

ASSESSING THE SCALE AND STRUCTURE OF UNTAXED ECONOMY IN UZBEKISTAN

Alimardonov Gayratjon Nuralievich

Researcher, Research Center “Scientific Bases and Problems of the Development of the Economy of Uzbekistan” under the Tashkent State University of Economics

ABSTRACT	KEY WORDS
The article assesses the scale and structure of the untaxed economy in Uzbekistan. In addition, it reveals the essence of the concept of the untaxed economy. Moreover, the article analyzes the reasons and factors envisaging the wide spread of shadow economic activity in Uzbekistan, as well as provides considerations on the limitations of the full coverage of informal economic activity. The situation of entities engaged in the shadow economic activity in Uzbekistan in 2021-2023 has been analyzed and appropriate conclusions have been developed in reliance upon the research results.	Untaxed economy, social factors, cultural factors, social networks, poverty reduction, income distribution, formalization.

Introduction

The untaxed economy in Uzbekistan is an essential but complicated aspect of the country’s economic situation and requires a comprehensive investigation to fully understand its scale and structure. This shadow sector includes a wide range of activities, from small unregistered enterprises to informal labor arrangements, thus it is difficult to accurately evaluate them. In reliance upon the unique conditions of Uzbekistan, the untaxed economy has a developing character that is closely connected with the socio-economic structure of the country.

Understanding the scale and structure of the informal economy in Uzbekistan is very important for effective economic policy development and sustainable development. The untaxed sector often represents a significant part of economic activity, and without a clear understanding of its scale and structure, industry experts may not take into consideration important contributors to the national economy. By gaining an understanding of informal practices, unregistered enterprises and informal labor arrangements, professionals can explore the specific needs and challenges of this sector and ultimately develop targeted strategies that can solve the issue. Furthermore, an unambiguous understanding of the untaxed economy can help create policies that promote inclusive growth, as it allows for the integration of informal workers into the core business. By its essence, comprehensive knowledge of the scale and structure of the untaxed economy creates a solid basis for making rational decisions and ultimately ensures sustainable economic development in Uzbekistan.

The historical evolution of the untaxed economy in Uzbekistan is originated from the country's complex socio-economic and political trajectory. During the Soviet Union, Uzbekistan was an integral part of the centrally planned economy, characterized by state-controlled enterprises and collective farms. The breakup of the Soviet Union in 1991 was a turning point that resulted in the emergence of independent Uzbekistan. The transition to a market economy resulted in the implementation of the economic reforms, but it also created shadow economic activity as individuals sought alternative means of livelihood outside the formal sector.

Literature Review

There are different opinions on the concept of the untaxed economy and it is still a relatively new research topic. For example, Chen and Carré (2020) argue that although the concept of informality (untaxed nature) has been criticized by many scholars as being “too fuzzy and the formal-informal dichotomy too binary”, it cannot be abandoned in its definition. As Harriss-White (2020) points out, a clear description of what should and should not be included in the untaxed economy, remains important for positive, normative and measurement purposes.

The untaxed economy is a complex phenomenon, which determinants and consequences depend on the characteristics of the units involved, macroeconomic and institutional factors. The multifaceted nature of the untaxed economy explains the lack of a comprehensive theory of informality in the literature that is appropriate for both developing and developed countries. Indeed, a theoretical perspective that explains the emergence of the untaxed character (informality) as a survival strategy in a developing country may be ill-suited to understanding the widespread nature of the untaxed economy in developed countries (Goel and Nelson, 2016). Therefore, in order to avoid misunderstandings among scholars, it is crucially important to clarify which type of informality the theory aims to explain.

Dell'Anno (2007) proposes a micro-based macroeconomic modeling framework in which, in addition to taxes, a worker's choice to engage in informal activity depends on univariable input costs, lending market imperfections, and labor force composition (i.e., share).

Ulyssea (2018) has developed a competitive equilibrium model in which different firms can exploit two thresholds of informality: three different types of informal firms co-exist in an economy (“survival firms” are too inefficient to operate formally even if entry costs are removed; “parasitic firms” are sufficient to survive as formal firms after entry barriers are removed, but prefer to remain informal; “informal firms” (they are kept out of formality due to high entry costs, but if they are removed, they become formal and improve).

