

The existence of the informal sector was recognized when massive additions to the labour force failed to show up in unemployment statistics. However, no need for a separate model has been considered, probably on the grounds that existing theory could explain this phenomenon. In terms of classical theory (of surplus labour), the urban informal sector contains that stock of surplus labour which makes the labour supply curve infinitely elastic at a constant subsistence wage and allows the modern sector to expand rapidly. The rapid expansion of the modern sector ultimately is supposed to absorb all the stock of human resources lying in the urban informal sector, after which there will be no informal sector and wages will start moving up from the subsistence level. However, the experience, over the last four decades, of several countries, including those which deliberately included this model in their development plans revealed that despite the accelerated growth of employment in the modern sector (much higher than the growth of the labour force), the size of the urban informal sector (as well as those seemingly employed in the rural/ agriculture sector at subsistence level) continued to increase.

In terms of the neo-classical model, those, in the urban informal sector, remain at a subsistence level, because, due to the risk of starvation, they do not want to use the new technology or improved methods of production.

The neo-classical model does not explain how to neutralize the fatal implications of risk bearing for such labour. It is this aspect that makes the profit-loss sharing based system more relevant in promoting human resource mobilization.

There are two points to be noted about the approach of the existing models to the informal sector. One point is that both models consider creating wage paid employment opportunities in the formal sector as a primary source of human resources mobilization. Those who cannot be accommodated in the formal sector are required to be comfortably absorbed in the informal sector as a second-best alternative. To assign a secondary importance to a sector, (which in some developing countries such as Pakistan, is as big as 70 per cent of the total urban labour force)⁽⁷⁾, is not a justified approach.

The other point is that neither of these models pays any attention to the role of the financial system which may be the key factor in the persistence or non-persistence of the urban informal sector. It has already been mentioned that the existing financial system in most developing countries exaggerates the impact of risk bearing for human resources without capital. These people are likely to be motivated to improve their

economic condition by utilizing better technology and improved means of production, if, in case they are unable to succeed in their enterprise, the following two elements are taken care of :

- (a) The capital lost in the process of utilizing it to improve technology and the means of production.
- (b) The subsistence of the family in order to save them from starvation, in case the new methods of production are not successful.

In other words, if some institutional arrangement can cover the loss of borrowed capital and can guarantee the subsistence survival of the family, then it may be sufficient to induce the individual to take steps to improve his productivity. Once he is made to pass through the critical situation, then it will give him a chance to build up some assets to meet any unfavourable situation later on without any external help.

3.5 KEYNESIAN MODEL

The Keynesian model, in fact, is a model that aims at human resource mobilization in a global context rather than explaining it in terms of a labour market phenomenon that is concerned only with those who report themselves to be in the market. The Keynesian model requires measures to increase effective demand in the economy, which in turn will induce productive activities in the economy and, hence, will mobilize human resources. As a response to increased effective demand, new large scale and small scale enterprises as well as self employed productive activities may be generated and a cycle of demand-output- employment may succeed in mobilizing the entire stock of human resources. Depending on the composition of the induced aggregate demand, those who are not willing to move may also find opportunities to have an activity of their own choice at the place of their own choice.

In this model, the financial system of an economy is simply required to inject the appropriate finances to stimulate effective demand. This can be supplemented by other fiscal and financial measures in order to synchronize the increased demand and the supply response. The efficiency of the loan market is particularly important for this model to adequately induce private investment and productive efforts to match the increased demand.

However, in our context, this approach is an indirect one in the sense that the measures suggested by it do not directly address the target population, which is the unemployed or unutilized stock of human resources. They are expected to mobilize themselves in response to the

increase in the aggregate effective demand. It is quite possible that the increase in demand may come in those sectors which may leave the unutilized and unemployed human resources unmoved⁽⁶⁾.

4. LESSONS DRAWN FROM THE ECONOMY THEORY

Our theoretical program of employment had little success in mobilizing human resources in developing countries, in general, and in Muslim countries, in particular. The review of existing theories presented in the previous section suggests that there is a need to develop an entirely new approach.

