

Market development of informal services sector with formal sector linkages in India

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Abstract

Objective of this study is to analyse variables affecting development of market for services in informal or unorganized sector. The extant literature studies informal sector from view point of manufacturing enterprises, emergence of informality and urbanization with migration of labour from primary activities and challenges of dualism of urban and rural as well as formal and informal employment resulting in income disparities. The services sector which is now a bigger contributor to economic growth in India as also in developed economies mainly discusses tradable services in formal enterprises and its linkages with informal sector. There is a large space remaining uncovered of personal and household services and human development services where infrastructure support and intervention from public and private institutions could upgrade services offered and provide marketability to the sector. The changes taking place in Indian economic policy and technology environment presently in the direction of formalization needs to be examined. Services in informal sector have an important bearing on human capital and social capital development.

Keywords: Formal and informal sector linkages, Non-tradable services, Social capital, Human development.

Introduction

In India, there is no unique form of government registration for identification as formal enterprise though some voluntary and mandatory registration systems for specific purposes could be availed. Another characteristic is the employment size which in Indian context, is nine workers. System of National Accounts (SNA) (1993)³⁰ defines informal sector “in terms of characteristics of the enterprise rather than in terms of the characteristics of the worker.” However, the National Commission for Enterprises in the Unorganized Sector (NCEUS)²¹ census of informal sector employment - NCEUS decided to complement the definitions of unorganized/ informal sector with a definition of informal employment. “Informal workers consists of those working in the informal sector or households other than workers with social security benefits provided by the employers as well as the workers in the formal sector without any employment and social security benefits provided by the employers” as Naik A K (2009)¹⁸ cited National Statistical Commission (2001)¹⁹ in his paper “Informal Sector and Informal Workers in India”.

The prevailing definition accepted across disciplinary and ideological boundaries is that the informal economy refers to income generating activities that operate outside the regulatory framework of the state (Portes, A., Castells, M., and Benton, L.A.) 1989;²³ see also De Soto 1989;² Feige 1990;³ Harding and Jenkins 1989.⁴ An important development in this regard has been the ILO’s (2002)⁷ amendment of the definition of informality to cover not only informal firms and their workers, which was the focus of the original term “informal sector”, but also unregistered or unprotected labour working in formal sector firms. This has resulted in a more precise terminology laid out by Chen (2012)¹ in a recent working paper. The ILO (1972)⁷ WIEGO¹⁶ terminology defines economic informality in terms these central concepts.

Materials and Methods

Methodology used is of literature study as the subject matter is related to historical evolution of informality in economies the world over and how between 1990s till now, there is a particular interest in services marketing. Subject matter of my enquiry is to fill the research gap in applying formal-informal sector linkages to market development of services provided by informal sector with reference to non-tradable services. I have referred to close to 30 resource-materials for the study.

Features of Informal Service Sector Units

The informal service provisioning unit are characterized by ease of entry with reliance on indigenous resources or in-house skills, mostly being family ownership of enterprises with few employees if any. These units are a tiny scale of operation in labour-intensive technology with mostly life-sustenance model in place, they do not generate any additional resource for future growth. They acquire skills with the job training. They specialize in skills and craft based service delivery and work in unregulated and competitive markets, nor can they invest in keeping up with contemporary best service delivery practices.

Chen (2012)¹ citing Swaminathan M (1991)²⁹ have identified different schools from different proponents as listed below under two sets. This distinction is based on empirical characteristics of production, distribution and technology activities of marginal and traditional enterprises compared to formal sector units. The different approaches to causal analysis could help us also to articulate approaches to work on market development strategies for informal sector services.

Dualist, Structuralist and Flexible Specialization School

This set of school of informality owes it to internal factors affecting units such as flow of cheap labour with rural migration into a family or community failing to get

absorbed in formal sector or structure of industry or flexibility of adapting to changes in environment because of smaller size enabling changeover without much investment or transferring the risk of technology obsolescence to informal sector respectively.

