CHAPTER II

PERSPECTIVES OF INFORMAL ECONOMY AND THE STATUS OF INFORMAL WORKERS IN INDIA
PERSPECTIVES OF INFORMAL ECONOMY AND THE STATUS OF INFORMAL WORKERS IN INDIA

In India, the formal sector employs only a small proportion of the labour force. A majority of the workers come under the category of informal workers and the proportion has been recording continued expansion. Informalisation process resulted in various forms such as outsourcing, contract appointments, part-time jobs, ancillarisation, sub-contracting, home production and sweatshop production. Mobility of international capital has been given an unprecedented leverage to companies which appoint informal workers internationally. Moreover, the international flight of capital leads to drive-down wages and a large number of labourers in insecure and irregular employment. In this scenario, the perspectives of informal economy and the status of its workers in India are to be examined in this study.

Growth of Employment and Occupational Structure

Indian economy has experienced a long-term average annual growth rate of over 2 per cent in employment. However, since 1950, the growth of GDP has been slow at an average of about 3.5 per cent per annum. In the Indian context, an anxiety in the employment front is that the labour force has been growing faster than employment. The backlog of unemployment has been increasing year after year, at the rate of about 2.5 per cent per annum in the labour force. In the liberalisation era, the anxiety has further been aggravated because of slowdown in the employment growth.¹

The relatively unchanging composition of the occupational structure of the Indian workforce is another phenomenon. It is well known that the share of the primary sector in the national product has steadily and
significantly declined and those of the secondary and tertiary sectors have increased. A similar change has not been observed in the distribution of workforce. After Independence, the share of agriculture and allied sectors in GDP declined from around 75 per cent to 21 per cent; but its share in employment increased from around 8 per cent to 11 per cent. It is often contended that the shift in employment from the primary sectors has primarily been to the services sector, thus reflecting a movement of workers towards residuary and unproductive activities. In fact, the shift in favour of the secondary sector has been more significant. The share of service sector in GDP has increased from 24 per cent to 29 per cent. While in the longer period of over four decades of planned economic development, the employment structure of the Indian economy has remained relatively stagnant and a major shift in favour of the secondary sector has not been realised. During this period, the industrial sector has shown a relatively higher rate of growth on a sustained basis. One important reason for the relative absence of structural change in the workforce is due to the growth in population and labour force.

The historical experiences of growth in other countries have not been based on a rapid rate of growth of population and labour force. In a situation where an overwhelming majority of the workers were engaged in agriculture, a significant shift to the secondary sector would require a rapid expansion of industry. In the absence of it, with a rapid increase in population and labour force, most of which, again, takes place in agriculture. Even a reasonably high employment content of industrial growth would not be able to lead to a significant change in employment structure. Though increment to industrial
workforce has been significantly large, a rapidly increasing number of workers were added to agriculture. In the recent years, with a slowdown in the growth of labour force and a relatively high rate of industrial growth, with a low and declining employment elasticity, matters have led on to a significant shift in employment, in favour of the industrial sector. But with the growth of population and even a relatively high growth of industrial employment, it is not likely to produce a major structural change in employment in a short or even medium term.

The impression is that the industrial sector has failed to generate employment because of the relatively slow growth of employment in the organised manufacturing sector. Most of the manufacturing employment is in the unorganised section, and, its share has in fact increased from 67 per cent in 1972-73 to around 86 in per cent 1987-88.

The Indian Industry has been undergoing a structural change over the past four decades. Initially, primary raw-material based industries dominated the industrial structure. Their predominance reduces with the faster growth of metal-based industries. At present, industries using processed intermediates and inputs have emerged as important segments of the Indian industrial structure. Transition implies higher technology, increase in labour productivity and decline in employment potential of output growth. The slow down in employment growth could be attributed to this structural change. An analysis reveals that the structural changes, though significant, have not been of the order that would lead to a rank reversal among the major industry groups. The labour productivity has shown an increase in
some different industry groups; and there is an increase in the employment elasticities in some others.  

The two conditions for opting for a technological change are physical availability and economic efficiency in terms of cost reduction. Industrialists argue that the organised sector employment has not grown primarily because of the labour legislation. Further, they argue that the workers once hired could not be fired, due to the heavy protection provided by labour legislation. A faster growth of employment in the unorganised sector is often referred to as an evidence of the employers' unwillingness to expand employment in large-size factories in which the protective labour laws are applicable.

The employers do not hire workers because they cannot fire, and 'exit' is very difficult due to labour legislation. Union and public pressure has limited validity in the face of the experience in many industries where the workforce has been drastically reduced in a short period. In Ahmedabad, about 36,000 regular full time workers were eased out of textile mills in a short period of two-years. In Kanpur, employment in the private factory sector declined by 44 per cent during a short period of five years between 1983 and 1988. The decline in actual numbers is estimated at 40,000. Quoting rapid employment growth in the unorganised sector has a similar fallacy. Unorganised manufacturing has always dominated manufacturing employment in India. Ancilliariisation has made very little progress. The linkage between the large sector and small units has generally been found very weak and diffused. A major part of the manufacturing activity in the unorganised sector is independent of the organised sector and produces final
products for the consumer market rather than intermediate products and is part of the organised sector. 

Relaxation of labour laws removing restriction on firing of workers can increase employment in large factories. The trend is likely to continue with liberalisation and the opening up of the economy: The compulsions of international competition are likely to further reduce the employment intensity partially because of the need for cost reduction on the one hand and improving the quality of the products on the other. Organised manufacturing sector accounting for about one-fourth of the manufacturing employment contributes only about 2.6 per cent of the total workforce. Unorganised sector that accounts for the major part of the manufacturing employment has shown significant potential for employment growth. It is quite clear that about 53 per cent of the employment in the manufacturing sector is located in rural areas and almost all of it is in the unorganised sector. It has registered an employment growth of around 4 per cent per annum during 1972-73, 1987-88.

