MODULE 1: NATURE OF THE LABOUR MARKET

1

BASIC INFORMATION ABOUT LABOUR MARKETS

Unit Structure:

1.0 OBJECTIVES

- To understand the meaning of labour market.
- To study the characteristics of labour markets.
- To study of types and search in labour markets.

1.1 INTRODUCTION

A labour market is the place where workers and employers interact with each other. In the labour market, employers compete to hire the best, and the workers compete for the best satisfying job. In a labour market, services of human labour are bought and sold like other commodities. But there is a vast difference between labour market and commodity market. Labour market can never be perfect market.

Labour market is defined as the market for hiring and supplying labour to perform certain jobs at a wage rate.

Labour market can be defined as a process by which supplies of a particular type of labour and demands for that type of labour balance or seek to obtain a balance.

1.2 CONCEPT OF LABOUR MARKETS

The labour market, also known as the job market, refers to the supply of and demand for labour, in which employees provide the supply and employers provide the demand. It is a major component of any economy and is intricately linked to markets for capital, goods, and services.

The labour market refers to the supply of and demand for labor, in which employees provide the supply and employers provide the demand.

The labour market should be viewed at both the macroeconomic and microeconomic levels.

1.3 CHARACTERISTICS OF LABOUR MARKETS

The basic characteristics or features of labour markets are as follows -

1. Labour market is concerned with labour which is a human resource.
2. The relationship between a buyer and a seller in a labour market is likely to the continued for some time.
3. It is process in which a balance between supply of a particular kind of labour and demand is maintained.
4. It is a market where wage rates differ for the same kind of work due to lack of perfect mobility.
5. Labour markets are normally local markets.
6. In labour market price does not change very often, but remains constant for a period of time.
7. As labour is not homogeneous, we find different types of workers in labour market.
8. In the labour markets, workers try to increase their strength by forming their trade unions and resort to collective bargaining.
9. There is exploitation of labour in the labour market.
10. Wages, terms and conditions of employment etc. are determined in the labour market through bargaining tussles between workers and employers.
11. Labour cannot move with the same ease and facility with which goods are transported from one place to another. So, there is lack of mobility of labour.
12. Labour market is essentially an imperfect market.

1.4 TYPES OF LABOUR MARKETS

In labour markets, labour is supplied by households and demanded by firms Labour Market in India can be classified into following types:

1) National Labour Market:

A national labour market is one in which most job search by employers and firms takes place on a national level. The markets for college professors, top management positions in large corporations, and similar occupations are national labour markets.

2) Local Labour Market:

Most job search takes place at a local level in a local labour market. Secretaries, carpenters, truck drivers, electricians, and lathe operators are employed through local labour markets. A national labour market exists only when there are few employers and employees in most geographical regions. Local labour markets exist when there are many employers and employees in most geographical regions.

3) Internal Labour Market:

An internal labour market is said to exist within a firm if the firm fills higher level positions in the firm primarily by promotion from within the firm

4) Primary Labour Market:

Jobs in the primary labour market are characterized by high wages and stable employment relationships. Examples of jobs in the primary labour market include: accountant, lawyer, teacher, carpenter, and plumber.

5) Secondary Labour Market:

Workers employed in the secondary labour market receive low wages and experience unstable employment relationships. Workers in fast-food restaurants, gas station attendants, dishwashers, janitors, etc. are employed in the secondary labour market.

1.5 SEARCH IN LABOUR MARKETS

Search theory was originally applied to labor markets but has applications to many subjects in economics. In labor markets, search theory is the basis for explaining frictional unemployment as workers change jobs. It has also been used to analyze consumer choices between different goods.

In search theory, a buyer or seller faces a set of alternative offers of varying quality and price to accept or reject, as well as a set of preferences and expectations, all of which may vary over time. For workers, this means the wages and benefits of a job in combination with working conditions and characteristics of the job. For consumers, it means the quality of the good and its price. For both, the search depends on their preferences for price and quality and their beliefs regarding other possible alternatives.

Search theory describes the optimal amount of time that the searcher will spend on their search before settling on one alternative to accept. Search time will depend on several factors:

- **Reservation Price:** The individual's reservation price is the minimum they are willing to accept/maximum they are willing to pay. For example, a buyer who has a fixed budget of $5,000 cash to spend on a car will search long enough to find a car of suitable quality for under $5,000. Because they raise reservation wages, welfare and unemployment benefits may induce a qualified worker to sit at home and collect unemployment checks instead of seeking a job.

- **Costly Search:** If there are costs that increase with the length of the search, optimal search time will tend to be shorter. For example, if a worker's skills may degrade or become obsolete over time, then they will tend to shorten their search for a new job.

- **Price and Quality Variance:** The amount of variation in price and quality of offers will also influence the optimal search length. Greater variation can convince the seeker to hold out longer in their search expecting to find a superior alternative.

- **Risk aversion:** Risk aversion can also play a part in search time. For example, a longer job search often means that the searcher may be spending down savings and face an increasing risk of becoming destitute as the search lengthens. A risk-averse seeker will tend to shorten their search under this condition.

1.6 SUMMARY

The search theory is a study of transactional frictions between two parties that prevent them from finding an instantaneous match.

- Search theory explains how buyers and sellers decide when to accept a matching offer for a transaction.
- Search theory extends economic analysis beyond the idealized world of perfectly competitive markets.
- Search theory helps explain why frictional unemployment occurs as workers search for jobs and businesses search for new employees.

1.7 QUESTIONS

Q1. What is meaning of labour markets? What are the characteristics of labour markets?

Q2. What are the types of labour markets?

Q3. White a note on 'search in labour markets'.

❖❖❖❖

2

NATURE OF LABOUR MARKETS – II

Unit Structure:

2.0 OBJECTIVES

- To understand the concept of human capital.
- To analyse model of human capital theory.
- To discuss various aspects of investment in education

2.1 INTRODUCTION

Some activities influence the future wellbeing of workers. According to Becker, investing in the activities that influence future incomes through imbedding of resources in people is called investing in human capital.

There are many ways to invest in human capital.

- On the job training
- Schooling
- Vitamin consumption.
- Acquiring information about an economic system

All these activities differ in their impact on earnings, amount of investment, extent to which there is a connection between investment and return. But one common thing about all these activities is that they improve physical and mental abilities of people and thereby raise future income prospects.

Over years, it has been observed that the factors other than availability of physical resources play important role in determining the level of wellbeing of people or a country. These factors include less tangible resources like knowledge possessed or education, skill acquired or training or health, etc. In this unit, we will focus on the impact of human capital investment in education, training and migration.

2.2 THE THEORY OF HUMAN CAPITAL

2.2.1 What Is Human Capital?

Human capital is a loose term that refers to the educational attainment, knowledge, experience, and skills of an employee. The theory of human capital is relatively new in finance and economics. It states that companies have an incentive to seek productive human capital and to add to the human capital of their existing employees. Put another way, human capital is the concept that recognizes labour capital is not homogeneous.

Human capital the intangible economic value of a worker's experience and skills. This includes factors like education, training, intelligence, skills, health, and other things employers value such as loyalty and punctuality.

The human capital theory posits that human beings can increase their productive capacity through greater education and skills training.

Critics of the theory argue that it is flawed, overly simplistic, and confounds labour with capital.

2.2.2 The Origins of the Human Capital Theory

In the 1960s, economists Gary Becker and Theodore Schultz pointed out that education and training were investments that could add to productivity.As the world accumulated more and more physical capital, the opportunity cost of going to school declined. Education became an increasingly important component of the workforce. The term was also adopted by corporate finance and became part of intellectual capital, and more broadly as human capital.

Intellectual and human capital are treated as renewable sources of productivity. Organizations try to cultivate these sources, hoping for added innovation or creativity. Sometimes, a business problem requires more than just new machines or more money.

The possible downside of relying too heavily on human capital is that it is portable. Human capital is always owned by the employee, never the employer. Unlike structural capital equipment, a human employee can leave an organization. Most organizations take steps to support their most useful employees to prevent them from leaving for other firms.

2.2.3 Critiques of the Human Capital Theory

Not all economists agreed that human capital directly raises productivity. In 1976, for instance, Harvard economist Richard Freeman argued that human capital only acted as a signal about talent and ability; real productivity came later through training, motivation, and capital equipment. He concluded that human capital should not be considered a factor of production.

Around the same time, Marxian economists Samuel Bowels and Herbert Gintis argued against the human capital theory, stating that turning people (i.e.labour) into capital essentially squashes arguments around class conflict and efforts to empower workers' rights.

In the 1980s and 1990s, with the rise of behavioural economics, new critiques were levelled at the human capital theory in that it relies on the assumption that human beings are rational actors. Therefore, the human capital theory will experience the same defects and limitations when it attempts to explain phenomena because its basic assumptions on human motives, goals, and decisions are, it turns out, not well-grounded.

More modern critiques from sociologists and anthropologists argue against the human capital theory, saying it offers extremely simple principles that purport to explain everyone's wages, all the time or, a universal connection between human capital, productivity, and income. But when researchers look closely at this, for the most part, productivity differences between individuals cannot be measured objectively.

According to a 2018 paper, studies that claim to find a link between income and productivity do so by using circular logic. And when we restrict ourselves to the objective measurement of productivity, we find that individual productivity differences are systematically too small to account for levels of income inequality.

2.3 INVESTMENT IN HUMAN CAPITAL

Workers undertake three kinds of labour market investment:

1. Education and Training

2. Migration

3. Search for a new job

All the three involve initial cost in the hope and expectation that they will gain in future. Such an investment is called as investment in human capital. Here, the workers embody a set of skills in themselves which can be rented out to the employers. Knowledge and skills that workers get by investing in education and training help them generating a stock of human capital whereas migration and job search increase the value of capital. Society's total wealth includes human and non-human capital. Human capital includes expenditure on education, training and migration. Non-human capital includes expenditure on building, machinery, equipment, etc.

Investment in human capital and particularly on education and training takes place in three stages.

1. During early childhood – When generally parents resources and guidance are used to acquire knowledge in basic language, mathematical skills and attitude towards learning.

2. During teenage – it includes the acquisition of knowledge and skill at the high school or vocational training.

3. After entering into job market – here workers may decide to add to their human capital on the part-time basis, through on the job training or by participating in short-term training programmes.

2.4 COSTS AND LIFE-TIME BENEFITS TO EDUCATION

People invest in education because they believe that additional schooling would make them better off or would make them better off or would increase their living standards. It was noted earlier that additional years of schooling involve two types of costs for the investor.

1. Monetary cost – for tuition fee, books, etc.

2. Psychic cost – toil and trouble of additional schooling.

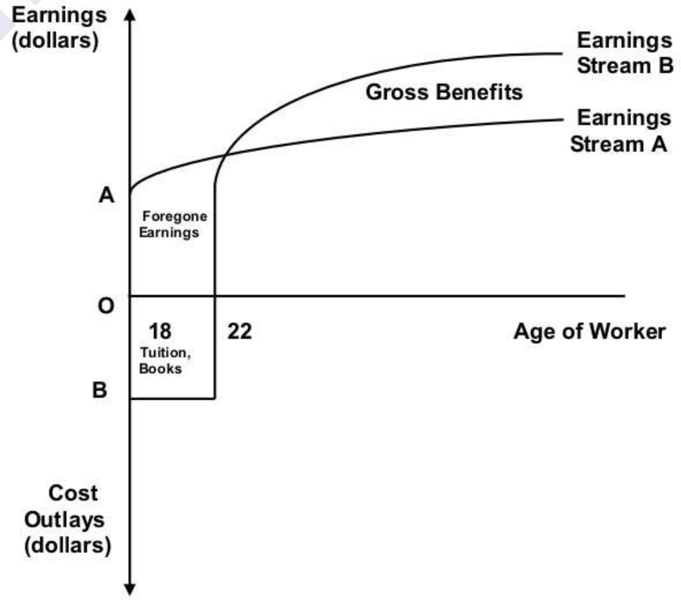
Also, it is noted that additional benefits from schooling are in the form of increased future earnings. A person would invest in education when he expects his earnings to rise with every additional year of schooling.

Following diagram depicts a situation in which a human capital investor has two choices:

1. Taking up stream A of schooling where earnings begin at very early stage (at the age of 18 years)

2. Taking up stream B of schooling where earnings begin at a later stage (at the age of 18 years) and there is an additional cost involved in schooling.

Figure No. 2.1



The earnings curve of stream A begins immediately but does not rise much. The earnings curve of stream B is negative in the beginning (due to additional cost of schooling) and then it rises above the earnings curve of stream A. the basic points to be noted from the discussion so far and the diagram above are as follows:

1. Those who value present period more than the future period would go for stream A and spend less on education. But those who are future oriented would invest more in schooling. The present oriented people would have very high discount rate ® in the equations (1) and (2) and hence for such a person, benefits of schooling would be smaller.

2. Most of those who would invest in schooling would be young. Younger people have larger present value for future benefits on investment in education simply because they have more years with them to enjoy these benefits. That is the reason why the younger people are likely to invest more in schooling and training than the older people.

3. Investment in education would be inversely related to cost of schooling. That is, if the tuition fees are high (other things remaining the same), investment in education would be low.

4. Higher the gap between the earnings of high school educated and college educated, more will be an investment in education. Earning differentials are important determinant of investment in schooling. Human capital theory predicts that the demand for education is positively related to the increases in lifetime earnings that occur due to college education. And hence, if the average earning differentials between college graduates and high school graduates decline, the demand for college education would also decline.

More recently, the importance of friends, ethnic affiliation and neighbourhoods have become important in the decision making regarding human capital investment. The educational and occupational choices of friends appear to have a significant effect on an individual's human capital investment. This may be because the experiences of others may be considered as useful in the environment of uncertainty regarding the future benefits of any human capital investment or investment in college education.

2.5 SUMMARY

1. In the recent years, importance of investment in human capital vis-à-vis an investment in physical capital is clearly emphasized.

2. Investment in human capital may involve an investment in education, training, health, migration, etc.

3. Human capital investment, like any other investment involves current expenditure for future earnings.

4. Schooling is an important form of human capital investment that tends to increase future earnings and employability of a worker.

5. Returns on investment in human capital are compared with the cost of investment before taking a decision regarding investment.

2.6 QUESTIONS

Q1. Explain the theory of human capital in detail.

Q2. Write a note on –

a. Investment in Human Capital

b. Costs and Life-Time Benefits to Education

❖❖❖❖

MODULE 2: APPROACHES IN LABOUR MARKETS

3

LABOUR DEMAND

Unit Structure:

3.0 OBJECTIVES

- To analyse demand for labour.
- To understand short run and long run theories of labour demand.
- To discuss the determinants of labour Demand.

3.1 INTRODUCTION

In economics, labour is a measure of the work done by human beings. It is conventionally contrasted with such other factors of production as land and capital. Labour economics seeks to understand the functioning and dynamics of the markets for labour. Labour markets function through the interaction of workers and employers. Labour economics looks at the suppliers of labour services (workers), the demands of labour services (employers), and attempts to understand the resulting pattern of wages, employment, and income.

The labour in India consists of about 487 million workers, the second largest after China. In 2011, India had about 487 million workers compared to China's 795 million and United States' 154 million.

The labour market is like other markets in that a commodity (labour services) is bought and sold. It differs from most product markets in several important ways. Among these differences are:

- labour services are rented, not sold,
- labour productivity is affected by pay and working conditions, and
- The suppliers of labour care about the way in which the labour is used.

Labour demand is a derived demand; that is, hiring labour is not desired for its own sake but rather because it aids in producing output, which contributes to an employer's revenue and hence profits. The demand for an additional amount of labour depends on the Marginal Revenue Product (MRP) and the marginal cost (MC) of the worker. The MRP is calculated by multiplying the price of the end product or service by the Marginal Physical Product of the worker. If the MRP is greater than a firm's Marginal Cost, then the firm will employ the worker since doing so will increase profit. The firm only employs however up to the point where MRP=MC, and not beyond, in economic theory.

3.2 THE THEORY OF LABOUR DEMAND

3.2.1 Short Run Demand for Labour:

Marginal revenue product of labour

Marginal revenue productivity of labour (MRPL) is a theory of the demand for labour and market wage determination where workers are assumed to be paid the value of their marginal revenue product to the business.

Marginal Revenue Product (MRPL) measures the change in total revenue for a firm from selling the output produced by additional workers employed.

MRPL = Marginal Physical Product x Price of Output per unit

- Marginal physical product is the change in output resulting from employing one extra worker.

- The price of output is determined in the product market – in other words, the price that the firm can get in the market for the output that they have produced A simple numerical example of marginal revenue product is shown in the next table:

Table No. 3.1

Numerical Example of Marginal Revenue Product

Labour	Capital (K)	Output (Q)	MPP	Price (Rs.)	MRP = MPP × P (Rs.)
0	5	0	-	5	-
1	5	30	30	5	150
2	5	70	40	5	200
3	5	120	50	5	250
4	5	180	60	5	300
5	5	270	90	5	450
6	5	330	60	5	300
7	5	370	40	5	200
8	5	400	30	5	150
9	5	420	20	5	100
10	5	430	10	5	50

We are assuming in this example that the firm is operating in a perfectly competitive market such that the demand curve for its output is perfectly elastic at Rs. 5 per unit. Marginal revenue product follows directly the behaviour of marginal physical product. Initially as more workers are added to a fixed amount of capital, the marginal product is assumed to rise. However beyond the 5th worker employed, extra units of labour lead to diminishing returns. As marginal physical product falls, so too does marginal revenue product.

The story is different is the firm is operating in an imperfectly competitive market where the demand curve for its product is downward sloping. In the next numerical example we see that as output increases, the firm may have to accept a lower price. This has an impact on the marginal revenue product of employing extra units of labour.

Table No. 3.2

Labour	Capital (K)	Output (Q)	MPP	Price (Rs.)	MRP=MPP×P (Rs.)
0	5	0	-	10.0	-
1	5	25	25	9.60	240
2	5	60	35	9.00	315
3	5	100	40	8.70	348
4	5	150	50	8.20	410
5	5	210	60	7.90	474
6	5	280	70	7.70	539
7	5	360	80	7.00	560
8	5	430	70	6.80	376
9	5	450	20	6.50	130
10	5	460	10	6.00	60

MRP theory suggests that wage differentials result from differences in labour productivity and the value of the output that the labour input produces. The MRP theory outlined below is based on the assumption of a perfectly competitive labour market and rests on a number of key assumptions that realistically are unlikely to exist in the real world. Most of our labour markets are imperfect – this is one of the many reasons for the existence and persistence of large earnings differentials between occupations which we explore a little later on.

