



## WAGE ACT AMENDMENT AND ITS IMPACT ON EMPLOYMENT (DIRECTLY, CONTRACTUAL, OTHER EMPLOYEES) : EVIDENCE FROM INDIAN MANUFACTURING SECTOR



**Anup Tiwari<sup>1</sup>**

<sup>1</sup>Research Assistant  
London School of Economics and  
Political Science  
Delhi, India

### ABSTRACT

*There are lot of literature focus on the effect of government expenditure and its impact in employment, tax, etc. This paper focus on the amendment of fiscal policy (the payment of wage act amendment 2005) and its impact on categories of employment like directly, contract and other employees using the Indian manufacturing data. I find that due to wage act amendment there is not only increase in wages to workers and total emoluments but also led to an increase in the directly employed, contractual employed and other employed workers in the Indian manufacturing sector. But the increase in the employment with respect to the wage rate increase sustained for only 1 year. After that the employment figure reduced due to financial crisis and low public and private investment.*

**KEYWORDS:** *Employment, Tax, Government Spending, Fiscal Policy, Productivity, Manufacturing Sector*

### Section 1

#### INTRODUCTION

The relationship between the government expenditure and labor market employment status is sign for the development of the sector/economy, not only in the field of employment, but also led to an increase in the productivity of the sector/economy. The Government improves the market/economy status with the help of fiscal policy, through government spending, taxation and transfer payment and through continuous amendment in the running policies or act. But time lag would be the problem associated with the fiscal policy i.e if fiscal policy would be implemented today, then the results would be shown after some time. In this paper, I find one period time lag after the amendment in payment of wage act and its impact on employment status using the data from Indian Manufacturing Sector. In other words, the amendment in payment of wage act improves the employment status in manufacturing sector with one year

lag effect. I also find that the rate of increase in employment is more after the amendment in fiscal policy than before the fiscal policy implemented, but the effect can be sustained only for one period.

There are plethora of study conducted so far, which focus on the effect of fiscal policy, i.e. the effect of government expenditure on employment, private consumption, consumption, debt and deficit, etc. Fatas and Miho (1998) find that increase in government expenditure lead to an increase in consumption and employment. Similarly Edelberg, Eichenbaum, and Fisher (1999) find the consequences of an exogenous increase in U.S government spending. They find that the increase in government expenditure lead to an increase in employment, output and non residential investment and fall in residential investment, real wages and consumption expenditure etc. But none of the study focused on the effect of amendment in fiscal policy and its impact on category of employment, i.e. directly, contractual and other employees employment.

Burnside, Eichenbaum, and Fisher (2000) find that there is a high correlation between the increase in government and tax rate, and hours worked, which would lead to a decline in the real wage rate. Blanchard and Perotti (1999) characterizes the dynamic effects of shocks in government spending and taxes on economic activity in the United States in the post-war period. They find that the positive government spending shocks lead to a positive effect on output and positive tax shocks as having a negative effect. Finn (1998) find that the components of government spending, i.e. good purchase and wage compensation are important. He finds that shock to government good purchase and government employment have a positive effect on private output, private employment and private investment.

Aiyagari and Christiano (1992) find that the impact on output and employment of a permanent change in government expenditure exceeds to that of the temporary change in government expenditure. On the same front, Linnemann and Schabert, (2003) finds that the rise in government expenditure effects labor demand and at the same time it would also boost the labor supply in the market. Gali (1993) also finds the empirical relationship between the government size and macroeconomic stability and investigate. All the above literatures focus on the government expenditure and its impact on the employment etc. But this paper would look at the effect of amendments in fiscal policy on the categories of employment.

The payment of Wage (Amendment) Act 2005 - This Act applies to wages payable to an employed person in respect of a wage period if such wages for that wage period do not exceed six thousand five hundred rupees per month or such other higher sum. According to the amendment of wage act 2005, when any application related to wage fraud is entertained, the authority shall hear the applicant and the employer or other person responsible for the payment of wages under section 3, or give them an opportunity of being heard, and, after such further enquiry, if any, as may be necessary, may, without prejudice to any other penalty to which such employer or other person is liable under this Act, direct the refund to the employed person of the amount deducted, or the payment of the delayed wages, together with the payment of such compensation. According to the amendment of wage act, every employer shall be responsible for the payment of all wages required to be paid under this Act to persons employed by him and in case of persons employed in factories, industries, and contractor.

