

ICTSD Series on Trade-Supported Strategies for Sustainable Development



Trade Integration and Labour Market Trends in India: an Unresolved Unemployment Problem

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LIST OF ABBREVIATIONS AND ACRONYMS

BSE	Bombay Stock Exchange
BPO	business process outsourcing
FRBM	Fiscal Responsibility and Budget Management Act
FII	foreign institutional investors
ICT	Information Communications Technology
IT	information technology
IMF	International Monetary Fund
NASSCOM	National Association of Software and Service Companies
NREGA	National Rural Employment Guarantee Act
NSS	National Sample Surveys
Sensex	Sensitive Index
SLR	statutory liquidity ratio
WTO	World Trade Organization

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FOREWORD

Structural reforms and the liberalization of foreign trade and investment have occurred all over the world. The majority of developing countries have embraced reforms that differ regarding the timing and speed of implementation but not in character. The economic model pursued has combined adjustment and stabilization reforms with the liberalization of foreign trade, increasing the level of competition in international markets.

As a result of their increased integration into the world economy, developing countries today are more exposed to the risks associated with external shocks. Indeed, most of them have suffered greatly from the decrease in global demand, the drying up of trade finance and the decline in investment and remittances resulting from the recent financial and economic crisis. While several developing nations have shown early signs of recovery, the crisis may have reversed modest progress towards poverty alleviation. Furthermore, social indicators suggest that natural rates of unemployment are likely to be higher in the future, prompting concerns about possible jobless growth.

As pointed out by several analysts, despite the liberalization that has occurred over the past few decades, many Asian economies were less affected by the crisis, due to the relatively lower degree of trade and financial integration in international markets, especially if compared with developed economies. This is also the case with India. In the immediate aftermath of the global crisis, the Indian economy experienced a downturn, which was then followed by an early and quite robust recovery. Nevertheless, the ongoing recovery presents many of the features that made the earlier growth strategy inadequate in terms of sustained employment growth. Since the mid-1980s, India has undertaken a series of economic reforms which have progressively liberalized its economy and integrated it into the world economy. These reforms have had a significant impact in terms of GDP growth, economic diversification, and productivity gains in the non-agricultural sector. Nevertheless, they had modest effects in terms of employment generation, leaving India with a significant unresolved unemployment problem.

This paper titled ‘Trade Integration and Labour Market Trends in India’ by C.P. Chandrasekhar (Centre for Economic Studies and Planning, Jawaharlal Nehru University), focuses on the Indian pre-crisis strategy of liberalization and integration into the world economy and its impact on labour market trends. It then examines the specific ways in which the crisis affected the country, with a focus on the labour market. Finally, it draws some concrete policy recommendations which are perceived as an example of successful global integration through liberalization.

With this paper, which was published in combination with three other country-studies (Chile, Mexico, and South Africa), ICTSD aims to contribute to a knowledge based debate on the impact of trade liberalization and the economic and financial crisis on trade and labour market. These studies also aim to inform the debate on whether development assistance and aid for trade in particular, can help to mitigate different impacts of the trade liberalization process and the crisis on the labour market.



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1. INTRODUCTION AND BACKGROUND

A noteworthy feature of the global economic crisis of 2007-08 and the Great Recession that has followed is the differential impact it has had across regions and countries. Experiences both in terms of the length and intensity of the recession and the speed of the recovery have varied substantially. Moreover, the impact of the crisis on the labour market and employment has been significantly different across locations. Asia in general and countries like India within that region are seen to have been less affected, because a lower degree of trade and financial integration is considered to have helped (partially) insulate these countries from the effects of the crisis.

This is surprising because, even if the winds of liberalization blew into many (though not all) countries in Asia rather late, most have been through a process of reform over the past two decades that has substantially increased their integration through trade and investment flows with the rest of the world, especially the developed countries. Furthermore, well before the onset of the recent crisis, analysts began noting the significant effects that post-liberalization trajectories were having on labour markets and the level and nature of employment and unemployment. This paper focused on India is, therefore, concerned with the pre-crisis experience with integration through trade and its impact on labour market trends as a prelude to examining the specific ways in which the crisis affected the country.

Over the past two and a half decades, in most developing countries that have pursued a trajectory of economic reform - either voluntarily or under the influence of assistance-related conditionality - a crucial component of the process has been the liberalization of trade, involving a combination of the weakening or removal of non-tariff barriers and a reduction in applied import tariff rates. This has been true of India as well. India launched on a trajectory of liberalization in the mid-1980s and pursued the policy aggressively after 1991.

The objectives of the process as stated by the advocates of trade liberalization were manifold. In particular, it was expected that the process, by subjecting domestic producers to the cutting edge of international competition, would:

- (i) Revitalise agriculture, which was provided much lower rates of protection compared with manufacturing under the import-substitution regime. The expectation was that the elimination of differentials in protection would turn the terms of trade in favour of agriculture and spur output and employment growth in the sector.
- (ii) Restructure domestic industry so as to weed out high-cost production sustained by protection, thereby improving the efficiency of the use of resources available in the system. This process was to be aided by easier access to imported capital goods and intermediates at internationally comparable prices.
- (iii) Increase exports by removing the relatively higher incentives offered to production for the home market (secluded from international rivalry) as compared with the export market. Exports were also expected to expand because international producers, who were discouraged by restricted access to imports from setting up capacity for production for the world market, would now choose the country as a site for world market production.
- (iv) Ensure a depreciation of the currency and correct for the overvaluation of the exchange rate that had ostensibly resulted from protection, so that imports, especially of capital goods, were rendered expensive in terms of local currency while exports were cheaper when denominated in foreign currencies. This was expected to expand employment and reduce the backlog of unemployment by encouraging

labour-intensive exports and discouraging the use of capital-intensive techniques that had previously been relatively cheap owing to the overvalued exchange rate.

It should be noted that the pursuit of such outcomes requires supportive policies, such as liberalized foreign investment rules and exchange rate regimes as well as freedom for firms and agents to enter or exit from different activities. Further, adoption of trade liberalization necessitates and comes as part of reforms in other areas. For example, it is to be expected that the release of domestic pent-up demand for importables would result in an immediate post-liberalization surge in imports, while export benefits would take time to materialize. Therefore, governments would have to attract foreign capital during the transition to successful trade liberalization to finance the trade deficit. This would require liberalization of rules related to foreign direct and portfolio investment inflows. Trade liberalization, therefore, is inevitably part of a larger package of policies. This makes it difficult in practice to separate the impact of trade reform per se on a particular sector or section of the population. Observed outcomes are the result of the simultaneous operation of a “package” of policies that come under the heading of economic reform.

In addition, although advocates of trade policy liberalization focus attention on the potential gains from liberalization, in practice there are bound to be losses as well. To the extent that liberalization of imports does result in the displacement of some producers who cannot compete with imports and the restructuring of other areas of pre-existing production as a result of international competition, the overall effect of liberalization depends on the degree to which the above-mentioned positive effects, even if realized, outweigh the negative effects of liberalization. From the point of view of employment, both displacement and restructuring (inevitably involving downsizing) are likely to result in a decline in employment. Unless the growth of sectors that benefit from liberalization or the emergence of new firms or activities delivers a larger volume of employment, either the rate of growth or the absolute level of employment is likely to decline.

The paper examines the degree to which each of these processes has delivered the expected outcomes, analysing separately the implications of growth trends in the agricultural, manufacturing and services sectors. It then goes on to assess how these trends and processes have influenced the impact of the global financial and economic crisis on growth rates and patterns and on labour market developments.

2. TRADE LIBERALIZATION IN INDIA

External trade liberalization in India, which marked a departure from the import-substitution strategy that began in the mid 1980s, received a major impetus from the launch of the neoliberal economic reform strategy in 1991. Not only were import controls lifted and quantitative restrictions removed, but also import tariffs were continuously lowered.

The changes were significant for manufacturing goods from the early 1990s; in agriculture the shift from quotas to tariffs reflected the requirements of membership in the World Trade Organization (WTO) and occurred in

the late 1990s. The weighted average import duty, which was about 130 percent in 1991-92 was reduced to an average of about 20 percent by 2004-05 (Mathur and Sachdeva 2005), although India's commitments at the WTO implied tariff bindings of as much as 150 percent in particular sectors, and average tariff bindings of about 80 to 100 percent. The decline in tariffs is also evident from Table 1, which shows the dispersion of import duties between 1991-92 and 2004-05. In most cases trade liberalization measures went well beyond the country's commitments to the WTO.

Table 1. Number of Commodities at Different Duty Rates (6-Digit Level)

Duty Rates (per cent)	1991-92	1994-95	1999-2000	2004-05
300 and above	38	212	0	0
200-299	183	0	8	20
100-199	3913	249	12	49
50-99	756	3670	4	47
25-49	24	633	4546	787
0-24	126	476	569	4261
Total	5040	5040	5139	5144

Source: Mathur and Sachdeva, 2005

This would have implied increasing competition for domestic producers as a direct result of the trade policy chosen by the government. In fact, the stated purpose of liberalization was to align domestic and world prices so as to subject domestic producers to the cutting edge of international competition, while providing them easy access to imported capital goods, intermediates and technology that could help restructure and improve the competitiveness of domestic production.

As is well known, effective rates of protection (which are plagued by computational difficulties) and an index of the extent of coverage of non-tariff barriers on trade are better indices of the efficacy of trade liberalization. Based on such measures, Table 2 indicates that other than for some weakening of non-tariff barriers in the second half of the 1980s, any significant relaxation of protection occurred only after 1991.

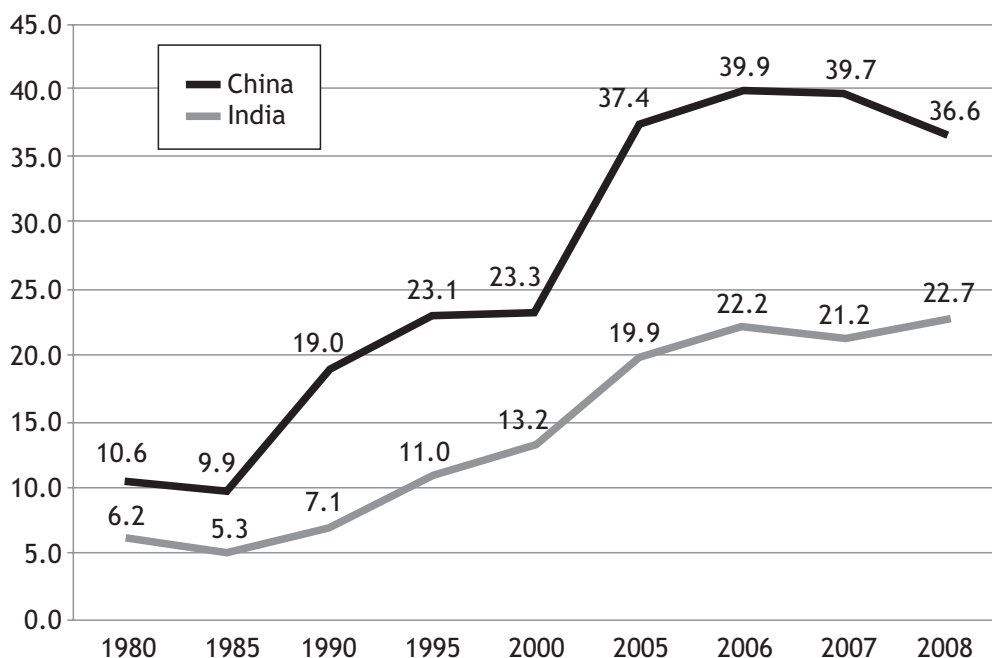
3. TRADE PERFORMANCE SINCE LIBERALIZATION

On the surface, trade liberalization seems to have had a significant impact on India's trade integration. The ratios of both exports (Chart 1) and imports (Chart 2) to GDP rose quite sharply during the 1990s, although to a much lower degree than in China—a country of comparable dimensions and levels of development pursuing a policy of economic reform. However, there is one significant difference between the two countries: China's export success was concentrated in manufacturing while India's was concentrated in services. If we examine the trends in the ratio to GDP of the exports of goods alone (Chart 3), this shows the same trend as the exports of goods and services in China. However, growth has been much less impressive in India, especially since the mid-1990s despite the fact that trade restrictions applicable on goods were substantially liberalized. Since much of trade liberalization was focused on the manufacturing sector, this makes it difficult to directly link trade

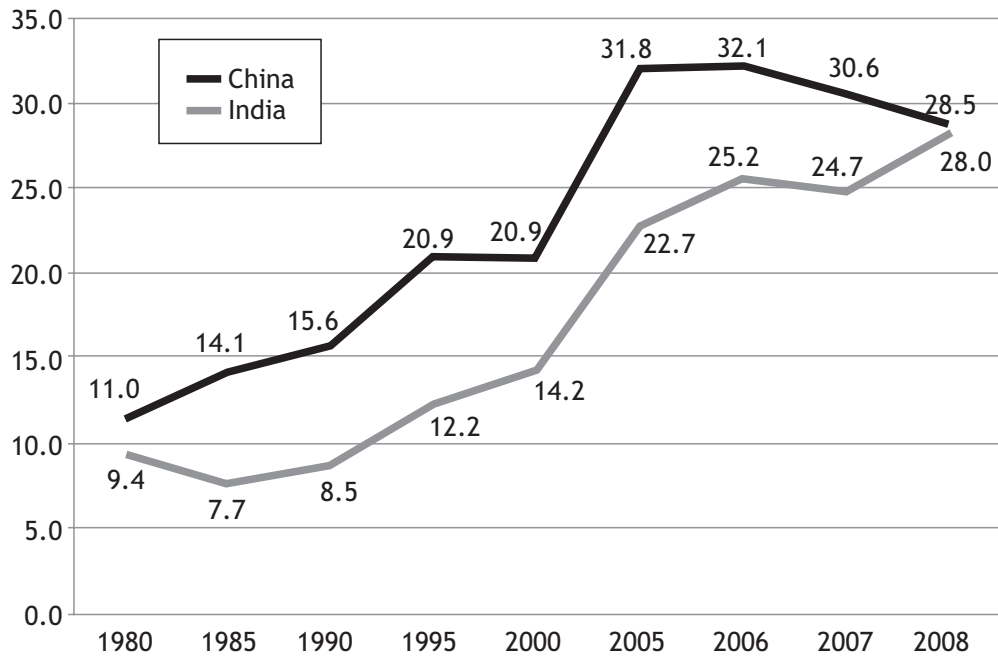
liberalization to the country's export performance, although liberalization did affect the level of manufactured imports into the country.

The ambiguous performance of the country with respect to exports of goods (as opposed to services) comes through when we examine the evidence more closely (Table 3). While the growth of merchandise exports in the 1990s was more rapid than in the previous decade, it did not match up to the growth experienced in the 1970s when the economy was much more closed. Meanwhile, the growth of merchandise imports in the 1990s was much more rapid than in the 1980s (although much less than in the 1970s when it reflected the oil price shocks). There were signs of a revival in merchandise exports during the first six years of this decade. But since imports have grown faster than exports, the merchandise trade balance has deteriorated.

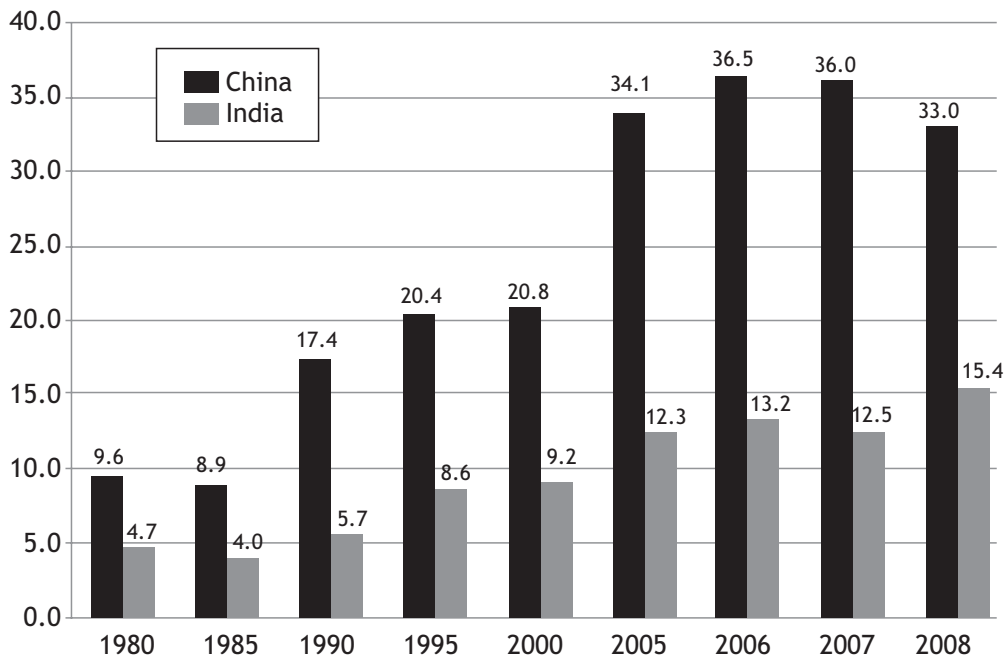
Figure 1. Exports of Goods and Services (as % of GDP)



Source: World Bank, World Development Indicators Online.

Figure 2. Imports of Goods and Services (as % of GDP)

Source: World Bank, World Development Indicators Online.

Figure 3. Merchandise Exports to GDP ratio (%)

Source: World Bank, World Development Indicators Online.

Table 2. Indices of Protection

Industry Group	Phase-1	Phase-2	Phase-3	Phase-4	All Phases
	1980-85	1986-90	1991-95	1996-00	1980-2000
Average Effective Rate of Protection (Percent)					
Intermediate Goods	147.03	149.18	87.58	40.13	112.36
Capital Goods	62.77	78.45	54.23	33.3	61.87
Consumer Goods	101.51	111.55	80.55	48.28	87.47
All- Industries	115.11	125.93	80.18	40.43	95.19
Average Import Coverage Ratio (Percent)					
Intermediate Goods	98.31	98.26	41.77	27.6	71.47
Capital Goods	95.11	77.21	20.47	8.15	54.37
Consumer Goods	98.69	87.85	45.69	33.43	68.77
All- Industries	97.59	91.64	37.97	24.82	67.11

Source: Das 2003, p.18.

