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Labour Reforms and Impact on Business in India

Using reforms as a path to economic growth and progress

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Fond of reading, travelling and trying out new cuisines.

One of quotes she lives by is- "It is our choices that show what we truly are, far more than our abilities."

One of the biggest contributors to the current recession in our country is the investment cycle downturn. This has happened more from non-monetary reasons than the RBI's monetary tightening policies. Some of the major factors of this are the bureaucratic logjams, outdated land acquisition, ancient labour laws and last year's policy paralysis. The present article takes stock of the archaic labour laws blocking industrial progress.

India has a complex number of laws governing labour regulation in India. These have been basically enacted for the protection of workers and the marginalised groups. However, Indian labour laws are considered to be one of the most restrictive in the world and hence over the past few years many critics and observers have argued that labour laws need to be reformed since they have constrained the growth of the formal manufacture sector.

The Ease of Doing Business in India report by CII and KPMG, published in May this year ranks India very low. India is at the 134th rank this year compared to 131 in 2013 which is a 3 point decline. The study has identified key areas for reforms which will enable doing business in India easier, including setting up of business, land acquisition, taxation and contract enforcement. According to the KPMG CEO in India, Richard Rekhy said that having an environment that facilitates entrepreneurship, promotes investments, productivity and growth is critical for improving business climate in India. The susceptibility of India in the current standing in the Doing Business index means that reforms in these areas are most significant.

Understanding the importance of reforms and to set the ball rolling, the stable BJP led NDA government has initiated many reforms in the landmark archaic laws such as the Factories' Act 1948, Apprenticeship Act 1961 and the Labour Laws Act 1988. Within weeks of forming the government, the NDA, through the Labour Ministry, had begun consultations towards amending these laws that are seen as a major challenge by companies in doing business in the country. The Union cabinet on 30th July 2014 approved amendments to these three aforementioned labour laws with the aim to easing regulations which have acted as an obstacle to faster growth and hurt employee interests. The more controversial provisions on retrenchment are expected to be taken up later. The ministry is also in talks with trade unions to make changes in the Industrial Disputes Act for enabling easier hiring and firing of workers in the National Investment and Manufacturing Zones. Making these reforms is also in tandem with the Prime Minister's *'Make in India'* campaign.

Just before the Maharashtra and Haryana polls, the PM also unveiled various other reforms such as a single-window labour compliance process for industries and friendlier provident fund (PF) facilities. Alongside these changes, the 'Rashtriya Swasthya Bima Yojna' for labour in the unorganised sector has also been revived. He also unveiled the new inspection scheme that is expected to end the so-called Inspector Raj. He also stressed on giving more importance to skills development and increased apprenticeship training.

While Modi's strong initiative and a drive to remove all these problematic laws is commendable, the real test of his resolve, however, will be in his ability to actually get these laws passed in the Parliament. These Labour laws that also make it difficult to fire workers, will bring his government up against strong labour unions, who are bound to oppose this move. Rigid labour laws have meant that more than 90 per cent of Indian workers are hired informally as firms dodge the laws. As most companies want to avoid these stringent rules, they hire contract labourers in place of full-time permanent labourers reducing decent employment, thereby causing insecurity, lowered standard of living and reduced access to good healthcare and education facilities deteriorating the quality of human resource in our country. If India wants to reap the benefits of its demographic dividend, it must stop this deterioration. These laws have also led to zombie companies i.e. loss-making state-run firms that have stopped operations but continue to pay staff. One such ridiculous example is that of the British India Corporation, a textile firm that stopped operating nine years ago but whose 1,800 workers continue to clock in each workday to be paid and promoted. The solution proposed for some of these firms is to revive them but make them more independent of the state.

Reforms are being seen as a bold move expected to help attract investments and improve the ease of doing business in the country. Labour reforms would help create a business environment more conducive to investments, thereby reviving the investment cycle which is in a downturn right now and is the root cause of India’s recession today. Also, changes in laws such as those of social security shall also bring the much needed transparency. Small factories employing less than 50 workers that constitute nearly 84% of India’s manufacturing sector shall also find it easier to function. Industrial body ASSOCHAM (Associated Chambers of Commerce and Industry of India) too has applauded this move and has said that removal of such laws will indeed bring a positive business climate, which is conducive for the growth of trade and industry.

In a five-year term, the best time to do the difficult reforms is immediately after elections leaving the easier things for later. This also facilitates reaping the benefits just before the next elections. Since the PM now heads a stable majority government he is much more likely to get these reforms passed unlike his predecessors. Labour reforms will also make way for other urgently needed reforms that will pave way for further economic growth and prosperity.

