The Informal Labour Market in India: Transitory or Permanent Employment for Migrants?¹

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1. Introduction

The informal labour market is a very important sector of the Indian economy. Urban areas attract numerous migrants from the rural areas in the hope of a better life. This paper is interested in studying the characteristics of the workers in the informal economy and whether migrants treat this sector as a permanent base or only as a temporary location before moving on to the organised or formal sector to improve their life style. We analyse the incomes of people in the informal sector compared to the formal sector. Our study shows that the incomes of informal sector workers are lower than the formal sector after controlling for human capital and other variables.

2. The Informal Labour Market: Definitions; review of some earlier studies

In most developing countries there is a large sector of the economy that is called the informal sector or the unorganised sector. Informal labour market employment plays an important role in most developing economies. Very broadly, the informal labour market consists of workers in the informal sector plus casual workers in the formal sector. The informal labour market is a very large part of the agricultural sector, but is also a significant part of the urban sector. There is a difference between employment in the formal sector and the informal sector in terms of the conditions of work, whether they are subject to government taxes, have access to social security, casual or contract workers, whether they receive minimum wages or not, etc.

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In the developing country context, the informal sector is sometimes defined in terms of the activities of the enterprises (ILO, 1972) and sometimes in terms of the kind of work done by individuals as employees or as self-employed people (Hart, 1973).

In 1972 the ILO characterised the informal sector as:

- (a) Ease of entry
- (b) Reliance on indigenous resources
- (c) Family ownership of enterprise
- (d) Small scale of operation, often defined in terms of hired workers less than (say) ten
- (e) Labour-intensive methods of production and adapted technology
- (f) Skills acquired outside the formal school system
- (g) Unregulated and competitive markets

Whereas, the formal sector was characterised by:

- (a) Difficult entry
- (b) Frequent reliance on overseas resources
- (c) Corporate ownership
- (d) Large scale of operation
- (e) Capital-intensive and often imported technology
- (f) Formally acquired skills, often expatriate
- (g) Protected markets (through tariffs, quotas, and licences)

Hart (1973) discussed the informal sector in terms of the conditions of work of the individuals and whether they worked for wages with good conditions or informally as self-employed workers. Informal activities included:

- (a) Farming, market gardening, self employed artisans, shoe makers, tailors, etc.
- (b) Working in construction, housing, road building
- (c) Small scale distribution, e.g. petty traders, street hawkers, caterers in food and drink, etc.
- (d) Other services, e.g. barbers, shoe-shiners etc.

- (e) Beggars
- (f) Illegal activities like drug pushing

Formal sector income earning activities included:

- (a) Public sector wage earners
- (b) Private sector wage earners (on permanent contracts, not casual workers)

Sengupta (2009, p. 3) define the informal economy thus:

Informal Sector: The unorganised sector consists of all unincorporated private enterprises owned by individuals or households engaged in the sale and production of goods and services operated on a proprietary or partnership basis and with less than ten total workers.

Informal worker/employment: Unorganised workers consist of those working in the unorganised sector or households, excluding regular workers with social security benefits provided by employers and the workers in the formal sector without any employment and social security benefits provided by employers.

Informal economy: The informal sector and its workers plus the informal workers in the formal sector constitute the informal economy.

The literature on the role of the informal sector in developing countries has oscillated between treating the informal sector as a backward sector that is holding back economic development to a dynamic sector that is helping to develop the economy rapidly without straining the foreign currency balances and with relatively low demands for (real) capital goods, see Mazumdar (1976), Weeks (1975), Bromley (1978), Gerxhani (2004). The informal sector is considered as a pre-capitalist form of production compared to the formal sector that is a profit maximising capitalist sector. There is a large literature on rural-urban migration (see, Harris and Todaro, 1970) that considers migrants arriving in the city and initially finding work in the informal sector as a temporary abode for migrants has been disputed by (amongst others) by Mazumdar (1976). The debate has also ranged over whether informal sector workers are living in poor conditions with

low incomes, or whether some of the informal sector workers are there out of choice and have a comfortable life, see Meng (2001). Some individuals may have employment in the formal sector *and* work in the informal sector as well.