4.1 A SUGGESTED APPROACH

In the light of the various issues discussed in chapter 3, the following approach towards a program of human resources mobilization is suggested. The approach is intended not only to take care of the weaknesses of the model discussed earlier but also to realize the maximum potential of the Islamic financial system towards human resources mobilization as will be discussed in the next section.

The program of human resources mobilization should aim at the following two specific targets:

1. Mobilizing the idle human resources (those unemployed or those retained outside the labour force) to raise their economically

2. Mobilizing those who are already "employed" to enable them to improve their economic condition.

5. A human resources mobilization program should concentrate on creating self-employment opportunities for the target population. The creation of wage-paid job opportunities should be left to the formal sector, which should take care of itself. Alternatively, there may be a separate program for the promotion of the formal sector independent of the human resources mobilization program. This should bring at least the following outcomes:

Firstly, it directly aims at motivating and enabling the target population to create jobs for itself. Any program that aims at creating wage-paid jobs will have to motivate an employer to create job opportunities. The motivation and ability for the target population to respond to this demand will still be lacking unless already been addressed. Several factors may not permit the target population to respond to such demands. Motivating and enabling the target population to create jobs is supposed to minimize

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1. A program of human resources mobilization should aim at the following two specific targets:

- i) Mobilizing the idle human resources (those unemployed or those reported outside the labour force) to make them economically active; and
- ii) Mobilizing those who are already the so-called "employed" to enable them to improve their economic condition.

2. A human resources mobilization program should concentrate on creating self-employment opportunities for the target population. The creation of wage-paid job opportunities should be left to the formal sector, which should take care of itself. Alternatively, there may be a separate program for the promotion of the formal sector independent of the human resource mobilization program. This should bring at least the following outcomes.

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these factors and, hence, increase the probability of success.

Secondly, the choice of a self-employment opportunity gives those human resources (who make the choice) more opportunities to improve their economic conditions compared to those who choose to be wage-paid employees. This is because:

- a) a self-employed person is in a position to make decision to expand his enterprise and, hence, his income earning capacity if opportunities exist. A wage-paid employee lacks this decision making power.
- b) a self-employed person has more motivation and incentive to save as he has an opportunity to use his savings to expand his business and further improve his economic status. This tendency is very likely to have a snowballing effect enabling him to accumulate more and more capital as the expansion of his business increases the capacity to save which gives him further motivation to expand his business. Such effects are lacking in a wage-paid job, as the individual can utilize his savings only by giving them to some one else, institution or individual, who may give him only marginal returns.
- c) a self-employed person has the opportunity and the option of utilizing the maximum time available to him. This opportunity and option may not be available to the wage-paid worker because he has no control over the amount of or the wages paid for overtime work.
- d) a self-employed person has the option and the opportunity to utilize two aspects of his human capital; the ability to do labour and the ability to make decisions and to bear the risks associated with these decisions. Both are productive abilities. But in a wage-paid job, the worker can benefit only from the former ability which is very limited and, hence, puts a limit on his capacity to improve his economic situation.
- e) a self-employed or family operated enterprise is the only source of mobilizing most of the women of working age in Muslim countries at least for any short- or medium-term planning purposes.

Therefore, the suggested model requires that a human resources mobilization program aim at creating self-employment opportunities in such a way that the above- mentioned advantages of such opportunities are fully exploited.

3. The urban informal sector and the rural sector are required to be accorded primary importance in the program even if this means that the support to the formal sector to create employment opportunities be given a low priority. This priority is required for the following reasons:

