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IN INDIA**

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Summary

This paper traces the evolution of labor market institutions in India since Independence. The primary concern of the worker in the organized sector in India is job security. The labor in the organized sector is unionized. The unions, which operate through the different political parties, have over the years, succeeded in establishing a legal regime where employers need the prior permission of the Government before retrenching a worker. Such permissions are almost impossible to get, given the compulsions of competitive politics in the country. These laws make it difficult for an industrial firm to respond quickly to technological changes or changes in the market environment. In the public sector, there are additional problems, because important decisions concerning labor-use are not made at the enterprise level. The Government sets down uniform norms to be followed by all public sector enterprises, irrespective of their own economic interests.

It is argued in this paper that these labor laws and procedural norms have, in the past, hindered the growth of labor-intensive industrialization in India. India's current effort at economic reforms are being adversely affected by its inability to initiate institutional changes in these fields.

Labor Markets as Social Institutions in India
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“Wage rates and jobs are not exactly like other prices and quantities. They are much more deeply involved in the way people see themselves, think about their social status, and evaluate whether they are getting a fair shake out of the society...Social institutions define acceptable and unacceptable modes of behavior in the weighty context like the labor market” Solow (1990).

I. Introduction

Robert Solow described the labor market as a social institution. However, as Solow acknowledges, the idea is not new. Alfred Marshall, the great exponent of the principles of demand and supply, spoke of “fair rates of wages” when he analyzed the working of the labor market in the 1920’s.’ Several other economists and social scientists working in the field of industrial relations have noted the importance of social norms in understanding the working of the labor market.² In fact, empirical studies on industrial organization clearly reveal widely differing characteristics in the working of labor markets, even among the mature capitalist economies of Western Europe, North America and East Asia.³ These differences have much to do with the varied historical experiences and cultural traditions of these societies. They manifest themselves in the working of what Solow called “norm-guided behavior” or the determination of wage rates and labor standards in different economies.⁴ Moreover, in many cases non-market

institutions have developed that now influence the working of the labor market directly. The case of the economy-wide apprentice program, established in Germany, is particularly notable. This program not only helps in the development of required skills like on-the-job training, it also creates a formal link between job-seeking workers and potential employers.'

The purpose of this paper is to discuss the emergence of institutions - that is, social, political and legal arrangements - that govern labor-use in the modern sector of the Indian economy. These institutions have developed in response to the demands of modernization and industrial development of the economy in the twentieth century, particularly after Indian Independence in 1947. The political process, which gave independent India its Constitution as well as the legal and administrative framework for governance, also played a decisive role in the creation of labor market institutions. This process also established new norms of behavior in the working of these institutions. However, the manner in which these institutions have evolved has introduced a new set of rigidities which are often inimical to productivity growth, skill formation and learning processes. This is particularly true in the public sector; this sector accounts for a substantial fraction of modern manufacturing industries, financial institutions and facilities like transport, communication and power in India.

Economists and policy-makers understandably attach a great deal of importance to capital formation in the development strategy of a backward economy. However, since the publication of Solow's seminal work,⁶ both theorists and empirical researchers working on the processes of economic growth have come to believe that it is not so much the pace of capital accumulation or the expansion in the quantitative base of the factors of production, but the ability of an economic organization to squeeze more out of given resources that explains much of the

performance of a growing economy. Exogenous technical progress alone, however, does not explain all the growth in productivity. The ability of workers and managers to adapt to new and efficient ways of performing their tasks is also important. Contractual arrangements for hiring, firing and wage determination, by creating incentives for workers to perform well, in turn influence this learning process.' This is how labor-market institutions come to play an important role in influencing the pace of economic development.

The agrarian and the informal sectors of the economy, where most people in India find gainful employment, has, by and large, remained outside the reach of modern labor laws and labor-market institutions. Therefore, the focus of this paper is on the organized sector of the Indian economy. The organized sector employs only about eight percent of the total labor force in India, but consists of all establishments in the public sector and all non-agricultural establishments in the private sector employing ten or more workers. The labor market in the organized sector is governed through legislative, administrative and political measures. The main thrust of economic reforms pursued in India today is directed towards this sector. Therefore, the success of reforms crucially depends on the possibilities of restructuring it, particularly its practices regarding the use of labor and other inputs.

