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Labour Market Regulation and Economic Performance:

A Critical Review of Arguments and Some Plausible Lessons for India

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Foreword

The view that labour market reforms for enhancing labour market flexibility is the key to being more competitive, to spurring economic growth and to create more employment is dominant in contemporary labour economics and in economic policy. This is not only true for the developed world, but this thinking and policy prescription extend to the developing world as well. Even in India labour market reforms have acquired a centrality and labour market flexibility is being prescribed to unleash the forces of the market, despite its pervasive informal sector that is –in the dominant view- also considered as being a result of the tight regulations that bridle the small tiny sector.

Such thinking is at the core of the so called Washington consensus, and is often still underpinning, at least in the realm of labour market regulations, policy advise as can be seen by the employing workers index of the doing business reports of the World bank. This implicitly suggests that in order to improve overall economic performance, it is absolutely necessary to deregulate the labour market and to remove or cut to minimum levels protective provisions for labour.

However, there are many economists who question the theoretical and empirical basis of the wisdom that castigates protective labour market interventions as hindrance to development; on the contrary, they take the position that such interventions may have a variety of positive effects, leading to more and not less decent work.

This paper gives a good overview of the theoretical positions of the orthodox and heterodox schools of thinking and then moves on to question the empirical evidence on the relationship between labour market reforms and labour market performance. It also asks the question whether the European debate on flexi-curity has any relevance for India and concludes that India's labour market reforms should move (and move) in this direction, albeit with its proper and adapted solutions. We are grateful to National Commission for Enterprises in the Unorganised Sector (NCEUS), Government of India to have allowed the ILO to publish this paper which was originally drafted for the Commission.

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1. Introduction

In the dominant discourses on contemporary economic policy, in India and as well as elsewhere, labour market reforms have acquired a centrality and labour market flexibility is being prescribed as the key to enhance productivity, to be more competitive, to accelerate employment generation and also to step up the tempo of economic growth (Blanchard and Wolfers, 2000; Besley and Burgess, 2004; Burki and Perry, 1997; Forteza and Rama, 2002; Heckman et al 2004; Salvances, 1997 among others). Such a thinking is at the core of the so called Washington consensus, or what Stiglitz (2002) called market fundamentalism, and the essential message is: to improve overall economic performance, it is absolutely necessary to deregulate the labour market and remove or cut protective provisions for labour.

However, there are many economists who question the theoretical and empirical basis of the wisdom that castigates protective labour market interventions as hindrance to development; on the contrary, they take the position that such interventions may have a variety of positive effects (Baker et al 2003, 2004, 2006; Freeman, 1993; Howell, 2006; Sengenberger and Campbell, 1994; Standing and Tokman, 1991; Wilkinson, 1992 among others). Thus, at a high level of generality, following Freeman, one may distinguish between two very distinct perspectives, namely, a ‘distortionist’ view and an ‘institutionalist’ view (Freeman, 1993). Arguments underlying these perspectives will be examined in some detail later; however, the essence of the major claims, in terms of causal connections, may briefly be stated here.

According to the “distortionist” view, labour market regulations are major obstacles to growth and employment mainly for the following reasons: First, as regulations in the labour market prevent wages to equal their marginal product in equilibrium, misallocation of resources are inevitable outcomes. Second, regulations may create major obstacles to the adjustment of labour markets to different types of economic changes in a dynamic setting. Finally, labour regulations that redistribute economic ‘rents’ from capital to labour (e.g. collective bargaining schemes, and expansionary fiscal programs to fund public employment etc.), may reduce profitability of the investors. Consequently, this may discourage investment and, hence, dampen the prospects of economic growth (Cesar and Chong, 2003).

On the other hand, it is argued in the “institutionalist” perspective that labour regulations may fulfil important redistributive roles in a market economy, particularly from the point of view of vulnerable categories of workers and this may provide necessary insurance from adverse market outcomes (Standing and Tokman, 1991). Equally importantly, this may be very significant for Keynesian reasons (i.e. for boosting economic demand), and thus expand growth as well as employment. Furthermore, provisions such as labour standards may create desirable pressures on the employers to focus on the enhancement of their labour productivity whether it is through training or technical innovations (Freeman, 1993). Finally, standards on mandated benefits may help to solve the moral hazard issues and all the workers will benefit (Summers, 1998).

In **Section 2** of this paper, these and other theoretical arguments, from both these broad perspectives, are critically examined. It clearly emerges from our discussion that the theoretical basis of the ‘distortionist’ perspectives is rather weak compared to the ‘institutionalist’ one. **Section 3** surveys some major cross-country empirical analyses examining linkages between labour regulation and different aspects of economic

performance such as employment, economic growth etc. Again, there is no compelling evidence to back the case of the distortionists. In this section, we also look at the relevant evidence, including the results of a couple of much talked about studies, on India, and it appears that the claims advanced by the distortionists are often exaggerated or dubious. Furthermore, it clearly emerges that many of these empirical studies are, methodologically and statistically, seriously flawed. As it happens, East Asian economies, (particularly China), have been the flavour of the day for a while and we attempt to draw some lessons from their labour market policies to highlight these which may be important in improving/ facilitating economic performances. This section also highlights the issue of social security and gives some useful insights towards socio-economic security for labour and flexibility in the labour market. Section 4 provides an account of the major labour laws in India, and this is followed, by a review of the critical issues in the current debate on reforming such laws. This section closes with some lessons and recommendations, which may be appropriate towards the reform of labour laws at the current juncture.

2. Theoretical Arguments on the Causal Connections between Labour Reforms and Relevant Economic Outcomes

As is well-known, labour markets across the world are usually characterized by a variety of regulations which impact directly (or indirectly) on wages, labour demand, labour supply etc., and do not permit unfettered rights and powers to the private agents. Also, through the standard fiscal systems, a whole range of redistributive measures are put in place, which include a degree of protection to the non-working population via unemployment benefits, welfare policies etc; further, labour in several countries have, to varying degrees, access to employment protection laws and some active employment policies by the government, among other supporting regulations.

One strand of the economic analysis argues that interventions in the labour market, or the existence of labour institutions in general, reduce the rate of job creation and generate higher unemployment (Salvances, 1997; Blanchard and Wolfers, 2000), apart from having an adverse impact on economic growth (Besley and Burgess, 2004; Forteza and Rama, 2002). Advocates of such a view obviously recommend elimination, or at least reduction, of labour market regulations in order to foster labour reallocation and higher competition, which, according to them, in turn, will enhance growth (Burki and Perry, 1997).

This group of economists argues that the success of economic reforms depends, in general, on whether labour costs can vary freely in response to changes in labour demand. This is because reforms necessitate a process of labour reallocation. Depending on the market flexibility the process of reallocation of labour takes place. It is argued that longer the time taken in the reallocation process, more inefficient are the outcomes. The proponents of labour market reforms assume that the absence of regulations results in employment of resources at the market-clearing prices, which leads to efficiency and it ensures full employment of almost all resources and all are rewarded according to their marginal contribution. Therefore, the full employment of all resources as well as optimal social welfare will be ensured if the regulations are completely eliminated.

It is generally argued that high minimum wages, often a consequence of the widespread collective bargaining through trade unions, compresses the wage structure. This may lead to less skilled workers being rationed out of the labour market, as is predicted by the usual supply-demand models. The basic idea behind such models is that constraining downward wage adjustments leads to employers responding with fewer jobs, which essentially harms workers. The outcomes may be particularly suboptimal in a context of unforeseen external stimuli such as demand shocks due to oil price hikes, significant technological changes, and intensification of trade competition etc. It is argued that to counter and mitigate such sudden shocks, downward wage flexibility, particularly for the less skilled workers, is required (ADB, 2005, p. 27); it is claimed that the significance of the trade unions and protective labour legislations as market-distorting agents, is highly amplified in such contexts. The assumption here is that the institutional interventions in the name of equity and social justice superimpose terms set above the market-clearing prices. It leads to an increase in the costs of productions, and thereby discourages investments. It is also argued that labour market institutions affect the freedom of employers to adjust the quantities of resources, one consequence of which is unemployment. Also labour market institutions create inequity by protecting the interests of insiders, and thus create obstacles to the outsiders who remain unemployed, as they can't enter the labour market. This creates a kind of subtle social divide and contributes to the perpetuation of inequality.

Advocates of the distortionist persuasion also oppose any income support to the families of workers as it is alleged to reduce the incentive for family members to take available jobs. Thus, as a recent ADB document puts it, for economists opposed to labour market regulations, “welfare-state interventions raise both the wage floor (the lowest wages that can be paid) and the reservation wage (the lowest wage at which workers will be willing to work), and these automatically reduce the demand for labour” (ADB, 2005 p. 27).

As should be evident from the foregoing, the essence of the criticism of the proponents of labour market reforms rests on the following: “labour market interventions misallocate labour; they waste resources through rent seeking; they impair adjustments to economic shocks; and they deter investment, thereby reducing rates of growth” (ADB, 2005, p. 27). Their targets of criticism are laws to minimum wage, unemployment benefits and other welfare supports, trade union activities, and the norms of labour standards. These arguments have been subjected to searching criticism, some of which are discussed briefly in the following; however the point may be made right away that typically these assessments are micro-theoretic and, as Freeman suggests, most of these are often of piecemeal nature.¹

The proponents of labour market regulations argue that interventions in labour market play important and positive roles and reject the standard neoclassical analysis (from which most of the case for reform is drawn) as being fundamentally flawed. One strand of

¹ As Freeman puts it: “Claims that labour market interventions have an adverse effect do not follow mechanically, it should be noted, from ‘pure theory.’ Distortionist analysts make selective use of economic theory. For example, those who believe that social security payroll taxes adversely affect savings and investment reject Ricardian equivalence; those who use nonwage costs to measure interventionist distortions reject the fungibility of models of compensation; those who argue that employment protection laws have efficiency costs ignore Coase’s theorem that property rights do not affect efficiency. Even distortionist criticisms of minimum wages involve more than applying optimizing calculus [...] Distortionist arguments are not the final word of economic theory” (Freeman quoted in ADB, 2005, pp. 27).

assessment focuses on the huge asymmetries in economic power of the workers and employers, and suggests that the weak bargaining position of the workers often leads to unfair outcomes such as underpayment to the workers, hazardous working conditions, or discrimination against certain groups of workers (women, children, for example). In general, private markets without proper regulations tend to do a poor job of protecting unemployed workers (ADB, 2005, p. 25). To the extent that certain kinds of regulation may be patently undesirable, proponents of labour market regulations also believe that the more equal the distribution of adjustment costs, the shorter and weaker the resistance to such regulations. Capturing the essence of this strand, the ADB report says: ‘that adjustment programs must be complemented by mechanisms to compensate the workers affected by the reforms. These include job separation packages, early retirement programs, and unemployment benefits. In general, these economists argue that the enforcement of labour standards and legally mandated benefits “force” employers to shift attention from cost-cutting issues to productivity-enhancement measures (for example, training and technical innovation)’ (ADB, 2005, p 27).

As Wilkinson 1992, Sengenberger and Campbell 1994, among others, suggest, firms may compete on the basis of two alternative trajectories: either reducing their unit costs by lowering wages and labour standards, that is, by opting for the ‘low road to growth’ or alternatively by increasing productivity with innovations in technology, product design, organisation etc., that is, by taking recourse to the ‘high road to growth’. As long as a firm can continue competing on the basis of low wages and bad working conditions, there would be little motivation to undertake innovations for improving productivity. If the path to competition on the basis of low wages and bad working conditions is banned by providing a floor of labour standards, the firms will be compelled to become enterprising and invest in technological and organisational innovation, which, in turn, might lead to better wages and working conditions. In fact, in the absence of a minimum floor of labour standards, which is important even from the human development perspective, an economy may inevitably end up being stuck in a vicious cycle of low wage and low productivity. This cycle leads to the race to the bottom, which finds a most convincing support in a multi-country study by Blanchflower and Oswald (1994). They also find strong evidence to suggest that higher wages are associated with higher employment almost all over the world.²

As is well-known, the neoclassical faith in the laissez-faire to achieve efficiency of resource allocation is rooted in the concept of perfect competition and Pareto optimality. But the labour market, like almost every other market, consists of various ‘imperfections’ as has

² In a well-known study, Gary Fields also dismisses the conventional mainstream argument that assumes an inverse relationship between minimum wages and employment. Using a model with the two sector labour market (one is covered by minimum wage and the other is not), Fields argues that the redistributive results of minimum wages will lead to higher employment for the economy as a whole simply because the demand for goods of the lower paid is expected to be highly labour intensive. This may happen through both the direct route of their own purchases as well as via the indirect route like multiplier effects. (Navin Chandra, 2006).

often been recognised by the mainstream economists themselves. Removing some of these imprecations is not sufficient to move towards the Pareto Optimality.³

Generally speaking, a very substantial chunk of the pro-regulation literature is organically connected with one or the other kind of ‘market-failure’. The idea of market-failure, which has several strands to it, became significant in economic theory way back in the 1920s itself and has gained in importance since then. In terms of microeconomic theory, to begin with, the phenomenon of market failure was linked mainly to the presence of externalities and the consequent problem in achieving ‘efficient’ allocation of resources. Subsequently, a whole range of reasons have been identified to have causal connections with market-failure and much of it has to do with the imperfections/ incompleteness of the relevant informations. This has spanned a huge literature in mainstream economic theory itself, a good deal around the notion of ‘efficiency wage’, which is often at sharp variance with the conclusions emerging from the distortionist perspective, and supportive of claims advanced by the institutionalist perspective.

Apart from the discussions in microeconomic theory, another major development of the 1930’s, with reference to the idea of market-failure, was the Keynesian contribution which sought to explain the Great Depression in terms of inadequate effective demand. Rational economic designs at the level of individual economic agents, so Keynes argued, may not add up to an optimal outcome for the system as a whole; thus insufficient aggregate demand may result in the economy getting trapped into under-employment equilibrium. Writings of Keynes (and those of Michael Kalecki, Richard Khan, N. Kaldor, J. Robinson, among others, in the 1930s) brought to the centre-stage the problem of market-failure at the macroeconomic level. It was such an understanding that was the cornerstone of economic policy of the post WW-II era, in the western world in particular but also elsewhere, and provided the basis for the so-called golden age of capitalism. However, and for no good reason, the Keynesian concerns have disappeared from the dominant mainstream canvass, and the proponents of labour market have managed to shift the attention from aggregate demand to a blinkered view of competitiveness.⁴

As we have already discussed in the foregoing, according to the mainstream argument, it is imperative to reform labour markets to increase competitiveness; and various cost-cutting policies via deregulation of labour market is the primary, if not the only, route to increase competitiveness and enhance productivity.

³ As Chandra (2006) argues, “Since the outcome of perfect competition is Pareto Optimal, remove imperfections or rigidities and the outcome will move towards Pareto optimal solution; this is implicit faith of all liberalisers. In this way of thinking, they even forget their own ‘Theory of Second Best’. The Theory of second Best simply and rigorously concludes that in the world of innumerable imperfections, removing only a few of them does not lead even to the second best solution. As Baumol (1965) noted, removal of only some of the imperfections may diminish social welfare” (Chandra, 2006).

⁴ As Bowles and Gintis (1995) put it “attention has shifted from the effect of egalitarian policies on aggregate demand to their effect on competitiveness which is to say on costs and productivity [...] and the growing focus on questions of wages and productivity under the general rubric of competitiveness has supported a near consensus that wage restraint and the limitation of social expenditures are necessary conditions for adequate economic performance. Society might still opt for egalitarian measures on moral grounds, many now believe, but at the cost of leaving even the poor to suffer in the long run” (Bowles and Gintis 1995,p. 409–410).

The obsession with competitiveness is reflected in separation of the productivity from the implication of such policies for the aggregate output and the employment objectives. As argued by Bhaduri (2005), an increase in productivity is not sufficient to maintain the higher total output, if the percentage of decrease in the level of employment is greater than the percentage increase in labour productivity. Therefore, the microeconomic efficiency-enhancing corporate strategy of 'downsizing' the labour force, may prove to be macro-economically counterproductive, if the size of the domestic market shrinks due to a lower level of aggregate employment. Thus, greater labour market flexibility may help individual corporations to gain a larger share of the national or international market by reducing unit costs; however, the overall macroeconomic effect may turn out to be counter-productive in terms of a shrinking size of the total market with lower employment level. Bhaduri (2005) also suggests that the strategy of maintaining high employment has a built-in mechanism for maintaining high domestic demand and relatively equitable distributions of income. Furthermore, such a strategy may also imply that the need for government interventions in several other areas, e.g. unemployment benefits, extensive subsidies, income transfers etc. can be curtailed, which may reduce the need for some of the administratively costly, wasteful and cumbersome forms of government interventions.

The problem of effective demand may tend to become quite serious, and relatively more difficult to manage, in the case of a liberalized/ globalized open economy, as has been argued by Patnaik (2004), with particular reference to the contemporary Indian economy. He argues that a deficiency of demand may arise, in an open economy, for several distinct reasons and may even lead to de-industrialization (in the sense of workers employed in the industrial sector losing their jobs). Patnaik's illuminating discussions, in the said paper and elsewhere (e.g. Patnaik, 1996), warrant much needed caution, as regards the difficulties in negotiating desirable macroeconomic policies in the age of globalized finance.⁵

Thus, it should be evident from our discussion in the foregoing that viewing labour flexibility as the cornerstone of economic policy may simply be barking the wrong tree. Economic performance of a system, in terms of growth and employment, hinges critically on other variables such as aggregate demand, appropriate investments in labour, among others. The central message emerging from the so-called Keynesian revolution, relevant in the context of present discussion, may be stated somewhat bluntly and crudely as follows: much of what happens in the labour market depends on the economic dynamics elsewhere, for instance in the product market. Our discussion here was at a general level without getting into the specificities of the developing countries, for which the advocacy of labour market flexibility as the key to growth and employment expansion is even more untenable. For such countries in general, public policies to accelerate aggregate capital formation, investment in physical and social infrastructure, and public provisioning of support (e.g. in terms of credit) for the overwhelming sections of the masses, particularly in rural area, struggling around or below the subsistence level have to be key elements of a broader macroeconomic framework for accelerating growth and employment generation. Developing country labour markets are, as is well-known, typically characterised by a dualism where the overwhelming proportion of labour is in the so-called informal sector, with negligible protection of any kind or any

⁵ In fact as Patnaik has argued elsewhere (Patnaik, 2006) theoretical argument for introducing labour market flexibility to improve macroeconomic outcomes employment is a flawed one. As he puts it, following, Keynesian-Marxian tradition a perennial excess supply of labour is essential for the functioning of capitalism.

support in terms of human capital policies. Thus, one could very well argue, that the inadequacy of active labour market policies in such countries has been a huge problem and counterproductive to the objective of decent and productive employment. Theoretical considerations would suggest that it is these issues that should be accorded priority by policy-makers in a country like India, instead of withdrawing a degree of protection available to a small segment of workers. We may conclude this section by recalling the key finding of a recent ADB study. Coming from what many would consider a ‘mainstream’ (if not ‘right wing’) institution, it may be worthwhile to quote the argument in some details: ‘A detailed examination of labour market policies in Asia, evidence from cross-country comparisons of labour market regulations, and stocktaking exercises for four countries – India, Indonesia, Philippines, and Viet Nam – lead to the conclusion that, in general, labour market regulations governing hiring and firing and minimum wage laws are not *the* binding constraint on employment generation; however, that there may be *some* aspects of labour market regulation in *some* countries that do indeed constrain employment growth and that must therefore be addressed. For example, in some cases regulations that make it difficult to reallocate workers may need to be modified. Where this is deemed necessary, labour market reforms will have to be complemented with reforms in other areas. *This conclusion undermines the case for across-the-board labour market reforms and advocates in-depth case studies to identify the specific policies that, in each country, constrain employment creation* (emphasis added).

