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CHARACTERISTICS OF HOUSEHOLD BUSINESSES AND THE INFORMAL SECTOR

While Chapter 2 used the 2014 Labour Force Survey, this chapter focuses on the prominent characteristics of household businesses using the 2014/15 HB&IS survey. It compares informal HBs with formal ones and questions what formality means in the context of Vietnam.

The HB sector includes formal and informal businesses. This divide, which is commonly used in labour statistics and for policy purposes, has to be explained. An understanding of the relationship between the informal sector and the state can contribute to shedding light on how the informal sector can be managed, promoted or monitored by a government. The informal sector, in comparison with the formal system, is seemingly

of a business. We look at the type of premises and occupancy status. Section 2 shows that there are important differences between formal and informal HBs in terms of conditions for operating a business. Section 3 explores the linkages between the informal sector and the state which can be partly captured through the lens of formalization with administrative registers as well as the attitude of the owners of HBs towards registration, taxation and informal payment for administrative costs. It highlights the blocking factors towards greater formalization, which are mostly a lack of incentive to formalize and poor knowledge of the regulations. In addition, the link of formal HBs with the state remains weak as formal HBs often do not have the expected attributes of formality such as tax and social security registration or bookkeeping.

1.

THE PREVALENCE OF SMALL-SIZE HOUSEHOLD BUSINESSES

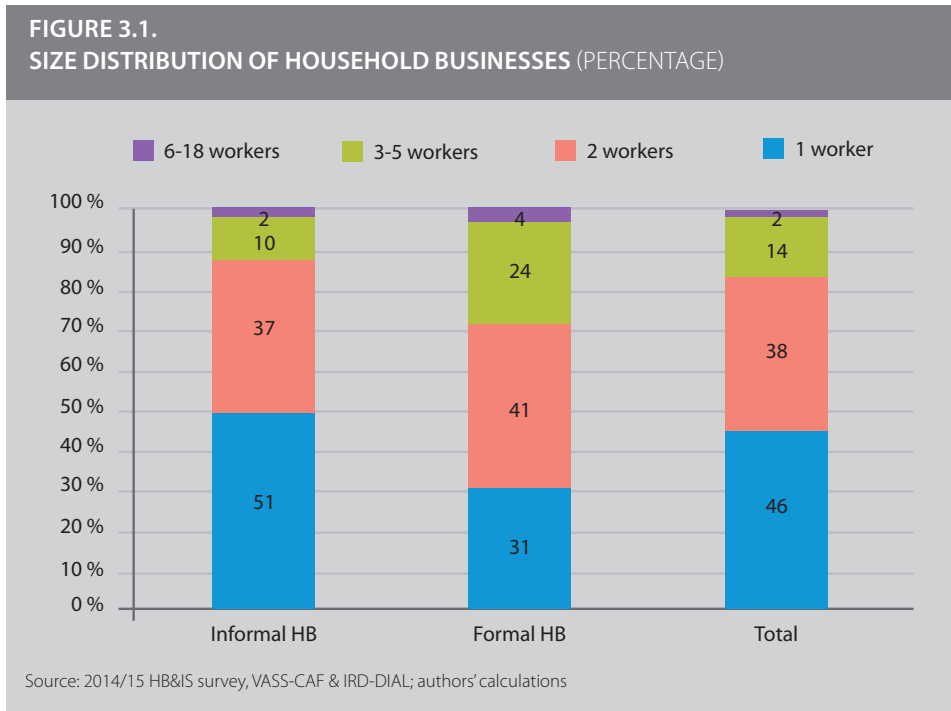
This section illustrates the distribution of formal and informal businesses by size using the number of workers. The size of establishments was not asked in the recent LFSs, so the information provided by the HB&IS survey is particularly relevant.

1.1. Distribution of HBs by size

The size of a business or scale of operation is a dominant criterion for defining the informal sector in the literature. It is most often measured by the number of people working in a unit. The small size of businesses in the informal sector has been mentioned in the literature since the first studies on this sector (ILO, 1972). Although there are some variations across countries, many papers mention the strong association between the scale of operation and formality, which indicates that the size (number of employees) is positively correlated to the possibility of formality (Maloney, 2004; La Porta and Shleifer, 2008; Pratap and Quintin, 2006; De Paula and Scheinkman, 2011). This is also the case in Vietnam (see section 4 below).

According to the HB&IS survey, informal HBs have an average of 1.8 people per establishment, including the owner of the business. One out of two informal businesses is comprised of just one person, and more than 40 per cent are comprised of the owner and his or her spouse and/or members of the family. This proportion has, however, sharply decreased compared to 2007 (65 per cent in the 2007 LFS). Only 8.5 per cent of the informal businesses have hired workers. Businesses with 3-5 workers and those with more than 6 workers account for 10 per cent and 2 per cent respectively (see Figure 3.1).

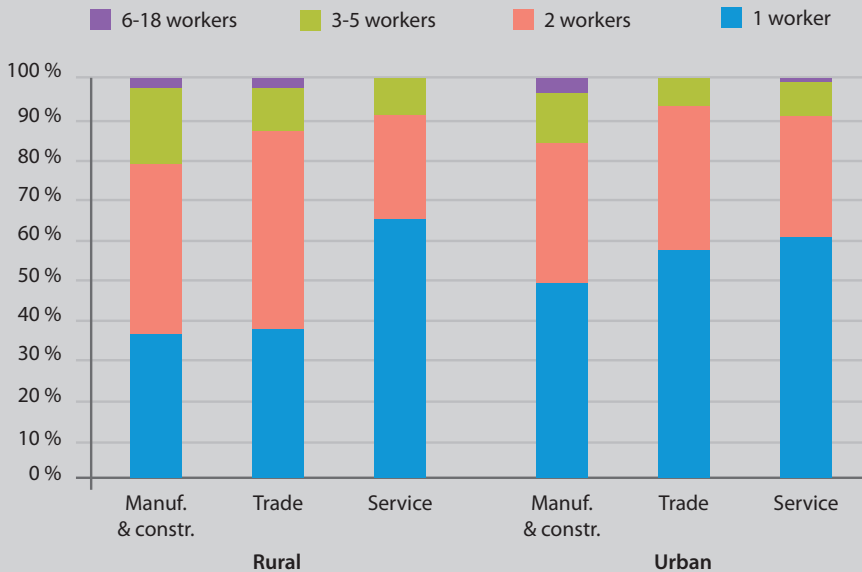
Formal HBs are larger than informal ones, but the scale of operation is still very small. The average size of a formal business is 2.3 workers. Nearly one third (31 per cent) are comprised of the owner only, and half are comprised of the owner, his or her spouse and members of the family. Although the number of formal HBs that hire workers is significantly higher than the number of informal HBs that do so, only one out of four formal businesses has at least one wage worker.¹ Formal businesses with 3-5 workers constitute 24 per cent of all formal HBs. This proportion is more than two times higher than that observed in the informal sector.



