KERALA ECONOMY
2020, VOL.1, NO. 3 pp 10-13.

ISSN : 2583-4436 MY

Labour law exemptions : Will the bitter pill heal?

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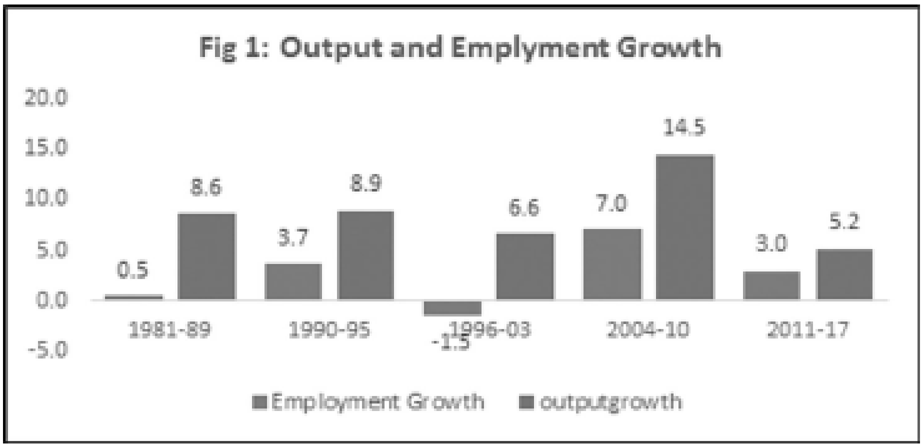
The nationwide lockdown to contain the COVID-19 pandemic brought economic activity to a standstill destroying the livelihood of millions of people. As per Centre for Monitoring Indian Economy (CMIE), nearly 122 million people have lost jobs in April 2020 itself. At a time when the economy is grappling with loss of jobs, Uttar Pradesh government passed an ordinance in support of labour compliance holiday for three years. Soon, other states joined the bandwagon to exempt industries from several labour laws for various lengths of time. Apart from provisions in the Industrial Disputes Act 1948 (IDA) which has been the backbone of workers' protection in industries in India, exemptions were also granted from the Factories Act, the Payment of Minimum Wages Act and the Contract Labour Act 1970 (CLA). State governments justified that these exemptions would attract investment, facilitate employment creation and thus help India battle COVID-19 induced economic crisis. However, such an argument is contentious as there is no strong empirical evidence to validate that doing away with labour laws enable employment creation. According to the data from Annual Survey of Industries (ASI), exemption of labour laws would increase contract labour, decrease wage rates and make workers more vulnerable.

Output and employment trends in India's manufacturing

The issue of employment generation in India's organized manufacturing has received considerable attention. Long term analysis of the trends reveals five distinct phases of output and employment growth. The first phase corresponds to the decade of 1980s where there was hardly any employment growth despite high output growth followed by a revival in employment growth during 1990-95 (Figure 1). Employment growth was negative (-1.5 percent) during 1996-2003 though output growth was 6.6 percent. This phenomenon of absolutely no growth in employment despite high output growth for about 25 years was termed as 'jobless growth' (Kannan and Raveendran, 2009). After a long stagnation for a quarter century, employment growth picked up (7 %) along with high output growth. The last phase (2011-17), however,depicts a steep fall in output growth along with employment growth (Figure 1). The growth rates further deteriorated from 2017 onwards and the outbreak of COVID-19 made it worse.



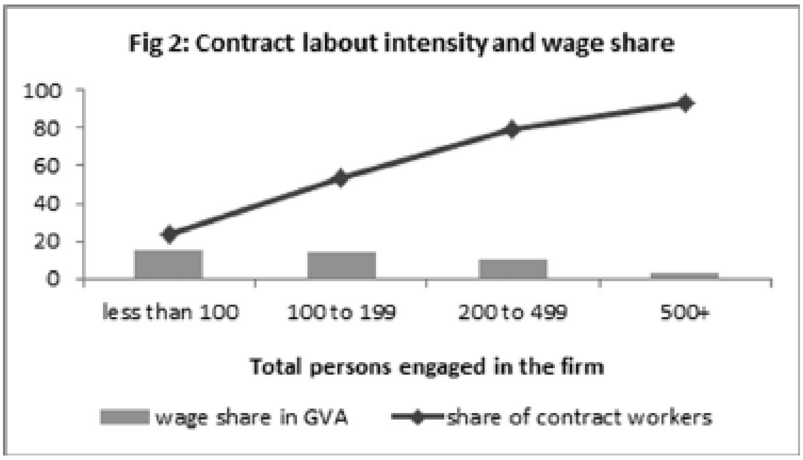
Source: Annual Survey of Industries, Various years

Who creates employment?

