

The Business of Doing (Informal) Business in India

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Background

The informal sector is vast, fast adapting and constantly evolving according to the market diktats. A nuanced understanding of the motivations, drivers and unique features is necessary to create an inclusive ecosystem, beyond just licensing and building common designated marketplaces. This study delves a little deeper into the lives of seven such businessowners, each distinct yet tied together by a few common narratives. The objective of the monograph is to understand the informal business according to its owner(s) and note shared insights, universal to all. The aim here is to provide an improved context to understand the business of doing informal business, not pure economic analyses. The report begins with a bird eye's view about employment scenario in India, followed by seven case studies, which leads to a few common features among them and finally concludes with a direction for the way forward.

Section I: Introduction

The informal sector does not conform to any established legal or organisational structure. Consequently, being a part of the grey economy, they do not file taxes and therefore have no obligation to disclose the size and scale of their operations to the government or any entity. Many fail to keep consistent records and rarely do they follow prescribed government guidelines. Therefore, it is not surprising that certain rules and regulations set by regulating bodies are often not designed to include them at all.

This single characteristic of being record-less or record-poor has many ramifications because no documentation also means no registrations and no formal contracts or accounts. On the positive side, they have lower operational and transactional costs, are more flexible and tend to have a higher tendency for providing employment given their low capital base. However, the lack of record-keeping also affects their operations and growth negatively. They do not receive any support from the judicial mechanism or protection by the law, besides, rarely do they obtain any benefits from the government and therefore cannot grow beyond a certain size. They are also not able to hire quality human capital or obtain credit from the formal sector. Such enterprises also have limited ownership of physical capital and therefore have scarce incentive which limits their ability to invest in businesses beyond a certain level.

Despite the odds, the informal sector makes up a significant part of developing economies, especially in countries such as India. However, hard data on its expanse is limited, although analyses of data from the NSSO's Large Sample Employment Surveys and the Periodic Labour Force Surveys provide an indication of the overall employment contribution of the informal sector.

Table 1: Enterprise Type and Employment Growth

Employment (in millions)			CARG		Share of Total Employed			
Enterprise Type	2017-18	2011-12	2004-05	2011-17	2004-11	2017-18	2011-12	2004-05
Informal/Unorganised	218	192	153	18	39	47.7	44.3	37.1
Formal/Organised	64	51	37	33	57	14.0	11.8	8.9
Agri-Cropping	174	189	219	-12	-24	38.1	43.7	53.2
Missing	0	1	4	-105	-212	0.1	0.2	0.9
Total	457	433	412	8	8	100.0	100.0	100.0

Source: Emerging Employment Patterns of 21st Century India, Laveesh Bhandari and Amaresh Dubey, 2019, Mimeo, Indicus Foundation

Note: Across all ages and population segments, as per the query whether employed in the last one week. Formal and informal sectors defined on the basis of answers to query on enterprise type. The multiplier is adjusted to conform to the total population of India.

Despite widespread acknowledgment of the role of the informal economy in India, it is still incorrectly believed that the informal sector is the ‘residual’ component, left over by the formal sector and perhaps as a result, the bulk of the government’s labour and economic policies are aimed at the formal sector.² However, the informal sector is the largest contributor to employment and this is not only rising, but in absolute numbers, has increased by double that of the organised sector.³ In the table above for instance, the informal sector employment increased by 65 million and that of the formal sector by 25 million between 2004 and 2017. The reasons for this increase have been the subject of much research on employment but will not be directly addressed here.

The purpose of this paper is to identify key qualitative characteristics of the informal sector and outline how they impact their possible growth and functioning. These same attributes may also affect the ability of the informal sector entrepreneurs to graduate to the formal sector. How that occurs is too discussed here.

Key Learnings

Although each of the businesses studied here is different in its own regard, there are a few useful learnings that need to be further studied.

- **Drivers of informal businesses:** The motivations for becoming an informal business entrepreneur are strongly connected with the availability of social networks. This social capital determines risk appetite (for example: to be able to afford encroaching on public land) and also growth expectations. Prevalent social norms and perceived status deter involvement of the children of most such business owners.
- **Growth of informal businesses:** Due to uncertainty of regulations, limited information availability and lack of contextual training avenues, there appears to be little desire for growth.
- **Tenure of informal businesses:** Despite presence of associations and unions, civil society and welfare groups, there is constant fear of the state among the business owners, further discouraging any desire for expansion.
- **Blurred lines between personal and professional:** The critical input of family in informal businesses goes unacknowledged by both business owners themselves and researchers. Further, the assets and liabilities of the owner and the firm are often intertwined
- **New Technology:** Since demonetisation, there has been an increasing (yet slow) pick-up of digital payment technologies. It also works as a business advantage by providing customer convenience.
- **Soft Competition:** There is subtle collaboration among the informal business owners for mutual monetary benefit.

² Informal Economy and the World Bank, Nancy Benjamin, Kathleen Beegle, Francesca Recanatini, Massimiliano Santini, 2014, Poverty Reduction and Economic Management Network, World Bank

³ Emerging Employment Patterns of 21st Century India, Laveesh Bhandari and Amaresh Dubey, 2019

Section II: Case Studies⁴

This section provides a brief socio-economic background on seven informal business owners. The businesses studied include a *paan wala* (betel leaf seller), a neighbourhood convenience store owner, a vegetable and fruit-seller, a tea-seller, tempo auto driver(s), cycle rickshaw drivers and a laundryman. The intent of providing personal and business details here is to put the unique features of such businesses, outlined in the next part, in a better context.