A breakdown of the size distribution of informal HBs by industry presents interesting findings (see Figure 3.2). Informal HBs in the service sector tend to be the smallest as nearly two thirds of the service businesses have only one worker, who is also the owner. This is mainly because the informal HBs in the service sector are food and beverage and land transport (motorbike taxis) services, and they do not require many workers. In contrast, the share of informal HBs with at least three workers in the manufacturing and construction sectors is the highest compared to those in trade and service sectors (19 per cent vs. 10 per cent and 9 per cent respectively).

1. 31 per cent of the wage workers at formal HBs are family members.

FIGURE 3.2.
DISTRIBUTION OF INFORMAL HBS BY MAIN ECONOMIC SECTOR AND SIZE
IN RURAL AND URBAN AREAS



Source: 2014/15 HB&IS survey, VASS-CAF & IRD-DIAL; authors' calculations

In addition, the proportion of informal HBs with more than two workers in rural areas is higher than in urban areas (see Table 3.1). This phenomenon can be explained in several ways. It can be due to underemployment in rural areas: Family members of the owners working in the agriculture sector have vacant hours to take part in activities pertaining to the family business during off-season months (e.g. after the winter and spring rice crops). Another reason is that there are fewer opportunities for them to do other non-farm jobs. Moreover, many of the informal self-employed have activities which are typical of an urban environment, e.g. motorbike taxi driver, fruit and vegetable street vendor and running a street restaurant. Hence, informal HBs in rural areas are less likely to provide services (34 per cent of the rural informal HBs are in the service sector compared to 49 per cent in urban areas). However, service activities in the informal HB sectors are those with the highest proportion of self-employed people (see Figure 3.2). Informal HBs in rural areas are more represented in the manufacturing and construction sectors (32 per cent of the rural informal HBs compared to 24 per cent of the urban informal HBs), which is where the proportion of informal HBs with more than two workers is the highest. Finally, incentives to get a business license may be weaker in rural areas, so large HBs which would be formal in urban areas are

informal in rural areas. This is the case in particular for construction businesses, which usually have more than two workers and are never registered in rural areas.

This explains why the average size of informal HBs is higher in rural areas than in urban areas (1.9 workers in rural areas vs. 1.7 in urban areas) while the size is nearly the same in both areas for formal HBs (2.5 workers). In particular, there are more informal HBs that have only one worker (self-employed) in urban areas than there are in rural areas (58 per cent and 47 per cent respectively) (see Table 3.1). The size gap between urban and rural areas is significantly wider for the trade sector (see Figure 3.2). In this sector, 37 per cent of the rural informal HBs are constituted of the owner only, compared to 58 per cent in urban areas. Again, this can be explained by the higher proportion of street vendors in urban areas. Although smaller, the same gap between urban and rural areas in the size of the informal HBs was observed in the manufacturing and construction sectors.

TABLE 3.1.
SIZE DISTRIBUTION OF HOUSEHOLD BUSINESSES BY AREA (PERCENTAGE)

	Rural			Urban		
	Informal	Formal	Total	Informal	Formal	Total
1 worker	46.5	32.8	43.7	57.2	30.5	48.3
2 workers	40.2	39.9	40.1	32.9	42.1	36
3-5 workers	11.4	23.8	13.9	8.6	23.5	13.5
6-18 workers	1.9	3.6	2.2	1.3	3.9	2.2
Total	100	100	100	100	100	100

Source: 2014/15 HB&IS survey, VASS-CAF & IRD-DIAL; authors' calculations

1.2. Evolution of the structure of employment

The average number of workers has increased slightly since 2007, at least in Hanoi when compared with the results of the survey in Hanoi and Ho Chi Minh City (Cling *et al.*, 2010). This is due to the fact that in both Hanoi and Ho Chi Minh City the share of those working alone has declined, especially in Hanoi: While 73 per cent of the informal HBs had one self-employed person and no other workers, in 2014 this was the case for only 53 per cent of the informal HBs in Hanoi. The number of HBs with at least one wage worker has increased in Hanoi but not in Ho Chi Minh City, and in both cities this number remains low for informal HBs: Nine out of ten have no hired (wage) workers. The relative decline of self-employed workers is mostly compensated by the increase in HBs where the spouse and other members of the family are involved (see Table 3.2).

2.

PRECARIOUS BUSINESS OPERATING CONDITIONS

For HBs, especially informal ones, one of the main difficulties in operating a business is not having an adequate premises. This can prevent them from growing in size and restrict their capacity to hire more workers (Cling *et al.*, 2010). Indeed, the type of premises is an important determinant of the stability or, on the contrary, of the precariousness of a business. Without an adequate premises, operating conditions in the informal sector are more likely to be insecure and poor. Although only one out of six business owners, formal and informal, reported difficulties related to having a premises (see Chapter 11), those who operate in improvised or non-permanent premises are more likely to be in a precarious situation.

2.1. Lack of a professional premises

Table 3.3 compares the types of premises in which informal and formal household businesses conduct activities in different economic sectors. Nearly a third of the informal HBs and 5 per cent of the formal HBs do not operate in a fixed premises.² They operate their businesses on streets like vendors, in improvised locations outdoors and in markets, and from vehicles or at their customers' homes.

Nearly half of the household businesses operate out of the owner's home. This type of premises is popular among household businesses because the proprietors can avoid spending money on rent or buying a premises. The owners can therefore spend their capital on other assets and equipment. Many of those working at home (half of the informal and two thirds of the formal HBs) have a dedicated space in their home in which to operate their business.

Moreover, working at home allows reconciling family and professional activities. As explicated in Chapter 11, this motivation is important when setting up an own-account business instead of working as a wage worker. This motivation is more important for those who work at home: One out of five heads of HBs who work at home, which is nearly twice as many as those who not work at home, mentioned that as the main reason why they decided to work on their own account. This motivation is

2. In principle, only businesses with a fixed premises can register their business. However, there are a few formal HBs which do not have a fixed premises, e.g. in the transportation sector. In these cases, the owners stated that their personal home is their professional premises even though they do not work there.

more important for women. However, working at home may impede the growth of a business, especially in urban areas, where the density of the population is high and the ability to expand the home is limited and costly.

More than half of the formal HBs, but only 25 per cent of the informal HBs, have a professional premises such as a permanent premises in a market, workshop, shop, restaurant or hotel. The high proportion of dedicated premises for operating a business in the formal HB sector illustrates that formal HBs tend to be more professional and stable, resulting in greater business prospects and more opportunities to expand their operation by increasing their business size. It should also be noted that it is more difficult to avoid registering a business when one has a professional premises.

