effect. Instead, the announcement was met with protests and criticism by SMEs in many private sectors who argued that they, due to their smaller sizes, weren’t generating enough revenue to bear these additional employment costs.

Such conditions have provided fertile ground for shadow activity to flourish, inevitably attracting illegal immigrants from around the region who enter Thailand looking for work. Barred from official employment, willing to work for much less, and exempt from social security, these workers are funneled straight into informal employment.

The demand-supply cycle of cheap – albeit illegal – labor perpetuates Thailand’s shadow market.



Beach massage huts



Vendors selling fruits at Bangkok's floating market



The middle class

Possibly the biggest misconception about work in the shadow sector is that all participants have been forced into it by desperate or unfortunate circumstances. While a large number certainly are, many actively choose informal work for a variety of reasons, including the possibility of higher earnings than in formal employment, and the independence of being self-employed.

In fact, an increasing number of people from Thailand's middle class are entering the fray. They, like the working class, have become disenchanted by the government's continuous promises to improve pension

benefit schemes and wage requirements, and are shunning formal employment in favor of starting businesses informally of their own.

Today, informal work in Thailand is not just reserved for the poor. According to NCG, the business of street vending began attracting workers from the country's educated middle class who were laid-off from their jobs during the 1997 financial crisis.

NCG estimates that 1.1 million Thai employees were laid off between 1997 and 2001, and at the same time, many small investors transformed themselves into self-employed entrepreneurs.

Former stockbroker and multi-millionaire Sirivat Voravetvuthikun did just that by becoming a sandwich vendor on the streets of Bangkok after losing his fortune to the stock market crash. His business flourished, and he slowly began to recover his losses, paving the way for other would-be entrepreneurs from Thailand's educated middle class.

Many indeed followed suit, marking the starting point of middle class street vending as an occupation.

Government response

Since shadow activity takes place "off the books," naturally one would wonder how such a large percentage of the national population are able to dodge tax payments (among other legal obligations), and how the government has responded to this endemic.

Ian Khoo, Director at Bangkok-based legal and business advisory services provider, ClasG, believes that rampant shadow activity in Thailand is a result of the government's inconsistent approach to law enforcement.

"Like most developing countries, tax collection [in Thailand] is not as efficient as compared to other developed parts of the world," he says. "Thailand's legal system is based on civil law which mainly relies on the interpretation of Codal provisions that may be widely drafted to allow for flexibility.

"So authorities here probably have more discretion when it comes to interpreting and applying the law, and as a result, fiscal enforcement may not be consistent across the board," he adds.