Case Study 1: *Paanwala* of Shahdara⁵

Kishan Kumar and his younger brother run a *paan* (betel leaf) shop in Shahdara, a low-income residential area in East Delhi. Started almost 40 years ago by their father, the shop is located in the main market area. They believe the location on the main road serves them well, except during times of traffic congestions and when there is road construction. Despite enjoying the legacy of being operational for the fourth decade, now run by the second generation of the family, there is an undeniable amount of threat posed by the landlord of this rented shop. The shop is open from 6:00 am and closes only at 11:00 pm, although most of the business happens in the evening. Together, both brothers are able to operate the shop for almost 14 hours daily. Kishan Kumar's brother manages the shop in the morning, while Kishan Kumar procures the raw materials on a shared scooter.

The daily revenue is approximately INR 8000 with a footfall of roughly 400 customers. Their long-standing reputation is why 80 percent of their customers are regulars, which enables the brothers to earn average monthly revenues of INR 2,50,000. After paying the suppliers for betel leaves, cigarettes, soft drinks, biscuits and chocolates, the monthly profit earned is around INR 40,000. Although items such as chocolate *paan*, ice *paan* and fire *paan* are trendy and earn higher revenues, the brothers refuse to be a part of the trend. *"It is not for our customers, they would not pay so much. Also, these new paans require special items and care. We can't do it."* The consistency of taste in their popular *paans* is preserved by having fixed suppliers.

Over the years, the business has changed from being just a *paan* shop, to selling cigarettes and now slowly transforming into a general store that stocks biscuits, chocolates and even basic stationery items such as notebooks and pens. This shift can perhaps be attributed to the falling demand for *paan*, now mostly comprising only their regular patrons and increasing demand for cigarettes and *bidis*. Despite these changes, Kishan Kumar and his brother believe that their financial needs are unmet, with health expenses of their mother and school and tuition fees of their children draining a major portion of their income. The brothers are also unable to

⁴ These case studies are based on in-depth interviews conducted by interns of Indicus Foundation.

⁵ Based on the interviews conducted by Anshika Prajapati

spend time with their family due to the long working hours. “One of us is always at the shop, we are never able to do a full family get together!”



The paan shop with all its products. Image Credits: Anshika Prajapati

Case Study 2: *Kirana* Store Owner of Lucknow⁶

Convenience or neighbourhood stores, popularly known as *kirana* stores are estimated to form 90 percent of the retail market in India with almost 12 million stores across the country.⁷ One such store studied is located in a densely populated market in Lucknow, surrounded by residential societies, housing colonies and low-income *kutcha* houses. The clientele served thus is spread over both low and middle-income communities. Being located on a peripheral road where a vegetable and fruit market is held on a bi-weekly basis, even conservative estimates suggest a traffic of 250-300 persons daily.⁸ The owner claimed this retail store is his sole source of income and reported zero savings, with his major expenditures being the school fees of his three children and rent of INR 7000 for his shop. However, the owner wished for a larger shop on the arterial main road merely 10-15 meters away which receives a significantly larger amount of traffic.

This shop has been running for the last 5 years before which he owned a temporary *paan* stall. Although the store provides daily amenities such as packaged food items and beverages, cigarettes and *paan* are top grossers. Despite having a lot of experience single-handedly operating a business, he states that there is no skill required to run such businesses, apart from primary knowledge about product prices. Despite expressing desire for a shop on a main arterial road, he believes his biggest asset is the shop and its location. The ability to access some working capital is further helpful in a business where credit is a distinct reality.

Another store, located just 10 meters away is owned and managed by two brothers. Largely similar to the previous store, it differentiates itself by functioning as both a wholesale and retail shop. Major sales amounting to 70 percent of the total are through wholesale. Even though it has been only 1.5 years since this wholesale business began, smaller *kirana* stores (such as the one aforementioned) are already regular customers. Retail shoppers are also shared between the two shops due to larger variety in daily amenities in the wholesale store. This contribution of retail sales in the latter is low, however, it is balanced by the revenues from the wholesale transactions.

The probability of profits is higher in this (wholesale) store, compared to the smaller retail store since it enjoys a larger volume of trade, better margins and the owners report comfortable lifestyle with a significant amount of savings. Although they were reluctant to share any details about specific figures, a recently purchased two-

⁶ Based on the interviews conducted by Namman Sachdeva.

⁷ Battleground Kirana: The anatomy of India's Raging Retail War, R. Sachitanand, The Economic Times, 2019, retrieved from: <https://economictimes.indiatimes.com/industry/services/retail/indias-ubiquitous-kirana-stores-are-finding-themselves-in-great-demand/articleshow/69707009.cms>.

⁸ During the course of the interviews, the researcher observed that the shop operated for 14 hours each day and served 10-15 customers in 30 minutes during peak hours.

wheeler and concrete plans to expand the business in the near future are strong indicators of the business doing well.



The paan shop turned retail kirana store, Image Credits: Namman Sachdeva



The wholesale kirana store, Image Credits: Namman Sachdeva

Case Study 3: *Subzi Wala of Vasant Kunj*⁹

Raju, along with his elder brother and mother runs a vegetable and fruit shop in a lane in Kishangarh village in Vasant Kunj, New Delhi. The siblings started off with a vegetable cart and have managed to expand to a small shop in 8 years. Initially operating on a one-way street, they encountered constant traffic congestions and were harangued by security guards of the housing societies which hindered business frequently. Additionally, the duo believed that customers prefer having a fixed location to buy their regular fruits and vegetables. Their current location on the busy, easily accessible *Gaushala Marg* suits them well, although it leads straight to the *Mehrauli Mandi* (Mehrauli vegetable market.) Being a bustling route, the resident families and bachelors, north-eastern migrants and students from the neighbourhood universities including Jawaharlal Nehru University and the Indian Institute of Mass Communication are unwilling to go to the wholesale fruit and vegetable market and rely on businesses such as Raju's. Since it is almost a daily interaction, almost all of these customers know Raju and his family by their names and not the name of their shop, KS Daily Needs. The brothers also home deliver vegetables and packaged drinking water for customers living within a one-kilometre radius. These relationships, Raju believes, is what keeps their business afloat despite the competition.

