



GST: Implementation diffusion or hierarchical spirals!

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Abstract

In my present paper, my effort is to detect the contributory economic factors explaining the policy of implementation of GST in India in recent past. The study has tried to unfold a few facets in correspondence to the “grey” informal localization of industries and services in India. It seems that such an exploration is crucial to make a successful policy orientation like GST. The incorporation of the changes in the nature of Formal-Informal linkages makes the scenario further intensified within the realm of diversified heterogeneity of linkages along with the issue of increased volume of informal labour mobility. The present paper consciously avoids the issues like digitalization and demonetization of the economy in order to make the present study more concise one with the expectation to have separate studies with them. The micro-level field surveys, sampling design and data analysis of the study conducted is based upon the standard model approach to avoid spatial homogeneity.

Keywords: informal sector, cluster, location, mobility

1. Introduction

The present paper is an effort to detect the contributory economic factors explaining the policy of implementation of GST in India fetching a huge debate on-going thereby hindering its targets in recent past. The study attempts to unfold a few contributory factors in correspondence to the “grey” economy of informal localization of industries and services in India. To do this, it is accrued that the changes in the nature of Formal-Informal linkages makes the scenario much intensified within the realm of diversified heterogeneity of the informal economy with increased volume of informal localized production of goods and services and increased informal labour mobility. To infer this, the present study consciously avoids the issues like demonetization and digitalization to make the study more precise one.

2. Methodology of Analysis

The logical argumentation of the study is based upon literature support, case studies conducted and primary survey results. The survey process is exhaustive in nature. The survey conducted is based upon qualitative purposive sampling procedure with semi-structured questionnaire and indirect interview method. The micro-level field studies, sampling design and data analysis procedure are based upon the standard model approach. The implication is that the selection of any sampling window does not depend on data availability (or non-availability), hence avoids any spatial homogeneity. However, the spatial distribution of sample units is cross-sectional, given and known. Sometimes an ethnographic study has been approached due to data non-availability and data non-responses in the sample survey area under the purview of the study conducted.

3. Hierarchical Structure in Operation: Formal-Informal Linkage Frame

The industrial organization after globalization is subject to

significant changes. The changes are particularly crucial if we consider informal sector production. The informal sector producing units, even small in operation, are now competing with formal sector production by producing similar products or services. To do this, the informal units are generating employment for other informal workers by following hierarchical production chains allowing both horizontal (spatial) and vertical (hierarchical) segmentation of production and market. In the “Bottom of the Pyramid” structure, the formal sector purchases intermediate and/or semi-finished products from the informal firms through out-sourcing, putting out and sub-contracting. In the process, the formal sector allows several formal and informal intermediaries to exist within the production chain.

The hierarchical structure in operation at the “Bottom” of the “Pyramid” starts with the Own account operators with “pure” or “open” market exchanges [Chen 2006] ^[1]. They appear in exchange of products, services and labour with the competitive formal sector. To do this, the formal sector forms networks with independent own account units, often informal ones. Some informal own account operators produce goods on their own within a Value chain in production. They operate through sub-contracting, putting-out and out-sourcing. The volume of such operations has simply increased after globalization. The terms and conditions of the transactions are controlled by the lead firms, mostly formal sector units. There are some informal Sub-sectors (even own account operators) who operate through domestic chains. In these domestic chains, producers directly collect production orders from the (formal) lead firm (s). Then there are informal Contractors /Intermediaries who collect production orders from the formal (even from informal) firms. They also produce without any direct competition with the formal sector over price. The informal Contractors out-source production orders to the informal sector producers. They simultaneously provide services to both the formal and informal sector. To provide

services, the Contractors form a network of formal-informal linkage. Such a linkage formation ensures work-orders from the informal sector and timely-delivery of finished and/or semi-finished products to the formal sector. The service becomes crucial particularly at the time of heavy work-load of the formal sector. The Formal Labour within the network operates in formal units with better work conditions and social security coverage. They collect work-orders for the informal sector operators. They also collect semi-finished products of the informal sector and deliver them to the formal sector^[1].

The presence of such a production chain in organizational structure conveys significant arrays in “relay” functions impeding multiplies effects to the small informal operators at the “Bottom” of the “Pyramid” in operation. The network connection in the form of linkage from the formal sector to the small informal operators in the production chain intensifies the situation of implementation of a single tax on goods and services a much complex phenomenon in the real world scenario.

