

Deconstructing Informality in the Indian Manufacturing Sector: Field Observations from the Early Days of Social Compact

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UNDERSTANDING THE TREND OF RISING INFORMALITY IN THE FORMAL SECTOR

Rising informality has been a persistent feature of India's labour markets post-liberalization. NSSO data reveals that of around 61 million jobs created in India in the 22 years post-economic liberalization in 1991, 92% were in the informal sector.¹⁴³ The 17th International Conference of Labour Statisticians held by the ILO in 2003 defines informal employment as those jobs where '...employment relation is, in law or in practice, not subject to national labour legislation, income taxation, social protection or entitlement to certain employment benefits such as advance notice of dismissal, severance pay, paid annual or sick leave'.¹⁴⁴ Employed without work contracts, workers in the informal sector operate on a non-permanent basis with lower wages and a glaring absence of social protection.

High levels of 'growth' in the country have paradoxically translated into limited job creation in the formal sector, which now sees a steep rise in informality in various forms. A close look at some important statistics reveals how pervasive this phenomenon is: While informal jobs increased by 13% between 1999 and 2011, formal jobs increased by only 3%.¹⁴⁵ Even the organized manufacturing sector, which saw 78% job growth between 2001 and 2016, saw the erosion of direct employment by 10.8% and a 12.4% increase in contract employment.¹⁴⁶ Contractualization of jobs has pervaded most industrial sectors, often in contravention of the Contract Labour (Regulation & Abolition) Act, 1970, which constrains contractual employment in core functions (except housekeeping,

maintenance, sanitation, and related functions). These statistics demand acknowledgement that the current model of industrialization favours informal or contractual workers over a formally employed, permanent workforce.

In the context of the manufacturing sector in India, in particular, the production processes are largely structured in ways that deepen informality. Driven by factors such as flexibility and lower costs, these processes are outsourced to small units that specialize in the manufacturing of subcomponents or specific smaller activities (such as welding or fabrication). The processes are typically divided into many tiers, depending on the complexity of the tasks involved. In the smaller units that form a major bulk of the supply chains, such fragmentation has also manifested into a wide prevalence of non-standard forms—such as piece-rate work or part-time work. Work arrangements are also diverse, moving from regular and permanent modes of employment to more temporary and casual forms of work that are seldom supported by a contract.

An important facet of the informal workforce in India is that migrant workers constitute a vast majority of it. Widespread rural immiseration¹⁴⁷ and declining potential for rural livelihoods, combined with a simultaneous increase in the pace of urbanization and expansion of urban labour markets, have triggered rural to urban migration on an enormous scale. New migration corridors have recently emerged following the migration of workers from the northern and eastern Indian states to the western and southern Indian states. This movement is triggered by the push of sparse livelihood opportunities in the home states and the pull of comparatively higher wage rates in

¹⁴³ Salve, P. (2019, May 9). *90% of jobs created over two decades post-liberalisation were informal*. IndiaSpend. 90% Of Jobs Created Over Two Decades Post-Liberalisation Were Informal (indiaspend.com)

¹⁴⁴ Hussmanns, R. (2004).

¹⁴⁵ Kapoor, R., & Krishnapriya, P.P. (2019). *Explaining the contractualisation of India's workforce Working_Paper_369.pdf* (icrier.org)

¹⁴⁶ Kapoor, R., & Krishnapriya, P. P. (2019).

¹⁴⁷ Jain, P., & Sharma, A. (2019). Super-exploitation of Adivasi migrant workers: The political economy of migration from southern Rajasthan to Gujarat. *Journal of Interdisciplinary Economics*, 31(1), 63–99.

the destination states.¹⁴⁸ With limited skills and almost no capital, the migrant workers get absorbed into the country's vast informal sector,¹⁴⁹ occupying precarious work sectors in downstream units that have been long vacated by local labour.

Constant mobility and exclusion from state entitlements exacerbate their vulnerabilities, an amplification of which was seen during the COVID-19-induced lockdown in 2020. Experientially, many employers show a keen preference for migrant workers over local workers:

[L]ocal boys will not do work like this, they are not interested in difficult work, they keep making too many excuses and taking leaves. But migrant boys, they do whatever you assign them, they are happy to work overtime and rarely create trouble, their capacity for work is much higher too.¹⁵⁰ (An opinion shared by a manager in a chemical plant in Vadodara [Gujarat], but which was echoed by several employers in the manufacturing sector).