Dell'Anno (2021) divides the potential drivers of the untaxed (informal) economy into six categories. These categories deal with: the taxation system (i.e. measured as total tax burden, tax mix, tax complexity, marginal tax rate); regulatory framework (i.e. overall regulatory burden, occupational health and safety legislation); labor force composition (i.e. self-employment rate, unemployment rate, significant number of illegal immigrants, presence of unskilled workers); enforcement system (i.e. detection probability, penalty rates, severity of criminal penalties); tax ethics and institutions (i.e. historical background, fairness of public policy, corruption, quality of political institutions, media and economic freedom).

In reliance upon the considerations specified above, it is obvious that research on the untaxed economy concept is still to be done, and clear conclusions have not yet been formulated.

Analysis and Results

In the early years of independence, economic liberalization and privatization processes resulted in the growth of unregistered small businesses and informal trade. The untaxed (informal) economy further expanded as people struggled to adapt to the new market conditions, leading to widespread underemployment and unregulated business beyond official statistics. Informal economic activity has become a coping mechanism for many in this period of economic change.

Over the following years the untaxed economy continued to play an important role in Uzbekistan under the impact of such factors as bureaucratic barriers, limited formal employment, and cultural norms. Despite the government's efforts to formalize the economy, informal practices persist and shape the economic process in ways that require comprehensive verification. Understanding this process is very essential to undertake effective policy measures in the current situation of the untaxed economy in Uzbekistan. The wide spread of untaxed economic activity in Uzbekistan can be referred to the combination of cultural and socio-economic factors that have shaped the national economic environment (Table 1):

In reliance upon the data in Table 1, understanding these cultural and socioeconomic factors provides important insights into the drivers of untaxed economic activity in Uzbekistan. Policymakers aiming to solve untaxed sector challenges and encourage formalization must consider this complex interaction of culture, history, and socio-economic conditions.

Table 1 Reasons and factors for widespread of the untaxed economic activity in Uzbekistan¹

Cultural standards and traditions	Cultural values that emphasize self-reliance and entrepreneurship support the adoption of informal activities. In Uzbekistan, where family and community ties are important, untaxed economic practices often conform to traditional assumptions and community support networks.
Historical inheritance	The historical legacy of Soviet-era central planning has made a lasting impact. The transition to a market-oriented economy created difficulties and uncertainties, which encouraged individuals to turn into untaxed economic activities as a means of adapting to changing conditions.
Limited formal employment opportunities	Formal employment opportunities may be limited, particularly in certain areas or sectors. As a result, people turn to informal activities to earn income and support their livelihoods out of economic necessity.
Bureaucratic barriers	Complex bureaucratic rules and procedures and regulatory barriers associated with formal business registration and compliance prevent individuals from entering the formal sector. Informal activities provide a more affordable and flexible alternative for those seeking economic opportunities.
Informal social networks	Informal economic activities often develop within existing social networks. Trust and familiarity within communities foster the growth of informal enterprises, as people prefer to do business with people they know or within their social circle.
Flexible work schedule	Informal employment offers a degree of flexibility not always available in formal employment.
Economic inequality	Socio-economic disparities can push people to engage in untaxed activities as a survival strategy.
Lack of access to financial services	Limited access to formal financial services may be an essential factor. In the absence of formal banking, individuals may rely on informal financial networks, further blurring the lines between formal and informal economic activity.

¹Developed by the author in reliance upon the literary sources studied.

Measuring the scale of the untaxed economy presents many challenges due to its inherently unregulated and often hidden nature. Key challenges in determining the scale of the untaxed economy, including unregistered businesses and informal employment, include:

- unregistered enterprises and informal labor structures often operate outside official sources, making it difficult to collect accurate data. Individuals engaged in untaxed activities may not voluntarily disclose their involvement, leading to under-reporting and incomplete data;
- the untaxed economy is dynamic and includes a wide range of activities. Traditional economic measurement tools may not capture the diverse forms and scales of untaxed enterprises, preventing a full representation of its scale and structure;
- untaxed employment arrangements, including self-employment, and outside official statistical data contribute to the complexity of the assessment. The lack of formal contracts, wage data and official documents complicates determining the level of untaxed employment;
- most informal transactions are done in cash, avoiding formal financial systems. Dependence on cash transactions and lack of formal financial reporting prevent proper monitoring and measurement of economic activity in the untaxed sector;
- due to data limitations, researchers often resort to estimation methods that may introduce uncertainties in the accuracy of measurements. Measuring the scale of the untaxed economy involves assumptions that do not fully reflect its complexity and leads to misleading perceptions;
- untaxed economic activities, particularly those related to agriculture or seasonal work, may experience significant changes throughout the year. Traditional measurement approaches have a hard time accurately accounting for these seasonal and cyclical fluctuations;
- globalization has facilitated cross-border untaxed activities and adds additional complexity to measurement efforts. Informal cross-border trade and economic interactions further complicate the task of accurately measuring the scale of the untaxed economy within national borders;
- some formal businesses may be engaged in untaxed practices to reduce costs or avoid certain regulations. Differentiating between formal and informal aspects within a single entity creates difficulties, making it difficult to classify enterprises correctly.

