

Business Case: Sky High Industries (Pvt.) Ltd. – Formalization Journey

1. About the Enterprise

Sky High Industries (Pvt.) Ltd., established in 2008 and located in Karachi, is a medium-sized auto parts manufacturer registered with the Securities and Exchange Commission of Pakistan (SECP). Since inception, the enterprise has maintained its formal status by fulfilling all procedural and regulatory requirements. The company employs 150 workers, of which 10 are registered with the Federal Board of Revenue (FBR), 100 are enrolled with Social Security and Employees' Old-Age Benefits Institution (EOBI), while the remaining are engaged on contractual or daily-wage arrangements.

Sky High Industries is an approved vendor of Honda Atlas, supplying precision auto components in compliance with OEM requirements. The company maintains strong linkages with its supply chain, where more than 70% of vendors are registered and formal. However, due to limited availability of formal raw material suppliers, the enterprise is sometimes compelled to procure from informal sources, creating challenges in record-keeping and compliance.

2. Pre-Formalization Status

Unlike many SMEs that begin informally, Sky High Industries formalized from the outset. Registration with SECP, FBR, EOBI, and Social Security laid the foundation for structured operations. Despite this, partial informality persists within its labor structure and in segments of the supply chain. The reliance on contractual labor and informal procurement reflects systemic challenges rather than strategic choices, as compliant suppliers are often unavailable in certain product categories.

3. Why They Formalized to Formalize

Discussions with the company director highlighted several benefits of maintaining formal status:

- **Market Access** – Formalization allowed the company to qualify as a vendor to. **Honda Atlas, a leading OEM and ready to opt any OEM compliance**
- **Business Opportunities** – Registration enabled participation in government procurement processes and vendor development programs.
- **Credibility & Growth** – Documented compliance improved trust with banks, regulators, and large buyers.

- **Supply Chain Integration** – Over 70% of its inputs are sourced from registered companies, supporting traceability and transparency. **During the last two years, formalization of supply chain goes up from 50% to 70%**

4. Challenges Enterprise Faced

Despite its commitment to formality, Sky High Industries faces several structural hurdles:

- **Partial Informal Procurement** – Limited availability of registered suppliers for raw materials forces reliance on informal vendors.
- **Employee Registration Gaps** – Contractual and daily wage workers often remain outside EOBI and Social Security coverage.
- **Tax Burden & Compliance Costs** – Advance taxation, multiple audits, and digital system inefficiencies increase operational costs.
- **Access to Finance Constraints** – High interest rates and lengthy loan processing reduce SMEs' ability to expand and modernize.
- **Weak Institutional Support** – Corruption and poor facilities for the labor in ESSi and EOBI discourage workers from seeking formal registration.



5. Strategies Enterprise adopted

- Engaged professional consultants to handle registrations and compliance
- Workforce training programs by OEMs and formal labor registration to bring them in the system
- Introduced processes and quality control systems

6. Recommendations from the Enterprise

The director of Sky High Industries emphasized several incentives and reforms that could accelerate SME formalization:

- **Tax & Finance Reforms**
 - Reduction in advance taxation for SMEs.
 - Lower interest rates and simplified loan processing.
 - Awareness programs on tax schemes and compliance.
 - Incentives such as rebates on international travel, trade fair participation, and school fee discounts for registered taxpayers.
- **Employee Welfare & Social Security**
 - A tri-party contribution model (employer–employee–government department) for EOBI and Social Security.
 - Issuance of standardized employee cards to ensure registration and benefit access.
 - Institutional reforms in EOBI and ESSI to curb corruption and improve service delivery.
- **System Improvements**
 - Digitalization of FBR and related processes for ease of compliance.
 - Introduction of third-party audit systems for transparency.
 - Awareness campaigns for SMEs on the benefits of formalization.

7. Outcomes of Formalization

- Recognition as a trusted OEM vendor (Honda Atlas and others).
- Increased credibility with banks, regulators, and industry stakeholders.
- Enhanced competitiveness by sourcing mostly from formal supply chains.
- Steady employment opportunities for 150 workers with partial social protection coverage.
- Readiness to expand further into government procurement and potential export opportunities, subject to improved financing and compliance environment.

8. Lessons Learned

- **Starting formal brings long-term advantages:** By registering with SECP and complying with regulations from the outset, Sky High Industries gained early credibility, avoided later transition shocks, and positioned itself for OEM contracts.
- **Partial informality limits efficiency:** Even when the enterprise is formal, reliance on unregistered suppliers or contractual labor complicates record-keeping and weakens compliance. A fully formal supply chain and workforce improve consistency and accountability.

- **Employee welfare drives loyalty:** Workers are more likely to value formal systems when social security and EOBI actually deliver benefits. Weak services reduce employee trust and push them toward informality.
- **Incentives matter more than penalties:** The enterprise learned that supportive measures—such as easier access to finance, lower interest rates, and recognition for tax compliance—are more effective than punitive approaches in encouraging SMEs to stay formal.
- **Partnerships are essential:** Collaboration with OEMs, industry associations, and institutions like ILO can strengthen advocacy, training, and awareness, making the formalization journey smoother for SMEs.

9. Conclusion

The journey of Sky High Industries demonstrates how early adoption of formalization can enable SMEs to integrate into structured supply chains and attract high-value clients like OEMs. However, the persistence of informal practices in labor management and procurement reveals systemic gaps in Pakistan's regulatory and institutional framework.

If supported with incentives such as reduced taxation, accessible financing, and stronger employee welfare mechanisms, companies like Sky High Industries can become role models for SME formalization, contributing to employment generation, value addition, and integration into national and global value chains. Development partners such as the ILO, alongside government institutions, can play a pivotal role in designing incentive-driven systems that bring both employers and employees into the formal economy.