

# OVERVIEW ON URBAN INFORMAL SECTOR IN INDIA

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## Abstract:

There has been an upsurge of interest on urban informal sector in India in recent years. A number of studies have been commissioned, books and articles published, and seminars and workshops conducted focussing both on its theoretical as well as operational aspects. The substantial increase in the volume of person days of employment, percentage of subsidiary and casual workers in the early nineties, after the formal launching of the programmes of structural adjustment, has given a boost to informal sector studies since much of this incremental employment has been generated within this sector. There has, however, been a hiatus between conceptualization of the informal sector in theory and its practical application in empirical research. Theoretical research on the development dynamics in India as also in other developing countries has stipulated several characteristics of the informal sector in terms of technology, production relations, conditions of work and workers, among others. It also envisages certain types of relationship between the formal and informal sector. Unfortunately, empirical studies analysing the pattern of growth of the informal sector at the national or state level have generally used a single criterion such as the number of workers, capital employed, use of electricity or registration with certain public agencies as the basis for identification of the informal sector. This is mainly due to limited availability of data from secondary sources and problems of temporal comparability therein.

**Keywords:** Informal economy, Grey economy, Shadow economy, Underground economy, unorganised workers etc.

## Introduction:

Street vending is one of the most visible and important sustainable occupations in the urban informal sector in India. Street vendors are identified as self-employed workers in the informal sector who offer their labour to sell goods and services on the street without having any permanent built up structure (National policy on urban street vendors [NPUSV], 2006: 11). Street vendors play a very important role in the urban economy of India by providing employment and income and other items. They sell different kinds of goods such as clothes and hosiery, leather made items, moulded plastic goods, and various household necessities, which are manufactured in small-scale or home-based industries where large numbers of workers are employed. It would hardly be possible for the manufacturers to market their own products. Apart from non-agricultural products, street vendors also sell vegetables and fruits. Thus, they provide a market for both home-based manufacturing products and agricultural products, supporting smallscale and home-based workers as well as agricultural workers. Therefore, several sectors and types of labour are linked with the street vendors. Street vendors also support the urban rich as well as the urban poor. They support the urban rich by providing daily requirements right on their doorsteps. Urban youth prefer to purchase clothes and accessories from street vendors, because the products the vendors sell are typically cheaper than those found in formal retail outlets.

**Lower Income Groups:**

People from lower income groups also benefit from the vendors, spending a large portion of their income on purchases from street vendors because their goods are cheap and affordable. It has been estimated that around 30% of the Mumbai workforce buy at least one meal a day from vendors. Thus, it can be said that they are in fact a solution to some of the problems of the poverty-stricken urban dwellers. According to the Government of India, around 10 million people in India as a whole, including about 250,000 vendors in Mumbai, are dependent for their livelihood on street vending (NPUSV, 2006). Interestingly, Mumbai contains the largest number of street vendors among all the major cities in India. The term informal sector and informal economy are used interchangeably to refer to that segment of the economy and labour market, which absorb significant numbers of job seekers and unemployed workers outside Government regulations and formal systems of labour and social protection. The informal sector is becoming gradually recognised as an imperative segment of the labour market in many countries, especially developing and transition countries and thus plays a major role in employment creation, production and income generation. Research efforts in urban employment and urban labour markets have most often focused on the formal sector with an emphasis on industrial employment\* (Mehta 1995: 326). In countries with high rates of population growth and/or urbanisation, the informal sector tends to absorb most of the growing labour force in the urban areas. Informal sector employment is a necessary survival strategy in countries that lack social safety nets such as unemployment insurance or where wages, especially in the public sector are low.