In urban areas, the unorganised sector contributes the major part of the manufacturing employment and has registered a significantly high rate of over 5 per cent growth in employment. It has been observed that the small-size urban settlements with a population ranging from 20 to 50 thousand have registered the fastest growth in employment. There seems to be emerging a trend towards a relative shift of small manufacturing activities from the larger to these smaller towns. There is also evidence to suggest that the economies of size, technology and market are leading to a shift of certain rural industrial activities to these towns.
Development Theories and Informal Workers

W. Arthur Lewis' theoretical model of economic development revolves around two basic assumptions that there was an unlimited supply of labour in most developing countries and the modern industrial sector would absorb the vast pool of surplus labour. The successful rebuilding of Europe and Japan after the World War II and the expansion of mass production in North America and Europe, many resource-poor traditional and agricultural economies transformed into dynamic, vibrant and modern economies. In this process, the traditional sector is inclusive of petty traders, small producers and a wide variety of casual jobs would eventually be absorbed into the formal economy. But the experiences of planned economic development in many of the developing countries, including India, did not create either sufficient modern jobs or reduce unemployment to evade the traditional sector.

The Indian situation does not conform to the Lewis model. The organised sector failed to absorb the labour engaged in the unorganised sector. The process of development of the latecomer developing countries was one of borrowing technology from developed countries which was labour displacing. The industrial structure was not favourable to the absorption of labour from the unorganised sector. The share of unorganised sector in National Income has been declining but the number in the unorganised sector continues to swell.

Conceptualisation History

By the fag end of 1960's, there existed an optimism about the increased economic growth as a means to give way to concerns about persisting widespread unemployment and the stable size of the traditional
sector. Reflecting this concern, the International Labour Organisation (ILO) conducted many employment missions to various countries. The first mission was to Kenya in Africa in 1972. The Kenya mission recognised the traditional sector as the informal sector. They found that the size of the informal sector not only persisted but also expanded. Once it was confined only to the marginally productive activities, however, it included profitable and efficient enterprises. The informal sector activities were largely ignored, rarely supported, often regulated and sometimes actively discouraged by policy makers and governments. The ILO mission found that the informal sector in Kenya was efficient, creative and resilient.

However, the concept, informal sector, received mixed responses in the development circles. Some opined that the persistence of informal sector in Kenya and in other countries was due to insufficient levels of economic growth. It means that, for them, the informal sector will shrink with modern industrialised growth. The survivalist segment focussed their attention on the least dynamic segment of the economy. For them, the informal economy was marginal or peripheral and not linked to the formal economy. This pluralistic view restricted the attention of mainstream developmental economists in many significant ways. Martha Alter Chen and others preferred to use the term informal economy for the informal sector because formal and informal parts of the economy are related and interlinked and it is therefore misleading to think of two separate sectors of the economy. Moreover, the term sector is commonly used as a classificatory device for industry groups and commodity chains. It is confusing to use it as a classificatory device for both the formality
and informality of work status. Therefore, they used informal economy and informal workers substituting for the word informal sector.

**Difficulties of Making a Unique Definition**

Of course, a person holding one employment status in multiple employments is often difficult to determine. It should be noted that employees of informal enterprises are included in the 1993 enterprise-based definition of the informal sector adopted by the 15th International Conference of Labour Statisticians (ICLS). This is because the 1993 ICLS defined the informal sector as the sum of the self-employed, family workers, employers and employees of informal enterprises but, thereby, excluded many wage workers who are hired causally and who lack protection. Some observers including the international network WIEGO (Women in Informal Employment: Globalising and Organising) recommend a broader employment-based definition of the informal sector to include all wage workers both in informal and formal firms. The employment-based definition recommended by WIEGO includes: (1) all employers of informal enterprises; (2) all self-employed persons, except self-employed professionals and technicians; (3) all wage workers who work without minimum wage assured work, or benefits, whether they work for formal or informal firms (including employees of informal firms, domestic workers, causal workers, home workers, temporary and part-time workers, and unregistered workers. Whichever definition is used for informal economy, it has two basic components namely non-wage employment (comprising independent workers) and wage employment. It is not easy to determine whether a person is a fully dependent waged worker or an independent entrepreneur. But there is a need at all times to distinguish
between policies and regulations that affect the self-employed and informal wageworkers.

For the purposes of policy analysis, in addition to their employment status, informal workers should be classified according to the industry in which they work and their place of work. Much of the literature on the informal economy focuses on the relationship between the informal and formal "sectors". The dualists view the informal economy as a separate marginal sector (ILO 1972). They argue that the informal sector exists or persists because economic growth or industrial development has failed to absorb the informal workers. The structuralists view the informal sector as being subordinated to the formal sector. They argue that, in order to reduce their labour and input costs, capitalists in the formal sector seek to subordinate petty producers and traders. The legalists view informal work arrangements as a rational response by micro-entrepreneurs to over-regulation by government bureaucracies. They argue that informal sectors do so to reduce their costs and increase their wealth.

The expert group, constituted by the Department of Statistics, Government of India, felt that 'Informal Own Account Enterprises' and 'Enterprises of the Informal Employers' as mentioned in the resolution adopted at the Fifteenth International Conference of Labour Statisticians (ICLS-1993) are conceptually close to that defined in the Indian Statistical System, i.e., 'Own Account Enterprises' and 'Establishments' with at least one hired worker. This definition which is enterprise-based provides a good coverage of enterprises to work out the value added by industry groups required for the National Accounts Statistics. The group also felt that the
work force in the Informal Sector could be better measured through the household surveys by taking into account the principal and subsidiary activities of each member of the household. The organised sector comprises enterprises for which the statistics are available regularly from the budget documents or reports, annual reports in the case of Public Sector and through Annual Survey of Industries in case of registered manufacturing. On the other hand, data of the unorganised sector are not regulated under any legal provision and or those that do not maintain under any regular accounts.

The National Sample Survey Organisation conducted the first ever nation-wide survey on informal sector non-agricultural enterprises during the 55th round (July 1999 - June 2000). Information on workers including those working in the proprietary and partnership non-agricultural enterprises was also collected for each member of the household during employment-unemployment survey. In this survey, all unincorporated, proprietary and partnership enterprises were defined as informal sector enterprises. This definition differs from the concept of unorganised sector used in National Accounts Statistics.¹⁰

There is much controversy about the concept of the unorganised sector in India. It is sometimes defined as the sector that is not recorded under any factory legislation. Since small and village industry is not generally registered, the unorganised sector is identified with the small and village industry sector, not all industries 'small' are unregistered. Some are registered under the Factories Act. The unorganised sector comprises own account workers and also casual labour employed in establishments. The
latter do not have access to the benefits of social security. The unorganised
sector is sometimes also identified with the informal sector.

