



INFORMAL ECONOMY IN INDIA AND COVID-19

INTRODUCTION

As the COVID-19 crisis continues to unfold across the world, informal workers remain exceptionally vulnerable to the economic and societal impact of the pandemic. Many of these workers are likely to lose their jobs and face extreme poverty and food insecurity as the disease intensifies despite large scale government efforts.

The core of the problem lies in the structure of the informal sector. But what exactly is informal sector and why is it so important? What are the major issues faced by the sector and how COVID-19 has aggravated them? What are the efforts made by the Government to address these issues? How can this challenging time be converted into an opportunity? In the following article, we will try to answer the aforesaid questions.



WHAT IS INFORMAL ECONOMY AND WHY IS IT IMPORTANT?

Informal economy broadly comprises of two parts- **informal enterprises** as economic entities and **informal workforce (employed both in formal and informal enterprises)**. Although, there is no standard definition for informal sector & informal employment in India, different institutions adopt different criterion to understand its extent.

For example, NSSO has been using **employment size (i.e. establishments employing less than ten workers)** for classifying an enterprise as an **informal sector enterprise** (except enterprises legally registered as formal enterprises). Despite their small size and limited individual impact, informal sector assumes importance due to the following reasons:

- **Backbone of the Economy:** Informal Economy **employs more than 90% of workforce** and **contributes about 50% of the gross national product.**
 - Also, share of informal workers is around **10% in the formal sector of the economy.**
- **Important for rural development:** Share of **informal sector in rural areas is significantly large (~75%)**, mainly in areas like agriculture and non-farm economy including low end services.
- **Witnessed substantial growth** in terms of output, share of employment and earnings. Thus ,special attention needs to be given to the sector to make this growth more inclusive and sustainable.
 - For instance, in **2017-18 the share of informal sector employment increased by 3.6%** while on the other hand the share of formal employment increased by only 0.9%.
 - Sustaining high levels of growth are also intertwined with **improving domestic demand** of those engaged in informal economy.
- **Forward and Backward linkages:** Informal sector is becoming **increasingly interlinked with the formal sector**, fulfilling the supply chain gaps and providing essential services.
 - For instance, the physical infrastructure which inhabits the formal sector is largely dependent on informal workforce employed in the construction sector. At the same time, the backward linkages involve the flow of raw materials, equipment, finance and consumer goods from the formal to informal sector enterprises.

GLOBAL STATUS OF INFORMAL ECONOMY

- More than **6 workers among 10** and **4 enterprises among 5** in the world operate in the **informal economy**. This amounts to over **2 billion workers** earning their livelihoods in the informal economy.
- Informal employment represents **90 per cent of total employment in low-income countries**, 67 per cent in middle-income countries and 18 per cent in high-income countries.
- Between 2010 and 2016, informal work made up around **40% of GDP across Sub-Saharan Africa, Europe and Central Asia, and Latin America and the Caribbean.**

CHARACTERISTICS OF THE INFORMAL ECONOMY

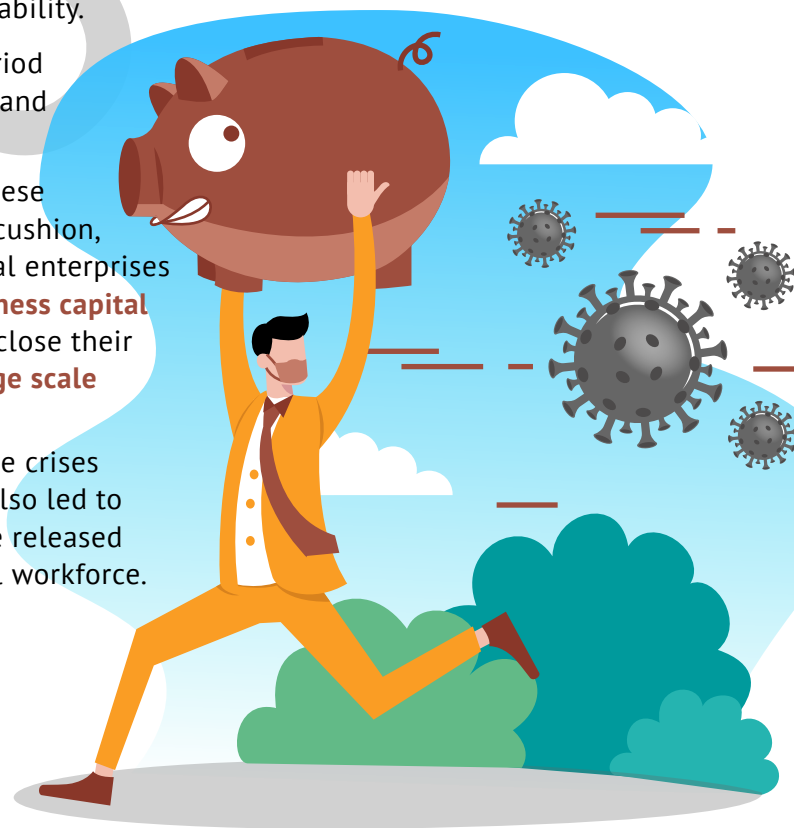
- **Characteristics of informal workforce:** Keith Hart, the Anthropologist who coined the term informal sector, identified the following characteristics- Low skill levels, easy entry, low paid employment and primarily immigrant nature of labour force.
- **Characteristics of the informal enterprises in India:**
 - **Labour relations are based mostly on casual employment**, kinship or personal and social relations rather than contractual arrangements with formal guarantees.
 - Informal enterprises typically operate at a **low level of organization**.
 - Little or **no division between labour and capital** as factors of production.
 - The **share of informal sector is highest in agriculture** as the holdings are small and fragmented, followed by trade, construction, real estate, professional services etc. and other services.