At the same time, labour regulations covering basic rights of workers are conspicuous by their absence - due either to deliberate policy or to weak enforcement of regulation—for the large majority of workers in the informal sector. These workers are also poorly protected from the many risks they face due to the weaknesses of the systems of social protection. Labour market reforms will have to provide basic rights and effective systems of social protection to achieve decent employment’ (ADB, 2005, p.4).

3. Empirical Arguments on the Causal Connection between Labour Reforms and Relevant Economic Outcomes

As discussed in the earlier section, the mainstream explanation of high unemployment usually runs in terms of inflexible labour market, in particular, its downward rigidity and consequent high wages. In contemporary discussions, the frequently used models to support such a claim hinge on the idea of the non-accelerating inflation rate of unemployment, or NAIRU. The basic argument behind NAIRU is that at any given time there is a certain level of unemployment that is consistent with stable inflation. If the government tries to increase demand to drive unemployment below that rate, it will lead to accelerating inflation. If the government wants to reduce the inflation rate, it must reduce demand so as to push unemployment above this rate.⁶

Thus, central to the notion of NAIRU is that there is no scope for demand-stimulating measures, *ala* Keynes, to increase output and employment. Obviously in such a world, only

⁶ As it happens, the NAIRU’s assumptions have frequently been challenged empirically by several studies. For a recent work, that provides evidence for declining unemployment rates at a time of low inflation (in 1990s) in Canada, the U.S., and Britain in Stanford and Vosko, 2004, (eds).

policy option available to reduce long-run unemployment (or NAIRU) is to remove frictions and rigidities (such as minimum wage); in other words, we are back to the standard neoclassical framework.

The Organisation for Economic Co-operation and Development (OECD) (1994) and International Monetary Fund (IMF) (1999, 2003) for example, fundamentally using the NAIRU-argument have insisted for several years that, in order to accelerate growth, Europe has to reform its labour markets so as to make them more flexible, in line with the US approach. Similar analysis underpins the advocacy for reformers' arguments for labour markets in the case of developing countries, (Heckman and Pagés 2004). Using the highly influential 1994 OECD Jobs Study, and similar studies from different regions of the world, which identify flexibility of the labour market as the key to promoting competitiveness in the contemporary globalized economy, business leaders and governments have been advocating flexibility as the most important policy instrument to increase productivity, overcome unemployment, and reduce labour costs. As is well-known, every country has a set of complex system of labour laws, addressing a whole range of concerns relating to its labour market.⁷ Thus there are different bodies of legislations, some aimed at social security, others addressing concerns of fair working conditions, etc. However, it is argued by the proponents of labour market reform that ultimately all these contribute to downward rigidity of the labour market and high wages. In the following, we attempt a brief account of the major results (without getting into critical scrutiny of the methodologies and other underlying technicalities), from the recent relevant empirical literature.

3.1. Cross-Country Evidences

Typically, in these studies, various regulatory measures are classified into broad categories, and attempts are made to test for their relative costs and benefits with respect to different indicators of economic outcomes. Several well-known empirical studies, both for developed and developing countries, try to show that labour market regulations are important determinants of economic performance (e.g., Nickell, 1997; Freeman, 1998; Blanchard and Wolfers; 2000, Fitoussi et al., 2000; Belot and van Ours 2002; Botero et al 2003; Cesar and Chong, 2003; Heckman and Pages, 2003; among others); however, the researchers are clearly divided in terms of their findings as regards both the direction and the magnitude of the presumed causal connection.

In a major study, by Juan C. Botero, Simeon Djankov, Rafael La Porta, Florencio Lopez-de-Silanes and Andrei Schleifer (2003), an attempt is made to examine the implications of labour regulations such as employment laws, industrial and collective bargaining laws and social security laws for 85 countries.

The main findings of their study are as follows:

- The richer countries regulate labour less than poorer countries; instead they provide a more generous social security system.
- The heavier regulation of labour is detrimental to labour force participation, and generates higher unemployment, especially of the young.

⁷ "In most countries, the system of labour regulation encompasses three bodies of law: employment law, collective relations law, and social security law, besides some basic civil rights protections" (Botero, et al, 2003, p.2).

- More protective employment, collective relations and social security laws produce lower male participation in the labour force.
- Political power of the left tends to result in stricter labour regulation and more comprehensive social security (p.20).

Another recent and well-known study, by Calderon Cesar and Alberto Chong (2003), attempts to examine the argument that “labour market regulations create distortions from an ideal competitive setting, thus slowing down wage adjustment and labour reallocation and hence, becoming an obstacle for economic growth” (p.1). They use panel data for 76 countries, over the 1970-2000 period, to test their hypothesis.

Using econometric analysis, the study highlights the following as major claims:

- Growth in industrial as well as developing countries are adversely affected by thicker labour codes.
- Growth among developing countries could be promoted by fewer regulations stipulated in the national labour codes.
- Among developing countries, minimum wages and trade unions are the major routes of transmission through which higher labour regulations impact adversely on growth (p. 3).

Nickell (1997), building on his earlier work with Layard and Jackman (1991), examines a sample of 20 OECD countries for two six year periods, that is, 1983-88 and 1989-1994, to test the linkages between labour market institutions and unemployment. The log forms of average rate of unemployment, long term unemployment, and short term unemployment, for each country in each period, are used as dependent variable in a set of regressions, and a set of independent variables such as employment protection, the replacement rate, unemployment benefit duration, active labour market policy, union density, union coverage, bargaining coordination and the tax rate have been used to capture the impact of key labour market institutions and regulations. Nickell interprets his results with a degree of caution.

- He suggests that there is not much difference in many institutional features that are supposed to contribute to labour market rigidities between the group of high unemployment countries compared to the low unemployment countries.
- The study also suggests that certain features of labour market institutions, such as bargaining coordination, may help reduce unemployment.

The study warns that “the broad-brush analysis that says that European unemployment is high because European labour markets are too ‘rigid’ is too vague and probably misleading.”⁸

The study by Elmeskov, Martin and Scarpetta (1998) examines roughly the same context as the one by Nickell (1997), and highlights the following as significant findings:

- A large significant positive relationship between employment protection and unemployment.

⁸ Cited in Baker et al (2004, p. 20).

- No statistically significant relationship between union density and unemployment.
- The study also suggests that for most countries “the vast majority of the change in the unemployment rate can be attributed to country-specific effects rather than any identified change in the labour market institutions.”⁹

In spite of such a guarded position, Elmeskov, Martin and Scarpetta (1998) strongly endorse the recommendations of the OECD Job Study (1994), and advocate thoroughgoing labour market reforms.

The study by Belot and van Ours (2002), which covers a longer period, compared to the preceding two studies, examines the interaction between the key relevant variables for the five years periods from 1960 to 1996. Based on its regression analysis, it claims that:

- The coefficients of the variables like tax rate, the replacement rate and union density are all positive and statistically significant, which is in line with the conventional rigidity views.
- The coefficients of coordination and employment protection variables are negative and significant, which are clearly dismissive of the conventional view, implying thereby that the employment protection legislations *lower* the unemployment rate.

The authors also suggest that all the relevant institutional variables are difficult to be accounted for in cross-country studies, and the policies that bring about lower unemployment in some countries might not produce the same effect on other countries, with a different set of institutions.

A number of econometric studies have tried to factor in explicitly the role of ‘macroeconomic shocks’, while testing for the linkages between the labour market institutions and the relevant economic outcomes. In one such study, by Blanchard and Wolfers (2000), slowdown in total factor productivity growth, trends in long-term real interest rates, and shifts in labour demand represent the macroeconomic shocks, and an attempt is made to examine the interactions between such shocks and different institutions. The authors group the time-frame of the study, which is 1960 to 1998, into five-year periods. Some of the institutions vary from period to period in some regressions, but labour market institutions are held fixed in most cases. The non-linear least squares regression method has been used to estimate the coefficients of the interaction terms in this study and it allows for the simultaneous estimate of the coefficients for the macroeconomic shock terms and the institutional variables. The key findings highlighted by the authors are:

- In the presence of adverse shocks, protective labour market institutions contribute to higher unemployment.
- It is claimed that their results help to explain the general increase in the unemployment in the period 1960s to 1990s while also explaining the variation across countries.

Fitoussi et al. (2000) in their study of the interactions between macroeconomic shocks and labour market institutions consider country fixed effects, a country specific persistence parameter, a country specific sensitivity parameter and a series of macroeconomic shocks

⁹ Cited in Baker et al (2004, p. 21).

over the last three decades. They consider the difference between the country unemployment rates in the 1990s and the 1980s as the dependent variable in their cross-section regression.

The key result claimed by this study is that the persistence of high unemployment in some countries can be explained to some extent by the labour market institutions. However, the study cautions that “the labour market reforms advocated by the OECD secretariat, although helpful in some cases, leave us far short of explaining why the countries that recovered in the 1990s did so, and the amounts they did” (pp.276).

In another such study, Nickell et al. (2002) try to find plausible explanations for the trends in unemployment rates, in the OECD, over the period from 1961 to 1995. The macroeconomic shocks in this study include the changes in labour demand, total factor productivity growth, real import prices, money supply, and real interest rate. Apart from the unemployment rate a broader set of labour market outcomes are also treated as dependent variables such as the inflow into unemployment, real compensation growth, and employment-to-population rates.

The key conclusion this study arrives at is: “broad movements in unemployment across the OECD countries can be explained by shifts in labour market institutions.”¹⁰

The study claims that the that changes in labour market institutions explain around 55 percent of the increase in European unemployment from the 1960s to the first half of 1990s, and goes on to suggest that with better data on union coverage and the administration of the benefit system, a more complete explanation could be generated. Further, the recession of the early nineties is also held responsible, in substantial measure, for the relevant period.

Bertola, Blau and Kahn (2001) is another well-known attempt, for OECD countries, to explain trends in unemployment rates through the interplay of macroeconomic shocks and labour- market institutions. Overall the study produces mixed results, but its basic assertion is that both high wage inequality and low wage level are related to low unemployment. Also, the authors claim that the process of globalization and adoption of new technologies make it increasingly problematic for OECD countries to provide favourable employment and wage opportunities to their workers.

Based on the above-reported sample of studies, which are frequently quoted by the economists of the distortionist persuasion, it should be obvious that the lock-stock-and-barrel dumping of the labour market institutions is simply no good. Obviously, there may be aspects of labour market interventions that are undesirable and can be improved upon. But a blanket position of the kind characteristic of the NAIRU or similar views is essentially a dogma, as should already be evident from the perusal of the major claims of the studies mentioned in the foregoing. Furthermore, we have not touched at all the tricky issues relating to data, methodology etc. of the studies mentioned in the foregoing; however, obviously, the credibility of several claims must be judged by a careful examination of such issues. In this context, a few cautionary remarks may be in order here.

(I) In most of these cross-country analyses, results often depend upon the proxy used in the econometric exercises as well as the sample of countries; one may get very different results by changing these.

¹⁰ Cited in Baker et al (2004, p. 28).

(II) Variables such as union strength, active labour market policies, unemployment benefit levels etc., used in statistical exercises frequently, to ‘measure’ various aspects of the labour market are very difficult to capture (Baker et al 2004). This is a particularly severe problem for the cross-country studies, because the wide variability of these institutional variables across countries makes it difficult to generate comparable robust measures. Due to this inherent data problem, the empirical studies may often throw up messy results. Several researchers (for instance Freeman, 2005), consider the cross-country aggregate data as ‘weak’ to draw reliable conclusions.

(III) Many empirical studies assume a direct link between different labour market institutions and policies (such as unemployment benefit replacement rate, unemployment benefit duration, employment protection laws, union density, bargaining coordination and taxes) and unemployment. Baker et al (2004) attempt a very simple exercise to examine this link using OECD’s standardized unemployment rates for selected countries. To identify the longer term determinants of the pattern of unemployment, they organize the data for the period 1980 to 1999, when most of the OECD member countries experienced very high levels of unemployment, and this is plotted against the commonly used institutional variables (mentioned above). From the graphical presentations, they got “no hint that labour market institutions and policies could explain even a small part of the post-1980 pattern of unemployment for these nineteen countries” (p. 41). It also didn’t show ‘any obvious link between the pattern of deregulation in the 1990s and trends in unemployment rates’ (p. 41).

(IV) Baker et al (2004) also provide a comparative assessment of some of the most influential studies; these use diverse methodologies and are generally considered empirically sophisticated. Their comparative survey includes studies by Nickell (1997), Elmeskov, Martin and Scarpetta (1998), Belot and van Ours (2002), Nickell et al (2002), Blanchard and Wolfers (2000), Fitoussi, Jestaz, Phelps and Zoega (2000) and Bertola, Balu & Kahn (2001), i.e. those whose major results have already been mentioned earlier. It may be worthwhile to recall a couple of key conclusions from Baker et al.:

- As we have already noted, these influential studies, on balance, do not provide a strong evidence for the labour market rigidity view; rather the evidence is actually quite mixed. It is suggested that only the tax rate and unemployment benefit duration variables are significant, as per regression analyses, in these studies.
- Although the studies use the well-known, standard datasets, the range of the estimated coefficients is quite large. For example, for the employment protection index, the coefficient ranges from 0.2 percentage increase (Bertola et al 2001) to a 4.45 percentage increase in the unemployment rate (Nickell et al. 2001). Same is true for the coefficients for benefit duration, replacement rate, etc. Consequently, many of the claims appear unconvincing.
- Overall, as they put it: “these studies are far from unanimous in their estimates of the impact of the standard institutional variables on unemployment,¹¹ and that a number of prominent papers explicitly refer to this lack of robustness in their own results across specification and variable definition” (Baker et al 2004, p.41).

¹¹ It is very difficult even to make a rough conclusion about the link between labour market institutions across the developed countries (See Table: 1 in Appendix) and their unemployment rates from the data.

Having discussed the findings of the studies supposed to be lending support to the distortionist perspective, now let us look at a sample of empirical research from institutionalist persuasion. Among the better known works in this context is an empirical analysis of the effects of labour market institutions on unemployment rates across OECD member countries, for the period 1960-1999, by Baker, Glyn, Howell, and Schmitt (2004). One of the central messages of the study is that the various kinds of regulatory measures may influence labour force participation rather than employment itself. Some of their important results include the following:

- For bargaining coordination, which has a negative effect on unemployment, the result was strongest particularly in the period since early 1980s.
- The positive association between high taxation and high unemployment up to the early 1980s is weakened for the subsequent periods.
- There is no strong evidence to suggest that the regulating institutions are major impediments to the employment growth. They claim that “it is less evident that further weakening of social and collective protections for workers will have significant positive impacts on employment prospects. The effects of various kinds of regulation on unemployment are very hard to determine and may be quite negligible.” (p.42)

A well-known study from the US economy, by Card and Kruger (1995), attempts to test empirically the neoclassical prediction that the minimum wage had an adverse impact on employment growth. Based on their case study of the two adjoining states, New Jersey and Pennsylvania, they in fact find a negative association between the two variables; thus employment growth was higher where minimum wage was higher.¹²

In a series of studies coming from the International Labour Organisation, the mainstream predictions that blame the trade union activities for adversely impacting on growth, trade competitiveness, employment etc. have been effectively challenged, and the importance of the provision of the minimum wages in protecting low-income workers have been highlighted. In one such well-known work, (Kucera and Sarna 2004), based on the information for 162 countries, it is shown that stronger trade union rights do not generally hinder trade competitiveness, including trade of labour intensive goods; further, the study offers a stronger conclusion that the countries with stronger trade union rights tend to do comparatively better in several respects such as aggregate trade flows, total manufacturing exports etc. (p.25). Further, the fact that deregulation of the labour market, even in most of the advanced capitalist countries, has not been able to contain high unemployment even after

¹² To quote from Chandra's (2006) succinct summary of the study: “In 1992, the state of New Jersey increased its minimum wages above the national wage, while the adjoining Pennsylvania did not. Now for the minimum wage employers such as fast food restaurants along the common border, conditions would be nearly identical but for the higher New Jersey Minimum wage. This provided to Card and Krueger a good situation of controlled experiment. In contrast to the expected lower fast food employment growth rate after the introduction of higher minimum wage in New Jersey relative to that obtaining in Pennsylvania, Card and Krueger's rigorous analysis of data found that employment growth rate was higher in New Jersey than Pennsylvania, *ceteris paribus*. They tested the neoclassical hypothesis repeatedly using other states and different datasets but found the same results. They went on to re-examine the results of previous studies and found that they too gave similar results if subjected to better statistical techniques” (p.18).

We may also note that in another well-known study for the US economy, Bowles et al. (1983) documented the existence of a positive relationship between wages and productivity.

years of implementation, ought to increase scepticism about deregulation and its supposed benefits.¹³

Similar conclusions have been reached by a series of studies by Buchele and Christiansen (1992, 1995, 1999a, 1999b), who suggest that the workers' rights have a generally positive effect on the growth of output per hour worked. They argue that all the basic determinants of productivity growth such as pace of innovation in technology, rate of growth of the capital-labour ratio, development of human capital etc. depend significantly on the cooperation and effective participation of workers. Given that the workers' labour power is a crucial input in production, they hold the key to the success of the production process and thereby occupy a unique position to contribute towards the improvements in technology, work organization etc., which contribute to the increases in labour productivity. The authors suggest that for the long-run success of the firm, treating workers as stakeholders is very important, and this includes guaranteeing their rights, including that of collective bargaining, implementing measures, which reduce their vulnerabilities against job loss etc. Thus, as suggested earlier, even if some aspects of labour market intervention may be questionable, it does not make sense to rubbish labour interventions in general.¹⁴

As was mentioned earlier, high levels of unemployment formed the backdrop of the famous OECD study on Job Strategy in 1994, whose suggestions were very similar to the mainstream distortionist perspective. Very recently, OECD has released its revised guidelines on the basis of reviewing the subsequent decade's experience with the earlier recommendations, which clearly shows a significant shift in its stance (Watt, 2006).