Raju and his brother estimate customer demand by averaging the daily sales and adjusting their purchases for the next day. For example, if a particular fruit or vegetable sells well, they buy more of it the next day, hoping the same trend continues and vice versa. They also always procure seasonal vegetables and fruits along with primary items - potatoes, onions, tomatoes, chillies and coriander. Their sole source for price details are the farmers and vendors in the Mehrauli market, since price fluctuations occur daily. On days when their calculations lead to slight overstocking, the remaining vegetables are stored in their home refrigerator and water is sprinkled over them to preserve their freshness till the next day. Since the purchase is in bulk, at times the vegetables lose their freshness or have gone bad by the time they reach their shop and when these are rejected by the clients the brothers incur losses. They are aware of competitive prices and better quality in the larger Okhla *Mandi*, but significantly higher logistical costs do not allow them to take advantage of the same. The business-owners strongly feel the need for their own tempo, yet are sceptical of availing a bank loan due to the perceived application complexity. They revealed being under severe debt due to their father's health conditions and the absence of any insurance, adds to their hesitation.

Between Raju, his brother and their mother, they operate the shop from 6:00 am to 11:00 pm. The mother takes over in the afternoon while her sons go home for lunch. Before Raju's father's health started deteriorating and becoming a significant expense to the family, they had employed a young boy from their village. However, with the

⁹ Based on the interviews conducted by Pratyasha Patel

rising medical bills, they decided to cut down on business costs and their mother replaced him at the shop. The primary monthly expenses are rent, transport from the *mandi* and electricity. Along with this shop, they also own a small-scale *kirana* store. The presence of which hints at the inability of their vegetable and fruit stall in meeting their financial needs. Interestingly, this shift isn't irrational (since the profit margins in vegetables and fruits are fairly higher than grocery items) and more in line with customer demands. "People find it convenient to buy vegetables along with grocery items such as eggs and bread." Another intriguing information shared by Raju was that his brother is trained as a plumber and is currently looking for a job, to supplement their income, the availability of which has been much lower since demonetisation.



The vegetable and fruit shop, Image Credits: Pratyasha Patel

Case Study 4: *Chai Wala* of Udyog Vihar¹⁰

Shankar is a *chai wala* (tea seller) working out of a small makeshift stall in the community parking in Udyog Vihar, Phase 3, Gurgaon. This shop is a rudimentary structure on the footpath that has a non-porous cloth for a roof to shield him from both the blazing Delhi heat and the biting cold winters. It is interesting to note that the current average market price for land here is INR 33,000/square meter.¹¹ This “shop” initially owned by his uncle was given to him in return for the cost of some supplies almost a decade ago. The shop serves both the low-income drivers and labourers and the middle-income corporate employees. It is still the same, the only difference being changes to the menu to keep up with the dynamic demand of its customers. When Shankar first began operating the shop, he only catered to the factory labourers working nearby. He reminisces, “*My (tea) vessel was never empty.*” However, four years ago, both these nearby factories shut down. To limit his losses, Shankar experimented by introducing Maggi (noodles), omelette, cigarettes and buns, along with more variety of *namkeens* (snacks) and biscuits. His idea worked because it attracted corporate employees from the vicinity, making them his most significant customer base. Shankar manages both these disparate groups with equal ease – serving the corporates with tea, cigarettes, omelette and Maggi (noodles) and the drivers and labourers with tea, bidis, *paan* (betel leaf) *masala* and the occasional namkeen and bun. Although all items are nominally priced, he manages to earn an average daily profit of INR 3000-3500, with 40-50 customers daily and almost a 100 percent mark-up.¹² Almost 90 percent of these are regulars, who make repeated trips (2-3) in a day. Tea is the commodity most in demand, followed closely by cigarettes, *paan masala* and omelettes. This demand further shoots up during the winter months. This tea shop is run single-handedly by Shankar, who is on a tight schedule – reaching his “spot” at 7:30 am, cleaning the space and setting up the stall for his customers. He serves his last customers by 7:00 pm, cleans his utensils and packs the remainder of his supplies. On the way back, he purchases items needed for the next day.

¹⁰ Based on the interviews conducted by Kinni Singh Kaushik

¹¹ Haryana State and Infrastructure Development Corporation Ltd, retrieved on 2nd October, 2019, <https://hsiidc.org.in/rates>

¹²

Item	Price (in INR)
Tea with milk	7
Black Tea	10
Lemon Tea	10
Omelette	25/2eggs
Maggi	20
Cigarette	10-17
<i>Bidi</i>	5-10
Mathri	5/piece
Biscuits/ <i>Namkeen</i>	Variable
<i>Paan masala</i>	5/sachet
Buns	7/piece
Bread	5/piece

Before becoming a mid-scale business owner, Shankar worked in hotels on Lodhi Road from the age of 13 when he first migrated from Bihar.