In this paper, I will investigate the effect of amendment of fiscal policy on the employment (directly employed, employed through contracts and other employees) and other variable of interest like labor cost, wages to workers, total emoluments and total number of employees. I will be using data from Indian Manufacturing sector. There are 22 sub sectors in the Indian Manufacturing sector<sup>1</sup>. I find the effect of amendment in payment of wage act on the each variable of interest and within each sub sector of the Indian Manufacturing sector. I also find that which sub sector response positively and negatively with the increase in the wage rate. I also find that the rate of increase in the variable of interest is more after the amendment in fiscal policy than before. The main idea is to look at the effect of amendment of payment of wage act on the overall manufacturing sector. At the overall level, the variable of interest increased till 2006 and sustained only for one period after that interested variables faced a downward trend due to financial crisis in year 2007. After that the variable of interest faced a zig zag trend except wages to workers due to low investment and financial crisis. Wages to workers and Total emolument is significantly less in year 2009 as compared to other years due to low level of employment.

This paper is divided into several sections. Section 1 is the introduction section, section 2 is the variable definition and data collection, section 3 is trends of variables of interest, section 4 is comparison of variable of interest before and after the implementation of wage act, and section 5 is Conclusion

#### **NOTE**

<sup>1</sup> *Food Products ,Tobacco Products ,Wearing Apparel ,Leather Products ,Wood Products ,Paper Products ,Publishing ,Petroleum Products ,Chemicals Products ,Rubber Products ,Non-Metallic Products ,Basic Metals ,Fabricated Metal ,Machinery and Equipment ,Computing Machinery ,Electrical Machinery ,Communication Equipment ,Optical Instruments ,Motor Vehicles, Trailers ,Transport Equipment ,Furniture; Manufacturing ,Recycling ,Textiles.*

#### **Section 2**

#### **VARIABLE DEFINITION AND DATA COLLECTION**

Contract Worker: All persons who are not employed directly by an employer but through the third agency, i.e. contractor, are termed as contract workers.

**Employees:** Employees relate to all persons engaged by the factory whether for wages or not, in work connected directly or indirectly with the manufacturing process and include all administrative, technical and clerical staff as also labour in production of capital assets for factory's own use. This is inclusive of persons holding position of supervision or management or engaged in administrative office, store-keeping section and welfare section, watch and ward staff, sales department as also those engaged in the purchase of raw materials etc. and production of fixed assets for the factory. Persons in the head office connected with the manufacturing activity of the factory are also included in this item.

**Wages (Rs. thousand):** Wages are defined to include all remuneration capable of being expressed in monetary terms and also paid more or less regularly in each pay period to workers (defined above) as compensation for work done during the accounting year. It includes: (i) basic wages/salaries, payment of overtime, dearness, compensatory, house rent and other allowances; (ii) remuneration for period not worked (i.e. basic wages), salaries and allowances payable for leave period, paid holidays, lay-off payments and compensation for unemployment (if not paid from source other than employers); (iii) incentive bonuses and good attendance bonuses, production bonuses etc.

It excludes layoff payments and compensation for employment except where such payments are for this purpose, i.e., payments not made by the employer. It excludes employer's contribution to old age benefits and other social security charges, direct expenditure on maternity benefits and creches and other group benefit in kind and travelling and other expenditure incurred for business purposes and reimbursed by the employer. The wages are expressed in terms of gross value, i.e., before deductions for fines, damages, taxes, provident fund, employee's state insurance contribution etc. Benefits in kind (perquisites) of individual nature are only included.

**Emoluments (Rs. thousand):** These are defined in the same way as wages but paid to all employees plus imputed value of benefits in kind i.e. the net cost to the employers on those goods and services provided to employees free of charge or at markedly reduced cost which are clearly and primarily of benefit to the employees as consumers. It includes profit sharing, festival and other bonuses and ex-gratia payments paid at less frequent intervals (i.e. other than bonus paid more or less regularly for each period). Benefits in kind include supplies or services rendered such as housing, medical, education and recreation facilities. Personal insurance, income tax,

house rent allowance, conveyance etc. for payment by the factory also is included in the emoluments.