WHAT ARE THE ISSUES FACED BY INFORMAL SECTOR AND HOW COVID-19 HAS AGGRAVATED THEM?

The informal sector in India, including the enterprises and the workforce, faces a multitude of issues. Informal enterprises have to deal with issues like limited availability of capital, poor infrastructure, low productivity of operations, limited technological access and need for a physically functioning market. At the same time, informal workers deal with issues like poor living and working conditions with no security or safety, absence of a job contract and absence of any kind of employer accountability.

The combination of these issues with an extended period of lockdown has led to disruption of business activity and is **affecting informal enterprises in following ways:**

- **Limited savings or capital availability:** Given that these enterprises have meagre savings or other financial cushion, in the face of the pandemic, most owners of informal enterprises may have no choice but to **use their negligible business capital for consumption**. As a result, they may be forced to close their business temporarily or permanently, **leading to large scale closure of such enterprises**.
- **Possibility of further increase of informalization:** The crisis has not only impacted the informal sector but has also led to **closure of several formal enterprises**. The workforce released by these firms tends to get absorbed in the informal workforce. (Especially in current times, when growth of formal employment is limited.)
 - Also, the uneven impact of the crisis in different sectors may trigger large-scale restructuring of economic activities. The resultant restructuring of economic activities and supply chains could lead to **frictional unemployment or further expansion of the informal economy**. For example, formal sector employees in tourism sector (negatively affected sector) may join informal workforce before they are employed somewhere else formally.





- **Absence of regulatory framework:** Informal enterprises largely remain unregulated in the normal times. But in the current time, the need for monitoring of these firms tends to generate **ad-hoc mechanisms which create multiplicity of regulations** from central, state and local authorities. This makes business environment very difficult to manage, indirectly forcing the smaller firms to deviate from the guidelines thus increasing the risks for everyone.
 - The circumstances of informal enterprises combined with institutional weakness and corruption tend to further **encourage rent-seeking behavior.**
- **Decreased marketplace in future for informal enterprises:** The measures to control the pandemic such as lockdowns & limited social contact has indirectly forced a change in the consumer behavior. This behavioral change has shifted a substantial section of informal market to formal market. For example, COVID-19 induced growth in the market of e-commerce firms.
- **Intensification of social issues prevalent in informal employment:** The informal sector was already grappling with issues like child labour, exploitation of workers, bonded labour and human trafficking. The large-scale unemployment, resultant loss of income and increased informalization created by the crisis could intensify these issues.