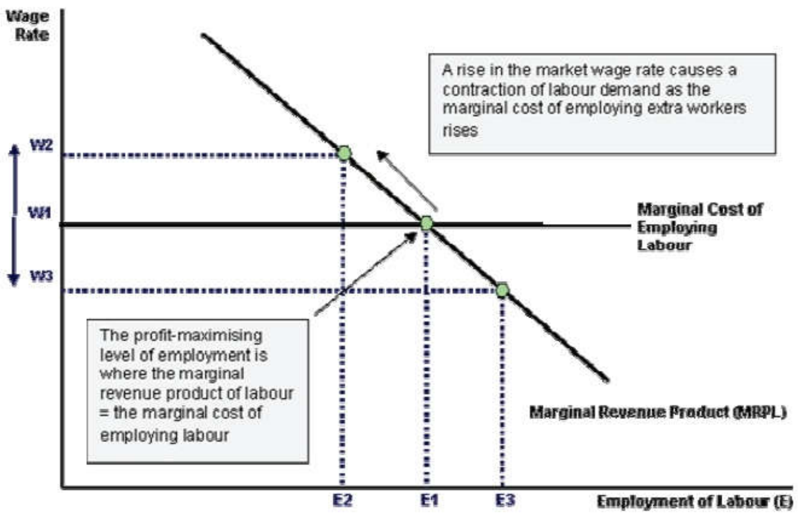
The main assumptions of the marginal revenue productivity theory of the demand for labour are:

- Workers are homogeneous in terms of their ability and productivity.
- Firms have no buying power when demanding workers (i.e. they have no monopsony power).
- Trade unions have no impact on the available labour supply (the possible impact on unions on wage determination is considered later).
- The physical productivity of each worker can be accurately and objectively measured and the market value of the output produced by the labour force can be calculated.
- The industry supply of labour is assumed to be perfectly elastic. Workers are occupationally and geographically mobile and can be hired at a constant wage rate.

The profit maximising level of employment:

The profit maximising level of employment occurs when a firm hires worker up to the point where the marginal cost of employing an extra worker equals the marginal revenue product of labour. This is shown in the labour demand diagram shown below.

Figure No. 3.1



Shifts in the labour demand curve:

Marginal revenue productivity of labour will increase when there is -

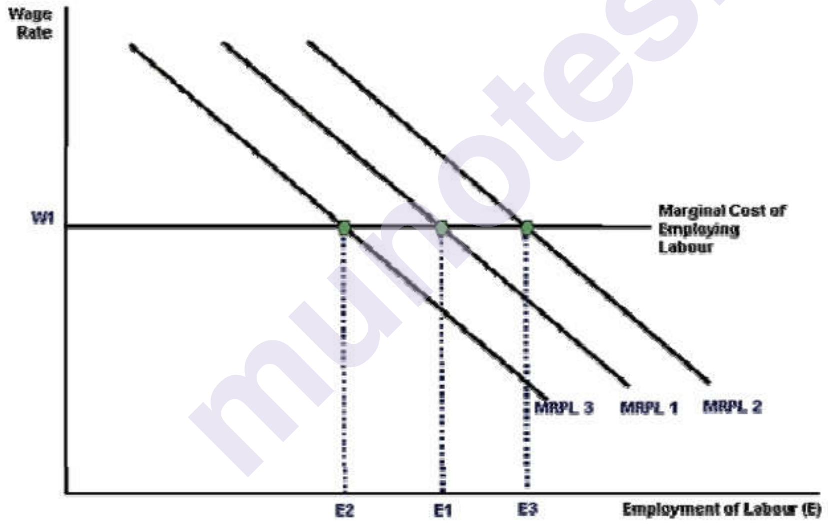
- An increase in labour productivity (MPP) e.g. arising from improvements in the quality of the labour force through training, better capital inputs, or better management.

- A higher demand for the final product which increases the price of output so firms hire extra workers and thus demand for labour increases, shifting the labour demand curve to the right.

- The price of a substitute input e.g. capital rises – this makes employing labour more attractive to the employer assuming that there has been no change in the relative productivity of labour over capital.

The next diagram shows how this causes an outward shift in the labour demand curve. For a given wage rate W1, a profit maximising firm will employ more workers. Total employment in the market will rise.

Figure No. 3.2



3.2.2 Long Run Demand for Labour:

Long Run Demand for Labour

- In the long run, the profit-maximizing firm can vary the inputs of both labour (L) and capital (K)

- o we assume that there are diminishing marginal returns to adding more units of K (holding L constant) and to adding more units of L (holding K constant)

- o we assume that the first derivatives of $Q = f(L, K)$ are positive and the second derivatives are negative.

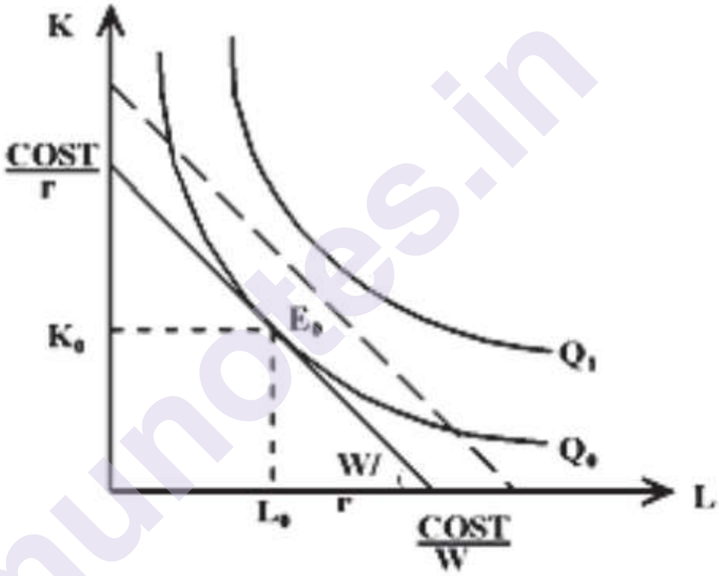
- An iso-quant-iso-cost diagram can be used [i] to determine the optimal combination of L and K and [ii] to derive the demand for labour when K is a variable input into the production process

Isoquants

- Each iso-quant depicts the various combinations of L and K which can be used to produce a particular level of output, say Qo in Figure 3.3.

- Iso-quants depicting larger quantities of output (such as Q1 in Figure 3.3) will be further from the origin (they require greater quantities of inputs).

Figure No. 3.3



- The shape of the isoquant reflects the technological possibilities for substituting L and K in the production process.

- Isoquants are convex to the origin.

- The slope of the isoquant is equal to MPL/MPK, where MPL is the marginal product of labour and MPK is the marginal product of capital.

- Given diminishing returns to hiring each factor, the slope of the isoquant exhibits a diminishing marginal rate of technical substitution between L and K.

- Larger and larger amounts of L must be substituted for each unit of K as the amount of K used in the production process decreases.

Iso-cost Lines:

- Assume that factor prices are given: 'W' is the wage paid to labour and 'r' is the implicit (rental) cost of using capital for a given COST outlay, a firm can purchase different quantities of L and K according to the following equation:
  COST = WL + rK,

- An iso-cost line depicts the various quantities of L and K which can be purchased for a particular COST outlay 45.

- Re-arranging the COST equation produces the following equation for an iso-cost line:
  K = COST/r – (W/r)L

- As shown in Figure 3.3, the slope of the solid iso-cost line is – (W/r), the horizontal intercept is COST/W and the vertical intercept is COST/r

- The greater the COST outlay, the further the iso-cost line will be from the origin (more of both L and K can be purchased).

In Figure 3.3, the dashed iso-cost line has a higher cost outlay than the solid iso-cost line; the dashed iso-cost line is parallel to the solid iso-cost line (both iso-cost lines have slope – W/r).

The Optimal Quantities of L and K

- A profit-maximizing firm will choose the least cost combination of L and K to produce a particular level of output, such as Qo

- The least cost factor input combination will be determined by the tangency of an iso-cost line with the Qo iso-quant the closer the iso-cost line to the origin, the smaller the cost

- As shown in Figure 3.3, the optimal tangency position is given by point Eo given factor prices (W, r), the optimal combination of inputs to produce Qo is Lo and Ko

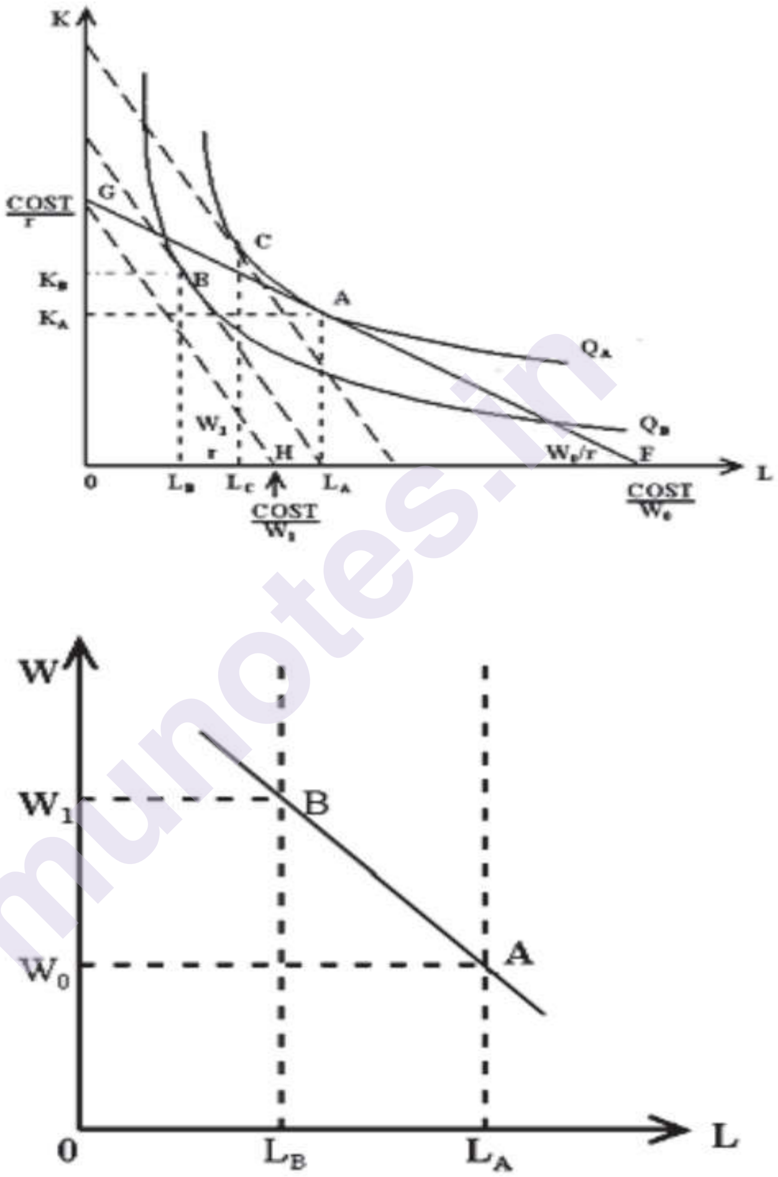
- At this optimal tangency point, the slope (W/r) of the iso-cost line is equal to the MPL/MPK slope of the iso-quant the ratio of factor marginal products is equal to relative factor prices; the firm's internal rate of factor substitution is equal to the rate at which the factors can be substituted in the market place.

To summarize, in the short run the firm hires labour up to the point where the VMPL (of MRPL) is equal to the wage rate and in the long run the firm hires labour up to the point where the relative value of the MPL (in terms of the MPK) is equal to the relative price of labour (W/r).

Deriving the Long-run Demand for Labour

As illustrated in Figure 3.4, the long-run demand for labour can be derived by determining the optimal combination of L and K for different wage rates, holding the cost of capital (r) constant.

Figure No. 3.4



Given a wage rate Wo the firm maximizes profits at point A in the upper diagram, the GF iso-cost line (with slope Wo/r) is tangent to the Qa isoquant at point A the firm uses La units of labour and Ka units of capital to produce Qa units of output in the lower diagram, in the long run the firm hires La unit of labour when the wage rate is Wo; point A is one point on the long-run demand for labour.

Now suppose that the wage rate increases to W1 the GF isocost line will rotate inwards to the dashed line GH (the horizontal intercept COST/W1 is now located closer to the origin) and the new 47 set of dashed iso-cost lines will be steeper (with slope W1/r) an increase in the wage rate also shifts firms' marginal cost curves upwards, resulting in higher output prices and a lower level of output demanded (say Qb) in the product market.

As discussed below, the reduction in output depends on the price elasticity of the product demand curve.

The firm now minimizes costs at point B in the upper diagram of Figure 4.6, where a dashed iso-cost line with slope W1/r is tangent to the lower Qb iso-quant the increase in wage rates from Wo to W1 has resulted in a decrease in the amount of labour (from La to Lb) and an increase in the amount of capital (from Ka to Kb) used in the production process in the lower diagram, the firm hires Lb units of labour when the wage rate is W1 (holding the cost of capital constant) point B is a second point on the long-run demand for labour an increase in the wage rate (from Wo to W1 in Figure 5) reduces the long-run demand for labour (from La to Lb) the reduction in the demand for labour from an increase in wage rates can be broken down into a substitution effect and a scale effect.

The substitution effect measures the effect of a change in an input price on the amount of inputs used to produce a given output level (say Qa) in Figure 4.6 the pure substitution effect from an increase in the wage rate from Wo to W1 is represented by the movement from point A to C to produce the same output level Qa at the higher wage rate W1, the profit-maximizing firm will use less labour (Lc) and more capital an increase in wage rates from Wo to W1 has a pure (output constant) substitution effect equal to La minus Lc the scale effect measures the effect of a change in output levels (the scale of operation) on the amount of inputs used, holding input prices constant.

In Figure 3.4 the scale effect is represented by the movement from point C to B holding input prices constant, a reduction in output from Qa to Qb results in less labour (Lb) and less capital used in the production process an increase in wage rates from Wo to W1 has a scale effect equal to Lc minus Lb both the substitution and scale effects reduce the quantity of labour demanded when the wage rate increases; the long-run labour demand curve unambiguously slopes down.

Since there is no substitution effect possible in the short run (with a fixed capital stock), the short-run demand for labour will be steeper than the long-run demand for labour in the long run, the firm can respond to an increase in wage rates by substituting capital for labour and thus the long-run effect on the quantity of labour demanded for a given change in the wage rate will be larger than the short-run effect.

3.3 TYPES OF MARKETS

In labour markets, labour is supplied by households and demanded by firms Labour Market in India can be classified into following types:

1) National Labour Market:

A national labour market is one in which most job search by employers and firms takes place on a national level. The markets for college professors, top management positions in large corporations, and similar occupations are national labour markets.

2) Local Labour Market:

Most job search takes place at a local level in a local labour market. Secretaries, carpenters, truck drivers, electricians, and lathe operators are employed through local labour markets. A national labour market exists only when there are few employers and employees in most geographical regions. Local labour markets exist when there are many employers and employees in most geographical regions.

3) Internal Labour Market:

An internal labour market is said to exist within a firm if the firm fills higher level positions in the firm primarily by promotion from within the firm

4) Primary Labour Market:

Jobs in the primary labour market are characterized by high wages and stable employment relationships. Examples of jobs in the primary labour market include: accountant, lawyer, teacher, carpenter, and plumber.

5) Secondary Labour Market:

Workers employed in the secondary labour market receive low wages and experience unstable employment relationships. Workers in fast-food restaurants, gas station attendants, dishwashers, janitors, etc. are employed in the secondary labour market.

3.4 INDUSTRY DEMAND FOR LABOUR

The demand for labour by an industry as a function of the wage rate. At any given wage rate, industry demand for labour depends on output. If wage rates fall, this can raise industry demand for labour in three ways. First, labour may be substituted for other inputs; second, a reduction in costs may lower price and increase demand for the industry's output; and third, in the longer run a rise in profits may induce new firms to enter the industry and take on additional workers. Industry demand for labour is more elastic the better the opportunities for substitution between labour and other inputs, the more elastic the demand for the industry's output, and the more elastic the supply of potential entrants.

3.5 DETERMINANTS OF LABOUR DEMAND

1. Product demand:

As seen earlier, the demand for labour is derived demand. It depends on the demand for product for which the labour is used. For example, if the demand for automobiles rises, the demand for labour in the automobile industry will go up. So, in other words, changes in the product demand will change the price of the product and hence the marginal revenue product of the labour will change and hence the demand for labour will change.

2. Productivity:

An increase in the marginal productivity of labour will increase the demand for labour (if the price of product remains unchanged). Conversely, a fall in marginal product will bring about a fall in the demand for labour.

3. Prices of other inputs:

If the price of substitute to labour rises, the demand for labour will increase and if the price of substitute input falls, the demand for labour will fall (other things remaining the same). For instance, if use of machines for a particular production process becomes cheaper, the demand for labour for that product will fall.

4. Number of firms:

Generally, an increase in the number of firms or employers leads to an increase in demand for labour. For example, if the number of educational institutions increases, the demand for teachers will go up.

3.6 SUMMARY

1. Labour economics aims at understanding functioning and dynamics of labour market.
2. Labour market has certain distinct characteristics and hence it is different from other types of market.
3. Demand for labour is a derived demand.
4. There are different components of labour market.
5. There are two major variants of theories of demand for labour – short run theory of labour demand and long run theory of demand for labour.
6. Marginal revenue productivity theory of labour is a short-run explanation of demand for labour.

7. Long run demand for labour is explained with the help of isoquants.

8. There are many factors influencing the demand for labour.

3.7 QUESTIONS

Q.1 Explain the concept of demand for labour. State how the demand for labour is different from any other demand.

Q.2 Explain the nature of demand for labour in the short as well as long run.

Q.3 Discuss the factors influencing the demand for labour.

❖❖❖❖

4

LABOUR SUPPLY

Unit Structure:

4.0 OBJECTIVES

- To study the theory of supply.
- To understand the work-leisure choice in indifference curves.
- To study budget constraint and utility maximisation.
- To study the backward-bending labour supply curve and its applications.

4.1 INTRODUCTION

The supply of labour signifies the number of workers of a given type of labour which would offer themselves for employment of various wage rates. The supply of labour may mean three things:

(i) Supply of labour to a firm,
(ii) Supply of labour to the industry, and
(iii) Supply of labour to the entire economy.