The proponents of flexible labour market often argue that exemption of labour laws would attract more investment and employment. This argument is based only on the cost dimension of wages and not the demand dimension arising out of its role of providing income to the workers. Labour regulations in India are applicable to firms above a threshold size and induce firms to stay below the threshold. Since the 1982 amendment, the Industrial Disputes Act [IDA] was applicable to industries which employed more than 100 permanent workers. Since certain provisions of this law prevent firms from indiscriminate hiring and firing, the state governments are justifying the exemptions from these provisions on the ground that "flexible" labour laws would lead to employment creation. However, a comparison of employment generation between firms where the IDA is applicable and those where it is not, shows that the IDA has not restricted employment creation in Indian industries. Data from the Annual Survey of Industries shows that although IDA is applicable to only 7 percent of firms in the organised manufacturing sector, they contributed to as much as 53 percent of new employment created in this sector between 2000-01 and 2014-15.They also accounted for 65 percent of all direct employment (permanent workers) created in this period, thereby affirming that firms where IDA is applicable contribute much more to employment creation both in terms of quantity and quality, compared to firms which are outside its purview. Instead of granting exemptions, employment generation might benefit if more firms are brought under the IDA. Further, firms employing 50-99 workers deliberately stay below 100 by employing more contract workers compared to other firms which are under IDA (Ramaswamy, 2013). Therefore, deregulation of labour laws would allow firms to hire more contract workers at lower wages.

Quality of employment and workers' wage share

Due to the weak implementation of the Contract Labour Act [CLA] which aims to restrict and minimize the use of contract labour, many firms have been bypassing the IDA by indiscriminate use of contract workers. In 2014-15, 16 percent of the largest firms with more than 500 employees bypassed the IDA by using 94 percent of contract workers in their workforce. The result was workers' wage share hitting the rock bottom of 3 percent of Gross Value Added (GVA) in these firms. Despite this, many states had already amended the IDA to increase the threshold level for its applicability from 100 to 300 permanent workers by first quarter of 2020 even before the lockdown was imposed. Now as the industrialists are given a free hand in the use of labour with the current exemptions, this would further escalate the use of contract labour in the industries. Since on an average contract worker earn half as much as direct workers, this could reduce workers' wage share in GVA.



Source: Authors' own calculation based on ASI unit level data

As such, most of the Indian states have been witnessing falling share of labour in income and output even before these exemptions were introduced. Among the top fifteen states in the organised industrial sector in terms of net income, in all except Tripura share of workers' wages in net income declined between 2000-01 and 2017-18. For the country, it declined from 18 to 30 percent reflecting the weakening bargaining power of workers. The share of wages in net income declined from 37 to 25 percent during the same period but it is higher than the national average and many other states like Gujarat and Maharashtra. While doing away with minimum wages would only worsen the labour bargaining power, increasing daily and weekly working hours would prevent firms from hiring more workers at a time when unemployment is already at a historic high.

Wrong medicine for the ailing economy

When the Indian economy was already slowing down, the severe demand crisis due to loss of jobs and income induced by the lockdown has deepened the crisis. Data clearly suggests deregulation of labor laws is no solution. Instead, it could make workers more vulnerable, let alone creation of more employment opportunities. The competition between states to dilute labour laws and give absolute power to firms to squeeze wages and disincentivise employment creation would only add to the demand crisis and prove to be perilous in the current context. The right medicine now includes injecting demand in the economy by increasing the purchasing power of people at the lower end of the income distribution who spend most of their earnings on consumption. While direct cash transfers in the hands of the poor is needed to provide immediate relief, creating decent employment opportunities is the only way to sustain this in the medium and long run.

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