The impact on informal enterprises combined with limited health and social security available to **informal workers** has resulted in the following:

- **Large-scale unemployment:** According to some estimates, more than **80 percent workers** in the informal sector **lost employment** in India. About 75 percent of these workers were small traders & daily wage-labourers. Also, even where work is still available, there is likely continued **loss of wages because working hours have decreased drastically.**
 - A direct corollary of increased unemployment was the **migrant crisis.** Majority of the migrant labourers lost their job during lockdown. Without any clear communication and subsequent increased social tension, they were left to fend for themselves. This resulted in a scenario where **millions of workers were on roads trying to walk back home, hundreds of kilometers away.**
- **Increased Poverty:** The '**Hand to Mouth**' nature of informal employment creates a scenario where any loss of income directly affects the consumption levels. It is estimated that, **lost labour income** may result in an increase in relative poverty for informal workers and their families.
 - Also, absence of income combined with little or no health coverage could result in **high incidence of indebtedness** among these workers. Some estimates suggest that around 53 percent workers had incurred additional debt during the lockdown.
- **Increased food insecurity:** Informal food markets play an essential role in ensuring food security, both as a **source of food and a place for smallholder farmers** to sell their products, and their closure could lead to increased food insecurity.
 - **Logistical challenges** created by the pandemic within the supply chains may lead to disruptions in food supply, further compounding the problem.
 - It is also indicative of the **lack of food reserves in poor households,** their inability to save and stock up and their low levels of enrolment and access to welfare schemes such as the public distribution system.
- **Disproportionate impact on Women in informal sector:** Women are more exposed to informality and are often in more vulnerable situations than their male counterparts.
 - For example, the new 'social restrictions' imposed on domestic workers have resulted in financial as well as psychological setbacks for them – these restrictions have led people to ostracize them.
- **Increased vulnerability both at work and at home: Lack of awareness** about the virus, its symptoms and preventive measures, **and lack of protective equipment expose** informal economy workers to the virus at work. Simultaneously at home, overcrowded and unsanitary living conditions make physical distancing nearly impossible.

The Pandemic has been pushing the informal workers to stay at home, but not working and staying at home means losing their jobs and their livelihoods. In the absence of any help or support, this creates a **cruel dilemma** for them- **"To suffer from hunger or from the virus."**

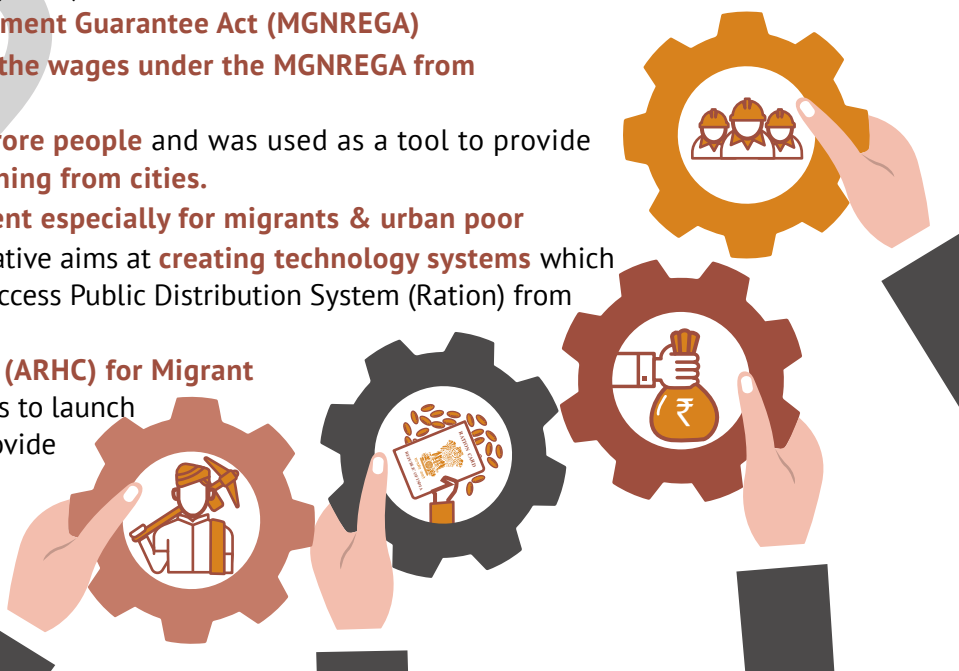
WHAT LED TO THE GROWTH OF THE INFORMAL ECONOMY?

- After independence, India adopted a **state-led industrialization model** which could not absorb large labour force and as a result, the **increased labour was nudged towards informal sector**.
- **Poor incentives structure for small enterprises** encouraged them to remain small, **in turn stalling the possible growth of formal workforce in those firms**.
 - Encouraging small firms to remain small creates a market dominated by tiny firms and large firms, with the share of medium sized firms being very small. This is referred as the **problem of 'missing middle'**.
 - The long-term consequences of this problem are economic inequality and persistent unemployment thus **encouraging a scenario of jobless economic growth**.
- Most of the state and central **labour laws** were applicable to larger enterprises.
 - This indirectly forced formal enterprises to be **become more technology-intensive rather than labour intensive**.
 - It also **disincentivized informal** firms to move to the formal sector.
- From the supply side, majority of the workforce then (and even now) **does not possess the requisite education & skills required** to enter the formal workforce. For instance, as recently as 2017-18, only 2.4% of the workforce has formally acquired any vocational education or training.