**Labour cost (Rs. Thousand) :** Labour Cost industry-wise break up of proportion of various components of labour cost on employee, viz., (i) wages/salaries; (ii) bonus; (iii) contribution to provident and other funds; and (iv) workmen and staff welfare expenses.

Total number of employees includes total number of workers in the firms.

The variables of interest are directly employed, contractual employed and other employees, labor cost, wages to workers, total emoluments and total number of employees. The data of all the mentioned variables are collected for all the sub sectors under the manufacturing sectors. The data is obtained from the Indiatat and annual survey of industries from 2000 to 2010.

### **Section 3 TRENDS OF VARIABLES OF INTEREST**

After the amendment of payment wage act in year 2005, the wages of the workers increases because according to wage act every employer shall be responsible to pay the wages to the workers employees by him and in case of person employed. In the next paragraphs we will discuss the trend of wages and emoluments, directly and contractual employees workers at the sub sector level before and after the amendment of wage act.

**Wages and emoluments:** The sub sectors under manufacturing sector like tobacco products, wearing apparel, leather products, wood products, paper products, petroleum products, non-metallic products, fabricated metal, machinery and equipment, electrical machinery, motor vehicles, trailers, transport equipment, furniture; manufacturing, textiles had witnessed an sharp increase in both wages and emoluments after the implementation of wage act 2005. The sub sector like publishing, chemicals products, rubber products, basic metals, computing machinery, communication equipment, optical instruments, recycling sectors faced a slightly fall in wages and emoluments once in 2006 after year 2005 and afterward they showed an increase in wages and emoluments.

**Directly employed:** There are several sub sector in the manufacturing sector like food products, wearing apparel, leather products, wood products, paper products, publishing, rubber products, basic metals, fabricated metal, machinery and equipment, computing machinery, electrical machinery, communication equipment, optical instruments, motor vehicles, trailers, transport equipment, furniture; manufacturing, textiles witness an increase in

the directly employed employees after the implementation of the wage act 2005. The sub sector like tobacco product, petroleum products, chemicals products, non-metallic products, recycling witness an decrease in directly employed workers.

Workers employed through contracts: The workers employed through contracts also witnessed an increase in employment after the amendment, but the increase in contractual workers would be less than the increase in directly employed workers. The sub sectors like petroleum products, rubber products, non-metallic products, basic metals, fabricated metal, electrical machinery, communication equipment, motor vehicles, trailers, transport equipment, furniture; manufacturing witnessed a constant increase in the workers employed through contracts after the amendment of wage act. The other sub sectors witnessed an decline or a slight increase in the workers employed through contract.

Total cost: with the increase in the wage, the cost of the company on the worker would also increase, and the almost every sub sector witnessed an increase in the total cost on the workers just after the amendment of the wage act. Total employees: total number of employees in almost all the sub sector of manufacturing sector increases

after the amendment of the wage act. Sub sector like tobacco product and chemicals product industry showed an decline in the total employees.

**Section 4**

**COMPARISON OF VARIABLE OF INTEREST BEFORE AND AFTER THE AMENDMENT IN PAYMENT OF WAGE ACT**

**Average value of the variable of interest before and after the wage act amendment:-**

Table 1 provides us the information about the change in the variable of interest before and after the amendment in wage act. The average value of the wage to workers, directly employed workers, other employees, total employees and total emoluments showed a significant increase after the wage act amendment. The wages to workers increased from 262623 to 568883, and in response to that directly employed workers increased from 363074 to 518468, other employees increased from 81346 to 112042, total employees increased from 663929 to 965496, and total emoluments also increased from 495681 to 1179443.

**Table 1: Mean variable of variables of interest before and after implementation of wage act**

	Before 2005			After 2005		
	Mean	SD	Count	Mean	SD	Count
Wages to workers	137020.7	129063.7	115	297569.8	249246.8	130
Directly Employed	190050.8	221981.4	138	272792	265283.8	103
Employed through contract	61187.9	76603.91	138	127487.3	108956.8	103
Other employees	42563.39	46469.78	115	58934	60269.26	103
Total labor cost	265274.2	310033.7	92	592707.9	479589.6	84
Employees	346397.9	350070.2	115	505028.9	427108.1	130
Total emoluments	258616.6	239705.1	115	616939.7	511616.7	130

**Average values of the variable of interest at yearly level:-**

In the further tables we will be looking whether the wage act amendment would lead to an increase in the variable of interest on incremental yearly bases.