SOCIAL COMPACT: EXPERIENCES THUS FAR

While the pandemic has left an indelible impact on nearly every Indian, informal and migrant workers suffered very cruel shocks during its first wave. The terrible humanitarian tragedy, the migrant exodus, brought the structural vulnerabilities and uncertainties of informal workers' lives to public attention. Attributing the exodus to only the lockdowns would be misleading—the income instability, lack of rainy day funds, housing instability, and precarity of employment were entrenched features of migrant workers lives, which the pandemic exacerbated. Dismay towards the tragic migrant exodus during the first wave of the pandemic prompted the origin of the Social Compact among a few conscientious employers seeking to prevent the recurrence of such a tragedy and address the vulnerabilities faced by workers in their ecosystems.

The process began with adopting a set of normative standards for dignified work, inspired by the Indian legal regime, the UN Guiding Principles on Business and Human Rights Principles, Decent Work, the Better

Work project, and similar international instruments. A necessary step in distilling these standards was acknowledging the diversity of manufacturing jobs and establishments in India to enable the customization of these standards across different sectors. The Social Compact journey seeks to adopt dignified and fair working conditions not only within the participating companies themselves but also among their supplier ecosystems in an incremental manner.

One fundamental step in the Social Compact journey is the creation of a baseline for each selected site nominated by the company, capturing a detailed assessment of their labour governance systems and practices. These have been carried out both inside the company gates and at the worksites of vendors within their supply chains, but always with a focus on the informal workers, who are temporarily employed with the companies or with their labour suppliers/contractors as well as with smaller units in their supply chains. The main intent of the baseline exercise has always been about finding joint solutions that ensure dignity and security to workers. It has also generated several data points on the situation on the ground, both within the work environments of leading industry chains themselves and in more external units within their supply chains.

The following section outlines some of the findings from our initial assessment visits, followed by a few recommendations for state and industry policies. These hold for most of the companies and their intermediaries we visited.

- *Outsourcing to labour suppliers and contractors reduces the visibility of principal employers:* Principal employers often outsource fundamental human resource functions such as recruitment, hiring, and employing to labour suppliers/contractors across both core and ancillary categories of workers. While this certainly leads to a shifting (and potential dilution) of employer responsibility onto external entities, it also significantly diminishes the visibility of the principal employer into the labour management functions performed by these players. This, in turn, affects the ability of the companies to institutionalize a feedback loop on labour practices and take corrective action—not only from a compliance perspective but also from the point of view of ensuring dignity and labour protection for the marginalized worker.

A site visit to a chemical company in Maharashtra revealed the existence of forced labour on its campus. The company had created on-site housing

¹⁴⁸ Mishra, D. K. (2021). Migrant labour during the pandemic: A political economy perspective. *The Indian Economic Journal*, 69(3), 410–424. <https://doi.org/10.1177/00194662211021209>

¹⁴⁹ Government of India. (2008). *Report on conditions of work and promotion of livelihoods in the unorganised sector*. National Commission on Enterprises in the Unorganised Sector.

¹⁵⁰ Opinion shared during interview at a chemical factory in Gujarat.

for migrant workers to ensure continuity of operations during the pandemic. A contractor had prohibited migrant workers from leaving the company premises, directing his supervisors to assist with their chores outside (buying supplies, mobile recharges, etc.). This arrangement violates the Bonded Labour System (Abolition) Act, 1976, and this coercion escaped the notice of the company due to an inability to create mechanisms to communicate with contract workers. Another pervasive form of forced labour observed during the Social Compact visits was debt bondage. Some migrant workers spend years paying off advances taken from their contractors or subcontractors that seem to never diminish. The company remains unaware of the commercial relations (the *vyavahar*) between migrant workers and their contractors. These human rights violations can also bring severe disrepute and penal consequences upon the principal employer.

- *Flexible work arrangements hamper income security of workers:* Several groups of workers were employed on flexible terms—such as on a daily wage basis or piece rates. Heavily casualized forms of work such as daily recruitment from factory gates were also common for specific types of work. The business logic of these practices is well understood—many companies must operate on narrow margins and in discontinuous or unpredictable volumes of demand, and a permanent workforce during economic instability would be expensive to sustain. However, such practices also severely compromise the employment and income security, especially those at the bottom end.

Companies are keen to avoid attracting the legal presumption of permanent or direct employment on their premises. Their legal advisors devise a complex list of strategies to interact with contract and temporary workers. In the past, workers have approached the judicial system to claim that their engagement through a contractor is a sham and that they are direct employees of the company. Such litigation has led to the adoption of two tests for what counts as proof of employment. These tests control the behaviour of companies towards their contract workers and limit the involvement of companies in the affairs of their contractors. A common practice among companies to prevent contract workers from claiming permanence is to employ them in a 'break system', with workers being employed for 6-month periods followed by breaks, and where possible, being shuffled between different plants of the parent company so they are kept in perpetual employment instability.

