

## ECOWRAP

### SHARE OF INFORMAL ECONOMY MAY HAVE SHRUNK TO NO MORE THAN 20% FROM 52% IN FY18

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A large chunk of the total workforce in India earns its livelihood as informal worker. Though the pandemic has led to huge devastating impact on all the sectors of the economy, the impact has been felt more by the informal sector. While, the formal sector is almost now back to its pre-pandemic level, the informal sector still continues to bear the brunt. **In this context, India's estimate done as of FY2018 suggests the size of informal economy at 52% of the economy. This number was expressed by NSC.**

Even globally informal economic activity is not specifically defined. Given existing GDP measurement dispensations, worldwide, heavily dependent on surveys and administrative data, it adds to the challenge of measuring informal economy. As such a globally accepted statistical framework of measuring informal economy is still awaited. Interestingly, if one leaves out illegal activity, informal economic activity at its core is either a data capture issue or a compliance issue. Recording economic activity is an issue where goods and services are produced by entities not registered with a government body. However, when a registered entity for purpose of tax evasion may under-report production or revenues it's a compliance issue, that could be traced through digital footprints.

**A sizeable informal economy is not just the issue of emerging and developing economies. For example, as per IMF, even in Europe informal economy is estimated at 20% of GDP.** For India, post 2016 plethora of measures which accelerated digitisation of the economy, emergence of gig economy have facilitated higher formalisation of the Indian economy - at rates possibly much faster than most other nations.

Our starting point is an assumption that the shrinkage in economy post pandemic is mostly informal and hence the loss in output across sectors gives us a measure of the informal sector. By making this assumption, we ensure that the size of the informal economy is still overstated as the shrinkage in economy also consisted of formal. This ensures that our estimate is at least free from any downward bias in measurement. **Employing this methodology and rigorous data validation, this article estimates that currently informal economy is possibly is at max 15%-20% of formal GDP. There is wide variation across sectors, though, with formal sectors like finance and insurance expanding post pandemic.**

The Government has made many efforts for formalisation in the last couple of years. For example, one of the sources to analyse the extent of formalisation is the monthly EPFO payroll report which provides data on establishments remitting first ECR (Electronic Challan-cum-Return) in a particular month. **Based on this data we estimate almost 36.6 lakh jobs have been formalised till Aug'21. Next is the E-Shram portal, which is the first-ever national database of unorganised workers. 5.7 crore unorganised workers (Oct 30/ and counting) have registered in the first two months after its launch, with 62% of workers belonging to the age-group of 18-40 years and 92.0% registered workers having monthly income of less than Rs 10,000. State wise data shows that top 4 states accounted for 72% of total registration, with West Bengal on the top followed by Odisha and Uttar Pradesh. Occupation wise, workers from agriculture sector account for 55% of registration followed by construction sector (13%). Of the 5.7 crore registered workers, 81.2% or 4.6 crore have bank accounts but only 24% of them or 1.1 crore workers have Aadhaar linked bank accounts. The E-Shram is a big step towards the formalisation of employment as our calculation indicates that till date the rate of formalisation of unorganised labour due to E-Shram is around 17% / Rs 6.8 lakh crore / 3% of GDP in just 2 months. Even in Agriculture, the usage of KCC cards has increased significantly and we estimate Rs 4.6 lakh crore formalisation only through KCC route, with more marginalized farmers coming under the banking sector ambit through such usage. The total number of insurance and pension accounts that have been opened across several schemes for the unorganised as well as organised is as much as 68.9 crore.**

Formalisation of an economy is always better from a policy perspective. **Our estimates show that 11.4 crore tax paying households, 8.5% of the total population contributes to Rs 75 lakh crore or 65% of the private final consumption expenditure and cross subsidises 91.5% of the population.** Hence it is important and ethical that even as we formalise, we must support honest tax paying households through a better designed tax structure, particularly indirect taxes on items like fuel!

