

LABOUR MARKET REFORMS IN INDIA: DEBATE OF FLEXIBILITY IN LABOUR MARKET

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Abstract

The debate around labour market flexibility has received a lot of attention in recent years. It is argued that rigidity in the labour market affects economic growth and, perhaps, is the reason for unemployment. It is argued that due to strict labour laws which results in inflexibility of labour market growth is hampered and flexibility will bring more growth and jobs to the economy. On the other hand, criticisms against pro flexibility view, labour market flexibility has no significant effect on output and employment creation but, instead, results in redistribution of income in favour of capitalist class. Moreover, critics point out that contract labour and casualisation of work have become ways in which employment is created in India, leading to redistribution of income from workers to employers. This paper discusses types of flexibilities in section 1 and flexibility debate in section 2. Then there is discussion of labour laws in section 3 and problems associated with them. In section 4 there is discussion of trends which show that there is a steady decline in organised sector regular employment while informal workforce in organised sector is on increase, clearly pointing to the phenomenon of informalisation of organised sector. Interestingly, across almost all Indian states there is an increase in employment through contractual arrangements in Indian factory sector, indicating increased flexibility in the Indian labour market. All these sections are linked together in conclusion to offer policy options regarding labour market reforms and their relevance in Indian context.

1. Understanding labour market flexibility

Firms' ability to make changes to their workforce in terms of the number of employees they hire and the number of hours worked by the employees. When markets are globalized and competition is drawn from domestic as well as foreign goods and services and if prices prevailing internationally are less than what in domestic market then to bring down input cost to competitive levels employers demand labour market flexibility.

Following are the types of labour market flexibility practiced at the firm:

1. Organizational flexibility: turnover of firm/worker increased during liberalization times and there was more use of subcontract regime when integrated to global network. As demand is externally decided so there is demand of organizational flexibility to create sub contract arrangements.
2. Numerical Flexibility: Here the number of workers is adjusted in accordance to the market demand and technological innovations. This flexibility helps the entrepreneur to hire and fire the workers as per his skill requirement. The employers in this case generally prefer hiring

through contractual basis or on temporary basis so that when need be the workers could be easily sacked.

3. **Functional Flexibility:** Here the workforce is reorganised at varying level by the firm due to technological changes. The methods like job rotation, multi-skilling, retraining and internal mobility, are used for practicing this flexibility. This flexibility helps the entrepreneur in running the firm with the already available worker and thereby helping in cost reduction.
4. **Wage flexibility:** Here the wages are adjusted in accordance to the changing cost competitiveness and product demand in the market. Under this regulations like the minimum wages are seen as the interruption to this form of flexibility. In this flexibility the labour would be given a full authority on wages setting and the labour unions and the organisation in-return would not have any power in deciding wages setting. This flexibility claims to help the adjustment needed in the market clearance.
5. **Working time (or temporal) flexibility:** This involves adjusting and utilising the labour hours according to the demand of product and its seasonal variation. This flexibility helps the firm in assuming practices such as overtime work, part time work, shift work and weekly or annual arrangement of work without actual change in the number of employed work force.(Murthy,)

Of the above, the flexibility used the most are Working time, wage and functional flexibility which sets up the workers either in and out of the firm or across different functions within the firm. Other than the above flexibility, firms also practice spatial or geographical flexibility. This flexibility replaces the semi-skilled homogenous workers class with the socially and geographically dispersed working class. In such a framework what we observe smaller workplace, weaker unions and wages being tied to business cycles.