- *Non-compliance with labour regulations denies workers of basic entitlements:* Basic labour regulations such as work hours and weekly holidays were not complied with for many workers employed in ancillary functions and within vendor units. A 12-hour workday was a standard practice for most temporary workers, with overtime (OT) not compensated on legally mandated rates. Several manufacturing and chemical companies had normalized this 12-hour workday for their blue-collar staff, despite clear legal mandates on limited OT. Longer working days, especially in jobs requiring manual labour, expose workers to greater body burdens and increase the risk of occupational injuries.

Employers attest that workers want longer working hours, and it is common for workers to quit jobs that limit OT for jobs that allow longer working hours. While the preference of migrant workers to work for longer hours to maximize earnings is well founded, it needs to be recognized that the suboptimal wage rates also leave workers with no option but to work for longer hours to ensure subsistence-level earnings for them and their families. Piece-rated employment deprives workers of paid weekly offs and OT compensation. Additional paid leaves (sick leave, casual leave) as per labour standards are even rarer for informal workers. Increments, if any, are calculated based on revised dearness allowances issued by the government, seldom recognizing or rewarding skills acquired through long years of experience.

- *Lack of social security contributes to precarity among workers:* Several categories of workers employed through labour suppliers were actively covered under the ambit of Employees' State Insurance Corporation (ESIC) and Provident Fund (PF), with the practice declining steadily as the supply chain progressed towards the downstream units. While this could also be a function of the threshold requirements for contributing to such schemes, a common observation across informal workers is that a vast majority of them do not have information about how much was deducted from their salaries towards contribution to ESIC and PF and how they can retrieve the same. In such a context, most workers prefer to take their wages in cash without deductions, which further perpetuates informality in the larger ecosystem. Maternity leave or allowance was almost non-existent, with pregnant women often having to terminate employment at the time of delivery. In most cases, rehiring was also not guaranteed.

- *Minimal gender sensitivity at work reduces the potential of women workforce participation:* The manufacturing sector reflects low employment for women. Roles for women are often clustered into certain categories—sanitation, housekeeping, canteen services, white-collar jobs. This indicates two possibilities—the exclusion of women from other jobs or the absence of women possessing the skills required for mechanical or civil work. Multiple sites we visited lacked female toilets (or toilets accessible to their blue-collar female staff). Female workers there reported defecating in the open, some distance away from the worksite or suppressing the urge to do so until they returned home. Not only is this immensely distressing, but it also poses immense consequences on their general and reproductive health.

While several companies proactively fulfil their responsibilities under the PoSH Act (creation of internal complaints committee [ICC], publication of material informing people of the procedure to make claims, annual training about sexual harassment), such compliance appears limited to the white-collar workforce. Very few female informal workers we interviewed were aware of the ICC or had undergone training about sexual harassment, despite their obvious vulnerability. The discontinuous nature of contractual employment also deprives workers of such sensitization.

- *Poor protection standards put workers at a life-altering risk:* While the architecture for worksite safety and protection was very robust in the manufacturing facilities of the principal employers, worksite protection standards, availability, and use of safety gear and infrastructure was much less promising in the smaller units run by their vendors. A few units also doubled up as places for dwelling for the workers, a suboptimal arrangement that allows for employers to call upon workers at any time for pending work.
- *Static labour costs in vendor contracts result in abysmal worker wages:* The principal employers engage with their vendors through a work order that covers the cost of manufacturing or production. However, these contracts are awarded on a competitive basis, and vendors have to compete to lower their bids (and, therefore, margins). Thus, the provisions for margins and labour costs that get built into these work orders are so insufficient that small business owners struggle to institute systems for labour protection and security since these would directly cut into their profit margins. Further, these rates remain unchanged for many years altogether, not

accounting for inflation, which further means that the wage rates of workers remain static.

Small manufacturing firms must operate within several constraints—market-sensitive material costs, fluctuating demand, narrow margins, lack of skilled workers, and competitive pressure to offer specialized services. Even in cases where smaller production units are part of global supply chains that mandate adherence to certain labour standards, they undertake the bare minimum required to pass the audits. Unless the bigger corporation offers very lucrative terms, there is no incentive to the supplier to adopt these standards into their internal system, especially since Indian work is allotted based on weight and the rates offered by the principal employers do not even keep up with the changes in the dearness allowance. Even conscientious vendors who wanted better working conditions and benefits for their employees found it difficult to adopt them due to the ‘race to the bottom’ manner of outsourcing adopted by larger companies.

