ABSTRACT

Since 1991, India initiated the process of national and sub-national economic reforms which included liberalization of economic agents from administrative controls and regulations and integrate the domestic economy with the global economy. Because of its economy-wide coverage, liberalization, in general, has impacted on the entire Indian economy, comprising both the formal and informal sectors. Specifically, performance of both the formal and informal sectors in terms of their size and growth of income, employment, technical efficiency and productivity have been changing between pre and post liberalization period. In fact, the growth and contribution of the informal sector in India raises analytically interesting and policy useful researchable issues on the relevance, applicability and impact of liberalization measures, especially for the informal sector. Thus, it is important to know the policy and non-policy factors which influence the economic performance of the informal sector during the liberalization period.

This thesis focuses on descriptions and analyses of the nature and magnitude of economic impact of liberalization on the economic performance (through contribution to output and employment generation) of the informal sector. It begins with a broad framework for analysis of output contribution and growth of the informal sector. Liberalization is measured by openness indices and inter-sectoral linkages. Impact of liberalization on growth contributions of informal sector is captured by openness indices (i.e. degree of openness to trade and principal component scores) and on technical efficiency (measured by Data Envelope Analysis and estimated by Tobit Censored Regression model) and components of productivity (computed by Malmquist total factor productivity index) of the informal enterprises by inter-sectoral linkages. The linkages are modeled theoretically in a neo-classical growth theory and empirically measured by sub-contracting arrangements between formal and informal enterprises. In addition, the determinants of informal sector’s employment are estimated (using Probit regression analysis) to derive implications on promotion of informal sector from the viewpoint of employment generation. Overall conclusions and implications of the study are obtained from within the descriptions and analyses of the entire thesis.

The database used is secondary in nature and is available and accessible in published and/or electronic form. Aggregate data at national level, disaggregate data at state and sectoral levels and unit level data from nationally representative surveys of National Sample Survey Organisation (NSSO) are used for descriptions, computations and estimations. Major macro sources include (i) National Accounts Statistics, published by CSO, (ii) World Investment Report
Select major results and conclusions of the thesis are as follows. 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. Trade liberalization and vertical inter-firm relationship through sub-contracting have significant and positive impact on the informal sector’s growth. Moreover, both the formal and informal sectors have positive externality effect and they are interdependent. Even if the informal sector is less productive, it still has a large externality effect besides making a significant contribution to economic growth. 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. Further, 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?

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. 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.