To a given firm, the supply of labour is perfectly elastic. That means, at a given wage rate, a firm may be able to get as many workers as required. This is because at the current wage rate, it can engage as many workers as it wants. A single firm's demand would constitute only a negligible fraction of the total supply of labour. But for the industry as a whole, the supply of labour is not infinitely elastic. In other words, an industry may not get as many workers as it wants, at a given wage rate. If it wants to employ more labour, it may have to attract it from other industries by offering a higher wages. It can also work with the existing labour force overtime which in effect will increase the labour supply for that industry.

The supply of labour for a particular industry is subject to the law of supply, i.e., at lower wages, supply of labour will be low and at higher wages, supply of labour will be high. This makes the supply of labour curve to be positive in slope. That is the supply curve of labour for an industry rises upwards from left to the right.

The supply of labour for the entire economy depends upon many economic, social and political and institutional factors. To mention a few

1. Attitude of women towards work,
2. working age of population
3. age of students for schooling and college education
4. Possibilities of part-time employment,
5. Size, age structure and composition of the population
6. Attitude to marriage,
7. Average size of the family

Concept of supply of labour under perfect and imperfect markets may be considered differently. A given supply of labour under perfectly competitive conditions gets distributed in various employments in such a way as to make the marginal productivity of labour in all the employment the same. This is because, labour can move freely from one job to another. But if there is no perfect mobility of labour, or labour cannot move freely from one employment to another; the marginal productivity will be different in different employments and wages will also be different even for the same kind of labour.

Further, the supply of labour may be affected by trade union activity. Working class may refuse to work for a certain period of time as a result of a call by the trade union. In such a case, there will be reduction in the labour supply. The workers may not accept wages offered by the employer if such wages do not ensure the maintenance of the standard of living to which they are accustomed. But it is only when higher wages are justified by higher marginal productivity, that high wages will be paid. In the long run, marginal productivity, wages and the standard of living tend to adjust to one another.

On the whole it may be said that the number of potential workers being given, the supply of labour can be defined as the schedule of units of labour to the prevailing rates of wages, which depends on the following factors: (i) the number of workers who are willing and able to work at different wages, and (ii) the number of working hours that each worker is willing and able to put in at different wages.

Determinants of the supply of labour

Supply of labour in a market depends upon many factors. Following are some of the –

(i) Other Wage Rates: An increase in the wages paid in other occupations for which workers in a particular labour market are qualified will decrease labour supply. In the case of a decrease in the wages paid in other occupations, there will be an increase labour supply.

(ii) (Non-wage Income: An increase in income other than from employment will decrease labour supply. On the other hand, a decrease in such income will increase the labour supply.

(iii) Preferences for Work versus Leisure: A net increase in people's preferences for work relative to leisure will increase labour supply. A net decrease in such preferences will decrease labour supply.

(iv) Non-wage Aspects of the Job: An improvement of the nonwage aspects of job will increase labour supply. A worsening of the non-wage aspects of job will decrease labour supply.

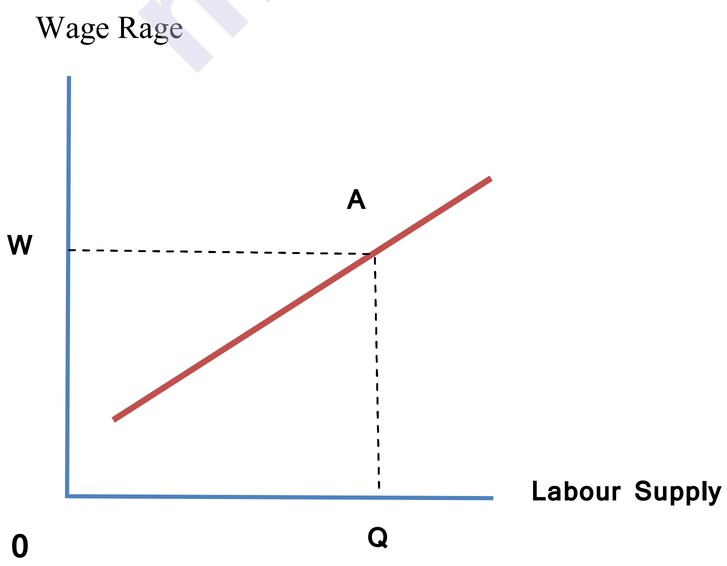
(v) Number of Qualified Suppliers: An increase in the number of qualified suppliers of a specific grade of labour will increase labour supply. A decrease in such suppliers will decrease the labour supply.

4.2 THE THEORY OF SUPPLY

In a competitive market, the supply of labour is determined by the rate of wages. The higher the wage rate, the more workers are willing to come to work, and the lower the wage rate, the lower the number of workers willing to work. Due to such a direct relationship between the wage rate and the supply of labour, the curve of the supply of labour in a competitive market tends to be positive, that is, from left to right.

Figure No. 4.1

Aggregate Labour Supply Curve



In a competitive market, in addition to wage rates, further factors lead to a shift in the labour supply curve.

A. The size of the able-bodied population:

Generally, the working population is made up of people between the ages of 16 and 60 who are willing to work and have the ability to work. The working population is affected by factors such as retirement age, school leaving age, and migration. If the size of the working population is large, the labour supply curve shifts to the right.

B. Migration:

Migration has a huge impact on the labour market. There is a general tendency to migrate from low-wage areas to high-wage areas, leading to higher labour supply in high-wage countries and labour shortages in low-wage countries.

C. People's preferences for work:

If people prefer work, the supply of labour increases. People's preference for work is influenced by factors such as return on work, other forms of work benefits, cost of living, and so on.

D. Non-financial benefits:

Non-financial benefits such as changes in the nature of work, financial security, leave at work, the possibility of promotion, etc. can also change the supply of workers in the market. The supply curve shifts to the right if such non-financial benefits improve.

E. Ratio of direct taxes:

When direct taxes, such as income taxes, are higher, people prefer leisure to work, which reduces the supply of labour.

F. Proportion of dependent population:

People prefer work if the dependent population, such as children, the elders, etc., are more dependent on the working population. This automatically increases the supply of labour. And the labour supply curve shifts to the right.

4.3 WORK-LEISURE CHOICE IN INDIFFERENCE CURVES

With adequate income, leisure is just as important to the worker.In the case of workers after a certain income level, there is a conflict between the time given for work and the time of leisure. In such a case, the worker has to decide whether to work harder and earn more income or to use the time left after fulfilling his usual responsibilities for leisure and recreation. Here it is time for him to choose between the two variables. We will explain how workers make this choice with the help of indifference curves.

Indifference curve analysis can be used to clarify a person's choice between income and leisure and to show why higher overtime wage rates need to be paid if workers want to get more working hours. One thing to keep in mind here is that extra time is earned by giving some free time to work. It means that extra income is earned by sacrificing leisure time. The higher the amount of this leisure sacrifice, the higher the amount of work, the higher the income.

Leisure time can be used for relaxation, sleeping, playing, listening to music on the radio and television, and so on. All these things give satisfaction to a person. Therefore, in economics, leisure is considered to be a common thing, the use of which gives satisfaction to a person. Income, on the other hand, represents the general purchasing power that can be used to purchase goods and services to meet various needs. Thus, income indirectly provides satisfaction. Therefore, we can draw the indifference curve between income and leisure by assuming two common objects.

Figure No .42.
Work-Leisure Choice in Indifference Curves

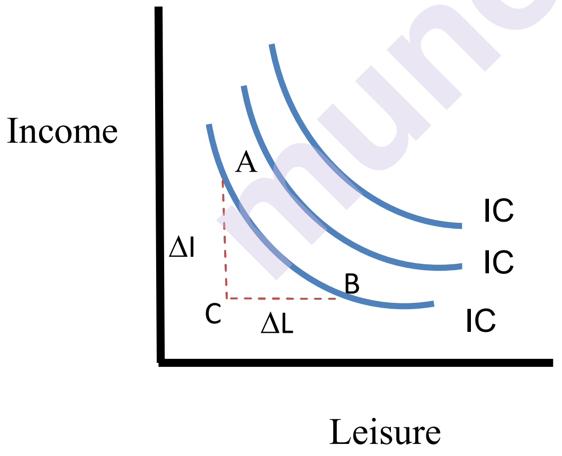


Figure 4.2 shows aindifference curve map between income and leisure. This curve has all the properties of a regular indifference curve. These properties are as follows.

1. Each indifference curve represents different alternative combinations of income and leisure that provide the same level of satisfaction to the individual.

2. The indifference curve is downward from left to right.

3. The indifference curve is convex to the origin.

4. Two indifference curves never intersect each other.

5. The indifference curve on the right is more satisfying than the indifference curve on the left.

The slope of the indifference curve measuring the marginal rate of substitution (MRS) between leisure and income represents the trade-off between income and leisure. It means that if a worker wants to earn extra income, he has to reduce his leisure and if he wants to get extra leisure, his income will decrease.

Figure 4.2 shows that the worker working on the indifference curve IC1 at point B is ready to accept an income reduction of ΔI (= AC) for one hour (ΔL) or BC leisure. On the other hand, at point A, the same working person on the indifference curve IC1 is willing to give up one hour (ΔL) or BC for an incremental income of (I (= AC).

4.4 BUDGET CONSTRAINT

The person's consumption of goods and leisure is constrained by her time and by her income. Part of the person's income (such as property income, dividends, and lottery prizes) is independent of how many hours she works. We denote this "nonlabour income" by V. Let h be the number of hours the person will allocate to the labor market during the period and w be the hourly wage rate. The person's budget constraint can be written as

C = wh + V

In words, the dollar value of expenditures on goods (C) must equal the sum of labor earnings (wh) and nonlabor income (V).

As we will see, the wage rate plays a central role in the labor supply decision. Initially, we assume that the wage rate is constant for a particular person, so the person receives the same hourly wage regardless of how many hours she works. In fact, the "marginal" wage rate (that is, the wage rate received for the last hour worked) generally depends on how many hours a person works. Persons who work over 40 hours per week typically receive an overtime premium, and the wage rate in part-time jobs is often lower than the wage rate in full-time jobs. For now, we ignore the possibility that a worker's marginal wage may depend on how many hours she chooses to work.

Given the assumption of a constant wage rate, it is easy to graph the budget constraint. The person has two alternative uses for her time: work or leisure.

The total time allocated to each of these activities must equal the total time available in the period.

We can then rewrite the budget constraint as -

C = w(T - L) + V (2-8) or C = (wT + V) - wL

This last equation is in the form of a line, and the slope is the negative of the wage rate (or – w).

4.5 UTILITY MAXIMISATION

Utility maximisation refers to the concept that individuals and firms seek to get the highest satisfaction from their economic decisions.

For example, when deciding how to spend a fixed some, individuals will purchase the combination of goods/services that give the most satisfaction.

Utility maximisation can also refer to other decisions – for example, the optimal number of hours for labour to supply their labour. Working more increases income, but reduces leisure time.

Classical economics

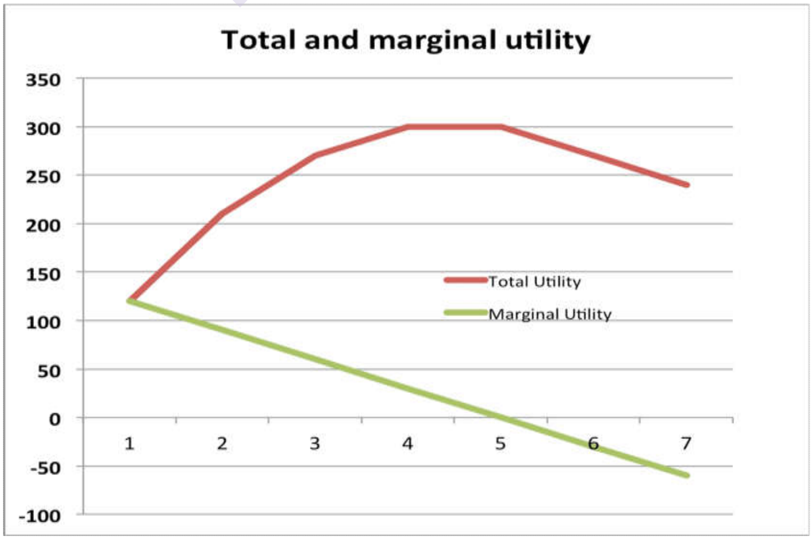
Utility maximisation is an important concept in classical economics. It developed from the utilitarian philosophers of Jeremy Bentham and John Stuart Mill. Early economists such as Alfred Marshall incorporated utility maximisation into economic theory.

An important assumption of classical economics is that the price consumers are willing to pay is a good approximation to the utility that they get from the good. If people are willing to pay £800 for an iPhone X, then this suggests the consumer must get a utility of at least £800.

Diminishing marginal utility

Economists such as Carl Menger, William Stanley Jevons and Marie-Esprit-Léon Walras. And Alfred Marshall developed ideas such as diminishing marginal utility. The idea that after a certain point, extra quantities of a good lead to a decline in the marginal utility. (For example – The first car gives high utility, but the utility of a second is much lower.

Figure No. 4.3



Marginal utility shapes an individual demand curve, as the utility from extra units declines, consumers are willing to pay a lower price – hence a downwardly sloping demand curve.

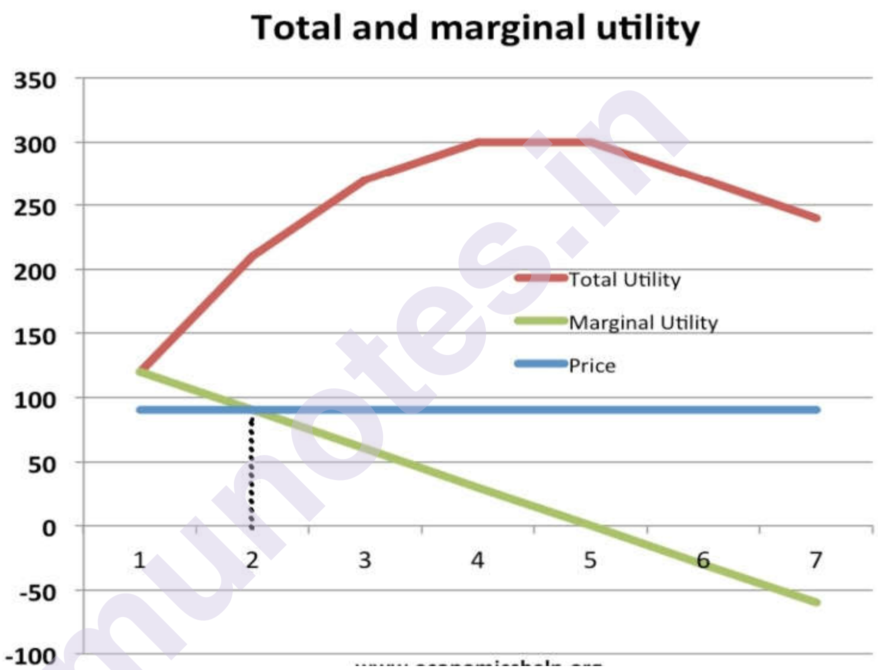
How individuals achieve utility maximisation

How much to consume?

A consumer will consume a good up to the point where the marginal utility is greater than or equal to the price.

If you feel a sandwich gives you more utility than the cost of buying then you will continue to buy

Figure No. 4.4



In this example, the optimal consumption of units is 2. A third one gives you a utility equal to 50p – but this is less than the price.

When choosing between different goods, the Equi-Marginal principle argues that consumers will maximise total utility from their incomes by consuming that combination of goods where:

$$\frac{MUa}{MUb} = \frac{Pa}{Pb}$$

Another way of showing utility maximisation is through the use of indifference curves and budget lines

- Indifference curves show different combinations of goods which gave the same utility.

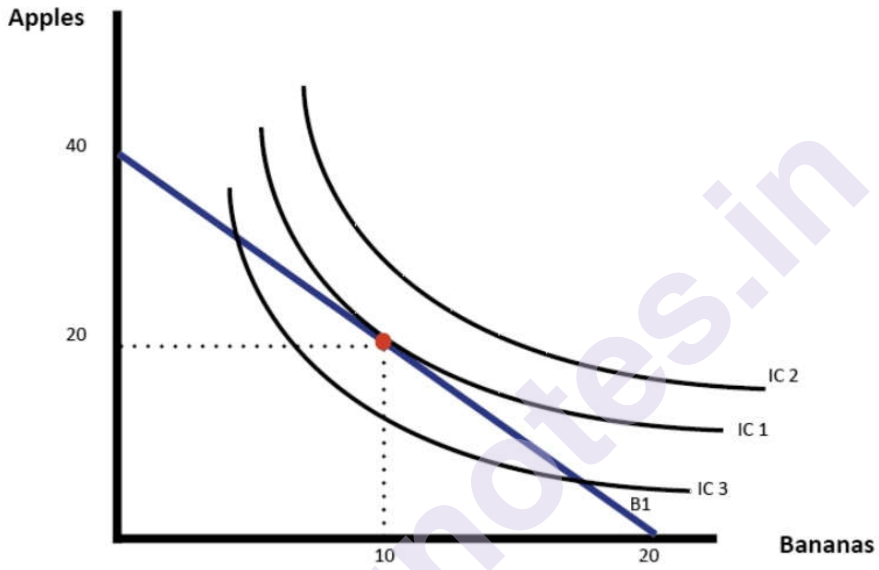
- A budge line shows disposable income and the maximum potential goods that can be bought

- Indifference curves further to the right are more desirable as they have bigger combinations of goods.

- Utility will be maximised at the furthest indifference curve still affordable.

Optimal choice of goods for consumer

Figure No. 4.5



Limitations of utility maximisation

Ordinal utility:

Ordinal utility states consumers find it hard to give exact values of utility, but they can order by preference – e.g. I prefer apples to bananas. This theory of ordinal utility was developed by John Hicks and gives less precise but rough guides to utility of consumers.

Irrational behaviour. Classical economics generally assumes individuals are rational and seek to maximise utility. However, in the real world, this may not be the case. Other factors affecting choice

- Impulsive behaviour – buying goods which are later regretted.

