

does the government not act proactively and consider their problem as a part of the general development process?

According to our finance minister Mr P. Chidambaram, "The hard fact is that there are certain situations like high oil and commodity prices in international market, expenditure on oil, fertilizer and food subsidy that have shot up and on which we do not have control, and so we have to face the consequences." As per his statement, the basic fundamentals of the Indian economy are still strong.

It might be easy for him to say that, but it is difficult for the people who suffer because of it. Poor people can't afford these prices; their lives have become a challenge. If we move around the countryside, we may find their plights overshadowing their happiness. The government should take immediate steps to reduce the prices of commodities and bring about real growth of our economy. When we will start considering villages and their problems as a part of the nation building process, then we would be a country that shall reach the heights of development.

Lifting the Veil: The Informal Economy

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There are 2 facets of our economy - the formal sector and the informal sector. While much is known about the formal sector, the informal sector is like a hidden chest of lost treasure. It constitutes everything outside the realm of the formal sector. From the private security guards, household help, drivers of cabs, *dabbawalas*, *presswalas* etc;

it includes all who work behind the walls of the formal sector. These people do not have fixed wages but rather work on a contractual basis. They are paid only when there is work. The rest of the time they are left to fend for themselves. They have no job security, or any Diwali bonus, pensions or medical benefits. They rely on sporadic employments.

The term 'informal economy' refers to all economic activities by workers and economic units that are, in law or in practice, not covered or insufficiently covered by formal arrangements. Their activities are not included in the law, which means that they are operating outside the formal reach of the law; or they are not covered in practice, which means that although they are operating within the formal reach of the law, the law is not applied or not enforced on them; or the law discourages compliance because it is inappropriate, burdensome, or imposes excessive costs. The International Labour Organisation describes the informal economy as follows: "According to a recent report, we are underestimating our GDP by almost 15%. This is because we fail to take into account the growth pioneered by almost half of our workforce falling under the informal sector".

The informal sector makes up for 50% of the economy and its workforce constitutes almost 90% of the total labour force. With such huge numbers, it is surprising how such a ubiquitous sector has been easily sidelined by our politicians. Half of India's \$1.85 trillion economy is informal. With 55%, only sub-Saharan Africa has a larger unorganised economy than India's. The reason why our GDP remains underestimated is due to outdated methods for such calculations. Most of the people in the informal sector are self employed and

there isn't adequate data about them. The GDP is underestimated between the ranges of 5% to 15%. For example, in Uttar Pradesh, the informal sector contributes about 65% of the output and about 85% of the non agrarian employment is generated by this sector. UP's economy consists of many small enterprises which constitutes the informal self employment model.

In developed economies, participation in the informal sector is more of a choice and it is done either to avoid paying taxes or to avoid regulations. But in India, it is the result of the failures of our system and government policies.

With this huge section lying outside the formal economy and thus the tax net, the burden ultimately falls on those who are inside it. The tax system in India is one of the heaviest in the world. Tax evasion remains the main attraction of the informal economy. The informal sector does not allow for the proper targeting of government schemes, undermines the rule of the land and hampers competitiveness and ultimately the growth of the economy. The government suffers losses because of this hidden economic activity. The biggest drawback of the informal sector is its inaccessibility to formal credit. Only 18% of credit to small and medium enterprises is formal. This encourages borrowing from money lenders who charge exorbitant rates. This money remains outside the banking system and the RBI doesn't have any control over it. Even revenue of the government, such as TDS, which is deducted from interest rates, finds its escape route.

It is, as if, an avenue for employment for the surplus labour of our country. It is the source of livelihood for almost 85% of the people. Especially after the global financial meltdown, more and more people are

finding it to be their safety net. A big downside of being a part of the informal sector is the absence of safeguards such as health benefits, pensions, fixed wages etc. Workers here hence end up saving more and there is less casual spending. Also, the workers do not experience any career advancement, but rather remain stagnant, unable to improve their standard of living. According to the data provided by the Indian government, between 2000 and 2005, the most recent year for which data is available, the number of formal jobs in India stayed flat at about 35 million, while informal jobs grew by 17% to 423 million. The real task at hand is to bring out excellent growth rates. In a country like India, where the population continues to outstrip job creation, people are left with little choice but to enter the informal sector. Even large corporations find workers hired on contractual basis less heavy on their balance sheet than those on full employment basis and hence are, in a way, growing accommodated to such a pattern. The proportion of informal workers in the formal sector has risen over time from 42% of total formal sector to 51% in 2009-10. The incentive for the firms is increased profits and easy escape from labour laws. This further highlights the urgency of proper implementation of labour laws.

An untapped potential of the informal sector is its vast ability to encourage self employment. People who do not have enough capital or find themselves lost in the maze of regulations find it easier to set up their businesses in the informal economy. Not being a registered entity makes it harder for them to protect their intellectual property. Also, while such entrepreneurs create more jobs, they do so in the informal sector. This is another reason why formalisation of the informal economy is all the more important.

Why do people not enter the formal sector?

This is mainly due to the difficult environment under which the formal sector operates, especially in developing countries. The Indian bureaucracy is plagued by red tapism, bribes, excessive taxes etc. The more popular reason is that the benefit of working in the formal sector is available only to the privileged ones. Strict market regulations are another force driving workers against entering the formal sector.

How to formalize the informal sector?

The government needs to bring in changes in different stages. It needs to create new jobs, enough to accommodate the young population. The huge barricades of costs and regulations need to be reduced to make the transition easy. The reason employers prefer hiring on contractual basis is that it is more affordable. Hence, labour laws should be made more flexible. The informal sector attracts many entrepreneurs because of the ease of starting a business, and the same needs to happen in the formal sector. The regulations governing the setting up of a business need to be mellowed down and made more accessible to everyone. It takes 71 days to register a business in India, compared with six in Singapore, and three years to close an insolvent business. The corporate tax code should be more business friendly to keep tax evasion in check and a strong administration brought in for its implementation. More tax amenities and tax based incentives should be introduced. A good example here is that of Spain, which reduced corporate taxes and streamlined labour laws. It managed to reduce unemployment by 40% and increase tax revenue by 75%. Until the informal sector is made less attractive, this web of the gray economy will continue to trap people and

the cycle of poverty will consume generations to come!

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The Fascinating Realm of Behavioural Economics

Swaril Dania II Year

Why is it that we sometimes find ourselves excitedly buying things that we don't really need?

What about the 'FREE' extra helpings that we pile up on the plates at a buffet even though our stomach is full?

Have we not ever bought two of a product that we wouldn't have chosen in the first place just in order to get the third one free?