There are two aspects of regulations as given by Freeman in 1993. These are “institutionalist” and “distortionist”. The institutionalist emphasises that the labour regulations need to by-pass all the ‘weakness’ of employees like weak bargaining power, insufficient insurance against unemployment risk, and enhancement of investments in human capital, consequently productivity growth. They say that if there are no labour laws then no protection for vulnerable section of society while facing problems. Until and unless there are protection of wages, effective demand of economy will get reduced and hamper production process.(goldar and Jha)

In contradiction to above view the distortionist holds that when there are institutions it leads to wages greater than marginal productivity. It hold institutions as obstacles towards dynamic setting as then labour becomes fixed investment and labour start demanding rent which leads to no rise in productivity. Distortionists argue that the strict Employment Protection Legislation (EPL) favours regular workers, thereby increase dualism of labour market, increasing effective labour costs, discourages hiring and impedes adjustment to economic shocks. Thus, in the way of avoiding adverse labour outcomes, there need to be the exchange between employment security and labour market flexibility (Eamets&Masso, 2004). According to them even unemployment happens because of these agencies, as by protecting the right of insiders hurt the chance of outsiders entering the market (Sharma, 2006). But the other economists counter this by saying that as long as an entrepreneur can make profits by lowering wages and making workers work in bad condition, it won't have any motivation to improve its productivity. Only

when there is a floor of labour standards, the firm will go for technological and organisational motivation which will lead to better wages and working condition (Sharma, 2006). Even according to the study by ILO, countries with strong trade unions also do equally well in world market.

On this note let's shift our focus towards labour market flexibility debate.

2. Flexibility: Debate and empirical evidences

Labour market flexibility has been a very actively debated topic in the recent years. The supporters of flexibility feel that removal of all the restrictions placed by different laws is the best for the economy which can further lead to full-employment. They believe such an economy will make room for a more efficient production system. Whereas the opposition of the labour market flexibility finds it to be the tool for cost reduction by foregoing essential labour rights and decent work practices. Firms for keeping pace with flexibility practice the popular strategies like outsourcing, conversion of formal work into informal work, etc. The result of this is the pool of workers who don't have access to their rights.

Whereas others say that these rights have averted the employers from adjusting to the economic fluctuations. The prevention of laying off in recession stops the employers from hiring on the upturns, thereby contributing to unemployment (Eamets&Masso, 2004).

Economists have been long arguing for labour market flexibility from quite a long time. 'Flexibility of labour' got recognition with the Washington consensus which was further based on, as Stiglitz called, market fundamentalism. The idea behind it was that the free market outcomes are free and Pareto optimal. There even is the impression that regulations on market lead to distancing from full employment of resources and optimal social welfare (Sharma, 2006).

A study by Basu(2006) argued that Labour market in India is indeed rigid and can lead to undesirable consequences. He lay that Indian labour laws have actually harmed the workers rather than helping them. Basu's argument has been criticised because of the underlying assumption of model and link between wage rate and level of employment was wrongly interpreted in this model (GOLDAN AND JHA).

One of the popular studies in favour of labour market flexibility was carried out by Falon and Lucas(1993) who measured impact of amendments of industrial dispute act and labour market regulations in India. They assessed the period between 1976-1982. Their conclusions were that extreme job security regulations in India are significantly reducing demand for workers at different levels and regulations were restrictive which inversely affect employment. Another conclusion was that India with more public enterprises were less affected in terms of decline in demand for labour because of presence of trade Unions. This study was heavily criticised by Dhalotra who explained that at same period there was tightening in labour market and if that happens how the demand had declined. Also the amendments led to increase in employment in factories employing 100-1000 workers whose explanation was missing in reading by Falon and Lucas. Bhattacharya() also criticised their reading by arguing that period chosen i.e. 1976-84 has specific historic context relating to emergency at that moment so results cannot be trusted as employees got a free hand to retrenchment which is reflected in decrease in demand in employment and therefore cannot be explained with rigid labour laws.(Guha)