- a) The self-employment sector is obviously a highly labour intensive and extremely low capital intensive sector. Small investments can mobilize more human resources to enter into economic activity in the rural sector and urban informal sector than it will do in a formal urban sector.
- b) The formal urban sector is in a better position to take care of itself than the informal and rural sectors. It is the informal and rural sectors that are more in need of a push.
- c) The promotion of the formal sector may help to mobilize only those human resources who are willing to work in the sector. There is evidence from some Muslim countries that a large part of the rural population as well as a substantial part of the urban population (particularly females) may not be willing to do so. A program to promote self-employment in the urban informal sector and the rural sector has a wider scope in view of the fact that in several developing economies about 80 per cent of the population of working age belongs to these two sectors.
- d) Income raising opportunities in the rural and urban informal sectors reduce the pressure on individuals to migrate to urban areas where they remain unemployed or live on subsistence earnings in the hope of getting a wage- paid job in the formal sector. Focussing self-employment programs on the rural sector and on the urban informal sector will have a direct impact on reducing urban open unemployment, a serious issue in most contemporary developing economies.
- e) The promotion of self-employment or very small enterprises in the rural and informal urban sectors will provide competition to the formal sector with respect to the hiring of labour. As soon as the average family income starts rising in the rural and urban informal sectors, the supply side reservation wage for employment in the urban formal sector will rise, because the formal sector draws labour from these two sectors. There will be pressure on the formal sector to raise wages (otherwise labour would prefer to go to the informal sector for self-employment jobs). Involvement in entrepreneurial self-employed jobs helps build up human capital which in turn will help labour to sustain the increase in the minimum

reservation wage for seeking employment in the formal sector. This competition will raise human resources mobilization along with an increase in wages in the formal sector and family incomes in the rural and informal urban sectors.

4. As self-employment opportunities are substantially promoted in the economy, there will be a need for a simultaneous follow-up program to be supplemented by the following:

- i) Identifying those successful self-employing enterprises which have potential for further growth and helping them to grow into small enterprises employing labour from outside on a wage basis.
- ii) Enabling these small enterprises to integrate into the formal sectors, if they continue to show potential for growth.

The above approach should not be taken as a strategy of perpetuating backwardness, as was the criticism of Fritz Schumascher when he suggested a similar strategy under the title "*Small is Beautiful*". The approach in this paper is not that of small is beautiful and, therefore, that only small should matter. The approach is to recognize that *Small is Important* because it potentially involves about 90 per cent of the population in most developing countries and, hence, the *small* should be given due attention, while promoting the large for the purpose of industrialization and technical progress. Secondly, and more importantly, the strategy of giving more attention to the *small* emerges from the fact that the Islamic financial system (to be discussed in the next chapter) already has a built-in mechanism to motivate and support the *small*. This potential should be exploited to benefit the *small*. Thirdly, it will be discussed later that the amount of investment required to mobilize substantial amounts of human resources under the above approach is so small that a medium-term plan adequately phased to implement the above approach should not substantially affect any existing programs for industrialization and technological progress. A proper integration of the small sector with the medium and large scale technology will, in fact, accelerate the industrialization and technological progress.

The approach suggested above, in short, boils down to the following:

Motivate and enable all such human resources that are either not working and contributing anything to family income or that are earning (or are living on) an income less than that of market wage of comparable skills to take up self-employing economic activity that can ensure at least an income equal to the formal market wage. As these self-employed human

resources gain experience and expertise, motivate and enable them to increase the size of their enterprise to employ more non-family members. As self-employment activities grow into small enterprises, efforts are made to enable them to integrate with the formal sector so that they ultimately are recognized as a part of the formal sector and are no longer a part of the informal sector.

In the three stages identified above, the first stage is the primary and essential step in human resources mobilization. The remaining two stages are meant simply (a) to reinforce the primary stage in order to accelerate the speed of human resources mobilization; (b) to help them move from informal sector self-employment to a formal sector production firm and, hence, be self sustaining in income and economic status and (c) to make the human resources mobilization program an engine of growth in the economy as well.

The last two stages, however, are not the direct subject of this paper. It will simply be the extension of the policies applied in the first stage. This paper concentrates only on the first stage.

The motivation and ability of the economically inactive or less active stocks of human resources to take up self-employment jobs depends essentially on the following factors:

- a) Ability to produce some goods and services in demand locally.
- b) Ability to market the goods.
- c) Access to required capital at the right price (or the correction of the financial system as already mentioned).