**Tables 2: Mean value of the variable of interest for all the years.**

	2002	2003	2004	2005	2006	2007	2008	2009	2010
Wages to workers	127019	130116.6	143497	160389.6	188101.7	217281.1	266961.7	308070	381326.5
Directly Employed	200577.4	194019.9	204614.1	214915.3	232167.3	238587.6	291784.6	299638.7	317535.5
Employed throughcontract	59598.17	63024.96	73471.04	85894.61	99693.61	107372.8	136811.1	142204.1	161440.8
Other employees	44904.96	40101.39	41245.65	43945.61	59573.09	49451.91	64277.32	58058.21	65171.16
Employees	334780.7	331812.9	355673.7	383081.7	433741.7	439491.8	501586	521907.5	558942.8
Total emoluments	236022	249141.8	274717	314911.6	375749.7	448096.3	566050	637802.2	795553.1



Table 2 calculate the mean value of all the variable of interest before and after the amendment of wage act 2005. Almost all the variable of interest increased after the amendment in wage act. Wages to workers increased from 160389 in 2005 to 188101.7 in 2006 to 217281.1 in year 2007 and 308070 in 2009 respectively. Similarly, the other variables of interest also follow the increasing pattern after the amendment in wage act.

In this section I show that the all the variable of interest after the implementation of the wage act increased over the period of time. But in order to look at

the incremental increase in the variable of interest, difference in mean estimate would give the accurate value.

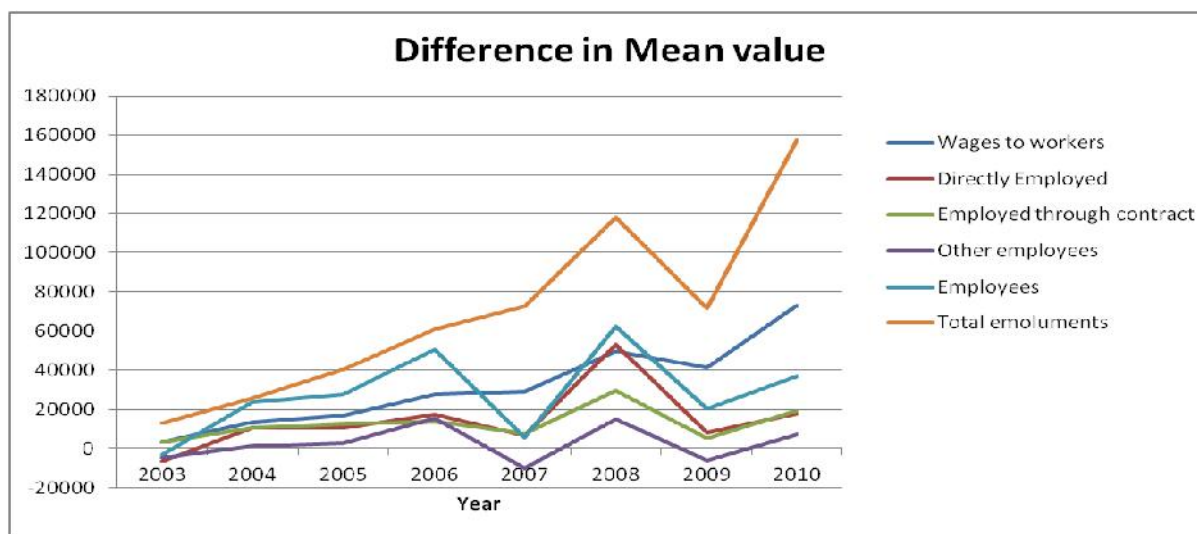
**Difference in mean values of variable of interest:-**

Table 3 consists of difference between the mean values of the variable of interest of two periods like wages of workers in year 2003 is 3097 i.e difference between wages of workers for year 2003 and 2002. Irrespective of looking at the number, the trend would be clear and explainable by preparing the graph using the difference in mean estimate in table 3.