It will be argued here that the institutional framework in which hiring, firing and the working conditions of workers and managers are determined in India has greatly influenced the performance and growth of Indian industries. This framework has discouraged employers from adopting more labor-intensive technology in organized industries, and has reduced the incentives for the workers to improve their productivity. Consequently., the industrial development of India during the last four decades has been accompanied by low rates of growth in total factor

productivity. In fact, compared to the fast-growing economies of East Asia, productivity growth in India has been quite dismal.' Research work with plant-level data has revealed that the amount of time taken by Indian workers and their managers to master new technology has sometimes been even higher than the economic life of new machines.⁹

After this introduction, the paper proceeds as follows: Section II presents a brief description of the Indian labor markets. Section III outlines the evolution of legal, administrative and political framework that governs labor use in the organized sector. Section IV discusses the Industrial Dispute Act, which is the single most important piece of legislation affecting labor-use in organized industries. Section V discusses the process of wage determination in the organized sector. The paper concludes with some remarks on the impact of labor market institutions on the Indian industries and on the importance of the reform of these institutions in the context of the ongoing economic reforms in India.

II. Indian Labor Market

Compiling employment statistics for the Indian economy is difficult. It is because about two-thirds of the Indian labor force¹⁰ finds employment in agriculture and rural industries. There is no official machinery for taking census of labor force and employment in the rural economy. Moreover, many people are self-employed. In these cases the duration of work, and even the intensity of efforts, vary considerably creating a syndrome of disguised unemployment. In such a situation, there are difficult conceptual problems in identifying the employment status of a person at any point of time. Therefore, estimates of rural employment are dependent on

variable concepts and definitions used in compiling employment statistics. ¹¹

Updated information is available for the organized sector, that is, for all the public sector units, for the nonagricultural private sector units that employ at least ten workers and for the plantations. In the public sector the nature and the duration of employment is easy to measure, because the agencies of the government are required to specify clearly the terms and the conditions of work for their employees. Plantations and the non-agricultural private sector units that employ ten or more workers come in turn under the Factory Act laws governing trade, transport or services. Accordingly, they are required to file annual returns on the various aspects of their activities, including the number of workers of different categories employed by them, to the appropriate regulatory authorities of the government. The Labor Ministry of the Government of India compiles and publishes these data.”

For the rest of the economy, there are no censuses to provide complete information. One necessarily needs to rely on sample surveys. The most reliable and comprehensive surveys are those conducted every five year by the National Sample Survey (NSS) of the Government of India. These are two-stage, stratified, random samples of households in India. The first stage of the survey picks up a sample of villages or settlements, and the second stage, households within these settlements. Much of India’s economic statistics, such as those relating to consumer behavior, demographic characteristics, employment and earnings, etc., **come** from the NSS.

The data presented in Table 1 are based on these two sources. The employment statistics relating to the **organized** sector is based on complete enumeration and compiled by the Ministry of Labor, Government of India. The data relating to the various unorganized sectors of the economy are estimates based on the sample surveys conducted by the NSS. **The totals are the**

sums of census information and survey estimates.

Table 1 indicates that out of the total labor force of 302 million, only about 24 million are employed in the organized sector of the economy. This is about 8 percent of the labor force. Of these 24 million employed in the organized sector, nearly 17 million (or about 70 percent) are in the public sector. Within the public sector more than half of the people are employed in the service sector, which consists mainly of public administration and defence services. Of the 7.3 million people working in the organized private sector, about 4.4 million (or 60 percent) are employed in manufacturing. Table 1 also reveals that of the various industry groups only mining, quarrying and electricity generation belong predominantly to the organized sector, the rest are predominantly unorganized. Further, over two-third of the Indian labor force are engaged in agriculture, which, except for the plantations in the organized sector, consists essentially of peasant farming.

The Indian development strategy 'since Independence has emphasized the importance of industrialization and modernization. This development strategy, spelt out clearly in the successive Five-Year Plans since the early fifties, has assigned special roles to modern large-scale industries, particularly the industries belonging to the public sector. These industries were supposed to play the role of the "leading sector" in India's quest for growth and development.¹³ The organized sector in Table 1, more or less represents this "leading sector". It is clear that even four decades after the initiation of this development process, the organized sector has failed to provide gainful employment to even a tenth of India's labor force. An attempt is made in the subsequent sections to show that the labor market institutions in the organized sector have been inimical to the growth of an efficient, labor-intensive industrial economy in India.