Dualist School

Lewis W. A. (1955)¹⁰ in his classic "Economic Development with Unlimited Supplies of Labor" developed Dualist Economic Development model to propose that development process goes on at two levels based on labour flow. 1) Modern or more productive sector which could also be formal enterprise employing better skilled labour and being capital intensive or technologically advanced attracts easy flow of labour for better skilled job for better wages. 2) Traditional or informal sector, less productive, small in scale and technologically backward running on subsistence wages would absorb the labour even at subsistence level only because it is available at a lower wage levels and ready to take on less skilled jobs. As per this school, it would seem that informal sector can never catch up with formal sector considering population growth resulting in excess labour supply.

Structuralist School

Whereas Moser (1978);¹⁷ Portes et al (1989)²³ suggest that informal enterprises are subordinated to formal units in a structure of industry or services where scope exists for informal sector to play second fiddle to formal enterprise for the reason of factor efficiency and cost control to meet competitive environment emphasizing the complementary nature, continuities and linkages between both sectors. It was suggested by Lewis W. A. (1955)¹⁰ that the solution lies in modernizing the traditional sector and progressively increase the space of formal units as informal sector size shrinks. However, the increasing labour supply which was not absorbed by the formal sector kept on increasing informal sector size and scope of activities.

Flexible Specialization School

As per Flexible Specialization School, Swaminathan (1991)²⁹ characterizes informal enterprises as enjoying organizational flexibility and operational responsiveness or nimbleness in offering new technological solutions or adapting to new ways of operations and thus being competitive and recommends to pursue flexible specialization and customization and ICT solutions purposefully. Swaminathan (1991)²⁹ suggested that small units can be dynamic with help of cluster development or area development policy to survive or perform competitively.

Exclusionist School and Legalist School, Voluntarist School

This set of informality is mainly the result of government policy and ability or inability of units to grow out of informality. Mazumdar (1976)¹³ defined exclusionist school of informal sector to explain how some informal

enterprises are excluded from the state regulations and outside the protection of government or union actions, either because of missing legislations or institutions. Government need to step in and legislate and provide support to them as a solution. On the other hand, D Soto (1989)² suggested of legalist school as how some units are happy to continue as informal enterprise in order to meet the challenge of excessive regulations as meeting the bureaucratic red tape would increase the costs of operations and decrease competitiveness. They see the hostile legal environment and registration formalities too burdensome and choose to voluntarily work at sub level or informal level. Chen (2012)¹ talks about voluntary school as cost benefit analysis of informality in comparison to formality, also perceived as ease of starting and operating a unit and encourage the self-employed or tiny unit to voluntarily remain at that level of informality. Added to that is avoidance of taxation. Feige³ in an article (1990:991-993) mentions the unreported economy where some incomes are generated by violating legality of commerce and some by circumvention or evasion of fiscal rules as codified in the tax code.

Formal and Informal Sector Linkages for Market Development

For different categories of informality, the different approaches would be needed for extensive mapping, tapping, vesting/divesting and contesting informal sector so that response from formal sector, institutional and government could be designed for effective linkages to formal sector without compromising interests of informal sector units.

Meagher, K. (2013)¹⁶ references literature study on linkages between formal and informal sector in developing economies and discusses about role of linkages between two sectors of the economy as a strategy for empowering informal sector and puts them in four categories based on nature of relationship as per literature study, while pointing out how some are complimentary while some are exploitative; some are result of choice and some are result of circumstantial compulsion. Forward linkages enable assured market for their services provisioning, provide market linkage platform and/or support by way of aggregation of services needed by formal sector units. This could be done by a formal sector unit helping non-formal sector unit in a backward linkages with skill and technology upgradation, setting quality standards and giving guidance in technical input and possibly. Meagher K. (2013)¹⁶ studied literature on linkages from four perspectives: mapping of economic linkages, linkages as mechanisms of institutional design, linkages and governance transformations and the politics of linkages.