Shankar in his tea shop, Image Credits: Kinni Singh Kaushik

Case Study 5: Tempo Auto Drivers of Meerut¹³

For most auto drivers, business begins at 7:00 am with the *Pradhan* (elected union leader) allotting numbers to decide an order. Interestingly, the price for ferrying is not fixed and is dependent on the said *Pradhan* and the amount charged by the substitutes including the public buses plying on the same routes. With every fluctuation in the cost of CNG, the drivers request the *Pradhan* to revise the rates. The current price is fixed at INR 8/per head for 3 kilometres.¹⁴ Each driver has a permit to operate on specific routes, however, some of them even own city and all-India licenses. After ferrying customers according to the order decided by the numbers, at noon, the drivers are free to choose their own routes and not wait for their “turn.” A driver interviewed stated the absence of “police checking” on a particular route as the sole reason for his preference to ply his auto rickshaw on that route. Although all the drivers interviewed claimed they possessed all the required

¹³ Based on the interviews conducted by Sakshi Mital

¹⁴ The quoted price is from July 2019 when the interview was conducted

documents and licenses, their fear of the police was due to not following business rules such as maximum number of passengers allowed by the permit and wearing the uniform. However, a few of them stated additional reasons such as harassment by the police leading to unnecessary waste of time and not being allowed to wait anywhere except at designated auto stands. Whenever there was trouble with the policemen, the Pradhan would get involved and resolves the issue. Most of the drivers claimed they paid a certain “fee” (INR 350) each month for not letting any further action being taken.

None of the drivers interviewed had expanded the business over the years, although some of them expressed desire to have another auto to double the frequency of their turns. For the auto drivers who ferry school children, there is no wish to expand the business, perhaps because of additional income provided by odd jobs such as ironing clothes etc. The revenue earned each day varies depending on the number of hours put and the number of autos plying that day. On an average it ranges from INR 500 to even INR 800 on a good day.



A tempo auto waiting for passengers, Image Credits: Sakshi Mital

Case Study 6: Cycle Rickshaw Drivers of Lajpat Nagar¹⁵

Arjun, a 28-year-old cook migrated to Delhi from Mumbai two years ago due to health issues. In his experience, the most crucial skill in this business is expert navigation. Ajay, a rickshaw driver since the past 30 years differs. He believes it all boils down to persuasion and networking, with income being directly proportionate to number of customer relationships. In New Delhi alone, there are an estimated 7,00,000 cycle rickshaws, either owned or rented through a chain-supplier for INR 40-50 per day.¹⁶ With such high competition wherein supply significantly exceeds demand, the social capital becomes crucial for success in this business.

The demand for cycle rickshaws is peculiar and limited to areas such as metro stations, colleges, markets and smaller lanes which are inaccessible by cars. The cycle rickshaw-drivers studied reported their average monthly income to be ranging from INR 4000-6000 varying based on the number of hours of operation, with the major expenses being food and accommodation and one-time emergencies such as medical issues, signifying their poverty levels.

Case Study 7: *Dhobi* of South Delhi¹⁷

Deepak, a 35-year-old migrant from Kolkata, works as a laundryman (*dhobi*) in Alaknanda, New Delhi. Although he's been in business only for a year, he already has 28-30 loyal customers, providing him an average monthly income between INR 25,000-30,000. This is excluding extra business gained by providing emergency services to people needing clothes urgently washed and ironed. He also earns additional commission by providing dry-cleaning and steam-cleaning through partnerships with these businesses. Customers come back to Deepak due to the aforementioned value-added services he provides which he outsources to nearby big shops.

Although he charges more than his peers, he claims that the higher cost has not come up as an issue with any of his clients. Perhaps it is due to his skill of understanding and remembering the customer needs, including details such as whether they want fabric softener to be used, how they like their clothes to be sorted etc. Not asking repeated questions is according to him the most important yet often overlooked skill. Deepak feels his payment is justified. Working at his "shop" from 9:00 am-5:00 pm, ironing clothes while entertaining customers, he goes back home to sort the clothes into piles of dark and light, completes the pending ironing and begins the next day at 4 am at the Okhla tank to wash the clothes.

¹⁵ Based on the interviews conducted by Kanishka Agarwal

¹⁶ Green Cab: Dial a Rickshaw Service, Delhi Integrated Multi-Modal Transit System (DIMTS) Limited, https://www.dimts.in/download/Concept_Paper-Green_CAB.pdf

¹⁷ Based on the interviews conducted by the author

Deepak wants to increase his business size, customer base and revenues. However, all he knows as of now is that he cannot do it alone. Having three children of his own, he confesses that he would never hand over his business to them. *“I am spending 5000-6000 thousand (rupees) every month on their tuition, they should get good government naukari.”* What’s interesting is that Deepak began his business in Paharganj but quickly moved on to South Delhi since it was too risky there, based almost entirely on the whims of the foreign tourists.

Section III: Characteristics of Informal Businesses

While there are many peculiarities of each case reported in the previous section, there are certain underlying patterns that are common not just among these seven cases, but arguably also across most informal service businesses. We briefly discuss each of these, the ordering is as per the hypothetical life cycle of the business.

Underlying Factors

The informal business comes into being because mostly that was the only option available to the entrepreneur. A critical factor of motivation is also the surrounding social network – which determines acceptability based on the contextual norms and customs. For instance, *paan walas* such as Kishan Kumar are more popular in tier two and tier three cities and towns and cycle rickshaw drivers such as Arjun are not allowed in certain localities like Greater Kailash in New Delhi. Formal sector or government jobs are highly paying but rarely accessible for the bulk of those with a poor education background. Formal sector business is out of the question as sunk costs of starting a business are extremely high. Most importantly, the informal sector business mostly tends to externalise costs by using public space, though not always.

Space is arguably the most expensive factor input and formally allocated spaces are out of reach of the entrepreneur. However poor policing, poorly defined accountability over who is in charge of protecting the public space combined with sometimes a system of side payment makes this input available to the entrepreneur at relatively low cost. Doubtlessly, this same mechanism also reduces the certainty of tenure, and that may impact operations as discussed later.

Capital is another input that is used economically. Service sector businesses typically require less capital than manufacturing, but even where required, the objective of the enterprise is to minimise investment in the business. The capital is typically provided for by friends and family and also informal sector credit agencies. It is obvious that the formal financial sector will be unable to provide credit when the business is located in a space that is technically illegal. Hence even if government policy favours or insures collateral free loans, the problem of legally sanctioned space will adversely affect formal sector credit provision.