Reserve Bank of India, Handbook of Statistics on Indian Econom , available at www.rbi.org.in.

Notes:

1. Period averages are computed as a value-added share weighted average of the yearly figures.

2. The import coverage ratio is defined as: $C_j = S D_i M_i / S M_i$, where D_i is a dummy variable defined as: $D_i=1$, if the product is included in banned/restricted, limited permissible or canalized lists and $=0$ if the product is under OGL

Table 3: Growth Rates of Exports and Imports in US Dollars

	Exports	Imports
1970-71 to 1979-80	17.61	19.92
1980-81-1989-90	6.74	3.27
1990-91-1999-00	9.72	10.84
2000-01 to 2005-06	19.79	25.59

Source: Computed from figs from Reserve Bank of India, Handbook of Statistics on Indian Economy, available at www.rbi.org.in.

4. EMPLOYMENT AND LABOUR MARKET CONDITIONS

4.1 1990s: Post Liberalization Period

In the 1990s, it became fashionable among critics of the plan-led, mixed economy-based strategy to argue that it was this very strategy that was responsible for the slow rate of employment growth. It was suggested that export pessimism and an inward-looking import-substitution policy had discouraged employment-intensive export production and spurred high-cost, capital-intensive production, which had low linkage effects with the rest of the economy and did not lead to more use of labour.

Related to this argument, as noted above, was that the liberalization of external trade and foreign investment would not only generate a higher rate of output growth, but also lead to a restructuring of production in favour of labour-intensive activities and therefore also an increase in employment. However, evidence yielded by the quinquennial National Sample Surveys (NSS) on Employment and Unemployment, indicated that till the end of the 1990s this expectation was not realized.¹ And even though, there had been acceleration in employment growth between 1999-2000 and 2004-05, the rates of growth recorded between 1987-88 and 1993-94 have not been equalled.

The NSS surveys (conducted in 1983, 1987-88, 1993-94, 1999-2000 and 2004-05) revealed a sharp, and even startling, decrease in the rate of employment generation across both rural and urban areas during the 1990s.² Indeed, so dramatic were the fall of work force participation and the slowdown in the rate of employment growth that they called into serious question the pattern of growth over this decade. The rate of growth of employment, defined in terms of the current daily status (a flow measure of the extent of jobs available) declined from 2.7 percent per year in the period 1983-94 to only 1.07 percent per year in 1994-2000 for all of India. This refers to all forms of employment - casual, part-time and self-employment. For permanent or secure jobs, the rate of increase was close to zero. In rural

areas, the decline in all employment growth was even sharper, from 2.4 percent in 1983-94 to less than 0.6 percent over 1994-2000. This included all forms of employment, whether undertaken as the principal or subsidiary activity and for part of the day. This was well below the rate of growth of population. In both rural and urban areas, the absolute number of unemployed increased substantially, and the rate of unemployment went up as well. The daily status unemployment rate in rural India as a whole increased from 5.63 percent in 1993-94 to 7.21 percent in 1999-00, and was more than 15 percent in some states. In addition to this, there was a sharp decline in the rate of growth of labour force. More people declared themselves to be not in the labour force, possibly driven to this by the shortage of jobs.

If we restrict the analysis to usual status (as opposed to daily status) employment, there is once again a very significant deceleration for both rural and urban areas, with the annual rate of growth of rural employment falling to as low as 0.67 percent over the period 1993-94 to 1999-2000. This is not only less than one-third the rate of the previous period 1987-88 to 1993-94, but also less than half the projected rate of growth of the labour force in the same period. Calculations of the employment elasticity of rural output growth based on these growth rates and on estimates of the rural share of GDP yield an employment elasticity of rural output growth of only 0.13 for 1993-94 to 1999-2000, compared with 0.38 for the previous period.³

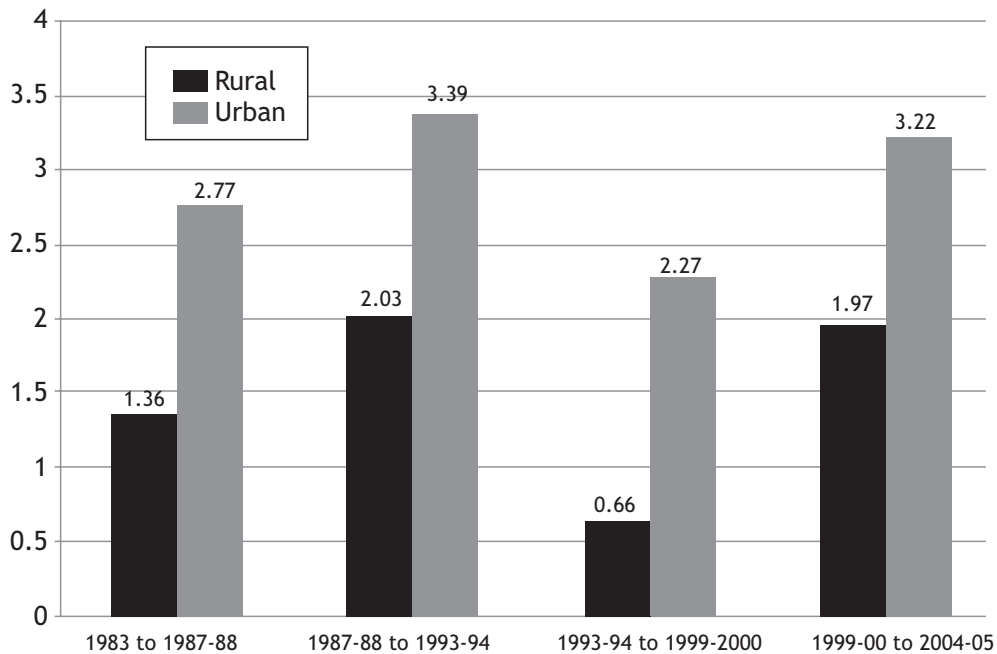
Some of this was because of the decline in public spending on rural employment programmes since the mid-1990s. As a percentage of GDP, expenditure on both rural wage employment programmes and special programmes for rural development declined from the mid-1990s. The total central allocation for rural wage employment programmes was only 0.4 percent of GDP in 1995-6, but it declined further to a minuscule 0.13 percent of GDP in 2000-1.⁴

4.2 Recent Recovery in Employment

While these were the trends during the 1990s, the most recently released NSS employment survey - the 61st Round, covering 2004-

05 - suggests that there have been notable changes in the employment patterns and conditions of work in India over the first half of this decade, with indications of a revival of employment growth.

Figure 4. Annual Rates of Employments and Growth for Usual Status Workers (%)



The first important change from the previous period (1993-94 to 1999-2000) relates to aggregate employment growth itself. As noted above, the late-1990s was a period of quite dramatic deceleration of aggregate employment generation, which fell to the lowest rate recorded since such data began being collected in the 1950s. However, the most recent period indicates a recovery, as shown in Chart 4.

While aggregate employment growth (calculated at compound annual rates) in both

rural and urban India was still slightly below the rates recorded in the period 1987-88 to 1993-94, it clearly recovered sharply from the deceleration of the 1993-94 to 1999-00 period. The recovery was most marked in rural areas, where the earlier slowdown had been sharper. This in turn reflects an increase in labour force participation rates for both men and women, as shown in Table 4. This includes both those who are actively engaged in work and those who are unemployed but looking for work.

Table 4. Labour Force Participation Rates

	Usual status (PS+SS)			Current daily status		
	1993-94	1999-2000	2004-05	1993-94	1999-2000	2004-05
Rural males	56.1	54	55.5	53.4	51.5	53.1
Rural females	33	30.2	33.3	23.2	22	23.7
Urban males	54.3	54.2	57	53.2	52.8	56.1
Urban females	16.5	14.7	17.8	13.2	12.3	15

Source: NSSO, *Employment and Unemployment Situation in India, Sept 2006*

For rural males, labour force participation rates have recovered to the levels of the earlier decade, and conform to broader historical norms. Similarly, rural females show labour force participation rates only slightly higher than in 1993-94. However, for both males and females in urban areas, the most recent period indicates significant increases in labour force participation according to both usual status and current daily status definitions.⁵

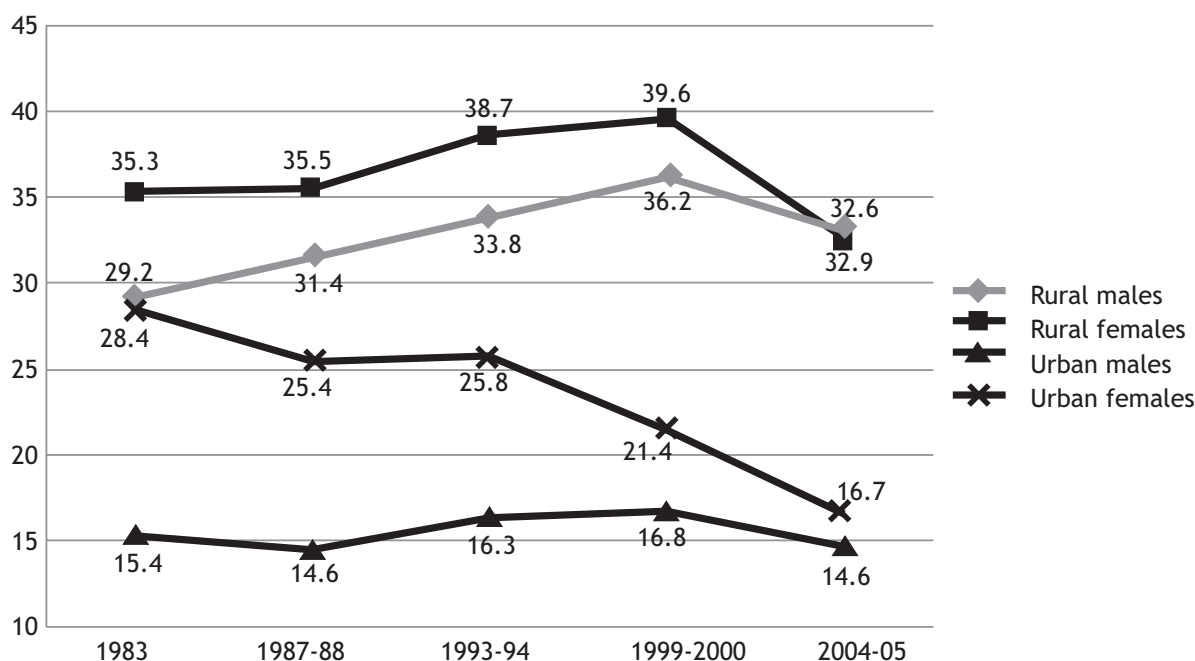
4.3. Characteristics of Employment

One of the more interesting features that emerge from these data is the shift in the type of employment. There has been a significant decline in wage employment in general. While regular employment has been declining as a share of total usual status employment for some

time now (except for urban women workers), wage employment had continued to grow in share because employment on casual contracts has been on the increase. But the latest survey round suggests that even casual employment has fallen in proportion to total employment, as indicated in Chart 5.

For urban male workers, total wage employment is now the lowest it has been in at least two decades, driven by declines in both regular and casual paid work. For women, in both rural and urban areas, the share of regular work has increased but that of casual employment has fallen so sharply that the aggregate share of wage employment has fallen. So there is clearly a real and increasing difficulty among the working population, of finding paid jobs, whether they are in the form of regular or casual contracts.

Figure 5. Share of Casual Labour in Total Employment (%)

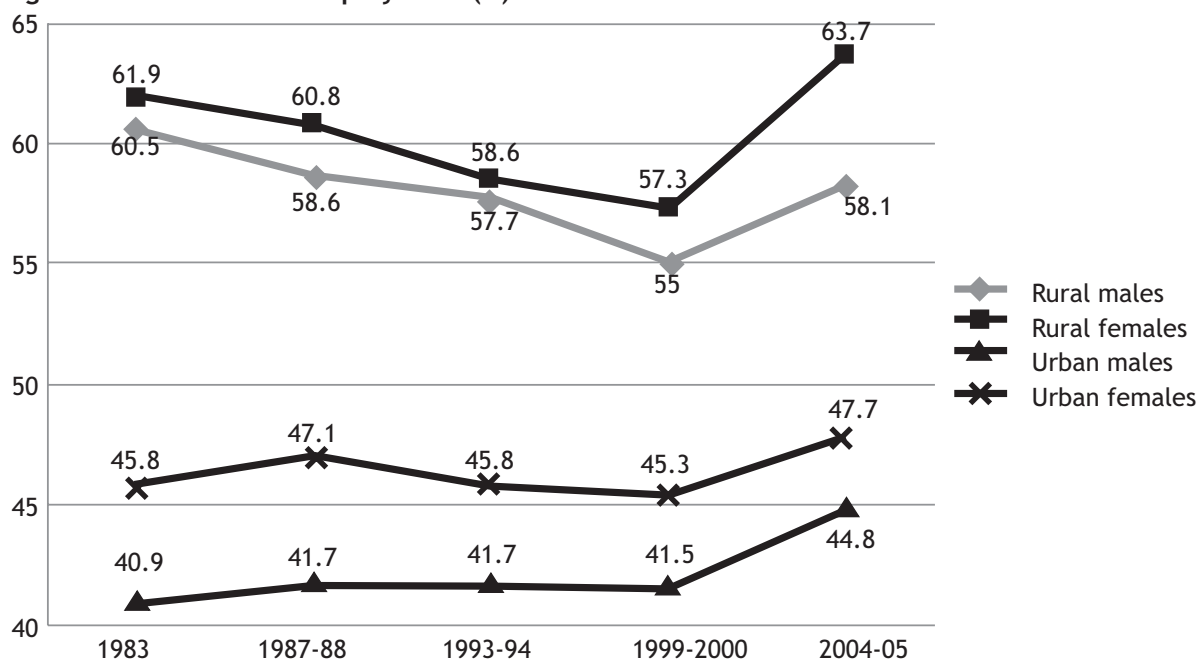


Source: NSSO, *Employment and Unemployment Situation in India, Sept 2006*.

The fallout of this is indicated in Chart 6 - a very significant increase in self-employment among all categories of workers in India. The increase has been sharpest among rural women, where self-employment now accounts for nearly two-thirds of all jobs. But it is also remarkable for urban workers, both men and women, among whom the self-employed constitute 45 and 48 percent, respectively, of all usual status workers.

All told, therefore, around half of the work force in India currently does not work for a direct employer. This is true not only in agriculture, but also increasingly in a wide range of non-agricultural activities. This in turn requires a significant rethinking of the way analysts and policy makers deal with the notion of "workers".

Figure 6. Share of Self-Employment (%)



Source: NSSO, *Employment and Unemployment Situation in India, Various Rounds*.

Table 5. Employment by Industry [percent of employment according to Usual Status (PS+SS)]

	1993-94	1999-2000	2004-05
Agriculture			
Rural males	74.1	71.4	66.5
Rural females	86.2	85.4	83.3
Urban males	9	6.6	6.1
Urban females	24.7	17.7	18.1
Manufacturing			
Rural males	7	7.3	7.9
Rural females	7	7.6	8.4
Urban males	23.5	22.4	23.5
Urban females	24.1	24	28.2
Construction			
Rural males	3.2	4.5	6.8
Rural females	0.9	1.1	1.5
Urban males	6.9	8.7	9.2
Urban females	4.1	4.8	3.8
Trade, hotels & restaurants			
Rural males	5.5	6.8	8.3
Rural females	2.1	2	2.5
Urban males	21.9	29.4	28
Urban females	10	16.9	12.2
Transport, storage & communications			
Rural males	2.2	3.2	3.9
Rural females	0.1	0.1	2
Urban males	9.7	10.4	10.7
Urban females	1.3	1.8	1.4

Table 5. *Continued*

	1993-94	1999-2000	2004-05
Other services			
Rural males	7	6.1	5.9
Rural females	3.4	3.7	3.9
Urban males	26.4	21	20.8
Urban females	35	34.2	35.9

Source: NSSO, *Employment and Unemployment Situation in India, Sept 2006*.

Table 5 provides the details of the industries in which workers are engaged. While, as expected, there has been a significant decline in agriculture as a share of rural employment, the share of manufacturing employment has not gone up commensurately for rural male workers. Instead, the more noteworthy shift for rural males has been to construction, with some increase in the share of trade, hotels and restaurants.

For urban males, on the other hand, the share of trade, hotels and restaurants has actually declined, as it has for other services. Manufacturing is back to the shares of a decade

ago, still accounting for less than a quarter of the urban male work force. The only consistent increases in shares have been in construction and to a lesser extent transport and related activities.

Interestingly, the big shift for urban women workers has been to manufacturing, the share of which has increased by more than 4 percentage points. A substantial part of this is in the form of self employment. Other services continue to account for the largest proportion of women workers, but the share of trade hotels and restaurants has actually fallen compared with 1999-2000.

Table 6. **Growth Rates of Employment (Annual compound rates percent)**

	1993-94 to 1999-2000	1999-2000 to 2004-05
Agricultural self employment	-0.53	2.89
Agricultural wage employment	1.06	-3.18
Total agricultural employment	0.03	0.83
Rural non-agri self employment	2.34	5.72
Rural non-agri wage employment	2.68	3.79
Rural total non-agri employment	2.26	5.27
Urban non-agri employment	3.13	4.08
Secondary employment	2.91	4.64
Tertiary employment	2.27	4.67
Total non-agricultural employment	2.53	4.66

Source: Computed from figures from NSSO, *Employment and Unemployment Situation in India, Sept 2006*.

These activity rates, combined with projections of population growth from the Registrar General, allow us to estimate the growth of employment by broad category over the period 1999-2000 to 2004-05 and compare it with the earlier period. The results are shown in Table 6. While there has been a slight recovery in the rate of growth of agricultural employment, this is essentially because of a significant increase in self-employment on farms (dominantly by women workers) as wage

employment in agriculture has actually fallen quite sharply.

