



## The Informal Sector Needs Credit

### What is the issue?

\n\n

\n

- The 2018 economic survey had recommended an urgent prioritisation of investment revival to arrest its impacts on growth.

\n

- As the slowdown is particularly centred in the informal sector, policies need to be recalibrated to specifically address this problem.

\n

\n\n

### What is the current investment scenario?

\n\n

\n

- While investments in the economy peaked 11 years ago, a slowdown started 5 years ago, and has currently become severe.

\n

- The slowdown in private investments in India is now well recognized and is visible chiefly in the informal sector and lesser felt in the corporate sector.

\n

- Notably, financial stress on company balance sheets and the severe bad debt problem hindered big ticket corporate investments only briefly in 2014-15.

\n

- Subsequently, corporate investments had picked up but private investments in the informal domain have been largely stagnant.

\n

- **Informal Sector** - It has been estimated by NSSO that about 6.34 crore unincorporated non-agricultural enterprises exist.

\n

- These often operate out of homes, typically employ less than 10 workers and do contribute a considerable chunk of the private investments

\n

- As informal enterprises are one of the principle engines of growth, the slowdown in the sector is delaying a full economic recovery.
- The fall is so severe that the government's macroeconomic stimulus by increased public investments hasn't been able to compensate for it.

\n\n

### Why is the informal sector more vulnerable?

\n\n

- Consuming households tend to be net savers, while the government, corporates and unincorporated enterprises are net debtors.
- **Competition for Funds** - A major chunk of saving are held with banks, insurance companies, from which the net debtors borrow from.
- When government borrows considerable sums to finance its deficits, it reduces the lending potential of financial institutions due to a smaller fund pool.
- Hence, while the big corporates can still access capital from the remaining or through the bond/share market, the informal enterprises get left out.
- Notably, informal sector does not have the resources required to access credit from diverse sources and is left to depend on extortionist money lenders.

\n\n

### What caused the present situation?

\n\n

- The government had increased its spending in the aftermath of the global economic slowdown to provide an economic stimulus.
- This saw a surge in fiscal deficits, which had to be serviced by borrowing.
- Concurrently, banks that were already stung by the bad loan problem, have been played safe by lending generously to government projects.
- Along with all this, the recklessness of some states governments also seems

to have crowded out the informal sector from formal credit avenues.

\n

- As a consequence, there has been a cut back in private informal sector investments due to lack of sufficient credit.

\n

\n\n

### **What needs to be done?**

\n\n

\n

- Given the anatomy of the private investments slowdown, a macroeconomic stimulus may not be the best policy choice.

\n

- Urgent fiscal deficit reduction, quick clean-up of the bad loans mess, and restoration of banks' health are more likely to revive private investments.

\n

- The current credit policy seems skew in favour of the visible and large organised enterprises, which needs to be corrected.

\n

- Recognising the credit needs of the unorganised sector is hence crucial.

\n

\n\n

\n\n

**Source: The Hindu**

\n



# **IAS PARLIAMENT**

*Information is Empowering*

A Shankar IAS Academy Initiative