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COVID-19, MSMEs, AND THE INFORMAL SECTOR

Introduction

Reden is the owner of a small online vegetable delivery service in Marikina. The lockdown saw the increase in the daily transactions that his small enterprise usually receives in a day – from 60 to 300. Reden counts himself lucky. However, he did experience difficulty in sourcing and transporting his vegetables due to the tighter government restrictions.

Reden is lucky compared to the 90,000 micro-, small-, and medium-sized enterprises (MSMEs) that had closed down by September 2020 (Romero & Romero, 2020), six months after the first community lockdown.

Among those MSMEs that had to close down was the private kindergarten school located a few meters away from Reden's vegetable warehouse. Owned by Ellen, the school had been educating kids living in the community for the last two decades. Already plagued by declining enrollees due to the increased competition, Ellen's cash reserves had been continuously decreasing. Like other MSME owners (Macaraeg, 2020), Ellen continued paying her employees a month after the lockdown, but the school's continuing expenses were already eating into her personal savings. Ellen has plans to reopen the school, but as to when, she has yet to decide.

Jun was one of Ellen's employees. Jun had been teaching in the said school for two years before it closed down in May. The school's closure forced Jun to convert the garage of his rented apartment into a sari-sari store. Jun enjoyed good sales for the first month, but this

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did not last long as the government started easing the restrictions on people's mobility. If this was not bad enough, Jun's store was visited by barangay officials to encourage him to register for a permit. Since the license fee would eat into his tiny circulating capital, Jun decided to lessen the store's hours to avoid being caught operating without a license.

A few kilometers from Jun's occasionally closed sari-sari store is Eva's table on the sidewalk, laden with foot rugs for sale. Eva has been a sidewalk vendor for a decade. Unlike Jun, Eva has spent a decade dodging authorities as vendors like her are not usually allowed by the local government to operate.

MSMEs' characteristics and what makes them vulnerable to the pandemic

The stories above demonstrate how MSMEs are differentially affected by the lockdowns brought about by the pandemic. The differences in the effects felt by the MSMEs depends on two things. First is if the enterprise is categorized as an essential business. The second is whether the enterprise can adapt to the new business normals such as a reduced number of people inside the premises and the stringent health protocols.

The lockdowns have had a deleterious effect on many MSMEs. Many MSMEs saw the slowdown, if not the entire wipeout for the demand for their products, problems with the availability of their raw materials, workforce problems, and stricter government policies on businesses' operations (University of the Philippines Institute for Small-Scale Industry, 2020). These problems cropped up as the government's primary strategy to slow the spread of the virus was to lock down localities to restrict the mobility of people. MSMEs are particularly vulnerable to the unintended economic consequences brought about by the pandemic for many reasons.

First, many MSMEs are heavily reliant on their cash flow (Macaraeg, 2020). This reliance meant that once cash from sales stopped, many MSMEs had to either temporarily or permanently close down. Usually, MSMEs lack the cash reserves to continue paying the expenses (think utility bills, loan payments, rent, etc.)

that will continue to be due despite the lockdown (Balea, 2020). Ellen's case exemplifies this in the stories told earlier.

Second, and related to the first, many MSMEs do not have the resources needed to shift to a work from home setting to continue their operations (if ever this option was available to them). As such, the likely responses to the pandemic of MSMEs had been limited to closure or reduced capacity. Further compounding this problem is the lack of know-how associated with taking advantage of the technology available to adapt to the new normal.

Third, many MSMEs do not have business continuity plans. A rapid survey done by the University of the Philippines Institute for Small-Scale Industry among 100 MSMEs revealed that 75% do not have business continuity plans in place. The absence of these plans makes MSMEs doubly vulnerable as they are not prepared to handle crises (University of the Philippines Institute for Small-Scale Industry, 2020).

Fourth, many of the MSMEs are informal. Informality hampers many MSMEs in the developing countries as it usually "places them out of the reach of governmental initiatives; constrains the ability of MSMEs to diversify their supply and customer base and implies a lack of compliance with norms and regulations" (UNDP, 2013, p. 14). This condition further increases the vulnerabilities of the people they employed (think about noncompliance in paying social insurance and other mandatory benefits).

Attempts to address these vulnerabilities

Acknowledging these vulnerabilities, the government has crafted a plan. It has made available programs to aid our MSMEs, coursed mainly through the Department of Trade and Industry (DTI) and other concerned agencies.

To address the first vulnerability and help MSMEs in the short term, the Bayanihan to Heal as One ACT (Republic Act 11469) extended the payments of loans and rentals. Displaced workers of MSMEs were also targeted by the Php 50.8 B Small Business Wage Subsidy Program. For the long term, the Bangko

Central ng Pilipinas (BSP) has decreased interest rates by 0.5% and increased the amount that banks can loan out. There is also the Php 1 Billion Economic Recovery Financing facility (COVID-19 ERF) of the Small Business Corporation (DTI-SBC), a government-owned financing corporation under the DTI. This financing facility has been earmarked explicitly for MSMEs and is viewed as a way to help MSMEs with their problematic cash flows (Penaranda, 2020).