One of the most publicised empirical study relevant to the flexibility debate is a study by Besley and Burgess(2004) which was one of the first paper that argued labour market flexibility

is required in India. They tried to investigate whether industrial relations climate in the Indian States have affected the pattern of manufacturing growth as well as employment in the period 1958-1992. They quantified amendments of Industrial Dispute Act and categorized them for the states as following: (a) If amendment pro worker- +1 to the state (b) if amendment pro employer- -1 to the state (c) If the amendment indifferent towards both- 0 to the state. Main conclusions of the study were: Pro-worker legislations had contributed to the lowering of investment and employment in the organized manufacturing sector and also facilitated the existence and growth of a very large informal sector. The net impact has been in terms of deterring productivity and constraining growth as well as poverty alleviation. It was claimed that the distributional effects appear to have worked against the poor and the analysis claimed to reinforce the growing sentiment that there may be large gains from legislative changes that make the IDA more employer-friendly (Goldar and Jha). This study was heavily criticised by Bhattacharya() who asserted that “classifying a state as pro-worker or pro-employer on the basis of a single amendment while all other central or state laws remain unchanged can be quite misleading”. A puzzling feature of Besley-Burgess results is that pro-worker legislative amendments did not show any clear indication to raise workers’ wages. To measure rigidities in labour market, as Besley and Burgess have done, directly from legal statutes could be misleading, as the translation of laws into outcomes is often through a complex intermediation process. Also same magnitude was given to all regulations and out of 113 amendments only 19 were taken as source of change. Labour law amended as pro labour cannot be withheld as only reason for decline in industries as there are other reasons as political disturbances, specific year, human capital etc. Due to space constraint all criticisms cannot be listed but a conclusion based on this study would be misleading.

Advocates of labour market flexibility often claim that there is an inverse relation between real wage and employment expansion. However, in a recent study, it has been shown that there is no systematic evidence of such a relationship between wage levels and employment in India’s manufacturing industry across the range of manufacturing sub-sector well as the sector as a whole (Ghosh, 2004). Dutta Roy (1998) argued in a study based on ASI data for the period 1960–61 to 1993–94 that job security regulations have not been responsible for the slow-down in employment growth. Three primary survey based studies on labour flexibility in India by Sudha Deshpande et al (1998), Sharma and Sasikumar (1996) and Lalit Deshpande (2004) have not been able to find any evidence that support the hypothesis that firms that have employees more than hundred face greater hurdles in laying off workers when compared to firms that employ less than hundred workers.

Papola (1994) found that increases in real wages were generally accompanied by a still higher increase in productivity across industry groups, resulting in lower unit cost across industry groups. Nagaraj (1993) disputes the extent of increase in real wages, as according to him, the increase in annual earnings was primarily accounted for by the increase in the number of person-days per worker during the year, and only to a small extent by the increase in earnings per day. Increase in union power to raise wages should have led to a rise in strikes. But there has been a decline in the incidence of strikes since the early 1990s and now lockouts account for a lion’s share in the total workdays lost [Datt 2003]. Atulan Guha() found no statistically significant dependence of employment and output growth on labour market flexibilities in Indian organized manufacturing sectors. The study notes that with increase in demand from both

domestic and global markets for capital intensive products, there is an increase in capital intensity in Indian manufacturing.

So in all after studying both aspects one can argue that India's industrial landscape certainly does not support claim of distortionists. Also this leads us to 2 further questions that is Indian labour laws actually making market rigid? Is Indian industrial market actually rigid? Lets find answers to these 2 questions.

3. Labour Laws in India

India has close to 50 central laws and around 175 state laws which have something to do directly with labour. But as said by Goldar and Jha "many of them are poorly designed and have massive confusions relating to matters of jurisdiction. There is a strong call from India's strongest and influential quarters for the need of the labour reforms in India. The argument provided for the reforms is that many of the labour laws are quite irrelevant and do not reflect the current requirements and needs of the Industry. Main argument of pro flexibilization theorists is reforms in Industrial Dispute Act relating to chapter V A.