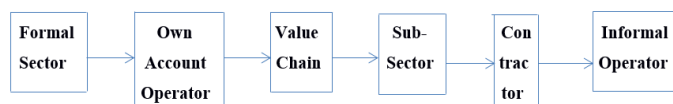


Fig 1: Hierarchical Structure of Operators.

Following the micro-level studies of 1970s, the linkages between the formal and informal sectors have become more complex due to the presence of the agents between the two sectors. The quantitative and qualitative methods in the structuralism approach has considered these as the “linkages as mechanism of institutional design”. For this, the labour market structures often shape (and re-shape) the nature and effect of linkages between formal and informal sector. Here, the labour market co-production appears from the “bottom of the pyramid” linked to social protection of labourers, hence challenge the voluntary entry model of the rational individualist approach. Here lies the theoretical debate between the alternative schools of thought regarding supporting or criticizing the event of application of any random shock like GST implementation to the existing production chain.

4. The Influences of Globalization: Changes in Production Relations

With Globalization and liberalization, the international value chain due to formal-informal linkages in production became a significant site to explore in the informal sector literature. These studies have considered the nature and effect of linkages as neither wholly beneficial nor wholly detrimental for growth of the economy that we have to keep in mind before commenting anything on GST. The two significant observations may be included here: first, the notion of a production continuum instead of two compartmentalized sectors of formal and informal, second is the prevalence of intermediaries taking active participation to link economic activities of the two sectors. With the acceptance of these two, the problematic of informal-formal linkage has become much more complex to understand, comment and explore. New empirical realities - such as globalization, market reforms,

growing prominence of the informal economy, and the crisis of the global (formal) economy - influence the relation between the formal and informal economies and their roles in economic growth of the developing nations in a complex way. Then the issue of GST places no one-way short-cut debate to be accepted or criticized.

It is this ‘complicated’ nature of the linkage between two ‘interlinked and subtle’ sectors of formal and informal in ‘Qualitative Mapping’ since globalization that has transformed the existing informal institutions to labour control to make them exploitative in contracting and forming tied-labour kind of relationships. Such a transformation has simply caused extensive implementation of sub-contracting, putting-out, out-sourcing and casualization of production orders with increasing volume of labour mobility^[2]. The existence of the ‘paradox of a relatively flexible labour market accompanied by a very large informal sector’ may be accrued to these linkages. In this, the labour movements between the formal and informal sector are not entirely determined by the regulatory incentives but by individual decision making in order to maximize income. This leads to a process of voluntary exit of the formal economy thereby segmentation and exploitation of the informal labour market. The implementation of a regulatory device like GST must include this ‘complicated’ informal institutional set up at proper in order to become a successful one – otherwise it may incur adverse influences to individual decision making thereby maximizing thrive of the informal economy and volume of the formal segment of the economy.

5. Informal Localization: The HME is in a Veil

What is crucial here is that many of the informal operators are operating in informal localization^[3]. It is worth to mention that the industry or business in one location within a cluster with repeated transactions among themselves promote better coordination, trust, and informal linkages between industries or businesses, better efficiency, effectiveness, flexibility, management linkages in partnerships and alliances, and many others. Any random shock like GST appears to incorporate a harsh negative influence to coordination, trust, and linkages. The influence becomes further intensified with Scitovskian “information spillover^[4]” due to “labour market pooling^[5]” in the informal production chains. It promotes further incentives to inter-firm knowledge spillovers thereby executing Marshall-Arrow-Romer (MAR) externality within the Marshallian “industrial district^[6]” context. The Jacobs and Porter externality suggest that the execution of knowledge externality by the producing firms simply become intensified in a competitive realm. A circular causation^[7] of all these provide maximum individual interaction in the informal industrial periphery from the ‘core’ with well-established social capital network^[8] through the functioning of the multiplier and “spread effects”. The result is a “relay” function through urban hierarchy at the peripheries from the “core”. All these have impeded a negative influence to reap the fruits of the implementation of GST with increasing volume of confusion and diffusion in the initial days of implementation of GST.

It is to refer that Becattini (1989, 1990)^[9] has raised the issue that government and/or government-sponsored institutions

like GST are not able to create an industrial organization with collective efficiency. Paul Krugman's (1991) New Growth Theory and Venable's (1996) New Economic Geography Synthesis opine that increased "labour market pooling" and knowledge externality inherit Home Market Effect (HME) that infer increasing confusion for the informal sector entrepreneurs. The reflection is accrued in reduced work-orders at the initial phase after implementation, thereby a reduced market growth, reflected in a further decrease in aggregate demand, hence growth of the economy. Any erratic implementation of GST may provide negative influences to growth at least at the initial phase. The policy makers have to consider the facet at proper. Further, the hierarchical structure in operation is charging higher product prices with multiple "spirals" at the receiving ends by the Informal Operators that is fetching short of the policy targets.