- *Lack of awareness and access to avenues for grievance redressal lend to the invisibility of workers:* Informal workers have almost no avenues for voicing grievances such as non-payment or delayed payment of wages or lack of social security. Very few companies have instituted such platforms. They are not accessible to workers informally employed in their ecosystem, especially in the downstream units. As an exception, we found an elaborate grievance registration system set up by one principal employer; however, even informal workers employed in the same premises lacked awareness of this. The absence of such systems and lack of information on accessing them renders workers quite powerless against labour rights violations in the system.

RECOMMENDATIONS FOR INDUSTRY TO ENSURE A BETTER FUTURE OF WORK

The observations in the earlier sections reflect the ‘decent work’ deficits that pervade the informal work arrangements in the manufacturing supply chains. Outlined below are a few fundamental policy propositions that would be imperative to address the current fault lines in the industry ecosystem:

- *Better wages and improved social security can aid the journey to formalization:* A concerted effort to bring in more formalization to the processes of recruitment, wage determination, payment of wages, and other social security benefits will be crucial to implementing

dignified working conditions for all workers and reducing the inequalities within the workforce. The new Occupational Safety, Health and Working Conditions Code, 2020, compels all employers with more than workers to issue an appointment letter detailing the terms of engagement. This document can contribute tremendously to workers' ability to claim wage dues or social security benefits down the line. The provision for fixed-term employment (FTE) reduces the need for 'break system'-based hiring and contractual hiring. More companies can employ workers directly for a determinate amount of time. This would allow larger companies far greater visibility into the terms of engagement of their workers.

- *Bearing the labour bill to enable a trickle-down effect:* The currently prevalent manner of outsourcing (discussed above) does not recognize vendors' efforts in providing dignified working conditions and additional benefits to their workers. Competition for bids discourages vendors from paying their workers' fair wages or making better social security measures available to them. Companies must recognize the importance of fair wages, OT pay, adequate occupational safety and health equipment, social security benefits, etc., and accommodate these expenses for their vendors to ensure that industrial manufacturing is not subsidized through diminishing expenditure upon workers' welfare. Companies could encourage the adoption of safer and fairer working conditions by prioritizing vendors (possibly verified through certification or auditing) who fulfil the normative criteria adopted through the Social Compact.
- *Boosting women's employment through requisite policy changes:* Purposeful inclusion of women workers into the workforce needs to be made an urgent priority to ensure that gender-related inequities are addressed. Ecosystem-level interventions such as skilling women can create a pipeline of trained women workers ready for industrial employment. Beginning with fairer recruitment processes that are deliberate about the inclusion of women workers, systems and processes that are more sensitive to gender issues will have to be instituted to ensure parity in wage rates, promotions, and stability of tenure. This is especially pertinent in the case of unskilled women workers who are compelled to take a break in their employments during pregnancy and maternity. Basic infrastructural facilities, including

separate washrooms and access to menstrual hygiene products, will have to be a fundamental tenet in ensuring gender-sensitive workplaces.

- *More stringent audits for contractors to enable ecosystem change:* The present means of auditing and oversight adopted by companies enable several legal violations by contractors to go unaddressed. In their haste to avoid the establishment of direct employment, the management becomes blind to the issues faced by its contract workforce (which is a majority of its total workforce in most cases). The transfer of employee management does not absolve the principal employer of all their legal and moral responsibilities towards contract workers. A more sensitive and transparent contracting system is possible within the confines of the law, which enables workers to report their issues either directly or through third parties such as CSOs to seek reformative action from the principal employer.
- *Maintaining the spirit of decent work for all beyond the legal minimum:* Few companies adhere to all applicable norms to treat their informal or contractual workforce. But even fewer still go beyond the legal minimum—the principle of responsible business and decent work is based on a broader philosophy of fairness and redistribution of profit shares among the shareholders and the workers. Unlike smaller vendors, larger corporations can adopt industrial practices that reward multi-skilling and experience among their workers (concessions already made for their white-collar workforce and their permanent blue-collar employees).

CONCLUSION

The Social Compact initiative places workers' rights at the centre of contemporary industrial sustainability discourse. It seeks to normalize decent working conditions for informal workers—to extend benefits that are routinely extended to formal and white-collar workers. Its most important attribute is its ability to penetrate, progressively, enterprises in the supply chains of larger companies. This ecosystem-based model has the potential to encourage smaller manufacturers to extend fairer conditions and pay to their workers—but their capacity to do so is limited in the status quo. To move towards a fairer social contract, the Social Compact encourages principal employers to help augment the ability of smaller employers through financial commitments and other measures.