Some of the important issues to investigate are whether (1) individuals who are informal sector workers are migrants; whether migrants move out of the informal sector into the formal sector after a few years; (2) whether they are from disadvantaged social and ethnic groups who do not have social networks to enter the formal sector; (3) whether those with low levels of education and skills are unable to enter formal sector employment and have to find low paid work in the informal sector; and finally, (4) whether the incomes of worker in the informal sector are lower than in the formal sector; and whether there are some well paid informal sector workers.

3. The Indian Informal Labour Market: Data and Descriptive Statistics

A recent Report of the National Commission for Enterprises in the Unorganised Sector by the Government of India (Sengupta, 2009) finds that 86 % of the total employment in 2004-2005 was in the informal sector. Further, the agricultural sector consists almost entirely of informal workers. The non-agricultural workers in the informal sector were 36.5 % of the total, most of whom were self-employed. From 1999-2000 to 2004-2005 most of the increase in employment in the formal sector was of informal workers! (Sengupta, 2009, p. 14).

In our study we are using data from the India Human Development Survey (IHDS), 2005 conducted by the Inter-university Consortium for Political and Social Research, Ann Arbor, Michigan, USA. The survey is a nationally representative, multi-topic survey of 41,554 households in 1,503 villages and 971 urban neighbourhoods across India. The data set has detailed information on household employment by industry and occupation, and detailed information about household characteristics including age, education, ethnicity, religion, and migration status. In this study we have limited our analysis to the informal labour markets in the urban sector.

Our data set consists of 7,421 heads of households for whom we had data on their age, education, marital status, gender, religion, caste, income source, migration status and years since migration to urban sector, education levels. The definition of informal workers used in our definition is non-agricultural workers who are artisans, petty traders, and business plus casual workers in the formal sector.

Table 1 in the appendix has the summary statistics for the key variables. In our sample, we kept only those individuals who are the head of their family and unsurprisingly 95 percent of the sample is a male headed household which is a common phenomenon in India. Average size of the family is near about 5 members and in the case of informal sector the average size of family is slightly larger than the formal sector. However a reverse patter is visible in the case of age whereby average age is about 4 years higher in the formal sector than in the informal sector. In case of education, as we move to higher ladder of the educational qualification, greater percentage of sample is concentrated towards formal sector which is what one can expect. Interestingly, if we look at the religion and caste based distribution, it appears that more Adivasi community is in the formal sector however comparatively higher percentage of Dalits and a big percentage of Muslim are in the informal sector.

4. Preliminary estimation

As we mentioned at the beginning of the chapter that we are interested in exploring whether migrants are more concentrated in the informal economy or not and whether migrants treat this sector as a permanent base or only as a temporary location before moving on to the organised or formal sector to improve their life style. One way to capture such issue is by using the duration of the migration variable. If migrants initially prefer to get a job in the informal economy only as a temporary location before moving to the formal sector then the duration of migration would be negatively associated with the informal equation. However, using the duration of migration variable as an independent variable could be troublesome due to the endogeneity of the migration duration issue on informal sector equation. The problem lies at the idiosyncratic error component of the regression where unobservable (say for example ability) could influence both the migration duration as well as the job at the informal sector. To say in another way, a high ability individual could migrate earlier in her life and could less likely be in the informal sector which could lead to a bias in our estimation.

Tackling such an issue, we employed Instrumental Variable (IV) approach to instrument for the duration of migration. Instruments used in our estimation are the disadvantaged cast and religion variables which are anecdotally known to as a source of discrimination in the traditional Indian societies. In India, certain caste and religion groups are typically separated out for the rest of community and these disadvantaged groups are usually discriminated in their social-economic experiences while they are in the village. Such discrimination is not pronounced in the urban areas and individuals belonging to some disadvantageous caste/religious groups find it beneficial to migrate. In our study we used dummies for Adivasi, Datil (untouchables) and Muslims as instruments for the migration duration to tackle the endogeneity issue.