6. The Concluding Remarks

It is this hierarchical "**Bottom of the Pyramid**" structure of industrial organization after globalization that has changed the nature of Formal-Informal linkage paradigm. Out-sourcing, putting-out and sub-contracting are at an increasing pace – indicating "jobless growth" of the formal sector. The Indian economy is of no exception. All these are causing to a horizontal spread of informal localization in different industries and services in India in recent past. The policy makers have to capture this changing scenario at proper in order to make successful policy implementation like GST. Further, the things appear to be ambiguous further when a "grey" economy is confusingly treated as the "black" economy. A combination of all of these phenomena has hindered to grab the desired successes of the policy of GST implementation in recent past.

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1. Ref: King, 1974; Breman, 1976 Bose, 1978; Bienfield, 1975; Weeks, 1975; Breman, 1977; Papola, 1978; Tokman, 1978; and Peattie, 1980; John Harriss, 1990; S. V. Sethuraman, 1992; Breman, 1996; Levenson and Maloney, 1998; Ranis and Stewart 1999; Harriss-White and Gupta, 2001; Maloney, 2004; Kanbur and Guha-Khasnobis, 2006; Devey *et al.*, 2006; Marjit and Maity, 2006; Chen, 2006; Perry *et al.*, 2007; Pieters *et al.* 2010; Breman, 2010; Meagher, 2013.
2. Several researchers have shown, by using labour frontiers, that migration tends to decrease only at later stages of the development process of any region and the region is transmitted from net labour exporters to net labour importers Bohning, 1994; Rotte *et al.*, 1997; Olesen, 2002.
3. To examine the issue informality and its localization in any particular industry, the search for its literature support may be searched from the literature of Alfred Marshall 1890, 1892 in his industrial district concept with spatial concentration of small and medium enterprises - though the analysis of location started much before than Marshall with monocentric city model of Von Thunen Von Thunen's *Der Isolierte Staat in Beziehung auf Landschaft und Nationalökonomie*, 1826.
4. To Scitovsky. incorporation of imperfect competition initiates internal economies of scale that implies the existence of market power. Scitovsky distinguishes between pure technological and pecuniary external economies. The former affects firm's production function e.g. Marshallian information spillover, 1954.
5. To the revised version of the Central Place Theory of Walter Christaller by August Losch the spatial economy of the region then tend to be dominated by a central primal city, the hinterland of which owes to be characterized by smaller settlements and alternating areas of industrial concentration and dispersion. The Christaller model of central place is, however, inductive rather than deductive in the sense that the model is primarily based on observations rather than exploration of any schema constructed from first principles. To Parr 2002, the Loschian approach is completely deductive and a microeconomic foundation has been approached to understand the urban system. It shows that industrial concentration and urbanization may arise independently of local peculiarity and particularity, 1933, 1944, 1954.
6. The term 'agglomeration' of firms refers to decline in average costs in production as more production occurs within a specified geographic area Anas, Arnott and Small. In other words, it relies strongly on increasing returns to scale, considering internal and external economies of scale. Cluster of enterprises is a geographical concentration of micro, small, medium and large enterprises producing same or similar type of goods and services. As referred by Brulhart 1998, while concentration analyzes location across space of a few well-defined sectors, agglomeration analyzes location across space for a larger part of economic activity, and specialization deals with share of a particular location in specific industry in comparison to share of other locations in that industry, 1998.
7. In Gunnar Myrdal introduced the concept of circular or cumulative causation. In this, once a region or country takes lead in the process of economic development, positive external economies of scale in the region or country appears there - which ensures that the location will become an attractive place to invest and more attractive location for the labourers to work. The existence of strong localized spillovers leads to the establishment of a core in the region with large market and a periphery Dicken and Lloyd 1990-1957.
8. Social capital is social organizations such as trust, norms, reciprocity, co-ordination, interactions belongingness and networks between producers and workers that facilitate better co-ordinated actions among themselves.
9. In the Big Push theory Rosenstein-Rodan, the solution to the insufficient size of local market is referred to a co-ordinated government-led expansion of investment - hence big push enters into. This enables firms to reap the benefits of economies of scale effect, thereby promoting industrialization of a backward region. Without such a big push, the backward periphery cannot catch up with the core, 1943.
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