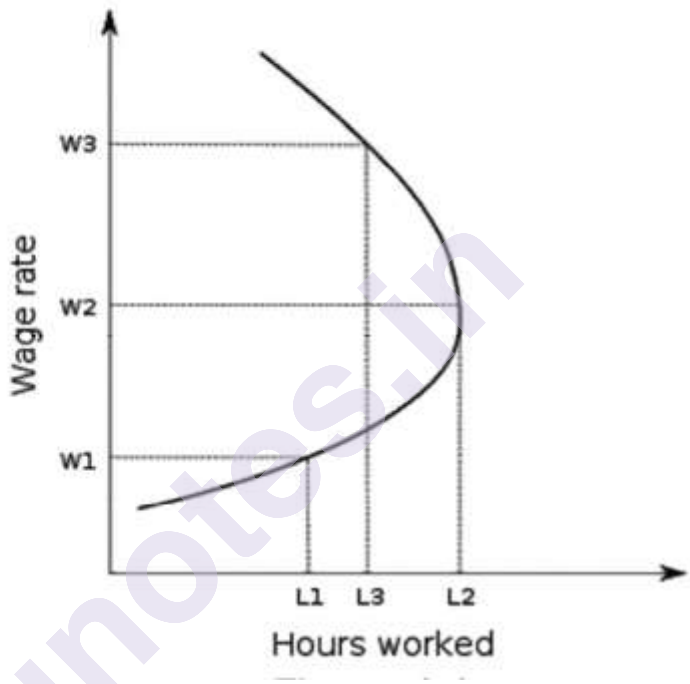
- Loyalty, e.g. loyalty to local shops rather than buy cheaper from supermarkets.

- Sense of morality, e.g. not drinking alcohol.

4.6 BACKWARD-BENDING LABOUR SUPPLY CURVE AND ITS APPLICATIONS

Backward bending supply curve is a theorem that holds that as wage increases, people substitute leisure for working and hence when wages are very high, the supply of labour in the market is low.

Figure No. 4.6



As per the diagram above, if the wages go up from W1 to W2, the supply of labour increases from L1 to L2. This is because the substitution effect is stronger than the income effect. Increase in wages is accompanied by an increase in hours of work and leisure is substituted for work. On the other hand, as wages go up from W2 to W3, the supply of labour goes down from L2 to L3. This is because an income effect is stronger than the substitution effect. The working class is paid sufficiently high to sustain their current standard of living.

4.7 SUMMARY

- Labour market is a place that allocates jobs to the people and co-ordinates employment related decisions.

- The supply of labour signifies the number of workers of a given type of labour which would offer themselves for employment of various wage rates.

- The supply of labour for the entire economy depends upon many economic, social and political and institutional factors.

- Supply of labour in a market depends upon many factors such as Other Wage Rates, Non-wage Income, Preferences for Work versus Leisure, Number of Qualified Suppliers and Non-wage Aspects of the Job

- India labour market has many peculiar features such as migratory nature of workers, low levels of literacy, etc.

4.8 QUESTIONS

1. Explain the concept of supply of labour. How is the labour supply determined in the labour market?

2. Write a note on backward bending supply curve of labour.

❖❖❖❖

MODULE 3: WAGE ISSUES IN LABOUR MARKETS

5

WAGE ISSUES IN LABOUR MARKETS – I

Unit Structure:

5.0 OBJECTIVES

- To study the theories wages and wages in different markets.
- To understand the wage structure and components of wages.
- To study the share of wages.
- To study the distribution and inequality of wage income.
- To study male-female and inter-sectoral wage differentials.

5.1 INTRODUCTION

The issue of wages is considered to be important not only for raising the standard of living of workers' class but also as a tool to raise production. The economic wellbeing of a worker, their efficiency, standard of living, the wage cost as a part of cost of production and the competitive strength of an industry, is all dependent on the wage-structure. So the problem of wages has all economic, social and political implications. Wages are looked upon differently by different segments of society.

1. Workers and trade unions look at wages as income and not as a price of labour.

2. Management looks at wages as an item of cost and according to them. profit is greatly dependent on the existing wage rate.

3. For community, low wages may be uneconomical in the sense of social cost. That means, low wages may lead many social evils like industrial sickness, reduced efficiency of workers, slum dwellings, etc.

4. For an economy, wages like price of any commodity must perform the function of allocation of labour among different industries.

The term wages is the price paid for the services rendered by the labour in the process of production. Relative wages in different industries are the important determinants of allocation of labour in different sectors. Wages are important in many ways as they affect many macroeconomic variables in the economy like savings, consumption, employment and price level.

Theory of wages has evolved through last two to three centuries and it has undergone different stages of development reflecting the changes in economic and social conditions of different periods of time. A historical review of the wage theories distinguishes three broad divisions:-

i. The classical period (1870s)
ii. Marginal Productivity Theory of Wages (period of great depression-1930s)
iii. Contemporary wage theory in the recent years

In this unit, we will first define and understand all the concepts related to wages and wage determination. Then we will evaluate various wage theories, then we will understand the process of wage determination in competitive and non-competitive markets, we will understand the concept and types of wage differentials and finally we will explain the wage differentials in India.

5.2 THEORIES OF WAGES

5.2.1 Subsistence theory of wages

The main principle of the subsistence theory of wages is that the labourer should be paid wages just sufficient to maintain minimum standard of living for him and his family. If they are paid more than minimum, their families will become bigger and hence the supply of labour will go up in the next generation. For mercantilists, subsistence amount of wages for labourer was to allow traders and manufacturers to accumulate gold and silver. This was because the aggregate amount of precious metal was believed to be an indicator of richness of a country.

Both Adam Smith and Ricardo advocated the doctrine of subsistence wages by restating that the natural price of labour is that price which is necessary to enable the labourer to subsist or maintain minimum standard of living and to perpetuate their race without either increase or decrease. According to Adam Smith, "Full value of any commodity … to the person who possesses it and who means not to use or consume it himself, but to exchange it for the other commodities, is equal to the quantity of labour which it enables him to purchase or command. Labour, therefore, is the real measure of exchangeable value of all commodities… labour was the first price, the original purchase money that was paid for all things". According to him, masters, who enjoy better position, keep wages down to the minimum possible level. Minimum level is that "in order to bring up a family the labour of husband and wife together more than what is precisely necessary for their own maintenance."

To further develop subsistence theory of wages, David Ricardo wrote, "the natural price of labour is that price which is necessary to enable the labourers, one with another to subsist and perpetuate their race without either increase or diminution". According to this theory, wages were supposed to be settled at that level, just sufficient to maintain the workers and his family at minimum subsistence. If wages rise above that level, workers are encouraged to marry and have larger families. The larger the supply of labour, the lower are the wages. If wages fall below subsistence level, the marriages and births are discouraged, labour supply goes down and wages come back to the level of subsistence.

It was the subsistence theory of wages that made economics a dismal science. The theory was criticised on many grounds: -

1. Population is not indefinitely elastic to amount of wages.

2. Trade union activities do not allow wages to remain at subsistence.

3. Higher wages may increase standard of living and this may infact reduce the birth rates, reduce the size of families and not increase as postulated by the theory.

4. It ignores the demand side of the market.

5.2.2 Residual Claimant Theory of Wages

This theory was put forward by American economist, Walker. The process of production is carried on by four factors of production – land, labour, capital and organisation – and each of them get their rewards in the form of rent, wages, interest and profit respectively. According to Walker, rent, interest and profit were determined by some definite laws but wages are not determined in that way. Whatever remains after the payment to land, capital and organisation, is paid as wages to the labourer. In other words, the residual is paid to the labourer.

5.2.3 Wage Fund Theory

Wage Fund Theory was put forward by J.S.Mill. In his book "Principles of Political Economy". He stated that wages depend upon the relationship between supply of population and the capital available to employ workers. In his words, "Wages depend on relative amount of capital and population." By population, he meant the number of people ready to work and by capital he meant the amount to be used for the payment of wages. Accordingly, wage level is determined by dividing total wage fund by the number of workers. The wage fund depends upon the demand for labour and number of workers is determined by labour supply. Wage fund consists of those goods which are the means of subsistence for the labourer. Wage fund may also be defined as the part of working capital that the capitalists have kept for the payment of wages.

According to the wage fund theory, demand for and supply of labour will determine wage rate in the market. If actual wage rate is higher than the one indicated by the wage fund analysis, there will be unemployment in the economy. In other words, if wage rate is higher, the number of workers that can be employed, given the wage fund, would be less. Thus wages cannot rise unless either the wage fund increases or the supply of workers decreases.

Main criticism against this theory was that it ignores the possibility of increased wages accruing from greater productivity of workers.

5.2.4 Marginal Productivity Theory of Wages

Marginal Productivity Theory of wages is one of the oldest explanations for the determination of wages. It is also the most generally accepted theory of wage determination. According to J.B. Say, the most important proponent of this theory, wages paid to the workers are equal to additional contribution to production from the last worker employed. That means, wages are related to the marginal productivity of labour. Produce of labour as a determinant of wage rate can be traced back to Adam Smith's writings. Since then, efforts were made to bring marginal utility analysis in the wage determination. The marginal productivity theory of wages is based on many assumptions such as:-

i. Homogeneity of labour
ii. Mobility of factors of production
iii. Existence of perfect competition
iv. Law of diminishing marginal returns
v. Possibility of substitution of factors of production for each other

As per the theory, employers go on hiring the workers till the marginal revenue from the worker is higher than the cost of employing the additional workers. They will stop hiring the workers at that point where MC = MR i.e. the payment to the workers (marginal cost) is just equal to the amount of value added by the last worker of the firm (marginal revenue). Hence all the workers get wages equal to the productivity of the last worker employed.

Some of the limitations of the theory are – due to lack of perfect mobility of labour, workers of the same skill and efficiency, may not receive the same level of wages at two different places, productivity of workers is determined by many factors like quality of capital, efficiency of management, productivity is also a function of wages.

5.2.5 Exploitation Theory of Wages

A wage theory put forward by Karl Marx is known as Exploitation Theory of Wages. According to this theory, labour was considered to be the only productive factor of production as the value of a commodity was determined by the amount of labour used in production of that commodity. Hence anything that was retained by others (say profit or interest) in the process of production was a surplus. A surplus would be created as a result of exploitation of working class, according to Karl Marx.

5.2.6 Demand and Supply Theory of Wages

In perfectly competitive free market, wages will be determined on the basis of demand for and supply of labour. Demand for labour basically depends upon demand for a good or service that is produced with the help of labour. But at the same time, demand for labour and wages workers receive is also influenced by the government policy towards the workers. Social security measures like minimum wages act, pension schemes, retirement benefits, safety requirements at work, rules and regulations about working conditions, greatly influence the demand for labour. A downward-sloping demand curve clearly indicates that when the wage rate is high, demand for labour is low. It implies from the statement that any government policy decision taken in favour of labour will lead to increase in the cost of employing the workers and hencethe employment level will come down. It is therefore, very essential to understand the economic theory behind labour demand, characteristics of labour demand curves and various factors influencing the demand for labour.

Supply of labour, on the other hand, is determined by the labour force participation rate. It is positively related to the wage rate. Wage rate is an opportunity cost of leisure. Through the price mechanism, supply is brought in equality with demand. If demand for labour is high in relation to supply of labour, price of labour will go up, i.e wages will be pushed up. If demand for labour falls in relation to supply of labour, wages will go down. The determination 65 of wages according to demand and supply theory of wages does not go counter to marginal productivity theory of wages. Demand for labour basically would be determined by marginal productivity of labour and hence it will be an important factor in wage rate determination.

5.2.7 Bargaining Theory of Wages

It was propounded by Thornton, Davidson, Maurice Dobb and Webb. As per this theory, wages are determined by the bargaining power of the employers and employees. Wages will be higher if bargaining power of workers is high and vice versa. Wages would be settled between the upper and the lower limit. Employers would pay less and less considering the productivity of labour cost of investment and borrowing and the degree of competition in the market. Workers will demand higher and higher wages depending on cost of living and desire for improvement in standard of living. The actual wage rate will be determined by bargaining power of both the parties.

In non-competitive/imperfectly competitive markets, wage rate determination will be done by collective bargaining. Here both the trade unions as monopolist supplier or employers' association as monopolist buyer, function in imperfect market. Inter-sectoral or inter-occupational differentials in wage rates will be explained by different degrees of bargaining powers of respective trade unions.

It is maintained by the critiques of bargaining theory of wages that the trade unions can only increase the nominal wages (wages in terms of money) but they cannot raise real wages (purchasing power) beyond marginal productivity of labour. This is because the employers would always employ labourers up to the point where marginal productivity is equal to wage rate. So of wages go up beyond marginal productivity of labour, the employment level will come down.

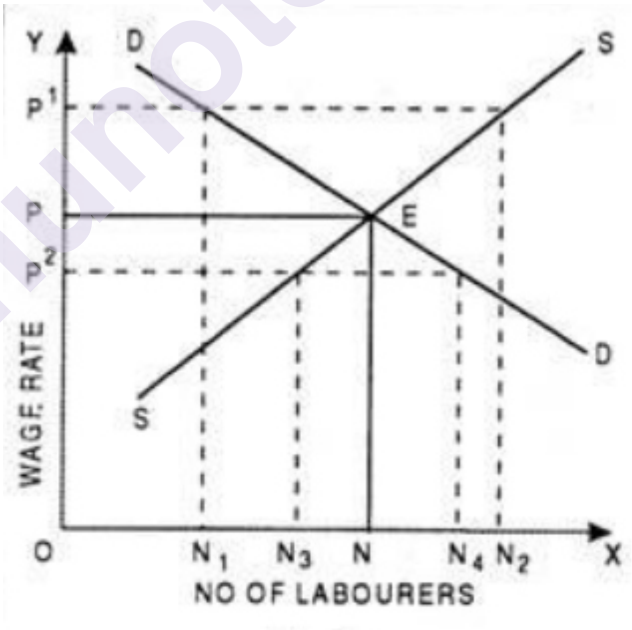
5.3 WAGES IN DIFFERENT MARKETS

Under perfect competition, equilibrium wage rate is determined where demand for labour is equal to supply of labour.

In other words, under perfect competition, a labourer will get wage equal to its marginal revenue productivity in the long run.

In Fig. 5.1 units of labour have been measured on X-axis and wages on Y-axis. DD and SS are the demand and Supply curves of labourers respectively. Both the curves intersect each other at point E which determines wage rate OP in the market.

Figure No. 5.1



At this level of wages, ON units of labourers will get employment. Now suppose, wages go up to OP_1. At this price, demand is ON_1 and supply ON_2. Since, the supply is more than demand; it will lead to competition among labourers to get employment which in turn results in a decrease in wage rate. On the other hand, if w age rate falls to OP_2, demand will be more than the supply. This results in competition among the producers to get the services of labour which in turn leads to an increase in wage rate.

Therefore, we may observe that equilibrium will be restored at that point where demand curve of labourers intersects the supply curve of labourers.

Time Periods to Study Firm's Equilibrium:

The study of firm's equilibrium can be studied in the following two time periods:

1. Short Run

2. Long Run

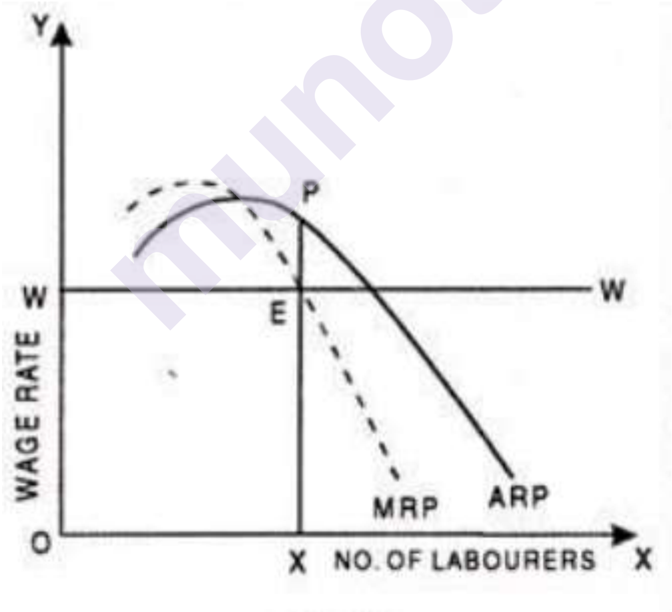
1. Short Run Period:

Short run refers to a period in which it is not possible for a firm to fully equate the demand for and supply of a factor. Therefore, a firm in the short run may face three situations.

Supernormal Profit:

If at OW wage rate, a firm provides employment to as much labourers whose ARP is more than the prevailing wage, the firm earns supernormal profits. In the Fig. 5.2 a firm at its equilibrium provides employment to OX labourers. Here ARP i.e. PX is greater than the wage rate EX. Thus, firm earns EP as supernormal profits.

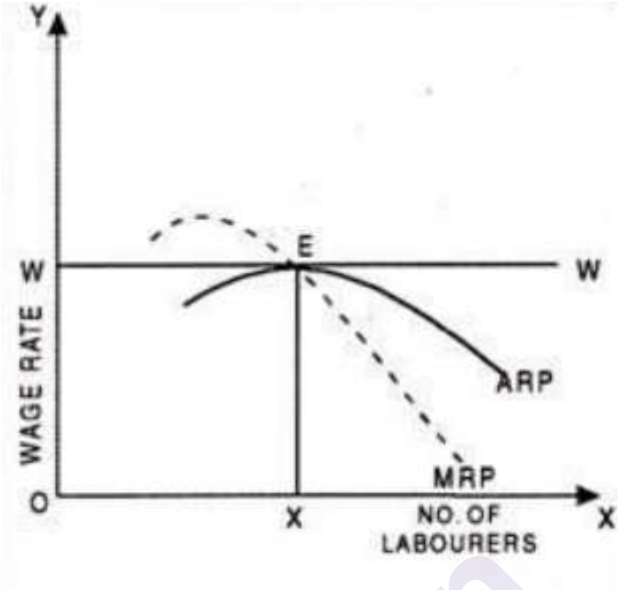
Figure No. 5.2



Normal Profit:

A firm enjoys normal profits, if ARP is equal to wage rate. In Fig. 5.3 when firm employs ON number of labourers, their ARP is EX which is equal to prevailing wage rate OW. Thus, the firm gets only normal profits.