The 'unorganised' sector in a labour surplus developing country
refers to the traditional segments either in the rural or urban sectors of the
economy. In the rural sector, the unorganised sector workforce mainly
comprises landless labourers, small and marginal farmers, share croppers,
rural artisans, forest labourers and fishermen, while in the urban sector, it
consists of manual labourers like construction workers, head-load workers,
wage labourers employed in manufacturing, trade, transport, communication,
service and self employed, like street vendors, hawkers, etc. Nevertheless,
the available statistics indicate that the unorganised sector contributes more
than 65 per cent to the national income in terms of value added11 (CSO1992).

According to many studies, the traditional definition of the informal
sector focuses mainly on the size of the firm, the type of technology and the
occupation of the worker (Cole and Fayissa, 1991; Saavedra and Chong:
1996). However, the broad definition of urban informal sector is centred on
two issues:

1. In general, firms and workers in the informal sector do not pay fees or
taxes and follow simple administrative procedures.

2. It is difficult to protect the rights of the agents employed in the informal
sector which does not always comply with the rule of law.

Consequently, there are the costs of entering the formal sector and
benefits should be higher than those costs to allow firms or individuals to
change their legal status. One can argue that the size of the informal sector is a
reflection of the cost-benefit decisions of the individuals. Another point is that
two types of agents may be considered in the informal sector, independent workers and wagemakers. In fact, this point is important and needs to be mentioned because their rationality and their behaviour may be different.

Informal Economy in India

As in 1991, the share of the unorganised sector in Indian economy was as high as 90.66 per cent. There has been very little decline in the share since 1961. Employment in the unorganised sector over the period of three decades grew at an annual rate of 1.1 per cent. In absolute terms, the annual addition to employment in the unorganised sector during the three decades was 2.68 million. Employment in the organised sector has not grown to such an extent as that of the unorganised sector. The employment statistics in organised and unorganised sectors between 1961 and 1991 is given in Table 2.1.


<table>
<thead>
<tr>
<th>Year</th>
<th>Organised</th>
<th>Unorganised</th>
<th>Total</th>
<th>Share of Unorganised</th>
</tr>
</thead>
<tbody>
<tr>
<td>1961</td>
<td>14.60</td>
<td>174.10</td>
<td>188.70</td>
<td>92.26</td>
</tr>
<tr>
<td>1971</td>
<td>20.20</td>
<td></td>
<td>226.90</td>
<td>91.10</td>
</tr>
<tr>
<td>1974</td>
<td>22.50</td>
<td>206.70</td>
<td></td>
<td></td>
</tr>
<tr>
<td>1981</td>
<td>22.90</td>
<td></td>
<td>236.90</td>
<td>90.33</td>
</tr>
<tr>
<td>1983</td>
<td>24.01</td>
<td>214.00</td>
<td>288.00</td>
<td>91.67</td>
</tr>
<tr>
<td>1987-88</td>
<td>25.70</td>
<td>264.00</td>
<td>293.70</td>
<td>91.25</td>
</tr>
<tr>
<td>1991</td>
<td>26.70</td>
<td>259.38</td>
<td>286.08</td>
<td>90.66</td>
</tr>
</tbody>
</table>

Note: It may be noted that work participation rates as per the NSS are higher than for Census. Unorganised sector employment is got by deducting workers in the organised sector from total workers.


The Net Domestic Product by organised and unorganised sectors at current prices is furnished in Table 2.2.
The share of employment in organised sector in 1981 was only 9.70 per cent. This may be compared with a corresponding share of Net Domestic Product of 30 per cent. Between 1980-81 and 1990-91, the share of the organised sector in NDP increased further from 29.97 per cent to 36.14 per cent. But the share in employment showed a decline from 9.70 per cent to 9.37 per cent. This shows the inability of the organised sector (even in the context of growth) to absorb the growth of labour force. Between 1981 and 1991, the annual addition to the labour force as per the demographic censuses was 4.9 million. Out of this, the absorption of the organised sector was only 0.38 million or around 8 per cent of the labour force.

Table 2.2. Net Domestic Product by Organised and Unorganised Sectors at Current Prices

<table>
<thead>
<tr>
<th>Year</th>
<th>Organised</th>
<th>Unorganised</th>
<th>Total</th>
<th>Share of Unorganised</th>
</tr>
</thead>
<tbody>
<tr>
<td>1980-81</td>
<td>33073</td>
<td>77267</td>
<td>110340</td>
<td>70.03</td>
</tr>
<tr>
<td>1985-86</td>
<td>72952</td>
<td>134610</td>
<td>207562</td>
<td>64.85</td>
</tr>
<tr>
<td>1986-87</td>
<td>84652</td>
<td>145555</td>
<td>230207</td>
<td>63.23</td>
</tr>
<tr>
<td>1987-88</td>
<td>96755</td>
<td>164755</td>
<td>261510</td>
<td>63.00</td>
</tr>
<tr>
<td>1988-89</td>
<td>114624</td>
<td>198895</td>
<td>314519</td>
<td>63.56</td>
</tr>
<tr>
<td>1990-91</td>
<td>151749</td>
<td>268030</td>
<td>419778</td>
<td>63.85</td>
</tr>
</tbody>
</table>


The National Accounts statistics, 1993, states that Electricity, gas and water, railway transport, communications, public administration and defence are exclusively within the organised sector. The unorganised sector accounts for much of the agricultural production, the bulk of trade and construction, major proportion of transport other than railways, and storage.

The entire employment in the public sector is considered under the organised sector, because of job security and social security. The employment in the public sector was 18 million against 7 million in the organised private sector.
Another problem is the question of marginal workers, those who do not work full time. If they are included, but not weighed differently, the estimate of the unorganised sector's contribution will be overestimated, while if these workers are excluded, their contribution will be underestimated. The current measures used by the CSO to study the informal sector are unable to capture the dynamism of the sector. More efforts are being made to increase the dynamism of the sector, and the ability of the informal sector to respond to change in market-conditions by filling new niches and its ability to integrate new techniques. It is the responsibility of national data collection agencies to debate all issues. The current indirect or residual methods of estimating the informal sector's contribution are to be expended in determining the methods of direct estimation.