3.1 Rise of Informal sector in India: Contractual labour and Market becoming flexible

One of the key features of this informal sector is its flexibility of labour. In fact informal and formal sector can be differentiated by the flexibility in it. It is this 'flexibility' because of which that we observe many workers changing different jobs quite frequently without any job security or social benefits. This gives the organisation the privilege of getting access to and getting rid of the workers whenever they want, thereby saving them from the slightest of liability towards its workers. This flexibility of workforce is from the perspective of the employer. The employers are the ones who want greater flexibility in their production process and employment system, and are the ultimate gainer from it. This is done so as to adapt to the environment of rapid technology development, diversified labour markets, growth in international and price competition in product markets, and restructuring of corporate financial in capital markets (Kallerberg, 2003).

Organisations save their labour cost by using temporary or part-time workers and have greater profits. They even practice outsourcing 'non-essential' activities thereby concentrating their 'own' labourers on the core things. But this leads to job insecurity among workforce which eventually creates a division as the workforce feel segmented within the core and periphery components, insiders and outsiders. This segmentation of the workforce into fixed and variable components are assumed to bring cost effectiveness. The core labour force is protected from the fluctuating demands with the help of the numerically flexible, nonstandard, peripheral workers. (Kallerberg, 2003).

In India there has been drastic increase in the unorganized component in the labour force employed in different sectors. In the agricultural sector the share of unorganized workers accounts for 97.6 percent of the total workers, out of which 64.8 per cent are self-employed and 34.6 per cent are casual workers. In the non-agricultural segment, unorganized workers account for 71.6 per cent of the total work force.(Roy,)

From the period 1995 to 2002, there is an increase in contractual employment proportion across states except Assam. Taking signs from the primary data on employment taken in 2008 it seems that temporary employment is gaining popularity within firms. Around 2/3rd firms in

manufacturing sector has 21-50% of the temporary staff in their workforce. There is a significant rise in the share of unorganized employment in almost all the sectors in non-agriculture and the organized segment of the non-agriculture is also undergoing a process of casualisation and contractualisation of the labour process.

Throughout the manufacturing sector, except Other Transport Equipments, Other Non-metallic Mineral products and Furniture and Other Manufacturing sectors, increase in proportion of employees and workers employed through contractual arrangements was observed. All over India, the workers hired proportion went up from 13% to 20%. It was even observed that Indian organised manufacturing sector was more and more going for contract employment. It was realised that the legislation which allowed the firms having more than 100 workers to lay off have resulted in reduction of permanent employees and adoption of contractual arrangements for production. Thus there would be increase in jobs without any security and with bad working conditions.

4. Labour Laws Flouted

Many empirical findings indicate that flexibility and inflexibility in India did not depend on India's legal structure (Roy,). Since 1980's there has been a steady decline in strikes and since 1980's ratio of days lost because of strikes was lower than days lost because of lock ups.

1. Workers can benefit from labour laws only when he is employed for 240 day consecutively but employer employs him for 239 days , then give him a break of 2 days and then employs him again under new contract. Due to this process employee does not come under industrial dispute act.

2. Strikes- Employer at time of strike bribes adjudicator and because of having higher bargaining power in Indian society is able to declare strikes illegal to avoid 15 days wage and helpless labours have to succumb to employer and restrict their strike as they cannot sustain strike for longer periods. As after 60 days employer has right to retrench worker.

