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CREATING KNOWLEDGE TO END POVERTY

EQUITY AND GROWTH IN INDIA

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Income distribution has emerged as an increasing concern in the last two decades, due to rising inequalities and a sharp decline in the wage share in many countries. A declining wage share represents a decline of the wage bill relative to total income (or capital incomes).

This raises important questions. Firstly, to what extent is a declining wage share a necessary feature of economic growth, or a consequence of inadequate policies? Secondly, to what extent does a declining wage share signal declining real incomes for different groups of workers?

These questions are particularly relevant for India. The country is witnessing a sharp decline in its wage share, despite a strong macroeconomic performance (annual growth rates have averaged 6.7 percent at constant prices between 1991-1992 and 2007-2008). One explanation for the declining wage share in Indian factories, in particular, has been an increase in the capital intensity of employment (and hence labour productivity).

Drawing on this hypothesis, our research examines the relationship between technical change, wage share variability, and labour incomes in two industrial areas. The case studies include a relatively capital-intensive production cluster (auto-components) and a labour-intensive production cluster (handicrafts).

A key finding is that the inequalities generated between and within income categories are not a necessary outcome of technological change, but a consequence of a widening gap in the balance of power between different income categories more generally. Another key finding is that the wages paid to most industrial workers (including in large/modern factories) lack any substantial relationship to rises in labour productivity (see Figure 1). In addition, a lack of industry-level bargaining, and the replacement of unionised workers by non-unionised (and hence lower paid) workers to do the same jobs, have led to an unequal distribution of productivity gains within the labour income category. Moreover, while capital can move to other economic activities in search of expected/higher returns, most workers do not have this option. These factors lower the bargaining power of many sections of the industrial workforce in India to command levels of pay in line with increasing needs.

The research finds that the benefits of growth do not automatically 'trickle' down to the labour income category. The issue of income distribution between capital and labour, at the level both of workers as workers (e.g. wage bargaining, employment generation) and workers as consumers (e.g. prices, public services) needs to be addressed more directly.

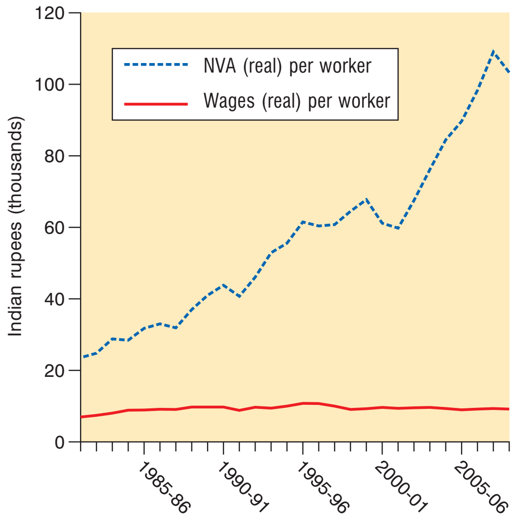

Figure 1: Trends in net value added (NVA) and real wages, Indian factory sector.

Source: Government of India, *Annual Survey of Industries*, various years.

Key policy points

- Income distribution needs to be addressed as a policy dimension in its own right, and not simply as an 'appendix' to the issue of how to increase accumulation and growth.
- Public policy has a major role in improving the bargaining power of poor workers (through rights, labour laws and economic and social policies), to facilitate sharing in the gains from growth.
- Since a declining wage share implies a rising capital share, other important policy dimensions are how capital incomes are invested, and taxation policies. These seem to be crucial for promoting investment priorities and public policy.

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Email: natcfg@gmail.com. This briefing is based on the author's PhD thesis.

Further reading

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