**FORMALISATION**

- ◆ India has a large informal economy with around 93% of its total workforce earning their livelihoods as informal workers (NSSO 2014). Though the pandemic has led to huge devastating impact on all the sectors of the economy, the impact has been felt more by the informal sector. While, the formal sector is now back to its pre-pandemic level, the informal sector still continues to bear the brunt.
- ◆ However, there has been a positive development in the Indian economy amidst the pandemic. Owing to the various efforts of the Government, there has been an increase in the formalisation of the economy. Based on specific examples, at least Rs 13 lakh crore has come under the formal economy through various channels over the last few years, including the recent scheme on E-shram portal.

**SIZE OF THE INFORMAL ECONOMY**

- ◆ The informal sector in India consists of enterprises which are own account enterprises and operated by own account workers or unorganised enterprises employing hired workers. They are essentially proprietary and partnership enterprises. The adjacent table presents the share of informal sector GVA to total for FY18. The share of unorganised sector is highest in agriculture as the holdings are small and fragmented. Since FY18, a lot has changed in Indian economy landscape. IMF has also noted that formalisation of economy has increased since the adoption of GST, enhanced digitalisation and demonetisation.
- ◆ We endeavoured to find out the share of informal economy for FY21. Our starting point is an assumption that the shrinkage in economy post pandemic is mostly informal and hence the loss in output across sectors gives us a measure of the informal sector. By making this assumption, we ensure that the size of the informal economy is still overstated as the shrinkage in economy also consisted of formal. This ensures that our estimate is at least free from any downward bias in measurement.
- ◆ Employing this methodology and rigorous data validation, we estimate that currently informal economy is possibly at max 15-20% of formal GDP. Though, there is wide variation across sectors.

Increasing size of formal economy~	
Number of jobs formalised since FY18 (as per EPFO records)	~36.6 lakh or ~0.66 lakh crore
Unorganized workers registered on E-shram portal (as on 30 Oct)	5.7 crore or ~Rs 6.8 lakh crore
Formalisation of cash usage since pandemic	~Rs 1.2 lakh crore
Amount of Agriculture credit formalised since FY18	~Rs 4.6 lakh crore
Increase in digital payments towards Petrol + Diesel on Petrol Pumps during last three years	~Rs 1.0 lakh crore

- ◆ The informal size of the trade, hotels, transport, communication & broadcasting that employs around 17 crore households as per 2011 census is at 40%. The informal sector in construction is also around 34% and that in public administration is around 16%. The manufacturing sector has an informal component of around 20%.
- ◆ However, the significant formalisation efforts of the Government have resulted in almost 100% formalisation in the finance, insurance, and to a large extent in real estate. Since FY18, agriculture sector has been formalised by 20-25% due to increasing penetration of KCC credit. This implies that in agriculture sector informal share is now in the range of 70-75%.
- ◆ The formal finance sector has even expanded by 10% post pandemic, with the Government DBT transfers gaining traction. As expected, the utilities services are also 100% formalised and in fact the formal size expanded by 1% during pandemic.

Share of informal economy across broad sectors to GVA (%)			
Sector	2011-12	2017-18	2020-21 P
Agriculture, forestry and fishing	96.8	97.1	70-75
Mining and quarrying	22.6	22.5	15-17
Manufacturing	25.5	22.7	19-21
Electricity, gas, water	4.3	5.3	0
Construction	76.4	74.5	35-40
Accommodation; food services; trade	86.6	86.6	40-45
Transport, storage, communication	47	47.7	
Financial services	9.3	11.9	20-25
Real estate, ownership of dwellings	63.1	52.8	
Public administration and defense	0	0	0
TOTAL GVA at basic prices	53.9	52.4	15-20