However, urban non-agricultural employment certainly appears to have accelerated in the latest period. In rural areas, this is the case for both self and wage employment, although the rate of increase has been more rapid for self employment. In urban areas, the increase has been dominantly in self employment. Such expansion would indeed be a sign of a positive

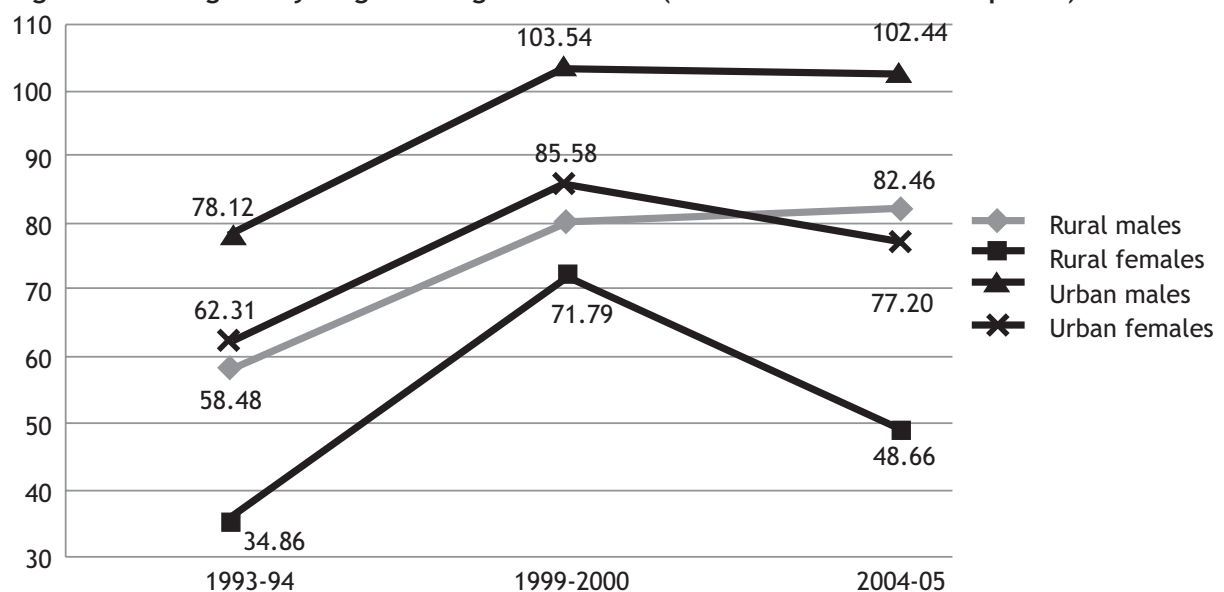
and dynamic process if it is also associated with rising real wages, or at least not falling real wages. Therefore, in order to appreciate the nature of this new employment, it is important to examine the trends in real wages and remuneration for self-employment over this period.

Chart 7 presents the average wages of workers by category, in constant 1993-94 prices. All the wage data used here refer to the wages received by workers in the age group 15-59 years. (In this chart as well as in the following charts and

tables in which real wages are presented, the current price wage data have been deflated by the Consumer Price Index for Agricultural Labourers for rural workers and the Consumer Price Index for Industrial Workers for urban workers.)

It is evident that for most categories of regular workers, the most recent period has not been one of rising real wages. While real wages have increased slightly for rural male regular employees, the rate of increase has certainly decelerated compared with the previous period.

Figure 7. Average Daily Wages of Regular Workers (Rs. at constant 1003-94 prices)



Source: Calculated using figures from NSSO, *Employment and Unemployment Situation in India, Various Rounds and the Consumer Price Indices for Industrial and Agricultural Workers from Labour Bureau Shimla at <http://labourbureau.nic.in/>.*

For all other categories of regular workers, real wages in 2004-05 were actually lower than in 1999-2000. The economy has therefore experienced a peculiar tendency of falling real wages along with relatively less regular employment for most workers. The sharp increase in real wages of regular female workers in rural areas in 1999-2000 may be the result of statistical error, since it reflects a large - and unlikely - increase in wages of only one category of such workers (those women workers who had up to primary education only). Therefore the changes in such wages are unlikely to be as sharp as suggested by Chart 7.

All this should be seen in conjunction with dramatically increasing rates of open unemployment, especially for women. Unemployment rates according to the latest survey

are the highest ever recorded. Unemployment measured by current daily status, which describes the pattern on a typical day of the previous week, accounted for 8 percent of the male labour force in both urban and rural India, and between 9 and 12 percent of the female labour force.

The real expansion in employment has come in the form of self-employment, which now accounts for around half of the work force in India. The increase has been sharpest among rural women, where self-employment now accounts for nearly two-thirds of all jobs. But it is also remarkable for urban workers, both men and women, among whom the self-employed constitute 45 and 48 percent, respectively, of all usual status workers.

As mentioned earlier, this raises a number of issues. For example, how does one ensure decent conditions of work when the absence of a direct employer means that self-exploitation by workers in a competitive market is the greater danger? How do we assess and ensure “living wages” when wages are not received at all by such workers, who instead depend upon uncertain returns from various activities that are typically petty in nature? What are the possible forms of policy intervention to improve work conditions and the possible strategies of worker mobilization in this context?⁶

These questions are significant because of the evidence on remuneration from self-employment. If working people are moving away from paid jobs to more independent and

more remunerative forms of self-employment, that is certainly to be welcomed. But if they are forced to take on any activity on their own in order to survive, simply because a sufficient number of paid jobs is not available, that is another matter altogether. This is especially the case for less educated workers without access to capital or bank credit. Self-employment for such workers often means they are forced into petty, low-productivity activities with low and uncertain incomes.

The latest NSS report confirms this, with some very interesting information about whether those in self-employment actually perceive their activities to be remunerative. This information is presented in Table 7.

Table 7. Perceptions Regarding Remuneration in Self-Employment

	Percent finding their self-employed activity remunerative	Percent finding this amount of INR per month remunerative					
		0-1000	1001-1500	1501-2000	2001-2500	2501-3000	> 3000
Rural males	51.1	12.9	17.5	16.5	11.4	12.9	27.3
Rural females	51.4	34.2	23.5	15.4	8.9	7.2	9.9
Rural persons	51.2	21.2	19.7	16	10.5	10.7	20.5
Urban males	60.9	4.9	8.2	9.9	7.2	12.2	56.5
Urban females	50.9	32.8	20.2	12.6	7.7	8.1	18.3
Urban persons	58.6	10.4	10.6	10.4	7.4	11.5	48.9

Source: NSSO, *Employment and Unemployment Situation in India, Sept 2006*.

It turns out that just under half of all self-employed workers do not find their work to be remunerative. This is despite very low expectations of reasonable returns - more than 40 percent of rural workers declared they would have been satisfied with earning less than INR 1500 per month (approximately USD 33 or just above USD 1 a day), while one-third of urban workers would have found up to INR 2000 (USD 44) per month to be remunerative.

This suggests that a large part of the increase in self-employment - and therefore in employment as a whole - is a distress-driven phenomenon, led by the inability to find adequately gainful paid employment. So the apparent increase in aggregate employment growth in the most recent period appears to be more an outcome of the search for survival strategies than a demand-led expansion of productive income opportunities.

5. TRADE, GROWTH AND EMPLOYMENT

Among the many ways trade liberalization is expected to impact employment positively is by accelerating growth. However, the labour market conditions detailed above were realized in a period when growth in the Indian context was accelerating. This raises two questions: First, did trade liberalization contribute to the acceleration of growth? Second, why did that growth not translate into proportionate increases in employment?

More generally, as noted earlier, the impact of trade liberalization on labour markets was expected to be mediated by four processes: (i) an increase in the overall rate of growth of the system; (ii) a shift of production in favour of sectors that are labour intensive in character; (iii) a shift of production in favour of more labour-intensive techniques within individual industries; and (iv) changes in the relative bargaining position of workers as a result of the changes in the extent of work participation. Which of these expected results did not materialize and why?

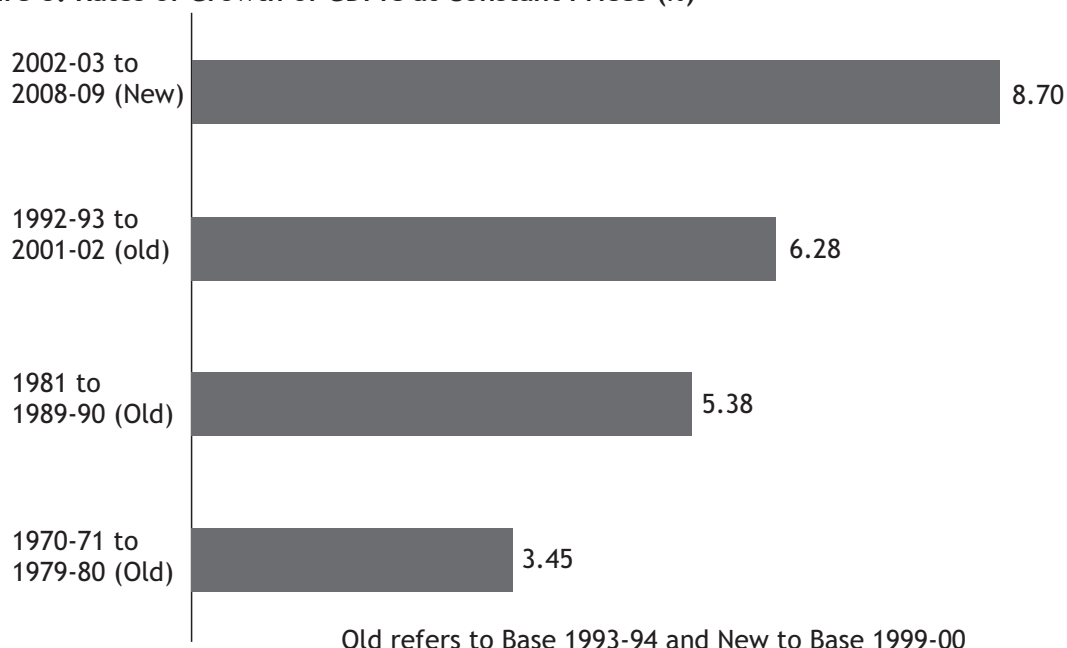
Conceptually, trade can prove positive from the point of view of growth, through possible direct and indirect routes. Directly, larger exports and/or a higher rate of expansion of exports triggered by liberalization can stimulate growth because of positive net exports or a trade surplus that serves as a demand stimulus and an inducement to invest for an individual country.

More important, however, are the indirect effects of trade on growth and employment, which can take many forms. To start with, export revenues allow a country to dissociate the structure of domestic supplies from domestic production. This permits use of the possibilities of transformation through trade

to ensure availability of adequate quantities of commodities crucial to growth. For example, while it is true that, given the incremental capital-output ratio, the rate of growth depends on the rate of investment, countries may fail to realize that growth because the commodity composition of the investable surplus may not be as per requirements. There could be a shortage of capital stock to employ the labour force, or there could be a shortage of wage goods that results in a bottleneck to growth. Finally, there could even be an intermediate goods bottleneck that restrains the pace of growth.

One way to overcome these bottlenecks is to import the requisite amount of the commodity concerned from abroad. But if the foreign exchange cost of such imports is not financed with earnings from exports, the danger of a balance of payments crisis is real. Thus, it may be crucial for a country to engage in trade merely to earn the foreign exchange to finance imports associated with a given rate of growth and a given trade policy regime.

This having been said, it should be noted that whether these forces operate is an empirical question. And the evidence on the relationship between trade liberalization and growth is ambiguous at best. In this context, India offers an interesting example, for during the years of liberalization the country sustained a high and accelerating rate of growth. According to official figures, GDP growth accelerated from its “Hindu rate” origins of around 3.5 percent in the 1970s and earlier to 5.4 percent in the 1980s, 6.3 percent during the decade starting 1992-93 and an annual average rate of close to 9 percent during the years 2002-03 to 2008-09 (Chart 8). However, when the global crisis affected growth, rates fell to 6.7 percent in 2008-09 and 7.4 percent in 2009-10.

Figure 8. Rates of Growth of GDPfc at Constant Prices (%)

Source: Central Statistic Organisation, Government of India

A point to note, however, is that the process of acceleration of growth began well before trade liberalization. While growth accelerated from 1980 itself, trade liberalization picked up momentum only in the 1990s, as noted earlier. Therefore, the acceleration in growth cannot be attributed to trade liberalization alone. But what is of interest is that such liberalization did not slow the process of acceleration. Thus, India is of interest because we can examine the impact of trade liberalization on the labour market in a context of creditable growth.

Even if the process of acceleration of growth cannot be directly attributed to trade liberalization, it is not necessarily true that growth in trade has not had positive effects on the growth in GDP. What is important is to take note of the distinction between the impact on growth of a “policy of openness” and of just greater involvement in trade. As Rodriguez and Rodrik (1999) emphasize, the question “Do countries with lower policy-induced barriers to international trade grow faster, once other relevant country characteristics are controlled for?”. Is different from the alternative question, “Does international trade raise growth rates of income?” While policy changes can influence trade volumes, their effect on growth need not be the same as the effect of an increase in trade due to a reduction in transport costs for

example. Moreover, there is much controversy surrounding the empirical validity of the view that an open trade policy in one country boosts growth when compared to growth in a similarly placed country with more restrictive trade policies [See for example Sachs and Warner (1995); Frankel and Romer (1999); Rodriguez and Rodrik (1999) and Srinivasan and Bhagwati (1999)].

To examine empirically whether there is any relationship between trade expansion and the creditable rates of growth India has recorded since the 1980s it is useful to begin by examining the pattern of growth. For some time now the rate of growth of services GDP has been much higher than the rate of growth of overall GDP. As a result the share of services in GDP, which was about a third in the early 1970s, had risen to more than a 57 percent by 2008-09. More than 60 percent of the increment in GDP during the period after 1993-94 was due to an increase in GDP from services.

Services have also contributed significantly to the recent acceleration of the growth rate, with rates of growth of services GDP averaging more than 10 percent in the 6years ended in 2008-09. Given the high share of services in overall GDP, that sector would account for an overwhelming share of the higher rate of growth.⁷

This trajectory does make India's growth experience unusual, if not unique. The sharp increase in the share of services in GDP in India has occurred at a much lower level of per capita income than characterized the developed countries when they experienced a similar expansion. There are, of course, reasons why growth in developing countries today would reflect a premature expansion of services. To start with, globally manufacturing units today rely as much or more on management and control as on technology to raise productivity and reduce costs. This has increased the services component in manufacturing GDP. The pressure to reduce costs leads to the outsourcing of many of these functions, resulting in the services component of manufacturing GDP appearing as a separate revenue stream and generating a consequent increase in services GDP. Inasmuch as liberalization leads to a faster adoption of imported best practice technologies in developing countries, they too would tend to reflect this tendency. In addition, the communications revolution has cheapened the cost of communication services, resulting in a much greater and earlier use of such services. Not surprisingly, the reach of and revenues from communication services has increased substantially in developing countries, contributing to an increase in GDP from services. Finally, the shift in emphasis in government spending from participation in production to provision of a range of public services tends to increase the share of public administration (not to mention defence) in GDP. Overall, these factors could trigger a diversification of economic activity in favour of services at an earlier stage of development than that expected on the basis of the historical experience of the developed countries of today.

However, even these factors cannot explain the Indian experience, wherein unlike many other similarly placed developing countries GDP from services now exceeds 55 percent of the total. Services must be growing faster than warranted by the above factors. What seems to matter at the margin, is an increase in the exports

rather than domestic supply (and consumption) of services. Services were earlier considered non-tradables since they required in most cases the presence of the supplier at the point of provision. But modern developments have made a number of services exportable through various modes of supply, including cross-border supply through digital transmission.

Such exports do seem to play an important role in India. Exports of software services, which amounted to an average of 7.1 percent of services GDP during 2000-01 to 2002-03, stood at an average of 11.2 percent during 2003-04 to 2005-06 and close to 14 percent in 2005-06. Software and business (largely IT-enabled) services dominate services exports, accounting for 52.8 percent of the total during 2004-05, 56.1 percent in 2005-06 and a massive 66 percent in the first quarter of 2006-07. Thus, trade expansion can be seen to have played a role in India's recent growth acceleration, though what matters is trade in services and not in goods.⁸

The question that remains is whether trade liberalization has played a role in this process. Advocates of liberalization argue that it has. Free access to cheap imports of information technology equipment was no doubt a facilitating factor, even if it cannot be seen as a driver. But more important is the liberalization of trade and entry conditions in the telecommunications sector that has resulted in substantial expansion and massive reduction in the cost of connectivity, which has helped shore up the competitiveness that India's pool of cheap, skilled English-speaking manpower ensures. Thus, while the transition to the higher growth trajectory occurred well before accelerated liberalization began in the 1990s there could be reason to argue that services exports expansion facilitated and pushed by liberalization has contributed to the recent acceleration of growth rates.