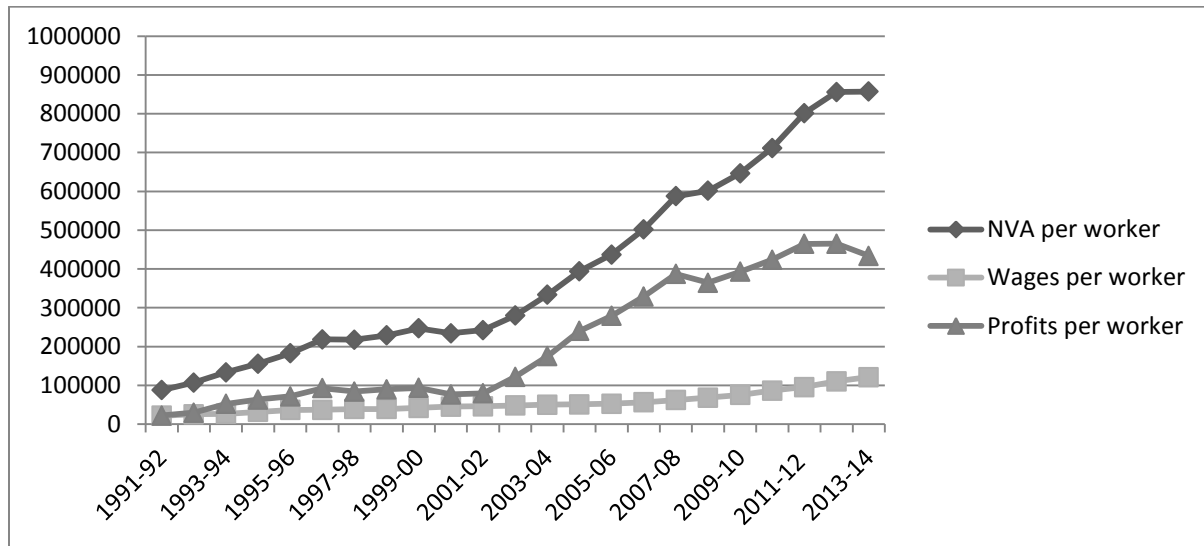
3. Due to nominal fines imposed when an employer is found not abiding by law so employer finds exploiting law more profitable than abiding it.

4. Contract and casual labours: As already seen in the earlier section that contract labour is on a rise in all over India and main reason behind that is that informal labour is beyond purview of Industrial Dispute Act and labour market becomes flexible.

5. Voluntary Retirement Schemes: Different schemes are introduced like this to reduce number workers where workers are offered money and forcefully made to leave job.

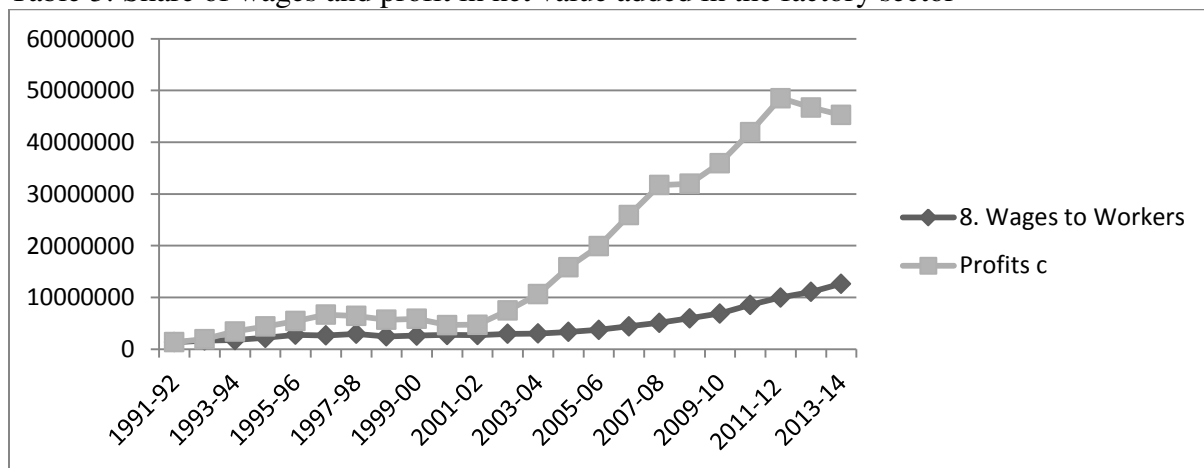
Because of the reasons cited in the above two sections we can very well say Flexibility and Inflexibility in India did not depend on legal structure of India. As employer has higher bargaining power over the worker he is outrightly able to take away all the share of surplus produced and worker is not able to accumulate capital as is evident from given 2 tables:

TABLE 2 : Annual Average Wage and Net Value Added Per Worker in the Factory Sector.