Precarious operating conditions for informal businesses involved in service and trade activities are remarkably widespread, and many of them (46 per cent and 30 per cent respectively) do not have a premises. Informal HBs in the manufacturing and construction sectors constitute a smaller share. Only 15 per cent of them have makeshift set-ups,

the periphery of cities, because of the need for space to conduct these activities and because there is less pressure on land in rural areas. On the other hand, formal HBs in the service sector are less likely to have a professional premises in rural areas. This suggests that HBs with high potential in the service sector are less developed in rural areas than in cities. For instance, activities in the telecommunication, human health and accommodation sectors are more frequently conducted in urban areas, while food and beverage services are more common in rural areas.³ Lastly, the proportion of informal HBs with a professional premises in the trade sector is lower in rural areas. This is because the retail sale of food at home is more common in rural areas and because markets are more organized in cities (permanent posts in a market are more common).

2.2. Space constraints

While having a fixed premises is a guaranty of stability and better working conditions, the space dedicated to an activity is a good indicator of the potential for growth of the business and of the working conditions as well. As expected, the space dedicated to the activity is much smaller among informal HBs than among formal HBs: On average, the surface dedicated for activities at informal HBs is 16 square meters, while the figure for formal HBs is more than 30 square meters. These are median figures. The amount of space is higher in rural areas, reflecting weaker pressure on land. Lastly, having a professional premises does not necessarily mean having more space in which to operate a business than at home.

TABLE 3.4.
MEDIAN SURFACE OF PREMISES BY TYPE AND AREA (m²)

	Informal HBs		Formal HBs	
	Rural	Urban	Rural	Urban
Home	20	12	35	32
Professional premises	20	16	40	25
Percentage with more than 100 m ²	10.0	3.1	28.7	21.1

Source: 2014/15 HB&IS survey, VASS-CAF & IRD-DIAL; authors' calculations

3. Figures are not reported here but are available on request.

Nevertheless, some HBs, mainly formal ones, have a rather large premises in which to conduct their activities. One out of four formal HBs operates in a premises that is larger than 100 square meters. Informal HBs rarely have large premises, especially in urban areas.

The lack of an adequate premises in the informal sector has been reported in many papers (La Porta and Shleifer, 2008; Barwa, 1995). Without a permanent premises, many informal HBs are likely to have insufficient access to public services such as water, electricity and the internet, and they are under continuous threat of eviction. In addition to having less access to fixed premises, informal HBs have less space when they have a fixed premises.

2.3. High rate of ownership of a fixed premises

Ownership of a fixed premises (e.g. a home out of which a HB operates, a shop or a permanent premises in a market or workshop) is an indicator of the level of stability of the operating conditions. If household businesses are located in a rented premises, they face the possibility of being shifted to other premises, which may affect their investment and growth in the long run. Moreover, renting constitutes a burden that reduces profit.

More than three out of four HB owners own their premises, and the proportion is similar for formal and informal businesses. In addition, a few of them (2 per cent) partly own their premises. Nine out of ten of those who work at home own their home, while the proportion of those who have a professional premises is lower but still important: 68 per cent of the formal HBs and 56 per cent of the informal HBs (see Table 3.5).

Among the three sectors of activity, manufacturing and construction had the highest degree of ownership (88 per cent), followed by trade (74 per cent) and service (65 per cent). The manufacturing and construction sectors are usually marked by a high level of fixity, which means that HB owners use secure and stable locations like their homes to run their businesses instead of renting a premises.

The share of both whole and part ownership is significantly greater in rural areas than in urban areas (82 per cent and 63 per cent respectively), and it is also greater among formal HBs than informal ones.

TABLE 3.5.
PERCENTAGE OF OWNERS OF PREMISES AMONG HOUSEHOLD BUSINESSES BY
SECTOR AND AREA

	Formal HBs		Informal HBs	
	Rural	Urban	Rural	Urban
Manufacturing & construction	89.2	88.9	78.2	87.4
Trade	85.1	81.5	72.5	63.1
Service	83.6	70.4	74.3	67.9
Total	85.9	81.6	74.2	72.3

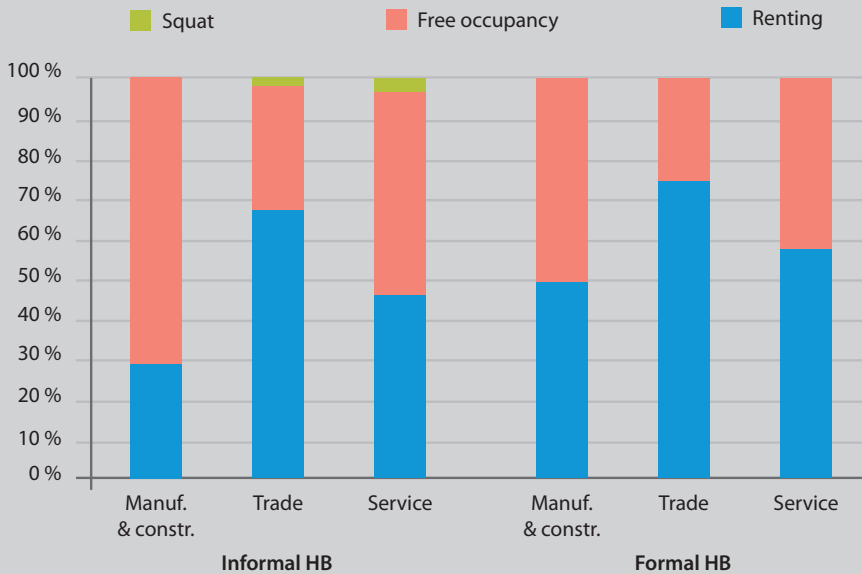
Source: 2014/15 HB&IS survey, VASS-CAF & IRD-DIAL; authors' calculations

Ownership of a premises, especially when the premises is the home where the household lives, is certainly a factor that facilitates the operation of a business. Many households conduct a little trade or another type of activity in their home. Nevertheless, this alone is not enough to develop a business, and, in certain conditions, it may be an obstacle to increasing the level of activity.

2.4. High rate of free occupancy

Among HBs that have a fixed premises, 22 per cent of the HB owners do not own the premises where they operate their business. However, only half of them have to pay rent. This proportion is lower for informal businesses: 45 per cent of the informal HB owners who do not own their premises and 61 per cent of those who have a formal HB pay rent. Others occupy their premises freely, and a few of the informal ones occupy their premises as squatters. The proportion of non-owners that has to pay rent is much higher in the tertiary sector, especially in the trade sector (see Figure 3.3). Chapter 10 shows that free occupancy of a premises is highly correlated with the relationship with the landlord. More than half of the landlords of professional premises are family members of the owners of the HBs, and because of this familial relationship, HB owners are often allowed to occupy a premises without paying rent, especially if they are close relatives.

FIGURE 3.3.
OCCUPANCY STATUS OF NON-OWNERS BY AREA AND BY MAIN ECONOMIC SECTORS



Source: 2014/15 HB&IS survey, VASS-CAF & IRD-DIAL; authors' calculations

All in all, only 9 per cent of the HB owners have to pay rent for their premises. This proportion is higher for formal businesses because more of them have a professional premises away from their home that they have to rent (see Table 3.6).

