It's Not the Labour Laws!

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The loud clamour for liberalisation of labour laws in recent times quite overlooks the fact that other institutional reforms are far more important for rejuvenating the sector.

Numerous editorials and even the Prime Minister's speeches of late have hit out at 'outmoded' labour laws holding up industrial growth rates and employment generation in the country. Partially structured econometric studies, often based on defective methodology and unaware of the database and its limitations in India, regularly arrive at the 'typical' conclusion that labour institutions are the cause of economic misery, which are then used *ad nauseam* by critics of labour regulation to call for labour law and governance reforms.

The typical argument is that liberalisation of labour laws will facilitate capital inflows which will in turn generate employment (direct as well as indirect). Recently, Tamil Nadu was reported to be poised to ink a Memorandum of Understanding with seven companies to fetch Rs 18,000 crore worth of investments which, it is estimated, will generate 36,855 direct jobs. The investment rate per job is around Rs. 5 million and even by adding the overly generous estimate of 100,000 indirect jobs created, is still quite high at Rs. 1.4 million. Labour law liberalisation will not change the increasing capital intensity-driven foreign investments in India. Further, the record of foreign investment inflows in India in the post-reform period shows that money is mostly flowing into sectors other than the manufacturing sector, viz. construction, telecommunication, information technology, etc. Also, investment expectations into the manufacturing sector need to be tempered by the reality check of competing with traditional exporting giants like China and Taiwan, notwithstanding the recent stories of slow growth in these economies.

However, even when we talk of the manufacturing sector being stifled by labour law rigidities, it is a point of fact that the organised component of the manufacturing sector accounted for only 21 per cent of total employment in the manufacturing sector in 2009-10. Employment generation lies in the smaller segments, as according to a recent newspaper report micro and small units are expected to create six or seven jobs per unit directly as 8,000 units will invest Rs. 9,000 crore (investment rate per job is Rs 9 lakh) in Tamil Nadu.

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Labour laws in general and Chapter V-B, one of the most contentious clauses in the Industrial Disputes Act, 1947, especially have very narrow coverage. According to the Economic Census, 2005, only 4.25 per cent of establishments employed more than nine people, accounting for 39 per cent of total workforce. Within the organised factory sector, according to the Annual Survey of Industries data for 2008-09, Chapter V-B applies to 15.63 per cent of total factories and these employ 72.31 per cent of workers.

Labour law reform from the employers' perspective depends on the economic enterprise/entity as a factor while labour law reform from the workers' perspective uses employment affected as a metric. T.S. Papola has reported in a study that do not cover even a respectable proportion of the workforce. The minimum wage law has the highest coverage; and although a critical law, is the least effectively implemented one. Indeed, none of the variables pertaining to labour regulation such as coverage, inspection, irregularity detection, prosecution, imprisonment and fines do not in any sense paint a domineering and autocratic regulatory figure.

The Ease of Doing Business' 2015 report shows that India has done relatively poorly, even as compared to its warring neighbor, Pakistan and much worse than China, which should not surprise anyone. However, it is clear that India's ease of doing business would be bolstered even if we tightened procedures relating to getting construction permits, getting electricity, dealing with taxation issues, enforcing contracts and so on.

As it stands, India has not ratified four of the eight ILO core conventions (called as 'fundamental human rights' by the global community) while its poorer neighbours have a much better record in this regard. Our defence is that we a have a strong democratic set-up unlike our neighbours. But this should be a greater reason to a better record of labour rights assurances as well; or else 'non-ratification' is a stigma for us.

The International Trade Union Council (ITUC) has released publications on labour rights violations for a long time and had recently come out with an index, rating 141 countries on a scale from 1 to 5 based on the degree of respect for workers' rights. As we move up the score from 1 to 5/5+ the intensity of labour rights violations rises. India scored a poor 5 along with 26 other countries for 2015. Though this index is not sound due to the limitations of the data points sourced – the more democratic a country, the more violations become visible and vice versa – India, according to the criticisms of labour regulation, should stand very *high* on labour rights thanks to a pro-labour regulation regime and the presence of overly-militant trade unions.

Do we require law and governance reforms? Yes, we do indeed -- but not the kind that has been currently whipped up. We need to rationalise labour laws, remove conflicting definitions, provide for a strong bi-partite system of governance supplemented by optional and not compulsory government intervention, clearly define minimum wages and a provide rational minimum wage regime as well as gradually move towards universal coverage of establishments with a special and economically sound focus on the unorganised sector (like constitution of a fund for social security).

In the interim, there could be special laws for the development of micro and small enterprises in order to grow and generate employment. However, labour law and governance reforms will produce benevolent growth and labour market outcomes if, and only if, other institutional variables are addressed.