Accounting the Unaccounted: Black Money and India

With all the estimates doing the round about Black Money, what should the new Government do to keep its election promise?

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"Anything I've done that was ultimately worthwhile, initially scared me to death"

-Betty Bender

The newly formed government has made a lot of noise regarding bringing back the Black Money stashed by Indians in tax havens of the world. They should be focussing more on making policy changes to get hold of the unaccounted money in the country itself. The Finance Ministry's think tank, National Institute of Public Finance and Policy (NIPFP) along with the newly formed Special Investigating Team (SIT) on black money has revealed recently that the extent of unaccounted money generated in today's globalised Indian economy could go up to 71% of the GDP.

What is black money?

Black Money is the proceeds received in cash from underground economic activity. *NIPFP defines black money* as the aggregate of incomes which are taxable but not reported to the tax authorities. According to the White Paper Written by the Ministry of Finance in 2012, the sources of black income can be subdivided into two categories, money generated from illegal activities and money accumulated as a result of failing to pay the public exchequer. The first category includes drug trafficking, weapons trading, terrorism, selling counterfeit or stolen goods and selling pirated versions of copyrighted items such as software and musical recordings. The second category includes income-tax evasion, Corporation tax evasion, Excise duty evasion, Customs duty evasion, Black income from exports, Evasion of state taxes, Bribes, illegal commissions, Goods supplied to black market, Unaccounted stock-market profit, Interest earned from unorganised credit markets.

Why the focus on black money abroad?

According to Global Financial Integrity's (GFI) Report the average value of illegitimate assets held by Indians since independence to 2010 is estimated to be $487 billion. This was followed by the director of Central Bureau of Investigation, A.P. Singh, in 2012 casually mentioning, that $500bn was held by Indians in Swiss Accounts. It leads us to think that maybe CBI just used the GFI estimate. This estimate does not even take into account the money that has returned to our economy from tax havens like Mauritius, Cayman Islands and others. All the brouhaha about the black money that we are currently witnessing within the country is on this very basis. In 2012, India was ranked 94 out of 176 countries in Transparency International's Corruption Perceptions Index. It was tied with Benin, Colombia, Djibouti, Greece, Moldova, Mongolia, and Senegal.

How is Black Money affecting us?

False Information: Black money results in false information about the economy as it is out of the gamut of economic policies. It will impact the data of a country and cast doubts on it. For example national income estimates per capita income, savings and investments.

Black Liquidity Misguides: The government gets misguided in forming monetary policy due to the presence of a sizeable amount of black liquidity. Black liquidity is the accumulation of black money in any form, i.e. cash or in form of gold/silver.

Misguided Resource Allocation: Black money creates errors in allocation of resources in the economy and it results in waste of money. People hide their real income and hence become beneficiary of the government schemes which are actually meant for the poor.

Impact on Fiscal System: The elasticity of the tax system will reduce in the long run as a result of revenue losses. These losses are occurring due to tax evasions on which the government is thriving. This will have a serious effect on the fiscal strength of the country.

The newly formed government of our country is trying hard to keep its election promise of bringing back all the black money stashed abroad. They should change their objective instead, even if they decide to focus on domestic black money rather than foreign, they can still deliver on their promise. There has been a lot of estimation from various entities like Bank of America Merrill Lynch about the amount of black money held by Indians abroad, like the analysts at the company say that even bringing back 50% of the total amount would affect the exchange rate so much so that it would come down to 58/dollar. All of these are just estimates and nothing substantial has been found yet. Hence, we should not be shooting arrows in the dark. A recent report by the Finance Ministry’s think tank NIPFP in 2014 said that every year within India from 1980 to 2007, black money has ranged between 45% & 70% of GDP. This means that every year over $1 trillion of black money is generated in India. So, we should be focussing on our own country and start looking inwards to curb this problem.

Therefore, changing policies to get hold of that 71% of the GDP that is bleeding our economy should be the objective of the BJP government. The report by NIPFP might change the way government is approaching this menace. At least the BJP is trying to work in that direction. This is only keeping my thoughts optimistic towards the growth of our country as the black money brought out will raise the government tax revenue which can be routed for the purpose of development leading to economic growth.

Antidumping Duty as a Trade Barrier

Anti-dumping measure is an instrument of fair competition but in most cases (if not all) it is more of protectionism practice that obstructs free trade.