In the 1994 Job Studies, all the major interventions in the labour market, such as the minimum wages, employment protection legislation, unemployment benefits, wage setting institutions, along with the tax wedge were blamed for high unemployment in Europe.

The revised job strategy, (henceforth, RJS) explicitly accepts that moderate legal minimum wages do not reduce employment,¹⁵ and, in fact, has other positive outcome as well. The RJS also accepts that employment protection laws and related benefit systems need not lead to higher unemployment provided they are not 'too strict', and characterized by bureaucratic and costly legal procedures. Further, the RJS finds 'new evidence' that active labour market policies can help offset the work disincentive effects, and also argues that

¹³ The experience of the East Asian economies during the 1980s, where unions were largely suppressed or severely restricted may lead some to believe that suppressing unions contributes positively to economic growth. However, as Freeman (1993) argues there is no robust empirical evidence to clinch this claim, and that the experience of a wide range of countries, both industrial and developing, indicates that unions do not seem to hamper growth.

¹⁴ Based on a thorough evaluation of the research conducted by the World Bank and ILO during the 1980's, Freeman (1993), in a "balanced scorecard", found little support for the distortionist notion that interventions are major impediments to better economic performance.

As is well-known, the relevant theoretical literature even in the mainstream tradition has increasingly recognized that labour markets are characterised by a range of market imperfections (Barr, 1998; Agell 1999; Gregg and Manning 1997, among others), and to improve their functioning different kinds of institutional interventions are necessary. As a recent IMF (2003) study acknowledges that 'the labour market does not function well without proper institutions, that is, without an appropriate mix of regulations, taxes, and subsidies affecting the relation between workers and employers' (pp. 131).

¹⁵ The significant success of introduction of minimum wages in the United Kingdom in 1999 also supports the beneficial aspects of minimum wages (Watt, 2006).

reducing benefits below a certain threshold level, may compromise social objectives (p.10). While wage flexibility is continued to be considered a desirable objective, it is acknowledged that there are different routes to achieve it. Greater relative wage flexibility (i.e. across space) is achieved through decentralised systems, whereas greater aggregate wage flexibility is produced through centralised systems, and there is no reason to privilege one route as a blanket prescription. RJS claims that ‘there is no single combination of policies and institutions to achieve good labour market performance’ (p.18); thus, the revised job studies marks a significant departure to its 1994 counterpart.¹⁶ The remarkable shift of the OECD stance from its decade long advocacy of deregulation strengthens further the claim of the institutionalist perspective.

Finally, it is now well-established that even in contexts where flexible labour market policies may be favourable for growth at certain junctures, it obviously can’t ensure the secure forms of employment, employment stability, equity with reference to race, gender etc., i.e. a whole range of worthwhile objectives rooted in the perspective of decent work.¹⁷

3.2. Evidence on India

In the recent years, the issue of labour market reforms has been very much at the centre-stage of policy debate in India. The view, that there are marked rigidities in the labour market due to a high degree of protection to the organised labour has gained considerable ground, and the official thinking has endorsed such a view explicitly.¹⁸ In the following, we take stock of

¹⁶ Heckman et al (2006) sharply criticise the new stance of the OECD’s job strategy. They argue that compared to the more flexible Anglo-Saxon labour market, the post-1994 performances of European labour market is not strong, in terms of productivity growth, employment generation, and human capital formation. This is contested by Howell (2006), who claim that the countries such as Finland, Denmark, Sweden, Norway, France etc. maintained a consistent better ‘total factor productivity’ growth between 1984 and 1997. According to the World Economic Forum, Finland, Sweden and Denmark, with highly regulated labour markets, and 75-90% of their workforce being unionised, among the top 4 countries in terms of global competitiveness. The fourth in the list is the US. Overall Howell (2006) considers the OECD’s recent policy recommendations based on the empirical evidence as more balanced compared to the previous reports.

¹⁷ In South Africa, for example, ‘regulated flexibility’ that is a strategy to address both the extreme forms of inequality established during the apartheid era, and foster competitiveness, ended up undermining minimum labour standards and supporting the spread of labour market insecurity. A series of Canadian-based studies also found that inequalities based on gender, race, and age were intensified, as labour market deregulation impacted most profoundly on those groups of workers already most marginalized (Thomas, 2006). Labour market deregulation exacerbated long-established patterns of racialised labour market segmentation. Job creation in workplaces of the so-called ‘new economy’ – for example call centres - combined insecure employment with feminised labour processes to create marginalized labour forces of women and young workers. Government interventions are indispensable to construct labour standards that provide effective protections for these emerging sites of employment.

We may also note here the findings of an inter-country study, which looks at the effects of core labour standards (as identified by the ILO declaration on fundamental Principles and Rights to Work) on several important economic outcomes. It is reported that labour standards have positive effects on per capita income and for countries, with medium or strong labour standard, the positive effect tends to be stronger (Bezeller, 2004).

¹⁸ “Various studies indicate that Indian Labour Laws are highly protective of labour, and labour markets are relatively inflexible, these laws apply only to the organised sector. Consequently, these laws have restricted labour mobility, have led to capital-intensive methods in the organized sector and adversely affected the sector’s long-run demand for labour. Labour being a subject in the concurrent list, State-level labour regulations are also an important determinant of industrial performance. Evidence suggests that States, which have enacted more

the evidence that has been marshalled to substantiate such a contention. But before that, it may be of interest to look at the key conclusions of an off-quoted paper by Basu (2005), which ostensibly drew upon the empirical literature, to argue that the labour market in India is indeed rigid and, consequently, leads to undesirable consequences.

The Paper claims that India's labour laws may have actually hurt the workers although they were supposed to protect them. He builds his argument by focussing on those labour legislations, which were drafted expressly to make the laying off labourers difficult.¹⁹ Basu constructs a model to show that, in equilibrium, an employer's inability to dismiss workers, who turn out not to possess the required skill, could hurt all workers, including the unskilled. The model shows that if some firms need specialised skills and talents but are disallowed to dismiss workers, (or it is very costly), then they would operate on a smaller scale or close down. If the firms close its operations, then both skilled as well as unskilled workers will lose their jobs. If those skilled workers join in the unskilled labour market, it would hurt the skilled workers directly; also, it may increase the competition for jobs in the unskilled labour market and in turn could lower wages. If this happens then unskilled workers will also be hurt. Such an outcome may materialize through another route also. If a firm faces a fluctuating-demand environment and is prevented by law from laying-off workers, it may close down or operate on a small scale. Basu argues that through this route a contraction in the demand for labour may take place and thereby depress wages. Assuming, obviously, that his model captures one of the core features of India's labour market, Basu argues that the existing legislations have resulted in the country's failure to deploy her large labour resources to compete better on the domestic and international markets; this, according to him, is in significant contrast to the East Asian and South East Asian countries where employment as well as wages witnessed impressive increases, precisely because they have fewer protective laws.²⁰ To draw empirical support for his basic conclusion, Basu relies on a much cited study by Fallon and Lucas (1993), who claimed to have shown that the demand for labour in large firms fell as the legislation preventing labour dismissal was made stronger.

Basu's argument, although sophisticated, is a typical micro-theoretic one; such arguments have significant limitations, as was discussed in section two, and we need not pursue it any further here. However, it may be noted that one can get very different results by playing around with the underlying assumptions of the model.²¹ More importantly, there are good reasons to believe that linkage between wages and unemployment, of the kind normally

pro-worker regulations, have lost out on industrial production in general" (Economic Survey 2005-06, Government of India, p. 209).

¹⁹ As he puts it "the eventual labour market equilibrium that emerges in an economy with such legislation may actually cause workers to have a lower welfare than in an economy with less protective legislation and that between legislating to prevent layoffs and legislating to maintain minimum wages, the latter may be the more desirable policy from the point of view of worker's welfare" (Basu, 2005, p.3). We may also note that the argument is not a blanket opposition to any protection for labour, a clearly a nuanced one. In another paper, Basu argues that the provision of a minimum wage can actually reduce unemployment (Basu, 2007).

²⁰ But a comparative analysis across Asian countries in the next section shows that this is not true.

²¹ D'souza (2005) argues that "if free contracting between workers and firms is allowed we show in an efficiency wage set up that both firms and workers can behave opportunistically requiring third-party enforcement of employment protection legislation" (p.939). He also puts in that "it is premature to conclude that anti-retrenchment laws are inefficient and end up hurting workers" (p. 944).

postulated by standard neo-classical economists, is, at best, a tenuous one. As has been shown by Mukherji (2006): “... the unique link between wage-rate and the level of employment depends crucially on the competitiveness of the labour market; that if this market is non-competitive, this link is snapped; and moreover, in the face of non-competitive conditions, wage determination has to depend on a variety of other factors some of which are pinned down; and, finally, that, therefore, there is no particular reason why a rise in minimum wages will affect employment.”

Let us now move on to some of the empirical exercises claiming to substantiate the presumed rigidity impacts of the labour laws. Among the major bones of contention in the labour market rigidity debate in India, the Industrial Dispute Act (in particular, its provisions contained in chapter V-B, which requires firms employing above a threshold number to seek government permission for retrenchment, closures etc.), and the Contract Labour Act, stand out. We will look at the significant implications of these, along with the major Acts, in a subsequent section. However, suffice it to note here that a substantial segment of the empirical literature in the rigidity debate directly or indirectly hinges on these acts. For instance, the study by Fallon and Lucas (1993) for India was largely motivated by the 1976 and the 1982 amendments of the chapter V-B of the Industrial Dispute Act.

Fallon and Lucas study attempts to measure the impact of changes in job security regulations in India (and Zimbabwe, where similar provisions exist). Using panel data for the period 1959-82 for India, and 1960/61 through 1984/85 for Zimbabwe, the central conclusions reached by the authors are:

- The ‘extreme job security regulations’ in India and Zimbabwe significantly reduced the demand for workers at given levels of output. However, the estimated decline in demand for employees varied considerably across industries.
- The industries with more public enterprises were less adversely affected, in terms of decline in labour demand, possibly due to the presence of strong trade unions.

The methodology underlying the Fallon and Lucas study, and consequently, its conclusions, have been subjected to searching criticism by several researchers (for details, see Bhattacharjea and the studies cited there), and we need not get into a detailed discussion of these here. Suffice it to note here that the empirical claim of the study do not stand up to a careful scrutiny (for details, see Bhalotra, 1998; Goldar, 2002; Anant et al 2005; among others).

Now we turn to the much-publicised empirical study relevant to the ongoing debate, which is by Besley and Burgess (2004). The presumed central concern of this study is 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. To map the direction of the change in the industrial relations climate, they track the state-level amendments to the IDA, and classify these amendments as pro-worker, neutral, and pro-employer and these are assigned scores of +1, 0, and -1 respectively. In all, 113 such amendments are identified and classified as such by the authors, and the assigned scores are cumulated over time for each state to arrive at a ‘regulatory measure’ for each state in each year. Such a measure is then used to explain a whole range of economic performance indicators with respect to the organized manufacturing sector using panel data for 1958 to

1992, at the level of states; these indicators include output per capita, labour use intensity, employment, among others.

As it happens, their regression analysis claims to prove all the claims of the distortionists: the registered manufacturing sector is adversely affected in every possible way because of a state being 'pro-worker'. Their major conclusions are:

- Pro-worker legislations have contributed to the lowering of investment and employment in the organized manufacturing sector, and thus have 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.
- Thus, in terms of welfare implications: "it is found that there is no evidence of the belief that pro-worker labour market policies redress the unfavourable balance of power between capital and labour, leading to a progressive effect on income distribution" (p.21). On the contrary, it is claimed that indeed the distributional effects appear to have worked against the poor.
- The analysis claims to reinforce the growing sentiment that there may be large gains from legislative changes that make the IDA more employer-friendly.

There are several issues relating to the Besley-Burgess study and its results which are deeply unsatisfactory, many of which have already been subjected to serious critical scrutiny (for details, see Bhattacharjea, 2006; Anant et al 2005, among others). We need not get into a detailed discussion of these here, but it may be useful to flag some issues, and the relevant empirical evidence, to get a sense of the flawed character of this study.

(I) On the basis of a single amendment at any time, a state can be classified as pro-worker or pro-employer. As Bhattacharjea (2006) points out, 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.²² Also, generally speaking, it should be obvious that when the multiple amendments take place within a single year, or over a short duration, the problem of awarding 'scores' becomes almost an intractable one.

Besides the various problems in case of classification, Bhattacharjea also points out some questionable results related to the econometric estimation. He argues that although the regulatory measure turns up significant in most of the regressions, the coefficients on most of the control variables, which seek to explain outcomes as disparate as output, employment, wages, entry and poverty etc., are statistically insignificant. Bhattacharjea thinks there are many other variables that could have been used. He also argues that serious flaws of Besley-Burgess methodology emerge when the state specific time trends are included in the regression.

²² Besley-Burgess classify Gujarat as pro-worker because of a solitary amendment which it passed in 1973; this amendment allowed for a penalty on employers for not nominating representatives to firm-level joint management councils, while all other labour laws remained intact. Bhattacharjea (2006) raises several important questions regarding the methodologies of giving scores to the states (in terms of states being pro-worker, pro-employer etc.). For instance, in Besley and Burgess' study, U.P. was classified as pro-worker on the basis of 1982 central amendment of the IDA. However, Bhattacharjea provides evidence to show that "on the basis of the 1983 amendment of its own IDA, U.P. should be classified as pro-employer" (p. 17).

(II) A puzzling feature of Besley-Burgess results is that pro-worker legislative amendments did not show any clear indication to raise workers' wages. As discussed earlier, the neoclassical literature treats the increase in wages as the main route through which the legislations hamper economic outcomes.

(III) 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.²³

(IV) Besley and Burgess study is not helpful in identifying specific components (of labour laws) impacting on particular economic outcomes, as it aggregates the former into one unique measure.

(V) Given that very significant changes have taken place, as regards the overall policy environment for labour, during the reform period, it is far from clear how much impact labour laws have had since the early 1990s. For instance, the introduction of a voluntary retirement scheme in the early 1990s, and its rapid spread subsequently, may well have legitimized layoffs and retrenchments across the board in India's registered manufacturing sector although the labour laws have largely remained unchanged. Also their enforcement appears to have been diluted substantially as the governments at different levels have become even for indifferent towards enforcing them in the recent years (Anant et al. 2005; Sharma 2006).²⁴

(VI) Although, there has been no change in labour laws, wage share has experienced significant compression in the liberalization period. The ASI reports that in 2003-04 wages to workers constituted only 2.4% of gross output of organised industry, which is likely to be among the lowest in the world. Hasan et al. (2003) find that the share of the wage bill, in either total output or value added,²⁵ is lower in the more open trading environment after 1991, and is lower in industries that have lower barriers to trade. For example, controlling for industry and location (via the introduction of industry-location fixed effects), their estimates of labour share equations suggest that labour shares would decline by around 4% (as a share of total output) and 5% (as a share of value added) for a reduction in tariffs from 150% to 40%. These results are consistent with the argument that workers in India's formal manufacturing sector have seen their bargaining power weaken as a result of trade liberalization. This is despite the fact, as noted above, that domestic labour laws have not changed on paper.

²³ "In fact, the effect of laws is translated into labour market outcomes indirectly through a range of intermediate factors such as the enforcement environment, background rules, and cultures of governance and compliance etc" (Anant et al, quoted in ADB, 2005, pp. 49).

²⁴ In a recent study, Nagraj found that: 'between 1995-96 and 2000-01, about 1.1 million workers, or 15 percent of workers in the organized manufacturing sector lost their jobs. These losses have been widespread across major states and industry groups' (p 3390). As he puts it : "Although the labour laws remained the same, their enforcement was diluted or government ignored their evasion by employers. In effect, it was reforms by stealth" (p 3388).

²⁵ Shrinking wage share is also confirmed from India's manufacturing sector from ASI Data (see Table: 2 in Appendix). In a very recent paper Nagraj (2007) also shows the declining trend of unit labour cost in manufacturing (see figure 3 in the Appendix) as well as in the public sector. The same paper also show the declining wage-rental ratio, which also goes against the workers.

(VII) As documented earlier, 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 relationship²⁶ 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).

(VIII) In general, there are several well-known features of India's labour market which simply do not square up with the expected outcomes as per the Besley-Burgess reasoning. For instance, protective labour legislations are supposed to increase industrial disputes (as they shore up the power of organized labour); however, as is well-documented, there has been a secular decline, through the 1980s and 1990s, in both the number of disputes as well as the number of person/days lost due to disputes.²⁷ Also, the person/days lost on account of the strikes have been fewer than those due to lock-outs since 1990.

(IX) As regards the presumed adverse employment effects, it is instructive to note the findings, based on the ASI data for 1973-74 to 1997-98, of a recent study by Anant et al. Looking at the percentage distribution of total employment in the size classes- 'workers below 100', '100-999', and 'above 1000', - the study concludes that: 'the expected compositional' shifts are not visible. What we see is that the above 100 size has increased (as a percentage of total employment) much more than that of below 100. The presumed deceleration of employment seems valid only in the case of above 1000 size class employment. It is possible that the employment decline in the above 1000 size establishment is less due to the labour laws than due to the substantial restructuring of the large public sector units and traditional manufacturing industries (cotton textiles, jute manufacturing, steel and engineering). Thus our preliminary exercise does not seem to support the presumed employment effect of the labour laws' (Anant et al., 2005, p. 27). Similar scepticism has been expressed by other studies as well (e.g. Goldar, 2002; Deshpande et al, 2004).

(X) The above-cited study by Anant et al also shows that the presumed labour substitution effect i.e. substitution of labour by capital due to protective labour legislation, is not borne by the ASI data. We may also note that as per the World Bank's Investment Climate Survey of the Indian States (World Bank, 2003), two states which were ranked 'Best' are Gujarat and Maharashtra; interestingly, as per the Besley-Burgess study, both the states were classified as 'inflexible' in terms of the labour market flexibility measure (for details, see Table 8)!

One may cite several other findings based on the secondary data which are at variance with the conclusions or the expectations of the Besley –Burgess and similar studies. However, for reasons of space, we need not pursue it any further here. But it may be of interest to look at the key findings of a field based study that examined a number of the relevant issues. In a survey of about 1,300 manufacturing firms across nine industry groups, Deshpande et al (2004) examine the determinants of the levels and changes in employment between 1991 and 1998. One of the main objectives was to find out the extent of flexibility enjoyed by employers in adjusting investment as well as other important decisions within an establishment to external changes; in particular, they ask whether the presence of unions, collective bargaining, and labour laws, especially the provisions of the Industrial Disputes Act hamper investment and employment decisions.