**Under Employment:** In such situation, indicators such as unemployment rates and time related underemployment are not sufficient to portray the labour market situation. In other countries, the process of industrial restructuring in the formal sector is seen as leading to a greater decentralisation of production through subcontracting to tiny enterprises, many of which are in the informal sector^ (Husmanns 1998). Starting from complete ignorance, the phenomenon of informal economic activity has grown to be a subject of study by many researchers, both Governmental and non-governmental level. The nature and the means of the informal economy changed with the deregulation and liberalisation while rules of competition were being set up. Informal labour obviously represents only a part of the underground or hidden or shadow or informal sector. Under employment or informal labour may be defined as additional or primary job, which is performed through by passing regulations of the labour or tax system. Such definition can be applied to both illegal employment between households and enterprises, irrespective of whether they are registered or not, and it also covers self-employment. This definition may also apply to outsiders and to work, which is not paid for. Informal labour can be grouped or classified according to various criteria. It may represent the principal or the additional place of employment. Underground employment may be permanent or temporary. As far as the economic sectors are concerned, illegal employment may be found in industry, construction, agriculture, transportation and services. Illegal employment may be provided by residents and non-residents of a country. The essence of an informal economy is to escape from being measured and captured, therefore both definition and methodologies shall be treated only as a way of approximation more economy is particularly flexible in reacting to changes in the regulatory framework, every ground breaking prohibition or regulation widens its scope and size. Though the term

informal sector has been used to describe a set of economic activities that take place outside the recognised institutional framework, it calls for some further elaboration and clarification. All enterprises operating on own account as well as most of the micro enterprises are assumed to fall outside the recognised institutional framework and hence belong to the informal part of the economy or simply the informal sector.

**Institutional Framework:**

It is obvious that the institutional framework is but a criterion by which the enterprises are classified into formal and informal. Redefining this criterion will no doubt affect the relative magnitudes of the two segments in an economy. But it is unlikely to influence the extent of informal employment because the fundamental causes that contribute to informality in these enterprises have not been misrepresented. It is therefore clear that the institutional framework is only a criterion by which the employment quality is reviewed, it is not by itself the cause of inferior quality. This raises the question concerning what factors contribute to informality in these enterprises. Study on the informal sector worldwide during the last three decades point out that the distinguished characteristic of these enterprises is that they operate in a different business environment than the firms in the formal sector. Fundamentally they lack free access to factor and product markets, public resources, information and opportunities as the formal enterprises carried out. Consequently they opt to operate in an informal manner, avoiding compliance with most regulations. Not only has they perceived diminutive benefit from compliance, more significantly fit compliance adds to the cost of running an enterprise. Lack of access to resources, markets and opportunities is in part the result of non-recognition of these enterprises by the authorities concerned. Without formal recognition few enterprises can anticipate to obtain either credit from the formal financial institutions or access to proper premises and infrastructure. It is difficult to articulate which comes first whether the lack of access to resources and markets forces these enterprises to operate outside the regulation or whether noncompliance with regulations limits their access.

**Self-Employed Unit:**

A self-employed unit operating in an unauthorised location within the country cannot obtain legal recognition until it moves into a proper location and without recognition, it cannot expect to get a proper location from the appropriate authorities which controls the allocation of space. Similarly without adequate economic means it cannot obtain a business license and without such a license, it cannot apply for a loan. But it is clear that both lack of access and non-recognition can help these enterprises by improving their access to resources and markets. It can thus contribute to a reduction in informality. But it cannot eliminate it completely. This is because there are also other factors, which contribute to informality. It is supposed that there exists an institutional bias against the poor and the illiterate, who are disproportionately represented in these enterprises. The markets in developing countries, besides being deficient in many respects are also supposed to be unfriendly to them. Both the regulatory and policy environment is also understood to be unfavourable for these enterprises, origins for this bias can be traced to the mistaken perception among the authorities concerned, most believe that these tiny enterprises are only marginally productive, if not unproductive. Finally, certain social and cultural factors also induce these enterprises to operate under conditions of informality because they limit their access to resources and markets. Women entrepreneurs often cannot have access to credit without the consent of men

in the household or carrot work far away from residence because of family and child care responsibilities. It is this hostile environment that distinguishes these enterprises from the formal ones. It should however be noted that the formal enterprises in developing countries are also often subjected to a variety of limitations including unfavourable policy and regulatory environment and market imperfections. But the consequences to small enterprises are overwhelming in part because of their weak economic base.