Table The structure of India's work force, 1983 (in Thousands)

Industry Group Total	Organized Sector			Share of the organized sector in industry	
	Public	Private	Total		
Agriculture	206,128	498	810	1,308	0.63
Mining & Quarrying	1,829	927	113	1,040	56.86
Manufacturing	32,435	1,717	4,423	6,190	19.08
Electricity	850	732	39	771	90.71
Construction	6,785	1,120	66	1,186	17.48
Trade	19,208	124	276	400	2.08
Transport	7,554	2,864	57	2,921	38.67
Services	26,848	8,895	1,503	10,398	38.73
Total	301,637	16,877	7,287	24,214	8.01

Source: Tendulkar and Sundaram 1992

III. Evolution of Indian Labor Laws

The modalities of labor-use in the organized sector in India are dictated primarily by the state, not by the market or by the results of collective bargaining between unionized workers and the management. The state plays a dominant role, through Labor Laws, Labor Judiciary and administrative officers, to “administer social justice keeping in view the power position and susceptibilities of workers...to eventually lead to a just industrial society”.” These arrangements have come to be established during the last fifty years through the working of India’s political process. The evolution of these arrangements is outlined next.

The first legislative actions to control the working conditions in factories and mines were taken by the British administration in colonial India in the last quarter of the nineteenth century. Before that time, the state did not interfere in the working of the factories and mines in India. The British initiated a series of regulatory measures governing child labor, working hours, safety and sanitation beginning with the Factory Act of 1881 and the Mines Act of 1923. The objectives of these Acts were to (a) specify minimum standards for safety, sanitation and the length of working hours particularly for women and children, and (b) to enable the government to appoint inspectors for factories and mines, who could enforce these standards. The major legislative reforms affecting the conditions of work in factories and mines came, however, after 1947, with Indian Independence.

The Factory Act of 1881 came in response to the criticism of the working conditions in Indian factories voiced by the urban intelligentsia in India and their sympathizers in England. There was no organized working class movement in the country to demand such reforms. In fact, there was **no** legal basis for freedom of association in British India at that time.

Nonetheless, the first Indian labor organization, the Amalgamated Society of Railway Servants, came into existence in 1887. The workers of the Assam-Bengal Railways resorted to strikes for higher wages in 1921-21. This was the first industrial strike in India, which was easily crushed.

However, many of the activists of the Indian Independence movement were active amongst workers in factories and mines. In 1920., they organized the first nation-wide trade union organization, All-India Trade Union Congress (AITUC), with affiliated unions all over the country. It is difficult to know the extent of support enjoyed by the AITUC, because union activities were not legal at that time. But it became legal with the passage of the Indian Trade Union Act of 1926, which allowed any **seven** wrkrers to combine in a **trade union**. By the year 1929, AITUC had 51 affiliated unions with a membership of 151,000.

During the colonial period the trade union movement became an important platform for the larger independence movement in India. The entire labor movement remained under the umbrella of the Indian National Congress, a political organization that led the independence movement. At that time unions were organized as plant-level unions with regional and national affiliation with **larger bodics**. **The leadcrs** of these unions came from urban **middle-class** intelligentsia associated with the independence movement. For example, Mahatma Gandhi was the organizing spirit behind the textile workers' union in Ahmedabad and Jawaharlal Nehru became the President **of** AITUC in 1929. Consequently, the ideological differences and group rivalries that ran through the body politic determined, to a considerable extent, the organizational characteristics and strategic behavior of the labor movement in India.

At the time of Independence in 1947, as ideological differences surfaced in the Indian National Congress, the labor movement started to fragment. First, the communists and then the

socialists left the Indian National Congress to form separate parties. Various other left wing groups also splintered away. Since these political groups were important in the labor movement, the labor movement itself experience successive splits.

Today practically every political party has its trade union wing. Given the flexibility of Indian party structure the number of trade union federations and their respective influence vary considerably over-time. In 1989, the Labor Ministry of the Government of **India** began an exercise to prepare a register of existing trade union organizations in the country. They listed eight major trade union federations - Indian National Trade Union Congress (INTUC), All-India trade Union Congress (AITUC), Centre of Indian Trade Unions (CITU), Hind Mazdoor Sabha (HMS). Bharatiya Mazdoor Savha (BMS), Hind Mazdoor Kamgar Party (HMKP), United Trade Union Congress (UTUC), United Trade Union Congress Lenin **Sarani** (UTUCLS) and National Labor Organization (NLO) besides a number of small independent unions.¹⁵ Due to the party affiliations, politics at national and regional levels finds its reflection in the trade union activity.

