8.1. Conclusion

This thesis is focused on description and analysis of the economic performance (through contribution to output and employment generation) of the informal sector during the liberalization period. Liberalization is measured by openness indices and inter-sectoral linkages. Impact of liberalization on growth contributions of informal sector is captured by openness indices. Impact of liberalization on technical efficiency and components of productivity of the informal enterprises is estimated by inter-sectoral linkages. Economic determinants of informal sector’s employment are estimated by Probit model to derive implications on policy factors for promotion of employment generation in informal sector. Overall conclusions and implications of the study are obtained from within the descriptions and analyses of the entire thesis.

1. Characteristics of enterprises in the informal sector are essentially different from unorganized sector in the manufacturing and services sectors. Thus, the unorganized sector should be divided into the informal and non-informal unorganized sectors for analytical and policy purposes.

2. Both the organized and unorganized sectors have remarkable contribution and showing increasing trends in absolute terms, but unorganized sector’s contribution in NDP is higher than that of the organized sector in terms of its percentage shares. Although there is a decreasing trend in the percentage share of unorganized sector in recent years, the share continues to be higher. Although sub-sector- I (agriculture, forestry, logging and fishing) has been making major contribution to the total unorganized sector’s growth, it has decreased over time rather drastically after the implementation of WTO norms. In the non-agricultural unorganized sector, sub-sector-VI (trade, hotels and restaurants) has contributed significantly to the growth. In the recent years (phase-VI), the contribution of the sub-sector-VII (transport, storage & communication) to both the unorganized and organized sectors’ growth has
increased due to special attention of the policy makers on the information and communication technology (ICT).

3. The formal sector’s employment increases due to the increase of informal employment in the formal sector. This is due to the fact that liberalization exposes all the formal units to the inherent free market competition. So, in a bid to reduce cost of production through changing their organization of production and, thereby, the percentages of contract work in the formal units are increasing overtime. Moreover, the employment elasticity for the entire informal sector is higher vis-à-vis the formal sector, implying that the informal sector can accommodate more labour force owing to an increase in income due to its uses of labour intensive production technique. Due to presence of regulations in formal sector pertaining to labour wage rates, higher employment generation may not be profitable.

Given the constraint in the formal sector’s employment, it is important to explore opportunities for promotion of the informal sector from the viewpoint of employment generation. In both developed and underdeveloped states, education and migration are found the main policy variables for employment generation. The person who doesn’t have any general or technical education possess higher probability to engage in the informal sector and as education increases their probability to get absorbed in the informal sector decreases. This is due to the fact that the illiterate and technically uneducated persons are unable to find jobs in the formal sector and they have the only option to get absorbed in the informal sector due to its easy entry. Since more mobility creates more opportunity to find better jobs, better migration facilities is the another important policy variables.

4. Trade liberalization has significant and positive impact on the informal sector’s growth. Moreover, the vertical inter-firm relationship through sub-contracting between the organized and unorganized manufacturing sector has significant and positive impact unorganized manufacturing sector. The share of labour income decreases in the organized sector decreases after liberalization (i.e., after 1991), while it remains same in the unorganized sector
as before. Our interpretation is that liberalization encourages the use of modern capital intensive technology in the organized sector, thereby enhancing the share of capital income overtime which in turn reduces the share of labour income.

5. Both the formal and informal sectors have positive externality effect and they are interdependent. With an increase in the marginal productivity differences between the formal and informal sectors, the externality effect of the formal sector decreases, while the externality effect of the informal sector increases. Even if the informal sector is less productive, it still has a large externality effect besides making a significant contribution to economic growth. Although the formal sector’s externality impact is lower, it is positive and significant. Further, both domestic and foreign investments make a positive contribution to economic growth.

6. Lack of markets or competition from larger units, enterprises operating within the household premises and enforcement of regulation are positively related to inefficiency in both the states. First, the informal firms face the problem of competition with larger units for capturing a market share. Further, firms producing their products within the household premises are more inefficient than the ones operating outside the household premises. This is due to the fact that the informal enterprises operating within the household premises are traditional in nature producing mainly consumer goods and enjoy a relatively low share of market surplus, while the enterprises functioning outside the household premises are relatively more modern and bigger in sizes which produce both consumer and capital goods. Moreover, the enforcement of regulation makes the firms more inefficient due to the extra cost of regulation. In fact, the enforcement of regulation making firms more inefficient, throws up a question, is the formalization of informal sector through enforcement of regulations really helpful for the informal enterprises as well as for the entire economy?

7. The average TFPG of the non-informal sector is higher as compared to the informal sector. The mean technical efficiency change and technological
change are also higher in the non-informal sector than those of the informal sector. Technological change exhibits a major contribution to TFPG in respect of both the informal and non-informal sectors. As compared to technological change, change in efficiency is quite low for both the sectors. Moreover, pure efficiency change and scale efficiency change are also much higher in the non-informal sector.