Informality will persist as long as these enterprises are not fixity integrated with the mainstream, i.e., the institutionalised part of the economy. One major consequence of not having free access to resources and markets is that few are able to improve upon their initial endowments in terms of physical and human capital and know how, by resorting to transactions in the market, they are obliged to rely on own savings from incomes that are already meagre. These enterprises, already disadvantaged because of the small scale of operation, are farther handicapped by the unsupportive business environment. The net result of all this is to oblige these enterprises to function in a manner that is in striking contrast to those in the formal sector - besides being small in terms of output and employment, they are also labour intensive, use little capital and skills, they often operate without proper business premises, work long hours, work from locations vulnerable to harassment by police, remain invisible, beyond the recognised institutional framework-the visible physical characteristics derived from informality. These are the underlying causes of informal employment, they explain why productivity and incomes are low and the conditions of work are poor in these enterprises. Another consequence of informality is that some of these enterprises choose to avoid dealing with markets altogether by seeking to operate on a subcontracting basis albeit under conditions that are considered less than fair. What distinguishes them from other own account or micro enterprises is that they often have special relationships with their contractors which influence the way they conduct their business as well as their income. Since this class of enterprises is a sub-sector of the informal sector, employment in them also forms part of informal<sup>^</sup> (Psacharopoulos and Tzannatos 1992). But the factors governing their income are different. Similarly some of those operating an enterprise on own account are labelled as home-based workers or home-workers if they operate on a subcontracting basis because they have their business premises within their home or residence, but they nevertheless also form part of informal employment as defined above. At the risk of over simplification it might therefore be stated that the term informal sector or economy refers to a segment of the economy where the agents of production are not only small in scale but also operate under conditions of informality. It thus encompasses all small scale economic activities carried out by individuals, either through enterprises established and operated independently on ovum account, or through micro enterprises with the help of hired workers. They also often engage family labour and apprentices. It should be evident from the above discussion that informality strikes different enterprises differently, because not all these enterprises are affected by various constraints to the same degree. Some are more informal than others, measured in terms of the deviation from the established norms. Evidence from countries show that the extent to which these enterprises have free access to factor and product markets, public resources, information and opportunities varies considerably across enterprises. Some enjoy better access to credit or premises while other do not. Similar observations hold regarding compliance with laws and regulations. Some comply with none

of the regulations while others comply partially e.g., they may pay the market fees or local taxes but not registered or licensed. Regulatory and policy environment affect some more severely than others. These considerations suggest that even though the enterprises are all classified as informal, in reality, the extent of informality varies across enterprises.

**Low Income:** In other words the enterprises are subjected to different degrees of informality. Informal sector is thus far from homogeneous. This also means that the extent of informal employment i.e., low income and poor conditions of work varies considerably in developing countries. From the point of view of efficiency and equity, the loss of output and welfare resume from the presence of informality should be obvious. These informal enterprises devote considerable part of their time and energy on how to overcome informality rather than on improving their business. No attempt however has been made in the literature to measure this welfare loss. This remains a challenge and belongs to the fixture research agenda. Based on evidence one can put forward some general propositions: Enterprises that are smaller, those headed by poor, less educated, women and recent migrants to cities are more likely to be informal\* (Sethuraman 1998). Looking at the various qualitative assessments undertaken in many developing countries, informality could aggravate poverty, either directly or indirectly, through increasing inequality in the access to services and opportunities, increased vulnerability and human abuse. The informality is an important coping means when formal systems have collapsed or are under enormous stress. People recognise that informality is harmful to their standards of living and to the distribution of income in general, but in most cases they have no choice because there are no viable formal alternatives. In some cases, however, there is a perception that through informal means it may be possible to get better deals by performing on connections or just by appealing directly for the understanding of the service provider. Indeed, in countries where formal cost recovery for services has been imposed to try and reduce under the table payments, it is not clear that the poor have been made better off.