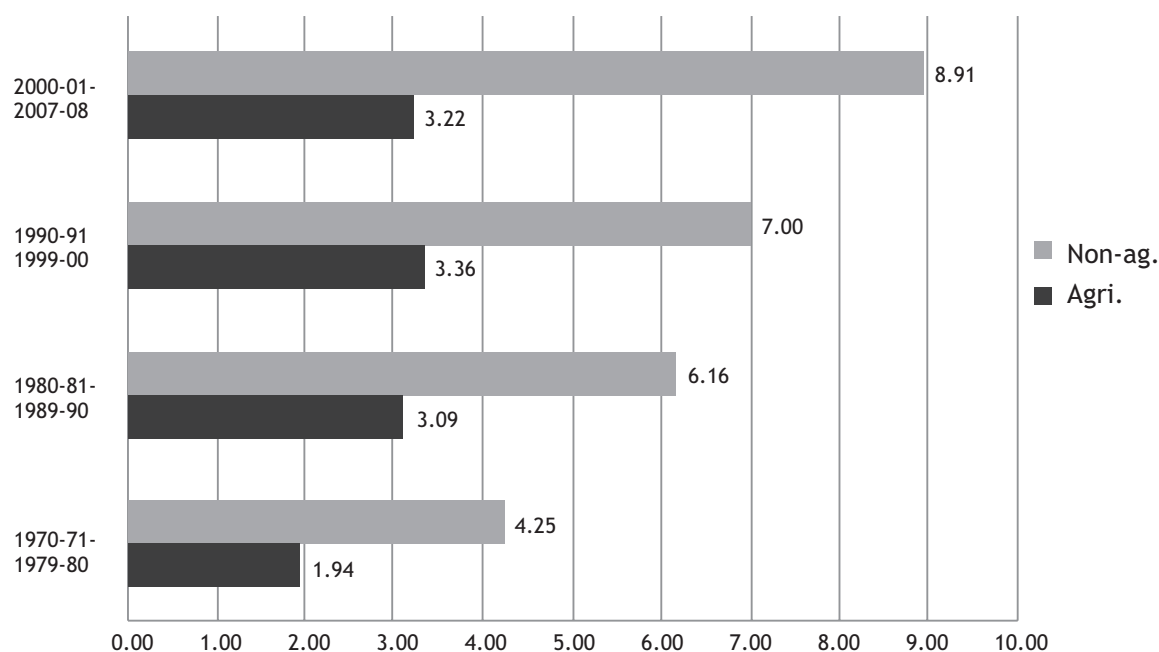
However, this gain from trade (and possibly liberalization) has been accompanied by losses in other areas. The rapid trade-led expansion of services has of course been accompanied

by the relatively poor performance of the commodity producing sectors. What is more, specific commodity producing sectors may be experiencing a process of retrogression, which the aggregate growth figures could conceal. This is, unfortunately, definitely true in the Indian case. While the factors accounting for the acceleration in GDP growth are still being debated, another unusual feature of this growth since the 1980s has received less attention: the growing disproportionality between agricultural and non-agricultural growth. As Chart 9 shows, the disparity in the rate of growth of agricultural and non-agricultural GDP increased significantly after

the 1970s, with the process being particularly marked after the mid-1990s.

What is particularly remarkable is that the acceleration of non-agricultural growth during the 1990s was accompanied by a decline in the rate of growth of agriculture, which was the sector accounting for a dominant share of employment. During the period 1999-2000 to 2008-09, while agricultural GDP had grown at 3.2 percent, the trend rate of growth of non-agricultural GDP exceeded 8.9 percent. The disproportionality is visible even when the comparison is restricted to industrial and agricultural growth.

Figure 9. Sectoral Rates of Growth



Source: Computed from figures reported in RBI, *Handbook of Statistic on Indian Economy*

These trends suggest that domestic agricultural growth is now not as much of a constraint on the growth of the non-agricultural sector as it has been in the past. This does mark a structural shift in the pattern of growth when compared with the first three decades of post-independence development, when the agricultural bottleneck was seen as an important factor responsible for the failure of the strategy of development based on the Mahalanobis model. The argument was that the Mahalanobis strategy underestimated the agricultural constraint by treating agriculture as a bargain sector in which output growth could be accelerated without much investment,

by making suitable institutional adjustments (Chakravarty 1992, Patnaik 1995). Investment could, therefore, be allocated disproportionately to manufacturing in general and heavy industry in particular to accelerate growth.

The fact that the agrarian constraint was in India's case binding was brought home by the balance of payments and inflationary crises that India experienced in the mid-1960s, which was the prelude to a long period of low rates of growth of non-agricultural GDP that India experienced till the late 1970s. What emerged from discussions on that period of "secular stagnation", to which many contributed, was

that there were three forms of intersectoral linkages between the agricultural and non-agricultural sectors that were important (Raj 1976, Vaidyanathan 1977). First, with the agricultural sector accounting for 61 percent of non-residential GDP in 1950/51 (at constant 1993-94 prices) and 76.2 percent of employment, demand from the agricultural sector was seen as crucial to sustaining the demand for non-agricultural products and services, especially manufactured products. Second, since agricultural commodities constituted a significant share of input costs in some industries and of the wage basket in most, increases in agricultural prices were variously analyzed as affecting industrial production. In particular, if an industry was agro-based or was characterized by a tendency for money wages to rise with increases in the prices of wage goods, it would experience an increase in costs that may not be neutralized by an increase in final product prices. In the event, profits could be squeezed and manufacturing investment affected adversely. Third, increases in agricultural prices would constrain the growth of demand in the manufacturing sector, since consumers would allocate a larger share of their incomes to food consumption and a smaller share to manufactures demand, and the government may reduce public expenditure to reduce absorption and dampen price increases. This constraint on demand growth would also adversely affect the ability of firms in industries producing mass consumption goods to raise prices in order to cover higher costs.

These different ways in which agricultural performance was expected to affect non-agricultural growth were predicated on the operation of two transmission mechanisms. First, increases in non-agricultural growth were expected to result in increases in the direct (inputs) and indirect (wage goods) demand for agricultural products. Second, since, agricultural growth was seen as constrained from the supply side, any disproportionality in industrial and agricultural growth was expected to result in an abnormal increase in the prices of agricultural goods, since those

prices were largely determined by the relative levels of supply and demand.

Thus, the agrarian constraint on non-agricultural growth was a problem that needed to be addressed if non-agricultural growth had to be sustained. This was also a partial guarantee of some balance in the pattern of growth. An aspect of the above discussion which is of relevance is the understanding that this disproportionality was self-correcting. This was not just because price movements triggered changes in private investment allocation, as some have suggested. Rather, governments that initially responded to inflationary crises and/or balance of payments problems by curtailing expenditure soon sought to improve agricultural performance in order to revive non-agricultural and overall growth. That is, faced with inflationary crises governments in developing countries were forced to address the factors responsible for slow growth in agricultural output and productivity, which had agrarian distress as its concomitant. In fact, the adoption of Green Revolution strategies in many developing countries, including India, was a response to the overall impasse in development resulting from poor agricultural growth. Some combined this with programmes of land reform, while others did not. However, in most cases the problem was at least partially addressed, unless factors like political strife prevented such action.

What is interesting, therefore, is that this kind of response from the state was not forthcoming during the 1990s and after. Public capital formation in agriculture has fallen, extension services for farmers neglected and the subsidies provided on inputs trimmed. One reason for this was that tax incentives for private sector-led development combined with fiscal conservatism had limited the growth of government expenditures. The other was that of the amount of outlays by the government, less was going to the agricultural sector.

The fact that the self-correcting mechanism has not been operative during the 1990s and the first half of the 2000s, when the disproportionality in non-agricultural and

agricultural growth widened considerably, suggests that structurally the Indian economy has changed from a position where it was hampered by the agricultural bottleneck, which constituted a supply side constraint on growth to one where agriculture appears to be demand rather than supply constrained.⁹ This implies that non-agricultural growth could accelerate while agriculture was languishing, with no self-correcting mechanisms in sight.

There are many factors explaining this shift. One element of change in the environment of obvious relevance was the transformation of the world of international finance that, for the first time, provided “emerging markets”, like India, access to private international finance. It is now widely held that the Indian government exploited that opportunity during the 1980s to overcome the development impasse of the 1970s. Deficit-financed expenditure was used to accelerate non-agricultural growth, and the resulting disproportionality between non-agricultural and agricultural growth was managed by using imports financed largely with external debt to change the structure of domestic supplies and dampen inflation.

However, this alone does not constitute the full explanation. Rather, the change in economic regime instituted since the mid-1980s, and especially since 1991, has changed the pattern of growth in a way that has resulted in structural shifts in the nature of

intersectoral linkages. An obvious change in the pattern of growth, which allows for growing disproportionality between agricultural and industrial growth, is a change in the pattern of demand and production, involving a reduction in the direct agricultural-input dependence of the non-agricultural sector. As Sastry *et al.* (2003: 2392) have shown, the available input-output tables for the Indian economy indicate that: “In 1968-69 one unit of rise in industrial output was likely to enhance demand from agriculture by 0.247 units, which was reduced to 0.087 by 1993-94. On the other hand, in 1968-69, one unit rise in industry was to cause 0.237 units demand from the services sector, which increased to 0.457 units in 1993-94”.

Finally, the lack of responsiveness of non-agricultural employment growth to the growth in non-agricultural production meant that the demand for wage-goods associated with a given rate of non-agricultural growth was lower than it was earlier—an issue we examine below. Increasingly, agriculture was taking on the characteristics of a demand-constrained sector rather than a supply constrained sector. This too relaxed the agricultural constraint on non-agricultural growth.

An implication of the resulting “neglect” of agriculture was that, though it constituted a sink for the unemployed, the ability of the sector to provide remunerative employment of reasonable quality was substantially undermined.

6. TRADE LIBERALIZATION AND AGRICULTURE

Yet, the evidence suggests that instead of the government pursuing policies to correct for the imbalance between agricultural growth, the process of trade liberalization has been allowed to further damage agriculture (Ghosh 2005). Trade liberalization affecting Indian agriculture began in the early 1990s with the progressive reduction or removal of trade restrictions of various types. The rupee devaluation of mid-1991 was followed by the removal of export subsidies on agricultural commodities, such as tea and coffee, and the subsequent reduction of various other export subsidies. The process accelerated from the late 1990s, in tune with WTO agreements, and involved liberalization of export controls, quantitative controls on imports and decontrol of domestic trade. Quantitative restrictions on imports and export restrictions on groundnut oil, agricultural seeds, wheat and wheat products, butter, rice and pulses were all removed from April 2000. Almost all agricultural products are now allowed to be freely exported as per current trade policy.

This has been associated not only with the removal of quota control on imports, but also the reduction of import tariffs, except in certain cases (such as soya bean) where the

tariff levels have reached the bound levels. In any case, the optimism surrounding India's agricultural export prospects after the signing of the Uruguay Round agreement was such that for a range of important agricultural commodities, including rice wheat and oilseeds, the Indian trade negotiators had declared zero rates of tariff binding. After world trade prices of various crops started crashing from 1996 onward, the government of India was forced to renegotiate the bound tariff levels for as many as 15 agricultural items.

As Table 8 suggests, tariff rates for most agricultural commodities were low or zero in the early 1990s, largely because quantitative restrictions on imports rendered tariffs irrelevant and because world prices were substantially higher than Indian prices over that period. Subsequently, and especially after 2000, applied tariff rates have generally been coming down, and (except in the case of soya bean) have been significantly below the bound tariffs. What is possibly even more significant, however, is that applied tariff rates have been relatively stable despite tremendous volatility in world trade prices, so that Indian agriculturalists effectively had to deal with all the volatility of world prices.

Table 8. Import Tariff Rates for Selected Agricultural Commodities

	1991-92	1995-96	1999-2000	2000-01	2001-02	2002-03	Bound tariff
Non-basmati rice	0	0	0	92	77	70-80	70-80
Wheat	0	0	50	108	100	50	100
Maize	0	0	0	60	50	50	70
Pulses	10	10	5	5	5	10	104
Oilseeds	55	50	35	35	35		100
Soyabean oil	45	30	18	45	38	45	45
Groundnut oil	45	30	18	35	35	75	300
RBD palm oil				75	75	65	300
Refined palm oil				100	85	75-85	300
Cotton	35	50	40	25	35	5	
Sugar	35	0	40	100	60	60	150

Source: Ramesh Chand (2004) based on Government of India data.

Table 9. Domestic Support Provided to Agriculture.

Product specific support (as percent of value of output)			
	1990-91	1995-96	1999-2000
Rice	-71.66	-52.59	-52.52
Wheat	-64.67	-242.35	-8.56
Groundnut	-34.25	0	-139.96
Soyabean	-58.06	0	0
Cotton	-566.67	-422.88	-192.79
Jute	-94.7	-131.04	-36.36
Sugar	24.36	-198.27	41.39
Non-product specific support (as percent of value of output)			
	1990-91	1995-96	1999-2000
Irrigation	1.45	1.58	1.44
Credit	0.05	0.07	0.07
Fertilizer	0.92	2.08	2.47
Power	2.32	3.97	4.58
Seed	0.05	0	0
Total	4.73	7.7	8.57

Source: Calculations by G. S. Bhalla (2004)

This meant that even as the uncertainties related to international price movements became more directly significant for farmers, progressive trade liberalization and tariff reduction in these commodities made their market relations more problematic. Government policy did not adjust in ways that would make the transition easier or less volatile even in price terms. Thus, there was no evidence of any coordination between domestic price policy and the policies regarding external trade and tariffs. For example, an automatic and transparent policy of variable tariffs on both agricultural imports and exports linked to the deviation of spot international prices from their long-run desired domestic trends would have been extremely useful at least in protecting farmers from sudden surges of low-priced imports and consumers from export price surges. Such a policy would prevent delayed reactions to international price changes, which allow unnecessarily large private imports. It would therefore have allowed for some degree of price stability for both producers and consumers, which is important especially in dominantly rural economies like India.

In the absence of such minimal protection, Indian farmers had to operate in a highly uncertain and volatile international environment, effectively competing against highly subsidized large producers in the developed countries, where the average level of subsidy amounted to many times the total domestic cost of production for many crops. Also, the volatility of such prices - for example in cotton - has created uncertain and often misleading signals for farmers who respond by changing cropping patterns. It has directly affected cultivators of oilseeds such as soya bean and groundnut farmers due to palm oil imports. While there has been some diversification in crop production, the downside of this has been the reduction of production of traditional staple food grains and declining per capita availability of food (which is an indicator of per capita consumption) in rural areas (Patnaik 2004).

Meanwhile, other government policies had direct and indirect effects on agriculture. The most significant related to the efforts at reducing subsidies, which affected both agricultural producers and consumers, and the reduction of public expenditure which would

have benefited cultivation. Thus, both food and fertiliser subsidies were sought to be reduced over this period. However, both of these strategies, which involved raising the prices for consumers of both food and fertilisers, had undesirable and even counter-productive effects, leading to the paradoxical results of reducing consumption and simultaneously increasing subsidies.

As a consequence, domestic support to Indian farmers was sharply negative through the 1990s for most crops, and it was negligible in non-crop-specific terms, as shown in Table 9. In addition, throughout the 1990s and even subsequently, there have been attempts to raise other user charges of public services and utilities relevant for farmers, such as irrigation water charges, power (used to run pump sets for ground water extraction) and the like. While these measures are typically under the control of state governments, the fiscal crunch of such state governments (itself a reflection of neo-liberal taxation policies and curbs on state borrowing) and the general atmosphere of reducing subsidies led many state governments to increase various user charges, especially for power to agricultural consumers.

The impact of trade liberalization on farmers' welfare works through various channels such as volatile prices, problems in imports and exports, impact on livelihood and other employment opportunities, etc. For farmers, perhaps the single most adverse effect has been the combination of low prices and output volatility for cash crops. While output volatility increased especially with new seeds and other inputs, the prices of most non-food grain crops weakened, and some prices, such as those of cotton and oilseeds, plummeted for prolonged periods. This reflected not only domestic demand conditions but also the growing role played by international prices consequent upon greater integration with world markets in this sector. These features in turn were associated with growing material distress among cultivators.

Such exposure to global price volatility has been associated with a growing reliance on

private debt, because of the lack of extension of institutional credit, coupled with growing inability to meet debt service payments because of the combined volatility of crops and prices. This in turn has led to a loss of assets, including land, by the small peasantry. This has been so marked that the proportion of rural households without any land increased dramatically over the 1990s, and by 1999-2000 accounted for about 45 percent of rural households according to NSS data. The pervasive agrarian crisis has been most harshly illustrated by the increase in suicides by farmers, which amounted to more than 20,000 documented cases across India by the end of 2005.

While the falling viability of cultivation has been an important reason for this, the collapse of rural employment opportunities, especially in agriculture but also in non-agriculture, has also been a major factor in the pervasive agrarian distress. It is sometimes argued that the trade liberalization and lower import prices are good for consumers while they may be bad for producers. But this perception misses the basic point that there are no pure consumers who have no relationship to production. Rather, the ability to consume depends upon income, which in turn depends upon employment and livelihood opportunities. If these are reduced by a more open trade strategy and the real incomes of workers and peasants decline as a result, then even as consumers they cannot benefit from more plentiful or cheaper imported goods. Only the rich and those with secure jobs and incomes would benefit from this trade policy. For the vast majority of the citizens of this country, it could actually mean they lose livelihoods, such that they would not be able to purchase necessary goods even at lower prices.

It is the crisis confronting agriculture that has made the sector incapable of providing decent, gainful employment, transferring the role of ensuring adequate employment for the unemployed and underemployed in India's rural majority on the non-agricultural sectors. The question is: have these sectors played this role successfully?

7. TRADE LIBERALIZATION AND MANUFACTURING

Until recently, advocates of reform held that the Indian economy had been put on a new and higher growth trajectory led by manufacturing since the launch of the reforms in 1991. The evidence relating to registered manufacturing, however, is that the turn around in growth occurred much earlier, in the 1980s.

As Table 10 shows, the lead indicator of industrial performance, the Index of Industrial Production, suggests that after close to two decades of depressed growth, the trend rate of growth of manufacturing recovered to 6.2

percent during the decade starting in 1985-86. That rate of growth was indeed a significant improvement relative to the previous three decades, even if below that touched during the decade and a half immediately after the launch of planned development. However, the evidence points to a marginal deceleration in growth between the periods 1985/86 to 1994/95 and 1994/95 to 2002/03, even though the former includes the “adjustment years” in the early 1990s when growth was extremely low.¹⁰ It is only since 2003-04 that industrial growth has gathered steam again.

Table 10. Annual Trend Rates of Growth Based on IIP

	Total	Manf.	Min. & Qu.	Elect.
1950-51 to 64-65 (a)	7.2	7.1	5.9	13.6
1965-66 to 79-80 (b)	4.7	3.8	6.9	6.2
1965-66 to 74-75 (b)	4.3	2.7	9.4	3.8
1975-76 to 84-85 (c)	4.9	4.3	6.6	7.3
1985-86 to 94-95 (d)	6.2	6.2	4.2	8.3
1994-95 to 2009-10 (e)	6.41	6.87	3.24	5.14
1994-95 to 2002-03 (e)	5.78	6.22	2.40	5.45
2003-04 to 09-10 (e)	7.08	7.56	3.64	5.44

Source: Central Statistical Organization, Government of India

Notes:

a) Based on series with base 1950-51 = 100

b) Based on series with base 1970 = 100

c) Based on series with base 1970 = 100

d) Based on series with base 1980-81 = 100

e) Based on series with base 1993-94 = 100

What explains the recovery in industrial growth sometime during the 1980s, the persistence of such growth during a part of the 1990s and the acceleration more recently? The picture of growth during the 1980s is, of course, far easier to explain. Exploiting the access to foreign exchange afforded by the rise to dominance of finance internationally, the government chose to pump prime the system. Rising government expenditure, however, was not accompanied by an increase in resource mobilization through rising taxes. The fiscal stimulus was financed through rising deficits, including a rising deficit on the revenue account of the government's budget. The demand stimulus resulting from such expenditure was serviced by domestic industry with the help of imported capital goods, intermediates and raw

materials, imports of which were liberalized. This essentially meant that the import intensity of domestic production rose. But such growth was not constrained by inadequate access to foreign exchange, since it was accompanied by an increase in foreign borrowing from the International Monetary Fund (IMF), the international commercial banking system and non-resident Indians.