²⁶ See regression results in Table: 3 in appendix.

²⁷ See Figure 1 & 2 in the appendix.

The study reports that both the *unionised and non-unionised firms increased capital intensity* over the relevant period; thus the presence of unions does not support the core conclusion of the distortionists as regards the adoption of capital-intensive technology; however, the absence of a union appears to be slightly more likely to promote growth in employment than its presence. As far as the impact of *statutory minimum wage provision* is concerned, it again does not support the case of the distortionists as only half the firms reportedly were paying the statutory minimum wage. Also, it is worth noting that nearly two-thirds of the firms employing less than 10 workers paid statutory minimum wages, whereas this percentage was lower for larger firms, who employ 1000 or more workers.²⁸

The study also reports that the share of permanent manual workers declined from about 69 per cent in 1991 to 62 per cent in 1998, increasing sharply in industries such as non-metallic minerals, beverages and tobacco. Further not only did the share of non-permanent workers increase but the share of casual workers in the non-poor permanent category increased even faster, and the bigger **firms resorted to greater use of non-permanent workers**. Firms employing 50-99 workers and those employing 500 or more workers increased their share of non-permanent workers significantly between 1991 and 1998 with all other factors remaining the same.

In sum, a careful consideration of the empirical evidence of India's industrial landscape certainly does not support the claims of the distortionists, and does not warrant privileging the labour laws as the key to understanding output or employment performances. Clearly one needs to look at the importance of a whole range of other critical variables, some of which were touched upon in section 2 of this paper. In section 3.3, we take a look at the labour laws in Asian context as a whole; in particular, our motivation is: are the policies in East and South East Asian countries, significantly different from India, and if so, what are the important lessons? But before we come to such a comparison, a brief overview of the labour market in Asia as a whole may be useful.

3.3. Labour Market Policies: Some Lessons from the Developing Countries in Asia

Asia's labour force, currently estimated to be approximately, 1.7 billion, accounts for 57.3% of the world's total labour force; furthermore, India and China together account for 71% of the continent's total labour force. It is also worth emphasizing that, unlike in the case of developed regions, Asia's labour force is growing rapidly. Based on the available projections for the working-age population, Asia's labour force is expected to grow by 14% by 2015 and by 24% by 2030 (ADB, 2005). Over the next 10 year span, as per the ADB's projection, although the absolute increase in China and India will be larger due to their sheer size, the percentage increase in the labour force will be significantly higher in countries such as Pakistan (30%), Bangladesh (25%) and the Philippines (24%), given the varying pace of demographic transitions in different countries.

As is well-known, very large sections of Asia's labour force is engaged in the agricultural sector and the expected share of employment in agriculture, in the foreseeable

²⁸ "The fact that 17 per cent of the firms employing 1,000 and more workers could pay merely statutory minimum wages despite the so-called restrictive industrial relations laws still being on the statute book is probably also due to the recent anti-labour twist in the approach to labour rights of both the executive and judicial arms of the state" (Sharma, 2006, p.2028).

future, will continue to be large in several countries, particularly in South Asia, but also in East and Southeast Asia. Needless to say, the overwhelming majority of these labourers have to sustain themselves at low and precarious levels of earning.

As regards the urban labour markets, most Asian developing countries exhibit notable dualism, that is, the coexistence of a **modern or formal** sector with overwhelmingly large **traditional or informal** sector. As is well-known, the development discourses of the early post-World War II years had almost been unanimous in the belief that the informal sector was a temporary ladder into the modern, and it was only a matter of time for such a transition to materialize. ‘Lewisian optimism’ seemed infectious and, for many, well-grounded. However, with the benefit of the hindsight, it is clear that in large parts of the global economy, such a dualism is no less acute compared to the 1950s and ‘60s, and we almost have a ‘Lewisian nightmare’ at hand, as very large sections of labourers continue to be trapped in a variety of ‘traditional’ and ‘informal’ activities, scrounging hard, to just about make a living, (or not even that) with no exit routes. Economists, across the ideological spectrum, generally agree that productive employment of labour force in most developing countries in Asia is a major problem, although it does not quite show up on the basis of the official rates. There is the widely held view that the poor, who constitute large sections of the population in these countries, can not afford to remain unemployed; sure enough, this is a truism but the real question is: whether they manage to get employed adequately for a decent living. Our sense is that the official data systems tend to overestimate the extent of employment, given their underlying methodologies of estimation, in case of developing countries.²⁹ Moreover, even if we take official data at face value, there have been increases in unemployment rates during the last decade. Furthermore, as is generally accepted by researchers, underemployment is a huge problem in most developing countries. As a recent ADB report puts it: ‘out of a total labour force of 1.7 billion ... around 500 million are underemployed in the time-based sense. It needs to be stressed that as large as this number may seem, it still constitutes an underestimate’ (ADB, 2005, p. 14).

As is well-known, economic growth in the Asian region during the last decade has been relatively faster compared to most other regions; in fact during the decade since 1995, Asia’s economic growth rate was more than double the global average, and there has been much speculation about the 21st century as being the Asian century. However, the growth performance has not been matched by expansion of employment opportunities, and problem of unemployment, disguised unemployment, poor working conditions, extreme vulnerabilities even to mild shocks, chronic insecurities, etc. are widespread. According to the most recent estimates from the ILO,³⁰ in 2005, close to 84 per cent of workers in the South Asia, 58 percent in South East Asia, 47 per cent in East Asia, and 36 percent in Arab States were unable to earn enough to keep above the \$2 a day poverty line; as one would expect, typically, the share of informal employment in total non—agricultural employment ranges from very substantial (e.g. 42 per cent in Syria) to overwhelmingly high (e.g. 83 percent in India) across different countries in the continent. Different indicators of the working conditions create an extremely grim picture, and work-related accidents and diseases result in loss of lives of close to one million workers annually. Clearly, these numbers indicate a widespread precariousness and fragility in the lives and livelihoods of very large

²⁹ For an elaboration of this argument, see Jha, 1997.

³⁰ Juan Somavia, Director-General of the ILO, *The Hindu*, 20th August, 2006.

sections of workers across Asia. Sure enough, there are examples of impressive performances, in terms of generating productive and decent employment for the majority of workers, such as Hong Kong, South Korea and Singapore; furthermore, there are regions and sectors in several countries with modest to impressive success records in special sectors/regions. However, large parts of the continent continue to be plagued by inadequate and insecure employment opportunities, and the problem has become more daunting in spite of strong economic growth. For instance, in the 1980s, in the People's Republic of China, a 3 percent growth of output was adequate to generate a 1 percent increase in employment; however, in the 1990s, to achieve the same rate of expansion in employment (i.e. 1 per cent), the required output growth rate had taken a quantum jump to almost 8 per cent.

With this brief backdrop of the labour market in Asia, it may be useful to address one of the key conventional mainstream concerns: that is, whether Asia is different from other regions in terms of policies towards labour regulation and protection and the implications of the same for employment and output growth. It may be recalled from section two that Botero et al. offer a data set on such provisions for 85 countries, which cover a wide range of regulatory and protective measures such as employment laws, industrial and collective relations laws and social security laws. Botero et al codify the relevant information and also generate measures of worker protection. Using this data set, a recent study by ADB attempts a synoptic comparative assessment of different regions such as Asia, Africa, Industrially Advanced Countries and Latin America (ADB, 2005). It may be worthwhile to quote the key conclusions reached by this study.

Box 1:

“Employment Laws: Asia is clearly not different. In the case of the dummy variables, the mode is the same as in at least two other regions (i.e., one of the other three regions is the different one). In the case of the averages, a cursory look at the data indicates that Asia does not stand out. For example, it has fewer days of annual leave with pay in manufacturing; the number of paid mandatory holidays ... is slightly higher than in the industrial countries and Africa, but the same as in Latin America; the cost of increasing hours worked ... is similar in the three developing regions, and substantially lower than in the industrial countries; legally mandated severance pay ... is substantially higher than in the industrial countries and Africa, but about the same as in Latin America; finally, the cost of firing workers ... is also higher in Asia than in the industrial countries and Africa, and about the same as in Latin America. It seems, therefore, that there could be two areas where Asia may be labeled as different, in the sense of having a restrictive legal system that may affect the creation of employment. These are legally mandated severance pay and the cost of firing workers. In the latter, all Asian economies bear a high cost (except for Hong Kong, China).

Collective Bargaining Laws: Once again, the overall Asian picture is not altogether different from that of the rest of the world. In Asia, workers’ councils ... are mandated by law, the same as in the industrial countries. Also, the law in Asia does not allow sympathy, solidarity, or secondary strikes, though they are allowed in the other three regions. However, Asia is the only one of the four regions where a strike is not illegal even if there is a collective agreement in force This is the only industrial relations aspect where Asia seems to be different and which may affect employment creation.

Social Security Laws: The evidence is once again clear: Asia is not particularly different from the other regions in terms of disability and death benefits or sickness and health benefits, although the number of months of required contributions is lower than in the industrial countries. Moreover, the social security system does not cover the risk of unemployment.

Civil and Political Rights: Most Asian countries have mandatory minimum wages ..., the same as the other two developing regions. Only Hong Kong, China; Malaysia; and Singapore do not have mandatory minimum wages. The industrial countries are split on this issue. Asia has the same union density (proportion of workers affiliated ...) as the other two developing regions, and about half that of the industrial countries.”

Source: ADB, 2005, p. 40-43.

Thus the essential message, as per the above-cited ADB study using the Botero et al data is: the Asian region is no more ‘rigid’ in terms of regulatory measures; furthermore, workers in the industrially advanced countries have a substantially higher degree of protection in terms of social security provisions. Also, within Asia, different regions can hardly be ranked in terms of labour market rigidity: for instance, the claim that East and South East Asia is less ‘rigid’ than South Asia is very much on a slippery ground.³¹

Going by the same dataset, the ADB study also looks at the relevant information for 15 individual economies within Asia, and suggests that it simply does not make sense to make grand generalizations.³² Further, it rightly suggests that particular labour market provisions need to be located in detailed analysis of specific countries, to look at the implications of such provisions.

As is well-known, China and India have been at the centre stage of the recent debates and discussions on economic transformation, for very well-known reasons that we need not recount here, and the issues relating to their respective labour regimes have been in sharp focus. Given that, these two giants of the global economy account for almost 40 percent of the global workforce, the significance of their labour policies can hardly be overstated.

A few words on a popular perception regarding the People’s Republic of China may be in order here. As is well-known, the Chinese economy, for well over two decades, has been among the fastest growing in the world, and one often hears that, compared to the Indian economy, the Chinese labour market is much less ‘rigid’, and this has been one of the key factors in the country’s remarkable growth rate. Such a perception, to put it bluntly, is simply wrong. China’s state-owned enterprises still account for close to 30 percent of the country’s labour force, and in terms of being covered by protective labour regulations, this segment can hardly be considered any less flexible than the much-maligned organised sector in India; also, it is worth-stressing that as a share of the total work force, India’s organised sector, at 7 to 8 percent, is only a fraction of the share of the SOEs in the Chinese case. Furthermore, at least on paper, labour regulations in China can hardly be considered any less binding, and possibly have a much broader reach in terms of the coverage of the workforce, compared to India (GOI, the Second National Commission on Labour, 2002; Banerjee, 2005). Sure enough, in terms of details, there are a number of significant differences³³ in the provisions for labour between these two giants of Asia, which account for more than 70 percent of the continent’s labour force; however, our contention is that there is no *prima facie* case to consider the Chinese labour market any more ‘flexible’ than that of India.

³¹ It may be emphasized again that there is not much to choose between the two regions in terms of several interventions in the labour market, which are often criticized by the distortionists. Data seem to indicate very little difference in the existence of minimum wage laws, notice period and severance pay required for laying-off workers. “In fact, severance pay in the case of Indonesia and Thailand was higher than that in Bangladesh and Pakistan. In terms of the percentage of labour force covered by trade unions, it is only India that stands out in comparison to countries of ESEA” (Islam, 2003). Also “not much difference appears to have existed with regard to non-wage benefits, e.g., old age, disability and death benefit, sickness and maternity benefits, and unemployment benefits” (Islam, 2003, p. 24).

³² ‘Some countries with different experiences in terms of labour outcomes seem to have similar labour market policies; and vice versa, some countries which on paper are perceived as similar, have different labour market policies’ (ADB, 2005, p. 46).

³³ The major differences are in the area of rights to organize, collective bargaining, and freedoms of association.

§Nonetheless, it is important to recognize that the problems of underemployment, informality etc. are major challenges to the policy-makers in the People's Republic of China (Brooks and Tao, 2003), and in many ways these have become more daunting in the recent years, as discussed in the following.

However, there is one area, with very important implications for a whole range of economic outcomes including labour market outcomes, where China has been significantly ahead of India; this has to do with the provisioning of basic social infrastructure as well as targeted policies for improving the quality of the human capital of the workforce. In fact, in this respect, within the Asian continent, the East and South East Asian Economies (henceforth ESEA) have a clearly better record than South Asia, which is reflected in a whole range of indicators, such as literacy levels of workers, proportion of workers with secondary education, mean years of schooling, access to programmes for skill up-gradation and training etc.³⁴ (for details, see Khan, 1994; Khan, 2001; Islam, 2001; Islam, 2003; ADB, 2005). It may be useful here, given the prominence of China in contemporary development discourses, to sketch a profile of the country's labour market, and the recent policies related to labour; this some relevance to the ongoing discussions in India.

3.4 Labour's Landscape in Contemporary China

China's remarkable economic transformation after the initiative of reforms in 1978 has drawn attention of many governments, policy makers and experts all over the world. During approximately two and a half decades, beginning 1980, China's GDP expanded seven-fold or about fourfold in terms of real GDP per capita. It is widely believed that China's fast growth wouldn't have been possible without economic reforms that are without a gradual marketisation of the economy and integration with the world market during the era of ongoing globalization. It is also generally acknowledged that instead of big-bang approach, China's strategy of reforms is piecemeal, partial, incremental and often experimental (Gallagher, 2004).

Since the inception of reforms, the structure of China's labour market has also been significantly transformed as may be seen from the Table 10 in appendix. Percentage of urban population has increased sharply in the period 1980-2002 although China still remains predominantly rural. Although the population growth has slowed in the recent years to just less than 1 per cent per annum, the labour force has tended to grow relatively faster, at about

³⁴ A few examples may be instructive. "In 1976, Korea introduced, the Basic Law for Vocational Training that requires private firms with 150 or more employees to conduct in house training for a portion of its employees, or to pay a training levy equivalent to no less than 6% of its wage bill. This levy is used to promote vocational training through government-sponsored vocational training schools. Likewise, Singapore has a series of programmes such as the Vocational and Industrial Training Board, set up in 1979 and financed with a levy of 1% on wages to subsidize efforts to upgrade the skills and expertise of employees or retraining of retrenched workers. Other initiatives like the Basic Education and Skills Development program to teach basic skills in arithmetic and literacy to workers, the creation of the National Productivity Board in 1972, and the National Productivity Council 1982, were also undertaken to promote productivity consciousness. Elsewhere, in Malaysia, Training costs are also subsidized and the Penang Skills Development Centre puts together training courses contributed by multinational corporations to upgrade their suppliers' skills. Thailand grants a tax deduction (150) percent for training expenses" (ADB, 2005, p.79-80). Higher productivities in East Asian countries may be attributed to some extent to their human capital policies.

1.5 per cent per annum. The labour force participation rate hovered around 60 per cent throughout the 1990s (see Table 10 in Appendix).

Around 1980, i.e. in the early years of reforms, an overwhelming majority of the labour force was either employed as agricultural workers in rural communes or as employees in urban state-owned enterprises (SOE), with virtually no labour flows between the rural and urban sectors. By 2002, however, over a third of the rural labour force had moved into non-farm activities, mainly in town and village enterprises (TVEs), and more than two third of the urban labour force had found employment outside of the state sector, in urban collectives, joint ventures and private enterprises (see Table 11 in Appendix). The most significant change is the drastic decline of the employments in the State Units.

During the period 1990 to 2002, employment growth was concentrated mainly in the urban areas where the number of jobs increased at an average rate of 3 percent per annum (or 6.5 million p.a.); this has happened in spite of the State-Owned Enterprises (SOEs) going for a huge layoff of its workers, as is evident from (Table 11). Although, employment in collectives also declined sharply from 1995 onward, the job losses³⁵ at SOEs and collectives were more than offset by the total job created. This was due to the growth in the private sector (including foreign-funded enterprises), which created 17.5 million jobs in the six years ending with 2001, and an unexplained increase of 75 million jobs over the same period (Brooks and Tao, 2003). This significant unexplained increase was ostensibly in the informal sector which includes street vending, construction and household services, among others, and many of these are not well covered by the official statistics. Therefore it is reasonable to conclude that the supply of quality job was hardly impressive although in the aggregate the total number of jobs clearly went up significantly between 1980 and 2002.

It is also worth noting that the job growth in the later years of 1990s was largely concentrated in particular service sectors and some costal provinces, especially Fujian, Guangdong, Shandong, and Zhejiang (Brooks and Tao, 2003). In these provinces, the private sector (and foreign direct investment) has flourished since the government started opening up special economic zones in the 1980s and adopted some preferential policies toward some export oriented industrial growth.

It is quite clear that the pace of employment generation has slowed down considerably as the labour market flexibilisation picked up momentum. In a recent paper Zhu (2007) shows that employment growth,³⁶ as well as employment elasticity of output, are

³⁵ “Under this arrangement, the workers who lost their jobs but enjoyed their unemployment benefits were not included in the data of registered unemployed workers in cities and towns” (Fang & Miyeng, 2004).

³⁶ On the whole, most researchers take a dim view of the employment prospects in contemporary China. However, there are differences as regards the pace and prospects of employment generation. For instance, Fang and Meiyang (2004) argue that employment growth has been substantial, mainly through the irregular channels; and according to them, “actually, the overall employment in China did indeed increase, and only regular employment in cities and towns was reduced. The employment number in work units in China’s cities and towns has been gradually decreasing since 1978, while the employment number outside work units has been increasing. That is to say, employment in irregular sectors has been increasing. In the period 1996 to 2001, the ratio between the employment number in irregular sectors and work units increased from 1:4 to greater than 1:2. Therefore, from the perspective of using general statistical data to observe the employment situation in China, it is usually easy for people to underestimate the actual growth of employment”. But most other researchers take the view that the pace of employment generation has declined intertemporally, particularly since the early 1990s.

much lower in primary, secondary and tertiary sectors in the decade 1990-2000 compared to 1980-1990 (see Table 13). In fact several other employment related indicators, with reference to China's labour market, suggest quite a dismal story, as may be seen from Table 6. It is hardly surprising that recorded unemployment has tended to creep up in the recent years. The registered unemployment rate, as reported by the Ministry of Labour and Social Services (MOLSS), was almost constant at around 2.5 –3 percent during most of the 1990s, but it rose to 4.0 percent by the end of 2002 (Table 10). Even those with university education are finding it increasingly difficult to get employed (see Table 14).