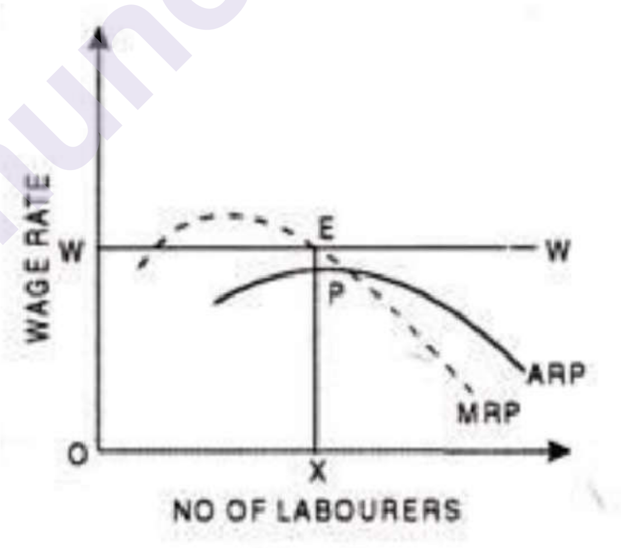
Figure No. 5.3



Losses:

A firm incurs losses, if at prevailing wage; a firm employs the number of labourers at which their ARP is less than the prevailing wage rate. In Fig. 5.4 when firm employs OX labourers, their ARP = PX is less than their wage rate OW. Thus, the firm has to incur losses equal to EP.

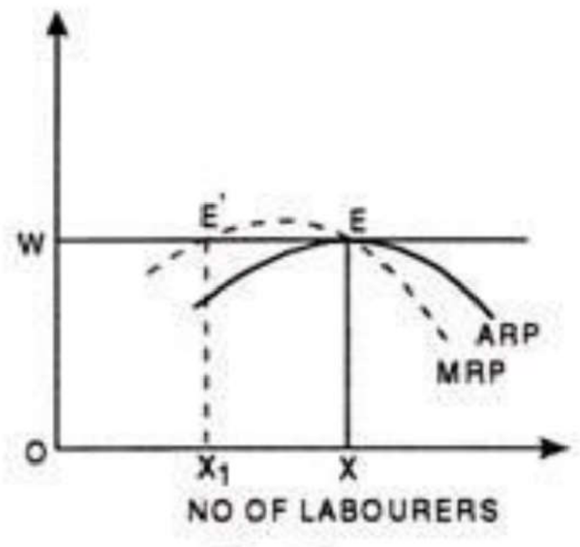
Figure No. 5.4



2. Long Run Period:

In the long run, a firm earns normal profit. A firm will be in equilibrium where ARP is equal to MRP. In Fig. 5.5 when firm employs OX labourer ARP is equal to MRP.

Figure No. 5.5



Wage Determination under Imperfect Competition:

In the world of reality there exists imperfect competition rather than perfect competition. Therefore, Mrs. Joan Robinson and Prof. Pigou gave the wage rate determination under the conditions of imperfect competition.

The wage rate determination can be explained fewer than two heads:

(a) Perfect competition in product Market and Monopsony in the Labour market.

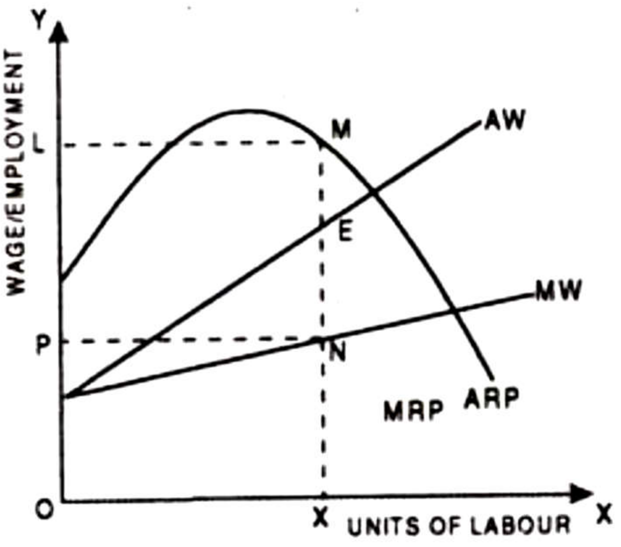
(b) Monopoly in the product Market and Monopsony in Labour Market.

(a) Perfect Competition in Product Market and Monopsony in Labour Market:

When there is a single buyer of labour in the market, monopsony is said to exist in the labour market. If there is an increase in monopolist's demand for labour, wage rate will follow the same path which in turn tends to increase the average and marginal wage rate. It can be shown with the help of a diagram.

In Fig. 5.6 units of labour have been measured on X-axis while wages on Y-axis. ARP and MRP is the average revenue product and marginal revenue product curves. AW and MW are the upward sloping average wage and marginal wage curves indicating that if the monopolist wishes to employ more and more labourers, he has to offer the higher wage rate.

Figure No. 5.6



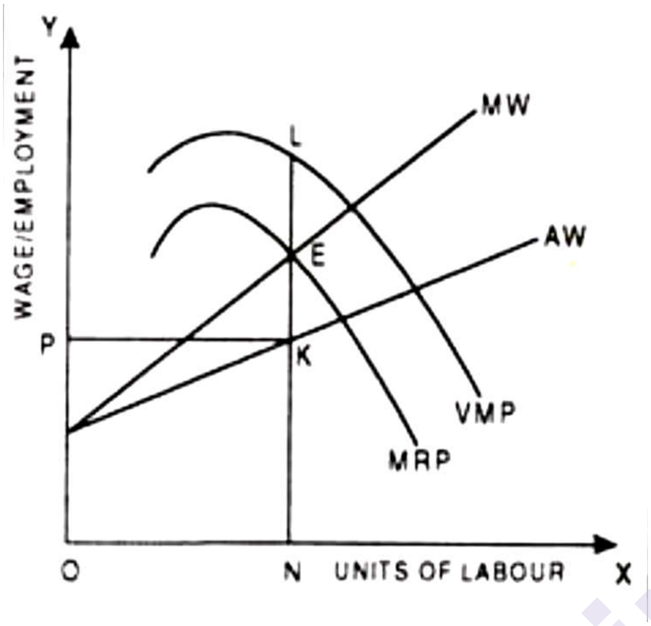
The monopolistic firm is in equilibrium at point E. At point E both the conditions of equilibrium are fulfilled i.e. marginal wage should be equal to marginal revenue product and the marginal revenue product curve must cut the marginal wage curve from above and then lies below it. Thus, at this equilibrium level, he will employ OX units of labour and OP wage rate will be determined.

Since wages are less than marginal revenue productivity, means that the monopolist exploits the labour. Thus, in this equilibrium the monopolist earns the supernormal profits equal to the area PLMN. Therefore, it can be concluded that imperfect competition in the labour market results in the exploitation of labour.

(b) Monopoly in Product Market Monopsony in Labour Market:

When there exists monopoly in product market and monopsony in labour market then there is difference between marginal revenue product and value of marginal product. Value of marginal product refers to the product of MPP and the price of the commodity. It can be explained with the help of a figure.

Figure No. 5.7



In Fig. 5.7 MRP is the marginal revenue product curve and VMP is the value of marginal product curve. The VMP curve is above the MRP curve. The monopsonist is in equilibrium at point E. The monopsonist employs ON units of labour and wage rate OP is determined in the market.

Monopoly in the product market and monopsony in the factor market leads to the double exploitation of labour, i.e., monopolistic exploitation and monopsonist exploitation. At this equilibrium level monopolistic exploitation is EL while the monopsonist exploitation is equal to EK.

5.4 WAGE STRUCTURE AND COMPONENTS OF WAGES

5.4.1 Wage Structure:

Wage structure may be defined as the internal pattern of varying job ranking and basic wage rates and differentials of different categories of employees in a company according to skill, qualifications and experience. Together with this, wage structure may also be influenced by labour market forces. But the outside market impinges only at certain points in the company wage structure.

There is a great array of semi-skilled and unskilled production jobs that are specific to a particular industry or even a particular company. Workers are usually not recruited into these jobs from the outside, but work up from within the company on a seniority basis. These types of jobs, if not easily available elsewhere, wage rates become subject to inside market.

Factors Affecting Wage Structure:

The wage structure in a modern plant may be influenced by the following factors:

- Collective bargaining and labour relations
- Management discretion and custom
- Skill and production operation sequence
- Job evaluation or job rating
- Minimum wage legislation
- Dearness allowance
- Bonus
- Wage incentives
- Wage differentials
- Company wage policy
- Governmental wage fixation methods
- Tripartite convention
- ILO convention.

Wage structure may be industry based or there may be inter-industry wage structure or Federation level wage structure. In India, wage structure for different industries has been set on the basis of Government wage regulation, and tripartite negotiation.

5.4.2 Component of Wages:

The components of wages are as follows -

- basic pay
- annual bonuses
- tips
- in-kind benefits
- productivity and performance pay
- allowances and premiums for non-standard work hours or dangerous work.

The fact that total wages or earnings are made of different components raises the question of which components should count towards compliance with the minimum wage.

5.5 SHARE OF WAGES AND DISTRIBUTION AND INEQUALITY OF WAGE INCOME

The Government of India appointed a committee in 1948 to determine the wage policy. In order to recommend the principle on which the fair wage rate should be based, this appointed committee clarified the concepts of the livelihood wage, the minimum wage and the fair wage.

1. Livelihood Wages:

The basic wage is the wage of a worker which can provide food, clothing, shelter as well as education of children, sickness, amenities to the family and provision for future disaster relief.

2. Minimum Wages:

The minimum wage is a wage that can meet the general needs of a man in a civilized society.The principle of minimum wage was widely accepted.The main objectives of the minimum wages are to increase wage rate in the industry, to reduce the exploitation of workers, to inspire peace in the industry by guaranteeing wages that meet the minimum needs of the workers.

3. Fair Wages:

A fair wage is slightly higher than the minimum wage and lower than the livelihood wage. The committee also said that the strength of the industry should be taken into consideration while deciding the fair wage. Where a fair wage falls between the necessities of life and the minimum limits will depend on other factors such as the productivity of the workers, the wage rate in other industries. In an industry where the bargaining power of the workers is large, that is, trade unions are strong, the current wage is around fair wages.

5.6 MALE-FEMALE WAGE DIFFERENTIALS

There are two prominent forms of male-female or gender discrimination in labour market. Firstly, the employers may pay less to women than men with the same experience and to work under same conditions in the same occupations. Secondly, women with same education and productive characteristics may be placed in lower paying occupations or with lower responsibility jobs as compared to men. Thus, the labour market differential is said to be present when wages paid by the employers to men and women with equal productive characteristics are not equal, even in the same occupations. This trend may be due to many reasons. To mention a few of them: -

1. Many of the women are married and hence they are not entirely dependent on their own earnings. This may make them accept lower wages.

2. The average wages of men are higher because the proportion of skill is greater among men than women.

3. Much larger proportion of men tend to work harder than women because they have dependents to maintain.

4. The absentee rate out of sickness is less among the men as compared to women.

5. Turnover or job-changing is more among the women than the men due to many reasons like marriage, children, etc.

Royal Commission on Equal Pay (1946) published a Majority and Minority Reports. Majority Report favoured wage differentials between men and women on the ground that men possess greater physical strength and are generally more efficient than women, that the sickness rate was higher among women, that they are more likely than men t absent themselves from work for trivial reasons, and that were generally less ambitious than men and in crises showed less initiative. The Minority Report admitted that where physical strength was concerned, men were more capable than women, but it was claimed that with this exception women were equally as efficient as men, the fact that in the past women had been promoted to few posts of responsibility being ascribed to the prejudice of employers and the jealousy of employees. (A Textbook of Economics – J. L .Hanson page 322)

5.7 INTER-SECTORAL WAGE DIFFERENTIALS

Since J.S. Mill, economic theorists have tended to explain occupational wage differentials by differences in costs of training or other obstacles to supply of labour. This however accounts for a long-run wage differentials. In the short run, the number of persons in an occupation is fixed and earnings are affected by the changes in demand and wage rigidities. The wages basically vary between one occupation and other because there is no single labour market. There are many labour markets depending upon different types of labour. For example, there may be deficiency of supply of labour in the market for doctors but there may be surplus in the market for engineers. Hence the wage rate in both these markets will differ. In the short-run, supply of labour of a particular kind (say doctors) cannot be raised as special, rigourous training may be required, special aptitude is required which may not be possibly accomplished in the short run. Hence, the first and foremost reason for wage differential is lack of occupational mobility.

5.8 SUMMARY

According to D.R. Gadgil, wage differentials in India are the characteristic of unorganised labour market and personal differentials are because of job-selling, individual bargaining and wage discrimination. Wage differentials by sex have also been very common in India. But the tendency appears to have reduced on account of government interference through the fixation of minimum wages, appointments of wage boards and pressures from the unions. Inter-industry and inter – state differentials are also on a continuous decline over years.

One of the Directive Principles of Indian Constitution is “Equal Pay for Equal Work”. The Fair Wages Committee and other wage fixing authorities in India have always recommended equal pay to equal work for men and women workers. But the things are difficult to implement because even though conditions, processes and products are standardised for the purpose of wage calculations, workpeople cannot be standardised. That is, the workers may differ on the basis of their experience, efficiency and hence the wages also may differ.

5.10 QUESTIONS

Q1. Explain the following theories of wages -

a. Subsistence theory of wages
b. Residual Claimant Theory of Wages
c. Wage Fund Theory
d. Marginal Productivity Theory of Wages
e. Exploitation Theory of Wages
f. Demand and Supply Theory of Wages
g. Bargaining Theory of Wages

Q2. Write a note on -

a. Wages in Different Markets
b. Wage Structure and Components of Wages
c. Share of Wages
d. Distribution and Inequality of Wage Income
e. Male-Female Wage Differentials
f. Inter-Sectoral Wage Differentials

❖❖❖❖

6

WAGE ISSUES IN LABOUR MARKETS – II

Unit Structure:

6.0 OBJECTIVES

- To know the concept of contract labour.
- To study the properties of contractual wages.
- To understand the concepts of labour market rigidities and flexibilities.
- To study wage and output relations in India during pre and post-reform period

6.1 INTRODUCTION TO CONTRACT LABOUR

Contract labour is not recorded on the payroll. It is not directly paid by the employer. The principal employer is not directly responsible for the payment of wages or any other matter arising out of employment of contract labour. The benefit of contract labour to the principal employer is in terms of cheap labour and avoidance of other attendant costs that may arise out of regular employment such as provision of welfare facilities, paid leave, social security, bonus, administrative costs, installation of plant and machinery which otherwise is provided by the contractor etc. Contract labour can be divided into two categories, namely; persons employed in job contracts and labour contracts. Big firms offer job contracts or certain operations, for example, loading and unloading of material to contractors. In this case, the contractor employs his own labour and also pays them.

In case of labour contracts, the contractor supplies only labour to the principal employer for employment in various categories of work. The contractor is responsible for payment of wages as determined by him to the workers. Contract labour is employed as unskilled and skilled labour. Unskilled labourincludes categories such as loaders, cleaners, sweepers, helpers etc and skilled labour include categories such as turners, fitters, electricians, gas cutters, carpenters, blacksmiths etc. Contract labour is generally found in industries such as engineering, textile, carpet weaving, building constructions, irrigation projects, road construction etc. Out of these, mining and building industries are found to be the major employers of contract labour.

Contract labour was one of the most exploited forms of labour. Both the contractor as well as the principal employer did not bother about contract labour. The Government of India therefore passed the Contract Labour Act to prevent the exploitation of contract labour. The Contract Labour (Regulation and Abolition) Act, 1970 provides for the regulation of the conditions of work, health and safety, wages and other amenities for the welfare of contract labour. A contractor is required to provide canteens, rest rooms, latrines, urinals, drinking water, washing facilities and first aid boxes for the use of contract labour. If a contractor fails to provide the amenities or to make payment of wages, the principal employer will be liable to provide the amenities or to make payment of wages to the contract labour and the principal employer can recover such expenses from the contractor.

The objective of the Act is to prohibit the employment of contract labour and wherever it is not possible to prohibit, conditions of work of contract labour is sought to be improved. The Act is applicable to every establishment employing twenty or more workmen as contract labour and to every contractor employing twenty or more workmen. The Act further empowers the Central and State governments to apply the provisions of the Act to any establishment or contractor employing less than twenty workmen. The Central Government has prohibited employment of contract labour in categories of work in coal, iron ore, limestone, dolomite, manganese, chromite, magnesite, gypsum, mica and fire clay mines, building industry, and railways. Contract labor is prohibited in the Central Food Corporation of India godowns and Port Trust.

6.2 PROPERTIES OF CONTRACTUAL WAGES

Properties of the contractual wages are as below –

1. Illiteracy:

Indian workers are extremely illiterate compared to other countries. It creates hinders to the workers in acquiring new technologies, skills, etc. in the industrial sector. As a result, their productivity and efficiency are reduced, their wages are reduced and their appearance is inferior.

2. Absence of Workers and Migration Problems:

The mentality of Indian workers is not to leave their geographical location, family and get a job outside. As a result, they get less salary in one place. His salary does not even cover his family's needs. As a result, he often avoids going to work.As India is an agricultural country, people earn by working in agriculture only.

3. Traditional Teaching Methods:

As the education system in India is traditional, it is difficult for the workers to get employment. It limits the development of workers.

4. Poor Health and Living Standards:

Due to the low wages of Indian workers, their per capita income is also low, overty is high, even their basic needs are not being fulfilled. These all things affect their health and quality of life. Lack of access to nutritious and nutritious food degrades the health of the workers and reduces their efficiency and productivity, which is not in the interest of the economy.

5. Salary Variation by Gender:

In India, men and women are discriminated against. Even today, women are given a secondary place in society. Women are paid less than men.

6. Seasonal Nature of Work:

Many workers do not get work all year round. They get work a few months out of the year. The rest of the month they have to stay unemployed. For example, Sugar mill workers get work only during the sugarcane crushing season. The factory closes at the end of the season, leaving many workers unemployed until the next season.

7. Lack of Bargaining Power:

Workers' wages are determined by their bargaining power. Bargaining power occurs between workers and employers when it comes to wage determination. On whose side the bargaining power is greater; the right to fix the salary/wages also goes to him. But due to various reasons, the bargaining power of the workers is low and he cannot decide the wages of his work. The wage rate, which is set by the employer class, is very low from the point of view of the workers.

8. Lack of Laws and Regulations:

The government has enacted various rules and regulations to provide security and welfare to the workers. But still the owners exploit the workers by evading it. They often violated laws and regulations. With the adoption of privatization in the new economic policy of 1991, the scope of private companies increased as government control and ownership diminished. The existing laws and regulations are proving to be ineffective as such employers are exploiting the workers in the form of overtime work, hiring child laborers, paying low wages to the workers etc.

