Improving Productivity and Employment Growth

Arup Mitra

..to help modernise the labour intensive goods industries, to enable the units to manufacture quality products which will generate export demand, and to help them expand so that their contribution to both growth and employment generation becomes significant, are still in the waiting list. Instead of merely importing technology, how innovation can be pursued which will contribute to productivity and employment, both have to be the important menu in the future discourses

Industrial growth and employment creation fall into the domain of primary objectives of the Government. India, or any developing country for that reason, needs to revive its industrial sector because services alone cannot provide enough outlets for productive absorption of the unskilled and semi-skilled work force and agriculture, on the other hand, comprises a great deal of underemployment. The total factor productivity growth in the industrial sector can be raised significantly through technological advancement, contributing to non-input driven growth. Even if technological innovation is believed to be capital intensive, the recent research (Vivarelli, 2013) shows a number of channels through which employment gains are actually possible. Product diversification, manufacturing of new products and by products without proportionate rise in capital and material and more importantly, the large scale adoption of the new technology can result in employment gains. So productivity gains and employment gains can be attained concurrently and they do not necessarily involve trade-offs. In the backdrop of this it would be interesting to take a quick look over the Union Budget 2017-18 in order to understand the short term implications and their extent of convergence to the long terms goals.

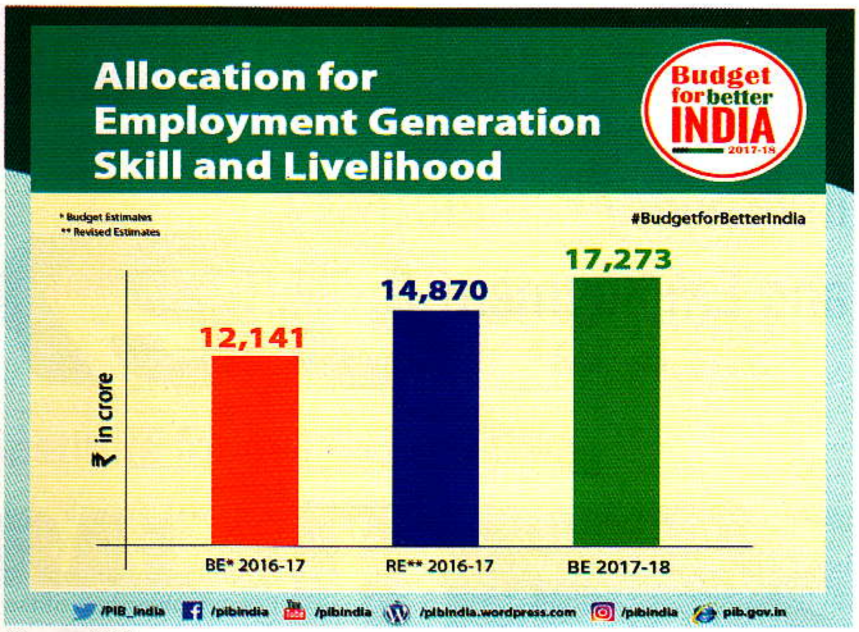
Just a little while ago the historic demonetisation took place. And it is feared to have had an adverse impact on growth at least in the short run, which in turn would raise unemployment. The non-agricultural investment and growth located largely in the urban areas are likely to suffer raising the urban unemployment rate and underemployment. The medium and small enterprises both in manufacturing and services are likely to suffer in terms of investment, growth and employment. However, the large units are also not completely out of risk. After all, many units subscribe to the practice of bribes in order to avoid regulations and carry out their businesses. The first negative impact of a cut down in investment is always seen in terms of a reduction in labour demand. This is because labour is the only input, particularly in the era of contractualisation, which is extremely fluid compared to other inputs. So cutting down the labour cost to cope with declining market trends is the easiest (and possible to implement) choice for the entrepreneurs. The rural sector unemployment is also feared to rise because, given that the agriculture sector is not in a position to absorb labour significantly, many of them

