Q1

How globalization has led to the reduction of employment in the formal sector of the Indian economy? Is increased informalization detrimental to the development of the country?

UPSC Civil Services Mains 2016 · GS III · 12 marks · Indian Economy

Indian Economy and issues relating to planning, mobilization of resources, growth, development and employment.

Core demand of the question

- Explain how globalization reduced employment in India's formal sector
- **State channels:** trade, capital, labour laws, and services-led growth
- Judge whether rising informalization is detrimental to development, with a balanced yes on quality of jobs

Revision summary

After 1991, trade opening, flexible staffing and capital-intensive technology cut regular factory hiring.

Services-led growth and a freeze on public recruitment added few mass formal jobs.

Informal work absorbed labour but kept wages, social security and productivity low.

A large informal sector also limits tax and social-insurance reach.

Development needs formalisation of growing firms, not permanent dualism.

Introduction

Globalization after 1991 opened trade, capital and technology. Formal factory jobs did not rise in step with output. Firms met global competition by cutting regular payroll, using contract labour, and shifting work to **unregistered units**. Informalization can absorb people in the short run. It is detrimental to development when it becomes the **main growth path**, because it weakens wages, social security and tax capacity.

Body

How globalization cut formal employment

- Import competition after tariff cuts forced many **small organised units** in textiles, engineering and consumer goods to close or to stay below the factory-act threshold.
- Export and multinational buyers demanded **flexible, low-cost labour**. Firms answered with contractors, trainees and home-based chains rather than permanent staff.
- **Capital-intensive technology** and imported machines raised output with fewer shop-floor workers, so organised manufacturing's job elasticity stayed low.
- Growth after 1991 was **services-led**. Information technology and finance created some formal posts, but most new urban work was in construction, retail, transport and domestic services that sit outside provident fund and Employees' State Insurance.

- Rigid **Industrial Disputes Act** exit rules and inspector raj made employers avoid crossing the worker-count that triggers standing orders, so units stayed small and informal by design.
- Public-sector **disinvestment and freeze on regular recruitment** shrunk a historic source of formal jobs, while contract staff filled the same desks.

Is increased informalization detrimental?

- Informal work gave a livelihood cushion when farms shed labour and organised industry did not hire. That is not the same as development.
- Informal workers lack **minimum wage enforcement, written contracts, maternity cover and old-age security**, so household risk stays high and human capital is under-invested.
- Informal firms have weak access to bank credit, technology and export standards, so **productivity** stays low and India misses the manufacturing-jobs ladder seen in East Asia.
- A large informal base shrinks **social-security contributions and income-tax** reach, which limits the State's ability to fund health, skills and infrastructure.
- **Some informalization is** statistical**:** own-account work and micro units that GST and **Pradhan Mantri Jan Dhan Yojana** may later formalise. That transition is useful; a permanent dual labour market is not.
- Development needs a shift from informal survival to **formal, productive jobs**, with contract labour used as a bridge, not as the destination.

Way

- Ease exit and compliance for genuine firms so they grow above the informal threshold, while enforcing **core labour standards** on contractors.
- Use **Make in India**, skill missions and MSME credit so global value chains hire in India with papers, not only through unregistered suppliers.

Flow diagram

Globalization -> Import competition

Globalization -> Flexible contract labour

Globalization -> Capital intensive tech

Import competition -> Fewer formal jobs

Flexible contract labour -> Fewer formal jobs

Capital intensive tech -> Fewer formal jobs

Fewer formal jobs -> Informalization

Informalization -> Weak security and productivity

Conclusion

Globalization raised output and some skilled services jobs, but it also pushed employers to shed regular factory posts and to use informal chains. Informalization is a shock absorber, not a development strategy. India develops when global integration is paired with formal, productive employment.

Facts & figures

1991 reforms

Liberalisation of trade, industrial licensing and foreign investment that exposed Indian firms to global competition.

Organised manufacturing

Factory-act units; their share of total employment stayed thin even when manufacturing output rose.

Contract labour

Workers hired through contractors to avoid regular payroll, provident fund and standing-order thresholds.

NSS informal sector

National Sample Survey estimates have long shown the large majority of Indian workers outside formal social security.

ESI and EPF

Employees' State Insurance and Employees' Provident Fund: the main statutory covers that informal workers usually miss.