9. Market Inadequacies:

Inadequacies in the market are the nature of the work that workers get, where they get work, what are the rates of wages. It means not getting proper information about it. As a result, many workers are deprived of work. Due to illiteracy in the working class, they do not get the information of the hiring agency in time.

10. Industrial Backwardness:

The industrial sector in India has not developed much faster than other countries. The industrial sector failed to provide employment to the additional population, so even today about 51% of the population in India is dependent on agriculture.

11. Unsatisfactory Place of Work:

The health and safety of the factory workers is not very satisfactory. Resting places at work, toilets, urinals, restaurants, nurseries for children of female workers, etc. Facilities are not available in adequate quantities. Lack of first aid equipment to protect workers from accidents while working. All of this has a detrimental effect on the health of the workers and adversely affects their productivity and efficiency.

12. Conflict Between Employers and Workers:

Due to the existence of trade unions in modern times, such unions have increased the wages of workers, increased flood dividends, increased the period of leave, etc. The owners take the matter to the class. If the working class does not agree to the demands of the trade unions, the workers go on strike and close the factories. This shuts down the manufacturing process and has an adverse effect on the economy.

13. No Increase in Real Wages of Workers:

Although the government has taken measures to increase the wages of the workers, it has not increased the actual wages of the workers.

14. Problems of Unorganized Workers:

After independence, many laws came into existence in our country for the welfare of the workers. At the same time, trade unions emerged, so that workers in the organized sector began to benefit from various schemes. But workers in the unorganized sector do not get the benefit of such government schemes. Unorganized workers are terribly exploited by the employers and the capitalist, and so the exploited workers remain exploited and these unorganized workers do not get the benefit of many good labour laws that exist.

15. Lack of Training and Skill Centres:

Given the rising rate of unemployment, the number of skill centres set up by the government are very low. As a result, many employment-oriented youth are deprived from training and skills.

6.3 LABOUR MARKET RIGIDITIES AND FLEXIBILITIES

Labour Market Flexibilities

Labour market flexibility refers to the market mechanism that enables labour markets to reach a continuous equilibrium determined by the intersection of the demand and supply curve. Labour market institutions were seen to inhibit the clearing functions of the market by weakening the demand for labour, making it less attractive to hire a worker by pushing up the wage costs; by distorting the labour supply; and by impairing the equilibrating function of the market mechanism i.e., by influencing bargaining behaviour.

The most famous distinction of labour market flexibility is given by Atkinson. Based on the strategies companies use, he notes that there can be four types of flexibility.

1. External Numerical Flexibility:

External numerical flexibility refers to the adjustment of the labour intake, or the number of workers from the external market. This can be achieved by employing workers on temporary work or fixed-term contracts or through relaxed hiring and firing regulations or in other words relaxation of employment protection legislation, where employers can hire and fire permanent employees according to the firms' needs.

2. Internal Numerical Flexibility:

Internal numerical flexibility is also known as working time flexibility or temporal flexibility. This flexibility is achieved by adjusting working hours or schedules of workers already employed within the firm. This includes part time, flexi-time or flexible working hours/ shifts (including night shifts and weekend shifts), working time accounts, leaves such as parental leave, overtime etc.

3. Functional flexibility

Functional flexibility or organizational flexibility is the extent employees can be transferred to different activities and tasks within the firm. It has to do with organization of operation or management training workers. This can also be achieved by outsourcing activities.

4. Financial or Wage Flexibility:

Financial or wage flexibility is in which wage levels are not decided collectively and there are more differences between the wages of workers. This is done so that pay and other employment cost reflect the supply and demand of labour. This can be achieved by rate-for-the-job systems, or assessment-based pay system, or individual performance wages.

Other than the four types of flexibility there are other types of flexibility that can be used to enhance adaptability. One way worth mentioning is locational flexibility or flexibility of place. This entails employees working outside of the normal work place such as home-based work, outworkers or tele-workers. This can also cover workers who are relocated to other offices within the establishment.

6.4 SUMMARY

- Labor market flexibility refers to the market mechanism that enables labor markets to reach a continuous equilibrium determined by the intersection of the demand and supply curve. The most famous distinction of labor market flexibility is given by Atkinson. Based on the strategies companies use, he notes that there can be four types of flexibility.

a) External numerical flexibility
b) Internal numerical flexibility
c) Functional flexibility
d) Financial or wage flexibility
e) locational flexibility or flexibility of place

6.5 QUESTIONS

Q1. Write a note contract labour.

Q2. Write a note on labour market flexibility.

❖❖❖❖

MODULE 4: LABOUR MARKETS IN INDIA

7

LABOUR MARKETS IN INDIA – I

Unit Structure:

7.0 OBJECTIVES

- To study the linkages in labour markets.
- To study the role of risk, information and incentives.
- To study the concept of dualism and segmentation in the labour market.
- To know the labour market flexibility.
- To know the relation between state and labour markets.
- To study the concept of employee turnover.
- To study the concept of migrant labour.

7.1 INTRODUCTION

Labour markets or job markets function through the interaction of workers and employers. Labour economics looks at the suppliers of labour services (workers) and the demanders of labour services (employers), and attempts to understand the resulting pattern of wages, employment, and income. These patterns exist because each individual in the market is presumed to make rational choices based on the information that they know regarding wage, desire to provide labour, and desire for leisure. Labour markets are normally geographically bounded, but the rise of the internet has brought about a 'planetary labour market' in some sectors.

Labour is a measure of the work done by human beings. It is conventionally contrasted with other factors of production, such as land and capital. Some theories focus on human capital, or entrepreneurship, (which refers to the skills that workers possess and not necessarily the actual work that they produce). Labour is unique to study because it is a special type of good that cannot be separated from the owner (i.e. the work cannot be separated from the person who does it). A labour market is also different from other markets in that workers are the suppliers and firms are the demanders.

7.2 ROLE OF RISK, INFORMATION AND INCENTIVES

The agricultural labor markets are incomplete. Risks are involved in agricultural production. Risk arises due to weather uncertainties, variability in input availability and absence of a market for output insurance.

There is a coexistence of casual laborers, hired on a daily basis and permanent laborers, hired on the basis of long-term wage contracts. Two-stage production process is involved in agriculture. Both buyers and sellers of labor face risk since wages have to be paid and received at the end of the crop cycle each year. This is ue to uncertainty in labor demand in the second stage of production, which in turn occurs because of weather uncertainties in agriculture.

Permanent wage contracts are the outcome of a situation where efforts cannot be monitored. Permanent workers are entrusted with responsibilities that require judgment, discretion and care as if they were family members. Permanent worker contracts are superior in comparison to a series of casual labor contracts since the income differential serves as a monitoring device, and any deviation from the required effort level can lead to unemployment. The coexistence of regular and casual labor is on account of hoarding costs of maintaining a pool of regular labor throughout the production period. Employers choose the size of permanent and casual labor force in order to minimize production costs. A hoarding cost to maintain a steady pool of regular or permanent laborers becomes necessary when resale of this input is not possible. Hoarding costs of regular labor vary inversely with the farm size and faced with such a cost farms may not only hire the regular laborers, they may also hire some casual labor.

Landowners create tenancy contracts in order to have access to unmarketable inputs like worker's effort and to minimize production risks. For example, when it is difficult to monitor the worker's effort, the landowner might lease his land at a fixed rent to the tenant where all the output goes to the tenant except the fixed rent. This kind of tenancy solves the moral hazard problem. Another common form of tenancy is sharecropping where both the tenant and the landowner share the output in a pre-determined manner. It is argued that sharecropping is an inferior system in comparison to the fixed rent system. In a situation where the effort of the tenant cannot be monitored, the tenant has an incentive to undersupply his effort as under this form of tenancy contract part of the output produced by the tenant is handed over to the landlord. The same reasoning can be applied to the less than optimal supply of all productive inputs in sharecropping.

Due to the existence of risk, asymmetric information and incentive problems, different labor markets exists in the rural areas. These are:

1. Subsistence Farming

Subsistence farming is small-scale and productivity is low due to low-technology used in production. Subsistence farming provides the household with the primary source of food. Any excess food is likely to be sold in local markets. However many poor households are in a vicious circle that begins with low calorie intake and under-nutrition, which directly affects productivity in what is highly physical work. Even when labourers can earn more from hiring out their labour to others they may remain farming their plot of land because of the importance of producing or providing food for the household given the uncertainty in agricultural production. This decision can appear uneconomic or irrational but because of no insurance markets, lack of credit markets, asymmetric information and incentive problems, it is in fact not irrational. The risk of not having food security for the household will in itself lead to diversification of income sources – importance of non-farm income and issue of migration/remittances.

2. Sharecropping

Sharecropping is a way of providing incentives to workers by employers so monitoring costs and screening costs are zero. Theoretically this model is a way of overcoming market failures of asymmetric information and incentives problems. It provides landless workers with access to land and tools. The landlord is providing, land, tools, credit and loans. The employer gains by having non-seasonal workers all year round. Landlords will offer sharecropping to individuals/households he knows that reduces transactions costs.

3. Tenant Farming

The tenant pays rent to the land owner, but there is little or no security in tenure on the land. Hence there is poor incentive to invest in capital and technology and no improvement in productivity. The tenant attempts to maximise his utility subject to effort levels and the contractual agreement with the land owner. The land owner tries to maximise his utility by manipulating contractual terms with consideration of the tenant's response to them under the constraint of guaranteeing to the tenant 'reservation utility,' meaning the utility the agent can obtain if he does not enter the contract.

4. Co-operative Farming

Small land-owners form larger areas to cultivate so can exploit economies of scale in inputs and outputs. The issue of access to markets exists if any surplus is produced. Transport infrastructure needs to be improved within rural areas and between rural and urban areas, where the surplus will be sold for more.

5. Commercial Farming

Commercial farming can lead to significant change in how rural labour markets work. The employer contracts small landowners to produce crops and provide them new technology inputs. Contract farming is good if the small landowner still retains some land for his own use and has other sources of income. If he is solely reliant on contract farming income then he will be exposed to the risk of obtaining poor wages. Work can be casual (day or so), seasonal (month or two), or permanent (more than 3 months). The issue of what kind of employment contract to offer to workers is based on type of work done. If easily monitored (e.g. harvesting) then wages can be based on the market.

7.3 DUALISM AND SEGMENTATION IN THE LABOUR MARKET

The labor market of less developed countries like India has dualistic character. Dualism in the labor market is due to the following reasons:

1. Job Preferences of the Workers:

Workers prefer to work in particular sectors even when better wages or more employment opportunities are available in other sectors. For instance, rural workers may prefer to stay back rather than migrate to urban areas where wage rates and employment opportunities are comparatively better. Thus unemployment in the rural areas and labor shortage in urban areas may be due to lack of geographical mobility of labor.

2. Indivisibilities in Labor Supply:

The working hours are indivisible. However, the workers in countries like India are not fully urbanized and hence have a dual nature which can best be described as rural-urban. Workers may like to work both in the factory as well as the farm as a matter of routine. However, such a system may not be permitted by the factories. The desire to work on the farm and sometime to go back to the farm during the agricultural season is an important cause of labor turnover and absenteeism in India.

3. Formal and Informal Labor Markets:

The formal labor markets are protected by labor legislation and they are also unionized. The wage rates and working conditions in the formal labor market are determined by legislation. In contrast, the informal labor markets are not governed by labor legislation and hence the wage rates and working conditions are very poor and there is a wide gap between the wage rates of the formal and informal sector workforce.

7.4 LABOUR MARKET FLEXIBILITY

Labor market flexibility refers to the market mechanism that enables labor markets to reach a continuous equilibrium determined by the intersection of the demand and supply curve. Labor market institutions were seen to inhibit the clearing functions of the market by weakening the demand for labor, making it less attractive to hire a worker by pushing up the wage costs; by distorting the labor supply; and by impairing the equilibrating function of the market mechanism i.e., by influencing bargaining behavior.

The most famous distinction of labor market flexibility is given by Atkinson. Based on the strategies companies use, he notes that there can be four types of flexibility.

1. External Numerical Flexibility:

External numerical flexibility refers to the adjustment of the labor intake, or the number of workers from the external market. This can be achieved by employing workers on temporary work or fixed-term contracts or through relaxed hiring and firing regulations or in other words relaxation of employment protection legislation, where employers can hire and fire permanent employees according to the firms' needs.

2. Internal Numerical Flexibility:

Internal numerical flexibility is also known as working time flexibility or temporal flexibility. This flexibility is achieved by adjusting working hours or schedules of workers already employed within the firm. This includes part time, flexi-time or flexible working hours/ shifts (including night shifts and weekend shifts), working time accounts, leaves such as parental leave, overtime etc.

3. Functional flexibility

Functional flexibility or organizational flexibility is the extent employees can be transferred to different activities and tasks within the firm. It has to do with organization of operation or management training workers. This can also be achieved by outsourcing activities.

4. Financial or Wage Flexibility:

Financial or wage flexibility is in which wage levels are not decided collectively and there are more differences between the wages of workers. This is done so that pay and other employment cost reflect the supply and demand of labor. This can be achieved by rate-for-the-job systems, or assessment-based pay system, or individual performance wages.

Other than the four types of flexibility there are other types of flexibility that can be used to enhance adaptability. One way worth mentioning is locational flexibility or flexibility of place. This entails employees working outside of the normal work place such as home based work, outworkers or tele-workers. This can also cover workers who are relocated to other offices within the establishment.

7.5 EMPLOYEE TURNOVER

Employee turnover refers to the shifting of workforce in and out of an organization and hence it is also referred to as the interfirm mobility of labor. Employee turnover may be defined as "the rate of change in the working staff of a concern during a definite period". Employee turnover measures the extent to which existing employees leave and new employees enter into services of an organization in a given period. Employee turnover is also defined as the measurement of inarticulate laborunrest because strikes are articulated expressions of labor unrest. Employee turnover measures the morale of the employees and their efficiency. The higher is the rate of turnover the lower is the morale and efficiency. These two aspects are central to the success of a organization and hence needs to be seriously addressed.

Statistically, employee turnover is expressed as the ratio of yearly or monthly separations to the average number of full time employees for that period. It is assumed that the total number of jobs available in a concern are constant. Employee turnover is measured in the following ways:

1. According to the total replacements formula, employee turnover is expressed by the formula:

$$T = \frac{R}{W} \times 100$$

Where, R is total replacements and W is average working force.

2. According to total avoidable separations like quits, discharges etc, employee turnover is expressed as:

$$T = \frac{S - U}{W} \times 100$$

where S stands for separations, U stands for unavoidable separations (retirements, deaths etc) and W is the average work force.

3. According to total accession plus separations, employee turnover is expressed by the formula:

$$T = A + S \div \frac{(P1 + P2)}{2} \times \frac{365}{M}$$

Where A stands for accession, S for separation, P1 and P2 for total number of employees at the beginning and at the end of the month respectively and M stands for the number of days in the month for which the figures were obtained.

4. Normally, employee turnover is computed in terms of percentage of the number of terminations of employment to the number employed during the period for which measurement is desired. Thus, employee turnover is:

$$T = \frac{S}{F} \times 100$$

Where T represents turnover, S stands for total separation during the period and F for average labor force during the period.

Causes of Employee Turnover

Retirement, resignation, lay-offs and dismissals are the common causes of employee turnover. Out of these, retirement is the inevitable cause. However, both resignation and dismissals can be reduced by implementing employee retention policies in the organization. Unavoidable turnover which is also called Natural Turnover arises because of factors like death, retirement, lay-offs and frictional unemployment. Employees may be laid off due to reduction in work on account of recession, seasonal variation and competition. Resignations and dismissals are found to be the main causes of turnover. Resignation may be due to dissatisfaction about the working conditions, poor wages, bad health, sickness, family circumstances etc. Dismissals may occur due to participation in strikes, misconduct, insubordination, disciplinary action in cases of inefficiency etc. The badli system in the textile industry was found to be an important cause of employee turnover. Employee turnover is also high amongst the highly paid managerial staff because of the belief that the more you shift from one organization to the other, the higher you will be on the growth ladder. Employee turnover is high amongst new employees, unattractive jobs, less skilled workers and young persons.

Consequences of Employee Turnover

Employee turnover lowers the efficiency of employees and they are not in a position to enjoy the benefits of loyalty. Employee solidarity is adversely affected by high turnover. The employers also lose on account of turnover. The productivity of employees during the learning period is low which means the cost of learning is borne by the employer. Once the employee becomes sufficiently skilled in his work and he or she leaves the employment, it is clearly a loss to the employer. However, if employee turnover is equally high across the industry, loss of skilled staff may be made good by acquiring skilled staff coming from other firms in the industry. However, acquisition of new employees is always at a higher cost. High employee turnover, however, prevents optimum utilization of resources in the country.

Remedies to Reduce Employee Turnover

In order to reduce employee turnover across the industry, a scientific study of the problem needs to be made to assess the extent of turnover across the industries and across the plants within industries. The recruitment or placement policy of the firm should be scientific enough to place the right person in the right place at the right time. There is a great likelihood of a misfit to leave the firm in a short period of time. Recruitment, placement and training policies of the firms must be correct to reduce the problem of employee turnover. Job specifications and man specifications should be matched before selection and placement is done. Finally, enlightened employee supervision, good working conditions, better standard of wages, a good system of career advancement, good separation benefits and an empathetic management can definitely reduce the problem of employee turnover.

7.6 MIGRANT LABOUR

Urbanization and industrialization are simultaneous processes. The process of industrialization and urbanization in any country would involve migration from rural areas to urban areas. Migration of rural labor to industrial areas continues as the industrialization process continues. This migration becomes insignificant once the industrialization process is complete and the country is transformed into a predominantly industrial country from a predominantly agricultural country. Rural to urban migration in an industrializing country takes place under compulsive conditions. Compulsive conditions involve the near absence of well-paying employment opportunities or the near absence of any employment opportunity in rural areas and the availability of endless employment opportunities in urban areas which are growing in size along with growing industrialization.

In India the migration of rural labor force to urban areas began with the destruction of village and cottage industries and the establishment of large factories in the big cities. The people who worked in the village and cottage industries, both landed and landless agricultural laborers and small and marginal farmers belonged to the fourth order of Caste Society known as Shudras, now known as Other Backward Classes (OBCs). This class of people also suffered from various religious, social and economic disabilities. However, they were located inside the villages and positioned above the outcastes or the ati-shudras. The people in the lowest order of the caste system i.e. the outcastes now known as Scheduled Castes who lived on the outskirts of Indian villages and suffered various types of religious, economic and social disabilities found the cities not only as centers of employment opportunities but also as opportunity to liberate oneself from the exploitative and inhuman caste system prevailing in Village India. The bulk of the industrial labor force in Indian cities was drawn from these two lowest rungs of the Indian caste society. While the pull and push of industrialization attracted hordes of low order people, the ones who belonged to the upper castes were also attracted to the cities because only the cities could provide employment opportunities to the educated labor force which was largely drawn from the upper castes in the early years of industrialization in India.