The DTI has launched its Livelihood Seeding Program – Negosyo Serbisyo sa Barangay for the second and third vulnerabilities. This program provides technical and business management assistance to the barangay-level (village-level) entrepreneurs. The seeding program also offers financial aid to a limited extent (Penaranda, 2020).

To a limited extent, the COVID-19 ERF addresses the needs of informal MSMEs as this loaning facility has been allotted to the DTI-SBC's Pondo sa Pagbabago at Pag-asenso or P3 microfinancing program (Desiderio, 2020). Started in 2017, the P3 was created and implemented to discourage MSME entrepreneurs from resorting to loan sharks (the 5-6 loaning system) that charge high fees (20% monthly or higher). P3 only charges a maximum of 2.5% monthly interest rate, with minimal documentary requirements, and can be accessed through rural banks, microfinance institutions, and even market vendor associations (Valdez, 2019). However, to be more inclusive, it is vital that we further understand the informal sector and the obstacles that they have to hurdle.

The informal sector and the challenges they face

Informal MSMEs are usually discussed under the general idea of the informal sector or informal economy. Due to the increasing complexity of what constitutes informality, a generally agreed-upon definition had mostly been elusive (Tokman, 2001). Despite this situation, the meaning of informality has come to be associated with the criteria of “undeclared labor, tax evasion, unregulated or unlicensed enterprises, illegality or criminality” (Dahles & Prabawa, 2013).

According to the International Labour Organization (2020), informal enterprises are “unregistered small-

scale units, often employing ten or fewer undeclared and low-skilled workers, including unpaid family workers, mainly women, who labour in precarious conditions, without social protection or health and safety measures at the workplace. They have low productivity, low rates of savings and investment, and negligible capital accumulation, which make them particularly vulnerable to economic shocks and are often excluded from COVID-19 crisis-related short-term financial assistance programs for businesses” (p.1).

Typical of informal MSMEs is the characteristic of "operating under the radar." This feature means that informal enterprises and their workers are not registered with the government. This noncompliance makes it difficult for the government to reach them (International Labour Organization, 2020). This unregistered status also excludes informal MSMEs from governmental short-term financing windows as registration documents are required to access these. Even the P3 cited earlier, while designed to include the informal sector, still requires documentary proofs such as the entrepreneur having a government-issued ID, barangay clearance, certificate of operation from the local government unit (LGU), and proof of one-year residence (Small Business Corporation, 2020). Since informal entrepreneurs are usually undocumented, this then translates to them not being able to avail of the Small Business Wage Subsidy Program for their employees. Such a situation results to further hardships for people in the informal sector.

Addressing ‘exclusion’ among informal MSMEs: A continuing challenge

Informal MSMEs cannot afford to halt operations as to do so would mean starvation for the entrepreneur and the people he/she employs. Even if expressly condoned by the government, many of these MSMEs continue to operate, albeit in a guerilla setting. Due to their limited funds, these informal enterprises would not have enough money to comply with the minimum health standard protocols meant to prevent the spread of the COVID-19 virus (International Labour Organization, 2020). This situation puts the informal entrepreneur, his/her workers, and their customers in danger, as they can be possible carriers of the virus.

Due to the financial hardships caused by the community lockdowns, many formal MSMEs have downsized, permanently closed down, or have resorted to informality as a means to deal with this challenging situation. The employment of these means increases the informal economy's size and, for the reasons already discussed, compounds the difficulty of stopping the spread of the disease.

While we can only infer data about the informal sector's contributions to the country's economy as no systematic data exists, a good proxy could be informal employment data. However, the International Labor Organization web site does not have data about the status of informal employment in the country (International Labour Organization, 2021). Despite

this, a 2019 World Bank report states that MSMEs comprise 99% of all enterprises and are responsible for generating 2/3s of the country's total employment.

As MSMEs, in general, are seen as key to the country's inclusive recovery from the pandemic, we must discuss the unique challenges faced not only by the formal MSMEs but also of the informal ones. By doing so, we can strategize ways of attracting the informal ones to become legal.

A call to action: A holistic approach needed

Given the importance of including the informal sector in the holistic prevention of the spread of COVID-19 and our economy's recovery, the question now is what

Case study: The inclusion of Manila's sidewalk vendors

Manila has faced various issues as to how it dealt with its illegal/informal street vendors. Images of "the ruthless" sidewalk clearing efforts had littered the media, and Mayor Francisco 'Isko Moreno' Domagoso had been painted as anti-poor in his strategies to clean up the city, a far cry from how he was portrayed during the campaign period. The Manila city government, however, went a step further from simply clearing the streets, and embarked on a move to legitimize the street vendors, providing evidence that formalization can be successfully implemented.