The household sector (equated with unorganised sector) contributes 76 per cent of total savings while only 23 per cent is the share of the organised sector. However, nearly 60 per cent of capital formation is in the organised sector. The CSO divides the economy into three sectors; viz, the public, private, corporate and household sectors. It is the household sector that contributes the most to savings. But the public and private corporate sectors reap the rewards of the savings of the household sector. Savings is divided into two categories such as savings in financial instruments and savings in the form of physical assets. In both cases, the share of savings of the public and private corporate sectors is netted out of the total savings, leaving the residual classified as the household sector's share of savings.
Debate on the Validity of the Informal Sector

The discussion about whether or not the informal sector should be used as the main engine of development is a very controversial one. There are researchers on both sides of the argument who have very strong feelings. The informal sector may be viewed as the driving force in the job creation process since it typically includes many small and micro-enterprises. Many researchers, however, believe that this sector is for the workers who are unskilled and poorly paid, owing to the fact that the jobs created in this context are not very productive (Saavedra and Chong, 1996; Cole and Fayissa, 1991; Tokman, 1989). It could be argued that the productivity of workers in the urban informal sector is not zero. Some researchers (Agénor and Arizonan, 1994) do analyse the interactions between the formal and informal urban labour markets by emphasizing the phenomenon of substitutability rather than complementarity in the short run. In this context, skilled and unskilled workers laid off in the formal sector may seek employment in the informal sector when the output growth is weak (Agénor and Montiel, 1996).

Informal Vs. Formal Economy

An analysis of the empirical characteristics of the informal sector will reveal more differences. Some of the issues differentiating informal sector from the formal are analysed as follows:

(I) Formal wages are high

It is obvious that the wages of the formal sector on average will be greatly superior to the same of informal sector because of the different level of human resources. The proper empirical approach, thus, is to compare
wages at the same level of qualification. According to Mazumdar (1973), in Bombay city, at least, there are many salaries which are higher in the formal (or industrial) sector at the same level of human resources; but this is not necessarily due to government policy or trade-union action. On the other hand, it seems that urban (formal) wages are kept high in order to stabilise manual labour (as understood by Stiglitz, 1974 and 1982). In fact, real wage cuts tend to decrease productivity as they directly lower incentives to provide efforts, raise the quit rates and increase turnover costs. In this context, urban rigidity can be explained as a result of efficiency considerations rather than government regulations.

(ii) Informal Sector: Transitional Passage toward the Formal Sector

If workers are hired on a daily basis, as is often the case in the LDCs, it seems that the hypotheses of the probabilistic models are confirmed. In the informal sector, wages are lower and workers are mostly young and new migrants.\textsuperscript{12} However, if we look at other studies, the passage role of the informal sector is not so obvious.\textsuperscript{13} Evidence shows that for India, on the contrary, new migrants integrate more easily into the formal sector than those who have been there for a year.\textsuperscript{14} In Asia, it plays the recruitment role in the urban formal sector, rather than the urban informal sector.\textsuperscript{15} Thus, even if the two-stage recruitment process in the urban formal sector is correct, nevertheless, it hardly seems verified, empirically, that the informal sector plays the role of the first stage. It is also possible that some rural workers work a certain time in the urban informal sector and then return to their homes.
(iii) The informal sector is more complicated

The empirical studies carried out in Africa,\(^{16}\) in South America (Psacharopoulos and Steier, 1988; Roubaud, 1991...) and in Asia\(^{17}\) well demonstrate the complexity and the heterogeneity of the informal sector.\(^{18}\) The latter is not in fact a simple low-wage, easy-access transition sector but indeed involves several segments. Various points raised by Fields\(^{19}\) casts renewed doubt on the simplistic version of the informal sector such as facility of access, lower wages than in the formal sector and the origin in rural areas. The inference is that people stay in the informal sector by obligation rather than by choice.

It can be observed that different types of jobs coexist in the informal sector which are, for the sake of clarity, classified in two segments: a lower segment which has all the characteristics of secondary jobs, including low wages, total freedom of access, and job precariousness; and an upper segment with high wages (even higher than those of the urban formal sector) and a certain level of physical and human resources.

Some of these interpretations cast renewed doubt about the urban labour market in which the informal sector played a transition role. Some authors\(^{20}\) go so far as to say that the job-search process takes place in three stages. People first go through the lower informal sector, which plays a transition role (following unemployment or rural employment); they next seek an informal urban job so as to accumulate the human and physical capital necessary for obtaining a formal job or, more exactly, so as to establish their own company in the upper informal sector. This reflects reality, based on the results obtained from the investigations carried out in South America.
It is absurd to keep both informal and formal sector in watertight compartments. Most segments of the informal economy have direct production, trade, or service links with the formal economy. For instance the industrial outworkers who produce under subcontracts, the street vendors who sell on commission and the sanities that clean the offices of formal firms are under subcontract. The question is not whether informal waggeworkers have direct ties with the formal economy but what is the nature of those ties, whether benign, exploitative, or mutually advantageous. Michael Piore classified informal business into three categories namely sweatshop production, mass production and flexible specialization. Sweatshop production involves minimum capital investment and workers being paid by units of output (i.e., piece-rate) and being deprived of a minimum wage and basic health or safety standards. They include those who work in workshops and those who work from their homes. Mass production involves huge capital investment and units of capital that are specialized; and workers being paid a minimum hourly wage and enjoying basic health technology or techniques with more general applicability; and a variety of work arrangement. In an earlier book "Second Industrial Divide," Michael Piore and his colleague documented that mass production in industrialised countries, rather than continuing to expand as Arthur Lewis and other neo-classical economists predicted, had given way to flexible specialisation.

Responses to Economic Policies

Very few economists have tested whether the informal and formal economies respond in similar ways as economic policies. In one such attempt, Urjit Patel and Pradeep Srivastava analysed the aggregate
behaviour of economic activity in the formal and informal sector measured by
the output - responded to the same set of monetary and fiscal policies in
India. In terms of intra-sectoral responses, they found that total output, total
non-agriculture output, and total manufacturing output in the formal sector
responded in similar ways whereas total output, total non-agriculture output,
and total manufacturing output in the informal sector responded in different
ways. That is, the formal sector proved for more homogeneity in behaviour
than the informal sector. In terms of inter-sectoral responses, they found that
the formal sector behaved or responded more or less as predicted to each of
the macro policy interventions while the informal sector did not respond as
predicted to any of the interventions (Patel and Srivastava 1992).