The causes of rural to urban migration can be summarized as follows:

1. Decline of village and cottage industries, rising pressure of village population on agricultural land and the resultant exodus.

2. Small and marginal farmers and the landless agricultural laborers found the new cities not only providing economic opportunities but also liberating from the rigid social hierarchy in villages.

3. Persons belonging to the scheduled or backward castes living on the outskirts of Indian villages and eking out a sub-human existence found the cities as liberating agents and immediately took to the cities as fish to the water.

4. Indebtedness in rural India amongst the laboring classes was chronic in nature. The cities provided an escape route to the highly indebted laboring classes.

Social scientists like McDonald, Jansen and McGee have earlier advocated the push and pull theory of migration. While the factors responsible for migration in different countries may assume different combinations, there is no denying the fact the rapid growth of cities all over the world since the beginnings of industrial revolution could not have been possible without the Great Pull the cities could exert on village populations.

Demerits of Rural to Urban Migration

The demerits of rural to urban migration are suffered by the migrants and the host cities and also the villages from which out migration takes place. These demerits or problems faced by the migrants, the cities and villages as a result of migration are as follows:

1. **Problems of Adjustment to Urban Way of Life**: The new village migrant into the city continues to have a rural mindset and attitudes. To him the city appears to be a hotchpotch of people coming from different parts of the country, speaking different languages and following different customs and practices. Unsatisfactory working conditions, poor living environment and a mechanical way of city life with impersonal relations is not something the new migrant had imagined before living his village. Adjustment to the urban way of life becomes a difficult issue to him. Those who continue to work and live in the cities make their adjustments over a period of time, those who fail to adjust go back to their villages and those who live, propagate and permanently settle down in cities become urban in their life and living.

2. **Poor Health and Efficiency of Migrants:** The migrants who lived on the margin of existence in the villages are the worst sufferers in the cities. They are forced to find shelters in shanties constructed along the

railway lines and in other slums and blighted areas of the cities. Slums are generally constructed by the cities' underbelly consisting slumlords and unscrupulous local politicians. The rural poor who are fresh migrants to the cities are forced to take refuge in these slums. Life and living in slums is open and exposed. There is little or no open space. The conditions are sub-human and degrading. The industrial workers working in the unorganized sector live in these slums, earn poor wages and barely manage to keep their and their family members' body and soul together. In the absence of any health and welfare facility in their work places, their health and efficiency becomes poor over a period of time.

3. **Absence of Family Life:** The rural poor who migrate to the cities are generally single. Migrants who are married with children are forced to leave their families in the villages for the absence of proper shelter in the cities. Loneliness and absence of a healthy sex life push these migrants to visit prostitutes on a regular basis. The poor village migrant visits the poor prostitute who also lives in sub-human conditions. These migrants suffer from sexually transmitted diseases (STDs) and they pass on these diseases to their wives either when they go back to their villages or when they get back their wives to live in the slums and shanties of the cities. While the incidence of STDs was very high amongst the slum population in the early years of industrialization, it is HIV and AIDS whose incidence is found to be the highest amongst the slum population.

4. **Uneducated and illiterate Industrial Workforce:** The first generation industrial workforce is the migrants from the villages who are generally drawn from the lowest and the poorest strata of the village society. They are undoubtedly illiterate and uneducated. Lack of literacy and education amongst these workers make them entirely dependent on professional trade unionists. The problem of outside leadership in the trade union movement in India is because of the problem of illiteracy amongst industrial workers. These professional trade unionists many a times exploit the poor and illiterate industrial workers by provoking them to create industrial unrest so that they can blackmail the exploitative employers.

5. **Poor Labor Commitment and High Labor Turnover:** Since the new rural migrants have not fully adjusted to the industrial life, they frequently tend to visit their native villages leading to the problem of absenteeism. Further those who fail to adjust to the industrial life return back to their villages causing high labor turnover. Labor turnover is the ratio of yearly separations to the average number of full time workers employed in the given period. Thus if the labor turnover is 5 per cent, it means that out of the 100 workers employed in a given year, 5 workers have terminated their services. While poor commitment reduces the efficiency of the workers, high labor turnover results in loss of trained manpower and the training expenses by the establishment.

6. **Poor Labor Commitment and High Labor Turnover:** Since the new rural migrants have not fully adjusted to the industrial life, they frequently tend to visit their native villages leading to the problem of absenteeism. Further those who fail to adjust to the industrial life return back to their villages causing high labor 151 turnover. Labor turnover is the ratio of yearly separations to the average number of full time workers employed in the given period. Thus if the labor turnover is 5 per cent, it means that out of the 100 workers employed in a given year, 5 workers have terminated their services. While poor commitment reduces the efficiency of the workers, high labor turnover results in loss of trained manpower and the training expenses by the establishment.

7. **Emergence and Growth of Women Headed Families**: In many parts of the country on account of men migrating to cities both within the country and outside the country for employment, the women are left behind to run the family affairs. Husbands as a result have become visiting husbands once in a year. Single parent women headed families definitely are not suitable for the healthy growth of family members. Such arrangement also affects the emotional health of women left behind in villages to look after the families. The problem of single parent women headed families is enormous in States like Kerala, Punjab, Uttar Pradesh and Bihar.

8. **The Problem of Over-urbanization:** Both push and pull factors operate to cause rural to urban migration. Overurbanization is the result of the excess of push over the pull factor. The pull factor determines the actual labor force that the cities demand and the push factor determines the actual labor force that villages supply to the cities. Thus if the push is greater than the pull, there will be excess labor supply in the urban areas. This excess labor supply constitutes the industrial reserve army in cities. The industrial reserve army exerts a downward pull on wage rates and other welfare facilities on the one hand and raises land and shelter prices on the other. This demand supply mismatch only contributes to all kinds of urban problems manifested in the form of mushrooming slums in the most unimaginable places in the cities, overcrowding, poor moral environment, undesirable exposure, petty crimes and what not.

Merits of Rural to Urban Migration

Some of the benefits of rural to urban migration that cities and villages may enjoy are as follows:

1. **Productive Utilization of Unemployed Rural Labor Force**: Employment opportunities are few and far in villages. The village economy is not big enough to employ the expanding labor force. Industrial centers and cities provide gainful employment to the expanding and excessive labor force in villages. Industrialization is a continuous process and to feed this process, an ever expandinglabor force is required. This labor force can be provided only by the villages

in the early years of industrialization. Once the industrial society is stabilized and the first generation urban bred labor force emerges, the need for rural labor force diminishes. However, able bodied, hard working and sturdy manual labor that is required in the cities and urban areas is continually supplied by villages to the cities.

2. **Availability of Cheap Labor to Cities:** Unemployed village labor force continues to migrate to the cities in large numbers thereby creating an industrial reserve army. Wage rates are pushed down by excessive labor supply thereby bringing down the labor cost of production in cities. Thus migration helps to bring down the cost of production. However, if the benefit of reduced cost of production is not passed on to consumers, it will not help to control inflationary pressures in the economy.

3. **Cultural Assimilation and Change in Rural Attitudes:** Culture is what we do twenty four hours a day. The migrants who live in cities and make them as their homes over time become urban in attitudes and culture. When these migrants go back to their villages on periodic visits, they perform the role of change agents in the social and personal sphere. The regular and personal interaction between the villagers and the visiting migrants bring about changes in village attitudes, norms and culture through a process of assimilation and acculturation.

4. **Paying Back to the Villages:** Successful migrants and particularly emigrants have the potential to pay back to their native villages in terms of taking up developmental activities like building schools and colleges, establishing health centers, creating awareness about health, particularly maternal and child health care, setting up village enterprises and contributing to the growth of rural industries, setting up micro credit institutions and helping the growth of small entrepreneurs in the villages etc. In village India, quite a few successful migrants and emigrants have started developmental activities thereby bring about perceptible changes in rural society.

Trends in Rural to Urban Migration

The process industrialization and concomitant urbanization in India is now more than 150 years old. It began with the setting up of the first textiles in Bombay in the second half of the 19th century. Since then the process have consolidated and strengthened. But India continues to be a predominantly agricultural country with more than 65% of the population being directly dependent upon agriculture. Only 25% of the population lives in the cities with the industry and services sector contributing to 75% of the national income. Rural to urban migration of people is therefore here to continue for some more time to come. Today we have urban settlers ranging from the sixth generation fully urbanized settlers to the first generation neo-urban settlers. Although every urban Indian citizen has a foot in the village, he is no more a villager. He goes back to his native village only to relax and relate to his people and not to work on his farm to earn some money. In fact most of them do not own any land in the village for they had already sold it bidding a final good bye to village life.

Today we have industrial societies which are fully urbanized and accustomed to the urban ways of life. The industrial and urban workforce today is greatly aware its rights, labor laws, strength of unionization and are politically conscious. The organized workforce although miniscule in terms of percentage of the actual workforce, its absolute size amounting to about 30 million workers is about 7% of the workforce in the country. In order to consolidate and strengthen the process of urbanization and industrialization, the organized workforce needs to be expanded. This is possible through unionization of the workforce on the one hand and voluntary compliance of labor laws by firms and establishments across the country.

7.7 STATE AND LABOUR MARKETS

State intervention in wage determination in India is based on the assumptions that it is socially desirable for wage earners to live on a healthy and decent plane and to participate freely in industrial governance and that the State should intervene in the economic relationship of its citizens whenever these achievable ideals are not achieved. The considerations that are important in the context of State regulation are as follows:

1. Wage regulation is necessary because labor markets are imperfect and exploitation of labor occurs.

2. The workers have poor bargaining strength in those markets in which there is an excessive supply of labor. Hence they are open to exploitation and sweating of labor has prevailed. State regulation is capable of abolishing such sweating of labor.

3. State intervention is essential to regulate wages to maintain economic stability. Lack of aggregate demand in the economy is the direct outcome of concentration of economic wealth in the hands of a few. Hence there must be redistribution of income in favour of the poor. A high wage economy is germane to greater productivity, better industrial relations, greater stability of demand and prices, better profits, higher investment, better utilization of resources and other benefits.

4. State regulation of wages is in keeping with the objective of establishing a Welfare State.

5. State regulation may raise the efficiency of the workers by ensuring improvements in health, productivity and income distribution.

6. State regulation of wages is essential because of the gap between marginal productivity of labor and actual wages.

State regulation of wages may assume several forms. Wage rates may be fixed directly by legislation, by statutory bodies set up by the Government, by wage boards, by industrial tribunals or by a process of arbitration, conciliation and adjudication. The State may also seek to regulate wages in the private sector by fixing wages in public enterprises, extending collective agreements to other enterprises and by arranging a fair wage clause in public contracts in order that the contractors could be forced to pay minimum wages to their workers. It may also be in the form of fixing a ceiling on a wage rise or the fixing of a minimum.

7.8 SUMMARY

1. Employee turnover refers to the shifting of workforce in and out of an organization and hence it is also referred to as the interfirm mobility of labor.

2. Retirement, resignation, lay-offs and dismissals are the common causes of employee turnover.

3. Employee turnover lowers the efficiency of employees and they are not in a position to enjoy the benefits of loyalty. Employee solidarity is adversely affected by high turnover. The employers also lose on account of turnover. The productivity of employees during the learning period is low which means the cost of learning is borne by the employer.

4. In order to reduce employee turnover across the industry, a scientific study of the problem needs to be made to assess the extent of turnover across the industries and across the plants within industries. The recruitment or placement policy of the firm should be scientific enough to place the right person in the right place at the right time.

7.9 QUESTIONS

1. Explain the concept of employee turnover and examine the causes, consequences and remedies to employee turnover.

2. Explain the concept of migration and examine the causes of rural to urban migration in India.

3. Explain the merits and demerits of rural to urban migration.

❖❖❖❖

8

LABOUR MARKETS IN MARKETS – II

Unit Structure:

8.0 OBJECTIVES

- To see the impact of trade unions on productivity.
- To see the impact of trade unions on wages.
- To study the concept of minimum wages.
- To study the concept of social security.
- To study occupational safety and security.
- To study wage and income policy in India.
- To know the impact of liberalization and globalization.

8.2 IMPACT OF TRADE UNIONS ON PRODUCTIVITY AND WAGES

8.2.1 Impact of Trade Unions on Productivity:

Understanding of unions' effects on productivity is critical to the assessment of labour unions, performance and labour law. Productivity means output for given levels of inputs. A firm that is more productive than another can produce more output using the same combination of inputs or, equivalently, produce the same output using fewer inputs. Increase in productivity attributable to union, mean a real shift in the marginal product schedule, and not just a movement up the labour demand curve (implying a higher capital-labour ratio) in response to a higher wage. If collective bargaining in the workplace were systematically to increase productivity and to do so to such an extent that it fully offset compensation increases, then a strong argument could be made for policies that facilitate union organizing. Productivity increases, it was argued, are affected through the exercise of collective voice along with an appropriate institutional response from management. According to this view, unions lower turnover and establish in workplaces more efficient governance structures that are characterized by public goods, complementarities in production, and long-term contractual relations. The thesis that unions significantly increase productivity has not held up well. Subsequent studies were as likely to find that unions had negative as opposed to positive effects upon productivity. A large enhancement of productivity because of unionization is inconsistent with evidence on profitability and employment. Attention has focused on the dynamic effect of unionization and the negative effects of unions on growth in productivity, sales, and employment. Effects upon productivity tend to be largest in industries where the union wage premium is most pronounced. This pattern is what critics of the production function test predict that union density coefficients in fact reflect a wage rather than a productivity effect. These results also support a "shock effect" interpretation of unionization, whereby management must respond to an increase in labour costs by organizing more efficiently, reducing slack, and increasing measured productivity. Positive effects by unions upon productivity are typically largest where competitive pressure exists and these positive effects are largely restricted to the private, for-profit, sectors. Notably absent are positive effects of unions upon productivity in public school construction, public libraries, government bureaus, schools, law enforcement and hospitals. This interpretation of the productivity studies has an interesting twist: the evidence suggests that a relatively competitive, cost-conscious economic environment is a necessary condition for a positive effect of unions upon productivity, and that the managerial response should be stronger, the larger the union wage premium or the greater the pressure on profits. Yet in such competitive environments that there should be relatively little managerial slack and the least scope for union organizing and wage gains. Therefore, the possibility of a sizable effect by unions upon productivity across the whole economy appears rather limited.

Evidence for other countries is far more limited. British studies, although few in number, show a negative relationship between union density and productivity levels. Evidence for Canada based on an aggregate manufacturing time-series data for the period from 1926 to 1978, suggests initially positive union "shock" effects on productivity, although slower productivity growth due to unionization offsets the positive effects within 5 to 8 years. German evidence is particularly difficult to sort out owing to the widespread presence both of unions with national or centralized bargaining and of mandatory works councils in union and sometimes in non-union settings. Brunello (1992) finds that unions, except those working for small suppliers facing competitive pressure, tend to have negative effects on productivity (and profits) in Japan. Although international evidence is limited, that which exists is broadly supportive of our interpretation of the American evidence. (Ref: Unionization and Economic Performance: Evidence on Productivity, Profits, Investment, and Growth by Barry T. Hirsch Professor of Economics, Florida State University).

8.2.2 Impact of Trade Unions on Wages:

The study of the impact of unions on the economic performance of firms and the competitiveness of the economy is important in the context of Government policy and the design of labour law. It provides the rationale for either strengthening or weakening labour legislation governing bargaining rights and the organizing of unions. Professor Barry T. Hirsch has conducted a study to research into the effects of unionization on productivity, profitability, investment, and employment growth. Barry's study is based on United States, Canada, Japan and Britain. He concludes that the effects of unions upon productivity and productivity growth are small. They do not offset the cost increase resulting from higher union wages. The evidence presented in his study clearly indicates that unionization leads to lower profitability. The impact of unions on profitability at the level of the industry or the firm is such that unionized firms have profits that are 10 percent to 20 percent lower than the profits of non-union firms. Further, the evidence from Britain also suggests that closed-shop unions have a stronger negative impact on profitability. Recent research also shows that union monopolies reduce investment in physical capital and in research & development and other forms of innovative activity.

In a study conducted by Professor Hirsch of 500 publicly traded American manufacturing firms, the capital investment of an average unionized firm was 6 percent lower than that of a comparable non-union firm. Hirsch also found that the average unionized firm made 15 percent lower annual expenditure on R&D. A Canadian study using aggregate data also finds that unions reduce investment in physical capital by a significant margin.

The wage rates are higher in unionized firms. Given higher wages and lower levels of profitability and investment in unionized firms, the employment growth is lower. Studies from Canada, the United States, and Britain on the effects of unionization upon employment show the negative impact of unionization upon employment growth. In the case of Canada, a study conducted in 1993 by Professor Richard Long confirms the international evidence. This study examined the performance of 510 manufacturing firms during the period from 1980 to 1985 and found that the median growth rate of non-union firms during this period was 27 percent while the growth rate of unionized firms was zero. After making adjustments in his analysis to account for the fact that unionized firms tend to be larger than non-unionized firms and found in declining industries, he concluded that unionized manufacturing firms grew 3.7 percent slower than comparable non-unionized firms; and unionized firms in the non-manufacturing sector grew 3.9 percent slower than their non-union counterparts. In sum, the evidence from research indicates that unions tend to increase wages but not productivity, reduce profitability, reduce investment in physical capital and R&D, and, most importantly, lower the rate of employment growth.

8.3 MINIMUM WAGES

According to the Fair Wages Committee appointed by the Government of India in 1949, a minimum wage must provide not merely for the bare sustenance of life but for the preservation of the efficiency of the worker. In order to ensure the efficiency of the worker, the minimum must be sufficient enough to provide for education, health and some amenities. The minimum wages thus provides the workers those comforts and decencies which can promote better habits, self respect and better citizenship. A minimum wage may therefore be defined as one which may be sufficient to enable a worker to live in reasonable comfort having regard to all obligations to which an average worker would ordinarily be subject to –

Fixation of minimum wages is of great significance to industrial workers because it affects their health, strength and morale. In the interest of social justice, wages of workers must be sufficient to ensure the worker a reasonable and fair standard of living. It is important to provide a sufficient living wage to the worker to maintain social stability. Minimum wages are important to maintain industrial peace and harmony. The workers are partners in the production of wealth and hence have a rightful share in the fruits of the industry. Further, the efficiency and productivity of the workers depend on good living and in order to live a good living, a fair amount of wages are required. Finally, the fixation of minimum wage prevents exploitation of the workers and would secure for them wages according to the value of work done, corresponding to the productive capacity of the workers.

