

Empirical Review on the Impact of Informal Tourism Sector Engagement in Sri Lanka Tourism Industry

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Received: 10 June 2023

Accepted: 20 September 2023

Revision: 20 July 2023

Published: 07 March 2024, **Volume-5, Issue-1**

Cite as: Ratnayaka, R. (2024). Empirical Review on the Impact of Informal Tourism Sector Engagement in Sri Lanka Tourism Industry. *ICRRD Journal*, 5(1), 133-139.

ABSTRACT: The purpose of this manuscript is to conceptualize the prevailing knowledge about the informal sector engagement in Sri Lanka tourism Industry. Though the research on the informal sector has been a growing field in the developing countries, the limited studies conducted about the informal sector engagement in Sri Lanka tourism industry is a significant problem. The empirical evidence brings new knowledge on informal sector engagement in Sri Lanka Tourism Industry to build the extent literature persistently. As the policy makers need the information about the informal sector for effective decision making, the organization and categorization of the information related to the area of the study is significantly important. This review paper is based on the current literature on the informal sector engagement in Sri Lanka Tourism industry and its impact to the formal sector.

Keywords: Informal Tourism Sector, Formal Tourism Sector, Sri Lanka Tourism

1. Introduction

Being a developing country for the last four decades, Sri Lanka has faced many economic challenges due to different civil conflicts at different times. One of the most vulnerable industries among them is the Tourism and Hospitality industry. As in many developing countries, Sri Lanka economy has internally classified as traditional and modern sectors, organized and unorganized sectors, urban and rural sectors and formal and informal sectors (Senanayake, Wimalaratana & Premaratne, 2016). The informal sector in any economy is the one that is neither taxed nor monitored by the government. According to the business dictionary, informal sector is the sector that includes the jobs which are not identified through the normal income sources and on that the taxes are not paid. It is an illegal activity in most of the countries. However, in some instances informal sectors are allowed at the rural economies to maintain an economic equilibrium. Informal sector sometime engages in unacceptable practices that are hard to be monitored. Australian Aid (2019) states that the Sri Lanka tourism industry is significantly driven by the informal sector and the government policy framework pays only a limited attention in managing the livelihood of the people who have engaged in the informal economic activities. This report also stated that due to the lack of awareness on the sector related value chain, Sri Lanka failed to execute the tourism strategic plan 2017. The informal sector engagement in Sri Lanka tourism has increased up to 60-70% during the last 10 years. Athukorala (2015) stated that 15.1 million guest nights were generated in the year 2014 and the informal sector

accounts 7.3 million guest nights which is a 50% contribution in terms of the guest nights are concerned during that year in Sri Lanka. The size of the informal sector in Sri Lanka accounts to 60% (TAN, 2020; MTDCRA, 2017). Many local tourism service providers in Sri Lanka that are registered with OTAs such as Booking.com, Expedia.com, Tripadvisor.com do not have proper licenses to operate as tourism service providers in Sri Lanka. Some of the unlicensed tourism service providers complain that outdated registration criteria do not allow them to register with authorities. Due to this Sri Lanka tourism loses the control over them and miss the chance of earning registration fee, TDL and other taxes. Huge sum of money is paid as commissions to the OTAs. This amount is 15-35% commission from the market price. Often this commission is untaxable and outflow of money from the country. Due to the competition in the market and inter-rivalry for price, most of the suppliers earn thin margins as their profits and they use undercutting as one of the business strategies for survival. Often the market prices of the tourism services are displayed through the internet and OTAs are the leading source for that. As the portion of the informal sector registered with OTAs is high, they have a supper control over the market price which is not healthy for the industry.

There are many regulations violations in Sri Lanka by the unlicensed tourism service providers and often they escape as there is no legal bond that they have signed with the authorities. Lack of entry barriers to the tourism industry has also enabled the Tuk-Tuk drivers and small taxi operators to become tourism service providers without any market orientation. Some TukTuk drivers have assaulted the tourists for refusing their services. As there is no legal right for a tourism service provider to operate in Sri Lanka without a license, they violate the tourism regulations in the country by operating as tourism service providers. Due to the competition in the online travel market, OTAs are registering more and more tourism service providers in Sri Lanka and most of them are unlicensed. As the informal sector has expanded its wings even bigger in the tourism industry during the last 10 years, the formal sector has been facing many challenges in the recent past. Objectives of this research paper is to identify the issues and challenges that are faced by the Sri Lanka tourism due to the informal sector engagement.

2. Literature Review

The informal sector has many critical concerns in economics and social sciences. The well-structured work patterns and formal work systems in many developed economies have low dominance in the informal economic activities compared to the developed countries (Jackson, 2019). The informal economy accounts more than 60% of the world's employed population. It exists in almost all the countries regardless of the level of economic development. But it is more common and dominating in the developing countries. Majority of the people enter informal sector not by choice. It is due to the lack of opportunities available in the formal economy and the absence of other means of livelihood (ILO, 2018). There are so many mythical beliefs and negative connections regarding the informal sector engagement in the economy. Encouraging them and making them feel elated about their involvement of economic development activities is needed to avoid their illegal practices (Jackson, 2019). Every economy has an informal sector. However, this sector in the developing countries is larger than the developed countries. The percentage of the informal sector engagement in the developed countries is 18.3% compared to the 69.6% in the developing countries in 2016 (ILO, 2018).