Table 2 reports the preliminary estimations of the regression with IV approach. Our preferred estimation is depicted in column (1) however we have also produces two additional regressions for robustness checks in column (2) and (3). In column (2) and (3) we have restricted the age at the time of migration to over 13 years and over 18 years respectively. All regressions show that duration of migration has strong negative association with the informal sector employment which means, with one additional year of migration duration, individuals will be less likely be in the informal sector, holding all other things equal. All the standard errors reported in the Table 2 are robust standard errors.

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Table 1: Summary Statistics

	Formal	Informal	Total
Male	0.950	0.949	0.950
	(0.217)	(0.219)	(0.219)
Duration of migration	12.653	10.287	11.365
	(15.448)	(14.736)	(15.110)
Income	117601.888	47480.093	79427.511
	(87918.992)	(43178.953)	(75866.426)
Age	44.227	40.463	42.178
	(8.935)	(10.835)	(10.188)
Size of the Household	4.640	4.804	4.729
	(1.846)	(1.909)	(1.882)
Married	0.986	0.979	0.982
	(0.120)	(0.143)	(0.133)
Primary Education	0.043	0.148	0.100
	(0.203)	(0.355)	(0.300)
Secondary Education	0.151	0.290	0.226
	(0.358)	(0.454)	(0.419)
Matriculation	0.163	0.177	0.171
	(0.369)	(0.382)	(0.376)
Tertiary Education	0.164	0.093	0.125
	(0.370)	(0.291)	(0.331)
Graduate	0.451	0.128	0.275
	(0.498)	(0.334)	(0.447)
Adivasi	0.056	0.028	0.041
	(0.229)	(0.165)	(0.197)
Dalit	0.158	0.202	0.182
	(0.365)	(0.401)	(0.386)
Muslim	0.078	0.206	0.148
	(0.269)	(0.405)	(0.355)
Observations	3381	4040	7421

*Standard deviations are reported in the parenthesis.

	(1)	(2)	(3)
Duration of Migration	-0.011**	-0.093**	-0.010*
	(0.005)	(0.047)	(0.006)
Age	-0.0084***	0.025	-0.013***
	(0.003)	(0.021)	(0.003)
Age Square	0.00012***	-0.000020	0.00013***
	(0.000)	(0.000)	(0.000)
Male	0.038	0.098	0.035
	(0.023)	(0.062)	(0.023)
No. of Households	0.0086***	-0.0070	0.010***
	(0.003)	(0.010)	(0.003)
Married	0.013	0.048	0.0069
	(0.039)	(0.062)	(0.038)
Primary Education	0.0014	-0.027	-0.0027
	(0.023)	(0.046)	(0.022)
Secondary Education	-0.025	-0.037	-0.027
	(0.021)	(0.041)	(0.021)
Metric Completed	-0.12***	-0.14***	-0.13***
	(0.022)	(0.044)	(0.022)
Tertiary Education	-0.18***	-0.22***	-0.18***
	(0.023)	(0.050)	(0.023)
Graduate	-0.22***	-0.25***	-0.22***
	(0.023)	(0.049)	(0.022)
Household Asset	-0.019***	-0.015***	-0.020***
	(0.002)	(0.004)	(0.002)
Father's Education Primary	-0.025*	-0.058*	-0.024*
	(0.013)	(0.032)	(0.013)
Father's Education Secondary	-0.031**	-0.041	-0.032**
	(0.014)	(0.031)	(0.014)
Father's Education Tertiary	-0.072***	-0.098*	-0.074***
	(0.024)	(0.055)	(0.024)
Father's Education Graduation	-0.038	-0.072	-0.040*
	(0.023)	(0.052)	(0.023)
Constant	1.20***	0.51	1.29***
	(0.115)	(0.458)	(0.109)
State Dummies	Yes	Yes	Yes
City Dummies	Yes	Yes	Yes
One digit Industry Dummies	Yes	Yes	Yes
One digit Fathers Occupation Dummies			
Observations	9273	9273	9273

Table 2: Preliminary Estimations

Robust standard errors in parentheses Source: Indian Human Development Survey 2005: Authors Own Calculation * p < 0.1, ** p < 0.05, *** p < 0.01