In the early years of China's reforms process, town and village enterprises (TVEs) developed rapidly to meet a built-up demand for consumer goods in rural areas, and also to take advantage of a vast pool of cheap rural labour force. As a consequence, the rural employment growth was rapid in the 1980s and early 1990s. But the situation has changed significantly since the mid-1990s when the TVEs began to face financial problems, as well as growing competition from the private sector, and the absolute level of employment in these enterprises was almost stagnant between 1995 and 2001. Moreover, employment opportunities in agriculture started declining during the 1980s itself and it accelerated the exodus of workers from the rural to urban areas. During the 1980s, as mentioned earlier, migrants from agriculture were inclined to move to rural TVEs, but subsequently faster-growing urban areas in the eastern provinces (Fang, 2001) became major destinations.³⁷

Most recent accounts suggest that the outflow of labour from the rural area have increased enormously. As per the estimates of the China's National Bureau of Statistics, there were about 80 million permanent migrants (i.e., those living in urban areas for more than six months) between 1990 and 2000. However, the estimates for the number of temporary migrants, had a wide range, e.g. 30-75 million (between 1990-2000) and for the more recent years, this number in the range of 120-180 million. Nonetheless, it is worth highlighting that, in spite of massive exodus from the rural areas, the problem of surplus labour is an acute one.³⁸

Essentially, many of the features of China's labour market today are obvious outcomes of the country's transition to the market economy and widespread adoption of capitalist labour practices by firms of all ownership types in the period of reforms. Labour relations in China have been fundamentally changed with the country's gradual movement towards privatization and its labour practices have shifted overwhelmingly toward favouring firm autonomy, flexibility, and managerial control of workers organization (Gallagher, 2004)

So-called irregular employment refers to employment in irregular sectors, which include self-employers, family enterprises, and micro-enterprises.

³⁷ "The largest concentrations of migrants are found in the Pearl River Delta (Guangdong) and Yangtze River Delta (Shanghai and Jiangsu), where average GDP per capita is 4 to 10 times that in poorer rural provinces such as Gansu and Guizhou. Estimates of the migrant population vary, ranging between 80 million and 150 million" (Brooks and Tao, 2003).

³⁸ "Despite increased migration, considerable surplus labour persists in the rural areas. The Organization for Economic Cooperation and Development (OECD) (2002) estimates that if the average GDP contribution per worker in non-agricultural jobs is used as a benchmark, rural hidden unemployment can be estimated to represent around 275 million (where hidden unemployment is defined as low-productive employment regardless of working time). If the benchmark is set more modestly at one-third of the productivity of non-agricultural workers (in line with other Asian countries), rural hidden unemployment would be around 150 million" (Brooks and Tao, 2003).

(see Box: 2 below). Once the transition to market economy gathered momentum, the central government's attempt to maintain some features of socialist labour relations such as greater employment stability, longer-term employment relations, and active worker organizations etc. were weakened considerably.

Box 2: Labour Market Reforms: Steps toward Labour Market Flexibility

- “In 1980, China’s first national work conference on labour market issues adopted a more flexible labour market strategy. Urban job-seekers were allowed to find work in the state, collective, or newly-recognized private sectors, and enterprises were granted more autonomy in hiring decisions. The authorities, however, continued to formulate a labour plan, but instead of unilaterally allocating workers to enterprises, labour bureaus began to introduce workers to hiring units.
- Wage flexibility has been increased gradually. From 1978, firms were allowed to reinstitute bonuses (subject to ceilings) and piece wages. In 1994, the introduction of a new Labour Law also gave management more discretion over wage determination. As a result of these reforms, the share of bonuses in total wages for all enterprises rose from 2 percent of the wage bill at the start of the reforms in 1978 to about 16 percent in 1997.
- A labour contracting system was introduced in the mid-1980s. This signaled a marked shift away from the system of lifetime tenures with its potentially distorted work incentives. The initial steps were modest and resulted in only moderate growth in the share of employees under contract, but further reforms in 1994 gave new impetus to labour contracting. As a result, the share of workers on contracts almost doubled from between 1994 and 1997, to about one-third of urban workers. Restrictions on movements of workers across firms were also removed, in an attempt to reduce the scale of the mismatch of labour inherent in the pre-reform system.
- SOEs gained the right to lay off permanent workers. Those employees without contracts had lifetime tenure with SOEs, but in the mid-1990s, this tenure was eroded. SOEs, however, were required to establish so-called “re-employment centers” (RECs) for laid-off workers (“*xiagang*”), which provide retraining and job search assistance and pay unemployment benefits. If the laid-off worker remained unemployed for more than three years, the employer could sever the relationship. From 2002, newly laid-off workers receive only unemployment benefits, and the RECs will be phased out by 2004.”

Source: Brooks and Tao (2003).

Capitalist practices have been encouraged through ownership expansion, i.e. the introduction of new types of firms, and ownership recombination, which is the fusing of the public and non-state sectors through novel forms of organization. Gallagher (2004) points out that “the much-needed panacea to this shift to capitalism—a state regulatory and legal regime that is capable of mitigating its excesses and effective organizations to represent labour—is not yet well established. Actually, in post-communist economies reforming was synonymous

to decline or death of state industry and socialist labour practices and the adoption of capitalist labour practices.”³⁹

The policy creating Special Economic Zones have also had far-reaching implications for labour in China. To begin with, four Special Economic Zones came into being in 1980, in underdeveloped coastal regions close to Hong Kong and Taiwan, and it was extended gradually to other coastal cities, and finally to all 31 provinces. Since the early 1990s number of economic zones has increased very rapidly; in fact between 1991 and 1993 itself this number went up from 100 to 8000 zones for the country as a whole, although for many of these there was little chance of substantive flows of foreign capital in several of these zones (Zweig, 2002: 93–94; Yang, 1997). In these special economic zones, local governments often pushed for greater liberalization for the benefits from large inflows of foreign capital and more linkages to the international economy. Besides, local firms also obtained flexibility and autonomy when they found any foreign partner and they were subject to different laws and regulations than those of the core public sectors in China’s cities.

It is well-known that the liberalization of the foreign investment and trade regime was not uniform across the country. Essentially, policy of SEZs sparked regional competition for inflows of both foreign and domestic capital, which further enhanced the bargaining power of capital.⁴⁰ An obvious outcome of the rapid expansion of SEZs was significant shrinking of land available for agricultural purposes in rural areas, leading to rising discontent.⁴¹ During 1996-2005, for the so called ‘development’ purposes, that is, mainly for highways, industries and SEZs, more than 21 percent of arable land was diverted to non-agricultural uses. Furthermore, between 1992 and 2005 around twenty million farmers had to leave agriculture due to land acquisition. Cultivable land holding now stands at a meagre 0.094 hectares per capita (Goswami, 2007).

As is well-known, that in the pre-reforms era, workers especially those employed in the SOEs and collectives, were under the coverage of various workers’ welfare schemes. Besides, there were specific policies towards livelihood, health, education, etc. for all

³⁹ Initially the transformation of labour relations began in core sectors of public enterprise in the cities but subsequently it spread to rural areas as well through the much talked about Special Economic Zones, which were set up as hubs for foreign direct investment, and in township-village enterprises (TVEs) which played a major role in soaking up surplus labour created by agricultural reforms. As Gallagher puts it: “Transformation of the core public sectors was achieved through the dynamic liberalization of investment and ownership, a process that occurred gradually across regions and types of firms. The decentralization of the economy and the devolution of authority and decision making power to local governments are key characteristics of the Chinese reforms” (Gallagher, 2004).

⁴⁰ It is worth emphasizing that in many of these zones migrant labourers had a great role in China’s industrial transformation in the non-state sector, especially TVEs and in the export zones and coastal factories funded by foreign and private capital (Solinger, 1999; OECD, 2002).

⁴¹ Recently in rural China protests against land acquisition and deprivation have become a common feature especially in the provinces of Guangdong (south), Sichuan, Hebei (north), and Henan province. The government admitted that in 2004, there were 74,000 riots in the country-side, a seven-fold jump in ten years and these are directly or indirectly related to those policies. Livelihood of a large section of population and Social stability is now a serious concern in these areas.

In April 2004, the State Council, China’s cabinet, halted the ratification of farmland for other uses and started to rectify the national land market. The Minister of Agriculture, Du Qinglin, promised “not to reduce acreage of basic farmland, change its purpose or downgrade its quality” (Goswami, 2007).

citizens. But, gradually the situation has changed substantially in the post-reform period, with the shrinking of employment opportunities in the SOEs and collectives, the expansion of the private enterprises, growing informalization, and disregards for workers' rights.⁴²

Informalization of labour market has reduced the range of social security coverage to a great extent. The shift to contract system has made layoffs and termination of employees relatively easier and large number of laid-off workers from state-owned enterprises have simply gone out of the purview of various employment related welfare schemes.⁴³

The vulnerability of the migrant workers is emerging as a major issue. Given their skill and education background, it is difficult for the overwhelming majority to find quality jobs. It is true that many among them might earn higher incomes compared with what they earned before their migration, but obviously they do not have any employment stability and are saddled with inhospitable working conditions. Furthermore, those who do not have residence permit in the areas where they work, miss out on a range of public goods.

The rising discontent amongst workers has put pressure on the Chinese state to take some corrective steps. The 1994 Labour Law⁴⁴ proclaims to "protect the legitimate rights and interests of labourers, readjust labour relationship, establish and safeguard a labour system suited to the socialist market economy, and promote economic development and social progress" (Chapter 1 of the law). Sections 2 and 3 specify that the law as a whole applies to all employers ("enterprises and individual economic organisations") and their employees, and that workers have "the right to be employed on an equal basis." In the new regime, for implementation of the laws, responsibilities fall upon the labour bureaus of central, regional and local governments down to the county level. On the face of it, the said Labour Law offers comprehensive coverage for labour related issues such as promotion of employment (Chapter 2), working time and holidays (Chapter 4), minimum wages (Chapter 5) employment of youth aged 16-18 and women (Chapter 7), social insurance (Chapter 9) arbitration committees (Chapter 10), the labour inspectorate (Chapter 11) and so on. In Chapter 9, i.e. for provision of social insurance it is acknowledged that "workers have a right to public social insurance covering retirement, illness, occupational injury and disease, unemployment and maternity."

However, even though an impressive set of provisions is supposed to be operational since the mid-1990s, implementation and enforcement of these mostly protective codes have lagged far behind. Clearly, during the reform period, the State's capacity and willingness to supply legal institutions and robust regulatory frameworks that can adequately protect the

⁴² "In 2001, in cases of labour disputes that labour arbitration agencies have processed, the ratio of cases involving labour salaries in private enterprises was 143 percent higher than in the state sector; on issues relating to security and benefits, the number of dispute cases in private enterprises was 14 percent higher than in the state sector; on the issue of labour protection, the number of disputes in private enterprises was 221 percent higher than in the state sector. These private enterprises were relatively formal ones, and at least they were registered. As for enterprises that have not formally registered, the impact of their irregular nature on labour protection and so on is more obvious" Fang & Miyeng (2004).

⁴³ Among the urban unemployed labourers in 2002, there were 6.52 million laid off workers, which was the largest segment among the various categories of unemployed.

⁴⁴ Labour Laws adopted at the Eighth Meeting of the Standing Committee of the Eighth National Peoples Congress on July 5, 1994, promulgated by Order No.28 of the President of the Peoples Republic of China on July 5, 1994, and effective as of January 1, 1995.

individual workers have been weak. Presence of a large and growing number of migrant workers, contract workers, and a range of informal workers makes it difficult for enforcement of many of the legal provisions (Gallagher, 2004).

Possibly there have been small achievements with regard to social insurance system, which has gradually been evolving during the last ten years. At present, five contribution-based programmes with “socialised” management – no longer controlled by employers – are now in place, although their implementation in practice has been gradual. After several pilot experiments, the schemes like Maternity insurance (1994), Work injury insurance (1996), Pension insurance (1997), Medical insurance (1998), and Unemployment insurance (1999) are being put in place, nationwide. In principle, social insurance (see details in Box 3 & 4 in appendix) is now compulsory for urban employees and voluntary for the self-employed; from 2003 it has been a national policy to promote the enrolment of rural migrants under the scheme.

The coverage of the total population under those schemes remains low by international standards. The coverage under pension insurance was 16% of the employed in 2003, or 21% including civil servants. Of the relevant population, coverage under other schemes was as follows: (a) unemployment insurance, 14%, (b) medical insurance, 11%, (c) work injury insurance, 6%, and (d) maternity insurance, 5%. Moreover, expressed as a percentage of employment in urban areas (including rural migrants), both pension insurance and unemployment insurance had similar or slightly lower coverage in 2003 than in 1995, while only medical insurance of the three biggest programmes increased between 2000 to 2003 (Reutersward, 2005).

The other factor which probably has been of some help to workers in China is its education⁴⁵ and health legacies from the socialist days, that is the provisioning of basic social infrastructure as well as targeted policies for improving the quality of the human capital of the workforce. There are a few proactive employment promotion measures to address the issues of the unemployed, workers laid off, new graduates and the surplus labour force in rural areas. Vocational training⁴⁶ is provided in parallel with regular education in China and

⁴⁵ In the reform period the quality of government schools is deteriorating, largely due to inadequate government expenditure and this has resulted in a mushrooming of private schools. From the late 1980s, private educational institutions have been growing rapidly (For details, see International Herald Tribune, 28th August, 2006).

⁴⁶ Labour Laws adopted at the Eighth Meeting of the Standing Committee of the Eighth National Peoples Congress on July 5, 1994, promulgated by Order No.28 of the President of the Peoples Republic of China on July 5, 1994, and effective as of January 1, 1995. the important provisions include:

Article 66 The State shall promote the cause of professional training through various channels and by various measures to develop the professional skills of labourers, improve their quality, and strengthen their employment and work abilities.

Article 67 Peoples governments at all levels shall include professional training into their programmes for social and economic development, and encourage and support enterprises, institutional organizations, social groups, and individuals to carry out professional training in various forms.

Article 68 The employer shall establish a system for professional training, extract and use funds for professional training according to State regulations, and provide labourers with professional training in a planned way and according to its specific conditions.

Labourers to be engaged in technical work shall receive training before taking up their posts.

it includes pre-employment training, training for people who are already employed, and training for people transferred to new occupations, covering elementary, intermediary, and advanced vocational qualification training for technicians and other types of training to help people acquire skills and adapt to different job requirements. As of December 2003, there were altogether 3167 technical schools in China (including 274 advanced technical schools) with a total of 1.91 million students attending the schools, and, in addition to these students the schools offered different types of training to another 2.2 million people from various social sectors in 2003. There were 3465 governmental employment training centres, and 17350 non-governmental training institutions, in 2003, and 10.71 million people trained through the year. Of course, given the enormity of the challenges, these numbers are obviously far from impressive. Nonetheless, it may well be the case that the policy makers in China are seized of the importance of active labour market policies.

In sum, China's transition to a market economy, for more than three decades now, has resulted in major changes in the world of work and the provision for the well-being of workers. As in most other parts of the world, Chinese policy makers have been persuaded by the logic emanating from the 'distortionist' perspective. In the process, workers' rights and entitlements have severely been affected, leading to the rising discontent among them. To address some of the problems, China put a regulatory system in 1994, which is being implemented gradually; there have been small initiatives to build up social safety nets thorough various schemes. Obviously one of the major objectives of the Chinese government is to contain the discontent of workers and to keep in check the growth of social tensions. However, on the positive side, some of the measures adopted in the area of the provisioning of universal social insurance and active labour market policies may have useful lessons for policy makers in developing countries.

Based on our perusal of the empirical evidence, we would like to reiterate that it is extremely important for policy-makers to not remain trapped in the narrow obsession with 'labour market rigidity', and to focus on the critical issues relating to human capital policies. Investments in education, at different levels, addressing specific training needs of workers, and other such interventions are obviously key to the better utilization of human resources.

Two core arguments that we would like to emphasize here, based on the perusal of the relevant literature, are the following. First, decent outcomes, for the economy as well as the labour market, can hardly be reduced to the presence or the absence of labour market flexibility. Two, to the extent issues relating to labour market flexibility are pertinent, it is important to locate them in the larger context of labour market policies.

3.5 Some considerations related to Flexibility & Social Security

Before we conclude this section, it may worthwhile to reflect on a couple of issues relevant to the ongoing debates on balancing flexibility and security for labour in the current era of globalization. At the current juncture, it is of obvious importance due to increasing interdependence between different countries through greater liberalization of trade, financial

Article 69 The State shall determine occupational classification, set up professional skill standards for specific occupations, and practise a system of professional qualification certificates. Examination and appraisal organizations authorized by governments shall be charged to carry out examination and appraisal of the professional skills of labourers.

markets and foreign direct investments and an increase in migration; this poses new challenges to the labour markets. It is obvious that in a context of increasing globalization, space for autonomous/ nationalist policies gets eroded, and with respect to the labour market, policy makers can hardly ignore issues relating to flexibility. It is in this context that the recent discussions on the labour market flexibility become important. However, it needs to be emphasized that labour market flexibility must go together with the socio-economic security for labour.

There are important lessons to be learned from economic history in this regard and there are alternative frameworks, which provide useful insights towards combining socio-economic security for labour and flexibility in the labour market. The arguments that developing countries cannot afford public provisioning towards social security and other protective/promotional policies for labour is rather a weak one. In fact the experience of developed world, in particular countries in Europe, towards the end of the 19th and the first half of the 20th centuries, when with modest per capita income levels many of them were able to put in place effective promotional/ protective systems, and gradually expand them, is quite instructive (Justino, 2003; Lindbeck, 2002; Dev, 1996; among others).

As is well-known, in the late 19th and early 20th centuries, various legislations were introduced, in several of these countries, for work injury compensation and to support modest pensions. Bismarck's initiatives in Germany in the 1880s are often considered path-breaking in this respect. In some countries, mainly on the European continent, the governments were also implicated in the organization of occupational pensions in the private sector, although it was limited primarily to large industrial firms. Comprehensive systems for income maintenance, say in the case of childbirth, single motherhood, unemployment, sickness, old age, etc. were introduced, mainly in countries in Western Europe soon after the World War II.

Around the same time, public systems for secondary and tertiary mass education and comprehensive health care for the entire population were also built up (Lindbeck, 2002). Also, two of the most influential initiatives of social security in the 1930s and '40s, namely the Social Security Act in the United States America and the Social Security Programme (as per the Beveridge Committee's Recommendations) of the United Kingdom, are justly famous as important milestones. Thus it was over an extended period of time that the 'modern welfare state', guaranteeing high-income security and generous provisions for various types of social services for all citizens, came into being; however, the point worth emphasizing is that a number of significant steps were taken when many of these countries, in terms of income levels, were possibly comparable to contemporary developing countries like India.

