



The Complementarity Between the Formal and Informal Sub-sectors of the Indian Industry

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Abstract

Indian economy is categorized as one of the fastest growing advancing economies. Much of the growth has been attributed to the industrialization process post-independence especially after economic reforms of 1990s. However, the formal industrial sector has been unable to absorb the growing labor force and thus majority of labor force have been forced to derive and find self-employment options in the informal sector. The current study is an attempt to analyze the Indian industry in light of this formal and informal bifurcation. Using the stochastic frontier analysis, the production functions are validated and technical efficiency (TE) is predicted. The study reveals that the formal industrial sector in India is relatively efficient. However, the informal sector, apart from absorbing higher number of labor force, is performing better than dictated by hitherto classic theoretic predictions. The study also analyzes the factors influencing the TE of the formal and informal sectors. The study concludes that the formal and informal sectors mutually reinforce the industrial growth in India, have positive linkages and contribute efficaciously to economic outcomes like output and employment.

Keywords Formal sector · India · Industry · Informal sector · Technical efficiency

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