More than 2 billion people engage in informal commercial activities with 60% of workers and 80% enterprises in the developing countries (ILO, 2020). Expanding the commercial opportunities for the small enterprises in the developing countries is significantly important for a rapid economic

development (Maksimov, Wang & Luo, 2017). These enterprises that engage in coordinated commercial activities without proper legal registration are falling under the category of informal sector (Al-Mataani, Wainwright, & Demirel, 2017). Informal sector includes four types of informality: informal employment (casual employees in formal forms), self-employed workers such as housewives, informal enterprises that engage in business without proper legal license and the bazar traders (Narula, 2019). Though the large informal sectors cause issues, they contribute to development. These informal enterprises are individual players that perform labor intensive activities in most of the economies. The informal sector is largely appeared in the rural as well as low income urban population (Godfrey, 2011; Narula, 2018). The share of the informal sector in the South Asia is very much as 88% (ILO, 2018). This is mainly due to the historical trading patterns in South Asia with the formal and informal sectors than other regions in the world (Narula, 2019).

2.1 Challenges in Informal Sector Dominated Economy

The organizations in the informal sector employ less than ten employees and most of them are immediate family members. They are paid an irregular manner. No gender restrictions. Even children and elders engage in work. Employees gather knowledge and skills through on the job training than pre job training. There is no employer – employee relationship. Little or no appreciation by the owners, less attention to workers' rights (Senanayake, Wimalaratana & Premaratne, 2016). Informal enterprises receive little or no support from the government for managing the challenges they face such as lack of finance, lack of skills, poor location and networking, poorly defines regulatory frameworks and weak capabilities in terms of technology (Mbaye, Golub and Gueye. 2020). The high occurrence of informality is a major challenge for the sustainable development. The fundamental rights of the workers such as social protection, working condition, rules and regulation are bigger challenges in informal sector. It also has a negative impact on public revenue, economic, social and environmental policies and competition in the national and international markets (ILO, 2018). As the informality delay the economic and human development, governments want to move way from informality and drive the policies towards formal sector development (Narula, 2019). The informality of an economy is always considered as inferior due to limited space for business growth, lower prices and poor quality of the products they offer. The public policy often pays less attention towards the informal sector activities (Australian Aid, 2019).

The nature of informal sector has been formed with three characteristics: high women domination, lack of social protection and low unionization. Informal sector also faces many challenges such as accessibility to credit facilities, unsafe working conditions and harassment by the public authorities (Awojobi, 2014). Many of the employees in the informal sector face different kind of hardships. Limited job security, no insurance, no medical, limited occupational mobility, lack of emotional support and low wages. They are the most affected segment in the working society (Alam, 2012). The informal enterprises often escape from the labor market regulations, tax payments and other government interventions (Mbaye and Gueye, 2018). However, they prefer to have the access to public services such as water, electricity, telephone and remain ineligible for VAT payments (MCC, 2017). The informal enterprises are less productive than formal enterprises. They pay lower wages but grow fast like the formal enterprises due to the flexibility and regulation exceptions. As the informal sector is not governed by the regulations, the quality, safety and reliability of the products and services are very low. Due to the omission of tax and regulation obligations, the informal sector

often creates unfair competition in the market which impede growth of the formal economy (Mbaye, Golub and Gueye. 2020).

2.2 Informal Sector in Sri Lanka Tourism Industry

Many authors have defined the informal sector in different ways. The terms “unorganized” and “informal” are used in Asia interchangeably in their descriptions about the informal sector. Some definitions include the terms such as “not being formal”, “grey economy” and “unregulated” in their descriptions about this sector. Due to the lack of standardized definition about the informal sector, the countries have the flexibility to adopt a definition that is appropriate to the requirements of the system (Ntseane, 2019). Informal sector in Sri Lanka tourism can be defined as the businesses and other individuals that operate in the tourism industry without having a membership of Sri Lanka tourist board. This includes unregistered hotels and restaurants, unregistered DMCS, unregistered guides, unregistered tourism vendors such as batik shops, wood carving centers, spice gardens and other unregistered service providers in the tourism industry (Australian Aid, 2019). After ending the three decades war, Sri Lanka failed to exploit the opportunities to increase the investment and jobs with a strategic plan. The visitor numbers, investment projects and international interest had taken place very much organically without coordinated planning. The strategic guidance for brand positioning, policies and plans have not been consistently executed. These failures of strategic planning have created the avenues to form a powerful informal sector in Sri Lanka tourism (MTDCRA, 2017).