Patel and Srivastava argue that their analysis raises several
important issues, both theoretical and policy related, for development
economies. First, that the lack of homogeneity of the informal sector implies
that the developing economies such as in India are "fragmented economies"
rather than "dual economies". Second, that the predictive power of
"fragmented economies" is weak. Of course, other observers question the
predictive power of standard economic models even in non-fragmented or
non-dualistic economies. And, third, those institutional details are relevant to
explaining aggregate economic activity in fragmented, dualistic, and non-
fragmented economies. They conclude that in the early 1990s, the informal
sector was virtually ignored: "no systematic data is collected to monitor the
activities of the informal sector in analysing the behaviour of these economies
and impact of various models." (Ibid: 32)
There is a need to examine the impact of macro-economic policies on the informal economy and its differential impact on the informal and formal economies. In many countries, macro-economic policies are biased in favour of large businesses in the formal economy. With globalisation, trade and industry policies are designed to foster international competitiveness. These policies have an impact on employment and enterprises in both the formal and informal parts of the economy.

**Link between Informal Sector and Poverty**

The relationship between informal employment and poverty is often not well understood. Despite the heterogeneity within the informal economy, there are links between working informally and being poor. Average incomes are lower in the informal economy than in the formal economy. As a result, a higher percentage of people working in the informal sector relative to the formal sector, are poor.\(^23\)

The relationship between informal employment and poverty appears only when informal workers are classified by employment status and by industry or trade. Moreover, there is a gender gap in incomes and wages in the informal sector. For instance, a relatively few women are employers who hire others, and a relatively few men are industrial outworkers. Even within the same trade or industry, men and women tend to be involved in different employment statuses.

A gendered approach means understanding the relationship between male and female workers; pro-poor approach that is gender sensitive and focused on work-status. The concept "social exclusion"\(^24\) has been developed to understand the problems of "new poverty," often located
in inner cities. It is a multi-dimensional concept, referring to people's economic position and their degree of integration in society. The concept of social exclusion emerges from a crisis in social policies.

Amitabh Kundu argued that economic explanations for this phenomenon such as a relative lack of employment creation in the modern sector do not suffice. At least, part of the explanation has to be sought in social-cultural factors, such as the desire to migrate or stay at home, and the fact that the poorest generally do not migrate. The gap between rural and urban areas has increased in terms of several indicators during the eighties. And yet the difference between the poor in urban and those in rural areas has gone down, which would explain the decline in the rate of rural-urban migration. The main reason for such a situation is due to the trend in industrial employment that is a continuation of the process of jobless growth.

In the backward economies, 'trickle down' argument seems to have limited relevance due to the existence of wide inequality in the distribution of income and wealth. Experience has also shown that growth alone is insufficient to eradicate poverty, and that it must be accompanied by equitable distribution of income and wealth through state intervention. This is the case for the extension of formal social security to the weaker sections of the society.

The risks faced by those who work in the informal economy differ by their employment status. Those who work in both formal and informal economies face general risks such as illness, property loss, disability, old age, etc. However, the workers in the informal sector face greater work-related risks than those in the formal sector. Dependent informal workers face
little assurance or guarantee of work, low wages or earnings, few worker
benefits, and unhealthy working conditions. The informal workers have fewer
mechanisms for dealing with risk than those who work in the formal sector.
As a general rule, informal wageworkers enjoy fewer career opportunities
than formal wageworkers.

Informalisation and Feminisation

In India, a study of the trends of women's participation in the work
force between 1981 and 1991 (Census), shows that the worker population
ratio (WPR) of women seems to have increased from 20 to 22 per cent.
Meanwhile, the NSS shows that the women's WPR has been around 28 per
cent. In the urban sector, initially growth in urban employment had connoted
increase in regular salaried wageworkers. But under the present context, it
means regular contractual work, which often implies low paid and insecure
secondary work.

According to Sutha and Ajit Deshpande, liberalisation would further
encourage urbanisation as well as feminisation through the sex discrimination
in the labour market. In some parts of the urban sector, the employment of
women seems to be increasing following the feminisation of work. However,
it is limited and the nature and quality of employment is extremely
exploitative. The emphasis has been primarily on the export processing
zones where the conditions of work are arduous and low paying, with little or
no security.

Link between Informal Sector and Economic Growth

The relationship between informality and economic growth has been
somewhat less explored than the relationship between informality and
poverty. The informal sector contributes to economic growth in at least two ways. First, the output and the low wages of informal wagemakers subsidise the growth of industries. Second, the output of informal enterprises also contributes to economic growth.

Until recently, few estimations of the contribution of the informal sector to Gross Domestic Product (GDP) had been carried out. With support from the Statistics Division of United Nations Secretariat, Jacques Charmes recently calculated the contribution of the informal sector to GDP in 21 developing countries. In sub-Saharan Africa, the informal sector contributes anywhere from 7 per cent to 59 per cent of non-agricultural GDP and from 7 per cent to 38 per cent of total GDP - the lowest and highest shares of both non-agricultural and total GDP being, respectively, in South Africa and Niger or Mozambique. In Asia, the share of the informal economy ranges from 17 to 48 per cent of non-agricultural GDP and from 16 to 32 per cent of total GDP: the lowest and highest share being in Korea and India, respectively. In India, a joint research project of the National Council of Applied Economics Research (NCAER) the Self-Employed Women’s Association (SEWA) and the Gujarat Institute of Development Research (GIDR) recently calculated the contribution of the informal sector. According to them, India generates about 62 per cent of GDP, 50 per cent of gross national savings, and 40 per cent of national exports.

Globalisation and informalisation

The environmental implications of globalisations and consequent liberalisation on economic changes are significant. In India, cities compete with one another to attract foreign investment on manufacturing and other
services, the bargaining items being mostly cheap labour. Thus modern economic activity is more towards informalising labour, especially in urban areas.