Source: IMF Policy Paper Feb-21; P: SBI Projections

State-wise, Sector-wise Registration in E-Shram Portal (in lakh)							
State	Total Registration	Of which,					Share of Agri in Total
		Agriculture	Construction	Domestic & HH Workers	Apparel	Capital Goods & Manufacturing	
India, of which	567.1	311.5	71.6	47.4	33.8	15.9	55%
West Bengal	131.1	75.6	12.2	9.3	8.2	2.2	58%
Odisha	101.8	72.2	10.8	3.0	5.1	1.4	71%
UP	99.2	50.3	9.9	14.9	6.1	4.0	51%
Bihar	77.0	38.9	11.3	11.0	4.4	2.4	51%
MP	20.4	9.8	2.7	1.1	1.5	1.1	48%
Jharkhand	19.4	12.1	1.5	1.8	0.5	0.9	62%
Chhattisgarh	18.2	13	1.6	0.6	0.8	0.7	71%
Rajasthan	17.1	6.3	4.5	0.7	1.2	0.9	37%
Punjab	14.3	4.4	3.4	1.8	1.3	0.5	31%
Assam	13.3	6.8	1.9	0.9	0.6	0.3	51%

Source: SBI Research

**FORMALISATION THROUGH E-SHRAM PORTAL**

- ◆ The Government launched the E-Shram portal, a database of unorganised sector workers, on 26 August 2021. The portal is the first-ever national database of unorganised workers including migrant workers, construction workers, gig and platform workers. It facilitates extending benefits of social sector schemes to the workers in the unorganised sector. In just two months, around 5.7 crore unorganised workers have registered with top 10 states accounting for 90% of total registration and top 4 states accounting for 72% of total registration, with West Bengal on the top, followed by Odisha and Uttar Pradesh.
- ◆ Occupation wise, workers from agriculture sector now account for 55% of registration followed by construction sector (13%). However in some states like Odisha & Chhattisgarh the share of agriculture in total registration is more than 70%. Age-wise, 62% of workers belong to the age-group of 18-40 years & registered female workers are a tad more than registered male workers. Of the 5.7 crore registered workers, 81.2% or 4.6 crore have bank accounts but only 24% of them or 1.1 crore workers have Aadhaar linked bank accounts.
- ◆ **We believe that E-Shram is a big step towards the formalisation of employment. Our estimates indicate that till date the rate of formalisation due to E-Shram is around 17% and will increase further.**

**FORMALISATION RATE BASED ON EPFO DATA**

- ◆ Monthly EPFO payroll report provides data on establishments remitting first ECR (Electronic Challan-cum-Return) in a particular month. Based on this data we estimate that since FY18, almost 36.6 lakh jobs have been formalised till Jul'21. We expect that this fiscal formalisation rate will be higher than FY20 but lower than the FY19 level.

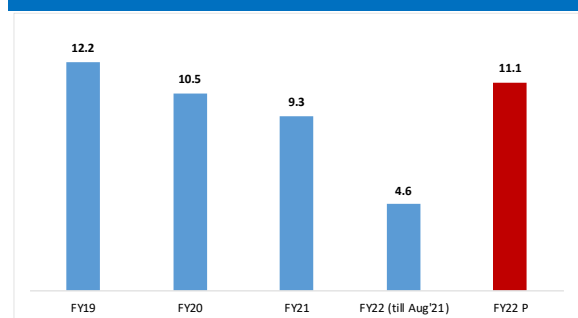
Level of formalisation through E-shram	
Worker population ratio	35.3%
Total number of workers (crore)	47.7
Share of informal sector in non-agriculture sector	72.1%
Workers in informal sector (crore)	34.4
Unorganised workers registered through e-shram so far (crore)	5.7
Formalisation through e-shram so far	17%