A large portion of the industry stakeholders have been categorized as the informal sector due to the failure of being registered with the SLTDA. The subsectors like homestays, food trails, historical trails, farm stays have not been identified as significant areas for the industry (Abeywardana & Priyadarshani, 2017). Due to the absence of data about the size of the informal sector in Sri Lanka tourism, it is difficult to state the exact size of the informal sector. However, according to the stakeholders in the industry, informal sector generates a significant contribution to the industry by creating job opportunities, catering to niche markets and generating a sizable income. Encouraging the informal sector enterprises to register with SLTDA is very important in this context (Ellepola, 2017). 15.1 million guest nights were generated in the year 2014 and the informal sector accounts to 7.3 million guest nights which is a 50% contribution in terms of guest nights are concerned during that year in Sri Lanka (Athukorala, 2015). SLTDA has estimated that the informal sector accounts to a 69% share in the Sri Lanka tourism industry that cause to reduce the much more needed tax revenue. After the Easter attack, they target to transform at least 70% of the informal enterprises to formal enterprises (Chandrasena, 2019).

Sri Lanka government has made a statement in 2019 budget reading that the establishments consists with more than 5 rooms should be registered with SLTDA. Most of these establishments are selling their rooms through OTAs such as Booking.com and Airbnb for years. The number of these supplementary accommodations are still unknown and the former DIG of police have been nominated to form an enforcement unit to find these establishments and penalize their owners by way of fine or imprisonment (Hospitality Insider, 2019). SLTDA has estimated that over 50,000 SME enterprises are operating in the Sri Lanka tourism industry and majority of them are not registered. The unregistered portion is approximately 60-70% in the industry and taking them to formal tourism economy is very much required. SLTDA has initiated provincial licensing to assist them to acquire the COVID-19 health certification to host the tourists in the future. SLTDA has also decided to relax the registration criteria (TAN, 2020).

2.3 Informal Tourism Sector vs Formal Tourism Sector in Sri Lanka

The supplementary accommodation is the highest portion in the informal sector in Sri Lanka tourism. Only around 28-32% are registered and the balance remain unregistered. These formal supplementary establishments have to pay 15% value added taxes (VAT), 2% nation building tax (NBT), 1% tourism development levy (TDL) and 10% Service Charge. These formal supplementary accommodations always face bigger challenges in facing the competition at the market as they are playing in the same field with the unregistered supplementary accommodation service providers those who don't pay taxes to the government (Miththapala, 2019; Ellepola, 2017). Sri Lanka informal tourism sector is fueled by the social media, networking and internet platforms. It has grown much faster than the formal sector from 2011. The low rates offered by the informal sector through the OTAs and other online channels have attracted more tourists. This has fuel to grow a new segment of adventure seekers who spend less for the accommodation and more for exploring and adventure. This segment is often called as "Affluent Backpackers". As there are no unique selling propositions to cater to this segment, the formal sector is losing their strength in Sri Lanka tourism industry (Emma, 2019).

The informal sector is playing a major role in promoting Sri Lanka for authentic and rustic experiences that has supported to earn the Lonely Planet's number 1 destination for 2019. However, there is a strong perception about the informal sector in Sri Lanka tourism that they suck the live blood out of the formal tourism sector in Sri Lanka as they are totally unregulated and exempted from tax payments (Miththapala, 2019). The formal tourism sector in Sri Lanka has been influenced by the informal sector growth, especially the expansion of informal accommodation. The informal sector has been dragging the overall tourism sector towards different direction. However, this sector has shown an indication of a decline post COVID-19 (Hettiarachchi, 2020).

3. Conclusion

The informal sector engagement in the economy is one of the most common incidents in the developing countries. Tourism has been one of the major industries in Sri Lanka that consists with more than 70% of the informal sector. After ending the 30-year war, Sri Lanka did not expect a tourism boom and the industry was not at all ready to face the demand for the tourism services in Sri Lanka. This is one of the major reasons to increase the informal sector engagement in Sri Lanka tourism industry. Though the informal sector plays a major role in Sri Lanka tourism, managing this sector effectively is needed to establish a sustainable tourism model in Sri Lanka. However, due to the lack of understanding about the tourism value chain by the policy makers in the industry (Australian Aid, 2019), Sri Lanka failed to understand the stakeholder categorization and regulation requirements at the right time to manage this informal sector engagement. The informal sector engagement in Sri Lanka tourism industry has influenced the industry in both positive and negative ways as explained in this paper. The formal sector has faced many challenges due to the informal sector engagement and they have also shown a lack of collaboration to solve the issues. This paper discussed the prevailing literature with empirical evidences about the informal sector engagement in Sri Lanka tourism industry. The paper also depicted which role the informal sector has played during the last decade to make Sri Lanka the leading destination in the world. However, most of the informal sector organizations are still struggling to make their presence in the industry after COVID-19. Though they are willing to come in to the formal process, no criteria have been developed for them to be registered as service providers in Sri Lanka tourism industry has become a major problem. As a result of this, Sri

Lanka tourism has failed to control informal sector and missed the chance of earning registration fee, TDL and other taxes.

Acknowledgement

This manuscript is a result of an extensive study on the prevailing literature on informal sector engagement in Sri Lanka Tourism. The appreciation is extended to all the previous authors for their valuable contributions to grow the extent literature. The support given by the industry professionals, SLTDA representatives, friends and the family members with their valuable comments to improve the quality of this paper is highly appreciated.

Conflicts of Interest

There are no conflicts to declare.

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