The second point worth recalling here is that even the post-WW II modern welfare state came in different types and shapes. For instance, within Western Europe itself, analysts often identify four kinds of social policy models, namely Nordic, Anglo-Saxon, Continental European and Mediterranean (Ferrera, 1998; Bertola et al 2001.) (See Table 4 in the Appendix). Likewise, the developing countries have to evolve their own models as they grope their ways forward. Current hegemony of neo-liberal globalization has put tremendous strain on socio-economic policies for labour, and even the developed countries of Europe are suffering hard to cope with the challenge of 'balancing flexibility and security'.

On the one hand, flexibilisation of employment and the labour market is being advocated in view of the goals of economic performance, competitiveness and growth (European Central Bank, 2002), whereas an equally strong demand for security is being advocated from a social policy perspective for providing security to employees – especially vulnerable groups - emphasizing the importance of preserving social cohesion within these societies (For example, the Laeken Declaration on the Future of the European Union, presented 15 December 2001). To address both the issues simultaneously, there are initiatives in EU countries to adopt the so-called ‘flexicurity’ model.

The concept of ‘flexicurity’, as the name suggests, attempts to combine the seemingly opposed objectives of flexibility as well as security in functioning of the labour market. Although there is no one agreed definition⁴⁷ of flexicurity, and there also exist variations in implementing this policy across some of the European countries, undoubtedly strongly felt need to balance flexibility and security is the main impetus behind this idea. The Employment in Europe Report, 2006 notes that flexibility and security are not contradictory, “but mutually supportive” for facing the challenges of globalization. According to the definitions used by Wilthagen et al, there are two dimensions of flexicurity model. From the perspective of the flexibility dimension, the major concerns are external and internal numerical flexibility, functional flexibility, wage flexibility; and the security dimension deals with job security, employment security/employability security, income security and combination security. Although there differences exist among the various observers regarding the different approaches towards flexicurity, the European Commission and the member States have arrived at a consensus on a definition of flexicurity (see interim report of the Expert Group on Flexicurity)⁴⁸ which comprises four components, as described by Auer (2007) as follows:

- “*Flexible and secure contractual arrangements and work organisations*, both from the perspective of the employer and the employee, through modern labour laws and modern work organisations.
- *Active Labour Market Policies (ALMP)*, which effectively helps people to cope with rapid change, unemployment spells, reintegration and, importantly, transitions to new jobs – i.e. the element of *transition security*.
- *Reliable and responsive lifelong learning (LLL) systems*, to ensure the continuous adaptability and employability of all workers, and to enable firms to keep up productivity levels.
- *Modern Social Security systems*, which provide adequate income support and facilitate labour market mobility. This includes provisions that help people combine work with private and family responsibilities, such as childcare.

As a process variable this definition includes:

⁴⁷ There is no one agreed definition of flexicurity; however, the following formulation by Wilthagen and Rogowski visualizes as “a policy strategy that attempts, synchronically and in a deliberate way, to enhance the flexibility of labour markets, the work organization and labour relations on the one hand, and to enhance security – employment security and social security – notably for weaker groups in and outside the labour market on the other hand” (Wilthagen and Rogowski, 2002, p.250).

⁴⁸ www.ose.be/files/RECOWOWE/DIAC/InterimRepFlexisecurityApril2007.pdf

- *Supportive and productive social dialogue*, mutual trust and highly developed industrial relations are crucial for introducing comprehensive flexicurity policies covering these components”⁴⁹ (Auer, 2007, p. 3).

Thus, on the whole, the common principles of flexicurity adopted by the EU Commission are ‘more and better jobs through flexibility and security’ (EU Commission, 2007). There is a consensus among most of the observers that globalisation and new technology has made labour demand more volatile and that necessitates a (partial) shift towards security based on broader shoulders than that of stable employment contracts with a single firm. In line with this, “the main thrust of the EU recommendation on flexicurity is to encourage a shift from job security towards employment security” (p. 8 of the chapter on Flexicurity in *Employment in Europe* 2006). But Auer (2007), instead of viewing it merely as ‘a shift from job security towards employment security’, opines that the present shift is a ‘job to labour market security.’ He also sketches the systematic routes of flexibility that the private and public sector can arrange for:

Configurations of flexibility (excluding wage flexibility)

	Numerical Flexibility	Functional Flexibility
External Flexibility	Hiring/firing Temporary jobs (including temporary agencies)	Outsourcing/insourcing
Internal Flexibility	Working time reductions/prolongations	Work organization changes Polyvalent skills Working time arrangements (shift work, etc.)

Source: Reproduced from Auer (2007)

Therefore, firms have a choice between internal and external types of adjustments as shown in the above table, for the purpose of balancing the flexibility and security i.e. for the ‘flexicurity’.

As far as the implementation and outcomes are concerned, various empirical evidences give some mixed results and paradoxes regarding the flexicurity and labour market outcomes. At the same time there is substantial empirical evidence that the flexible regimes, with sufficient protection by labour market policies and medium degrees of employment protection, perform better in terms of decent jobs (Auer, 2007).

Auer (2007) also argues that that the apparent paradoxes, mentioned above, might be reconciled in intelligently designed reform packages in the labour market where stability, flexibility and security are addressed simultaneously. Absence of any one of these, and that of a prudent social dialogue, may lead to suboptimal results either for productivity, employment performance or workers’ security. In fact, in the different institutional settings across countries and with their particular agents, a number of flexicurity models exist with some variations, and some of them perform well. So, there is no unique model, which would be applicable for every country. But there must be some common elements in every model, as suggested by Auer (2007), such as “medium-level employment protection through

⁴⁹ www.ose.be/files/RECOWOWE/DIAC/InterimRepFlexisecurityApril2007.pdf

innovative employment contracts, high social protection by activated LMPs, social rights such as maternity, parental and training leave, possibilities to shift between part-and full-time work, etc.,⁵⁰ complementarity between worker and firm oriented flexibility, high degree of internal flexibility in high performance work systems”, and lastly “the effective social dialogue.” And these are paramount requirements to confront the present challenges of globalization without hindering productivity competitiveness and workers’ welfare.

Now, for the developing countries, it must be kept in mind that the European countries have adopted different measures to bring flexibility in labour market in a background of a strong social protection system. Although there are some cut in the different social benefit schemes during 1980s and 1990s in most of the European countries, social sector expenditure is still very high, ranging from 22.52% to 28.45% of GDP (see Table 4). It stands to reason that to ensure a secure income or a decent employment in a more flexible setting some form of social security is a prerequisite. In other words, either-or-trade off between ‘security’ and ‘flexibility’ must be rejected as a false one.

Developing countries have to figure out, as mentioned earlier, ways and means of striking appropriate balances for themselves. It seems to be that developing countries like India must ensure a minimal income as well as social security to all its citizens. National Rural Employment Guarantee Act is obviously an important step in this regard. Hopefully, the Social Security Bill, proposed by NECUS, will soon get the legal mandate. Together, these may be viewed as the first couple of significant steps to provide a modicum of security to India’s worker.

4. Labour Laws in India and Current Debate on Reforming such Laws

As discussed earlier in this paper, labour laws have figured prominently in contemporary policy discourses in India, and the distortionist perspective, i.e. the view that rigidities in labour market lead to a variety of inefficiencies, including in terms of labour market outcomes (such as employment expansion, persistence of dualism etc.), has had a substantial following among the economists as well as the policy makers. It was argued in section 3.2, that such a view rests on a shaky foundation. However, there are a number of critical issues relating to the existing laws, their implementation and related issues, which require to be addressed. In this section, we try to flag, what in our view are, among the more important concerns in this regard.

Under Article 246 of the Indian Constitution, labour has been put on the concurrent list, which means that both the Centre and the States can legislate in this respect. As it happens, governments at both these levels appear to have been quite prolific in making laws. However, there has been inadequate coordination on the part of these two (i.e. the Central and State Governments), resulting in serious problems, which include poor and often conflictual formulations, confusions galore as regards areas and appropriate authorities for jurisdiction, as well as issues relating to implementation. Further, the evolution of labour

⁵⁰ They have an impact on flexibility and security as they link possibilities for temporary exit from the labour market (flexibility) with return options (security).

laws, from the pre-independence period until now, both at the level of the central and the state governments, has been characterized by adhocism.

The net result is that the country has no dearth of laws; there are close to 50 central and around 175 state laws which have something to do directly with labour, and if we include the ones which indirectly are relevant then even to draw a precise list of labour-related statutes is a difficult task. But, as already stated above, many of these are poorly designed,⁵¹ and coupled with the fact of massive confusions relating to matters of jurisdiction (for details, see Chandra, 2006; Shankaran, 2006; contributions in Debroy, 2005; among others), we clearly have quite an undesirable situation at hand. This is a widely shared conclusion by the experts within the academia as well as in the political spectrum across ideological divides. As Chandra puts it: ‘the complexity and contradictions of Indian labour regulations ...cry for resolution, simplification, rationalization and consolidation. The crusade of the employers’ organization for simplification of labour laws makes sense in this background’ (Chandra, 2006, p 35). Part of the explanation behind extremely poor implementation⁵² of many of these laws rests on the above noted problems. Before we dwell further on these critical problems, it may be useful to state the broad thrusts that the country’s labour laws aim at.

Although there is no universally accepted typology, but it may be useful to classify the major labour laws into following broadly, as is often done in the relevant literature,⁵³ Industrial Relations, Wages, Working Conditions, Social Security and Insurance.

Major acts relating to **Industrial Relations** in India include:

- I. The Trade Union Act, 1926, which specifies the conditions that trade union needs to satisfy in order to be recognised under the act.
- II. Industrial Disputes Act, (IDA) 1947, which sets out the institutions for adjudication of disputes.
- III. The Bombay Industrial Relations Act (BIRA), 1946, which specifies the nature of collective bargaining in the textile industry of Maharashtra and Gujarat, cooperative banks and the Bombay Electric Supply and Transport Undertakings of Maharashtra. These industries are not subject to the IDA, except on cases of retrenchment, closure, and dismissal.
- IV. The Maharashtra Recognition of Trade Unions and Prevention of Unfair Labour Practices of Act, 1971.
- V. The Administrative Tribunals Act, 1985.

⁵¹ As careful surveys by Shankaran (2006), Chandra (2006), among others, have shown, even on basic definitions such as ‘workman’, ‘employee’, ‘industry’, ‘wages’ etc., the situation is quite chaotic. For instance, to quote Chandra, ‘the term wage has been defined in 11 different ways in 11 different laws’ (Chandra, 2006, p.33), and thus, to use his phrase, we have a ‘cacophony of definitions’.

⁵² It is generally acknowledged that India’s record in enforcing labour laws has been quite dismal (Despande et al 2004; Chandrasekhar and Ghosh 2005; Shankaran 2006; among others). As Forteza and Rama note, the labour laws scenario in India is ‘most rigid on paper’ but ‘most flexible in practice’ (Forteza and Rama, 2002, p. 18).

⁵³ (Chandra (2006); Contributions to Debroy, 2005; FICCI-AIQE, 2006; Second National Commission (2002); Pages & Roy, 2006; Shankaran (2006); CII, 2006; CITU, 2006; among others).

Among these, the Industrial Disputes Act, (IDA) 1947 has been at the centre of controversy in the recent years. The IDA specifies a multi-tier conciliation-cum-adjustment system, created and maintained by the State Governments. Although the norms are decided by the centre, its working changes from State to State. In particular, Chapter VB of the IDA, which says that, for retrenchment and lay off, permission from the government is mandatory for all industrial establishments, of non-seasonal and non-intermittent nature, employing at least 100 workers. Critics of the IDA cite this as a major impediment to the flexibility in the organised sector. The Trade Union Act is also considered a major culprit in this regard.

The principal laws relating to **Wages** are:

- I. The Payment of Wages Act, 1937.
- II. The Minimum Wages Act, 1948.
- III. Payment of Bonus Act, 1965.
- IV. Equal Remuneration Act, 1976.

The Payment of Wages Act, 1937 is a central act but its enforcement responsibility of the States. The Act specifies the standard wage period, payment day, permissible deductions, mode of payment, and inspection and applies to workers below a certain salary range. The Minimum Wages Act, 1948 is also a central act, with enforcement responsibility being vested in the States. Taken together, these wage related laws are alleged to contribute significantly to the problem of rigidity in the country's labour market.

For governing the **Working Conditions** the main acts include:

- I. The Factories Act, 1948.
- II. The Industrial Employment (Standing Orders) Act, 1946.
- III. The Contract Labour (Regulation and Abolition) Act, 1970.

The Factories Act, 1948 attempts to deal with the issues relating to health, safety and welfare of the workers in factories and plantation with more than 10 workers. The Industrial Employment (Standing Orders) Act, 1946 is applicable to the industrial units with 100 or more workers (excluding management) and it deals mainly with specification of working conditions in line with a 'model standing orders.' The aim of the Contract Labour (Regulation and Abolition) Act, 1970 is the gradual abolition of casual labour hiring, and where permitted, to regulate the working conditions of casual labour.

The principal laws relating to **Social Security and Insurance** are:

- I. The Workmen's Compensation Act, 1923.
- II. The Employee State Insurance Act, 1948.
- III. The Employees Provident Funds Act, 1952.

The Workmen's Compensation Act, 1923 specifies compensation that the employers need to pay on account of injury by accident at work site or occupational diseases. An important provision of the act is the liability of the principal employer in case of contract labour employment. The Employee State Insurance Act, 1948 extends to all factories under the Factories Act, and other commercial establishments employing 20 or more persons and to workers earning less than a certain salary limit within these. It requires contributions from both employers and employees to be paid for insurance against sickness, maternity, funeral,

and disablement. The Employees Provident Funds Act, 1952 is applicable primarily to factories and specifies deposit-linked provident fund or pension scheme. But coverage of workers by formal Social Security and Insurance programmes is extremely limited – applying to less than 10% of India’s labour force⁵⁴ (World Bank, 2006).

Some of the laws mentioned in the foregoing, along with a few others, are *in principle* applicable to the informal sector as well. However, except the Minimum Wage Act in the some states and some sectors, informal sector activities, for all practical purposes, remain unaffected by the existence of these laws. Furthermore, overwhelming majority of the labour laws has been enacted to address the relevant labour relations in the organized sector.⁵⁵

Thus, the way the laws are designed, they are applicable, to a very small proportion of the workforce, and well in the excess of 90 percent of the workers are hardly affected, in a *de facto* sense, by the legislations. Close to 97 percent of the informal sector enterprises employ less than 10 workers and the overwhelming majority among them have less than 5 (Chandra, 2006). If we look at the contemporary discourses on labour laws in India, it is almost never the case that one hears the employers in the informal sector complaining about any ‘rigidity’ in labour market.⁵⁶

Keeping such a backdrop in view, it seems difficult to make sense of the shrillness with which absence of flexibility in India’s labour market is bemoaned. Add to that the well-known problems relating to implementation in the informal sector, partly because of extremely inadequate infrastructure for enforcement, which largely go against labour, the argument seems almost surreal. In fact, as we have argued in the foregoing, the problem with more than 90 percent of India’s labour market is that of inadequate laws in the *de jure* sense and almost a picture of lawlessness in the *de facto* sense. Thus a huge challenge confronting policy-makers in India is: to design and implement a floor of labour rights, with a vision of a national labour market in view; such a vision, that clearly spells out a set of core labour standards, including a national minimum wage, ought to be on the front burner of the policy agenda, so that the informal sector, which contributes around 60 percent of NSDP and accounts for over 90 percent of employment, is made an integral part of the national market in terms of a set of well-conceived and easily implementable regulatory and protective provisions. Given the massive heterogeneity of the Indian economy, it is simply unrealistic and meaningless to think of legislations that would address specific needs of all the different sectors, (and for this purpose, there is no getting away from sector-appropriate legislations); however, surely, a core of labour standards can certainly be envisioned for the country as a

⁵⁴ See Table 5 for India’s labour force and unemployment etc, and Table: 6 for detail social security coverage, in the appendix.

⁵⁵ As Chandra puts it: ‘most pieces of labour legislation appear to keep most enterprises and most workers outside the ambit of law with the help of some number and wage filters. Hardly any enterprise in the informal sector can be netted within these laws’ (p 23). Table 7, reproduced from Chandra 2006, shows how these ‘wage and number filters’, with reference to most legislations, exclude the informal sector.

⁵⁶ As Chandra notes, ‘It is therefore not surprising that MSEs in UP could not normally perceive negative impact of labour legislation as a barrier to their growth (Singh et al). This has been found to be the perception of the employers in the unorganised sector in other states as well (Chandra and Parasher, 2005). The surmise of Goyal et al (2004) that demand for abrogation of dilution of labour standards thus emanate from the substantial employers and not really from small ones appears to have a very sound empirical basis (Chandra, 2006, p. 25).

whole. Based on size, specific attributes of a sector, and other aspects of heterogeneity, separate provisions obviously make eminent sense to address the key specificities.

We have already drawn attention to another key area in urgent need of reforms: which is, simplification and rationalization of the unnecessarily complex and unwieldy maze of the existing labour regulations. As mentioned earlier, a huge number of laws has been created, which cover the regulation of minimum wages, hours of work, benefits, safety, security, conditions of employment, dismissal, trade unions and other aspects of industrial relations, which are often characterized by contradictory mandates, inconsistencies in the basic definitions and concepts used, (such as appropriate government, factory, worker, workman, employee and employer, child labour, establishment, wages etc.). These complexities have been further compounded by long- drawn judicial trials to 'interpret' these laws, sometimes without a resolution of the contested issues. Therefore, unification and harmonization of labour laws must be taken up on a priority basis (Contributions to Debroy, 2005; FICCI-AIQE, 2006; Second National Commission, 2002; Pages & Roy, 2006; CII, 2006; CITU, 2006; among others).

Another key area that requires urgent attention is: improving the infrastructure and processes for the enforcement and implementation of labour laws.⁵⁷ Labour laws are frequently violated in the organised sector by employers (Sharma et al, 2004), and of course, the situation is abominable in the unorganised sector. Part of the problem, as stated earlier, has to do with the way the laws have been framed, and hence a careful review⁵⁸ to address such concerns will obviously be helpful. However, issues relating adequate infrastructure and appropriate institutions need careful consideration.⁵⁹

It is important to emphasize that much of the discussion on labour market reforms within the mainstream discourses remains trapped in a narrow zone: which is, the presumed 'rigidity' of the labour market in the country's organised sector and a couple of statutes relating to industrial relation – e.g. the Industrial Disputes Act (in particular its chapter VB), the Contract Labour (Regulation and Abolition) Act, and the Trade Unions Act – which are considered the villains in the story. However, as should be evident from the foregoing, it is extremely important to broaden the scope of this discussion beyond the current obsession with the 'rigidity-inducing' labour laws, and bring into sharper focus a number of other concerns relevant for labour market outcomes.