The Author is Professor at Institute of Economic Growth, Delhi, presently Visiting Professor at Nagoya University, Japan. His specialization includes labour and welfare, urban development, industrial growth and productivity, development economics and gender inequality, areas in which he has more than hundred publications in various academic journals and edited volumes. Some of his recent books are on inclusive growth (Springer, 2013), industry-led growth (Springer, 2015) and on corruption (co-authored; Cambridge, 2016).

take recourse to rural non-farm sector, where business requires cash on day to day basis. So, demonetisation may not spare the rural non-farm sector growth and employment. However, much of this might have been exaggerated because business after all involves a great deal of transactions which are notional and which involve considerable time lags. Hence, the adjustment mechanisms may neutralize the growth-dampening aspect of demonetisation. Like the nationalisation of banks in the seventies demonetisation was necessary and long overdue. It had to be sudden; else the whole purpose would have been lost.

The Union Budget has made the highest allocation to MNREGA so that employment opportunities are created. One of the standard criticisms of the employment guarantee programme was that it did not create enough assets which could contribute to future growth. However, the Union Budget brings in a new dimension of using space technology to plan MNREGA works, so that work allocation does not have to take place in the last minute towards the end of the financial year when the expenditure has to be incurred hurriedly, else, the allocations have to be returned. During 2017-18, it is proposed that another 5 lakh ponds will be constructed, for drought-proofing. If this irrigation programme is linked up with the MNREGA program, it will be a highly effective strategy in addition to being productive from the point of view of agricultural growth. A total allocation for rural, agricultural and allied sectors for 2017-18 is 24 per cent higher than the last year's figures, indicating clearly that the Government wishes to deal with rural unemployment, underemployment and poverty issues more aggressively.

Allocations of PM's employment generation and credit support schemes has been stepped up by 3 times. PMEGP is basically a credit-linked subsidy programme which combines Rural Employment Generation Programme (REGP) and *Pradhan Mantri Rozgar Yojana* (PMRY). The Ministry of Micro, Small and Medium Enterprises (MoMSME) administers



(Source: PIB)

the programme and it is implemented by the Khadi and Village Industries Commission (KVIC). At the state level, KVIC directorates administer the programme. The primary aim is to generate jobs in both rural and urban areas through self-employment ventures, micro enterprises, and other projects. The dual objective is to bring back the tradition of village artisanship and to help (urban) youth not able to find jobs otherwise. The programme aims at providing employment in a continuous and sustainable manner and enhancing the earning capacities of the beneficiaries.

Keeping pace with the nationwide programme to go digital, the Budget emphasises that increased digital transactions will enable small and micro enterprises to access formal credit. Hence, rise in productivity of these units and meaningful contribution to be made by these units to national GDP are some of the expected outcomes which may help these units overcome the adversity of demonetisation. The small and micro enterprises are numerous while their contribution to value added, has been nominal. Take the example of unregistered manufacturing – their share in total manufacturing value added is around one-third or so. The move to revive them within the broad ambit of the country to go digital is interesting, particularly if we keep in mind that the organised manufacturing alone cannot reduce the mismatch between labour demand and supply in a significant manner. In order to avoid the incidence of taxes, many enterprises decided to remain within the unregistered/informal sector by splitting their activities into multiple units. Digitization may help consolidation, facilitating collection of taxes; while the units surviving on the margin can actually improve their financial viability and performance. For those who do not have debit cards or mobile phones, a merchant enabled Aadhaar payment system is proposed to be launched.

The small firms with a turnover of around 50 crore or less will have to pay a lower tax (25 per cent). The modern small scale industries are, therefore, likely to invest more, and in the process the industrial growth and employment are expected to rise. On the other hand, foreign investment which comes along with advanced technological configurations has received considerable amount of attention in the Budget given the fact that more than 90 per cent of the FDIs are proposed by automatic mode and that the Foreign Investment Promotion

Board has been abolished, economic activities are expected to pick up considerably without the compulsion of going through bureaucratic delays. A 36 per cent increase in FDI is likely to boost investment and generate employment considerably.