Fortunately for India, this was the time when remittances from Indian workers, especially in the Gulf, to sustain the consumption expenditures of families left behind in the country, provided the country with a fortuitous inflow of foreign exchange. Yet, India's foreign debt-to-GDP ratio doubled during the 1980s. It was when international creditors chose to

shut off such credit at the end of the 1980s that India ran into the balance of payments crisis of 1990-91, which provided the grounds for advocates of reform to push through an IMF-style stabilization and adjustment strategy (Patnaik and Chandrasekhar 1998 and Chandrasekhar and Ghosh 2005).

There were many lessons to be learnt from the 1980s experience. First, despite liberalization, however limited, given India's dimensions and its specific characteristics, growth depended on the fiscal stimulus that government expenditure provided, rather than on an expansion of exports. Second, if such government expenditure was not accompanied by tax and other measures aimed at mobilizing additional resources, but was financed through borrowing, the excess demand in the system was bound to spill over either in the form of inflation or a current account deficit. Third, if inflation was kept under control through enhancing supplies from the international market, borrowing to finance the resulting deficit on the current account would be inevitable. Fourth, if this process was accompanied by trade liberalization, the size of the current account deficit and the consequent level of external borrowing would be even higher, especially since there was a large pent-up demand for foreign goods or import-intensive domestically produced goods among the upper and upper-middle classes.

Underlying all of this was a more fundamental problem: the failure of the Indian State since Independence to redress the problem of asset concentration in both rural and urban India, and especially its failure to attack and undermine the monopoly over land. This had a number of implications. It meant that there emerged no large, autonomously growing market for industrial mass-consumption goods. It meant that the demand for manufactures was concentrated in a small section of the population driven by the desire for branded, import-intensive manufactures. And, it meant that, to the extent that the State chose to stimulate demand, it could not finance the necessary expenditures by taxing the surplus

of the rich who overwhelmingly commanded assets and investible resources in the system, and constituted thereby an economically strong lobby against such taxation.

Rather than understand this complex history, the IMF, the international financial interests it represents and the domestic advocates of reform who had internalized the IMF viewpoint chose to emphasize a partial reading of the problem. The 1990s crisis, it was argued, derived from three sources: an excessive presence of government both as a regulator and a participant in economic activity, which stifled private initiative; excessive government spending and a fiscal deficit that was too high; and inadequate reform that resulted in a situation where India's exports were not rising fast enough.

By framing the problem in this manner, the reform could focus on a chosen set of areas. It made curtailment of the fiscal deficit the fundamental task of fiscal policy. It accelerated trade liberalization, which involved doing away with quantitative restrictions on imports and reducing customs tariffs, with attendant revenue implications. It dismantled controls on the free operation of large industrial capital, domestic and foreign. It provided a host of direct and indirect tax concessions to industry, further reducing the tax base of the government. It provided a host of concessions to foreign investors in the hope that they would use India as a base for world market production.

One implication of this strategy was a significant reduction in the tax-to-GDP ratio at the centre. One striking feature of the period since 1989-90, which incorporates the years of accelerated economic reform is that despite evidence of high and accelerating growth rates and signs of growing inequality, there has been no improvement in the centre's ability to garner a larger share of resources to finance expenditures it considers crucial. Even when corporate profits and managerial salaries are reported to be rising sharply, taxes do not appear to be as buoyant. The central tax-to-GP ratios in India have been

declining for much of this period and have more recently recovered their relatively low late-1980s levels (Chart 10).

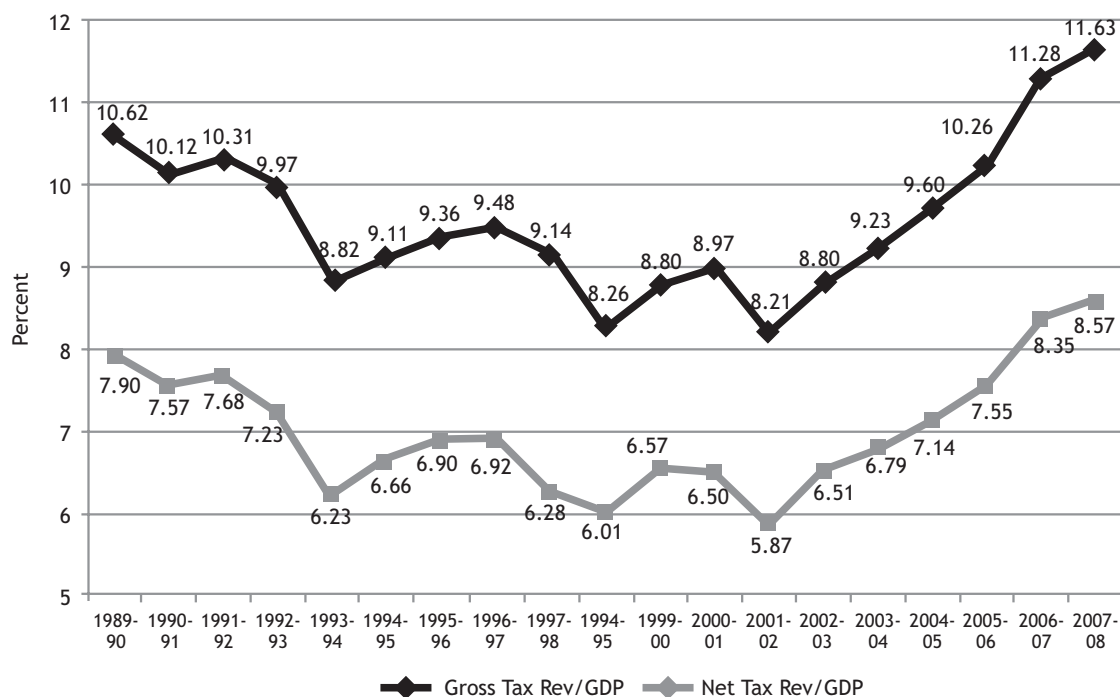
This failure to significantly improve the tax-to-GDP ratio, in a period when there has been a widening of the tax net through various means, is largely due to the tax concessions provided during the years of liberalization. While inequality increases, marginal tax rates have come down sharply during the liberalization years. In 1985-86, the marginal rate of taxes on personal income was brought down from 62 percent to 50 percent and the corporate tax rate from about 60 percent to 50 percent. In the budgets of the early 1990s, especially those of 1992-93 and 1994-95, the marginal rates were further reduced to 40 percent. Today, they stand at around 33 percent.

The tax-to-GDP ratio in India was also low by international standards, including those of many developing countries. The ratio of Central Government tax receipts to GDP was only 7.9 percent in 1989-90; by 2001-02 it had

fallen to a miserable 5.9 percent. Even if taxes levied by the state governments are included, the total tax-to-GDP ratio was still only 15.9 percent in 1989-90 and fell to 13.8 percent by 2001-02. This compared poorly with tax-to-GDP ratios in most developed and developing countries. India is by no means an over-taxed country, but it has much fiscal space to expand its revenues.

However, between 2001-02 and 2007-08 the tax-to-GDP ratio at the centre rose from 5.9 percent to 8.6 percent. The aggregate tax-GDP ratio of the Centre and the states rose even more sharply from 13.8 percent to 19.1 percent between 2001-02 and 2008-09. It must be noted that the period after 2002-03 was one in which profits in the organized sector rose sharply, the ratio of profits to value added also rose significantly, and saving and investment rates in the corporate sector recorded sharp increases. This was therefore a period when high growth was accompanied by significantly increased inequalities in the organized sector, leading to the rise in the tax-to-GDP ratio.

Figure 10. Trends in the Central Tax Revenue-to-GDP Ratio

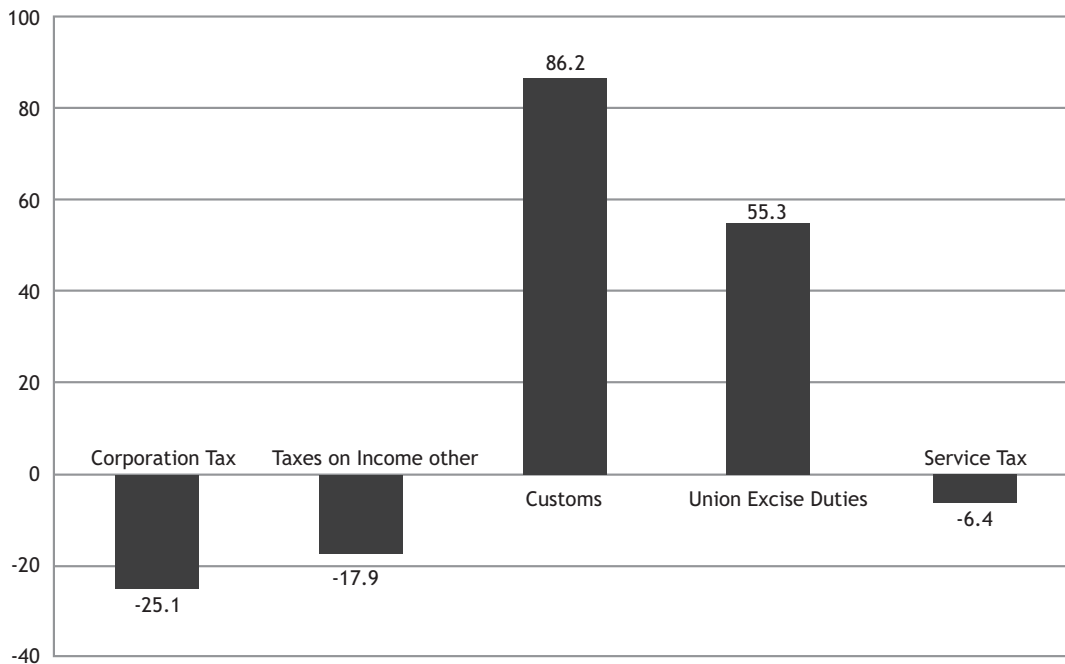


Source: Government of India, Ministry of Finance, Public Finances in India and CSO.

Not surprisingly, there has been a significant shift in the relative contribution of different components of taxes to the tax-to-GDP ratio at the centre over the years. Liberalization, involving reductions in customs tariffs and rationalization of the indirect tax regime, resulted in a decline in the tax-to-GDP ratio between 1989-90 and 2001-02. Customs and excise duties contributed 86 percent and 55 percent, respectively, to the decline in the central tax-to-GDP ratio during

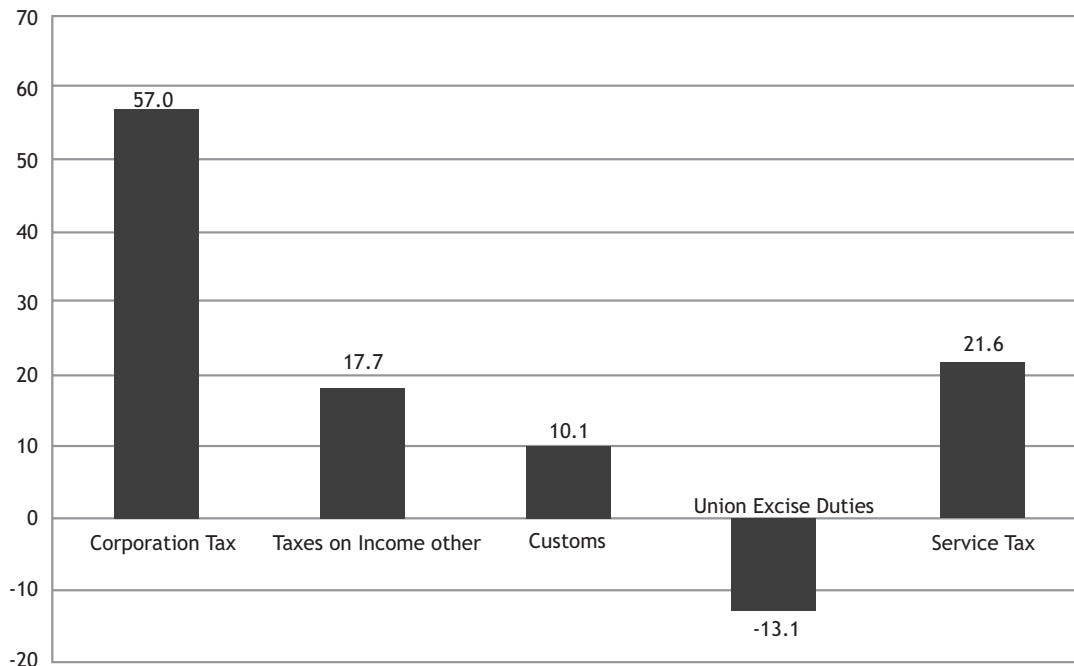
those years (Chart 11). However, subsequently corporate taxes, other income taxes and service taxes contributed 57 percent, 18 percent and 22 percent, respectively, to the increment in the central tax-to-GDP ratio between 2001-02 and 2007-08. Thus, higher tax collections from the industrial sector and better-off individuals and a widening of the tax net accounted for the improvement in the centre's revenue base (Chart 12).

Figure 11. Contribution to Decline in Tax-GDP Ratio 1989-90 to 2001-02 (%)



Source: Computed from figures obtained from Government of India, Ministry of Finance, Public Finances in India

Figure 12. Contribution to Increase in Tax-GDP Ratio 2001/02 to 2007/08 (%)

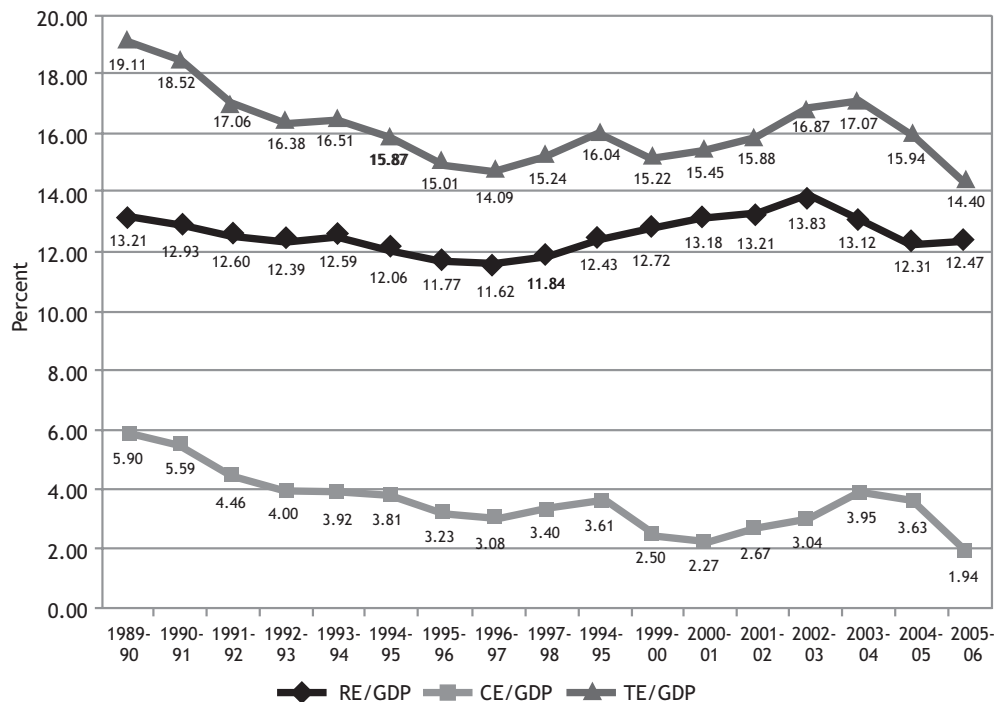


Source: Computed from figures obtained from Government of India, Ministry of Finance, Public Finances in India

However, the centre has indeed been strapped for resources to finance its expenditures. As Chart 19 shows, the ratio of central budgetary expenditures-to-GDP fell sharply between 1989-90 and 1996-97. While the ratio regained

some of the lost ground in the latter part of the 1990s and immediately thereafter, the decline resumed in 2003-04 and was at its lowest level since 1989-90 in 2005-06.

Figure 13. Trends in Expenditure-GDP Ratio



Source: Computed from figures obtained from Government of India, Ministry of Finance, Public Finances in India

Much of this is on account of the curtailment of capital expenditure. Revenue expenditures as a percentage of GDP, while fluctuating over time, have more or less retained their level across the period as a whole. Thus the fall in total expenditure relative to GDP has been largely on account of cuts in capital expenditure, which stood at less than 2 percent of GDP in 2005-06 compared with 6 percent in 1989-90.

What is noteworthy is that the decline in capital expenditure has been particularly sharp over the three years ending 2005-06, when the central tax-to-GDP ratio was on the rise. This was because these were the years when, armed with the Fiscal Responsibility and Budget Management (FRBM) Act, the government has been realizing its ambition to substantially curtail the fiscal deficit. With revenues not rising adequately and the fiscal deficit being curtailed significantly, expenditures had to be cut to fulfil the requirements of the FRBM Act, and the axe fell disproportionately on capital expenditures. This is why the government has

chosen to declare that investment and growth in the coming years will have to be driven by the private sector. Such fiscal compression implies that, unless exports provide an alternative stimulus to industrial growth, the basic tendency in the system would be one that involves a slowdown.

As noted earlier India's export performance under reform has been by no means exceptional. Occasional spurts in the dollar value of exports in general and manufactured exports in particular, do not constitute the basis for sustained growth. And post-reform export growth trends indicate that such spurts have indeed been the exception. Freer conditions and better terms for entry of foreign investors have not delivered the export thrust that had been expected - an issue that we turn to below. Add to this the fact that import liberalization does displace earlier sources of domestic production with imports or import-intensive products, and value addition in domestic industry is further eroded.