What is also critical in starting a business is finding the *right location* which has the potential to translate into *good relationships*. Micro informal businesses are typically servicing demand from a very small area, and both relationships and accessibility to the demand play an important role. While location characteristics may differ depending upon the business, they are all physically close to their clientele. A high traffic road or crossing for the *paan wala*, a busy market for the *kirana* store owner, a parking space of a business compound for the *chai wala* and a high frequency road for the auto drivers and cycle rickshaw drivers and the residential society for the *dhobi* are some obvious examples.

Limited Business Growth Objectives

Growth can be achieved through three different routes, not mutually exclusive. The first is through improvements in value addition and therefore margins, the second through greater scope of services or products being sold, and third through expansion to other venues.

In just one case of the *dhobi*, we found a desire in improvement and value addition. Deepak (the *dhobi*) took conscious effort and care to wear tidy clothes and keep his “shop” clean, which for not only convinced regulars but also attracted new clients. In all other cases there was little interest in ‘being different’ and looking for higher value add or margin possibilities. There could be two broad forces behind this case being an exception among the seven studied. The first being the endemic belief of the entrepreneurs that they are simply ‘takers’ of market signals and will be unable to generate extra revenues from any innovation. When living hand-to-mouth, the ability to do things differently is also limited. The second force could simply be lack of awareness. The reason behind this lack of experimentation is important to decipher, for more than 200 million people are employed in this sector, too important not to innovate.

The *dhobi* decided to also provide laundry services and was able to generate some extra funds from that. The *chai wala* also started to keep eatables to go with the tea. The *paan wala* were keeping other items of daily consumption even though the margins were lower. This growth component works, however the lack of space limits the extent of expansion possible through adding greater products or services, observed in the limited number of products which could be managed in the case of the *kirana* store owner and the *paan wala*.

The third type of growth, through ‘branch’ expansion to other venues is fairly constrained. A cash only business with limited record-keeping and low faith in the law, order and justice machinery affect hiring and delegation to employees. If required, record-keeping can be done, as was the case with the two brothers who shared a single *paan* shop. However, the problem of trust and inability to protect theft or fraud by employees is a key consideration, and arguably is the key reason that prevents expansion. This was also seconded by Shankar, the *chai wala* when questioned about expansion, “*If my business becomes bigger, how will I manage everything on my own?*” As a consequence, where expansion does occur, it is typically only at the margin.

The retail *kirana* store owner of Lucknow, denied any aspirations to scale the business operations, in spite of reporting zero savings. Being aware of loans to scale up and offer a greater variety of products, he cited not wanting to invest in a bigger store and to hire employees. Is this risk average behaviour as is often mentioned in literature,¹⁸ or simply the expectation of low returns vis-à-vis high interest costs of

¹⁸ Poverty, Risk Aversion and Path Dependence in Low Income Countries: Experimental Evidence from Ethiopia, Yesuf M., Randall A., 2009, American Journal of Agricultural Economics, pp. 1022-1037, retrieved from:

this segment (ranging from 20-50 percent)? It is difficult to tell, but the net outcome is low tendency to invest.

However, there is also evidence for the soundness of such decisions of not scaling by the owner. An increase in size or relocation to a more centralised location is associated with a shift to a more detached retail enterprise. Whether the highly local clientele will venture to travel distance would be a serious concern.¹⁹ The wholesale business owners (having a business to business -B2B model) on the other hand did have aspirations to move out of their current store into a larger facility and offer a higher range of products. They expressed their biggest constraint to expanding their business and improving their profits was the amount of rent of 12,000 INR per month that they had to pay for the store, which was their costliest area of expenditure.

They expressed a desire to relocate from their current rented location to their own brick and mortar store that they would own, thus doing away with the monthly rental expenditure and the uncertainty of tenure. The brothers had been operating the store for a relatively shorter amount of time as compared to the neighbouring retailer but had a more profitable operation. They were actively in search for land to purchase to build their own store on but were aware that they would have to operate for a long time to save enough money for their investment. While the retail store owner's reluctance to shift to a more centralised and larger operation was endorsed by sound economic reasoning of reduced personal interactions from traditional clientele, the same constraint did not apply to the wholesale store. The retail store's customers had much lesser purchasing power and the feeling of trust and availability of credit were attractive characteristics of the store. The wholesale store owners felt that relocation to an owned facility was necessary to be able to invest more and grow the business.

Poor Certainty of Tenure

In all businesses studied the team found a disinclination to invest in the business. Arguably one of the main reasons for the disinclination to invest in capital comes from uncertainty of tenure at the current location of the business. Yet the risk of encroachment on public land can only be afforded by those with a strong social network.

Excluding Kishan Kumar, the *paanwala* in Shahdara and the cycle rickshaw drivers in Lajpat Nagar, all business owners interviewed reported paying some kind of gift or protection money for operating their business from a particular space. For Raju, the vegetable and fruit seller in Vasant Kunj, a constant concern is losing the sole

<https://www.jstor.org/stable/pdf/20616258.pdf?refreqid=excelsior%3Abeecd86b82099df139dc76f8843da5e4>

¹⁹ The Role of the Neighbourhood Store in Developing Economies: The Case of Dagupan City, Philippines, Dannhaeuser N., 1980, The Journal of Developing Areas, pp. 157-174, retrieved from <https://www.jstor.org/stable/pdf/4190748.pdf>

livelihood due to the ongoing shop ceilings by the municipality officials. For Deepak, the *dhobi* even after almost two years of operation, he works out of a make-shift stall, with a table and tarpaulin sheet cover as the only set-up. The argument being that municipal officer raids could adversely and permanently damage such investments. “*Yeh Municipality ka kya hain, aaj kuch rule, kal kuch aur!*” (Who knows what determines the municipal officers’ actions, today its one rule tomorrow another!) This points that many informal firms remain so by choice.