Mapping Economic Linkages

While the vast majority of this literature focuses on initiatives to tap the informal economy for cheaper models of service provision, a critical dimension in the literature views linkages as means of tapping the informal economy for the benefit of the formal economy by either process of

co-production or outsourcing (Ostrom 1996).²² The section of formal sector which benefits from economic linkages outsource the part of their operation to informal sector units for the objective of being competitive, to control cost structure within their own enterprise and to remain adaptive to changes in market and technical upgradation. In many cases there is some modicum of training of manpower and forward and backward linkages tied to collaborative result.

However, it could be said that the exploitative nature of linkages could not be entirely avoided. Study of the patterns of linkages between the formal and informal economy, and the flows of resources such as labour and information between the two sectors, including analysis of national, sectoral, inter-sectoral units linkages in labour market, financial flows and linkages within global value chains could help decide how the benefits flow between formal and informal sector units. This could lead to market development strategy for informal sector services as follows.

ICT (Information and Communication Technology) Platform for Market Exchanges

Thus, accepting structuralist and dualist as well as flexible specialization schools argument of nature of existence of informal sector, market development strategy could emerge from enhancing the strength of individual tiny units by creating flexible specialization process for their aggregation in a virtual cluster as would have been the case in a physical environment for their coming together to create benign business environment of mutuality of interests among them. ICT can help in this process by enlisting the enterprises, imparting skill training on the job, creating access to better technology to be shared in value additive process or building up on complimentary nature of formal and informal sector, facilitation of networks for markets and inputs. ICT platform could be for a specific industry focused market development strategy with of aggregation of marketing for cluster based informal units. In this process, some of the units will specialize in subset of value additive process.

Producers' and Marketers' Co-operatives

The co-operatives could be formalized organization enlisting informal units as members to undertake market development for members run on economic parameters. They could be formal or informal in constitution depending upon size of membership or nature of scale of service activities. They could be assisted by other institutions or government. They could extend all help in market and marketing, including training, hiring of manpower, delivery platforms, sharing of premises and some finance. Some small scale co-operatives work on the basis of contributory approach of inputs from members in a small community or extended families of craftsmen or specialized skills. Self-help groups are quite effective in organizing manpower in part-time service provisioning by organizing unemployed men and women at homes.

ICT Platforms and Sharing Economy

One way of formal sector linkages is ICT support in "sharing economy" which connects markets for services such as transportation and haulage, renting of rooms and other assets, repair services, odd jobs and running of errands, care taking for children, old and sick. The sharing economy can be seen as an ICT-enabled informal economy which is able to deal with issues of trust, quality of services and reliability even though there is no direct personal connectivity by building service review feedback from users creating "the trust that the customers have on the Uber drivers, and the trust that Airbnb guests have on their hosts have successfully connected people with someone they have never known before. The peer-to-peer platforms of Uber and Airbnb have successfully enabled the customers and the supply side of both companies to interact with each other process of riding Uber cars or lodging the Airbnb properties" (Maznah Mohd Zin et al (2017)).¹² These ICT platforms would enable transactions in the sharing economy to provide a basis for data base creations and beneficiary schemes to reach informal units and enable authorities to evaluate the data for financial, technical and skilling aid and administer the schemes aimed for the purpose with efficiency and equity. Even the preferential sourcing by institutions can be organized to aim at market development. "The entrepreneur that supplies goods and services on the platform, typically an individual or small business" is mostly from among informal sector service providers. (Maznah Mohd Zin et al (2017)).¹²

ICT platforms with services like Uber and Airbnb could help create new business models for informal sector in skill development, financial help, for quality and skill upgradation with relevant technology and supporting with marketing networks. This model could be effectively used for market development of most of the presently non-tradable services such as referred above, e.g. personal, repair and maintenance etc....the list could be endless and make them more rewarding to informal sector units. Some would have opportunity to upscale previously informal and small-scale units into formal sector.