The objectives of minimum wages according to the Fair Wages Committee were as follows:

1. To prevent sweating in industry and to raise the wages in those industries where they are extremely low and inadequate.

2. To prevent exploitation of workers and to secure a wage according to the value of the work done, corresponding to the productive capacity of the workers; and

3. To promote peace in industry by keeping he workers happy with the guarantee of a wage rate which may enable them to meet their minimum requirements.

In accordance with the Minimum Wages Advisory Committee and the decisions of various Industrial Tribunals, certain general principles have been evolved by the Government which are to be kept in mind in fixing wages under the Minimum Wages Act.

The Need based Minimum Wages

The Labor Conference held at New Delhi in July 1957 laid down that the minimum wage should be need based and should ensure the minimum human needs of the industrial worker. The following norms were accepted as a guide for all wage fixing authorities including the minimum wage committees, wage boards, adjudicators etc:

1. In calculating the minimum wage, the standard working class family should be taken to comprise three consumption units for one earner, the earnings of women, children and adolescents being disregarded.
2. Minimum food requirements should be calculated on the basis of a net intake of calories as recommended for an average Indian adult of moderate activity.
3. Clothing requirements should be estimated on the basis of a per capita consumption of 18 yards per annum which would give the average workers family of four, a total of 72 yards.
4. The rent corresponding to the minimum area provided for under Government Industrial Housing Scheme should be taken into consideration in fixing the minimum wage.
5. Fuel, lighting and other miscellaneous items of expenditure should constitute 20 per cent of the total minimum wage.

The conference laid down that wherever the minimum wage fixed was below the norms recommended above, it would be incumbent on the authorities concerned to justify the circumstances which prevented them from following the norms. The Wage Boards in India followed the norms while fixing wages for industrial workers.

The Living Wage

The Committee on Fair Wages stated that living wages represented the highest level of the wage and it would include all amenities which a citizen living in a modern civilized society was entitled to expect when the economy of the country was sufficiently advanced and the employer was able to meet the expanding aspirations of his works. The committee observed that the living wages should enable the male earner to provide for himself and his family the bare essentials of food, clothing and shelter but a measure of frugal comfort including education for the children, protection against ill health, requirements of essential social needs and a measure of insurance against the more important misfortunes including old age. However, national income and capacity to pay of the industry must be taken into account while fixing the living wage. The committee set the living wage standard as the upper limit of wage fixation, the lower limit being the minimum wage.

Fair Wages

The Industrial Truce resolution passed in 1947 for improving relations between labor and management provided for the payment of fair wages to labor. Subsequently, the Government of India appointed a Fair Wages Committee in 1948 to determine the principles of fair wages and measures to implement fair wages. The Fair Wages Committee in its report submitted in 1949 observed that the minimum wage is less than the living wage. Fair 158 wages should be above the minimum wage and below the living wage. However, the upper limit of the fair wage should be determined by the capacity to pay, productivity of labor, prevailing rates of wages, the level of national income and the place of the industry in the economy. The family unit may be considered to be comprised of three consumption units.

The Minimum Wages Act of 1948

The statutory minimum wages are fixed according to the Minimum Wages Act, 1948. The Act was passed by the Government of India subsequent to the ILO Convention on minimum wages passed in the year 1921. The Act applies to the employment that are included in Parts I and II of the Schedule to the Act. Once the minimum rates of wages are fixed according to the procedure prescribed by law, it is the obligation of the employer to pay the said wages irrespective of the capacity to pay. The main provisions of the Minimum Wages Act, 1948 are as follows:

1. It provides for fixing minimum wages in certain employments where sweated labor is prevalent or where there is a great chance of exploitation of labor.

2. The Act provides for the fixation of (a) minimum time-rate, (b) a minimum piece rate, (c) a guaranteed time-rate and (d) an overtime rates appropriate to different occupations and different classes of workers. The minimum wage fixed or revised by the appropriate Government will include the following: (a) a basic rate of wage and special allowance at a rate in which adjustments will be made at such intervals and by those methods as directed by the appropriate Government, (b) a basic rate with or without a cost of living allowance and the cash value of the concessions in respect of supplies of essential commodities at nominal rates, (c) a rate in which the basic rate, cost of living allowance and cash value of concession etc all are included. The Act lays down that wages should be paid in cash and empowers the appropriate government to pay wholly or partly in kind.

3. The appropriate government shall review the rates at an interval of not more than five years and revise or amend the minimum wage rates.

8.4 SOCIAL SECURITY

The ILO defines social security as the security that society gives though appropriate organizations against certain risks to which its members are exposed. These risks are essentially contingencies against which the poor people cannot effectively provide on their own singly and collectively. These risks are sickness, maternity, invalidity, old age and death. These risks disable the working person to support himself and his dependents in health and decency. According to this definition only such schemes of the State which provide the citizen with benefits designed to prevent or cure diseases to support when unable to earn and to restore him to gainful activity may be regarded as schemes of social security.

Sir William Beveridge defines social security "as a scheme of social insurance against interruption and destruction of earning power and for special expenditure at birth, marriage o death. It is an attack on five giants namely wants disease, ignorance, squalor and idleness". According to Beveridge, an adequate level of employment, a comprehensive health service and a scheme of children's allowances are essentially required for the success of social security plan.

According to an ILO/Norway National Seminar held in New Delhi in 1977, social security was defined as "the protection furnished by the society to its members through a series of public measures against economic and social distress that are caused due to absence of earnings or substantial reduction or stoppage of earnings resulting from sickness, maternity, employment injury, occupational diseases, unemployment, under employment, invalidity, destitution, social disability and backwardness, old age and death land further to provide health care and prevention measures". According to this definition of ILO, social security measures would include social insurance, social assistance, family benefits, and health care and related social welfare services.

Social security measures have a twofold significance for every developing country. First, social security is an important step towards the goal of a Welfare State in which the living and working conditions of the people are improved and are protected against the uncertainties of the future. Second, social security is important in strengthening the industrialization process. It enables workers to become more efficient and reduces wastage on account of industrial disputes. Person-days lost on account of sickness and disability is also reduced. Lack of social security hinders production and prevents the formation of a stable and efficient labor force. Social security is therefore a wise investment which gives good dividends in the long run.

8.5 OCCUPATIONAL SAFETY AND SECURITY

Occupational hazards are a risk associated with employment. More than 1.8 lac workers die every year due to occupational accidents and diseases and 110 million workers are affected by employment related injuries. Prevention is always better than cure. Occupational health is a preventive measure taken to prevent and pre-empt all possible accidents and diseases that workers may otherwise go through in employment. The International Labor Organization vide its recommendations has influenced governments across the world to enact legislation on occupational health services. In 1981, the ILO adopted a convention and recommendation on occupational safety and health and the working environment which defines a national policy and action to be developed at the level of the industrial units.

The objectives of occupational safety are as follows:

1. Ensure protection to workers against health hazards arising out of work and the work environment.

2. Ensure the physical, psychological and mental welfare of the workers.

The functions of occupational health services are as follows:

1. Identification of occupational hazards and diseases and suggest preventive as well as controlling measures.

2. To ensure safe exposure limits to hazardous work processes by rotating the workers periodically so that no single worker is exposed to his or her own detriment.

3. To impart health education to all workers.

Occupational health and safety is greatly neglected in India due to the relative backwardness of the Indian economy. This is very true of the unorganized sectors of the economy where the workers are thoroughly exposed to all kinds of hazards without any kind of protection at the work place or any kind of compensation to the workers if they suffer from accidents or diseases. The National Commission on Labor, 2002 has recommended a comprehensive legislation for the workers working in the unorganized sector. Once the legislation is put in place, occupational health and safety will be greatly improved in Indian industries.

8.6 WAGES AND INCOMES POLICY IN INDIA

Wages perform two important functions in an economy. Firstly, they distribute the products of the industry among wageearners in the form of income. Secondly, they influence the cost of the output. Wages determine price level and employment. The problems of wage policy have three dimensions. At the national level, it is a matter of resolving the conflicting objectives of better standard of living of workers, expanding employment and increasing capital formation. At the plant level, the problem is that of evolving a system which provides incentives for better productivity. The other important dimension is that of evolving a wage structure which is conducive to economic development. An important objective of planned economic development is raising the standard of living of the people. A vast majority of the working population in a developing country is poor and hence the benefits of planned economic development must go to them. A national wage policy would therefore help the planners in the country to realize the most important objective. A national wage policy must aim at establishing wages at the highest possible level which the economic conditions of the country permit and it also ensures that the wage-earner gets a fair share of the increased prosperity of the country as a whole resulting from economic development.

The term ‘wage policy’ in India refers to legislation that affect the level or structure of wages or both for the purpose of achieving specific objectives of social and economic policy. The social objectives of a wage policy may include the elimination of low wages, the establishment of fair labor standards and the protection of wage earners from rising prices. Increasing the economic welfare of the wage earning community as a whole is an important objective of wage policy. According to the ILO, the objectives of a wage policy in a developing economy should be as follows:

1. To abolish malpractices and abuses in wage payment.

2. To set minimum wages for workers whose bargaining position is weak and to promote the growth of trade unions and collective bargaining.

3. To obtain for the workers a just share in the fruits of economic development and insulate them from inflation.

4. To bring about a more efficient allocation and utilization of labor power through wage differentials and where appropriate through systems of payments by results.

Importance of National Wage Policy in India

The problem of wages is one of the most important labor problems because it is related to every workers and it is a solution to the many of the problems faced by the average Indian worker. Increased individual real incomes mean greater economic welfare. The problem of wage constitutes the major source of friction between the employers and the workers. Industrial workers in India have low literacy levels. They are unorganized and have a weaker bargaining position. In India, the relative strengths of the workers and the employers have determined wage agreements and decisions. Industrial wages in India have remained low and in many occupations of sweating of labor prevailed for quite some time and it prevails to this day in certain pockets across the country. Wage policy and wage regulation therefore becomes essential to ensure fairness to the workers. Wage policy and wage regulation is an integral part of the labor market even in free market economies because justice cannot be left to the market forces and the benevolence of the employers.

8.7 IMPACT OF LIBERALIZATION AND GLOBALISATION

Impact of Liberalization:

With the liberalization of Indian economy in 1991 a number of private players started carving a major role in the economic output and simultaneously governments both at the centre and state levels started assuming a smaller role in running businesses. Increased domestic and foreign competition resulting from the economic reforms induced domestic manufacturers to improve efficiency and bring into use advanced technologies on a larger scale. This is supported by the fact that during the period 1991-98 there were about 3250 technical approvals in India with the top five technical collaborators. The subsequent break down of trade barriers, globalization, advancements in Information and Communications Technology (ICT) and well accepted management ideas such as TQM on quality, JIT, Computer Integrated Manufacturing (CIM) & Lean Production (LP) have served to magnify the impact of technology on employment relationship globally and India in particular.

Technological Change and Employment

Labour employment is affected by many factors, two major directly relevant factors are per unit labour requirement for a product (man hours per unit) and the total demand for the product. It is likely that technological improvement leads to reduction in per unit labour requirement but at the same time because of the increased demand made possible by the lesser cost of the technologically advanced product, it can lead to rise in overall demand for labour . This expected rise in demand for labour has however not been equally true for all sectors/industries . In a study of employment in organized manufacturing sector in India, it was found that even though real gross value added has grown at 7 .4 percent per year during 1981-2002, employment of workers increased only by 4 .3 and most of this growth happened in the early part of the 90s while the latter half of 90sand early part of the current decade have shown a reducing trend in organized manufacturing sector employment.

At the same time, employment in Organized Services sector has been picking up in the latter half of last decade and early part of this decade .Organized manufacturing sector seems to have shown a sharp decline in employment post 1996 while services have gained during this period.

As a consequence of technological modernization of banks it was found that though there was an overall increase in employment, this growth has been made possible by an emerging volume of employment in previously new areas such as systems analysts, console operators etc . In a case of technology transfer to an Indian engineering MNC from its foreign parent company during the period 1974-1984 ,even though the fixed capital increased by about 400 percent.

Further even within the same industry, there seems to be a shift in the occupational and work profile of the employees decreased by 8 percent whereas the total employment increased by 3to 5 percent, indicating.

A shifting of workforce from workers to supervisory and executive squads and a corresponding shift in the skill requirements. In an aggregate study of the organized manufacturing sector for the period 1982-2002, it was found that the increase in gross value added is accompanied by greater employment of employees in the supervisory unit as against the worker cadre. Further there has been a change in demand for the type of employees within the same occupational group, from operatives and labourers to professional and technical workers in many of the industries such as Banking ,Software Services and Textiles.

Impact on Skill Profile

As the manufacturing and service technologies continuously develop like in the case of just-in-time inventory, manufacturing cells, robotics and service quality concepts etc, there is an increasing pressure on the organizations to the largest contributor after agriculture to the employment providing jobs to about 21 million people. When new types of technologically advanced looms were introduced in textile firms, the skill requirements changed to those of monitoring and troubleshooting of the production process instead of directly getting involved in the production. This is because with the introduction of new automated machinery, the technologies are no more separate from each other and detection of faults requires a thorough understanding of the production process and familiarity with different equipment's used. Hence the skill required for the job, which previously emphasized manual dexterity, physical strength in manual and repetitive tasks has been taken over by the need for machine trouble shooting and process handling skills. The roles and responsibilities of the senior workers were more flexible in the modernized mill sand they were expected to handle a higher number of departments compared to rigid and specific allocations along different categories of work within department in the non-modernized mills.

The impact of new technology on skill requirement in the textile industry has been widely reported. Textile industry in India has a special place with 4 percent contribution to the GDP and 12 percent of the world's textile production (GOI 2009). The cotton mill workers account for 20 percent of the total employment in the manufacturing sector and the textile industry introduction of new production processes but may be related to even initiation of new management ideas.

For instance, at the beginning of the nineties, when Motorola started measuring workers performance against quality & outputs instead of measuring against a time clock, it became necessary for its workers to know their equipment and production process, and be able to initiate any trouble shooting process themselves which were previously not in their ambit . This required the worker to unlearn deeply held attitudes and values when they were just responsible for working on individual machines to those of understanding the production process as a whole .

However, the effect of increased investment in technology on wages has not always been positive. Study of the Indian subsidiary of a MNC found that the wages as a proportion to valueadded remained at about twelve percent and has not changed significantly with the introduction of new technology over the years. Further, in a study of sixty select MNCs, found that the aggregate rise in wages and salaries was much lower than the aggregate increase in operational expenses, suggesting that the growth rate of wage bills has not kept pace with investment in operations.

Impact On Wages

The impact of technological change on wages has been mixed. Budhwar (2003) in his study of 137 Indian firms in six manufacturing sectors in India found that collective bargaining and 56 provisions of labour laws have a significant influence in determining the basic wages and bonuses of blue-collared employees , hence indicating that the wages are still determined by factors not directly related to individual/firm performance and technological change . However, this is also sector specific . In a study by Singh & Nandini (1999) in the software industry, it was found that technological change does have a significant effect on salaries paid to employees. Chakravarty (2002) in her study of spinning mill workers found that the modernized mills required `unusual skills' from workers compared to the traditional ones.

The impact on wages because of technology change is also influenced by the political process .Betcherman (1991) argues that there is a positive correlation between wage levels and introduction of advanced technology but how the pie is distributed will depend on the balance of power between the negotiating parties . In the Canadian context, he found that skilled blue-collared workers, both unionized and non-unionised, could bargain a higher pay compared to those doing manual work. Further, the union' s bargaining power was lower for technology innovators than among non-innovators . In a similar vein, in the case of modernized textile mills in India there is an emergence of distinct and firm specific skills which require higher cost and time investments (Chakravarty 2002) . Hence companies are willing to pay higher wages in these mills as contrasted to non-modernised mills . This necessitated decentralized bargaining in the case of modernized firms while the non-modernised ones went in for industry wide bargaining. In the latter case since the skills are not specific to an organization but rather are generic to the industry they required support of the wider political base .Nagaraj (2004) in his study of employment in organized manufacturing sector notes that while real wages of workers have roughly stagnated during 1981-2002, the real emoluments of supervisors have gone up by 77 percent during the same period indicating that the increase in wages due to technology change has not been favourable to the workers in general .

Worker Acceptance

The reasons for introducing new technology vary from one organisation to another. New production system in a plant is brought in by the management typically in response to the change in market conditions, which require more `efficient' technologies to be adopted (Datta 1996). Studies have indicated that the technological improvements/changes lead to improved productivity, lower costs and better work environment (eg :Virmani 1990, Datta 1990) . The improvement in productivity seems to hold for varied sectors from Heavy Electricals (Virmani 1990), Software (Singh &Nandini 1999), Textiles (Chakravart y2002, 2006, Dhanaraj 2001) and Banking (Datta 1990, 1996) . Studies indicate that after a time lag major technological changes have always induced significant changes in the organisation processes.

The unions and the employees into confidence before introduction of automation. This was done through a free flow of information, education and training of employees in terms of what computerization means and what changes it can bring in. The transformation of Bank of Baroda from a large public sector bank with a legacy culture to a highly customer centric, technology driven bank through a variety of initiatives including implementation of Core Banking solutions is credited to clear and transparent communication with the employees (Khandelwal 2007). Studies in the Indian context have shown that attitudes in terms of job satisfaction and freedom and autonomy at the work place were found to be significantly positively related to technology acceptance (Gurtoo & Tripathy 2000, Venkatachalam &Velayudhan 1999) .Venkatachalam & Velayudhan (1999) in their study of a steel plant found significant and positive correlation between meaningful, interesting job and technology, indicating that new technology introduction does have an influence on how the employees feel at work . Unlike in the West Indian employees rarely differentiate the work and develop a feeling of "we-ness" if policies and practices instil among employees the feeling of acceptance and belonging.

8.8 QUESTIONS

Q1. Explain the Impact of Trade Unions on Productivity and Wages.

Q2. Explain the Impact of Liberalization and Globalisation.

Q3. Write a note on –

a) Minimum Wages
b) Social Security
c) Occupational Safety and Security
d) Wages and Incomes Policy in India

❖❖❖❖