The large number of trade unions has led to inter-union rivalry for members. This rivalry manifests itself in **labor** militancy. In 1950-75 almost 30 percent of the industrial disputes in India could be attributed the problems of union recognition and inter-union rivalry. As Ramaswamy (1984) says: "A union has to call an occasional strike to show that it is active in the cause of its members. Without such periodic displays of militant action, it may find it difficult to preserve its following".

Since trade unions are linked to political parties it is not surprising that narrow partisan considerations, an inevitable feature of politics, has also bedeviled the legal framework regarding the **recognition** of a union at the plant level. For example in 1950, the **ruling** party opposed

successfully the introduction of secret ballot as a method of union recognition on the ground that it would introduce bribery and poll-rigging. It favored a system based on the verification of membership through an impartial agency, such as the Labor Department of the Government. The fact that the Congress Party then controlled not only the Government at the Center, but also the governments at every State capital was not unrelated to the position it took. As a result, the Labor Department acquired an important position in industrial relations.

Trade unions have been able to steer the evolution of labor legislation in India. The Constitution of the Indian Republic and the various pieces of legislation enacted in the Parliament and the State Assemblies after 1947 tried to uphold the rights of the workers. Since it is difficult to make the laws reach the unorganized sector, the primary beneficiaries from these legislative actions are workers employed in the organized sector.

The behavior of labor unions and the mechanism of **collective** bargaining vary considerably even among the developed OECD countries • from decentralized bargaining as in the USA to highly centralized bargaining as in the Nordic countries of Europe. In India, the workers in the **organized** sector **constitute a small fraction of the country's labor force, but the** historical association of their unions with the political parties places them in a strategic position. Therefore, the labor movement has found it convenient to operate through the political process with legislative and administrative measures to further their collective goals. How exactly the trade union power shows in the current labor legislation will be discussed next.

IV. The Industrial Disputes Act (IDA)

The single most important piece of legislation that governs the relationship between the worker and his employer is the Industrial Disputes Act (IDA) of 1947. This Act applies to establishments employing 50 or more workers in the organized sector. It confers on the state the power to regulate labor-management relations. In most countries, the state enters the *labor-management relationship upon* the breakdown of bipartite bargaining. In India, the state assumes the role, of the arbiter in lieu of a bargained relationship. According to Ramaswamy [4 (1984): “the state occupies the centre of the stage. The legal framework of industrial relations is such as to inhibit the growth of voluntary relationship and foster dependence on the state. The state is often forced to play the role, not of a mediator, although it may be so labelled, but of an arbitrator.”

The role of the state as a regulator of labor-management relations has its origin in Section 8 IA of the Defence of India Rules announced by the British administration in India during the Second World War. These rules armed the government with powers to interfere in the labor-management relations. Under their provisions, the government could conciliate in industrial disputes, and if conciliation failed, compel the parties to submit their case to arbitration. The obvious objective of this measure was to maintain industrial peace during the War. When the Defence of India Rules lapsed, these emergency measures of the war years were incorporated into the IDA in 1947. Perhaps, with the various urgent problems faced by the new Government at the time of Independence (with Partition, religious riots, refugee influx), they found it prudent not to disturb the existing arrangements in too many areas.

The implementation of the provisions of IDA was left to the Labor Departments of the Central and the State governments. Once the Labor Department decides that a particular dispute merits its attention, it sets in motion a process of conciliation. If the process of conciliation fails, the conciliator is required under section 12(4) of IDA to submit a general report outlining the nature of the dispute, and a confidential report conveying his recommendation regarding adjudication to the government. If the parties fail to agree on voluntary arbitration, then the Ministry of Labor refers the dispute to the Labor judiciary for adjudication. Trade Unions prefer the adjudication process because the ministries and the Labor judiciary, as well as the appellate courts are expected to be sympathetic to the cause of the workers.¹⁶

In the Statement of Objects and Reasons of Amending IDA in 1982 it was stated: “a model grievances redressal procedure had been commended for adoption. But this voluntary arrangement has not proved effective. It is therefore proposed to make it obligatory for every industrial establishment employing 100 or more workmen to set up a time-bound grievance redressal procedure”. This procedure has paved the way for what Ramaswamy (1984) calls “ministerial intervention” or “political intervention”. In these cases, a minister gets involved in a dispute in the guise of a conciliator interested in settling the case. Since a minister has enormous powers to reward and punish the parties to the dispute, his intervention effectively assumes the character of an imposed solution.