Moreover, traditional economic indicators often fall short of capturing the full range of untaxed economic activity due to a number of inherent limitations. Traditional economic indicators rely mainly on official sector data such as registered enterprises and official labor journals. This focus excludes the large contributions of unregistered enterprises and untaxed labor arrangements, giving an incomplete picture of economic activity. The main limitations are presented in Figure 1.

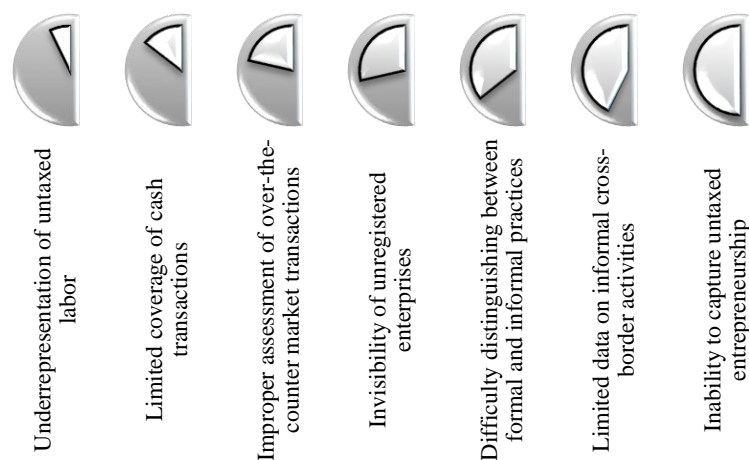


Figure 1. Restrictions on full coverage of untaxed economic activity²

² Developed by the author.

If we look at Figure 1, each restriction makes its own impact, so it cannot represent the full extent of untaxed economic activity. For example, considering these in sequence, standard employment indicators often do not take into account untaxed employment arrangements, including self-employment and employment outside of official statistics. This omission results in an underestimation of the true extent of employment in the untaxed economy.

Traditional economic indicators rely heavily on transactions within formal financial systems, ignoring the spread of cash transactions in the untaxed economy. Untaxed economic activities often involve cash transactions, making them less visible in traditional financial data.

Traditional indicators struggle to measure the barter exchange and non-market transactions prevalent in the untaxed sector. Informal economic activity often involves non-monetary exchanges or transactions outside of traditional markets, bypassing traditional means of measurement.

Many untaxed enterprises and businesses operate without formal registration, making them invisible to traditional business registration databases. Consequently, traditional indicators cannot reflect the economic contribution of this unregistered sector.

Traditional indicators cannot effectively distinguish between formal and informal practices in businesses operating in both sectors. Herewith they often lack the data on the informal cross-border trade and economic interactions. The globalization of the untaxed activity is not adequately reflected in traditional economic indicators, ignoring the international dimensions of the untaxed economy.

Business activity within the untaxed economy is not adequately reflected by traditional indicators. The innovation-based aspects of informal entrepreneurship are often not taken into consideration hindering a comprehensive understanding of economic change. Overcoming these limitations requires a shift to more comprehensive measurement approaches that capture the complexity of informal economic activity.

According to experts, the share of the shadow economy in our country is 40 percent and is estimated at approximately 32 billion USD. This value is mainly due to the secondary market of real estate and vehicles, wholesale and retail trade, services, smuggling of tobacco products, trafficking of illegal goods, agriculture, etc³.

Based on Table 2, we will analyze the data provided on the untaxed economy in Uzbekistan from 2021 to 2023 from the scientific point of view. The consolidated national indicator for the Republic of Uzbekistan demonstrates the trend of growth of both the number of entities and sales, during this period the total amount of sales accounted for 24 225.8 billion UZS. It shows the overall economic activity in the untaxed sector.