**Recent Research:** Recent research has identified a number of potentially negative impacts that informal payments have had on health care, including decreased access to healthcare for women and the poor. These informal payments, however, also allow for services that the State cannot fund to continue to exist. The problem once again is not the informal payment but the under-funding of health services. The relationship between informal payments and access is complex. It may not make much difference to the poor whether high health expenditure is official or unofficial, as hindrances would be equal in both cases. Informal payments, however, make it impossible for the government to modulate health fees in order to facilitate access by the poor. Health indicators and anecdotal evidence suggest that the increase in out of pocket payments has substantially brought down the utilisation of healthcare facilities. People tend to utilise these facilities only under exceptional circumstances. Moreover, many studies show that the poor have been forced to pay an increasingly larger percentage of their income on healthcare. On the other hand, the demand for informal payments may simply arise out of the need to survive.

**Health Insurance Systems:** The introduction of health insurance systems also has a negative impact on access because of the large informal sector in developing countries. The poor in the informal sector do not have formal labour contracts, so no contributions are made by their employer or by themselves to the State pension funds or for healthcare benefits. The result is



that these individuals are not eligible for those services and that little money is actually paid for health insurance. Principally, for those who are at the bottom of the socio-economic ladder and those in rural areas without access to key infrastructure, such as water and sewage systems, health and healthcare conditions are worse. The role of education is very influential in preventing people from falling into poverty and informality. The link between education and poverty is similar to that between unemployment and poverty as unemployment rates fall with every additional level of education. The poor suffer from the larger level of bribes than the non-poor or rich households. With the difficult economic conditions of transition, a number of people no longer value education as much as they did before the transition, their pinnacle priority is mere 8 survival. The interaction between informality and social protection raises two very different issues. First, the poor tend to rely on informal means in the traditional areas of social protection, including help for the aged, the extended family, and the handicapped and for those in extreme poverty. The high demand for benefits from the State and the low level of public funds available for this purpose in many of the countries under review limit the effectiveness of social protection systems. Consequently, many people among the elderly from large families handicapped or others have been left with no other means than their own or family support. The second issue is that the high level of informal activities considerably limits the financing available for formal social protection, especially in countries, in which payroll taxes constitutes the largest source of funds for pensions and other forms of support, such as unemployment benefits.

**Conclusion:** Analyses of informal employment in social assessment and other qualitative studies have emphasised the insecurity, hard work, very long hours, extremely low wage rates and sometime hazardous working conditions. The unemployed rarely choose to become involved in informality, preferring the security of formal employment. Nevertheless, the lack of formal employment coupled with an inability to meet household needs in the absence of welfare benefits or because of the inadequacy of the available assistance, encourages people to turn to the informal economy in response. Likewise perceive the informal employment strategies of the unemployed as a part of a survival strategy, through which some individuals develop alternative ways of working in the face of the existing limited opportunities and the failure of the welfare system. Informality enables the unemployed poor to get some basic income, but what is more important, it may help them maintain a sense of self confidence. Most individuals work in the informal sector only if they have to or if they can supplement their informal sector only if they have to or if they can supplement their informal sector earnings with their unemployment benefits and the social services, such as health care, that are available with these benefits. First of all, for the vast majority, informal sector wages are very low. The more illegal the work, the higher the wages, as well as the higher risks and fines if caught. In turn high taxes depress economic activity and income stabilisation, which brings us back to square one, making informality a mechanism of survival and coping, especially for the poor. Many poor people observe the lack of fair access to the legal system and the lack of security as major components of poverty. The lack of trust in the legal system and the possibility for people to have influence on it in a non-transparent way are major issues.

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