In 1950, the Government of India made an attempt at replacing IDA with two new bills: the Labor Relations Bill and the Trade Unions Bill. The goal of these Bills was to encourage labor and management to become self-reliant so that state intervention could be dispensed with. Three of the four trade union federations in existence at that time opposed these Bills and

successfully lobbied for retaining the existing system. As mentioned earlier, the labor unions felt that with the active involvement of the state and the political process, they would be on a stronger bargaining position - vis-a-vis their employers. According to the INTUC, the federation of trade unions affiliated with the ruling Congress Party, "only a system of state intervention would ensure the legitimate interests of labor."

The paramount concern of Indian workers, and thus of their trade unions, relates to the question of job security." Workers and their unions fight for higher wages and bonus payments, but they also fight for job security. Industrial disputes over wages and bonus payments are classified as those due to "economic causes". Disputes arising from dismissals, retrenchments or disciplinary actions against individual workers are classified as disputes due to "non-economic causes". Between 1951 and 1975, the percentage of disputes arising from non-economic causes varied from 49 to 63.8 percent. Trade unions fight bitterly even against the imposition of fines and suspensions, because these could go into the building up of a dossier against a worker and eventually be used in a tribunal to get the worker dismissed. According to Ramaswamy (1984): "Many Union leaders are of the view that there is practically no offence which merits dismissal. A part of the reason for this union condonation of misconduct is humanitarian. A far more important reason is fear of rival union propaganda. A union which accepts punishment to a defaulter is certain to be dubbed a management stooge".

Due to the pressures from trade unions, IDA itself was amended in 1976 and 1982. According to the 1976 amendment of IDA, if a firm employs 300 more workers, then the workers cannot be laid off or retrenched without the permission of the Government. The 1982 amendment of IDA made this provision applicable to all firms employing 100 more workers.

Three parts of the amended IDA are of crucial importance to industrial relations. These are sections 9A, Chapters V-A and V-B. Section 9A stipulates that an employer must give three weeks' notice in writing to the worker of any change in his working conditions. These changes include (a) changes in shift work, (b) changes in grade classification, (c) changes in rules of discipline, (d) a technological change that may affect the demand for labor, and (e) changes in employment, occupation, process or department. The worker, of course, has the right to object to these changes, leading to an industrial dispute with all its implications in terms of time and costs. This provision quickly to technological changes or changes in its market environment.

Chapter V-A requires an establishment **employing 50 or more workers to give a worker** (a) half-pay for 45 days in case of a lay-off (Section 25C), (b) thirty days' notice and 15 days' pay for every year of work in case of retrenchment (Section 25P), (c) In case of a closure or the sale of an establishment the employer must fulfil the same condition as for retrenchment unless his successor **takes** on these obligations (Sections 25FF and 25FFF). If the employer had **the** money to pay the workers, even if the firm were loss-making, the question of closure or sale of the firm would not arise. In such a situation the unit is usually declared sick and is **allowed** to continue functioning on the basis of government **subsidies**.¹⁹

The most onerous provisions of IDA is chapter V-B. It states that an establishment employing 100 or more workers must gain a prior permission from the government for lay-off, retrenchment or closure. Needless to say, government permission is seldom given. This last provision may sound strange to many outside observers. In fact the only country other than India, which has enacted similar Laws requiring prior permission of the government before lay-offs and retrenchment is Zimbabwe.”

It is evident from various High Court and Supreme Court judgements that these laws have acquired over the years a certain measure of moral legitimacy in India. For example, in 1990 a five-judge bench of the Supreme Court denied the management of the Delhi Transport Corporation the discretionary right to retire workers found unsuitable for specific duties? In 1992, a judge on the Calcutta High Court thought that if another private party took over a bankrupt private firm, there would be no guarantee that it would not itself go bankrupt in the future. Therefore, he directed the Government of West Bengal to take over the firm and run it with the existing workers.” One cannot fail to notice a similarity between this case and a judgment involving child-custody. Paternalistic concern for complete job security of a worker seems to have greater legitimacy than the questions of economic viability of an enterprise.

In an insightful essay, a former Chief Justice of a High Court, Mr. Mehta, analyzed a large number of important judgments given by the various High Courts and the Supreme Court of India on matters relating to the termination of service by employers. He made the following observations:²³ “Some judges are overwhelmed by the view that the only object and purpose of the Industrial Disputes Act is to take a view favorable only to labor, ignoring other facts and circumstances as also the necessity of preserving industrial peace. It is sometimes forgotten that the problem confronting industrial adjudication is to promote two fold objectives: (1) security of employment of the workers; and (2) preservation of industrial peace and harmony so that industry can prosper and employment can increase. Any lopsided view, that to favor labor is the only goal of the statute is counterproductive in as much as it ultimately harms the cause of labor itself”.