The new economic policy introduced in 1991 gradually and systematically accepted the pro-free market course by removing restrictive government regulations. This objective can be easily realised by increasing the flexibility in the labour market. The greater flexibility is advocated on the assumption that securing of employment is counterproductive to employment generation. A permanent employment involves more of rights and entitlements. For instance, a guaranteed wage-index is linked to the price of essential needs, paid holidays, bonuses and contributions to social provisions. As a result of these overhead expenditures, labour accounts for a much higher percentage of production costs than just wages. The latest labour use is a paradigm shift from a planned to a liberal market represents the loss of effort by the government in social democratic welfare and to protect the labour with a system of strict regulations under the watchful eye of the government.25

During 1980s, those countries experiencing economic transition found their informal economy continuously expanding. Thereafter, it has come to be recognised as a feature of economic transition. In those countries, the retrenched workers, as a result of downsize and the workers in closed public enterprises have joined the informal economy. Some of the workers of formal economy informally earned incomes in order to supplement their family income. Available evidences show that without appropriate policies and institutions, the informal economy expanded and there exists a
persisting expansion as a result of macro economy adjustment and stabilisation policies.\textsuperscript{26}

During 1980s, the countries with growing and established industrial sector exhibited expanding informal economy. The informalisation of the economy is as a result of three important factors. Firstly, capital intensification reduced the extent of workforce (downsizing) and the retrenched workers found asylum in the informal sector. Secondly, decentralisation of production resulted in formation of small, more flexible and specialised production units some of which recruited informal workers. Thirdly, cost cutting measures include ancilliarisation and sub-contracting of services eroded the employment relations. According to Portes, the recent expansion of informal economy is linked not only to the capacity of formal firms to absorb labour but also to its willingness to do so.\textsuperscript{27}

In the 1990’s, globalisation and competition accelerated the expansion of informal economy. Investors in some of the countries, because of the global competition, shifted their production to countries that have low labour cost or to adjust employment practices to more informal arrangements. There have been some changes in the production and distribution in some key industries characterised by subcontracting through global chains. It reduced the employment opportunities in the domestic economy which in turn created opportunities in the informal economy of the domestic or foreign country. This shift is accompanied by a parallel shift from regulation of labour standards to regulation of commercial contracts.\textsuperscript{28}

The informal economy continues to persist longer than already predicted, not only has it expanded in some developing countries including
transition economies but also in some industrialised developed countries. The new employment consists of informal workers to a level of 50 per cent in Latin America and 80 per cent in Africa. The net result is that employment and output in the informal economy accounts for a significant share of the GDP. The development economists never predict the notable shift from mass production to flexible specialised production or back to the sweatshop production.

The share of regular employees among urban males has come down since 1990-91, indicating that self-employment and casual labour among men has increased. There has been an increasing share of women casual and regular employment during the reform period. It is in mainly due to positive discrimination against women due to their temperament and accessibility. The increase of women in casual labour is more than the increase of them in regular employment.

There is also a movement of employment from organised to unorganised sector as firms began to adopt new technology and contract labour. Creation of cheap labour is one of the characteristic features of the New Economic Policy (NEP). Many assembly industries employ entirely unskilled and semi-skilled low paid female labour rather than employing underemployed and unemployed men leading to feminisation of workforce. There were 178 women workers for 1000 male workers in 1990-91. This has increased to 192 in 2000-01. The increase in the employment of women workers is due to the profits accruing from subcontracting, the docility of female workers and non-unionism.
Sub-contracting is one of the old systems of production which has been accentuated during the periods of economic reform. Subcontracting has emerged in order to evade labour laws, fragment the organisational power of labour, and enhances managerial control over the labour process by dividing the labour market into the non-union markets of small firms and to minimise and control labour costs. "When trade unions exploit product market advantages for their members, the management takes advantage of favourable market conditions to push more work into cheap labour.\(^{28}\) Thus different workers are paid differently for the same job in an industry.

**Wages in the Informal Sector**

The discussions and debates against erosion of their status as employees led to the reforms aimed at abolishing the dualism in the labour market with the introduction of a social safety net and the establishment of a minimum wage, which would ensure an income above the poverty line [ILO Report 1996; and Ghose 1999].

The concept of a minimum wage was introduced to reduce the vulnerability of labour. But it is applied with a great deal of caution. There is no precise answer to the question of what basic needs actually entail, in both a qualitative and a quantitative sense. Opinions vary widely on exactly what should be considered the minimum standard of living for a worker at the bottom end of the economy. In almost in all cases the actual calculated amount not only comes close to the poverty line, it even falls below it. The problem is not only that periodical reviews of the amount tend to lag behind the rising prices of daily necessities, but also that there is almost no effective
supervision on the part of the government to ensure that employers comply with their obligation to pay the minimum wage.

The existence of legislation guaranteeing a minimum wage for workers in the informal sector since 1948 has been unable to prevent an enormous fall in the income of workers who lost their jobs. The social safety net introduced to support the sacked workers turned out to be a complete failure. The National Renewal Fund, set up in 1992 by the Board of Industrial and Financial Reconstruction (BIFR), may have led to a number of the closed units being transferred to the public sector. The termination of their employment contract was offset by the pledge that all their accumulated rights (such as the provident fund and other payments) would be honoured and they would receive the statutory redundancy pay.

Government Regulation

The dividing line between being regulated and remaining non-regulated is difficult to explain. The official international definition is that informal enterprise is one whose size in terms of employment is below a certain threshold (determined nationally) and/or which is not registered under specific forms of national legislation. Some individuals and households take up informal economic activities for sheer survival, because of their relative ease of entry, reliance on local resources, small manageable scale, and minimum capital investment. Informal activities of this kind allow them to maximise their only real asset namely their labour power. What attracts this group is typically the flexibility in terms of time and location and the low investment.
It is important to note that a third category of informal activities is for the interests of formal economy. Some women prefer or opt for home-based work because it allows them to balance work and home responsibilities; other women are forced to work from their homes under subcontracting arrangements because the industry will not hire them under more secure work arrangements. From this, it can be understood that the informal economy is linked to the formal economy. The industrial outworkers have little bargaining power with the economic units who employ them. And those self-employed, particularly home-based, producers typically have limited market knowledge, market access, or bargaining power as compared to large manufacturers.

It is a pertinent question to ask “Should governments intervene in the operation of the informal economy?” One answer is that government interventions lead to inefficiencies and distortions, and that the informal sector will, in any case, decline with economic growth. The second is that the informal sector is beyond the reach of government. Many others subscribe to the notion that the informal economy is here to stay and requires appropriate regulation, laws, and policies to correct the biases in existing regulations.