WHAT ARE THE EFFORTS MADE BY THE GOVERNMENT TO AMELIORATE THESE ISSUES?

To address these issues, Government has adopted a multi-pronged strategy, simultaneously focusing on establishing clear and effective communication, provision of immediate financial support and expansion of health protection alongside institutional measures to strengthen the sector in the long-term.

- **To reinvigorate informal enterprises:** The primary objective is to provide immediate financial support to informal enterprises and create a growth trajectory for future. For example, **collateral free Automatic Loans for Businesses** were announced in order to provide them with **working capital**. (An **Emergency Credit Line** has been created under it.)
- **To address the plight of informal workers:** These measures collectively aim to provide income & food security to informal workers which indirectly fills the social security gap present in the current setup of informal economy.
 - **Pradhan Mantri Garib Kalyan Yojana (PMGKY)**
 - ✓ It **aims to provide free food** (through Pradhan Mantri Garib Kalyan Anna Yojana or PMGKAY) by acting in concert with the Public Distribution System (PDS) to provide food rations to **80 crore beneficiaries** registered under the National Food Security Act (NFSA).
 - **Mahatma Gandhi National Rural Employment Guarantee Act (MGNREGA)**
 - ✓ The Union government has **increased the wages under the MGNREGA from Rs 182 to Rs 202**.
 - ✓ **MGNREGA now covers more than 27 crore people** and was used as a tool to provide employment to migrant workers returning from cities.
 - **Other key efforts made by the Government especially for migrants & urban poor**
 - ✓ **One Nation One Ration Card:** The initiative aims at **creating technology systems** which will be used for **enabling migrants** to access Public Distribution System (Ration) from **any Fair Price Shop in India**.
 - ✓ **Affordable Rental Housing Complexes (ARHC) for Migrant Workers/Urban Poor:** Government plans to launch the **scheme under PMAY** in order to provide ease of living at affordable rent.
 - ✓ **Special Credit Facility for Street Vendors:** Scheme aims to facilitate easy access to formal (up to Rs. 10000) for street vendors.



LABOUR LAW REFORMS AND INFORMAL ECONOMY

The envisaged consolidation of all the **labour laws into four labour codes** will also impact the institutional framework in which the informal sector operates. It can be seen through following provisions:

➤ Code on Wages, 2019

○ A concept of statutory **Minimum Wage** for different geographical areas has been introduced which may also indirectly push the wages of the informal workforce upwards.

➤ The Industrial Relations Code, 2020

○ An establishment having at least 300 workers is required to seek prior permission of the government before closure, lay-off, or retrenchment. The **relaxation** may **encourage several informal enterprises to move towards the formal sector**.

➤ Code on Social Security, 2020

○ The code expands the **definition of employee to include informal workers**, widening present social security net.
○ It states that the central government will set up **Social security funds for informal workers, gig workers and platform workers**. Further, state governments will also set up and administer separate social security funds for informal workers.

➤ Code on Occupational Safety, Health & Working Conditions, 2020

○ Several measures like mandatory health check-up in factories, appointment letters for all workers, penalty on employers and relief for employees in case of accidents could help **improve the health security available to the informal workforce**.
○ Also, **mandatory license for every contractor** who provides or intends to provide contract labour will indirectly ensure better wages and working and living conditions for contract workers.

The consolidated labour codes will by and large subsume all the major laws indirectly regulating the informal sector such as Contract Labour (Regulation and Abolition) Act, 1970, Interstate Migrant Workmen Act, 1979, Building and Other Construction Workers (Regulation of Employment and Conditions of Service) Act, 1996 and Unorganized Sector Workers Social Security Act, 2008.

CAN THIS CRISIS BE CONVERTED TO AN OPPORTUNITY? IF YES, HOW?