The target population we are concerned with in developing countries, by definition, does not have the education or training for substantial production skills. Yet, it should also be recognized that we are not talking of a productive activity requiring any substantial skills to start with. There may be numerous activities for self-employment which do not require substantial skills. Whatever skills they require can be informally acquired locally with little time and money. We are talking about activities like vending, tailoring, shoemaking, carpentry, iron-mongery, running a small eating place, running low cost public transport (which, in rural areas, may even be animal driven) and so on. The ability to do these things can be acquired at one's own initiative with very little cost, which, in most cases, can be afforded even by people of the lowest means, provided there is sufficient motivation to do so. This will, hence, not be a major area of intervention at least as far as the first stage of the scheme concerned.

The same is true for the ability to market the goods. Again, in the first stage, we are talking about the production of goods and services in local demand. Clothing, shoes, textiles, low cost household utensils and pottery, low cost household furniture, groceries, food products and services, etc. are only some examples. The goods, being a part of the bare minimum needs of the local population and, hence, essential are not likely to face a marketing problem. The household's income generated from the production of these locally demanded goods and services will also reinforce the demand for local products. Hence, in the first stage, as far as the model is concerned, even marketing is not assumed to be a major area of intervention. The major area of intervention would be the financial system to ensure adequate access to capital requirements at the right price.

4.2 CORRECTIONS IN THE FINANCIAL SYSTEM

This is an area requiring substantial intervention. The target population we are talking about obviously lacks any amount of capital, however small it may be, to initiate small self employing productive activities. Also, the poor possess latent skills which, when complemented by adequate capital, can be harnessed for more remunerative self-employment. It is important that financing programs for the poor should be appropriately designed, implemented and managed in a way that fits the circumstances in which the poor find themselves. There are, of course, two dimensions of intervention in this area. One relates to generating the supply of required capital and the other to creating demand for available capital.

4.2.1 Supply of Required Capital

Supply of capital required by the target population is constrained by two factors. Firstly, the target population is devoid of any collateral to guarantee the principal amount and a return on it. Secondly, doubts about the capabilities of the target population to produce and market the goods and, hence, make substantial profits to repay the capital with return make the investment a risky proposition. This sector will, therefore, fail to attract a substantial amount of funds to ensure supply of capital for meeting the needs of the sector as long as there are opportunities for earning a risk-free and guaranteed return on capital. As long as some sectors of the economy continue to guarantee a fixed return on capital, some special fund will have to be created to ensure a substantial supply of capital to finance the productive efforts of the self-employed activities of the first stage. This fund will have two prominent features. Firstly, it will supply capital to the target population with no physical collateral. If the target population fails

to offer any personal guarantee, that too may be waived, in some cases, it should suffice if the potential client can provide a trustworthy reputation of good character. Secondly, it will be willing to expect no income for some time, until the self employing activities start generating sufficient income to pay some return on the capital. The capital will also be willing to bear a partial or total loss in case the self-employed activities fail to take off in a reasonable period of time.

4.2.2 Demand for Required Capital

The existence of a need for capital requirement for financing activities to improve household incomes and productivity through self-employed activities may not be sufficient unless that need is not translated into an effective demand for capital. The constraining factor is the same as already discussed by the conventional economic theory in the context of explaining the lack of motivation to adopt new technology. As has been mentioned earlier, human resources living at the subsistence level in the rural and urban informal sector do not readily accept innovative methods of production because the risk is too great. The risk is of starvation if the new methods fail to produce results. It is this same risk that prevents idle human resources from engaging in entrepreneurial or self-employment activities.

Although idle human resources are already subsisting on someone else's income, the risk is that entrepreneurial or self employment activity will require capital that will have to be borrowed and in the event of failure, the income of the rest of the family will be at stake, which may then lead to starvation.

This bottleneck requires at least three elements to be resolved :

- i) The burden of bearing a loss by human resources should be made negligible at least in the short-term.
- ii) There should be a system of social security that would take care of the subsistence of the entrepreneur and his family during the lean periods of his enterprise.
- iii) The (factor) price in the market should be set right so as to provide the necessary incentive to idle human resources to opt for an entrepreneurial activity rather than to wait for a fixed wage-paying job.

In short, there are two areas of intervention:

- a) Guarantee of minimum needs of the population through some formal system of social security