An economist will easily agree with Justice Mehta that excessive concern for job security can be a powerful deterrent to the growth of employment in the economy. It seems, however,

that the judicial **and** the political fraternities in India are prepared to promote job security for few at the cost of job prospects for many.

V. Wage Determination in the Organized Sector

In the organized private sector, salaries and other benefits are determined by the process of collective bargaining between the management and the labor unions. By and large, collective bargaining in India is a decentralized process. In most cases, the management of an enterprise negotiates with the union representing its workers. In some cases, such as the tea plantations of Northeast India, or the jute mills around Calcutta or the coal fields of Eastern India before their nationalization in 1973, there is often industry-wide collective bargaining between the representative associations of the industry and the labor unions. The government, as mentioned earlier, often intervenes in this process either formally or informally, as it has the power under IDA to do so,

In the public sector, the government is both the owner and the regulator. The state-owned enterprises in India do not function as autonomous entities; they are usually run by ministries and departments of the government almost like other administrative departments of the government.

In the public sector, wages, salaries, bonus payments and other conditions of work are not determined at the enterprise level. These are determined centrally, keeping in view the parity among government employees in the different sectors.

There is an established procedure for the determination of salaries and other benefits for the employees of the Central Government in public administration, posts and telegraph and the

railways. Periodically, the Government of India appoints a Pay Commission.²⁴ Members of the Commission are usually retired judges, members of the Parliament, senior civil servants and academics. The Commission holds hearings, solicits opinions and makes recommendations "having regards, among other relevant to the prevailing pay structure and retirement *benefits*, economic conditions in the country, the resources of the Central Government and the demand thereon such as those on account of economic and social development, defence and national security and requirement of sound fiscal management".²⁵

The award of the Pay Commission for the Central Government employees becomes the reference point for wage determination in the rest of the public sector, such as the State Governments, universities, financial institutions and the industrial and commercial undertakings. For example, the University Grants Commission sets up its own expert committee, which in a similar fashion, determines the salary structure of the people employed in Indian universities. A professor or a lecturer is placed on the same scale of salaries irrespective of where he or she is employed.

For the public sector industries the apex body is the Bureau of Public Enterprises (BPE) of the Ministry of Finance, Government of India. BPE sends guidelines for wage settlement to all administrative ministries, setting down norms to be followed *in* determining basic salaries and the various categories of benefits for different classes of employees. Although technically individual enterprises have the right to offer financial incentives to their employees, BPE strongly discourages such actions. For example, in 1984, BPE sent to all public sector undertakings a circular, which read as follows: "It has, however, been brought to the notice of the Government that some public sector enterprises have concluded additional or supplementary agreements apart

from the main agreements/pay revision proposals in respect of salaries or fringe benefits of the executives. This is not in order. It has to be appreciated that liberalization of any fringe benefits or revision of the scales of pay through separate agreements has serious financial implications and as such requires approval of the Government.²⁶

Mathur (1991) analyzed the labor standards prevailing in 18 private and public sector industrial enterprises in India. It is informative to quote him on certain aspects of industrial relations prevailing in one of the best known public sector industrial enterprises in India, Bharat Heavy Electricals Ltd. (BHEL). BHEL is a multiplant conglomerate which produces a wide variety of electrical and electronic goods. Mathur's findings have important bearing on the nature of the task involved in India's current efforts at economic reform. Mathur observed: "The centralized bargaining structure for wage negotiations taking all of BHEL units into consideration did not result in any differences in wages between BHEL workers in different units although their financial health *varies considerably*. *Further*, the bargain limits are set by the Bureau of Public Enterprises to ensure parity in wage levels and structures in public enterprises across industries and enterprises...This has also resulted in the perception that sales are a responsibility of the Government, so are employee costs". He goes on to say: "In a recent initiative, the Government has signed Memoranda of Understanding with several public enterprises in 1989 aimed at providing a higher degree of autonomy in indecision-making. However, this autonomy does not extend to determination of pay and employment levels commensurate with what the consumer is willing to pay in free market conditions. Nor would the enterprise like the freedom from the Government, because so many numbers were employed in the first place due to the Governments' policy of providing employment one of the stated objectives at the time of establishing public

enterprises in the 1960's. In fact, pressure from *BHEL executives and* officers is in the opposite direction for terms and conditions identical with Central Government employees”.