Those who subscribe to the intervention of the government in the informal sector base their arguments on some mix of equity, efficiency, or political economy principles. They argue that the poor, especially women, who are concentrated in the informal sector, face uneven market power and discrimination. The current process of informalisation - where by more and more people are working under informal arrangements - threatens to do away with decades of social progress.
Those who recommend state intervention on efficiency principles argue that the informal sector contributes to GDP which produces a large share of consumer goods, particularly those bought by middle and low-income groups; it represents a potential source of capital goods and provides a training ground for entrepreneurs. The nature of technology in the informal sector is more labour-intensive and, therefore, more labour-absorbing than the formal economy. They argue that governments should intervene to promote productivity and growth in the informal economy.

Weak Trade Unions

The trade unions hardly succeeded in vanguarding the benefits of labouring classes during the periods of liberalisation. The strategy of the employers is that employees can be hired and fired according to the needs of the situation and the price of labour is determined by supply and demand. Such a situation is treated as a conducive atmosphere for economic growth. The connecting thread of globalisation is termed as free trade and competition that is determining the characteristics of economic activity. The World Bank claimed that the dualistic structure of the labour market be abandoned without delay.

Range of Urban Policies and Regulatory Controls

Intervention of other Institutions

In addition to the government, there is a range of different stakeholders with interest in how the informal economy operates. For example, the International Labour Organisation (ILO) has been charged with regulating labour markets. At present, there is a debate as to whether the WTO (through trade sanction) and/or the ILO (through labour conventions)
should promote international labour standards. None of these international institutions has been charged with understanding or addressing how product, labour, or capital markets affect informal workers or informal operators.

In response to mounting pressures, the corporate sector has begun to adopt "voluntary" codes of conduct to self-regulate their treatment of labour. However, the codes of conduct and related monitoring efforts have not been extended to cover home workers and other isolated informal workers. When informal workers earn less than their counterparts in the formal economy and less than micro-entrepreneurs, how can they share in the benefits of growth in the specific industries or trades? One mechanism is to tax the aggregate output of designated industries to finance benefits for the informal workforce.

One dimension of welfare reforms has been the privatisation of social insurance: that is, social insurance funds to cover pensions, health insurance, and other contingencies have been consolidated and replaced, wholly or partially, by individual savings plans.32 One of the important measures of economic reforms has been the privatisation of the insurance industry. The associated concern is that workers in the informal economy are unlikely to be able to save enough to subscribe to private insurance schemes to protect themselves. Also, the privatisation of insurance has led to the loss of government-mandated coverage for informal workers. In India, so long as insurance companies were public corporations (that is, until 2001) they had special schemes for workers in the "unorganised sector."

Globalisation of the economy is often referred to as the withdrawal of the state from the economic realm. However, the importance of regulation
should not be underestimated. There is growing evidence that regulation of economic activities, including an active role for governments, is needed to deal with the impact of globalisation on labour relations.

**Social Security for Informal Workers**

Social security schemes are intended to provide a minimum living to people unable to earn due to invalidity, unemployment and old age. However, many social security schemes are mainly meant for employees in the formal sector. Workers in the informal sector are deprived of such benefits. In the backward economies, the formal sector constitutes only a small segment of the working population while the majority belong to the unorganised sector.

The need for social security for the unorganised sector is justified essentially on grounds of equity and social justice. The unorganised sector is characterised by irregular employment, unstable income, prevalence of piece wage rates and absence of any legal protection in regard to income, employment and health and safety measures. The unorganised sector suffers large-scale exploitation in terms of hours of work as well as wages. A majority of the casual workers in the unorganised sector are illiterate and relatively less skilled, there is hardly any scope for them to achieve ‘vertical mobility’ on the occupational ladder.

The formal social security for the masses in the unorganised sector is, constrained by many a factor like irregularity of employment and income, absence of a permanent employee-employer relationship and above all, the poor resource base of the backward economies. Because of their poor
economic conditions, the real benefits of government expenditure on education and medical care inevitably by-pass the very poor.35

The household sector is extremely heterogeneous, including pure households, farm households and unincorporated enterprises, leading to problems in instituting policies directed at mobilising savings, since savings behaviour will vary within the household sector. The decapitalisation among informal sector workers illustrated the importance of including social security. The difficulty in implementing social security programmes will be in obtaining contributions by employers, especially for casual and home-based work. The impacts of liberalisation and structural adjustment policies have had negative effects on savings, investment and overall conditions within the informal sector. The urban policies and regulatory controls declare to different areas of a city for different purposes. Street vending space is more visible, and street vendors generally want to be at the heart of commuter and transport nodes. It is often the case that it is not a case of enough space, it is the high competition for the same. A second set of policies are those to do with regulating health standards. The traditionally separate institutional domains of 'occupational health,' 'public health,' and 'environmental health' mean that the local authority cannot easily respond to either of these situations. A third set of policies relate to regulating and registering business. The perception of many is that informal operators want to escape such registration. Traders cite the height costs, to their enterprises, of becoming registered. There are other groups of informal workers, not in fixed positions, on streets. Garbage and paper pickers will be affected by local policies regarding recycling, sanitation, and environmental health.
The relationship between informal and formal operators is often complicated. Informal workers feel that they are excluded from structures and processes through which their own concerns can be expressed, and their rights to work protected.

**Tax Policies**

The impact of tax policies on the informal workforce both consumers and producers are quite important. The informal workers who do not have assured work or who do not receive benefits are to be taxed at the same rate as workers who do have regular contracts and receive benefits.

The value-added tax (VAT), affects those who work in the informal economy as both consumers and workers. Because they operate in highly competitive and price-sensitive markets, the informal producers and traders often find it difficult to “pass on” the value added tax to their customers. This is because of low-income households.

Half of the world’s population will be living in cities by 2010. Informal employment currently constitutes an increasing proportion of urban employment (Charmes 1997; op.cit). Parallel to the increase in homework, there has been an increase in street vending in towns and cities worldwide. Informal trade, most of which is street trade, constitutes anywhere from 30 to 50 per cent of total urban informal employment (Ibid).

**Labour Standards**

There is also widespread international agreement, reflected in international conventions, on the right to collective representation (Convention 87) and the right to free expression of grievance (Convention 98). The conventions, which encompass these core fundamental rights, are
either directed at all workers or, if directed at formal workers, include provisions for coverage of other categories workers. It is important to recognize that these core rights are seen as the rights of all workers, including informal workers. At a minimum, extending these rights to informal workers is called for. While many of the international conventions relate indirectly to the informal economy, there is one ILO Convention that is specific to a large and important segment of the informal economy: the 1996 ILO Convention and Recommendation on Homework. This Convention (C177) sets out minimum standards for pay and working conditions for home workers (also known as industrial outworkers) that can form the basis for national laws and policies. The related Recommendation (R184) details a whole programme of possible actions to improve the conditions of home workers and other home-based workers. Although only two countries (Ireland and Finland) have ratified the 1996 Convention, several countries are considering national legislation that would reinforce certain provisions of the Convention and related Recommendation.