A host of factors have been identified as the determinants of productivity growth in the industrial sector as we have seen in terms of our research on Total Factor Productivity Growth (TFPG). Among them trade openness, agglomeration economies, infrastructure & ICT and innovation are the four major sets. Innovation is also another variable which can enhance productivity. Through innovation higher level of technology is attained which in turn raises the non-input driven component of growth. The importance of infrastructure is widely recognised in the literature. For example, public infrastructure is considered to be a crucial factor in enhancing productivity and technical efficiency through complementary relationship with other factors of production and external economies of scale. Poor employability of the labour force is seen as a major constraint to investment and employment growth and over time, this skill mismatch has grown, particularly in relation to the manufacturing sector (Mitra, 2013). The Union Budget methodically addresses these constraints. According to the Budget, the Government in the ensuing 2017-18 financial year will launch a scheme *Sankalp* (Skill Acquisition and Knowledge Awareness for Livelihood Promotion Programme) at a cost of Rs 4,000 crore. Around 3.5 crore youth will be trained under *Sankalp* program launched by the Government. *Sankalp* will provide market relevant training to the youth. *PM Kaushal Kendras* will be extended to 600 districts; 100 international skill centers are to be opened to help people. *Kaushal Kendras* are being set up as community skill centers focused on rural population with facilities for language lab, digital library, assessment and career guidance and skill room. All this is expected to improve the employability.

Budget 2017-18: Measures for Growth and Employment Generation

- The next phase of Skill Strengthening for Industrial Value Enhancement (STRIVE) in the next financial year 2017-18 at a cost of Rs 2200 crore to be launched. STRIVE will focus on improving the quality and market relevance of vocational training provided in it and strengthen the apprenticeship programmes through industry cluster approach
- Special Scheme for creating employment in leather and footwear industries to be implemented. This will be on the lines of the already launched Special Scheme for creating employment in the textile sector.
- Five Special Tourism Zones, anchored on SPVs in partnership with the States to be set up, tourism being a big employment generator with a multiplier impact on the economy. Incredible India 2.0 campaign to be launched across the world.
- *Pradhan Mantri Kaushal Kendras* to be extended all over the country from current 60 to cover more than 600 districts across the country. 100 India International Skills Centres to be established across the country. These centres would offer advanced training and also courses in foreign languages. This is expected to help those of our youth who seek job opportunities outside the country.
- "SANKALP" (Skill Acquistion and Knowledge Awareness for Livelihood Promotion Programme) to be launched at a cost of Rs 4000 crores
- SANKALP is expected to provide market relevant training to 3.5 crore youth.
- Income tax for smaller companies with annual turnover upto Rs 50 crore reduced to 25 per cent in order to make MSME companies more viable and also to encourage firms to migrate to company format. This will make the MSME sector more competitive as compared to large companies.
- Concessional with-holding rate of 5 per cent being charged on interest earned by foreign entities in external commercial borrowings or in bonds and Government securities extended to 30.6.2020. This benefit is also extended to Rupee Denominated (Masala) Bonds.
- To give a boost to Start-ups, the condition of continuous holding of 51 per cent of voting rights which had been given to Start-ups to carry forward losses, has been relaxed subject to the condition that the holding of the original promoter/promoters continues. Also, the profit linked deduction available to the start-ups for 3 years out of 5 years is being changed to 3 years out of 7 years.