TABLE 3.6.
DISTRIBUTION OF HBS BY OCCUPANCY STATUS

	Informal HBs	Formal HBs	Total
Ownership	52.5	75.2	58.5
Free occupancy	8.0	6.7	7.7
Renting	7.4	13.2	8.9
No fixed premises	32.1	4.9	25.0
Total	100	100	100

Source: 2014/15 HB&IS survey, VASS-CAF & IRD-DIAL; authors' calculations

The precariousness of activity is primarily shown by the high rate of informal HBs operating without a premises. The rate of ownership of a premises is quite high, especially among formal HBs. It is possible that not owning a premises might deter informal HBs from formalizing their business.

2.5. Some improvement between 2007 and 2014

A comparison of the types of premises used by informal HBs in Hanoi and Ho Chi Minh City between 2007 and 2014 shows a structural change in progress (see Table 3.7). The share of informal HBs without a permanent premises in the trade sector declined considerably between 2007 and 2014, by 15 points of percentage in Hanoi and 22 in Ho Chi Minh City, and it increased in the service sector in Hanoi (among street restaurants and motorbike taxis). Meanwhile the proportion of informal HBs with a professional premises increased in Ho Chi Minh City. This change is particularly important in the trade sector in both cities, where the share of informal HBs with a professional premises increased considerably. This result converges with the decline of self-employed people in both cities and suggests that informal trade is conducted in a fixed premises more often than by itinerant petty traders.

TABLE 3.7.
EVOLUTION OF THE TYPE OF PREMISES AMONG INFORMAL HBS IN HANOI AND HO CHI MINH CITY

	No permanent premises	Hanoi			Ho Chi Minh City			
		Home	Professional premises	Total	No permanent premises	Home	Professional premises	Total
2007								
Manuf. & constr.	22.7	69.8	7.5	100	7.1	86.4	6.5	100
Trade	49.0	29.6	21.4	100	42.9	41.8	15.3	100
Service	52.3	34.4	13.3	100	55.1	34.4	10.6	100
Total	45.7	39.1	15.3	100	40.6	48.2	11.2	100
2014								
Manuf. & constr.	23.9	65.4	10.7	100	11.0	70.1	19.0	100
Trade	34.4	34.2	31.5	100	20.8	43.3	35.9	100
Service	61.4	28.6	10.1	100	47.8	37.8	14.4	100
Total	47.8	36.6	15.6	100	32.9	47.0	20.2	100

Source: 2007 HB&IS, GSO-ISS/IRD-DIAL, 2014/15 HB&IS, VASS-CAF & IRD-DIAL; authors' calculations

To conclude on premises, the type of premises used for an activity and their occupancy status are diverse among HBs. A non-negligible proportion of them, one third of the informal HBs, have no fixed location from which to run their business, reflecting a high level of instability and precariousness. However, this proportion is on the decline. Around half of the HB owners benefit from a high degree of stability as they operate their business out of their home, which they generally own. However, they are restricted in their growth prospects as space in their home is limited. Another segment is comprised of people who have a HB and do not own their premises but occupy freely premises owned by family members. Although they do not own their premises, as a family member they benefit from a certain assurance regarding their stability. However, free occupancy generates moral debt towards their family that can impact the functioning of their business (see Chapter 10). Finally, a minority of HBs, mostly formal ones, pay rent for a professional premises. That is why they can be more vulnerable to economic shocks, but they also have the highest potential for growth as they can adapt the surface of their premises to the size of their activity, and they operate in more adequate conditions.

3.

THE INFORMAL SECTOR AND ADMINISTRATIVE REGISTRATION

Whether or not a business has been registered is one of the criteria commonly used to determine if it belongs to the informal sector. It is recommended by the ILO as an official definition of the informal sector, although the type of registration varies according to the national context. In Vietnam, the GSO uses business registration to differentiate formal from informal businesses.

We consider here three types of administrative registration: business, tax and social security registration. Registration reveals what the institutional relationships are between household businesses and the state. Household businesses, except for street vendor, mobile trading, petit services and low-income services (the low-income line is defined by the provincial authorities), are obliged to register.⁴ Registered HBs are granted a tax code for business tax, income tax and value added tax, while non-registered HBs can register to pay an annual lump sum business tax.

Before exploring the characteristics of HBs in terms of administrative registration, we present some findings about the practice of bookkeeping. The absence of accounting

4. Article 49 (Item 2) in Decree 43/ 2010/ ND – CP concerning business registration.

records is a major characteristic of both the informal sector and formal HBs. It is linked to administrative registration, in particular tax registration, because a lack of accounting makes it difficult to have a consistent policy of taxation for this sector.

3.1. Lack of accounting tools

Bookkeeping is an important indicator of the quality of management. Proper bookkeeping contributes to improvements in an entrepreneur’s financial performance and budgeting plans. However, most HBs, even formal ones, do not keep books or records of their activity. This means that in terms of management practice, formal HBs are closer to informal HBs than to domestic or corporate enterprises.

Most informal HBs (78 per cent) do not keep any accounts at all. Only around one out of five (21.8 per cent) keep some kind of personal books, and virtually none have formal accounts. These proportions are similar across all the economic sectors.

These figures are not surprising as not keeping accounts is one of the main characteristics of the informal sector. But formalization itself does not guarantee progress in bookkeeping. Only 5 per cent of the formal HBs do bookkeeping as required by law, and more than half of them do not keep any record of their accounts (see Table 3.8).

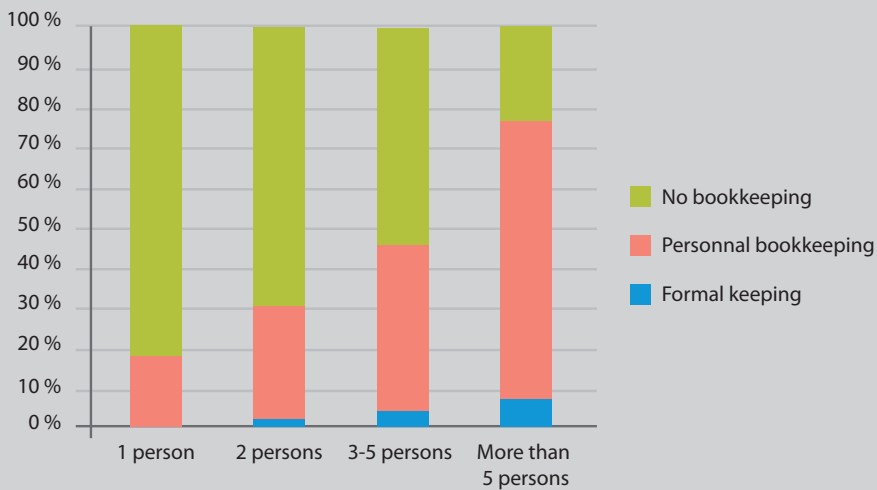
TABLE 3.8.
BOOKKEEPING BY SECTOR, FORMALITY AND SIZE OF HBS

	Informal HBs			Total	Formal HBs		
	Formal book-keeping	Personal book-keeping	No book keeping		Formal book-keeping	Personal book-keeping	No book keeping
Manuf. & constr.	0.1	24.0	76.0	100	8.1	31.9	60.0
Trade	0.0	29.5	70.5	100	4.6	43.9	51.6
Service	0.1	14.4	85.5	100	4.7	39.8	55.5
Total	0.1	21.8	78.1	100	5.3	40.3	54.4