The strong disinclination to invest in capital can be seen in almost all informal business set-ups. Kishan Kumar, the *paanwala* in Shahdara provides a token for cold-drinks to his customers which they need to collect from him at his home, where it is stored in the refrigerator. Shankar, the tea seller in Udyog Vihar and Deepak, a *dhobi* in Alaknanda both work out of make-shift stalls.

There is also a hesitation to shift to a structured licensed shop. Attractive location of the current business is not the only issue, there is an uncertainty of municipal rules and regulations, and also an inability to access or even understand these rules. Shankar, the *chai wala* possesses concrete knowledge about the financials of a licensed government built shopping space and the various instalment payment options, and yet is hesitant in making the shift.

Moreover, government departments overseeing space and its usage are used to a policing function, whereas what such businesses require is a service and advisory function. The absence of associations or NGOs dealing with such businesses further works against them.

It is not merely investment in the physical element of business. The voluntary interview method is unable to decipher how such businesses may also be investing less in their social capital, or personal relationships, which have a strong role to play in the success of their business. But we can conjecture that an entrepreneur unwilling to invest in physical capital will also be less likely to invest in intangibles.

Hesitation in Embracing New Technology

The ability to keep up with new trends is a strong indicator of survival for all informal businesses, however, it becomes more crucial for those with competition from big corporations such as laundromats and vegetable supermarkets. Deepak, the *dhobi* from Alaknanda, differentiates himself with his enthusiastic encouragement of technology. “*Jab jarurat padta hain, tab apne aap haath-pair maarna padta hain.*” Each time the customer asks if he uses a certain payment application, he makes a note of it in his diary and searches it on YouTube later that night. Currently, he is comfortable using Paytm, Google Pay (Tez) and BHIM. It also ensures immediate payment in a lot of cases since when customers say they do not have enough cash or the exact change, he offers them to accept the payment digitally. It actually works well

for him, since the digital payment systems allows him to keep tab of the business each customer is giving. . Moreover, though he has studied only till the eighth grade he is unable to decipher the written material on various financial instruments available to him. He is most comfortable with videos where such content is available only to a limited extent. Though he has heard of investment options such as mutual funds and fixed and recurring deposits, he hasn't ever tried using them because according to him there is so much information on the internet. Moreover, different kinds of content on the subject appear to confuse him more. He shared quite aptly, "*I may not be smart, but am smart enough to know not to get into something without understanding it completely.*"

On the other hand, the vegetable vendor Raju's mother is quite forthright in her opposition to digital payment applications. "*We only do transactions in cash, with all this online thing, who knows where the money is. There is no safety.*" Her fear is strong and perhaps the perceived benefits not high enough for her son to explore these technologies either.

None of the auto drivers of Meerut interviewed showed any inclination to adapt new technology, even if it were to help their business. One of the reasons cited by an auto driver was lack of options. For example, there was no spread of corporations such as Ola and Uber, Meerut being a small town.

New technologies, whether digital or otherwise, have two characteristics that appear to work against them. The first is the informational gap, as conventional means of sharing information are not appropriate for the low literacy and education levels of such entrepreneurs. And the second is lack of examples or show cases. While the mobile phone was embraced rapidly for communication purposes, technologies that require the user to understand how to use and benefit from tend to have a slower take-up. Finally, the risk associated with digital money to be out of their control is stronger as the ability to access and communicate with formal sector institutions is also limited.

Important Role of the Family

For small-scale businesses including those studied here, the role of family is crucial to the business. For the *paanwala* of Shahdara, the engagement of family members in the business is not limited to the two brothers. Their mother and wives are involved in preparing the *chuna* and *kattha*, the main quality indicators, differentiating the *paan*. The owners proudly claim it takes almost 72 hours to prepare the *chuna* and 24 hours for the *kattha*, the raw materials for which are sourced only from their native village to ensure consistency in taste and flavour. The two brothers are also able to operate their shop for longer, from 6 am to 11 pm. It is note-worthy that the children of both the brothers refuse to contribute and associate themselves with the shop, for better acceptance within their peer network. This is

also true for the wholesale shop owner of Lucknow, wherein the two brothers together run the shop for almost fifteen and a half hours daily. Similarly, for Raju, the vegetable seller in Vasant Kunj, their mother joined the business replacing their paid helper after their financial crunches. Her presence allows them to keep their store open throughout, even during lunch time.

Although Shankar, *chai wala* of Udyog Vihar has to do it all himself – sweeping his spot, serving customers, keeping accounts and even procuring raw materials, he is hesitant to hire a helper. This sentiment is also echoed by Raju and his mother, “*While hiring an outsider, it is important to be convinced of their loyalty and dedication.*” Deepak, the *dhobi* from Alaknanda is unable to expand his business through additional services such as home deliveries which he believes makes a lot of difference, since he too runs his business single-handedly.

The issue is not simply of lack of formal labour contracts, but the inability of such entrepreneurs to access the law and order machinery. The recognition that such moral hazard opportunities exist lead to the hiring of workers from the community or even better, the family. Therefore, rather perversely, the largest employer (the informal sector), is unable to employ from the market and has to depend upon social network and family, to maximise earnings.