To summarize, the basic tendency in the system is for industrial growth to decelerate. This raises the question concerning the need to explain the persistence of a reasonably high, even if not remarkable, rate of industrial growth during the 1990s and the acceleration more recently. This can usefully focus on a seldom noted feature of manufacturing growth during the 1990s: an increase in volatility.

A closer look at the distribution of rates of growth in individual years is quite revealing. The 1980s, with the exception of two or three years, were characterized by rates of growth near or above the average. Growth rates at or above the average were far less frequent in the 1990s. The picture that emerges shows that, while in the 1980s industrial growth was on average high, the sharp recovery and boom in industrial growth during 1993-94, 1994-95 and 1995-96 was followed by a downturn in the period ended in 2002-03. Then there was a significant revival in growth rates until the recent downturn induced by the global crisis.

There are three factors that seem to explain instability. First, the evidence indicates that public expenditure was far more unstable in the 1990s, partly because of variations in the government's degree of adherence to its irrational fiscal deficit targets agreed with the IMF, partly because of a sudden burgeoning of public expenditure towards the end of the 1990s because of the implementation of the Vth Pay Commission's recommendations and partly because of the influence of the political business cycle, which results in a ramping up of public expenditures of certain kinds in the run up to an election.

The second factor explaining the instability in manufacturing growth is the fact that in the initial post-liberalization years, the sudden increase in access to domestically assembled or produced import-intensive manufactured goods resulted in the release of pent-up demand for such goods among sectors who had had the ability and the desire to consume such goods, but whose consumption of such commodities was limited by import regulation of both final products and intermediates

and components. Inasmuch as such pent-up demand is soon satiated, the spur to growth provided by this specific factor evaporated, resulting in a slowing of the growth rate pending an expansion of the market for such manufactures among a larger section of the population.

Finally, instability in the pace of manufacturing growth has resulted from the specific way in which that market for manufactures has been expanded, especially in urban India, during the years of neo-liberal reform, but especially since 2003-04, through a boom in housing and consumer credit. One consequence of financial liberalization and the excess liquidity in the system created by the inflow of foreign capital, has been the growing importance of credit provided to individuals for specific purposes, such as purchases of property, consumer durables and automobiles of various kinds. This implies a degree of dissaving on the part of individuals and households. It also implies that financial institutions, which are willing to provide such credit without any collateral, are betting on the inter-temporal income profile of these individuals, since they are seen as being in a position to meet their interest payment and amortisation commitments based on speculative projections of their earnings profile. These projections are speculative because with banks and other financial institutions competing with each other in the housing and consumer finance markets, individuals can easily take on excess debt from multiple sources, without revealing to any individual creditor their possible over-exposure to debt.

One implication of the expansion of the market for manufactures through these means is that the occurrence and the extent of such an expansion depend crucially on the "confidence" of both lenders and borrowers. Lenders need to be confident of the future ability of their clients to meet interest and repayment commitments. Borrowers (excluding those consciously involved in fraud) need to be confident of their ability to meet, in the future, the commitments that they are taking

on in the present. This crucial role of the “state of confidence” in triggering this form of demand is what is captured in the oft-used phrase “the feel good factor”. Since there is a strong speculative element involved in lenders providing credit and borrowers increasing their indebtedness, the state of confidence of both parties matters. When such confidence is “good,” we can experience growth or even a mini-boom. When such confidence is low, in the case of either borrowers or lenders, we can experience recessionary conditions. To the extent that financial liberalization provides the basis for an expansion of debt - mediated either through bank accounts or plastic cards -

a degree of volatility in manufactures demand is inevitable.

The role of these factors is partly corroborated by the pattern of manufacturing growth during the 1990s. As Table 11, providing rates of growth of sub-groups based on the use-based classification of the IIP indicates, a major source of growth has been the contribution made by the consumer goods sector. Moreover, even though its low weight makes its contribution to aggregate manufacturing growth less significant, the growth performance of the consumer durables sector has been the best.

Table 11: IIP-Based Rates of Growth of Manufacturing Production (Use-based Classification): 1994-95 to 2004-05

	Growth Rate	Contribution
Basic Goods	4.49%	1.59%
Capital Goods	6.92%	0.67%
Intermediate Goods	6.39%	1.69%
Consumer Goods	6.45%	1.83%
Durables	9.16%	0.47%
Non-Durable	5.65%	1.31%
General	5.83%	5.83%

Source: Computed from Index of Industrial Production data released by the CSO.

Implicit in these explanations of growth is the understanding that exports triggered by the effects of liberalization are not an important source of growth, even if it has played a role in specific industries. The growth performance of the 17 major industry groups shows that growth was unevenly distributed across the manufacturing sector, with 7 of these 17 groups characterized by growth rates significantly above the manufacturing average,

3 by rates close to the average and 8 by rates well below the average (Table 12). Indeed, in a couple of the industry groups growing at or above the average rate, such as leather and leather and fur products and basic chemicals and chemical products (except products of petroleum and coal), export growth has been creditable. But, exports do not constitute even a partial explanation for growth of most of the better performing industry groups.

Table 12: IIP-Based growth in seventeen major industry groups (1994-95 to 2003-04)

	Growth Rate	Contribution
Food products	3.60%	0.41%
Beverages, tobacco and related products	12.70%	0.38%
Cotton textiles	1.47%	0.10%
Wool, silk and man-made fibre textiles	8.33%	0.24%
Jute and other vegetable fibre textiles (except cotton)	0.59%	0.00%
Textile products (including wearing apparel)	5.50%	0.18%
Wood and wood products; furniture & fixtures	-4.53%	-0.15%
Paper and paper products and printing, publishing and allied industries	6.17%	0.21%

Table 12. *Continued*

	Growth Rate	Contribution
Leather and leather & fur products	6.76%	0.10%
Basic chemicals and chemical products (except products of petroleum & coal)	7.83%	1.38%
Rubber, plastic, petroleum and coal products	6.56%	0.47%
Non-metallic mineral products	9.00%	0.50%
Basic metal and alloy industries	4.36%	0.41%
Metal products and parts (except machinery and equipment)	5.27%	0.19%
Machinery and equipment other than transport equipment	7.19%	0.87%
Transport equipment and parts	8.95%	0.45%
Other manufacturing industries	3.86%	0.12%
Manufacturing (Total)	6.14%	6.14%

Source: *Computed from Index of Industrial Production data released by the CSO.*

An important implication of debt-financed manufacturing demand is that it is inevitably concentrated in the first instance in a narrow range of commodities that are the targets of personal finance. Commodities vary from construction materials to automobiles and consumer durables. However, their importance in terms of contribution to growth is corroborated tangentially because of the nature of aggregation, by the data provided in Table 12. To the extent that these commodities are capital and import intensive in nature, the domestic employment and linkage effects of this expansion would be limited. Not only would employment growth be limited, as has been the case, but sustaining the growth process would require generating more of the same kind of demand. Manufacturing growth would become increasingly dependent on speculative factors.

It hardly bears stating that a large share of the commodities for which demand is triggered by credit are both capital and import intensive in character. There are a number of other reasons manufacturing outputs sucked out by a credit boom tend to have these characteristics. First, the liberalization of policy with respect to foreign direct investment has meant that much of the credit-financed, “new” market for manufactures is catered to by transnationals, endowing these products with a greater degree

of import and capital intensity. This tendency has been helped along by the fact that those favoured with credit fall in the middle classes, which too is characterized by a pent-up demand for “foreign” goods that could not be satiated earlier, not just because of protection, but also because they lacked the means (including credit) to acquire these commodities rapidly. A second reason domestic linkage and employment effects would tend to be low is that a combination of import competition, the induction of larger firms into the small-scale sector through the redefinition of “small” and “dereservation” of areas of production has undermined the ability of smaller firms to service certain markets. Finally, with end of the era of development banking in general and directed credit in particular, the possibility of such firms obtaining the finance to emerge and survive has declined.

The net effect of all these has been a set of disconcerting trends. To start with, despite claims to the contrary by the government, manufacturing growth performance during the 1990s and more recently has been worse than in the 1980s. As mentioned earlier, not only has the trend rate of growth tended to be at best similar to that observed in the 1980s, but also the pace of manufacturing growth has tended to be extremely volatile with creditable growth rates being concentrated in one- or

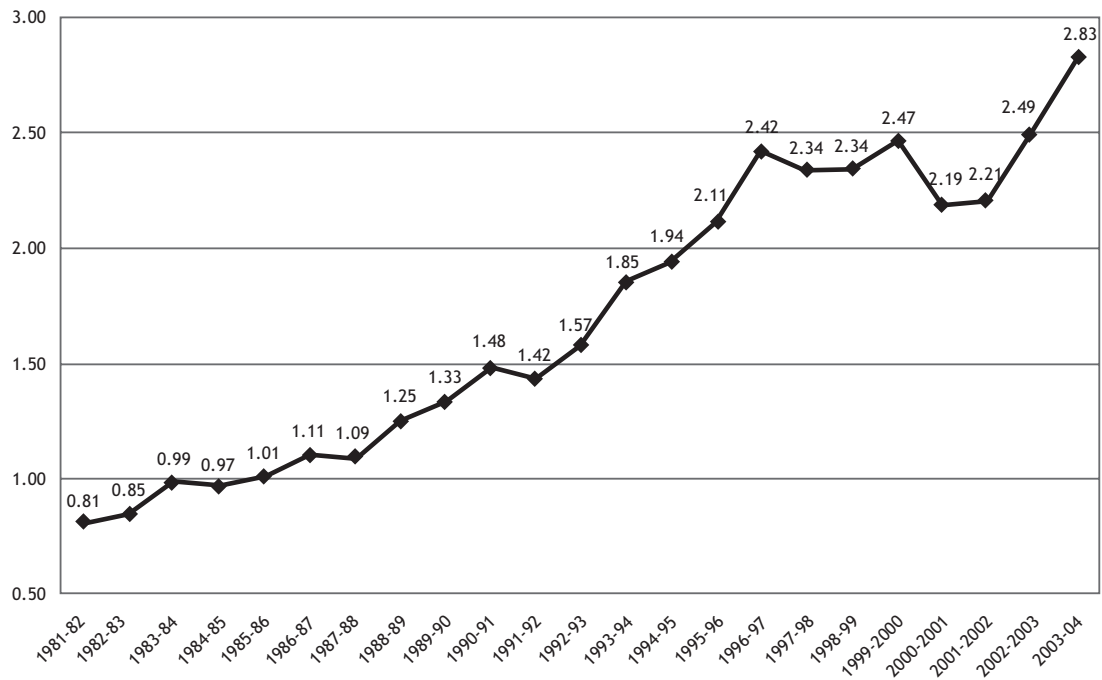
two-year periods separated by slow growth and recessionary conditions. Second, there are some signs of the “hollowing of the middle” in Indian industry, with growth occurring in the very large-scale sector, while medium- and small-scale industry has witnessed slow growth and high rates of mortality because of competition from imports or import-intensive “domestic” products, a recessionary environment, waning state support and inadequate credit access at times of distress. The small-scale sector that tends to persist is that which caters to the ancillarization needs of large firms, to niche markets and to low margin markets that persist because of low per capita income and high poverty. Third, there are clear signs of consolidation within the large industrial sector, in which foreign firms encouraged by liberalization of rules governing foreign direct investment, play a major part. Since these firms invest and expand in India to cater to domestic and not export markets and since they are characterized by large outflows on account of intermediate imports, royalty payments and profit repatriation, their growing presence not only limits the manoeuvrability of the government when it comes to industrial policy, but also has adverse balance of payments implications in the form of a rising trade deficit that encourages dependence on purely financial flows to help finance that deficit. Finally, the most disconcerting feature of industrial development during the 1990s is the lack of any contribution of output growth in the organized sector to employment growth. In fact, there appears to be a negative relation between output and employment growth. While it is known that the manufacturing sector tends to be far less labour absorbing than agriculture or services, this feature of growth in organized industry is extremely disturbing and needs to be corrected.

As Patnaik (2006) notes, there are reasons to believe that the pattern of manufacturing growth under an open economic regime is such

that the responsiveness of employment growth to the growth in output tends to decline. Thus, the combination of high output growth and low employment growth is a feature characterizing both India and China during the years when their economies were opened to trade and investment. This makes sense since (i) with tastes and preferences of the elite in developing countries being influenced by the “demonstration effect” of lifestyles in the developed countries, new products and processes introduced in the latter very quickly find their way to the developing countries when their economies are open, and (ii) technological progress in the form of new products and processes in the developed countries is inevitably associated with an increase in labour productivity. Hence, after trade liberalization, labour productivity growth in developing countries is exogenously given and tends to be higher than prior to trade liberalization, leading to a growing divergence between output and employment growth.

These expectations are corroborated by evidence related to India’s factory sector. One striking feature of the organized manufacturing sector during the years of liberalization has been a sharp and persistent increase in labour productivity as measured by the net value added (at constant prices) generated per worker. As Chart 14 shows, labour productivity tripled between 1981-82 and 1996-97, stagnated and even slightly declined during the years of the industrial slowdown that set in thereafter. It has once again been rising sharply in the early years of this decade. However, the benefits of this labour productivity increase went largely to those deriving rent, interest and profit incomes, rather than workers. The share of wages in value added, which was stable through much of the 1980s (Chart 15), declined almost consistently in the period from the late 1980s until 1996-97 and then after a period of stability fell sharply to touch less than half its mid 1990s level.

Figure 14. Value Added Per Worker

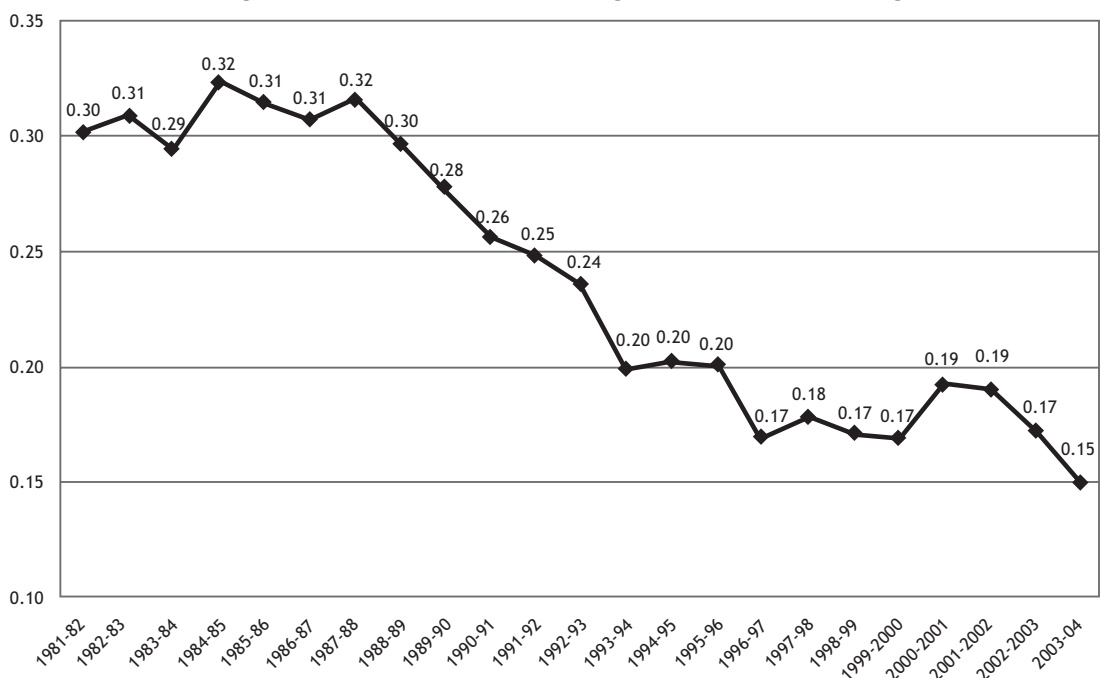


Source: Central Statistical Organisation, Annual Survey of Industries data deflated by GDP deflator for manufacturing. Data available at www.mospi.nic.in.

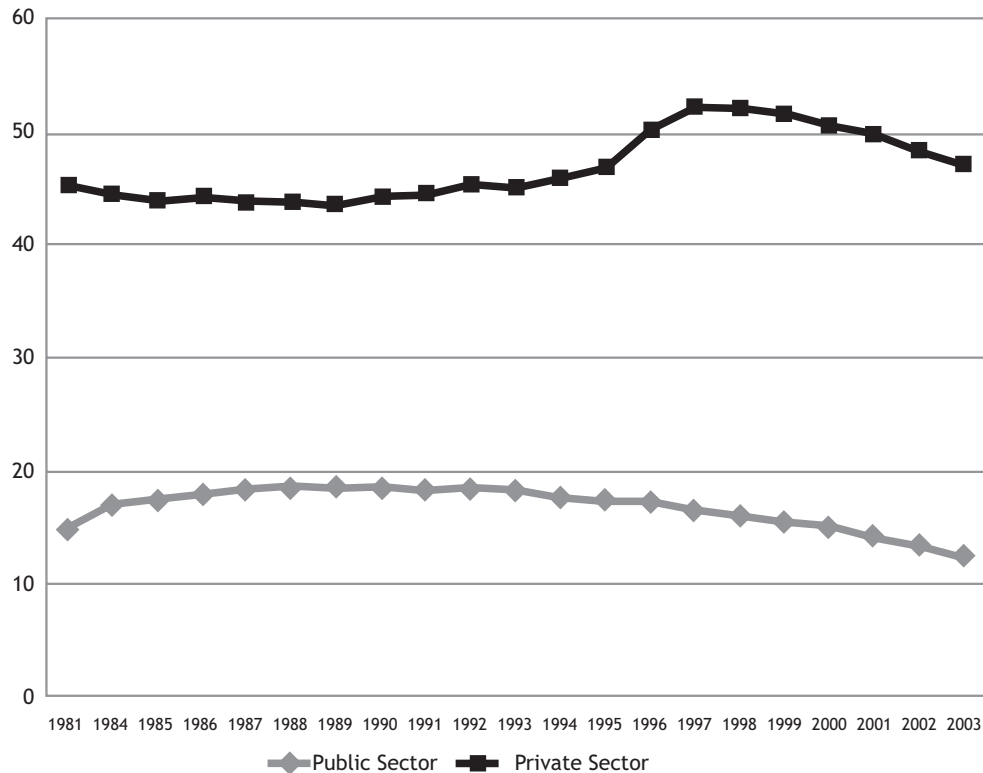
This was the result of two developments. The restructuring of the public sector has meant that public sector manufacturing employment, which was rising during the 1980s (Chart 16), was on the decline during the years of liberalization and fell particularly sharply after 1997. Private organized manufacturing employment, which was stagnant during the 1980s, rose marginally

during the early 1990s and particularly sharply during 1995-97, after which it has declined to return to its mid-1990s level by 2003. In the event, aggregate (public and private) organized manufacturing employment rose from 6.1 million in 1981 to 6.4 million in 1994 and 6.9 million in 1997, and then declined sharply to 6 million in 2003.