Source: 2014/15 HB&IS survey, VASS-CAF & IRD-DIAL; authors' calculations

However, larger HBs are more likely to do bookkeeping than smaller ones. Legal accounting and personal bookkeeping make up 4 per cent and 42 per cent respectively of the HBs with 3-5 workers, and 7 per cent and 69 per cent of the HBs with more than 5 workers. Obviously, growing in size requires better management tools, but it is difficult to know the direction of causality: Do those who have a better system of management grow in size, or is it having workers that determines whether or not HBs owners do bookkeeping? In any case, even among the largest HBs, only a small share of them (7 per cent) utilise a legal accounting system, and there are still a significant number of HBs that do no bookkeeping at all (53 per cent of the HBs with 3 to 5 workers and 23 per cent of the HBs with more than 5 workers).

FIGURE 3.4.
BOOKKEEPING BY SIZE OF HB



Source: 2014/15 HB&IS survey, VASS-CAF & IRD-DIAL; authors' calculations

Moreover, although the number of HBs with only one person has declined in Hanoi and Ho Chi Minh City, the practice of having legal or personal accounting for one's business has also greatly declined. Among both formal and informal HBs in both cities, the percentage of HBs that do no accounting at all increased between 2007 and 2014/15. More worryingly, this percentage more than doubled in Hanoi and in Ho Chi Minh City among formal HBs (see Table 3.9).

3.2. One quarter of the HBs have a business certificate

Business registration is the criteria used by the General Statistics Office to differentiate formal from informal HBs. About one fourth of the total number of HBs (26 per cent) have a business certificate and are therefore considered to be formal HBs, which suggests relatively loose administrative links to the state of household businesses in general. Business registration is higher in the trade sector (37 per cent of the HBs) than in the service and manufacturing sectors (20 per cent).

Business registration is more important in urban areas, although, as we have seen, the average size of HBs there is not larger. While one third of the HBs in urban areas have registered as a business, in rural areas only 20 per cent have done so. Thus, the rate of formality is much higher in cities. This is probably due to looser administrative monitoring of businesses in rural areas. As the implementation of the rules concerning business registration is at the discretion of district authorities, it seems that outside cities there is less pressure to register (see Table 3.10). This has been confirmed by an estimation of the probability of being registered (see the appendix). Rural HBs are much less likely to be registered than urban HBs. This can be seen once size, sector of activity, value added, premises and other characteristics are controlled for.

TABLE 3.10.
ADMINISTRATIVE REGISTRATION BY SECTOR AND GEOGRAPHICAL AREA

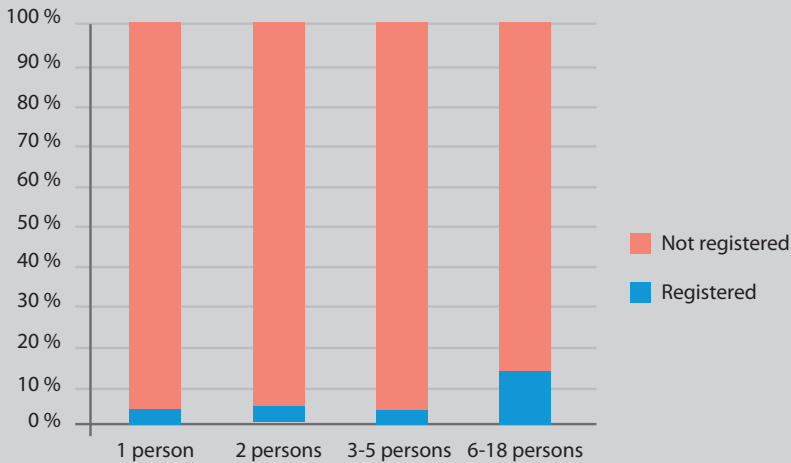
	Rural	Urban	Total
Manufacturing & construction	15.8	26.0	19.5
Trade	31.2	46.0	37.3
Service	12.0	27.4	20.3
Total	20.5	33.4	26.3

Source: 2014/15 HB&IS survey, VASS-CAF & IRD-DIAL; authors' calculations

More generally, and as expected, the estimation of the probability of being registered shows that the bigger a HB is, the more likely it is to be registered: The number of workers in an HB and the annual value added are positively and significantly correlated with the decision to register. The type of premises is one of the main determinants of registration as HBs with a professional premises are more likely to be registered. Interestingly, the owners of HBs whose motivation in running a HB is to be independent (see Chapter 11 for more details) are less likely to register. Finally, female owners are less likely to register their business. This can be seen once other characteristics of HBs are controlled for.

security registration among formal HBs is not correlated to the size of a HB once the other characteristics of the business are taken into account (see Model 3 in the appendix). So enforcement of the legal regulations on social security contributions is very limited, even among formal HBs.

FIGURE 3.5.
SOCIAL SECURITY REGISTRATION BY SIZE OF HB



Source: 2014/15 HB&IS survey, VASS-CAF & IRD-DIAL; authors' calculations

The very low rate of compliance with social security registration aggravates the vulnerability of all the workers in the HB sector. Incentives to comply with social security regulations should be envisaged to improve the social protection of not only the informal sector but also workers at formal HBs.

There is hope for social security enrolment when one considers the evolution of social security registration over time in Hanoi and Ho Chi Minh City. There has been some progress in both cities among both informal and formal HBs, but not very much (2 to 6 points of percentage in seven years), and the number of HBs which are not registered is still considerable (19 out of 20).

An opposite trend can be seen concerning tax registration: a decline in both cities among formal HBs. The increase in formalisation, i.e. in business registration, that has been seen in the past years (see Chapter 2) has not translated into increased registration with the tax department. This shows that formalisation is very fragile (see Table 3.12).

TABLE 3.12.
TYPES OF REGISTRATION IN HANOI AND HO CHI MINH CITY IN 2007 AND 2014

	Tax registration		Social security registration	
	2007	2014	2007	2014
Hanoi				
Informal HBs	1.2	0	0	2.5
Formal HBs	77.8	64.6	2.7	7.7
HCMC				
Informal HBs	0.1	0	0.4	2.2
Formal HBs	86.3	75.4	2	7.9

Source: Cling *et al.* 2010 and the 2014/15 HB&IS survey, VASS-CAF & IRD-DIAL; authors' calculations

Formalisation has little impact on the social protection of workers. Concern about the social protection of workers goes beyond the informal sector. Even at formal HBs the vulnerability of workers is high. Extending social security to workers at household businesses should be a main axis of policies towards this sector (see Chapter 8 for further discussion).