Practice of Subcontracting and Linkages with Empowered Informal Enterprises

Pressure to cut costs and increase flexibility of production planning, together with strict labour laws affecting only formal enterprises provide incentives to formal enterprises to subcontract activities to the informal sector (Mazumdar & Sarkar 2008;¹⁴ Ramaswamy 1994;²⁶ Siggel E., 2010.²⁸ Similarly, subcontracting is the natural response of large unionized firms in India. (Ramaswamy, 1988.²⁵ Thus formal enterprises and informal enterprises also tend to exist in a complementary relationship, born of socio-economic and legal environment, and are at a comfort-level niche operational existence in their own scale of enterprise. Siggel E., (2010)²⁸ explains how, after economic reforms in India in the 1990s helped informal sector thrive with expansion, both in labour supply and in

demand, through outsourcing, skill transfers and new enterprises” and informal sector thrives to tackle the issue of labour retrenchment from formal sector.

By the early 1990s, research on formal-informal literature on linkages had generated two reviews, the first, an ILO working paper by Harriss J. C. (1990)⁵ and second, by S.V. Sethuraman (1992),²⁷ a note in a bibliography on “The Urban Informal Sector in Asia”. Both reviews focus on the nature of linkages and their effect on the prospects of the informal economy development. The understanding of formal-informal linkages involved was based largely on analyses of resource flows via interfirm linkages. And assessing how linkages structured flows of resources between the formal and informal economies and whether these were beneficial or detrimental to the growth of informal sector enterprises focusing on local or national level linkages, and on direct (forward and backward) and/or indirect (factor markets, production structure or consumption) linkages recognizing that effects of linkages were mixed, not totally beneficial or detrimental. In two decades since then, with effects of liberalization and globalization such as network analysis, global commodity/value chains, focus is also on for whom those benefits are and what regulations are necessary to ensure benefits percolate to informal sector too, besides formal sector by analyzing the nature and effects of linkages between the formal and informal economies.

Linkages as Mechanisms of Institutional Design

Institutional designs could be around the theme of tapping linkages like in case of “the Bottom of the Pyramid” (BoP) marketing approach by Prahalad, C. K. (2004),²⁴ in which linkages are used for creating institutional mechanisms for linking formal business by building ties and synergies with informal service providers and formal sector institutions for creating a marketing platform while meeting social goals. As BoP gurus London and Hart (2011:10)¹¹ explain, “BoP ventures thus seek to combine the best of both worlds – the resources and technological capacity of the formal economy and the indigenous knowledge, human face and local embeddedness of the informal sector” as quoted by Julius Gatune (2015)⁸ add “is a market-based approach for poverty reduction that considers the four million poorest people in Sub-Saharan Africa resilient entrepreneurs and value conscious consumers” as quoted by Karin Nijenhuis Weblink: <http://includeplatform.net/downloads/developing-the-informal-sector-for-inclusive-growth>.

Self Help Groups

Linkages could be used as a means of “tapping” institutional resources across the formal-informal divide for purposes of informal sector empowerment. This includes co-production and social sector or nonprofit sector participation in informal economy e.g. micro finance companies advances credit to tiny units by tapping them and creating helpful linkages for them. There is an increased emphasis on creating institutional mechanisms to connect

and make effective formal-informal linkages in addition to economic connectivity such as market development and resource flows.

Non-profit Sector Linkages for Social Capital Development to help in Market Development

As non-profit sector provides some services as public good to a specific segment of informal sector or society or to a selected geography for reasons of their organizational charter or resources or kind of services or activities, they also develop a connectivity to beneficiary units or households. This could be used for mapping and tapping those in need of support to reach out to remunerative markets. NGOs or non-profits would like to facilitate this process for augmenting their social objectives. When they reach out, the beneficiaries could also develop connectivity among themselves by their own initiatives.

Linkages and Governance Transformations

The role of the state is very relevant and significant. One thing it could do is the outsourcing of public functions to the informal economy with legal identity such as cooperatives to ensure that informal units are formalized and service provision or market development is on fair consideration basis.