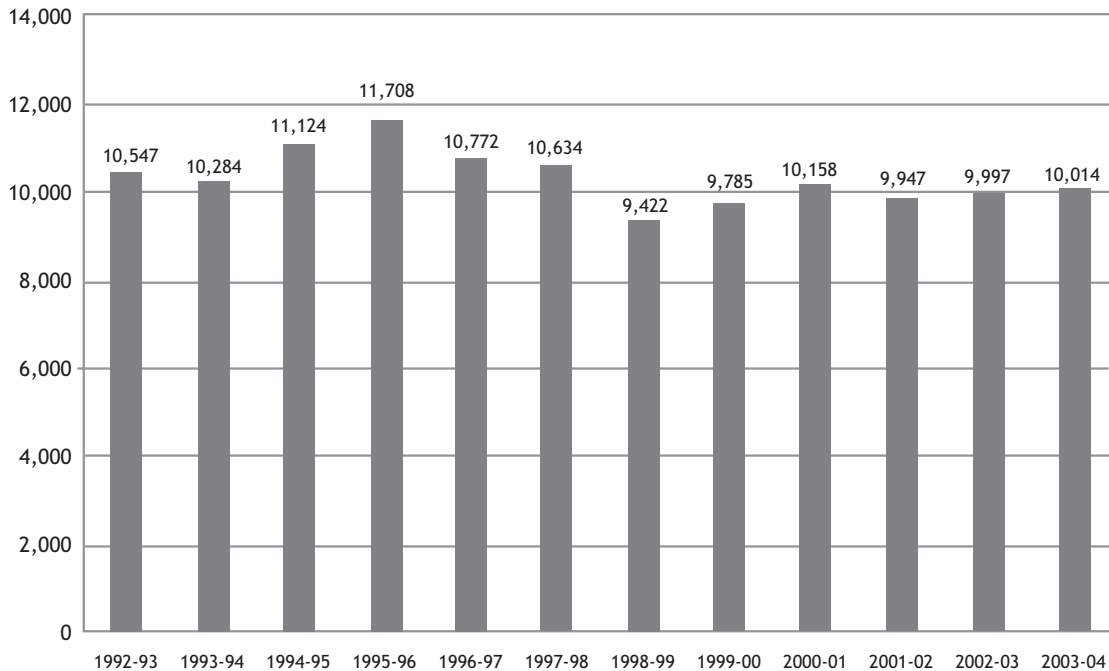
Figure 15. Ratio of Wages to Net Value Added in Organized Manufacturing



Source: Central Statistical Organisation, Annual Survey of Industries data available at www.mospi.nic.in.

Figure 16. Organized Sector Employment

Source: Ministry of Finance, Economic Survey, Various issues.

Figure 17. Average Annual Real Wage Per Worker: Organised Manufacturing

Source: Central Statistical Organisation, Annual Survey of Industries data deflated by CPI for industrial workers.

The second development of significance is that the average real wage of workers in the organized manufacturing sector has been more or less constant right through the 1990s (Chart 17). Together, these have ensured that the benefits of

the rise in labour productivity have largely gone to the surplus earners in the sector, who have been the main beneficiaries in the organized manufacturing sectors of the policies of liberalization in general and trade liberalization in particular.

8. THE ROLE OF SERVICES

This argument is, however, not a complete explanation for this divergence in the case of India because of the dominance of services in total growth noted earlier. Given the technological trajectory, it should be expected that the potential for increases in productivity is far greater in industry than in services. Hence, when services dominate growth the expectation is that employment growth would be more responsive to output growth

The reasons this is not so emerges from an analysis of the software and information technology (IT)-enabled services sector, which is one of the leading segments in the post-liberalization growth of modern services in the country. In absolute and relative terms the size of the IT sector in India is now impressive. The National Association of Software and Service Companies (NASSCOM) estimates¹¹ the size of the industry in 2005-06 at USD 36.3 billion, of which USD 29.5 billion consisted of revenues

from software and services. As much as USD 23.4 billion of these were export revenues: comprising USD 17.1 billion software and services export revenues and USD 6.3 billion of revenues from exports of IT-enabled services and business process outsourcing (BPO).

The Central Statistical Organisation (Government of India 2010) has estimated that the share of Information Communications Technology (ICT) services in total GDP has increased from 3 percent in 2000-01 to 6 percent in 2007-08. ICT services dominate the ICT industry as a whole accounting for 90 percent of GDP. Moreover, ICT services have increased their share in service sector GDP from 6 percent in 2000-01 to 10 percent in 2007-08. All this makes ICT services an important segment of the non-agricultural sector and gives rise to the impression that modern and more productive services are responsible for the dynamism of services and its contribution to GDP growth.

Table 13. Employment Indicators 2004-05 (millions)

Estimated total workers (principal usual status)	416.92
Estimated non-agricultural workforce (principal usual status)	189.13
Estimated workers in textile industry (principal usual status)	8.84
IT and enabled services sector employment (principal usual status)	0.88

Source: NSSO 2001 and 2006.

However, the sector's contribution to employment does not compare with its role in the generation of income and foreign exchange. According to the surveys of employment and unemployment conducted by the NSSO (2001 and 2006), employment in computer-related services rose from 2,70,150 in 1999-00 to 8,84,080 in 2004-05.¹² As the figures in Table 13 indicate, in 2004-05, relative to the current weekly status estimates of employment yielded by the NSS (2006) survey on employment and unemployment, employment in India's IT sector amounted to just 0.7 percent of the non-agricultural workforce in the country, 10 percent of employment in the production of textile products and 0.21 percent of the aggregate workforce. The fact that a sector with revenues

amounting to 4.5 percent of GDP contributes only 0.21 percent of aggregate employment is indicative of the lack of responsiveness of employment growth to growth in revenues.

To explain this we need to turn to the fact that the domestic industry has turned out to be a multi-layered, heterogeneous formation, with firms operating in different hardware, software and services segments, characterized by extremely wide margins. At the top are the successful firms, focusing on the export market for software and IT-enabled services, especially the former. At the bottom are the large numbers of independent assemblers who find their margins depressed by falling duties on imported systems and components.

A study of 65 small and medium enterprises in the IT sector (Shirsat 2006), with revenues ranging from INR 100 million to INR 2 billion, found that their revenues in 2005-06 amounted to just 8.9 percent of the revenue garnered by the top four IT firms (TCS, Wipro, Infosys Technologies and Satyam Computer). Their profits aggregated INR 5.8 billion or 6.9 percent of the INR 84 billion earned by the top four.

This skewed distribution explains the “winner-takes-all” scenario in the industry, showcased by a few highly successful firms with skyrocketing

stock values and billionaire owners, while the fact that the experience of a majority of firms in the sector does not match this scenario goes unnoticed. Extreme concentration with attendant implications for income inequality is a core feature of the industry. And underlying that inequality is a sharp divergence in employment and “output” growth rates.

The net result has been that despite the rapid growth of services in the Indian economy, employment growth has failed to respond significantly to output growth.

9. THE CRISIS AND ITS IMPACT

It is against this background that one needs to assess the impact of the Global Financial Crisis and post-crisis recovery on employment in India.¹³ It is clear now that while the crisis did impact growth adversely, India is one of the countries where enhanced public spending and a quick return of foreign capital that initially flowed out have ensured an early and quite robust recovery. But that recovery has many of the features that made the earlier growth strategy inadequate from the point of view of ensuring adequate employment growth.

In the immediate aftermath of the global crisis, the Indian economy experienced a downturn. Industrial growth faltered while inflation remained at double-digit levels; the current account deficit widened; foreign exchange reserves were depleting; the rupee depreciated and the benchmark stock exchange index (the Sensex or Bombay stock exchange sensitive index) crashed.

Given the greater integration through trade of the Indian with the world economy after 1991, it was only to be expected that the global slowdown would directly affect exports and economic activity in India. Merchandise trade was the first to be affected. Merchandise exports in October-December 2008 were more than 10 percent lower than their value a year earlier. Import values on the other hand continued to increase, albeit at a slower rate, because of falling world oil prices. As a result, the trade deficit for the period from October to December 2008 widened to USD 36.3 billion, 40 percent higher than a year earlier and estimated to be as much as 12.6 percent of GDP (calculated from data in RBI 2009a).

To some extent the implications of the widening trade deficit were mitigated by the neutralizing effects of exports of services and remittance inflows, which continued to increase in this period. Therefore, the current account deficit was significantly lower than the trade deficit, but even so it increased to 5.1 percent of GDP for October-December 2008, more than double

the ratio for the same months in the previous year (Reserve Bank of India, 2009a and Central Statistical Organisation 2009).

A lag in the effects of the global crisis on net services exports from India was to be expected, given that contracts in software and BPO services are typically signed for long periods, such as two to three years. However, by early 2009 it was evident that these lags had been covered, as several software and IT services firms in India predicted lower revenue growth, cut back on recruitment and even started laying off workers.

9.1 Capital Inflows and the Financial Sector

Employment declines in the non-export sectors suggest that the route by which the effects of the international crisis were being transmitted went beyond just external trade. One obvious alternative route was the effect of the crisis on cross-border capital flows, which had shown a dramatic increase in the preceding boom. Foreign investment flows rose sharply from USD 4.9 billion in 1995-96 to USD 29.2 billion in 2006-07 and then more than doubled to USD 61.8 billion in 2007-08 (Reserve Bank of India, 2009b). In 2007-08, capital inflows into India amounted to over 9 percent of GDP even though the current account deficit of the balance of payments stood at just 1.5 percent of GDP (Subbarao, 2009).

This occurred even as capital was fleeing other Asian emerging markets: net equity investment into Asian emerging markets (China, India, Indonesia, Malaysia, Philippines, South Korea and Thailand) fell from USD 122.6 billion in 2006 to USD 57.9 billion in 2008 (Institute for International Finance, 2009). This suggests that India was serving as a hedge for financial investors when uncertainties were engulfing emerging markets elsewhere in Asia and the world.

Capital inflows rose also due to large increases in commercial borrowing by private sector

firms. As constraints on external commercial borrowing by domestic companies were relaxed and because interest rates ruled higher in the domestic market, large Indian firms at the margin took the syndicated loan route to borrow money abroad at relatively lower interest rates. They engaged in a version of the carry trade, borrowing money in foreign exchange from the international markets where interest rates were lower and making investments in India (in addition to leveraging investments and acquisitions abroad). Net external borrowing by India rose from USD 24.5 billion in 2006-07 to USD 41.9 billion in 2007-08, with the bulk of the increase in the form of short-term borrowing. The stock of India's liabilities in the form of debt securities, trade credits and loans rose from USD 105.1 billion at the end of June 2006 to USD 175.6 billion at the end of September 2008 (Reserve Bank of India, 2009a).

Dependence on portfolio equity and debt inflows of this magnitude meant that if any internal or external development was seen to warrant pulling out of India, the exit could be as strong as the earlier inflow of foreign capital. The outbreak of the global crisis resulted in a sharp outflow of capital, especially portfolio capital brought into the stock market by foreign institutional investors (FIIs). Needing cash to meet commitments and cover losses at home, these FIIs sold out in Indian markets and repatriated capital abroad - the net outflow amounted to as much as USD 56 billion in the period April-December 2008 (Reserve Bank of India, 2009a).

By October-December 2008 the entire capital account turned negative, with a deficit amounting to an estimated 1.3 percent of GDP. While this was mainly due to net outflows under portfolio investment, banking capital and short-term trade credit, there were also falls in foreign direct investment and external commercial borrowings inflows. Even inflows under short-term trade credit declined. This led to an overall balance of payments deficit for that three-month period of as much as 6.2 percent of GDP.

One consequence of the capital outflow was a collapse of India's stock markets, just as the earlier capital inflows had triggered a speculative bubble in both stock and real estate markets. They had caused an unprecedented rate of asset price inflation in India's stock markets and substantially increased volatility. FII investments were an important force, even if not always the only one, driving markets to unprecedented highs, with a high degree of correlation between cumulative FII investments and the level of the Bombay Stock Exchange (BSE)'s Sensitive Index (Sensex). Another consequence of the outflow of capital was a sharp depreciation of the rupee, by more than 30 percent vis-à-vis the US dollar in the year to March 2009, taking the currency's value to more than INR 51 per dollar.

9.2 The Crisis and Credit-Financed Demand

A third way integration has influenced the way in which the global crisis has affected India is its impact on the role played by credit in financing private consumption and investment. Internal financial liberalization in India had resulted in a process of institutional change in which the role played by state-owned financial institutions and banks was substantially altered. As regulatory structures for private banks were dismantled over the 1990s, and private banks cornered the most lucrative clients, even public sector banks had to alter their strategies to seek new sources of finance, new activities and new avenues for investments, so that they could shore up their interest incomes as well as revenues from various fee-based activities. So banks linked up with insurance companies and entered other "sensitive" markets, like the stock and real estate markets. This led to a relatively rapid transformation of banking in India, with growing exposure of commercial banks to the retail credit market with no or poor collateral, the associated accumulation of loans of doubtful quality in their portfolios and a growing tendency to securitize personal loans.

Total bank credit grew at a scorching pace from 2005 onward, at more than double the rate of increase of nominal GDP. As a result, the ratio of outstanding bank credit to GDP (which had declined in the initial post-liberalization years from 30.2 percent at the end of March 1991 to 27.3 percent at the end of March 1997) doubled over the next decade to reach about 60 percent by the end of March 2008. Thus, one consequence of financial liberalization was an increase in credit dependence in the Indian economy, a characteristic imported from developed countries, such as the United States of America. This increase in credit could appear to be positive inasmuch as it reflected a greater willingness on the part of banks to lend: the growth in credit out-performed the growth in deposits, resulting in an increase in the overall credit-deposit ratio from 55.9 percent at end March 2004 to 72.5 percent at end March 2008. This increase was accompanied by a corresponding drop in the investment-deposit ratio, from 51.7 percent to 36.2 percent, which indicates that banks were shifting away from their earlier conservative preference to invest in safe government securities in excess of what was required under the statutory liquidity ratio (SLR) norm. (Data in this and the subsequent four paragraphs are from CFSA 2009.)

However, rapid credit growth meant that banks were relying on short-term funds to lend long. From 2001 there was a steady rise in the proportion of short-term deposits with the banks, with the ratio of short-term deposits (maturing up to one year) increasing from 33.2 percent in March 2001 to 43.6 percent in March 2008. At the same time, the proportion of term loans maturing after five years increased from 9.3 percent to 16.5 percent. While this delivered increased profits, the rising asset-liability mismatch increased the liquidity risk faced by banks.

These changes do not appear to have been driven by the commercial banking sector's desire to provide more credit to the productive

sectors of the economy. Instead, retail loans became the prime drivers of credit growth. The result was a sharp increase in the retail exposure of the banking system, with overall personal loans increasing from slightly more than 8 percent of total non-food credit in 2004 to close to 25 percent by 2008. Of the components of retail credit, the growth in housing loans was the highest in most years.

This rapid increase in credit and retail exposure, with inadequate or poor collateral, would have brought more tenuous borrowers into the bank credit universe. A significant (but as yet unknown) proportion of this could be "sub-prime" lending. According to one estimate, by November 2007 there was a little more than INR 400 billion of credit that was of sub-prime quality, defaults on which could erode the capital base of the banks.

These changes in the financial sector point to two further ways in which the global crisis would have affected India. First, the credit stringency generated by the exodus of capital from the country and the uncertainties generated by the threat of default of retail loans that now constitute a high proportion of total advances could freeze up retail credit and curtail demand, as happened in the developed industrial countries. Second, individuals and households burdened with past debt and/or uncertain about their employment would prefer to postpone purchases and not take on additional interest and amortization payment commitments. Thus, the off-take of credit can shrink even if credit is available, resulting in a fall in credit financed consumption and investment demand. Since growth in a number of areas, such as the housing sector, automobiles and consumer durables had been driven by credit-financed purchases encouraged by easy liquidity and low interest rates this would immediately affect the demand for housing, automobiles and durables. This, in turn would have second-order effects in terms of contracting demand for other sectors and economic activities.

9.3 Impact on Employment

By early 2009 the adverse employment effects of the merchandise export decline were evident despite the absence of large survey data on employment. Official surveys indicated rapid and accelerating job losses in sectors such as textiles and garments, metals and metal products, automobiles, gems and jewellery, construction, transport and the IT/BPO industry (Labour Bureau, Ministry of Labour and Employment, Government of India 2009). While employment declines were predictably higher in the export-oriented sectors, it is noteworthy that these surveys found growing job losses in activities that cater dominantly to the domestic market as well. In addition to quantity adjustment in the labour market, workers' incomes were also hit, with reports of falling real - and sometimes even nominal - wages of workers in industry and services as well as reduced incomes of self-employed workers who constituted more than half the work force by 2005 (NCEUS 2008). Agriculturalists, especially those producing export crops whose prices had collapsed, faced growing difficulties on top of their existing financial problems, reflecting rising input costs and large burdens of debt. Meanwhile, liquidity trap conditions were evident as "secure" borrowers were unwilling to invest because of greater uncertainty. Small-scale producers in all sectors were squeezed by the pincer movement of falling demand and the credit crunch as even informal sources of credit dried up. Since these producers account for the bulk of employment in manufacturing and services and typically hire workers on informal casual contracts, their economic difficulties translate directly into reduced employment. Surveys of home-based workers reported rapidly declining orders and falling piece rate wages even in nominal terms, for work that formed part of wider production chains for both domestic and export markets (AIDWA 2009).