The concept of India International Skills Centres (IISC) to be established across the country is really interesting as these centres will offer advanced training and courses in foreign languages. This is expected to help those who seek job opportunities outside the country. There has been a strong criticism against the ITIs relating to the quality of training imparted to the participants. 'A plumber had to be retrained by the recruiting agency before he can be sent to the middle-east to pursue work'. From this point of view, the recent move is very encouraging; it will facilitate labour mobility across countries, reducing the excess supplies in the domestic economy, and on the other hand, the country's foreign exchange earnings through remittances will rise sizably. Remittances contribute significantly to the well-being of the relatives who stay back. How remittances can be utilised for creation of productive assets through mechanisms which incentivise the process can be the policy agenda in the future. As a first step, this explicit

Budget 2017-18: Measures for increasing Ease of Doing Business

- The threshold limit for audit of business entities that opt for presumptive income scheme, has been raised from Rs 1 crore to Rs 2 crore. Similarly, the threshold for the maintenance of books for individuals and Hindu Undevided Families (HUF) is proposed to be increased from turnover of Rs 10 lakhs to Rs 25 lakhs or income from Rs 1.2 lakhs to Rs 2.5 lakhs.
- The Foreign Portfolio Investor (FPI) Category I & II will be exempt from indirect transfer provision under the IT Act. Besides, indirect transfer provision shall not apply in case of redemption of shares or interests outside India as a result of, or, arising out of redemption or sale of investment in India, which is chargeable to tax in India. This will remove apprehensions over taxation upon transfer of stake of investors of India-based funds located abroad.
- Individual insurance agents will be exempted from the TDS provision of 5 per cent being deducted from commission payable after filing a self-declaration that their income is below taxable limit. Professionals with receipt upto Rs 50 lakhs p.a. can pay advance tax towards presumptive taxation in one installment instead of four.
- Scope of domestic transfer pricing proposed to be restricted only if one of the entities involved in related party transaction, enjoys specified profit-linked deduction. This is expected to reduce the compliance burden for domestic companies since the number of entities being covered under domestic pricing had gone up substantially resulting in longer scrutiny.

move on the part of the government to create employable labour force which will match the international standards and thus contribute to spatial and upward mobility is noteworthy; and it reflects a highly progressive long term vision that the government holds.

Allocation for infrastructure has been evidently large. This will also generate employment as building of massive infrastructure would require manpower. However, more desirable outcomes could have been expected if this infrastructure building strategy could have been accompanied by a regional dimension. Regional inequalities have grown over time, instead of convergence, divergence is seen to have taken place in terms of economic growth across the states. And one of the effective ways of curbing regional inequality is to foster infrastructure in areas which are lagging behind. Of course we understand that concentration begets agglomeration economies and to benefit in terms of agglomeration economies, more investment has to be pumped into the areas which already have a significant initial base. But, in the process, some of the areas remain completely neglected and industrialisation for example, tends to become highly area centric, resulting in regional tensions. In order to curb these problems, it is desirable to pursue a more regional approach when it comes to building infrastructure. The pace of industrialisation in the north-east has been negligible.

Besides a new metro rail policy is expected to be announced which will open up new job opportunities for the youth. This is a great solace for the urban based educated youth! The metro rail project will also add significantly to the infrastructure network, efficiency in commuting and work performance. In the face of the growing urban population prompted by the village-to-city migration, more such employment oriented projects with an 'urban bias' would have been desirable.

However, more should have been done for the manufacturing sector if industry-led-growth is going to be the mandate. The Government should have proposed tax incentives for the labour-intensive industries including leather, gems and jewellery as part of the "Make in India" initiative to boost manufacturing, create jobs and revive exports. The China-style mega industrial cities across the country equipped with production units, public utilities, residential areas, schools and hospitals are very much in the offing under the smart cities programme but any significant mention of a big fiscal boost in the budget 2017 for such growth centers is not significantly noticeable. The labour intensive goods based industrialisation does not seem to have been the major focus of the Budget. Rather the Budget is more agriculture and rural centric, which is, in any case, warranted given the fact that a large majority of the population still lives in the rural areas and nearly half of the work force is engaged in the agriculture sector. However, to help modernise the labour intensive goods industries, to enable the units to manufacture quality products which will generate export demand, and to help them expand so that their contribution to both growth and employment generation becomes significant, are still in the waiting list. Instead of merely importing technology, how innovation can be pursued which will contribute to productivity and employment, both have to be the important menu in the future discourses.

Readings

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(E-mail:arup@iegindia.org)