The structural void created by the crises in terms of economic activity and employment gives us an opportunity to redesign more equitable and effective economic architecture. Also, the process of this transformation can be made more inclusive by involving all stakeholders and building trust in order to provide better interventions for the future:

➤ Strengthening health systems to ensure access and protection for all:

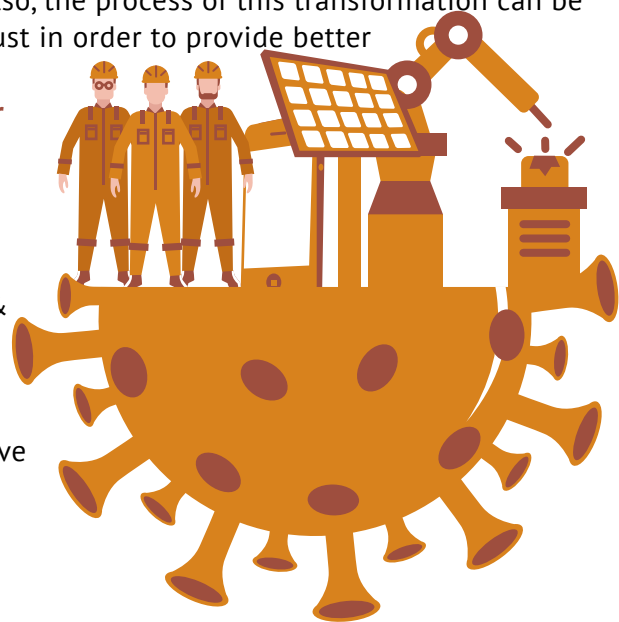
The health issues created & aggravated by COVID-19 have underlined the imperative need to strengthen health systems' capacity and resilience in following ways:

○ **Closing gaps in health coverage and ensuring equity in the use of services**, in particular to avoid gender-based discrimination & secure access for groups particularly vulnerable to exclusion, such as low-income households, migrants, and disabled or chronically ill persons.

○ **Capacity building of healthcare systems:** Healthcare systems have to overcome the structural inefficiencies like poor accessibility and affordability and fragmented nature of the system among others. These inefficiencies create barriers that are particularly high for those in informal employment.

○ **Increased allocation:** The aforesaid measures need a sizeable increase in the public resources allocated to the health system and, equally important is greater effectiveness and efficiency in the use of available resources.

➤ **Building universal social protection:** The COVID-19 emergency has underscored the worrying consequences of insufficient coverage and efficiency gaps in social protection for workers in the informal economy. It must trigger reforms on following lines:

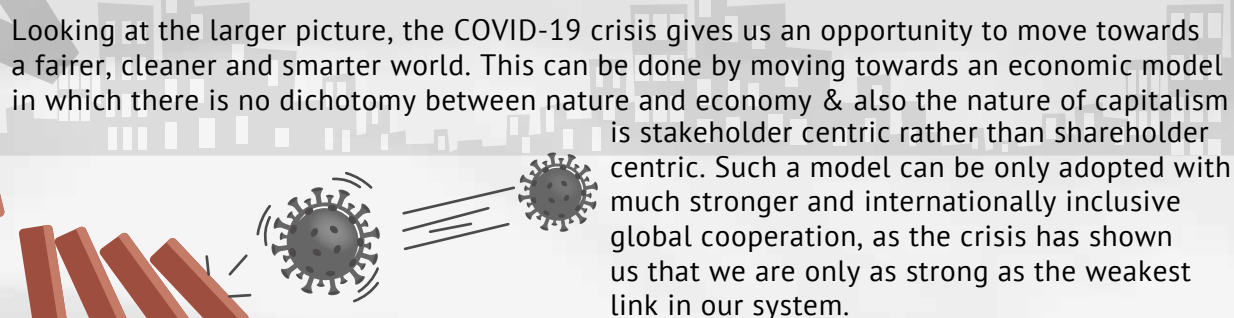




- **Employment security:** Providing employment security directly provides income security to the informal workforce. The positive impact created by MGNREGA over the years and especially during the pandemic has reignited the **idea of an urban equivalent of MGNREGA**.
 - ✓ Such a programme could help **mitigate any further shocks to urban economy** in the future. Also, providing urban workers a legal right to employment could lead to positive effects on low earnings in the urban economy and a possible slowdown of unsustainable concentration of migrant workers in only a few cities.
 - ✓ **Several states have already taken the first steps** in this direction. For instance, Kerala, Odisha and Himachal Pradesh run urban employment programmes.
- **Adequate social protection** coverage for workers in **all forms of employment, adapted to their circumstances**. In particular, in the areas of sickness & social assistance benefits in the form of both cash transfers & food support.
- **Fair cost-sharing:** The Social protection has to be based on a fair sharing of the cost between employers, workers and governments, and ensuring compliance with labour and social security legislation.
- **Building Back Better-Informal Economy:** In supporting the recovery of productive economic units, there is an opportunity to step up their productivity, resource utilization and networking ability through:
 - **A conducive business environment that** will ensure that the firms are recovering at their optimum speed. Rebuilding the business environment also gives us an opportunity to iron out the structural deficiencies like reformation of labour laws.
 - **Adequate incentives and technical assistance** that can facilitate increase in productivity of both informal units and workers along with encouraging a more competitive economy.
 - **Reaching and connecting informal units:** By working in concert, financial technologies, workers' organizations, business associations and networks, and the local government agencies can help connect the informal units with the ecosystem.
- **Strengthening representative workers' and employers' organizations:** During the last decade, employers' and workers' organizations have made great progress in affiliating those in the informal economy and/or in delivering services to them. The current crisis is an opportunity to strengthen these ties further:
 - **Foster social dialogue:** These organizations need to further strengthen their relationships with workers and enterprises in the informal economy. This will foster social dialogue that is inclusive and more responsive to the specific needs of informal economy operators.
 - **Increase inclusiveness through women participation:** It also provides an opportunity to enhance women's participation in social dialogue processes so that their specific constraints in the informal economy are addressed.
- **Facilitating the transition to formality:** The COVID-19 crisis has again highlighted the issues associated with informalization of economy i.e. absence of appropriate data, absence of registration and consequently recognition and financial and social vulnerability of these firms. This urgency could be used in following ways:
 - **Further strengthening various efforts made by the government** to increase formalization in the form of Goods and Services Tax, Demonetization, EPF reforms, Skill India initiatives, Fixed Term Contract Reform, as well as the Maternity Benefit reform.
 - **Measures to mitigate the contraction of the formal economy**, especially micro and small enterprises, are critical to prevent further "informalization". Special attention should be paid to those enterprises hovering on the edge of informality, as they could easily shift to the informal economy in order to survive.

CONCLUSION

The ideal solution to the problem of informal economy would be complete formalization of the economy. But reaching the ideal stage would require a transition period which is economically inclusive, socially protective & institutionally supportive of every worker participating in the economy. Such a scenario is only possible if due recognition is provided to the informal sector, from creation of a comprehensive statistical database to being a part of policy considerations.



Looking at the larger picture, the COVID-19 crisis gives us an opportunity to move towards a fairer, cleaner and smarter world. This can be done by moving towards an economic model in which there is no dichotomy between nature and economy & also the nature of capitalism is stakeholder centric rather than shareholder centric. Such a model can be only adopted with much stronger and internationally inclusive global cooperation, as the crisis has shown us that we are only as strong as the weakest link in our system.

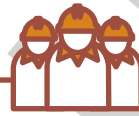
- **Meaning**
 - **Comprises of informal enterprises and informal workforce.**
 - **No standard definition**, different institutions adopt different criterion.
- **Importance**
 - **Backbone of the Economy** (~50% contribution in GNP and ~90% in employment)
 - **Important for rural development**
 - **Witnessed substantial growth** in terms of output, share of employment and earnings
 - **Forward and Backward linkages with the formal sector**

INFORMAL ECONOMY

ISSUES AGGRAVATED BY COVID-19

➤ **Related to Enterprises**

- Limited savings or capital availability
- Possibility of further increase of informalization
- Absence of regulatory framework creating ad-hoc regulatory mechanisms
- Decreased marketplace in future for informal enterprises
- Intensification of prevalent social issues such as child labour



➤ **Related to Workforce**

- Large-scale un-employment
- Increased poverty
- Increased food insecurity
- Disproportionate impact on women working in the sector
- Increased vulnerability and risk of COVID infection

Measures taken by the government to ameliorate the above issues

- **To reinvigorate informal enterprises** by providing them with working capital.
- **To address the plight of informal workers** through schemes like PMGKY & MNREGA.
- **To support migrants and urban poor** through schemes like One Nation One Ration Card, Affordable Housing Complexes, Special Credit Facility for Street Vendors etc.
- **Codification of labour laws**

How can this crisis be converted to an opportunity?

- **Strengthening health systems** to ensure access and financial protection for all
- **Building universal social protection framework**
- **Building Back Better-** by stepping up recovery and productivity in Informal Economy
- **Strengthening representative workers' and employers' organizations**
- **Facilitating the transition to formality**