8. The informal sector is concentrated heavily in own account enterprises, whereas the non-informal unorganized sector concentrates only in directory manufacturing enterprises (DME). Due to large in size, DME avails the advantages of economies of scale which, in turn, helps the units for more growth in terms of total factor productivity growth. The main reason for productivity decrease of the enterprises, besides technology regress and the lack of adequate investments, is the limitation of activities and scale along with the optimal allocation of resources.

9. The firms working on contract show lower efficiency change and technological change at the all India level. However, it is noticeable that in most of the cases, scale efficiency either increases or remains the same. This fact indicates that decline in TFPG is either due to decline in managerial efficiency or technological regress. Thus, liberalization is unable to bring substantial technological progress and efficiency enhancement for the firms working on contract.

Since the informal sector is the a major source of employment of the working poor in the developing country like India, any discouragement of the production of these enterprises will lead to a high unemployment, poverty and income inequality. Trade liberalization has the positive impact on the informal sector’s growth. At the same time, imposition of fiscal regulations of the informal enterprises makes the enterprises more inefficient due to extra cost of regulation. Thus, the regulations should be imposed in such a way that it should not be burdensome of the enterprises. Specifically, the enterprises need to be identified for the protection in terms of different subsidy policies. The factors that determine informal employment in developed regions are in some cases different from the factors that determine
employment in the underdeveloped one. Moreover, in terms of efficiency, the empirical analysis supports that firms operating on contracts are less efficient in developed state (Delhi), while they are more efficient in less developed state (Orissa). The analysis suggests that there exists duality in terms of the determinants of informal sector’s employment and efficiency within a country. Thus, policy may be prescribed separately for developed and underdeveloped regions.

8.2. Policy Implications

On the basis of our empirical analysis the policies are suggested for (i) employment generation, (ii) economic growth, (iii) efficiency enhancement of the informal enterprises, (iv) productivity improvement of the informal sector and (v) competitiveness of the informal enterprises. The results and analysis of the study have the following select implications for promotion of the informal sector.

1. Education is the main policy variable for employment generation. Policies should have special attention to promote education for all. In addition, policy maker has to take special initiative so that educated persons should get quality jobs as they deserves. In that case, technological upgradation in the informal production units will increase the quality of jobs for the educated persons. This kind of technological upgradation may also lead to unemployment. Incentive (especially, loan for self-employment) may be given to increase the number of the informal units.

2. The persons who don’t have any technical education possess higher probability to engage in the informal sector both in the developed and underdeveloped regions. In the developing country like India formal sector is unable to absorb all the work force. This implies that the informal workers may be properly trained skill formation and vocational training so that they can produce better quality of product using less time and it would also help in reducing the wage gap between formal and informal sectors.
3. More mobility creates more opportunity to find better jobs. Thus, one should note that the person under consideration may be efficient enough to work at a higher wage rate in some other places. Information regarding better jobs should easily available to the working poor. Thus, policies may focus on the better migration facilities.

4. Formal-informal sectors’ linkages have significant contribution on economic growth. Moreover, when the relationship is complementary between the two sectors, one sector helps to grow the other sector. Inter-firms vertical linkages through sub-contracting make the informal firms more efficient in underdeveloped region. Thus, policy may give a focus on strengthening the linkages between the formal and informal sectors.

5. Lack of market and competition from larger units is making the firms more inefficient in both developed and developing regions. Thus, a promotional policy needs to be implemented for better marketing facilities for the informal enterprises.

6. Firms producing their products within the household premises are more inefficient than the ones operating outside the household premises. Since household premises are traditional in nature producing mainly consumer goods and enjoy a relatively low share of market surplus, a promotional policy needs to be implemented in terms of credit for start-up and expansion capital and skill formation of these enterprises.

7. Since government can regulate rate of interest of loan through priority sector lending, it is an important policy variable to enhance the efficiency of the informal enterprises.

8. Within the unorganized sector, the non-informal sector is much better off than the informal sector. Thus, informal sector may be identified for policy suggestion instead of suggesting policies for the unorganized sector in general.
9. The main reason for productivity decrease due to technology regress and the lack of adequate investments. Thus, state intervention is required to enhance the productivity growth and reducing cost through technological transfers, education and training of the informal sector’s workers which, in turn, will enhance the competitiveness of the enterprises both in the domestic and international market.

8.3. Direction for Future Research
The scopes for further research includes the following.

1) In order to understand whether or not the determinants for informal sector’s employment are different between 2004-05 and 2009-10, one can extend the analysis by estimation of the determinants of informal sector’s employment using the 66th round NSSO data on employment and unemployment survey 2009-10 data which is yet to come in public domain. This comparative analysis is useful not only at the national level but also at the state and sectoral levels.

2) 11th five year plan has a special attention on social security and inclusive growth. Thus, our analysis can be extended in the light of social security and inclusive growth of the informal sector’s workers and informal workers. This may be useful to derive distributive implications of the output and employment growth in the informal sector.

3) We have measured the total factor productivity growth and its components of the informal and non-informal manufacturing sectors. Since the characteristics of the informal sector are different from the non-informal unorganized service sector, one can extend the analysis for the enhancing the productivity and competitiveness of the service sector.