VI. Economic Implications of the Labor Market Institutions

What are the economic implications of India's labor laws? It turns out that these labor laws, or more generally the norms of industrial relations in the organized sector of the Indian economy, have created a small privileged class of labor aristocracy, and constrained the growth of employment. In the 1980's the employment in medium-sized and large industries in India remained stagnant even though output and investments of these industries grew at a relatively high rates. The Census Sector of the Annual Survey of Industries (ASI) indicates that the value added by these industries grew at the average rate of 7.4 percent per annum between 1980-81 and 1990-91 whereas, employment declined at the average rate of (-) 0.6 percent per annum.²⁷

This decline in employment during the last decade is partly traceable to the 1976 and 1982 amendments to the Industrial Disputes Act. If an employer is required to take the prior permission of the Government before laying-off a worker, and if he knows that it is impossible to get that permission, he will try to avoid getting into such a rigid and inflexible commitment. He would buy machines instead of hiring a permanent worker, or he would try to perform the job with casual workers or by contracting out work to small enterprises which are not covered by stringent regulations. Goswami (1990) shows that employers, like the powerloom industry, have used all these options. According to ASI, the share of the casual workers in the total employment more than doubled from 4.6 percent in 1980-81 to 10 percent in 1986-87.

Ramaswamy (1988) has also found micro-level evidence of these phenomena in India. He describes the emerging phenomenon of labor-contractor, who hire men who do the work on the premises of the employer but are not deemed to be his employees. This phenomenon is observed in the capital-intensive fertilizer and chemical industries for packing and storing. Fallon and Lucas (1993) report that among larger Indian plants, the decline in employment is estimated to be largest in industries where the coverage of IDA (V-B) is more extensive, private ownership dominates and there are fewer union members. They did not find any comparable reduction in labor demand in small scale plants uncovered by job security regulations.”

IDA introduces economic inefficiencies in two ways: It introduces undesirable automation and thereby reduces employment opportunities; and it increases the resource-costs of domestic outputs by sacrificing scale economies. Sub-contracting certain operations to small farms sometimes introduces economic inefficiency by sacrificing scale economies. In some cases, as in powerloom industries, inefficient techniques are introduced only in order to evade the rigidities introduced by the Labor Laws. Moreover, the substitution of permanent workers by casual employees has also the negative dynamic impact on the growth of productivity by discouraging firm-specific learning.

There is some indirect evidence to suggest that the organized private sector has sometimes been able to evade the legal requirements of IDA and restructure their technological and managerial practices.²⁹ But the cost of overcompensating the affected workers, in the face of opposition from their unions, may have been quite high. Stringent Labor Laws are proving to be a serious barriers to direct foreign investments in the industrial sector.³⁰ During 1991-94, the flow of foreign investments to India has gone up perceptibly, but the preferred avenue for

this investment has been the financial sector: rather than manufacturing industries.³¹ The fear of not being able to correct mistakes, or to alter production plans in response to market signals, due to the imposed inflexibilities in labor-use is a serious deterrent to investments in manufactures.

The reform of Labor Laws will primarily help the organized private sector. For efficient manpower use in the public sector more than the reform of the Labor Laws is necessary. The prevailing practice of letting of the Bureau of Public Enterprises (BPE) determine uniform norms of labor-use for all enterprises does not allow individual enterprises to seek efficiency in their use of labor and other inputs. These enterprises can operate in a market environment only if *their* management have greater control over their own commercial activities.

Economic reform programs everywhere tend to give overwhelming importance to restoring macro-economic stability and removing barriers to foreign trade. India's current effort at economic reform also follows this strategy. The basic assumption behind such a strategy is that with price stability and foreign competition, the supply side of the domestic economy will automatically adjust to the norms of efficient industrial progress. The analysis here, however, suggests that without direct attempt at institutional reforms - particularly of labor laws and of public sector management - current liberalization efforts may not induce efficient industrial growth in India.