4. FACTORS OF FORMALISATION

As hinted above, the frontier of formalisation is fragile. Indeed, a significant number of informal HBs are willing, and are even preparing, to formalise their business by registering and getting a business certificate. However, they are a minority of the informal businesses. For the majority, the advantages of formalisation are not so obvious, and there is clearly a lack of knowledge about the regulations.

In this section we first examine why informal HBs do not register and formalise their business, and we discuss the opinions of owners of informal HBs concerning registration and having a business certificate. In the second part we look at the expected advantages of having a formal business.

4.1. Why informal businesses are not registered

Owners of informal HBs were asked what their main reason was for not registering and getting a business certificate, which would formalise their business. Most of them (68 per cent) think they do not have to register to get a business certificate (see Table 3.13). This statement is quite surprising because owners of all kinds of informal

businesses, small and big and in all economic sectors, said this. The precise requirements for each HB, whether or not it should be registered, are unknown because it depends on the district context. However, those who have no premises, such as street vendors and motorbike taxi drivers, were more likely to say that they did not have to register. However, this is not the case. A similar proportion of informal HBs in all kinds of premises, including professional premises, think they are not subject to registration. Even HBs that have several workers or have high value added or make a high profit share this opinion. This clearly shows a lack of knowledge of the regulations, not only among the owners of HBs but among the local authorities as well.

Other reasons for not registering are much less prevalent. 12 per cent do not want to register, probably because they do not see any advantage in formalising their business. Having an instable income is another reason (10 per cent), and a rather good one, although it might not be accepted by district authorities. This shows, however, that formalising a business is a step towards a steadier and more established way of conducting an activity. This reason was given slightly more often by HBs which were created in recent years. This is also the case for those who do not know if they have to register. Here again, there is a lack of information. Finally, the cost of registration and the complicated procedures are not the main reasons for not registering (less than 1 per cent). Most of the informal HBs can afford the cost (the median cost has been 200,000 VND since 2010, and only 5 per cent of the HBs had to pay more than 3 million VND).

TABLE 3.13.
REASONS INFORMAL HBS HAVE FOR NOT REGISTERING

	Too complicated	Too expensive	Not mandatory	Do not know if they have to register	Unstable income	Do not want to	Total
Manufacturing & const.	1.2	1.2	64.6	7.9	11.9	13.2	100
Trade	0.3	0.1	70.4	7.2	8.3	13.2	100
Service	0.6	0.4	69.6	5.7	11.6	11.3	100
Total informal HBs	0.7	0.6	68.4	6.8	10.7	12.4	100
Urban informal HBs	1.1	0.6	69.5	5.5	12.3	10.6	100
Rural informal HBs	0.4	0.5	67.6	7.6	9.6	13.7	100
Willing to register*	66.2	22.8	21.1	44.8	16.8	22.6	22.7

* Read as follows: 66.2 per cent of those who stated that they have not registered because it is too complicated are nevertheless willing to register; 22.8 per cent of those who said it is too expensive are ready to register.

Source: 2014/15 HB&IS, VASS-CAF & IRD-DIAL; authors' calculations

The reasons for not registering are similarly distributed across economic sectors and among rural and urban HBs. Cost or complicated procedures were given as reasons for not registering by a very small number of HB owners everywhere. This was the case in Hanoi and Ho Chi Minh City in 2007 (Cling *et al.*, 2010). If the objectives of policies are to facilitate registration, the problem to tackle is not so much the fees or the procedures but rather the lack of information about registering among HB owners.

Most of the owners of informal HBs do not intend to formalise their business. Only about one quarter of them (23 per cent) are eager to register.⁷ Interestingly, willingness to formalise is not related to the number of workers or to the amount of value added or profit of a business. The same proportion of informal HBs owners willing to formalise is found among all kinds of informal businesses. This is verified when the operating conditions of a business (the type of premises in which the business is operated) are considered. Among those with no fixed premises (who are therefore not obliged to register), the proportion which stated that they were prepared to register is similar to those who work at home and even those who have a professional premises.

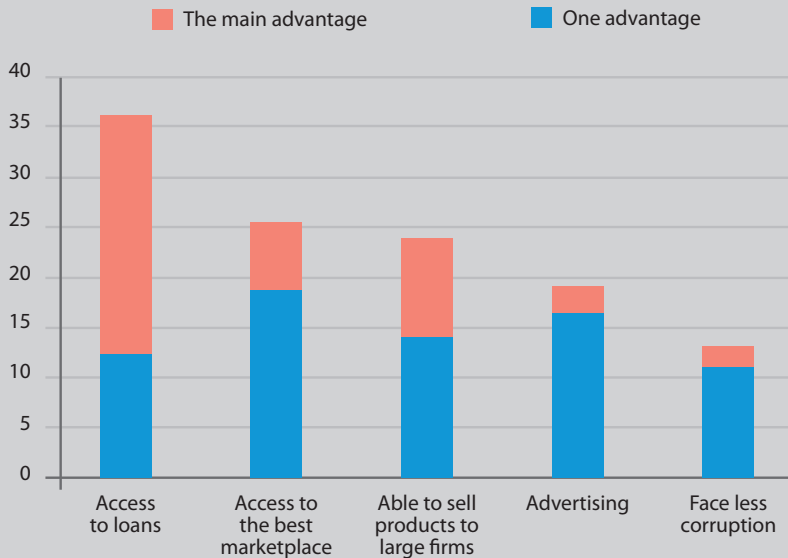
4.2. Advantages of being registered

Willingness to register greatly depends on how HB owners perceive the advantages of formalising their business. More than half of the informal HBs (53 per cent on average, but 58 per cent in rural areas) see no advantage in registering their business.

Access to loans is by far the main advantage of formalisation in the opinion of informal HB owners. 36 per cent of them stated this as an advantage of formalisation, and 24 per cent said this is the main if not the only advantage of formalisation. Other reasons are access to a better marketplace (in markets in particular) and the possibility to sell products to large firms. Formalisation has resulted in facing less corruption for only 13 per cent of the informal HBs owners.

7. A few of them (0.5 per cent) stated that registration is in progress.

FIGURE 3.6.
WHAT INFORMAL HB OWNERS THINK ABOUT BUSINESS REGISTRATION
 (PERCENTAGE)



Source: 2014/15 HB&IS, VASS-CAF & IRD-DIAL; authors' calculations

For formal HBs the decision to register is mainly motivated by the obligation to have a business certificate rather than by the benefits they expect to receive as a result. 60 per cent stated that they registered because it is compulsory and 22 per cent said that they were forced to register. Only 17 per cent of the formal HBs registered because they thought that being officially registered would facilitate their business.