Apart from the issues already raised in this in this section, another critical area is that of social infrastructure. In particular, decent public provisioning of education and health for workers and their families ought to be accorded high priority; coupled with active labour market policies which emphasize investments in human capital, such measures can go a long way in improving outcome for the labour market as well as the economy in general.

⁵⁷ Violation of the Contract labour (regulation and Abolition) Act, 1970, has frequent been reported by researchers (e.g. Jha, 2005). The use of contract labour has increased substantially during nineties climbing from 15 to 25 percent of manufacturing labour force.

⁵⁸ Harmonization and standardization of laws will obviously go a long way in improving the atmosphere for implementation.

⁵⁹ For instance, tripartite dispute redressal mechanism may not be most desirable in several contexts. Wherever feasible, collective bargaining, which may contribute to a healthy labour-management relation, should be encouraged.

Furthermore, along with these, the provisions for social security, including guaranteed employment/ unemployment insurance,⁶⁰ should be high on the agenda of labour market reforms. It should be immediately obvious that the costs towards ensuring the above noted measures have to be substantially, if not entirely, underwritten by the State. Making individual employers responsible for these investments and initiatives is theoretically meaningless and practically a non-starter.

As of now, the overwhelming bulk of the labour force in the country is largely untouched by these concerns. A move forward means putting them on the front burner. Part of the reason for India being stuck on a 'low road' of the economic transformation has to do with the neglect of such concerns. We may close this section by listing the key issues, in the context of the reform of labour laws and labour market, which require urgent attention of the policy-makers. Most of these have already figured in our earlier discussion, but it may be useful to have a set of summary recommendations.

- Streamlining and simplification of labour laws should be addressed on a priority basis. There has been a consensus amongst academics and activists along the entire ideological spectrum on the need for doing so for some time now. Existing laws should be broadly grouped into four or five categories, such as industrial relations, wages, social security, safety, welfare and working conditions etc. (or some other appropriate typology). As has been frequently suggested, various labour laws should be integrated into one single 'Labour Code', and the draft of such a 'Labour Code' presented by the Indian Labour Law Association in 1994, already provides a strong foundation.
- While undertaking simplification and rationalisation, the problem, that most of the laws are quite old and often anachronistic, will obviously need to be addressed. A vision of a process of economic transformation that generates decent and productive employment should be the broad framework, within which rationalisation of labour laws needs to be located. Further, appropriate enforcement mechanisms have to be put in place so that the transaction costs for firms and rents for enforcement agencies are minimised, while workers are ensured the designed benefits.
- In the existing laws, basic definitions (e.g. workers, employees, industry, child labour, establishment, appropriate government etc.) are full of ambiguities, which must be removed at the earliest.
- Although the Minimum Wage Act, the Equal Remuneration Act, the Contract Labour Act, and even the IDA, are applicable to substantial sections of unorganised labour, the sheer practical difficulties and high costs associated with implementation and enforcement of such legal provisions ensures that most workers do not benefit from them. Again, this reinforces the need for rationalisation of the existing laws.
- Linked to the preceding points is the provision of a set of 'core labour standards' which we as a society have already accepted, (for instance, through our Constitution, ratification of the ILO treaties etc.).

⁶⁰ National Rural Employment Guarantee Act, in spite of its limitations including limited coverage, is a most laudable initiative in this regard.

- The rationale for fixing minimum wage should be based on unanimous recommendations of 15th Indian Labour Conference. Minimum wage payable to anyone, in whatever occupation, should be such that it satisfies the basic needs of the worker and her/his family. There should be a national minimum wage that the central government may notify, and it must be revised periodically. The recommendation of the Second National Labour Commission (2002) that the minimum wage rate be revised every two years may be implemented.
- Most of the laws should be 'Central Laws' and must cover all types of workers (both from organised and unorganised sectors), so that it can be implemented universally within the country.
- Given the country's federal structure, it is not possible to eliminate the multiplicity of authorities completely, but it must be rationalized and robust mechanisms for efficient coordination between multiple authorities should be accorded the importance that it deserves.
- Legal provisions to ensure greater attention to the investments in human capital of workers have been hitherto a seriously neglected area. Lessons from the East Asian countries may be instructive, as initial steps, in this regard.
- Formal education always does not match with the industrial requirements. Laws may be put in place which encourages industries to assist in skill development of the workers. There is a need to revamp the existing technical and vocational training courses in cooperation with the concerned Industry Associations.
- As discussed earlier, there is very small part of the country's labour market, namely the organised sector, which is relatively inflexible. Attempts to increase flexibility in this segment, wherever desirable, must be accompanied by social security measures. For instance, expanding unemployment insurance and/ or other support measures including training and skill upgradation for alternative employment options, under the social security laws would seem a necessary step if a change in the IDA provisions with respect to retrenchment and lay-off are being contemplated.
- Absence of social security provisions has been among the biggest problem towards efficient functioning of India's labour market. Recent proposal of NCEUS, aimed at social security for unorganised workers may be seen as an important first step in this regard.
- The enforcement infrastructure and processes are extremely weak in India, which need to be addressed, at different levels, and on an urgent basis.
- The existing mechanisms for dispute resolution are extremely tardy and time-consuming. One innovative way to deal with the problem has been to set up Alternative Dispute Redressal mechanisms, which can speedily dispose the pending cases. Fast track courts, including Lok Adalats, have been in existence for close to a couple of decades; based on a through review of such experiences, appropriate legislations may be put in place.
- Sometimes, one hears the argument that specific areas, such as Special Economic Zones, should be out of the coverage of labour laws; such arguments are simply ludicrous and absurd. Such a demand was rightly rejected by the Second Labour Commission on Labour.

- In recent times, there has been much talk about ‘self-certification’. Sure enough, where feasible, such ideas may be experimented with, but as part of system of well-organized system of regular inspection, and should not become an excuse for non-compliance of labour laws. Independent auditors, for instance, could be roped in, to monitor self-certification process.
- Transparency, simplicity, effective implementability etc. are obviously the key operational issues in any system of labour legislation, and must be addressed. However, prior to the issues related to monitoring, one has to necessarily, be clear about the basic vision that forms the foundation of such legislations; the core of such a vision must be right-based, where workers have rights as workers and as citizens.

It is interesting to note that there is substantial agreement on most of the above-noted concerns, as should be evident from the responses received by the NCEUS from the representatives of the trade unions as well as spokespersons of the industries (Chandra 2006; Contributions in Debroy (ed), 2005; FICCI-AIQE, 2006; Second National Commission (2002); Pages & Roy, 2006; Shankaran (2006); CII, 2006; CITU, 2006; among others). Obviously, to move forward, areas of consensus ought to be the first steps.

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Appendix

Table 1: Standardized Unemployment Rates by Gender and Age in 2003

	Male		Female	
	15-24	25-54	15-24	25-54
Liberal OECD Countries				
US	12.9	4.6	11	4.6
Australia	12.2	3.9	11.1	4.3
Canada	14.9	6.1	11.8	5.9
Ireland	8.7	4.5	7.4	3.1
New Zealand	8.7	2.5	10.1	3.3
UK	11.8	3.8	9.9	3.4
Average	11.5	4.2	10.2	4.1
High Unemployment European Countries				
Belgium	15.8	6	19.5	7.4
Finland	22.2	7	19.4	7.6
France	20.8	7.4	22	9.8
Germany	13.3	9.8	9.7	9
Italy	20.7	5.2	27.2	9.2
Spain	18.7	6.9	26.4	13.8
Average	18.6	7.1	20.7	9.5
Lower Unemployment European Countries				
Austria	11.3	4.3	10.7	4.4
Denmark	8.5	4.4	7.1	5.1
Netherlands	7.9	3.7	8.1	4.4
Norway	12.6	4.3	10.7	3.3
Sweden	17.8	5.7	16.1	5.2
Switzerland	8	3.5	7.3	4.6
Average	11.0	4.3	10	4.5

Source: OECD, 2005: Statistical Appendix, Table C.

Table 2: Ten Major States: Wages and net value added in the factory sector compared in selected years, 1980-81 to 1997-98

Year	(Wage Per Worker / Value Added Per Worker)*100 (%)				% Change in 1997-98 over 1980-81
	1980-81	1985-86	1990-91	1997-98	
Assam	24.8	12.8	11.1	27.4	10.5
Bihar	49.5	35.5	33.1	14.8	-70.0
Madhya Pradesh	26.5	23.1	20.0	17.6	-33.6
Maharashtra	28.0	25.3	23.8	18.9	-32.5
Orissa	42.8	44.7	22.0	18.8	-56.1
Punjab	21.3	30.3	30.0	25.0	17.2
Rajasthan	28.7	32.8	24.5	15.8	-45.0
Tamil Nadu	31.4	30.6	24.0	26.7	-14.9
Uttar Pradesh	41.9	43.0	26.9	19.5	-53.3
West Bengal	47.1	48.3	42.0	30.9	-34.4

Source: Computed by Debdas Banerjee (2005) from CSO, ASI Factory Sector.

Table 3: Regression exercises for the relationship between employment, product wages and output growth (Dependent Variable: employment)

Industry	Coefficient for product wage	Coefficient for gross real value of output	R ²
Food and food products	0.31 (10.6)	0.24 (12.02)	0.91
Cotton textiles	0.25 (0.7)	-0.11 (2.6)	0.32
Textile products	0.27 (2.51)	0.33 (2.27)	0.99
Leather and leather products	0.41 (1.93)	0.18 (1.54)	0.95
Chemicals	-0.05 (0.57)	0.23 (4.76)	0.97
Rubber, plastic, petroleum and coal	0.47 (4.29)	-0.09 (0.64)	0.96
Non-metallic mineral products	0.39 (3.2)	-0.09 (2.02)	0.74
Metal products	0.14 (1.04)	0.1 (1.6)	0.87
Machinery and equipment	0.1 (1.14)	0.04 (0.04)	0.82
Transport equipment	0.25 (2.11)	-0.05 (-0.88)	0.53

Note: Figures in brackets are t values. Employment figures include 'casual workers' but not subcontracted workers; calculated from data from Annual Survey of Industries.

Source: Reproduced from Ghosh (2004).

Table 4: Social Security Expenditures in Europe (2001)

	Continental		Northern		Anglo-Saxon		Southern	
	% of GDP	% of Total Exp	% of GDP	% of Total Exp	% of GDP	% of Total Exp	% of GDP	% of Total Exp
Social Assistance	0.95	3.32	1.67	5.97	1.73	6.93	0.18	0.79
Family	2.88	10.14	2.36	8.41	2.26	9.07	0.82	3.65
Pensions	12.33	43.32	11.14	39.72	11.31	45.28	12.92	57.36
Non-Employment Benefits	12.29	43.23	12.87	45.91	9.67	38.73	8.60	38.19
Total	28.45	100	28.05	100	24.98	100	22.52	100

Source: Reproduced from Tito Boeri (2002)

Notes: figures weighted by GDPs. The country groups are defined as follows: **Continental**, Austria, Belgium, France and Germany; **Northern**, Denmark, Finland, The Netherlands and Sweden; **Anglo-Saxon**, Ireland and United Kingdom; **Southern**, Greece, Italy, Portugal and Spain.

Source: EUROSTAT, Esspross Database (2001)

Table 5: Population and Labour Force (in millions, UPSS)

	1983	1993-94	1999-00	2002*	2004*
Total Population	719.6	894.2	1005.3	1050.6	1087.1
Population, 15-59	387.0	517.5	580.2	612.6	648.8
Male	196.4	264.9	295.9	314.3	335.5
Female	190.5	252.5	284.4	298.3	313.2
Labour Force (UPSS),15-59	270.6	335.8	370.0	387.7	399.4
Male	181.8	228.8	257.1	272.5	285.3
Female	88.8	107.0	112.9	115.2	114.2
Work Force (UPSS), 15-59	265.0	328.5	360.9	379.5	n.a.
Male	177.4	223.4	250.1	265.9	n.a.
Female	87.7	105.0	110.7	113.6	n.a.
Unemployment Rate (%) (CDS)	8.3	6.0	7.2		9.0
Unemployment Rate (CWS)					
Rural Male	3.7	3.0	3.9	2.8	4.7
Rural Female	4.3	3.0	3.7	1.6	4.5
Urban Male	6.7	5.2	5.6	5.5	5.7
Urban Female	7.5	8.4	7.3	5.7	9.0

Source: Sundaram and Tendulkar, 2005; World Bank Staff calculations from NSS; World Bank Staff calculations using ILO Laboursta data base; NSS 60th round Report and Economic Survey various issues.⁶¹

Notes: **UPSS**: Employed on Principle and Subsidiary Status, **UPS**: Employed on Principle Status, **CWS**: Workers in Current weekly activity status, **CDS**: Workers in Current daily activity status.

⁶¹ Reproduced from World Bank 2006.

Table 6: Coverage rates of Social Insurance for Organised and Unorganised Sector, 2004

	Organised Sector (%)	Unorganised Sector (%)
Public Schemes		
Employees' Provident Fund	25.1	0.18
Employees' Pension Scheme	12.2	0.02
Government Pension Scheme	48.7	0.24
Government Provident Fund	54.0	0.21
Contributory Provident Fund	4.0	0.02
Any Formal Pension Coverage	Around 95%	Less than 1%
Commercial Schemes		
Life Insurance (endowment)	54	23
Personal Accident Insurance	3.6	1.2
Private Health Insurance	2.0	0.5
Non-General Insurance	2.8	1.4

Source: O'Keefe (2005) based on MoF/ADB Pension Survey, 2004.

Table 7: Major Labour Laws and their Applicability

Sl. No.	Laws related to Industrial Relations	Applicability Criterion (Number Filter)
1	The Industrial Disputes Act, 1947	Generally applicable to all establishments (limitations are Chapter V A) (Lay Off and Retrenchment not applicable to establishments of seasonal nature or less than 50 workers; VB (Provisions relating to lay off, Retrenchment and closure in certain establishments applies to establishments with 100 or more workers)
2	The Industrial Employment (Standing Orders) Act, 1946	100 or more, State Amendments Karnataka, West Bengal, Gujarat and Tamil Nadu the no. of workers is more than 50, in UP this limit is further reduced and all the factories under section 2m are covered i.e., 10 workers with power or 20 without power.
3	The Payment of Wages Act, 1936	Applicable to Factories
4	The Minimum Wages Act, 1948	One or More employees in any scheduled employment where min wage rate have been fixed under this act
5	The Payment of Bonus Act, 1965 The Payment of Bonus Rules, 1975	Where 20 or more workers are employed inclusive of those also who are drawing more than Rs. 1600 per month. The establishment shall continue to be governed by this act notwithstanding that the number of persons employed therein falls below 20.
6	The Factories Act, 1948	10 or more workers on any manufacturing activity with the aid of power, and 20 or more workers working without any aid of power.
9	The Contract Labour (Regulation & Abolition) Act, 1970	Applies to all establishments where 20 or more workmen are employed Applies to contractor employing 20 or more workmen
10	The Workmen's Compensation Act, 1923	Applicable to all establishments
11	The Employee's State Insurance Act, 1948	In the first Instance to the Factories and could be extended to other establishments with due process.
12	The Employees' Provident Fund & Miscellaneous Provisions Act, 1952	To every establishment which is a factory and in which twenty or more persons are employed
13	The Shops and Establishments Act	Applies to every shop and establishment, not registered under Factories Act
14	The Maternity Benefit Act, 1961	Applies to every shop and establishment employing 10 or more persons are employed
15	The Equal Remuneration Act, 1976	Applicable to all establishments
16	The payment of Gratuity Act, 1972	All factories and establishments where ten or more persons are employed

Source: Chandra 2006, p 27.

Table 8: Labour Market Flexibility across States

State	Besley-Burgess (2004) based measure	Investment Climate Study (World Bank, 2005)
Andhra Pradesh	Flexible	Good
Assam	Inflexible	...
Bihar	Inflexible	...
Gujarat	Inflexible	Best
Haryana	Inflexible	...
Karnataka	Flexible	Good
Kerala	Flexible	Poor
Madhya Pradesh	Inflexible	...
Maharashtra	Inflexible	Best
Orissa	Inflexible	...
Punjab	Inflexible	Medium
Rajasthan	Flexible	...
Tamil Nadu	Flexible	Good
Uttar Pradesh	Inflexible	Poor
West Bengal	Inflexible	Poor

Source: Besley Burgess (2004) & Investment Climate Study (World Bank, 2005); Reproduced from Anant et al.

Table 9: Some of the recent incidences of brutality on workers & Violation of Labour Laws

Date	Place/ Company	Incident/Accident	Type of Violation of Labour laws/ Rights
September 10, 2004		Brutal repression on the peaceful struggle of workers demanding payment of minimum wages in Banihal. One died in the police firing and 45 workers were injured in the police action.	
October 2, 2004	The Hindustan Times	The Hindustan Times management has sacked 362 permanent employees on and victimised several others.	Without seeking mandatory permission of the state government under Industrial Dispute Act,
07.12.2005	Vishwas Nagar, New Delhi	12 workers were burnt to death in a government factory. The workers couldn't escape as they were locked from outside.	1. Inhuman working conditions of lakhs of workers. 2. Managements violate safety norms with impunity.
March 27, 2006	Visakhapatnam district, Andhra Pradesh	The fishermen were demanding the government not to displace them from the sea and pay them fair compensation and assure employment. The police resorted to brutal repression on fishermen.	
June 2, 2006	Sitarganj block in Udham Singh Nagar district of Uttarakhand	Attack on Kisan Sabha leaders and activists, including large number of women in Shakti Farm under	
Mid of July, 2006	Chamera III hydro-electric project in Chamba district, HP	3 workers were killed. A number of protesting workers were arrested. A local leader was tortured in the police custody.	1. workers were getting very low wages. 2. various other labour norms are being violated frequently.
July 25, 2005	Honda Motorcycles & Scooters India Private Limited (HMSI), Haryana	The exploited workers, who are also victims of blatant denial of basic trade union rights, were subjected to the inhuman brutality of the police.	

Source: Various national dailies and other sources.