ENDNOTES

- Marshall (1925)
2. For references to studies in various social science disciplines on the importance of social norms in wage determination, see Akerlof (1982), Pigors and Myers (1977), Goldthorpe Lockwood, Bechhoper and Platt (1968), Hirschman (1970), Cain (1976) and Piore (1983).
 3. See, for example, Garrett and Lange (1986), Aoki (1984, 1988), Koike (1990), Calmfors (1990), Gordon (1987), Yamamura and Yashuba (1987), Bain (1983), Lane (1990) and Williamson, Wachter and Harris (1975).
 4. See, Solow (1990) page 71.
 5. Lane (1990).
 6. Since the publication of Solow (1957), there has been a large volume of empirical research on this all over the world. Denison (1967) is an illustration of findings for the OECD countries. Chen (1977) does a similar work for the so-called Asian tigers, Ahluwalia (1992) is an example of recent work on India.
 7. Stiglitz (1987).
 8. Chen (1977) computed Total Factor Productivity (TFP) for the four fast-growing developing economies of East Asia for the period 1960-70. According to his computations the annual percentage rate of growth of TFP for Hong Kong was 2.03; for Singapore, 3.34; for South Korea, 3.08 and for Taiwan, 3.7. Ahluwalia (1992) computed the growth rate of TFP for Indian industries for 1959-79, which was (-) 0.3
 9. Desai (1980, 1984).
 10. In 1983, about 206 million workers out of an estimated labor force of 302 million were employed in agriculture. If one takes out the organized sector of agriculture, which is mostly plantation, employment in peasant agriculture was about 205 million. See Table 1.
 11. Sen (1975).
 12. Different departments of the Central and the State Governments publish employment statistics for the units under their jurisdiction. Consolidated data for the organized sector of the Indian economy are regularly published in the two journals, the Indian Labor Statistics (Ministry of Labor, Government of India) and The Employment Review

(Director-General of Employment and Training, Government of India).

13. For a clear exposition of this strategy, see the first three Five-Year Plans (1951-56, 1956-61, 1961-66), Planning Commission, Government of India.
14. Saini (1994).
15. The Labor Ministry of the Government of India-also tried to compile statistics relating to the membership of these organizations. Different Trade Union Organizations sent their claims regarding membership, which the officials of the Ministry are trying to verify. Till December 1994, this verification process has remained bogged down by objections and disputes. The Ministry rejected many of these claims. The rejection rates varied from 25 percent to 99.3 percent.
16. Mehta (1994).
17. Ramaswamy (1984).
18. For a detailed discussion of this issue, see Ramaswamy (1985), Mamoria and Mamoria (1991).
19. By March 1992, there were 1,336 units in the organized private sector, which were listed 'sick', with a bad debt of Rs. 5,786.55 crores. In 1989-90, there were 98 sick enterprises in the public sector incurring a total (annual) loss of Rs. 1,959 crores.
20. Fallon and Lucas (1993).
21. Delhi Transport Corporation vs. DTC Mazdoor Congress and others, 1990 (61) FLR 768(SC).
22. Veegal Engine and Engineering Industries Limited (in Liquidation), CP:393 of 1985, Calcutta High Court, Original Jurisdiction'.
23. Mehta (1994).
24. Between 1948 and 1994, five Pay Commissions have been appointed by the Government of India in 1948, 1957, 1970, 1985 and 1995. The Fifth Pay Commission appointed in April 1994 is expected to submit its report to the Government of India by the end of 1995.
25. See The Terms and Conditions of the Fifth Pay Commission, Government of India, April 1994.
26. D.O. No. 2(146)72-BPE(WC) dated June 6, 1984 quoted in Nigam 1994.

27. This sector includes all factories employing 50 or more workers with power and 100 or more workers without power.
28. Fallon and Lucas (1993) estimated a dynamic labor demand function, derived from a CES cost minimization model for 64 manufacturing industries. They attribute 17 percent of long-term loss in industrial employment to job-security regulations.
29. See, Mathur (1991).
30. Numerous prospective foreign investors have spoken on this. For example, in 1992, the Japanese Ministry of International Trade and Industries (MITI) sent to India a high-power delegation led by Mr. R. Ishikawa, President of the Japanese Chamber of Commerce, to explore investment opportunities in India. Liberalization of the exit-policy regime figured prominently in the list of "humble requests" submitted by this delegation to the Government of India. See The Economic Times, Bombay and Delhi, January 30, 1992.
31. Less than 20 percent of the capital flow from abroad during 1992-93 and 1993-94 has been Foreign Direct Investment (FDI).

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This article also mentions, without specific citations, a number of Government of India publications and Reports. These are (a) the successive Five-Year Plan volumes, (b) the successive Reports the Pay Commissions and (c) the journals of the Labor Ministry.