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If you can dream and not make dreams your master,
If you can think and not make thoughts your aim,
Yours is the Earth and everything that's in it

World is becoming increasingly globalized with distances and barriers reducing. There is movement of goods, services and other resources from one country to another. Because of reductions in barriers, the whole world has become a single market place where anyone can participate based on their competitive advantage. Opening up of economies has led to more opportunities and threats alike.

Although we feel with globalization we are moving towards one state, we are far from reaching there. Most countries of the world are members of trade organizations (like WTO) or trade blocks (Mercosur- a sub-regional bloc comprising Argentina, Brazil, Paraguay, Uruguay and Venezuela, GAFTA- Greater Arab Free Trade Area, ASEAN, EU) which promote hassle-free movement of resources based on its competitiveness. But in reality, most countries have created barriers to free trade which may be economic or non-economic. One such type of economic barrier which is used by countries to protect their interest (local companies) is called Anti-Dumping duty or countervailing duty.

If a company exports a product at a price lower than the price it normally charges on its own home market, it is said to be 'dumping' the product. It is often taken to mean cheap or low quality goods for the importing country. However, it is a misperception of the term. Thus, dumping implies low priced imports only in a relative sense (relative to the normal value), and not in absolute sense. Importing countries see this as a practice which can have adverse effect on its own local producers. *Anti-dumping is a measure taken by governments to rectify the situation arising out of the dumping of goods and its* *trade distortive effect.* It is very subjective as it is not easy for a government to monitor dumping practices.

This information is usually provided by local manufacturers who find that they are adversely and unfairly impacted by dumping of products by foreign countries. These duties are imposed by government over and above the custom duty payable at ports. There are two fundamental parameters used for determination of dumping, namely, the normal value and the export price. Both these elements have to be compared at the same level of trade, generally at ex-factory level, for assessment of dumping. Usually committees are set by governments to analyze and understand the impact of dumping on complaint from local manufacturers having total of more than 50% of domestic capacity. Assessment is done on the basis of economic indicators having a bearing upon the state of industry such as the magnitude of dumping, and the decline in sales, selling price, profits, market share, production, utilization of capacity etc.

Although as per WTO, Anti-dumping measure is an instrument of fair competition but in most cases (if not all) it is more of protectionism practice that obstructs free trade. The purpose of anti-dumping duty is to rectify the trade distortive effect of dumping and re-establish fair trade by creating level playing field. The use of anti-dumping measure as an instrument of fair competition is permitted by the WTO.

The objective for imposing duty is to have fair ground for competition with local industry but it has to be understood that these measures do not assist the local manufacturing industry to become competitive in the globalized market on long term basis. Efforts have to be made by industry to become more competitive by better utilization of resources to become sustainably competitive rather than relying on government intervention and help. Also, it should be seen that many of the products on which anti-dumping duty is levied are manufactured by 2-3 producers who can form cartel to block competition. This is not good for downstream users who buy from them locally at higher price and thus, may become uncompetitive globally.

Let us look at an example of PTA (Purified Terepthalic Acid). It is used in several industries like PET manufacturing, Paints, Resins amongst others. India has only 3 producers namely Reliance, Indian Oil and Haldia Petrochemicals. The total capacity as of now is not enough to meet the total local demand. Import price was anywhere between USD 10-50/MT lower then local price allowing the downstream industries to be competitive internationally. An application was filed by these 3 producers that imports are affecting their margins. Because of lobbying and insufficient representation from domestic users, an Anti-dumping duty was levied. But as a result, it was found that the several downstream users became uncompetitive internationally, some of them likely to even close down now!

Also recently a definitive anti-dumping duty was imposed on imports of recordable DVDs from China, Taiwan and Hong Kong by the Finance Ministry. This levy is valid for five years (till 2013). Moser Baer, a dominant producer of DVDs in India, had in July 2013 filed a petition seeking continuation of anti-dumping duty at enhanced rates which has been accepted. In the case of recordable DVDs from China, the revenue department has now imposed an anti-dumping duty of $36.67 per 1,000 pieces. Although an anti-dumping measure, it would lead to local production of DVDs generating employment.

Where anti-dumping duty is levied on intermediate goods, it can lead to loss of jobs, closures, affecting national exchequer and reducing our competitiveness internationally. Anti-dumping measure should be used in cases where it is really inevitable. (Farm sector, Small scale industries, unorganized sector) and the government should put conditions on the local industries too to become more competitive as these protectionist measures cannot be considered as a long term solution.

As per Darwin 'Survival of the fittest', as we move towards a world without boundaries, such measures cannot lead to sustainable competitive advantage. Governments and companies should have policies in place to become more competitive rather than relying on protectionism which ultimately turns out to be harmful to the national economy.