Table 10: Population, Labour Force, and Employment, 1980–2002 (in millions)

	1980	1990	1995	2000	2001	2002 (Est.)
Population	987.1	1143.3	1211.2	1265.8	1276.3	1284.5
Urban	191.4	301.9	351.7	458.4	480.6	502.1
Rural	795.7	841.4	859.5	807.4	795.6	782.4
Urban (percent of total)	19.4%	26.4%	29.0%	36.2%	37.7%	39.1%
Rural (percent of total)	80.6%	73.6%	71.0%	63.8%	62.3%	60.9%
Working Age Population (15 – 64)	594.1	763.1	829.0	888.0	894.3	903.0
Labour Force^a	429.0	653.2	687.4	739.9	744.3	751.3
Participation Rate (in percent) ^b	72.2	85.6	82.9	83.3	83.2	83.2
Employment^c	423.6	647.5	680.7	720.9	730.3	737.4
Unemployment^d	5.4	5.7	6.7	19.1	14.1	13.9
As percent of total labour force	1.3%	0.9%	1.0%	2.6%	1.9%	1.9%
As percent of urban labour force	4.9%	3.2%	3.4%	7.6%	5.6%	5.3%
Urban						
Employment	105.3	170.4	190.4	231.5	239.4	247.8
Unemployment						
Registered	5.4	3.8	5.2	6.0	6.8	7.7
Laid-off workers (xiagang) ^e	....	....	....	9.1	7.4	6.4
Registered unemployed and xiagang	....	....	....	15.1	14.2	14.1
Unemployment rate (in percent)						
Registered	4.9%	2.5%	2.9%	3.1%	3.6%	4.0%
Registered unemployed and xiagang ^f	....	....	....	6.0%	5.6%	5.4%
Rural						
Employment	318.4	477.1	490.3	489.3	490.9	489.6

Source: Estimated by Brooks and Tao (2003) from *China Statistical Yearbook*, various years; and CEIC database.

- a. From the labour force survey, defined as economically active persons 16 years and older, either working one hour or more in the reference week or looking for work.
- b. Labour force as percent of working age population. Data for the working age population defined consistent with the labour force (16 years and older) are not available.
- c. From the labour force survey, defined as those working for one hour or more in the reference week.
- d. Defined as difference between labour force and employment.
- e. Those *xiagang* remaining attached to re-employment centers, at the end of the year.
- f. Calculated as percent of the urban labour force.

Table 11: Employment by Enterprise Ownership, 1980–2002

	1980	1990	1995	2000	2001	2002 (Est.)
(In million at the end of the year)						
Total Employment	423.6	647.5	680.7	720.9	730.3	737.4
Urban Employment	105.3	170.4	190.4	231.5	239.4	247.8
State units	80.2	103.5	112.6	81.0	76.4	75.1
<i>Of which:</i> SOEs	67.0	73.0	76.4	43.9	39.5	...
Institutions	22.0	21.6	26.1	26.4	26.2	...
Governments	4.7	8.9	10.1	10.7	10.7	...
Collectively owned	24.3	35.5	31.5	15.0	12.9	12.5
Joint units ^a	0.0	1.0	3.7	13.4	15.2	...
Foreign funded ^b	0.0	0.7	5.1	6.4	6.7	...
Private units	0.8	6.7	20.6	34.0	36.6	...
Residual	0.0	23.1	16.9	81.6	91.6	...
Rural employment	318.4	477.1	490.3	489.3	490.9	489.6
TVEs ^c	30.0	92.7	128.6	128.2	130.9	133.0
Rural privately owned	...	1.1	4.7	11.4	11.9	...
Self-employed	...	14.9	30.5	29.3	26.3	...
Residual	288.4	368.4	326.4	320.4	321.8	...
(In percent of total)						
Urban Employment	100.0	100.0	100.0	100.0	100.0	100.0
State units	76.2	60.7	59.1	35.0	31.9	30.3
<i>Of which:</i> SOEs	63.7	42.8	40.1	19.0	16.5	...
Institutions	20.9	12.7	13.7	11.4	10.9	...
Governments	4.4	5.2	5.3	4.6	4.5	...
Collectively owned	23.0	20.8	16.5	6.5	5.4	...
Joint units ^a	...	0.6	1.9	5.8	6.4	...
Foreign funded ^b	0.0	0.4	2.7	2.8	2.8	...
Private units	0.8	3.9	10.8	14.7	15.3	...
Residual	0.0	13.6	8.9	35.3	38.3	...
Rural employment	100.0	100.0	100.0	100.0	100.0	100.0
TVEs ^c	9.4	19.4	26.2	26.2	26.7	27.2
Rural privately owned	...	0.2	1.0	2.3	2.4	..
Self-employed	...	3.1	6.2	6.0	5.4	...
Residual	90.6	77.2	66.6	65.5	65.6	...

Source: As estimated by Brooks and Tao (2003) from *China Statistical Yearbook*, various years; and CEIC database.

- a. Joint owned, limited corporations, and shareholding units.
- b. Includes Hong Kong SAR, Macao SAR, and Taiwan Province of China funded.
- c. Town and village enterprises.

Table 12: Employment by Different Sectors

	1980	1990	1995	2000	2001
	(In millions)				
Primary	291.2	389.1	355.3	360.4	365.1
Secondary	77.1	138.6	156.6	162.2	162.8
Tertiary	55.3	119.8	168.8	198.2	202.3
Non-agricultural	132.4	258.4	325.4	360.4	365.1
	(In percent)				
Primary	68.7	60.1	52.2	50.0	50.0
Secondary	18.2	21.4	23.0	22.5	22.3
Tertiary	13.1	18.5	24.8	27.5	27.7
Non-agricultural	31.3	39.9	47.8	50.0	50.0

Source: As estimated by Brooks and Tao (2003) from *China Statistical Yearbook*, various years; and CEIC database.

Table 13: Decreasing Employment Elasticity

		Employment Growth	Employment Elasticity
1980- 1990	Primary Industry	2.8	0.45
	Secondary Industry	5.9	0.62
	Tertiary Industry	7.9	0.65
	Total	4.1	0.44
1990-2000	Primary Industry	-0.8	-0.21
	Secondary Industry	1.6	0.12
	Tertiary Industry	5.1	0.56
	Total	1.1	0.11

Source: Zhu (2007)

Table 14: Graduates from higher education institutes, employment ratio, employment (10000 or %)

	Total Graduates	Employment Ratio	Unemployed
2000	107	86.39%	30
2001	115.02	89.40%	34.5
2002	145	85.00%	52
2003	212	83.00%	70
2004	280	73.00%	75
2005	338		

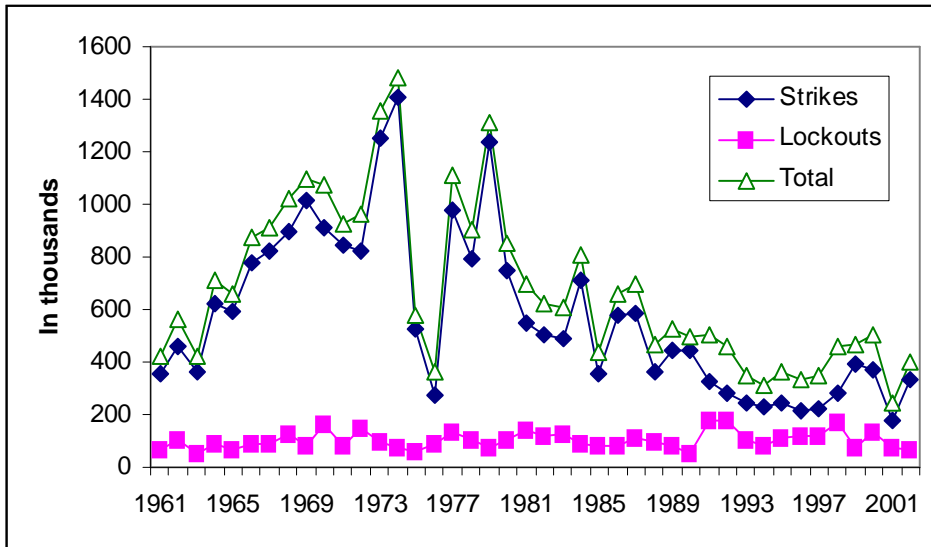
Source: Zhu (2007)

Table 15: Some Labour Related Statistics, 1981-2001 (percent)

	6 th Five Year Plan (1981-85)	7 th Five Year Plan (1986-90)	8thFive Year Plan (1991-95)	9 th Five Year Plan (1996-00)	1981-1995	1996-2001
SOE employment Growth	2.34	2.85	1.72	-6.15	2.3	-6.08
City Collective enterprise employment growth	6.64	1.33	-2.33	-13.14	1.88	-13.26
Staff and workers employed by manufacturing sector, growth	3.2	2.81	0.51	-9.42	2.17	-9.03
Total staff and workers, growth	3.43	2.62	1.19	-5.29	2.41	-5.1
Total employment growth	3.32	5.51	1	1.15	3.28	1.18
Share of employment in formal sector	97.89	93.12	81.02	60.67	90.68	58.07

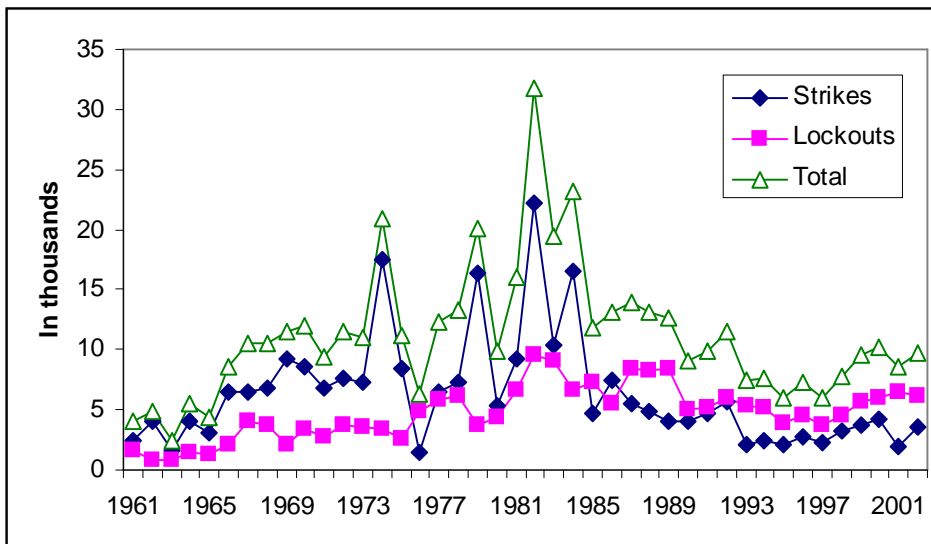
Source: Zhu (2007).

Figure 1: Number of Workers Involved in Disputes, 1961–2002

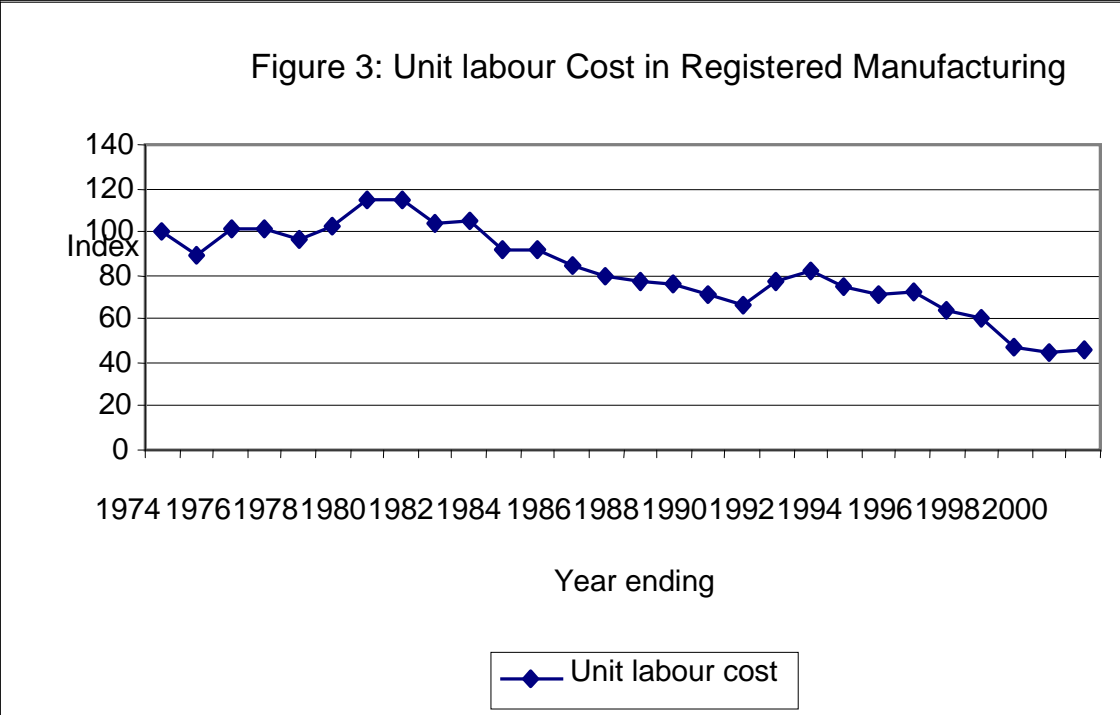


Source: Ministry of Labour, Government of India; (Reproduced for P. Mahapatra).

Figure 2: Number of Person-Days Lost in Disputes, 1961–2002

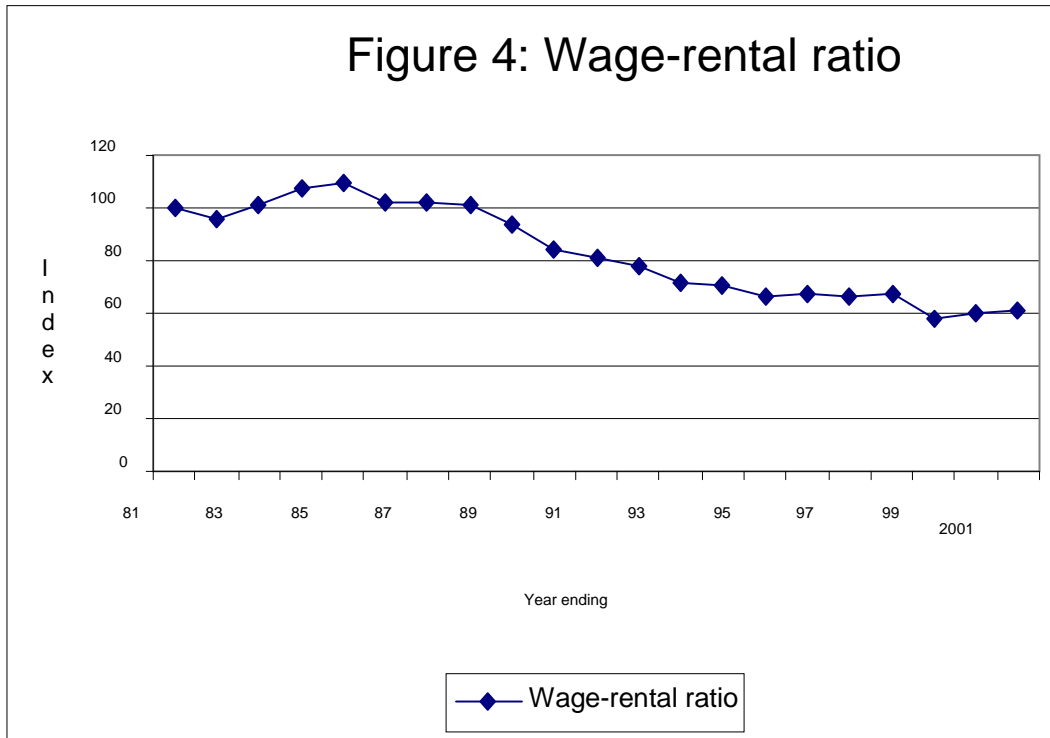


Source: Ministry of Labour, Government of India; (Reproduced for P. Mahapatra).



Source: Nagraj (2007)

Figure 4: Wage-rental ratio



Source:

Nagraj (2007)

Box: 3 The public pension system

“Urban workers

Three pension tiers, of which the first two are mandatory for employees in all enterprises, but voluntary for the self-employed. Transitional rules for those who contributed before 1997.

First tier: A pay-as-you-go defined-benefit programme

Financing: Employer contributions vary around a national standard of 20%, of which 17 percentage points for the first tier. Pooling mostly at prefecture (city) level, sometimes by province or by county.

Benefits: After at least 15 years of work, the benefit is 20% of the local average wage. The pension age is 60 (men) and 50 (most women). No first-tier benefits with under 10 contribution years.

Second tier: A defined-contribution programme with individual saving accounts

Financing: Employee contributions, now usually 7% of the wage, to be raised to 8%. In addition, 3 percentage points of the employer contribution go to the individual accounts.

Administration: The government can either invest the money, mostly in bank accounts and bonds, or use it on a pay-as-you-go basis. In the latter case, which is most common, the government pays a certain rate of interest to the notional accounts.

Benefits per month: 1/120 of the fund as accumulated on retirement. Thus, the programme assumes an average life expectancy of 10 years on retirement, but pensions are paid until death.

Workers who stop contributing after less than ten years in a locality (pooling unit) can withdraw the individual accounts. But they receive no first-tier pensions.

Third tier: Voluntary pension saving

Mostly enterprise pensions for employees.

Rural workers

Entirely voluntary saving, possibly with some support from communities. Benefits according to the accumulation on individual accounts.”

Source: (Reutersward, 2005)

Box 4: Social insurance on special conditions for rural migrants: two examples

“**Chengdu, Sichuan** introduced an optional low-cost insurance package for migrants in March 2003, covering second-tier pension insurance, work injury insurance and basic medical insurance (hospitalisation).

Flexible contributions calculated on a “base wage”, defined as the previous year’s average wage in the city times one of the following multiples: 60%, 70%, 80%, 90%, 100%, 120%, 150%. The employer chooses a multiple for each worker, with effects on benefits as well as on contributions.

The contribution rate, applicable to the chosen “base wage”, is 14.5% for the employer and 5.5% for the employee. For the self-employed, it is 20%.

At the end of 2003, this scheme covered 84 000 workers, or 10% of the rural migrants in Chengdu.

Note: For urban workers in Chengdu, the standard contribution rates for pension, work injury and medical insurance are, respectively, 20%, 0.6 to 2% and 7.5% for employers and 8%, 0% and 2% for workers. In other words, rural migrants and their employers contribute at about half of the rates that apply to urban workers.

Chengdu also gives employers in the urban private sector a 3 percentage-point rebate on their pension contributions, down to 17%. This affects the city’s revenues to the pay-as-you-go first tier, not the individual accounts. Such workers get the full insurance package despite the rebate.

Xiamen, Fujian offers reduced contributions to rural migrants and their employers in the standard social insurance. Contributions are then calculated on the basis of the city’s minimum wage, and employers are offered an 8 percentage point rebate on the pension contribution rate, down to 6% compared with Xiamen’s standard rate of 14%. The employee contribution rate (for second-tier pensions) is the same as for urban workers: 8%.

The rebate only affects the city’s revenues in the first-tier pay-as-you-go pension scheme.”

Source: (Reutersward, 2005)