Synergies with Other Businesses

An interesting commonality among most businesses studied was that despite the lack of formal contracting, there is a strong element of synergies with other businesses that helps such units survive. These business ‘synergies’ although seemingly basic and almost trivial, play an important role in differentiating the business from others and create a value-addition in comparison to the other similar businesses. For example, Arjun, the rickshaw-puller from Lajpat Nagar has an understanding with the juice-seller which gives him a place to sleep on most nights. This bond between the two is further cemented with monthly deposits of INR 2000-4000 Arjun makes to him, since he lost his bank passbook and the registered mobile number. He pays back the juice-seller by disposing the leftovers, fruit peels and used plastic glasses to the dump yard each night after the shop closes. Another noteworthy symbol of collaboration in this business is the tying up of all the cycle rickshaws together in the closest open space to reduce the probability of theft of any one of them.

This cooperation extends to pure monetary benefits for the *kirana* store owners of Lucknow. The retail store owner does not sell Marlboro cigarettes in lieu of an unofficial contract made with a competing brand, entailing no sale of these cigarettes. Though technically he keeps his side of the bargain, the retailer has tied up with a neighbouring store. The agreement, again informal, entails the purchase of Marlboro cigarettes by the retailer which he then supplies to his neighbouring

store. The returns on those sales made by the neighbouring store are shared with him.²⁰

For the auto driver of Meerut who ferries school children, the trust the children's parents have on his family's presence in their neighbourhood, is a critical element. This helps provides him a constant income over and above his unpredictable daily revenue from ferrying people. Moreover, it also gives him access to interest free loans of up to INR 50,000 whenever need be through the children's parents.

Deepak, the dhobi of Alaknanda provides services of dry-cleaning and steam-cleaning wherein he acts as the agent of other businesses. Note that in this case as well the dhobi is liable in case the clothes are harmed or stolen.

The synergies may be horizontal or vertical or even be with unrelated businesses. But there is a deep connection between various informal sector service entities that help their operations. These relationships need not be based on community or family, but are more related to the operations and are highly idiosyncratic to each business.

Also note that in each of these cases, what makes these synergies work is the fact that transaction values are not very high, returns significantly higher, and the repeated nature of transactions enables a long-term relationship to develop between such businesses despite the lack of contracts.

Another set of relationships are related to those with the customers which are discussed next.

Social (Relationship) Capital or Trust²¹

Trust plays a key role in the operations of the businesses studied here. The reason that *kirana* store owners are still able to capture the market despite the increasing presence of supermarkets is the feeling of mutual trust allowing them to offer credit services to their middle and low-income customers. The retail store owner did not explicitly advertise his credit facilities to the customer, however, he allowed regular and familiar shoppers to pay later in case of insufficient cash or exact change. This convenience raised his sales yet it also increased risk of non-payment as he did not maintain any record of the pending payments and relied on the trust and his own memory. The entire tea selling business of Shankar in Udyog Vihar is based on trust. Of the 40-50 daily customers, 90 percent are regulars working in the nearby offices, making multiple trips in a day for tea and cigarettes. All these customers do not pay immediately and instead make a lumpsum payment at a later date, because the cost per trip is low. Most of these patrons come in groups and Shankar finds it challenging

²⁰ The retail store owner did not divulge the exact figures, however, the surrounding *paanwalas* reported being paid up to INR 15,000 monthly to deter them from selling Malboro cigarettes.

²¹ What is social capital, OECD Insights Human Capital, <https://www.oecd.org/insights/37966934.pdf>

to prepare, serve and track all the items picked up by them. He confesses he relies heavily on goodwill of his customers, asking them what all should they be charged for.

Trust also allows the auto driver of Meerut to earn additional monthly revenue by ferrying school children.²² The primary reason for the parents entrusting just this driver with their children is their association with his father since a long time. Interestingly other auto drivers of Meerut also provide such a service (of ferrying school children) and also sometimes provide credit to such customers. The probability of default is much higher however with other customers who are picked up and dropped from non-fixed locations, and credit is also less likely in such circumstances.

Despite having a strong social network of Bengali friends around the city, Deepak, the *dhobi* from Alaknanda feels intense sense of shame in asking for monetary help. “*Most of my friends are a part of my larger social circles, it is quite embarrassing if they ask for their money in front of others.*” This social network is important to him, more so since it acts like his family in Delhi, but it is not the preferred source of his credit needs, that is more likely to be from the business, including both vendors and customers.

Competition

Though each informal service studied is one among many in the vicinity, we find that each has created conditions wherein there is some differentiation. These complex relations show cases of both dynamic cooperation and competition. This could be location, relationship with customer, variation in products or services, etc. The wholesaler-retailer in Lucknow for instance keeps higher end products for retail, but acts as a wholesaler for lower end products as well as cold drinks etc. (items that he does not retail). The retailer also enjoys his own niche in the local market. The presence of a larger variety of tobacco products and *paan* is an advantage in attracting customers. This retail store is dependent on the wholesale store for its purchases and supply of goods, but was able to attract customers through greater lending, availability of *paan*, and refrigerated products not available in the immediate surroundings.

Deepak, the *dhobi* from Alaknanda, Delhi has a mutual understanding with the other laundrymen, almost working as a small monopolies with maintaining similar prices and distinct customer base. For the cycle rickshaw drivers of Lajpat, this understanding of fixed area of operations is done by their unions with the e-rickshaw association.

In other words, though at the macro level, there are many similar informal sector service businesses, at the micro-locality level, there are avenues for small premiums to be made due to product or service differentiation or simply cartelisation.

Lending and Borrowing Patterns

All the business owners studied here exhibit informal lending and borrowing behaviours. Kishan Kumar, the *paanwala* of Shahdara is involved in both – availing

²² This auto driver drives 16 children (8 in each round) for INR 700/child. The monthly costs are limited to CNG, amounting to INR 5000, earning him a monthly profit of INR 6200.