Amid the pandemic around June 2020, the Manila city government's efforts to formalize the street vendors formerly located beside the city hall along Antonio Villegas Street started. As opposed to the previous administration's selling store tents to the sidewalk vendors for Php 15,000, the current government provided the metal stalls to the vendors for free. These stalls were also installed with electricity and submeters, and these were also offered for free by the LGU. Aside from this, the vendors are only charged a minimal tax of Php 40 per day. The fees collected equates to Php 1,200 per month. Even the mode for collecting this fee had been tailor-fitted with the vendors in mind. Php 20 is paid once in the morning and then another Php 20 in the afternoon. This way, the LGU has simulated the 5-6 loan shark's system of collecting a certain amount per day. This collection system also ensures that the former informal entrepreneurs will not view the taxes as an added burden and will then change their mindsets about the perceived costs of formalization. Mayor Isko says that he is training these vendors to become responsible entrepreneurs and to pay their taxes properly (Moaje, 2020).

This effort is also aligned with the mayor's efforts to make sure that there are no persons illegally collecting "protection money" from the vendors, making it more attractive for the vendors to operate under the government's folds (Moaje, 2020).

The mayor plans to provide stalls in other parts of the city like Ylaya Street in Divisoria. However, he remains adamant that no booths will be installed in other parts of the city where street vendors are known to operate. Recto Avenue, Soler Street, Juan Luna Avenue, Carriedo, Taft Avenue, Avenida, and Raon Street will remain stall-free. Such a policy ensures the smooth flow of traffic, especially on the main roads (Moaje, 2020).

In a sense, a balance has to be struck between various stakeholders of the city. LGUs can achieve inclusive governance in many ways. This strategy might have worked for the street vendors, but the LGU might need to think of other ways to deal with other informal entrepreneurs like pedicab drivers.

In conclusion, LGUs can do a lot to make sure that formalization becomes attractive to the informal sector. Manila has made efforts that other LGUs can learn from. LGUs can create solutions as long as it establishes a continuous dialogue with its constituencies and remains sincere about its efforts in making sure that governance is genuinely inclusive.

to do with them. While they are not registered and, therefore, not part of official statistics, we cannot afford to pretend that they do not exist.

We advocate for varied strategies given the diverse characteristics, circumstances, and backgrounds of informal enterprises and their employees. While we concede that absorbing all of the informal enterprises under the formal system would be difficult to achieve, it is imperative that the government, specifically LGUs, engage this segment under the principle of inclusive governance.

Ideas on how to attract informal entrepreneurs can be found as to why they do not comply with governmental administrative requirements. The usual reason is the cost associated with doing so. In general, the estimated cost of compliance represents a 50% cut into profits for 75% of these informal MSMEs (Tokman, 2001). Therefore, LGUs could create policies specifically targeting those operating under the informal economy [Note: Read the Case study: The inclusion of Manila's sidewalk vendors]. Even assuming that an informal MSME can shoulder the costs, compliance procedures are challenging to understand, and steps are often convoluted enough to demotivate any informal entrepreneur.

To an extent, the Barangay Micro Business Enterprise (BMBE) Law or RA 9178 of 2002 is a recognition of the need to differentiate small- and medium-sized from micro-sized enterprises. However, looking at the requirements for registration and renewal of registration, we say that there is still a need to make a law or revise the BMBE law to reflect micro-enterprises to the tune of asset sizes less than Php 300,000. A tiered and differentiated approach might also be called for instead of the blanket approach that many of our laws are so fond of. For example, street vendors like *Eva* and *sari-sari* store owners like *Jun* have different asset sizes. They might have different tolerance for the amount of registration fees to be levied upon them. Alternatively, local governments might opt for a flexible policy instead of opting for mere registration without any costs to fees as small as Php 100.

It is also equally essential to make compliance even easier, consistent with the BMBE Law's spirit. Thinking about the informal entrepreneur, it can be the case that the entrepreneur feels overwhelmed with dealing with the forms and processes as many are undereducated or uneducated. Therefore, it is crucial that procedures are shorter than it is right now and forms are simple to understand and translated to the local vernacular.

More importantly, the government should clearly and effectively communicate to informal entrepreneurs the benefits of being part of the formal economy. As additional capital may be a sufficient enticement to the entrepreneur, a useful way to encourage formality is to course the simple registration procedure through microfinance lending institutions, cooperatives, market associations and can be added through their registration procedures to access microloans.

Lastly, local government should be active in reaching out to the sector through labor organizations, market vendor associations, and other grassroots organizations to get informal entrepreneurs' thoughts (International Labour Organization, 2020). The government should do so indirectly as informal entrepreneurs are wary and afraid of their representatives (Tokman, 2001). This action will ensure that any policy developed or program implemented will be genuinely responsive to the informal sector's needs.

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