Informal workers around the world are demanding a holistic set of workers’ rights, including the core rights listed above and other basic rights, including the right to a minimum wage, safe and healthy working conditions, reasonable working hours, severance notice and pay, and other workers’ benefits such as paid sick leave, paid vacations, and retirement compensation. Many of these are also incorporated in existing international standards. There are other workers’ rights around which there is less international agreement and, therefore, less scope for international standard setting and monitoring. Most notably, setting a minimum wage depends on
local conditions and, therefore, does not lend itself readily to a fixed international standard. However, most countries have minimum wage regulations, which can be extended to cover informal workers.

The Minimum Wages Act 1948 was passed to reduce discrimination in the wages of the workers. But it has very little impact over the actual wage payment. These conditions of the workers have been shown by numerous such studies conducted in different parts of India. In such cases, female workers are the greater victims. It is reported that in many places, they are not even paid half of the minimum wages prescribed. Paucity of employment, competition, threat of losing even the existing work, helplessness and lack of workers' organisations are some of the reasons for their sad state of affairs.

A systematic study of the workers' industrial situation started when the Royal Commission on labour was set up in 1929, the report of which appeared in 1931. The Royal Commission came to the conclusion that the industrial workers in India had not been able to adapt themselves to industrial situation. It was for this reason that in India, workers were found to be wanting in the level of commitments to industrial jobs. It was obvious that the village-based workers had not been able to cut-off their links with villages and the families left behind in the villages. The incidents of absenteeism in industrial jobs were on the higher side. The study further pointed out that this situation lasted for quite some time and it was very difficult to predict how long it would persist.

**Monitoring Agency**

Monitoring Agency brings the issue of monitoring and enforcement. Ideally, monitoring and enforcement of rights should be left to negotiations (or
collective bargaining) between workers and employers. However, informal workers are not unionised by formal unions and labour negotiations. Moreover, globalisation is eroding the potential for collective bargaining in several fundamental ways. Firstly globalisation privileges capital relative to labour leading to the erosion of employment relations. Secondly, global competition creates disincentives for local governments to enforce labour standards and Thirdly, when globalisation takes the form of global commodity chain production, the primary or real employer may be located in a different country. Hence Kaushik Basu proposes a "third approach" that involves "collusion among the southern countries for raising labour standards, which none of these national governments can do alone, without driving out capital." What Basu proposes is cooperation between countries in the South to raise labour standards uniformly and, thereby, to avoid investors from touring from one country to another for cheaper labour markets.

The growth of informal economy means that millions of workers have no access to formal mechanisms of social protection such as health insurance, disability allowances, or retirement benefits. One of the characteristics of informal work is that it carries high risks, both economically and physically. At present, they are losing the comprehensive forms of protection they once had. The demands made by informal workers may even easily lead to loss of job. The social protection for the informal workforce is first in terms of their basic human rights; and a healthier and more secure work force that most developing countries have found it difficult to implement. However, some developing countries extend selected components of this formal model to designated categories of the informal workforce. In India,
there are Acts that empower the Government – both at the national and state levels – to constitute special funds to provide social security benefits to workers. Tamil Nadu Construction Workers Welfare Board (TNCWWB) is one such organisation at the state level, such as the head loaders funds in Gujarat and Maharashtra states.

The government of India is not always willing or able to extend the full coverage of social assistance to all kinds of informal workers. However, workers with low earnings and irregular employment are unlikely to save enough to protect themselves against economic risk. The informal social security mechanisms should not be seen as a substitute for more formal mechanisms.

The existing social protection schemes suggest that even very poor workers are willing and able to save, as long as the transaction costs are low. The large interest groups, such as private insurance agency and government are willing to carry some of the costs and are willing to negotiate with organised groups of informal workers. However, the challenge is immense, and it is clear that programmes and policies must be built on a careful analysis of different options for different categories of workers in specific industries or sectors. Integrated Social Security Scheme, started in 1991, now insures more than 90,000 informal workers. The scheme includes health insurance, life insurance, and asset insurance. Workers themselves make contributions to the Life Insurance Corporation of India, and form interest groups, on a revolving fund.

The official policy towards the informal economy in India has shifted from one of neglect to recognition. The Government attempted to bring the
workers under some form of protection. The report of the First National Commission on Labour (1969) was a step towards this direction. There was no mention of the "unorganised sector," in the terms of reference for the Commission. There was very little attention paid to it in the report submitted by the Commission. Some of the pertinent objectives of the report were to review the existing legislative and other provisions intended to protect the interests of labour and to advise how far these provisions serve the national objective of establishing a socialist society and achieving planned economic development" and the approach throughout has to be inspired by a quest for industrial harmony." The bulk of the Commission's report dealt, therefore, with industrial labour; less than 10 per cent of the report (45 out of over 500) pages explicitly referred to the non-industrial workforce.

By 1985, when the Government of India began a process of economic liberalisation, it had come to recognise the size, importance, and persistence of the rural sector and the informal economy. The setting up of a series of Commissions to review the working conditions in the informal economy reflected this official recognition. In 1986, the National Commission on Self Employed Women and Women in the Informal Sector was set up. In its final Report, Shramshakti provided a wealth of information on women workers and proposed a comprehensive set of policies and programmes. In 1991, a Commission on Rural Labour was convened. Most recently, in October 1999, the Government of India established the second National Commission on Labour. In setting up this second commission on labour, the Government of India recognised that the country had undergone major economic changes since the earlier Commission submitted its Report and
that it is time to take a fresh look at the situation of labour in the new and fast-changing economy.

END NOTES


29. E. Ramasamy, op.cit.
35. Public provision of social welfare and social infrastructure facilities entail large subsidies. Most of these subsidies benefit the better-off groups who are able to 'capture' these subsidies [Economic Reforms: Two Years After and The Task Ahead, Discussion paper, Government of India, Ministry of Finance, Department of Economic Affairs, 1993, p 22].