**Table 3: Difference in mean values**

	2003	2004	2005	2006	2007	2008	2009	2010
Wages to workers	3097.6	13380.4	16892.6	27712.1	29179.4	49680.6	41108.3	73256.5
Directly Employed	-6557.5	10594.2	10301.2	17252	6420.3	53197	7854.1	17896.8
Employed through contract	3426.79	10446.08	12423.57	13799	7679.19	29438.3	5393	19236.7
Other employees	-4803.57	1144.26	2699.96	15627.48	-10121.2	14825.41	-6219.11	7112.95
Employees	-2967.8	23860.8	27408	50660	5750.1	62094.2	20321.5	37035.3
Total emoluments	13119.8	25575.2	40194.6	60838.1	72346.6	117953.7	71752.2	157750.9

From the graph below, we will look at the trend of the variables of interest before and after the implementation of wage act.



Before the amendment in wage act, the difference in mean values of the variable of interest is small and for some variable like directly employed, other employed and employees are negative during 2003. During 2004, the difference in mean values of the variable which were negative during 2003 increased and reached to positive number. The difference in mean value of variables in year 2005 increased but this difference in mean value is almost or slightly greater than the difference in mean values of the variables in year 2004. This shows that the fiscal policy is not very much effective on the policy implementation year.

In 2006, the difference in mean value of the variable of interest increases more than the increase in years before 2005. Difference in mean value of wages of the workers increased to 27712, total emoluments increased to 60838, total employees also increased to 50660 and other variable also increased with a significant difference in mean value as compared to the period prior to the implementation of wage act.

The growth in the Indian manufacturing sector was slow since 2007 due to low level of private and public sector investment T.P Bhatt(2014). In year 2007, the wages to workers and the total emoluments increases continuously but the average increase in the directly

employed, contractual employed and total employees reduces by significant number compared to an average increase in year 2006.

Although after 2007 there was increase in the variables of interest till 2008. After 2008, due to the global financial crisis the growth of the manufacturing sector reduced to 4 percent during 2008 as compared to 9.8 percent in the previous year and continues job losses in manufacturing sector Research Unit, Rajhya Sabha (2009). Therefore, due to global financial crisis, the employments figure (directly, contractual and total employees) showed a decline after 2008.

## **Section 5 CONCLUSION**

This study estimates the effect of amendment in payment of wage act on the employment, wages status of workers in Indian manufacturing sector. Data like wages to workers and total emoluments is collected for Indian manufacturing sector collected from indiastats and annual survey of industries. I claim in this paper, that due to amendment in wage act 2005 not only wages to workers and total emoluments increases but there is also increase in the directly employed, contractual employed and other employed workers in the Indian manufacturing sector. But the increase in the employment with respect to the wage rate sustained only for one period. After that the employment figure reduced to the financial crisis and due to low public and private investment. As per I know, this is the first paper to look at the impact of payment of wage act amendment on employment, wages etc.

Future work would be to look at the similar kind of relationship using the same variable of interest at the state level, firm level and sub sector. The idea would be to prove the similar hypothesis.

## **Section 6 REFERENCES**

1. *Bhatt, T.P (2014), INDIA: Structural Changes in the Manufacturing Sector and Growth Prospect, Institute for Studies in Industrial Development, New Delhi.*
2. *Gali, J (1993), Government size and macroeconomic stability, European Economic Review 38 (1994) 117-132. North-Holland.*
3. *Burnside, Eichenbaum, and Fisher (2000) Assessing the effect of Fiscal Shocks, National Bureau of Economic Research, working paper no.7459.*
4. *Aiyagari, and Christiano (1992), The output, employment, and interest rate effects of government consumption, Journal of Monetary Economics 30 (1992) 73-86. North-Holland.*
5. *Blanchard, and Perotti (1999), An empirical characterization of the dynamic effects of changes in government spending and taxes on output, National Bureau of Economic Research, working paper no.7269.*
6. *Blanchard o, (1984), Debt, Deficits and Finite Horizons, National Bureau of Economic Research, working paper no.1389.*
7. *Fatas, and Mihov, The Effects of Fiscal Policy on Consumption and Employment: Theory and Evidence.*
8. *Linnemann, and Schabert (2003), Fiscal Policy in the New Neoclassical Synthesis, Journal of Money, Credit and Banking.*
9. *Finn. G (1998), Cyclical Effects of Government's Employment and Goods Purchases, Economics Department of the University of Pennsylvania Institute of Social and Economic Research — Osaka University.*