Source: Computed from ASI data summary results, several years

Table 3: Share of wages and profit in net value added in the factory sector



Source: Computed from ASI data summary results, several years

Table 2 shows the increase in gap between wages and labour productivity in the factory sector. So as already seen from 1980's there is rise in hiring of contractual labour. All the value produced by worker is going in hands of employer. And by working in inflexible market without laws there is no rise in wages of workers.

Same fact can be further substantiated with table 8 which shows that wages/NVA are declining from 1980's and Profits of capitalist class are on a rise. It reflects the freedom already enjoyed by the capitalists in our country in squeezing the claims of the labouring class. (Roy,2008)

5. Conclusion

To summarize all the arguments listed above we can very well say that instead of debating on whether labour laws are effective or not main issue put forward should be to see how employer is able to flout labour laws and make market so flexible. All these trends together indicate that even if there is a substantial growth in manufacturing output, workers are not benefiting. The capitalist

class is reaping the whole benefits of the output growth. This is being done through the combination of adopting capital-intensive technologies and greater labour market flexibilities. Therefore, greater labour market flexibilities have no influence on output, employment growth, apart from making a redistribution of income in favour of capitalist class. Those who argue in favour of labour market flexibility try to pitch the whole debate in terms of micro-efficiency and ignore the consequences at the macro-level. The review of literature suggests that the evidence about the link between labour protection and employment is weak. We feel that the demand for more reforms to flexibilize Indian labour market further lacks adequate factual support as the Indian labour market is already rendered flexible due to presence of vast informal sector, informalisation of formal sector and lack of strict application of the already existing labour protection laws. Capitalists argue for flexibility just so that they can increase their share of profit in market legally which they are doing right now illegally and main demand for flexibility from capitalist classes come to undermine change and control production process. So as in the words of Roy() “in order to create more employment capital should enjoy the privilege to throw people out of job!”

This too much of flexibility not only harms the workers but also the employers as they lose industrially accumulated useful skills. The philosophy of social and labour policy of India believes that labour should not to be merely treated as resource of development but as a partner in and beneficiary of social and economic development. This had its roots in national movements. This is one of the reasons why it's difficult to get rid of all rules in the countries like India (Sharma, 2006). There is one more aspect associated with flexibility that all flexibilities are not detrimental towards growth. Functional flexibility can actually benefit both employer by increase in productivity and employee by increasing his skills.

There is apparently need of the cautious balanced approach towards the market flexibility. It need to be understood that too much of flexibility may be as bad as too much of rigidity. The main challenge before the Indian industrial relation system is to find a way in which the system is the combination of both the efficiency of the enterprise and the interests of the workers (Sharma, 2006).

The need of the hour is the emphasis on how the implementation of labours could possibly be improved. Over 13626 cases are currently pending in the central tribunal (Source: Business Line). Steps to make the grievance redressal process more effective and simultaneously more efficient so that the labours get the maximum possible benefit of its purpose. Most importantly, ways to improve collective bargaining and ways to improve solving disputes. Holding LokAdalats should also be encouraged to enable faster disposal of cases. A database should be built on all aspects relating to industrial relations and the officers of the Labour Departments should have access to such database through computer connectivity. Codification and simplification of Labour Laws it is also suggested for creating online single window system for making compliance as user friendly, simple and for bringing transparency. Employers can seek the registration, license etc. online and can also file returns etc. online.

The ongoing initiatives in India, from the State and civil society, to attain inclusive growth, towards skill formation, decent work, and sustainable livelihood need to attain more gravity for resisting the ongoing informalization and resulting inequities.

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