Beneficiary relationship for Enumeration of Informal Sector Units and Government Role

Some government steps are necessary for creating enabling rules and regulations framework to reduce illegality by encouraging registrations with easier norms and possibly creating beneficiary status for new enlisted informal entities to gain easier access to markets with finance, technology upgradation help, quality assurance help, aggregation platforms for government’s procurement et. India has recently made many policy changes and adopted measures in this direction. The tiny units and unemployed household members could be provided necessary skill set and initial finance at a subsidized rate of interest to enable them to upgrade their skill levels and improve the tradability of their services which could become self-sustaining units in time to come. This way, they become part of mainstream economy and might be able to create employment for others.

ICT and Institutional Access for Mapping by creating non-legalistic beneficiary registry for tiny units could be an effective strategy in an answer to Exclusionist, Legalist School and Voluntarist Schools by facilitating ease of starting an activity and helping it grow with various incentives and access to finance, technology, skills and markets. The fear of legalese would be nullified when the units learn that the mapping and enumeration is for their benefits rather than to necessarily regulate them or to just collect some tax or charges. The benefits to the macro economy as a result of this this initial IT infrastructure and other facilities would be an essential fulfilment for a state towards the informal sector growth.

Mobile money applications such as India's BHIM and Bharti Airtel's micro-insurance products on mobile communication based technologies could provide financial services access to tiny units. DBT schemes being administered by Indian Government prevent leakages in benefits transfers and provide an excellent platform for automatic registration of informal activities made easy for beneficiary relationship between government and informal sector.

Market for Primary Services (Health, Education, Cultural and Skill Training) Provisioning to Unorganized Sector: Human Capital and Social Capital of an Economy

These services build up human capital at an individual level and a social capital at collective level as the knowledge is added; talents, skills and abilities are acquired with training and experience, making an individual intelligent and rational decision maker and help the persons from informal sector to move to formal sector. Creating social infrastructure for facilitating service delivery and improving standard of living of those engaged in informal services might not happen if left to private capital alone as the revenue model is weak. As service sector is labour intensive, the growth in this sector can also make a big contribution to employment generation and becomes a socially desirable objective for business organizations. Thus, services in basic needs category such as primary education and health care, nutrition, sanitation, hygiene, child care, old care, crèches, family counselling, affordable housing at minimal level, and an equally essential needs like skill development, open spaces for sports, fresh air, cultural activities and performing arts, hobbies and crafts from the perspective of human empowerment and getting access to better standard of living could collectively create a huge market development framework with government initiatives.

The Politics of Linkages

In context of market development for informal sector, political dialogue could facilitate initiatives to be taken by government with steps bordering on social welfareism as a state policy by providing pricing support by way of subsidized rates of inputs for the services provided by informal units singly or through a collective organization and alliances, multi-stakeholder networks involving informal economies.

Results and Discussion

Basic finding of the study relates to ease of application of four perspectives discussed above with literature study compiled by Meagher, K. (2007)¹⁵ suggesting how linkages are not absolutely beneficial or exploitative to informal sector units and how after globalization, though the application of linkages to marketing of tradable services has helped trade expansion, question remains as to for whom the benefits flow. I have attempted to discuss in detail under each of four perspectives, keeping in view the origin of

informality, to apply the formal-informal linkages to non-tradable services as social and human capital development strategy.

Conclusion

Informal service sector has to benefit from potential to create employment opportunities and thus market development of non-tradable services could be facilitated by making them productive and marketable services from its present subsistence nature of production and consumption. For this to happen, informal service sector would need a sustained state support, inter-sector linkages and creation of social infrastructure as well as ICT network platforms by mapping and enumeration. One way is to make voluntary compliance to enumeration and regulations beneficial and easy as part of incentivizing process where registration of units leads to visible benefits like monetary incentives or access to common infrastructure. Further research scope with large sample size exists as present study has resource limitations.

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