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India needs an Employment Guarantee Scheme

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India reduced poverty during the 1990s. However, since income inequality increased at the same time and in a generalised way, the momentum on poverty reduction might decline in the future.*

Only employment-intensive growth will make continued poverty-reduction attainable. Again, the prospects for a strong employment generation process are not bright. The capacity to create jobs in tandem with production in manufacturing fell in the 1990s. It is only in services where urban employment has been growing rapidly. That confines the majority to depend upon India's slow-growing agriculture for a source of income. Agriculture still accounts for 59% of total employment. Most poor families are in casual employment or self-employed, while those with regular employment are least likely to be poor.

Thus, direct action by the government to spark job creation could dramatically reduce rural poverty. The government has introduced a bill in parliament providing a minimum guarantee of employment to poor households. The proposal is to give a statutory right to 100 days a year of employment at the minimum wage in each state to one person per household. On the basis of a minimum wage for all states of R$ 60 per day, 100 days work will raise two-thirds of India's population above the poverty line. It will initially cover the 150 poorest districts in the country.

The scheme can bring a number of benefits. In fact, labour-intensity can be very high in such work as watershed development, land regeneration, and prevention of soil erosion. This would protect the environment, but also enhance land productivity and increase output in future.

It would also have positive second-round effects on incomes, by raising rural wages and thus investment in human capital. One reason children of poor parents drop out of school is because they cannot afford schooling costs; raising incomes would reduce school drop outs. Add to this the increase in land productivity – together these can have profound economic growth effects.

Besides, improving watershed development could reduce damage to life and property caused by frequent flooding, and save future costs in government flood relief. The benefits of the employment guarantee scheme spread beyond its immediate impact on poverty.

Over the long run, the bill's implementation would not obviate the need for transfer of labour out of agriculture, where few have regular employment; most are self-employed or casual labourers. Much of the new regular wage jobs should be for low-skilled workers. This implies a growth strategy of manufactured exports requiring low-skilled labour, and producing low-skill intensity goods for the domestic market – rather unlike the current strategy.

But with a 222 million work force in agriculture, even a fast transfer out of agriculture will not pull all the working poor out of poverty. Hence direct employment creation through the act is an essential component of policy.

Is the employment guarantee scheme feasible? The economist Jean Dreze has estimated the total cost of the programme with phased implementation rises from 0.5% of GDP in the first year (2005) to 1% of GDP in the last year of the inception phase (2008). Thereafter, the ratio will decrease, as the number of below-poverty line households decreases. The consolidation of existing employment generation schemes with the programme of employment guarantee will increase efficiency in resource use.

The scheme, and these costs, are modelled on a similar scheme implemented successfully for 20 years in Maharashtra. But the preceding calculations assume a labour-material ratio of 60:40. The corresponding ratio is much lower in Maharastra, and unit costs could come down with more labour intensity.

These costs are not outrageously high but they are not low either. However, reverting the downward trend on the already low tax base of India will provide enough resources to pay for the employment guarantee act. Compared to central tax revenues for low-income countries of 14.1% of GDP over 1990-2001, or 22 for China in 2003, India's centre collected around 9% of GDP average between 2001 and 2004. Despite rising incomes in India the ratio of central taxes to GDP has actually fallen from 10.6% in 1987/8 to 9.3% now.

There are still at least 200 million poor people in India, and increasing inequality could lead to serious social tensions and urban turbulence. The social consequences of rising inequality in India in the midst of 200 million poor – a given if the current pattern of jobless growth continues – can be dire. There is a case for direct government intervention to create jobs: the employment guarantee act might be a good option.

* *Nota bene*: See Kakwani's One Pager 2 on the debate on poverty and inequality in India. (OnePager's editors).