Available online at www.sciencedirect.com

ScienceDirect

Procedia Economics and Finance 35 (2016) 173 – 178

Procedia Economics and Finance

www.elsevier.com/locate/procedia

7th International Economics & Business Management Conference, 5th & 6th October 2015

Are Shadow Economy and Tourism Related? International Evidence

Badariah H. Din[*a], Muzafar Shah Habibullah[b,c], A.H. Baharom[d], and M.D. Saari[b,c,e]

[a]College of Law, Government and International Studies (COLGIS), Universiti Utara Malaysia
[b]Financial Economics Research Centre (FERC), Faculty of Economics and Management, Universiti Putra Malaysia
[c]Department of Economics, Faculty of Economics and Management, Universiti Putra Malaysia
[d]Taylor's Business School, Taylor's University
[e]Institute of Agricultural and Food Policy Studies, Universiti Putra Malaysia

Abstract

The present study attempts to investigate whether shadow economy and the tourism sector are related. In the European countries, Schneider reported that 20 to 25 per cent of the shadow economy is represented in the tourism-related industries – wholesale and retail, automotive and motorcycle sales and maintenance; transportation, storage and communications; and hotels and restaurants. For the tourism sector, the services given by operators (unregistered and/or underreporting) operate in the shadow economy will ultimately wiped off the map of high quality tourist destinations and destroyed the development of the tourism industry itself. This study examines the short-run and long-run relationships between international tourism receipts and shadow economy for 149 countries over the period 1995-2008. We use a generalized one-step error-correction model (ECM) in combination with a system Generalized Method of Moments (GMM) to explore the long-run relationship between these two variables. Our results suggest that tourism receipts and shadow economy are cointegrated. This implies that shadow economy and the tourism industry worldwide are related in the long-run. The long-run elasticities indicate a negative impact of the shadow economy on the tourism sector suggesting that increase in shadow economy activities will adversely affecting the tourism industry.

Peer-reviewed under responsibility of Universiti Tenaga Nasional

Keywords: Tourism, Shadow economy, Governance, Error-correction, System GMM

[*] Corresponding author. Tel.: +604-9287922; fax: +6049284205.
*E-mail address:*badariahdin@uum.edu.my

Peer-reviewed under responsibility of Universiti Tenaga Nasional
doi:10.1016/S2212-5671(16)00022-8

1. Introduction

The tourism sector is an important driver for economic growth by contributing foreign exchange earnings, increasing wealth and provides employment and business opportunities for the communities. The tourism industry can also play a leading role in the alleviation of poverty particularly in the developing economies. The World Travel and Tourism Council (WTTC, 2014) reports that the tourism industry contributed 9.5 per cent of the global gross domestic product, 8.9 per cent of the worldwide total employment and 5.4 per cent of the world's export in 2013. During the same period, the tourism sector, in terms of international tourist arrivals have reached a record 1.1 billion arrivals worldwide, with USD1160 billion in international tourism receipts. International tourism receipts are the earnings generated in destination countries from expenditure on accommodation, food and drink, local transport, entertainment, shopping and other services and goods. Europe share the largest number of international tourist arrivals (563.4 million) followed by Asia and the Pacific (248.1 million), the Americas (167.9 million), Africa (55.8 million) and the Middle East (51.6 million). In terms of growth, the Asia and the Pacific recorded a 6 per cent increase in international tourist arrivals, followed by Europe and Africa (5.4 per cent), and the Americas (3.2 per cent).On the other hand, the Asia and the Pacific region (+8 per cent) recorded the largest increase in international tourism receipts, followed by the Americas (+6 per cent) and Europe (+4 per cent). However, for the year 2013, the Middle Eastern countries experienced a decrease in both international tourist arrivals (-0.2 per cent) and international tourism receipts (-1.9 per cent)(WTO, 2014).

Tourism has become one of the largest and fastest growing industries (UNEP, 2013). The importance of tourism is not only limited to its contribution to the nation's income, job and business opportunities, but it is also importance as it involves diverse tourism-related industries as well. The tourism value chain incorporates many sectors of the economy through both the backward and forward linkages: tourism needs the development of basic infrastructure services such as energy, telecommunications and environmental services; agriculture, manufacturing and other support services; and the tourists need supplying services from the financial, telecommunications, retail, recreational, cultural, personal, hospitality, security and health services, among others (UNEP, 2013). However, it has been recognized that the prevalence of the shadow economy can be an obstacles that can limit and disrupt the development of the tourism industry (Smith, 2011).

As pointed out by Webb et al. (2013), Armbrecht and Carlback (2011) and Smith (2011), shadow economy will affect competition and progress in the tourism sector; loss of revenue since tax evasion is prevalence in the shadow economy and fund cannot be plough back into the tourism sector, thus impairing the industries potential for growth and development; avoid labour, health and environmental regulations – with untrained staff without any social security and with working conditions that does not follow any health and safety regulations, and using harmful fuels, chemicals and other raw materials creating negative externalities to the environment and local communities. Armbrecht and Carback (2011) stress that "the unfair competition due to tax evading activities potentially affects serious businesses' possibilities to stay on the right side of the law and consequently the tax morale in the industry and in the country". Furthermore, less investment and new talent could then speed up the downward spiral of the tourism industry.

The purpose of the present study is to investigate the long-run relationship between tourism and the shadow economy in 149 countries for the period 1995-2008, by using the error-correction model combined with the system Generalized Method of Moment estimator.

The paper is organized as follow. In the next section we discuss some related literature relating tourism, crime and shadow economy. In section 3 we present the method used in the analysis. Section 4 elaborates the results, while the last section contains our conclusion.

2. Tourism, crime and the shadow economy

The number of tourist arrivals has been linked to the level of safety of the destination countries. It has been pointed out that the developing countries and particularly the least developed countries suffers from law and order problem and therefore a risk to potential tourists (Levantis and Gani, 2000; Perry and Potgieter, 2013; Moyo and Ziramba, 2013). Altindaq (2014) point out that besides terrorism and war, countries with higher crime rates will receive fewer visitors from abroad. The negative impact of terrorism on international visitor demand are supported by Fleisher and Buccola (2002), Smyth et al. (2009), Feridun (2011), and Drakos and Kutan (2003). On another note, organized crime