³ <https://kun.uz/news/2023/10/03/ozbekistonda-yashirin-iqtisodiyot-ulushi-32-mlrd-dollariga-baholanmoqda>

Table 2 Analysis of the condition of untaxed economic entities in 2021-2023⁴, billion UZS

№	Region	2021-2023			including								
					2021			2022			January – September 2023		
		number	sales amount	purchase amount	number	sales amount	purchase amount	number	sales amount	purchase amount	number	sales amount	purchase amount
Throughout the Republic, total		2424	24 225,8	21 023,6	525	2 991,7	3 848,9	532	8 116,4	7 172,5	1367	13 117,7	10 002,2
1	Republic of Karakalpakstan	113	353,1	368,7	16	39,9	93,8	23	152,8	172,4	74	160,4	102,5
2	Andijan region	197	2 410,3	2 420,8	69	374,1	545,3	46	1 115,6	1 308,1	82	920,6	567,4
3	Bukhara region	71	179,2	108,3	20	26,5	35,9	13	81,4	34,0	38	71,3	38,4
4	Jizzakh region	56	157,2	259,9	30	74,5	209,3	10	57,2	38,0	16	25,5	12,6
5	Kashkadarya reg.	139	712,7	582,5	48	48,6	109,1	25	131,5	107,5	66	532,6	365,9
6	Navoi region	61	393,1	397,0	6	3,2	2,1	8	30,9	17,9	47	359,0	377,0
7	Namangan region	210	2 019,3	1 244,3	37	450,4	262,2	53	508,6	333,6	120	1 060,3	648,5
8	Samarkand reg.	92	542,8	497,1	12	29,3	106,2	15	71,3	43,5	65	442,2	347,4
9	Surkhandarya region	72	595,6	585,9	23	241,7	284,7	12	39,8	45,1	37	314,1	256,1
10	Syrdarya region	114	475,3	167,7	13	243,9	31,1	10	17,9	17,4	91	213,5	119,2
11	Tashkent region	382	5 388,8	4 804,2	45	297,4	661,3	102	1 749,2	1 436,7	235	3 342,2	2 706,2
12	Fergana region	240	2 342,1	1 838,4	108	777,1	857,8	51	600,4	426,4	81	964,6	554,2
13	Khorezm region	84	225,2	191,9	12	13,7	8,8	16	98,8	22,2	56	112,7	160,9
14	Tashkent city	592	8 377,4	7 495,1	85	317,8	579,6	148	3 461,0	3 169,7	359	4 598,6	3 745,8
15	Large taxpayer inspectorates	1	53,6	61,7	1	53,6	61,7	0	0,0	0,0	0	0,0	0,0

The difference between the regions is clearly visible, Tashkent city is distinguished by the largest number of enterprises and trade. This corresponds to the expected results due to the economic significance of the capital. Some regions, such as Andijan, Namangan and Fergana, have remarkable indicators, while other regions, such as Karakalpakstan and Navoi, have relatively low levels of activity in the untaxed economy.

A closer look at the annual distribution reveals changes in sales by number of entities and regions. The data provide insight into the networks that drive untaxed economic activity in each region. Analysis of the distribution of entities by sector and the volume of sales allows for a more detailed understanding of the structure of the untaxed economy.

Taking into consideration the observed disparities and general trends, recommendations should be tailored to solve specific challenges in each region. For example, regions with low levels of formalization can benefit from targeted incentives and support programs.

⁴ Developed by the author in reliance upon the data of the Tax committee

Table 3. Analysis of enterprises engaged in “cash-out transactions”⁵, billion UZS

№	Period	number	Sales amount	Purchase amount
TOTAL		4 848	48 451,5	42 047,1
1	2020	2 424	24 225,8	21 023,6
2	2021	525	2 991,7	3 848,9
3	2022	532	8 116,4	7 172,5
4	January – September 2023	1 367	13 117,7	10 002,2

From the data in Table 3, there is a significant change in the amount of sales and purchases from 2021 to 2022. 2 424 transactions totaling 24 225.8 billion UZS were made and the volume of purchases amounted to 21 023.6 billion UZS in 2020. In 2021, the number of transactions increased by 525, and the amounts of sales and purchase amounted to 2 991.7 billion UZS and 3 848.9 billion UZS respectively. In 2022 the amount of sales (8 116.4 billion UZS) and purchases (7 172.5 billion UZS) increased by 532 transactions. In January-September 2023 1 367 transactions were made and their sales and purchase amounts were 13 117.7 billion UZS and 10 002.2 billion UZS respectively.

Consolidated data for the entire period demonstrates a significant increase in cash transactions. The total number of transactions has reached 4 848, which total sales amount constituted 48 451.5 billion UZS and the purchase amount accounted for 42 047.1 billion UZS. Calculating the percentage change of sales and purchase amounts from year to year enables to understand the growth rates of cash transactions.