Source: SBI Research

Key Indicators of E-shram registration		
Total Registration so far		5.7 crore
Monthly Income	Below Rs 10K	92.1%
	Rs 10-15K	5.8%
	Above Rs 10K	2.1%
Gender Share	Male	49.1%
	Female	50.9%
Age-Share	18-40	61.7%
	40-50	22.1%
	Above 50	12.4%
Social Category Share	ST	7.9%
	SC	23.4%
	OBC	41.7%
	GEN	27.0%
Aadhaar Linked bank A/c	Yes	23.4%
	No	76.4%

Source: SBI Research

**Formalisation Rate based on EPFO data (in Lakh)**



Source: SBI Research

**FORMALISATION OF AGRICULTURE CREDIT**

- ◆ Over the years the usage of KCC has increased significantly. In the last 3-4 years the per card outstanding has increased from Rs 96,578 in FY18 to Rs 1,67,416 in FY22, an increase of Rs 70,838. At 6.5 crore cards, the amount which is formalized i.e. Rs 4.6 lakh crore.

**FORMALISATION THROUGH DIGITAL PAYMENTS AT PETROL PUMPS**

- ◆ With the rise in economic activities, the consumption of petrol and diesel is estimated to increase by 7215 million liters in FY22. By assuming 50% of additional petrol and 25% of Diesel is paid by digital modes at Petrol, approx. Rs 23,686 crore has been formalized at petrol pumps.
- ◆ So, in the last 5 years, around Rs 1 lakh crore has been formalized.

**POWER OF FORMAL ECONOMY IS LARGE: 8.5% OF THE POPULATION CONTRIBUTING TO 65% OF THE CONSUMPTION**

- ◆ According to the World Bank data, 61.7% of our population lived spent less than \$3.2 per day, or Rs 224 per day and 20.6% of population lived on less than \$1.9 per day or Rs 133 per day.
- ◆ Considering 25% of population still lives below \$1.9 per day and 47% of population lives below \$3.2 per day, only 80% of the remaining 71.6 crore, i.e, 57.2 crore people work in the formal economy.
- ◆ Furthermore, if we take each household supporting a family of 5, we get 11.4 crore which is roughly equal to the total number of tax payers in the economy. Adjusting for the consumption of those below poverty line, these 11.4 crore tax paying HH or 8.5% of the population contributes to Rs 75 lakh crore or 65% of the private final consumption expenditure.
- ◆ We believe that the Government should ensure that the existing tax structure is favourable to this tax paying population that constitute 8.5% of the population but cross subsidises 91.5% of the population. To that extent, the existing tax structure particularly of indirect taxes on fuel should not be consumption negative.

Formalisation of Agriculture Credit		
	FY18	FY22*
1. Per KCC card O/S (Rs)	96,578	1,67,416
2. Increase per card	Rs 70,838	
3. Total KCC cards	6.5 crore	
4. Agri credit Formalised (2*3)	Rs 4.6 lakh crore	
Source: SBI Research; *Apr-Dec		

Formalized of Petrol Pumps through Digitalization				
	Change in Consumption		Estimated Amount	
	Million Liters	Total Amount (Rs Crore)	Rs Crore	Assuming % of Transactions in Digital Mode
Petrol	2443	25066	12533	50%
Diesel	4772	44609	11152	25%
Estimated amount Formalized at Petrol Pumps (Approx.) in a year			23686	In 5 Year: Approx. Rs 1 lakh crore
Source: SBI Research, PPAC				

Estimate of tax payers' consumption (Rs crore)	
Total population	135
Population living <\$1.9 per day (20%)	33.8
Population living <\$3.2 per day (50%)	63.5
Remaining population	67.5
population in formal sector (80%)	57.2
Total taxpayers households (assuming a person supports a family of 5 members on an average)	11.4
<b>Rs lakh crore</b>	
Private Final Consumption Expenditure	115.7
Consumption of those living below \$3.2 per day	40.7
Consumption of 8.5% of population or 11.4 crore tax paying HH	75.0
Consumption of 8.5% of population or 11.4 crore tax paying HH (% of PFCE)	65%
Source: SBI Research	

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