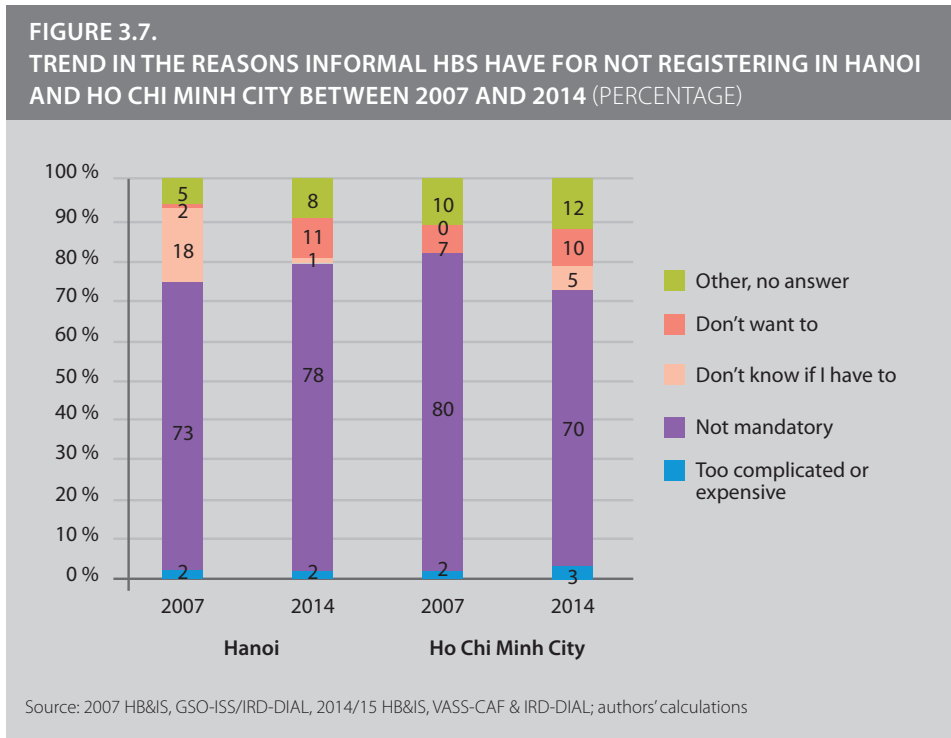
4.3. Evolution since 2007

Although this study was limited to the two main cities in Vietnam, the evolution of the attitude of informal HBs towards formalisation sheds light on the applicability of business registration. This is done through three questions we have previously seen: Why have informal HBs not registered? What are the main advantages of registration they foresee? and How many of them are prepared to register?

Although at first glance the reasons for not registering appear to have been stable between 2007 and 2014, with the majority of owners saying registration is not mandatory in their case, there have been significant evolutions among the other reasons (see Figure 3.7). As seen above, the majority of the owners who said that business registration

is not mandatory were unaware that the regulations stipulate that most of them should register. Some of them said that they did not know whether or not they were supposed to register. In 2007 these were two reasons given by 90 per cent of the owners (more in Hanoi than in Ho Chi Minh City) who had not registered. In 2014, one of these two reasons was given by three quarters of the respondents in both cities. Awareness of the regulations has increased, but a lot remains to be done. This progress is tempered by the fact that an increasing proportion of informal HB owners (an increase of 10 points of percentage in both cities) stated that they do not want to register anyway.

It is clear that registration is not a problem of cost or red tape. Only a low percentage of the owners in 2007 stated this as their reason for not registering, and there has been no noticeable change since then.



In 2007 less than half of the informal HBs owners could not see any advantage in formalising their business (45 per cent in Hanoi and 49 per cent in Ho Chi Minh City). In 2014 the share of owners who did not foresee any advantage had jumped to 59 per cent in both cities. In addition, the advantages have significantly changed (see Table 3.14). While in 2007-2008 the main advantage was facing less corruption (58 per cent in Hanoi and 55 per cent in HCMC), other advantages were greater in 2014, with only 9 per cent

of the respondents in Hanoi and 4 per cent in HCM stating that facing less corruption would be the main advantage of formalising their business. Corruption is no longer a major concern for informal HBs owners. In 2014 HB owners were much more concerned with finding a way to expand their business, either by having easier access to loans or by selling to large firms.

TABLE 3.14.
TREND IN THE PERCEIVED ADVANTAGE OF REGISTERING A BUSINESS AMONG
INFORMAL HB OWNERS IN HANOI AND HO CHI MINH CITY IN 2007 AND 2014
 (PERCENTAGE)

	Hanoi		Ho Chi Minh City	
	2007	2014	2007	2014
Access to loans	10.3	28.1	6.1	45.6
Access to a marketplace	18.0	19.3	20.1	1.8
Sales to large firms	5.8	34.6	4.9	37.7
Advertising	2.2	5.7	1.0	5.5
Face less corruption	57.8	9.8	55.1	4.0
Other	5.9	2.4	12.8	5.4
Total	100	100	100	100

Source: 2007 HB&IS GSO-ISS/IRD-DIAL, 2014/15 HB&IS, VASS-CAF & IRD-DIAL; authors' calculations

The proportion of informal HBs that are prepared to register in order to become formal is relatively stable in Hanoi and Ho Chi Minh City, except in the case of the trade sector in Hanoi, where willingness to register has declined. In Ho Chi Minh City willingness to register has significantly increased in the manufacturing sector (see Table 3.15).

TABLE 3.15.
HBS PREPARING TO REGISTER IN HANOI AND HO CHI MINH CITY IN 2007 AND 2014
 (PERCENTAGE OF INFORMAL HB OWNERS)

	Hanoi		Ho Chi Minh City	
	2007	2014	2007	2014
Manufacturing & construction	18.9	18.6	19.2	27.6
Trade	17.6	9.5	21.0	19.0
Service	14.1	15.3	18.4	20.1
Total	16.3	14.4	19.4	21.8

Source: Cling *et al.*, 2010, p 174; 2014/15 HB&IS, VASS-CAF & IRD-DIAL; authors' calculations

CONCLUSION

An examination of the classical characteristics of informality among HBs and more specifically in the informal sector confirms in some respects that there is a typical informal sector in Vietnam, e.g. small-size businesses, a disregard for state regulations and a lack of modern management tools. It also shows some heterogeneity in terms of the types of premises where businesses are operated and the degree of instability this implies. Likewise, it shows that some characteristics of informality are shared by formal HBs, which are not so different than informal ones in terms of size and respect for regulations.

As elsewhere, the HB sector, and more specifically the informal sector in Vietnam, is characterised by its small size. However, the trend in the size of informal HBs shows that a structural change is at play, as self-employed workers, in particular those in precarious trade activities, are being progressively replaced by family HBs.