Examining which sectors or industries contribute the most to these cash transactions can provide a more detailed understanding of economic activity. Taking this fact into account, we present the analysis of the share of the industrial sector in the untaxed economy (Table 4).

Table 4. Analysis of the industry share in the untaxed economy⁶, in percent

№	Industry	Share in the untaxed economy(%)	Types of business related to the field
1.	Consumer domestic services	22.1	House cleaning, hairdressing, beauty salons, dry and chemical cleaning, catering, pest control, computer maintenance, security, healthcare, pet care and others.
2.	Hospitality industry	16.4	Restaurants, cafes, bars, dining places, hotel service.
3.	Retail services	15.6	Retail stores, mass (or open) markets, etc.
4.	Construction	15.6	Construction and assembly works, home repair services, etc.
5.	Others	30.3	Automotive sales and maintenance, agriculture, transportation, tourism, real estate (including rentals), recycling, freelancers, entertainment, leisure and other similar services.

⁵Developed by the author in reliance upon the data of the Tax Committee

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The information about the contribution of the industrial sector to the untaxed economy in Uzbekistan is analyzed in reliance upon the data presented in Table 4. The consumer domestic services sector contributed 22.1% to total industrial activity. It includes a variety of household services such as house cleaning, beauty salons, food cooking, computer maintenance, home security, health care, and pet care.

The hospitality industry contributes 16.4% to the industrial sector. This includes services provided by hospitality services in restaurants, cafes, bars, entertainment venues and hotels.

Retail trade makes up 15.6% of the industrial sector. This includes retail stores, public (or open) markets, and other commercial platforms that contribute to overall economic activity.

Construction activity contributes 15.6% to the industrial sector. This includes construction and assembly works, home repair services and other related construction enterprises.

Others constitute 30.3%. This sector includes various services including car sales and technical services, rural development activities, transportation services, tourism, real estate rental, re-employment initiatives, freelancers, entertainment and other related services.

The data demonstrates the different types of businesses in the industrial sector. The distribution of shares by different sectors gives an idea of the relative importance of each category in the formal economy.

The inclusion of various services such as healthcare, consumer services and construction offers a stable and flexible industrial sector capable of meeting diverse economic needs. Identifying the sectors with high percentages can provide valuable information for investors and indicate areas with potential for further expansion and development.

Although the presented data and analysis are focused on the formal industrial sector in Uzbekistan, it does not provide a direct understanding of the scales and structure of the untaxed economy. However, we can make some comments on this issue. The data primarily highlights the contribution of various formal sectors such as consumer services, hospitality, retail, construction and others. This highlights the significance of these formal sectors in the overall industry share.

The lack of specific data on the untaxed economy in the analysis indicates difficulties in measuring and describing untaxed economic activity. The untaxed economy often operates outside formal channels and may not be adequately captured by traditional economic measurements.

The “Others” category, which represents 30.3 percent of the industrial sector, refers to the potential presence of untaxed businesses in various service sectors. Untaxed economic practices such as freelancing, unregistered businesses, and certain service operations may be included in this miscellaneous category.

In order to make clear conclusions about the scales and composition of the untaxed economy, special studies focused on informal economic activities are crucially important. It is essential to rely on methodological research, including surveys, interviews and other methods, to gather information about unregistered enterprises, informal operations and untaxed labor practices.

It should be noted here that significant contributions of the formal and informal (untaxed) sectors should be recognized. Understanding the dynamics of the untaxed economy is quite essential to developing effective interventions that address the needs and challenges of businesses operating outside of formal regulation.

Conclusion

Summing up, while the presented analysis highlights the untaxed industrial sector, making a conclusion about the scale and structure of the untaxed economy requires a specialized research focused on informal activities. It would not be wrong to say that the untaxed economy in Uzbekistan was developed by the complex interaction of cultural and historical factors deeply rooted in the national heritage. The historical inheritance of Soviet-era centralized planning, along with the subsequent transition to a market economy, has resulted in a changing process in which people manage uncertainty through untaxed economic practices.

Rich traditions of entrepreneurship deeply embedded in the culture of Uzbekistan contribute to the widespread distribution of informal business and trade. Relationships based on trust, which is a peculiarity of Uzbekistan's society, further contribute to the growth of informal economic transactions in social networks. Resilience embedded in the cultural fabric enables people to adapt to economic changes, while informal activities serve as the mechanisms for survival.

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