Two other effects of the crisis on general living conditions deserve to be noted. First, the state governments - who in India's federal system are directly responsible for much of the public

expenditure that directly affects citizens, such as on health, education, sanitation and infrastructure - found their tax receipts falling below projections due to the downswing. Since they face hard budget constraints and many of them are subject to stringent fiscal responsibility conditions forced on them by the central government, this constrained their expenditure and reduced essential spending on basic services, not to mention development. Second, while aggregate inflation rates had been near zero for the year April 2008 - March 2009, the prices of food and essential medicines continued to increase, even as unemployment increased, wage incomes stagnated or fell and cash crop producers faced falling prices.

9.4 The Response and the Recovery

The Indian government's response to the downturn went through three stages. When the financial crisis erupted in a comprehensive manner on Wall Street, government spokespersons argued that India would be relatively immune to this crisis, because of the strong fundamentals of the economy and the fact that India's banks were well capitalized and well regulated. Growth, it was argued, would slip marginally and the stock market may experience some volatility, but the economic health of the country was essentially robust.

The initial signs of a change in the government's position came when the exodus of FII investments began. In this uncertain environment, banks and financial institutions concerned about their balance sheets, cut back on credit. This uncertainty affected lending not just to the corporate sector, but also to other areas, such as the housing, automobile and individual retail credit markets. According to RBI figures (reported by the Business Standard, 17 October 2008), the rate of growth of auto loans fell from close to 30 percent over the year ending June 30, 2008 to as low as 1.2 percent. Loans to finance consumer durables purchases fell from around INR 6,000 crore in the year to June 2007, to a little over INR 4,000 crore up to June 2008. Direct housing loans, which

had increased by 25 percent during 2006-07, decelerated to 11 percent growth in 2007-08 and 12 percent over the year ending June 2008. It is only in an area like credit-card receivables, where banks are unable to control the growth of credit that expansion was, at 43 percent, quite high over the year ending June 2008, even though it was lower than the 50 percent recorded over the previous year.

The government's response to these developments was to declare that the country was faced with a liquidity and credit crunch, necessitating a reduction in the cash reserve and statutory liquidity ratios to pump liquidity into the system and a cut in interest (repo) rates at which banks could access funds from the central bank.

Finally, the government acknowledged that India too was threatened with recession because of the global crisis. It, therefore, combined the huge increase in expenditures warranted by the need to implement the recommendations of the VIth Pay Commission for government employees with a host of other stimulus measures. The stimulus together with the quick reversal of capital outflows ensured that India came out of the crisis relatively quickly.

Interestingly, the recovery first occurred in the stock market. From its March 9, 2009 level of 8,160, the Sensex soared and doubled by end 2009. There are two noteworthy features of this surge in the index. First, it occurred when the aftermath of the global crisis was still being felt and the search for "green shoots and leaves" of recovery in the real economy was still on. Real fundamentals do not seem to have warranted this remarkable recovery. Second, the speed with which this rise was delivered was dramatic even compared with the boom years that preceded the 2008-09 crisis. The last time the Sensex moved between exactly similar positions, it took a year and ten months to rise from the 8,000-plus level in early 2005 to the 16,000-plus level in late 2007. This time it traversed the same distance in just six months.

With firms just looking to exit from a recessionary phase, this rapid rise in stock prices cannot be

justified by movements in sales and profits. This implies that the bull run can be explained only as the result of a speculative surge that recreated the very conditions that led to the collapse of the Sensex. This surge appears to have followed a two-stage process. In the first, investors who had held back or withdrawn from the market during the slump appear to have seen India as a good bet once expectations of a global recovery had set in. This triggered a flow of capital that set the Sensex rising. Second, given the search for investment avenues in a world once again awash with liquidity, this initial spurt in the index appears to have attracted more capital, triggering the current speculative boom in the market.

While these are possible proximate explanations of the transition from slump to boom, they in turn need explaining. In doing so, we have to take account of the fact that, as in the past, foreign investors have dominated stock market transactions and had an important role in triggering the stock market boom. As compared with the net sales of equity to the tune of USD 11.97 billion by foreign institutional investors during crisis year 2008, they had made net purchases of equity worth USD 8.75 billion in the period till early September 2009. According to the Securities and Exchange Board of India, net purchases were negative till February, but turned positive in March with the net purchases figure being high during April (USD 1.3 billion); May (USD 4.1 billion); July (USD 2.3 billion) and August (USD 1 billion).

It is not surprising that foreign institutional investors returned to market. They needed to make investments and profits to recoup losses suffered during the financial meltdown. And they had been helped in that effort by the large volumes of credit provided at extremely low interest rates by governments and central banks in the developed countries seeking to bail out fragile and failing financial firms.

It is to be expected that a country like India would receive a part of these new investments aimed at delivering profits to private players but financed at one remove by central banks and governments. However, India has received

more than a fair share of these investments. One way to explain this would be to recognize the fact that India fared better during the recession period than many other developing countries and was therefore a preferred hedge for investors seeking investment destinations. The other reason is the expectation fuelled by the return of a stable government that intended to push ahead with the ever-unfinished agenda of economic liberalization and reform. The new government has, for example, made clear that disinvestment of equity in or privatization of major public sector units is in the cards; caps on foreign direct investment in a wide range of industries, including insurance, are to be relaxed; public-private partnerships (in which the government absorbs the losses and the private sector skims the profits) are to be encouraged in infrastructural projects, with government lending to or guaranteeing private borrowing to finance private investments and that corporate tax rates are likely to be reduced and capital gains taxes perhaps abolished.

All of this generates expectations that there are likely to be easy opportunities for profit delivered by an investor-friendly government in the near future, including for those who seek out these opportunities only to transfer them for profit soon thereafter. These opportunities, moreover, are not seen as dependent on a robust revival of growth, though some expect them to strengthen the recovery. In sum, whether intended or not, the signals emanating from the highest economic policy making quarters have helped talk up the Indian market, allowing equity prices to race

ahead of earnings and fundamentals. Once the speculative surge began, triggered by the inflow of large volumes of footloose global capital, Indian investors joined the game financed very often by the liquidity being pumped into the system by the Indian central bank. The net result is the current speculative boom that seems as much a bubble as the one that burst a few months back.

There are three conclusions that flow from this sequence of events. The first is that using liquidity injection and credit expansion as the principal instrument to combat a downturn or recession amounts to creating a new bubble to replace the one that went bust. This is an error that was made the world over, where the so-called stimulus involves injecting liquidity and cheap credit into the system rather than using public spending to revive demand and alleviate distress. The second is that so long as the rate of inflation in the prices of goods is in the comfort zone, central bankers stick to an easy money policy even if the evidence indicates that such a policy is leading to unsustainable asset price inflation. It was this practice that led to the financial collapse triggered by the sub-prime mortgage crisis in the US. Third, governments in emerging markets like India have not learnt the lesson that when a global expansion in liquidity leads to a capital inflow surge it does more harm than good, warranting controls on the excessive inflow of such capital. In the event, we seem to have engineered another speculative surge the employment effects of which are minimal.

10. CONCLUSION

The net implications for employment and conditions of work of the process of growth remain adverse. *Ceteris paribus*, higher growth rates should lead to higher employment growth. However, the problem here is with the *ceteris paribus* assumption. It does not take account of the implications of the pattern of growth.

A consequence of that pattern of growth has been that output per worker has risen significantly in the non-agricultural sector where output growth has been particularly high. Overall, GDP per worker, which rose by 2.30 percent and 1.87 percent, respectively, during the 1950s and 1960s, fell to a low of 0.69 percent in the 1970s. Since then, the rate of increase has been remarkable, standing at 3.53 percent and 4.32 percent, respectively, during the 1980s and 1990s (Sivasubramonian 2004: 4, Table 1.1). While a part of this rise in output per worker may have meant an increase in the wages of sections of the already employed, it would principally mean an increase in income inequality because of an increase in managerial salaries and profits. For the majority of those available for and seeking work, the result has been a tendency to fall back on forms of work that do not offer a decent wage and involve poor work conditions.

There are three important implications for policy that emerge from this analysis of the Indian experience, widely perceived as an instance of successful global integration through liberalization. India's experience indicates is that even when successful in accelerating growth rates, the process of integration could result in a pattern of growth that does not have positive employment implications, and can therefore be inequalizing. This would imply that countries faced with a significant unemployment problem, in the form of a backlog of unemployed and underemployed workers, should not see liberalization in general and trade liberalization in particular as a development panacea, even if expectations are that growth can be accelerated through

liberalization. This implies that the extent of liberalization required of these countries either as part of adjustment strategies aimed at dealing with balance of payments problems or as part of negotiated agreements in organizations like the WTO should be limited and calibrated, if the international community is committed to targets such as those incorporated in the Millennium Development Goals. In particular, bound tariffs must be at levels that allow for adjustments in the face of changes in international prices. Further, developing countries themselves should not unilaterally or through terms agreed in bilateral or regional trade agreements take liberalization beyond levels considered appropriate given their contexts.

When adopting even limited and calibrated integration, developing countries should consider adopting policies that counteract the adverse fall-out of such liberalization for the labour market. One such policy could be an effort by the State to undertake programmes that guarantee a minimum of employment in public works of different kinds to the poorer sections of the population. India is currently experimenting with such a strategy through an employment guarantee provided by the National Rural Employment Guarantee Act (NREGA) passed by Parliament. The Act provides a legal guarantee for at least 100 days of employment on asset-creating public works programmes every year at minimum wage for every rural household. This involves providing 100 days of work to any member of the household at the minimum wage. The minimum wage varies across states, but the weighted average can be taken as INR 60 per day.¹⁴ This means that the wage component of the cost per participating household would be INR 6,000 per year.

Assuming that wages will account for two-thirds of the total cost, so that the non-wage component would come to INR 3,000 per year, results in a total cost of INR 9,000 per year per household. The non-wage component is slightly

less than it has been in recent years in existing employment schemes, but it is argued that this is easy to achieve especially with decentralised panchayat-level control over such resources and the implementation of this programme. This means that the total cost of such a programme would probably come to somewhere between INR 440 billion and INR 530 billion per year.

At first glance this may seem like a large amount for an annual outlay. However, a number of points have to be borne in mind. First, even if such employment generation yielded no other positive result, increased wage incomes in rural areas would generate more demand for rural goods and services, and thus generate positive multiplier effects. In a condition of major economic slack, such as operates in the rural economy of India today, this would have large beneficial implications for material conditions and even contribute to increased tax revenues because of higher levels of economic activity.

Second, it must be remembered that such a programme does not involve an expenditure of resources for the sole purpose of creating employment. Rather, the idea is to use the workers productively in activities that will build or maintain assets in the countryside or provide important social or economic services. So, such expenditure will yield dividends not only in terms of higher levels of economic activity in the present, but also through improving the conditions of production in rural areas. There are many such potential activities that can have important effects on supply conditions, productivity and sustainability of rural economic activities in both agriculture and non-agriculture.

For example, constructing and maintaining roads and other connectivity (which has thus far been the most popular form of activity in such schemes) has direct and indirect effects in agricultural marketing and a whole range of other economic activities, besides generally improving the conditions of rural residents. But other activities, which are often far less capital-intensive, such as building and maintaining bundhs, minor irrigation works, and clearing

out and desalting ponds and rivers, also have very positive short-run and long-run effects on production conditions and can improve the sustainability of cultivation patterns generally, implying important social gains.

But even these do not cover the full range of possibilities in terms of productive and useful activities that can be undertaken under such an employment programme. There is a huge range of social services that must be performed, which are now systematically underprovided across rural India. These include activities such as those performed by workers in educational and health institutions who provide maintenance and support, the provision of mid-day meals in schools, sanitation services and the like. There is no question that greater provision of such necessary public services would greatly improve the quality of life of rural residents and contribute directly and indirectly to economic growth.

So, this amount is really not very much when seen as part of a broader public investment and development programme that is particularly focussed on rural regeneration, which is unquestionably the most urgent policy focus today. In any case, the projected amount likely to be spent on the employment guarantee is a trifling percentage of GDP amounting to around 1.5 percent of projected GDP at the coverage of one-third of rural households and only 1.9 percent of GDP at 40 percent coverage.

Another possible policy initiative being discussed in the Indian context to deal with the adverse fall-out of reform is the provision of some form of social security for the poor. The first report of the National Commission for Enterprises in the Unorganised Sector ("Social Security for Unorganised Workers: Report of the National Commission for Enterprises in the Unorganised Sector", Government of India, May 2006) makes far-reaching but workable proposals to provide some minimal social security to the vast majority of India's workers. It also provides the framework for important and necessary legislation to ensure that this is provided, which should become an immediate priority of this government.

The Commission divides the social security problems of all informal workers into two categories. The first is seen to arise out of capability deprivation and essentially relates to the terms, conditions and remuneration of employment. This creates such problems as inadequate work availability, low earnings from work, insecurity of contract and possibility of termination, low health and educational status leading to access to only low productivity jobs. The second category of problems consists of those arising from both predictable and unforeseen adversity, because of the absence of any safety nets to meet ill health, accidents, old age and death.

The first set of problems clearly require more than social security measures, since they reflect broad development processes and macroeconomic strategies that have involved the persistence of poverty, low levels of education, aggregate low productivity and so on. It is clearly unrealistic to expect social security measures to address these larger problems in any meaningful way. Instead, this report focuses on measures to alleviate to some extent at least, the second set of problems and to provide to the bulk of citizens in India who have hitherto been excluded, at least a modicum of basic protection against adversity.

The scheme suggested by the Commission incorporates the following features, which if accepted would lead to landmark legislation:

- It would be a national initiative proposing universal coverage of all informal workers in both rural and urban areas, and in both unorganized and organized sectors.
- It would be a rights-based scheme, proposing a legally enforceable entitlement.
- All informal workers would be eligible to join, irrespective of occupation or duration of employment.
- It would be a voluntary and contributory scheme, whereby the worker, the employer and the government each pays INR 1 per day

per worker. (In the case of below-the-poverty-line workers, the worker's contribution is to be borne by the central government.)

- It would be designed to provide a minimum combination of health, life and old-age benefits at the national level. State governments are free to add to this as they choose, in terms of contributions or additional benefits.

Measures such as the NREGA and the above social security proposal can go a long way in alleviating the adverse labour market effects of growth processes unleashed by unavoidable trade and economic liberalization.

The third implication that emerges from India's experience relates to the aid-for-trade discussion that has recently gained currency. Conceived narrowly, aid for trade is aimed at enabling poorer developing countries to enhance their trade competitiveness through means, such as the establishment of appropriate standards, diversification of their agricultural, industrial and services capabilities and exports and capability to deal with their myriad human, institutional, trade-related physical infrastructure and other supply-side constraints. This it is hoped will allow them to avoid being affected too adversely by trade liberalization. But, even for this purpose, the policy must go further. It should also help them adequately address short-term adjustment problems (such as fiscal and terms of trade losses); deal with other short-, medium- or long-term preference erosion (textiles and clothing, sugar, bananas); and cover implementation costs of trade agreements (eg. trade facilitation, intellectual property, sanitary and phyto-sanitary standards, and regulatory demands of services trade liberalization) that they have entered into.

But the above discussion indicates that even all this would be inadequate unless aid for trade is conceived as an aid-for-development initiative to compensate the losers in the process of trade liberalization through measures of the kind that are being experimented with even in a large developing country, such as India.

ENDNOTES

- 1 This refers to National Sample Survey Organisation, *Employment and Unemployment in India*, 38th, 43rd, 50th, 55th and 61st Rounds. The NSS data on employment is based on the distinction between “principal” and “subsidiary” status of activity as well on whether the person is “usually” or otherwise engaged in the activity. The activity status on which a person spent relatively longer time (i.e. major time criterion) during the 365 days preceding the date of survey is considered as the principal usual activity status of the person. The activities pursued by a person are grouped into three broad categories: (a) working or employed (b) seeking or available for work (i.e. unemployed) and (c) not in the labour force. A “non-worker” (on the basis of the usual principal status) is someone whose major part of time in the preceding year was spent as either unemployed or not in the labour force. However, he or she could still be involved in some economic activity in a subsidiary capacity - when this is usually the case the person is referred to as a “subsidiary status worker”. The two categories together - usual workers by both principal and subsidiary status - constitute “all usual workers”. The surveys also provide evidence on weekly and daily status. The current weekly activity status of a person is the activity status obtaining for a person during a reference period of seven days preceding the date of survey. It is decided on the basis of a priority-cum-major time criterion. The current daily activity status for a person is determined on the basis of his or her activity status on each day of the reference week
- 2 The results of the 2009-10 survey are not yet available.
- 3 For a detailed analysis of the responsiveness of employment to output growth refer Ghosh (2006).
- 4 Based on budget documents of the Government of India for the relevant years.
- 5 It should be noted that this aggregate increase incorporates declining rates of labour force participation among the youth, that is the age group 15-29, and a rise for the older age cohorts
- 6 This significance of self-employment also brings home the urgent need to consider basic social security that covers not just general workers in the unorganised sector, but also those who typically work for themselves, which is what makes the pending legislation on this so important.
- 7 All figures based on the Central Statistical Organisation’s *National Accounts Statistics*, available at http://www.mospi.nic.in/mospi_nad_main.htm.
- 8 Computed from figures available from www.nasscom.org and http://www.mospi.nic.in/mospi_nad_main.htm.
- 9 For a detailed elaboration of these changes refer Chandrasekhar (2007).
- 10 The years 1991 and 1992 were characterized by a massive contraction of imports because of balance of payments difficulties and a collapse of India’s foreign exchange reserves. A concomitant of import compression was a decline in investment and capacity utilization.
- 11 Figures from “Indian IT Industry Factsheet”, available at http://www.nasscom.in/upload/5216/Indian_IT_Industry_Factsheet_2006.doc accessed November 28, 2006.
- 12 NASSCOM on the other hand placed employment in the Indian IT-ITES sector at 2,84,000 in financial year 1999-00 and 10,45,000 in 2004-05.

- 13 This section draws heavily on Ghosh and Chandrasekhar (2009).
- 14 Of course the assumption must be that the wages would be equal for men and women workers - which is what is legally required but has not always been followed in employment programmes thus far.

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