The characteristics of a premises for an activity reflect the heterogeneity of the HBs. Although most of the HB owners operate their business out of their home and own their premises, a segment of the informal sector has either no fixed premises or a precarious occupancy status. One third of the informal HBs have no fixed location from which to run their business, reflecting a high level of instability and precariousness, and around half of the HB owners benefit from a high degree of stability because they operate their business in their home, which they generally own. However, they are restricted in their growth prospects as space in their home is limited. Finally, a minority of the HBs, mostly formal ones, rent a professional premises. Even though that results in an additional cost, these HBs operate in more adequate conditions and have a higher potential for growth as they are not constrained by the limited space in their own home.

About one fourth of the total number of HBs are formal HBs that have a business certificate, suggesting relatively loose administrative links to the state of household businesses in general. While one third of the HBs in urban areas are registered, only 20 per cent of the HBs in rural areas are registered, even though the average size of the HBs in rural areas is not smaller. Rural HBs are even larger on average and more oriented towards manufacturing and construction activities. This suggests a lack of enforcement of the regulations in rural areas.

The main reason why formalisation is not enforced and why informal businesses are not willing to formalise is a lack of information related to the regulations. Indeed, a

large proportion of the informal HB owners think that they are not subject to registration, and this proportion does not vary according to the size of the business or the kind of premises. This clearly shows a lack of knowledge of the regulations, not only among the HB owners but also the local authorities. A lack of incentive to formalise is another obstacle as more than half of the informal HBs see no advantage in registering their business. Only 17 per cent of the formal HBs registered because they thought that being officially registered would facilitate their business. The decision to register is mainly motivated by the obligation to have a business certificate rather than by any advantages they may expect as a result of registering.

In addition to the predominance of informal HBs, a non-negligible share of HBs defined as formal do not have the expected attributes of formality. Formal HBs, those which have a business certificate, are required register with the tax department. A little more than two thirds comply with this rule. While formalisation of HBs has had an effect on tax registration, this has not been the case with social security registration. The very low rate of compliance with social security registration requirements, even among formal HBs, aggravates the vulnerability of all the workers in the HB sector. Incentives to comply with social security regulations should be envisaged to improve the social protection of not only the informal sector but also workers at formal HBs. Finally, most of the HBs do not keep books or records of their activities, not even the formal HBs. In that respect formal HBs are closer to informal HBs than formal enterprises. If bookkeeping is an indicator of the quality of management of a business, then it can be said that formal as well as informal HBs in Vietnam have weak management. This calls for policy aimed at improving the accounting of small businesses, especially formal ones, by training the owners and by implementing some tools adapted to the conditions of operation at these businesses.

APPENDIX - DETERMINANTS OF REGISTRATION OF HBS IN VIETNAM

This section applies the probit regression model to identify factors behind the decision to register or not among household businesses in Vietnam using data from the 2014/15 HBIS. The dependent variables are the binary response showing whether an HB has registered its business or not for all HBs (Model 1), whether an HB has complied with tax registration requirements or not (for formal HBs only) (Model 2), and whether an HB has complied with social security registration requirements or not (for formal HBs only) (Model 3). In order to identify the determinants of why owners decide to register their business or not, the marginal effects of all explanatory variables X on the probability of registering is calculated. This corresponds to a change in the probability of registering due to an increase of one unit of the explanatory variable from the baseline or reference group.

TABLE 3.A DETERMINANTS OF BUSINESS REGISTRATION, TAX REGISTRATION AND SOCIAL SECURITY REGISTRATION

	(Model 1) Probability of being formal (registered as a business) vs informal	(Model 2) Probability of tax registration among formal HBs	(Model 3) Probability of social security registration among formal HBs
Urban (ref. rural)	0.354*** (0.0535)	0.130 (0.0928)	0.365** (0.159)
Sector of activity (ref. manuf & construction)			
Trade	0.887*** (0.0691)	0.323*** (0.120)	0.350* (0.196)
Service	0.561*** (0.0685)	0.211* (0.121)	0.353* (0.197)
Number of workers (ref. 1 worker)			
Two workers	0.242*** (0.0594)	0.00726 (0.105)	0.262 (0.171)
3-5 workers	0.542*** (0.0775)	0.0402 (0.126)	0.370* (0.193)
6-18 workers	0.748*** (0.142)	0.0960 (0.212)	0.295 (0.320)
Quartile of value added (ref. 1 st quartile)			
Quartile 2	0.108 (0.0783)	0.191 (0.147)	0.218 (0.246)
Quartile 3	0.424*** (0.0765)	0.524*** (0.139)	0.0209 (0.238)
Quartile 4	0.605*** (0.0824)	0.566*** (0.143)	0.123 (0.239)
Duration of the business (ref. 0-4 years)			
5-9 years	0.140* (0.0744)	0.107 (0.128)	0.0391 (0.190)
10-16 years	0.387*** (0.0704)	0.257** (0.118)	-0.0814 (0.180)
More than 16 years	0.315***	0.360***	0.00862

Type of premises (ref: no fixed premises)			
At home	0.941*** (0.0839)	0.113 (0.177)	-0.718*** (0.218)
Professional premises	1.125*** (0.0841)	0.197 (0.176)	-0.737*** (0.216)
Motivation (ref: no job as wage worker or farmer)			
Higher income	0.0766 (0.0729)	0.194* (0.115)	0.284 (0.179)
Independence	-0.199*** (0.0770)	0.0190 (0.132)	0.325 (0.206)
Family tradition or other	-0.0835 (0.0665)	0.262** (0.112)	0.250 (0.182)
Female owner	-0.149*** (0.0552)	0.00388 (0.0926)	-0.0191 (0.135)
Education level of the owner (ref: no diploma/certificate)			
Primary	0.229*** (0.0614)	0.129 (0.108)	0.360* (0.184)
Lower secondary	0.429*** (0.0663)	0.270** (0.113)	0.420** (0.184)
Upper secondary	0.572*** (0.125)	0.363* (0.187)	0.141 (0.284)
Superior	0.130** (0.0570)	0.0922 (0.0936)	0.0980 (0.138)
Constant	-2.968*** (0.134)	-0.891*** (0.261)	-2.218*** (0.400)
Observations	3,406	1,028	1,028

Note: Standard errors in parentheses; *** p<0.01, ** p<0.05, * p<0.1

Source: 2014/15 HB&IS, VASS-CAF & IRD-DIAL; authors' calculations



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The Importance of Household Businesses and the Informal Sector for Inclusive Growth in Vietnam

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This book draws on an original and innovative data collection to provide new evidence on household businesses and the informal sector in Vietnam. This 2014/15 HB&IS survey conducted in late 2014 and early 2015 is the first national survey ever on this sector in Vietnam with full coverage of its different components.

The purpose of this book is threefold. First, it aims at filling the knowledge gap as to the role of household businesses and the informal sector in the Vietnamese economy. Second, it provides new insights for policymakers to unlock household business potential by identifying the factors blocking their performance and productivity. Thirdly, it identifies the sources of worker vulnerability in household businesses and the informal sector to inform the design of a suitable policy to tackle this vulnerability.



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