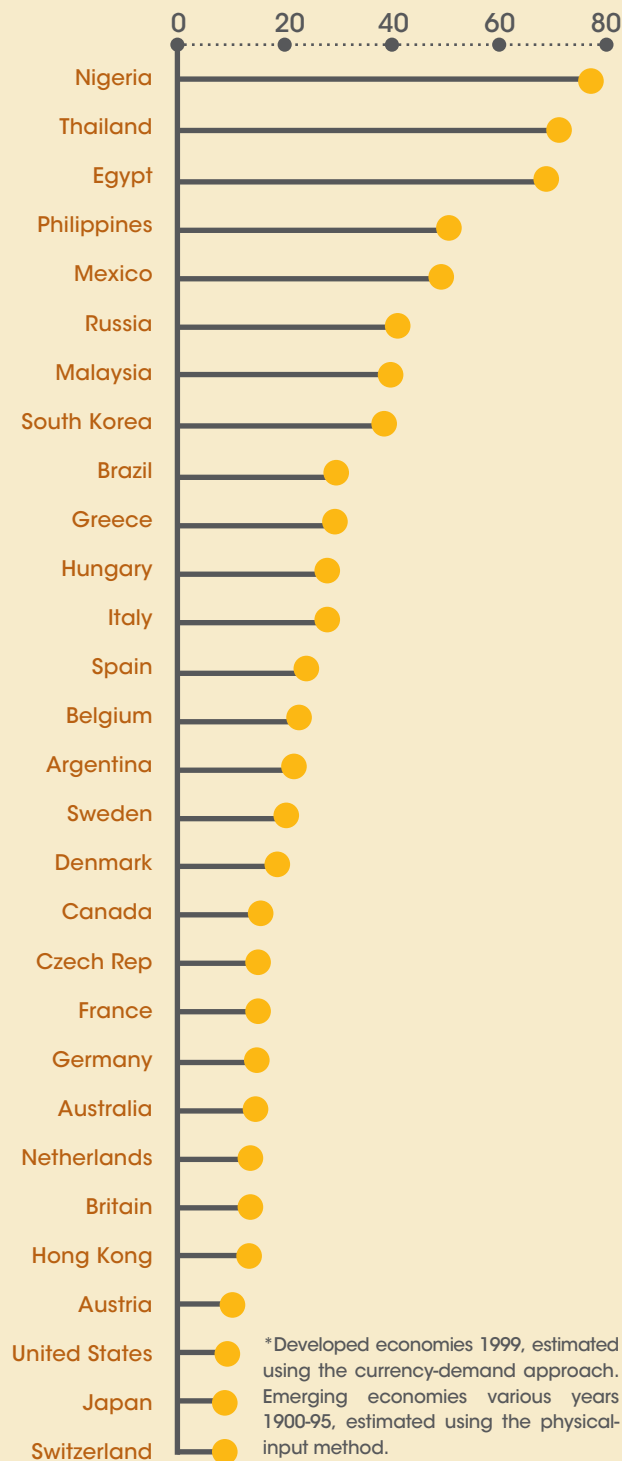
Implications for Thailand

Many argue that Thailand's shadow sector has not only given many underprivileged Thais a chance at a better quality of life, but also encourages entrepreneurship and fosters a healthy sense of competition among the local business community.

In theory, as more competition is introduced into the shadow market, government standardization should see overall business standards rise, such as food hygiene and quality within the street vending industry.

Economic penumbra

Shadow economy as % of official GDP*



Source: The Economist

Many hope that progress at grassroots level will have a ripple effect across other layers of the economy, which will help to drive Thailand forward.

Practically speaking however, players in the shadow market still have a long way to go before they become key economic drivers that induce government participation.

"Businesses in the shadow economy do not have access to credit from banks, and usually have no choice but to resort to loan sharks for financing. So it's very hard to grow and build scale within the shadow economy. What you are left with is a business landscape that is littered with 'mom and pop' style players, compared with so called 'first world' economies in which the business landscape is much more institutionalized," says Khoo.

Whatever opinions people may have about the shadow sector, the reality is that it has provided a crutch for Thailand, without which the country wouldn't be where it is today, economically and characteristically.

It is blindingly apparent that many businesses operating within the shadow economy are helping to support the "official" economy. "Take tourism as an example, a huge industry here, which is being supported by a range of businesses from famous street food vendors to various recreational outlets," says Khoo.

Implications for foreign businesses

For foreign businesses looking to enter the official Thai market, Khoo reassures that the country's shadow economy is of little consequence.

"In general, the shadow economy should not have too much of an impact on foreign businesses and investors looking to legally do business in Thailand. The Foreign Business Act of 1999 regulates all foreign business activity in Thailand, listing out which business activities allow for foreign majority participation," he points out.

"What you find is that many of the business activities found within the shadow economy do not allow for foreign majority participation anyway. Thus, any impact between overlap of shadow and formal business activities will be largely felt by local Thai businesses," he adds.

Although the shadow economy has played an enormous role in shaping Thailand's current economic landscape, no one can say for sure how long it will continue to hold a key place in the country's future.

But uncertainty following the Thai king's recent passing, piled heavily on top of the nation's deeply divided political atmosphere, will likely continue to generate negative consequences for the country's overall economic performance; in which case it will need all the help it can get. For now, at least, it pays to do business in the shadows.