40 percent purchase credit from his 8-9 fixed suppliers and providing credit up to 30 percent of his sale to his regular customers. The payments to be made and received are cleared at the month end, according to the records maintained throughout. Raju, the vegetable seller in Vasant Kunj also makes purchases on credit, although he is cautious and pays back as soon as possible, so as not to be burdened by recurring interest. He reports that during demonetisation, only credit from his suppliers helped him keep his business afloat, allowing him to pay back after a few months. Demonetisation was a major set-back to this business since they were unable to pay back smaller denominations and hence had to let go of considerable amount of payment from their otherwise dependable customers.

Having fixed suppliers works well for Shankar, the tea seller from Udyog Vihar as well, since he is now permitted to buy multiple items through multiple trips and pay only once, towards the month end when he has liquid cash. Surprisingly, there is no set timeline for repayment either for the suppliers or by his own customers.

For the auto drivers of Meerut, sales representatives from the auto companies helped them obtain a loan for the same. Although they were not aware of the different interest rates charged by different banks. One of the driver interviewed had received the same through Kotak Mahindra Bank, the auto was of Mahindra, and the sales representative of the latter helped in availing the loan. The initial down-payment, however, was arranged through an informal loan and a friend with regular transactions at the bank needed to act as a guarantor. The auto drivers of Meerut take daily loans from local agents, which are returned to at the auto-stand where the agents visit frequently. The collateral in these loans is trust and the auto drivers did not report any harassment in case of non-payment, just revised 5 percent additional interest rates. This is not surprising, as the auto rickshaw business is a highly liquid business and repayments are not too difficult.

While taking such loans to replace tyres etc, the drivers also defer fares to the next day by their regular customers. Other sources of immediate funds for emergencies is committees and Self Help Groups the women in their family are participants in.

For Deepak, a *dhobi* in Alaknanda, the need for capital is quite critical, whether to buy a new industrial steam iron replacing his coal-fired one or to manage emergency health expenses. *“Right now, I take loans from a local goon here.”* The cost is not only the 45-50 percent interest, but the fear of being harassed for repayment publicly. Banks don't offer him loans above Rs 5,000, and he laughs saying *“I give more credit to my customers!”* He is referring to the overdraft facility of the Jan Dhan Bank account. Banks have refused him loan for the lack of a credit history. *“Why would I save my money in a bank for merely 3-4 percent return? I am a part of a committee with my friends, I lose money, but when I do receive, it will be a good sum.”*

This is an interesting element in the relative failure of banks in becoming accessible to the informal sector, the effort, reporting and time required for obtaining a loan are so high, that the formal sector with its low returns, is also not an attractive savings option.

The small Lucknow retail store was serviced by 6-8 suppliers for its products but most of them did not provide any credit facilities and the owner was required to pay them on receiving the products. He did however receive credit facilities for packaged food products for up to a fortnight. The owner indicated that availability of credit was not a huge constraint as it did not hinder his business operation, nor did he have to resort to borrowing from other sources.

The wholesale store in turn was supplied by more than 50-60 suppliers and had a much larger variety of daily amenities and household goods that it offered. All the suppliers provided credit facilities to the business owners and the owners were required to pay them within the week, but this was not a binding constraint and the dues could be cleared in the following week also. The owners did not have to resort to any borrowing and had sufficient working capital to pay for their intermediary goods, indicating no dearth of working capital.

The wholesale *kirana* store owners in contrast to the retail store owner, did keep a formal record of the customer credit offered in a diary that was meticulously maintained. Maintaining a record of the credit offered was necessary in their business as there were two people who could be operating the store at different points of time and in the absence of a formal record, communication of the credit offered between them would be extremely difficult and error prone.

The brothers' operation was however similar to the retail store owner's in their limited range of customers that they would offer these credit facilities. The wholesale store only provided credit in small amounts to reliable and regular customers who would purchase in bulk. Purchases made in retail were typically not allowed to be paid at a later date and credit facilities were offered only as the last resort to regular customers occasionally. This indicates that the more established business could dictate terms better and therefore controlled the credit that they gave.

Section III: Conclusion

The growing informal sector employment is significant, yet the sector's contextual analysis has been marginal. Since some or all such aspects of informal enterprises are off formal record, there exist significant knowledge gaps in terms of difference in behaviour of informal firms and extent of assistance to that should be provided. Understanding this heterogeneity within the informal businesses is crucial for designing appropriate policies. The coexistence of both formal and informal firms has critical policy implications and there is a need to differentiate and acknowledge the two.

Perhaps inclusive growth shall not be possible by merely redistributing the fruits of growth. An inclusive growth plans needs to be strategised to enable participation of such entrepreneurs in meaningful economic processes. Certain identifiable constraints of most informal businesses include lack of suitable and secure premises in good locations, limited or no accounting skills, lack of financial skills (such as credit and insurance etc) and vulnerability. A step forward would be to invest in providing basic financial information and targeted training programmes, which are both accessible and action-oriented, along with providing suitable premises for the businesses. This approach instead of enforcing formalisation (which is often limited to tax registration and business licensing), would make a considerable difference to employment, earnings and the working conditions of the poor, being an instrument of inclusive growth.

Appendix

Below is a list of government initiatives aimed at the informal businesses in India.

1. Street Vendor's (Protection of Livelihood and Regulation of Street Vending) Act, 2014, <http://legislative.gov.in/sites/default/files/A2014-7.pdf>
2. Thee Unorganised Workers' Social Security Act, <http://legislative.gov.in/sites/default/files/A2008-33.pdf>
3. Pradhan Mantri MUDRA Yojana (PMMY), <https://mudra.org.in/>
4. Pradhan Mantri Shram-Yogi Maan-Dhan Yojana, <https://labour.gov.in/brief-pm-sym>
5. National Commission for Enterprises in the Unorganised Sector, <https://pib.gov.in/newsite/PrintRelease.aspx?relid=68099>