

Rising LFPR/falling unemployment does not mean tightening labor market in India

- According to the annual Periodic Labour Force Survey (PLFS) report for 2020-21 (year-ending June 2021), India's unemployment rate (for 15-59 years age group) fell to 4.6%, the lowest in the past four years (since the annual PLFS began) and the labor force participation ratio (LFPR) increased to 58.4% in 2020-21 from 53% in 2017-18, same as in 2011-12. In any developed/advanced economy, this combination of higher LFPR and lower unemployment rate is a sign of tightening labor market, generally associated with strong economic recovery. For a low-per capita income economy such as India, however, the unemployment rate does not hold too much significance and rising LFPR indicates weak labor market. Therefore, not only the headline numbers suggest weak labor market, but the internals also confirm this view.
- **Labor force and employment go hand-in-hand:** India's LFPR (for all ages) increased to 41.6% in 2020-21, from 40.2% in 2019-20 and the highest in more than a decade (*Exhibits 1, 2*). Rising LFPR means more people are entering the labor force, looking to work. There are two interesting facts to note: 1) rural sector accounted for about four-fifths of the rise in LFPR, and 2) the rise in female LFPR contributed more than three-fifths of the increase in LFPR in 2020-21 (*Exhibits 3, 4, 5*).
- An increase in rural LFPR can be understood considering the reverse migration that happened during the past two years. As COVID spread, the migrant workers went back to their native places, as job markets in the urban and metro cities became uncertain. Nevertheless, what makes this narrative confusing is the fact that the rural female accounted for 57% of the increase in the labor force in 2020-21, while the rise in rural male labor force was much lower (*Exhibit 5*).
- Another interesting fact is that the rise in LFPR was inversely correlated with education profile of the population (*Exhibit 6*). LFPR among the illiterate population increased to 53.8% in 2020-21 (from 51.6% in 2019-20), while it fell to 67.9% (from 68.4%) for the most-educated section (i.e. post-graduate and above). These trends were similar across rural and urban sectors among males and females.
- **Internals of employment suggest weak labor market:** Not only LFPR, but India's worker-population ratio (WPR) for all ages also increased to 39.8% in 2020-21, the highest in more than decade (*Exhibit 7*). The rise in WPR was pervasive in all age groups – it rose to 55.7% for 15-59 year age groups in 2020-21 (*Exhibit 8*).
- The internals of employment, however, are not so encouraging. There are four trends: 1) like LFPR, WPR increased the maximum among the illiterate and low-educated groups, while it was broadly unchanged in the high-educated population (with secondary and higher education; (*Exhibit 9*), 2) like in 2019-20, the share of self-employed workers increased, while the share of regular wage/salaried workers declined in 2020-21 (*Exhibit 10*), 3) in one of the clearest signs of very weak employment, more than 80% of the rise was in the agricultural sector (*Exhibit 11*). The share of agriculture increased to 46.4% of total employment in India, while it declined for the manufacturing and services sectors, and 4) the number of workers engaged in the informal sector in the non-agricultural activities increased further to 79.4% in 2020-21, from 78.7% in the previous year (*Exhibit 12*).
- One of the positive developments, however, is in the conditions of employment. The percentage of regular wage/salaried workers engaged in non-agricultural activities with no written job contract fell further to 64.3% and who are not eligible for paid leaves declined to 47.9% in 2020-21. The share of regular wage/salaried workers who do not have any social security benefits (such as PF/pension, gratuity, healthcare, maternity benefits etc.), however, was stagnant at 53.7%. Overall, workers with none of these three conditions fell to 38.1% in 2020-21, from 39% in 2019-20 (*Exhibit 13*).
- In general, although India's LFPR and WPR increased sharply in 2020-21, they were primarily driven by low-educated population and concentrated in the low-skilled sectors (agriculture and construction). This is not something that has happened for the first time in 2020-21. As we had highlighted in our previous [research](#), in stark contrast to the advanced nations, there is an inverse relationship between India's employment/labor force and real GDP growth (*Exhibit 14*). This is largely because the expansion in labor force is driven by higher employment (*Exhibit 15*), which, in turn, is primarily happening in the low-productivity areas, riddled with disguised employment.

- In line with the economic model explained by Arthur Lewis in the 1950s, India is a dual economy characterized by two sectors – a relatively large unorganized sector and smaller organized sector. While the organized sector is driven by demand factors, the labor market in the unorganized sector is dominated by supply factors. It means that the unorganized sector is highly accommodative in the sense that whoever wants to join the labor market enters the unorganized sector as employed without affecting its overall output (as a corollary, labor productivity tends to fall). On the contrary, the organized sector represents modern profit maximizing firms operating in a competitive environment, and thus, it is a highly productive sector.
- During the high growth period, the demand for workers in the organized sector goes up, a relatively large part of which is supplied by the unorganized sector, and a small part is absorbed from the pool of educated/skilled unemployed. Further, a portion of the under-employed or disguised workers tend to leave the labor force, as the income growth improves during better GDP growth episodes. Therefore, in contrast to advanced nations and in line with Lewis model, labor force and total employment tend to fall during high-growth episodes. However, the internals tend to improve led by falling share of agriculture and construction sector, rising share of regular wage/salary workers, lower share of unorganized/informal workers and higher employment among educated sections.
- Moreover, although India's LFPR appeared unusually low – at 41.6% for all ages, the LFPR among the working-age population was decently high at 69.2% in 2020-21 (*Exhibit 16*). Further, while the LFPR among men was as high as 97% in the 25-59 years age group, it was only 42.4% for females (*Exhibit 17*).
- Unemployment rate does not hold too much value: Owing to these peculiarities of India's labor market, the information about unemployment rate does not hold too much value because low per capita income almost forces a large section of the population to remain employed, irrespective of the earnings or the quality of employment.
- Not surprisingly then, the unemployment rate for all ages fell to 4.2% in 2020-21 from 4.8% in 2019-20 (*Exhibit 18*). Although the youth unemployment rate (aged 15-24 years) remained high at 16.4% in 2020-21, it has come down sharply from 26.1% in 2017-18 (*Exhibit 19*).
- In conclusion, the combination of rising LFPR (or WPR), along with falling unemployment rate does not indicate strong labor market in India. In contrast, the details confirm that employment situation remains concerning in the country, due to which the agricultural and construction sectors have seen higher share in employment, explaining a large part of the falling productivity and thus, GDP growth.

Exhibit 1: India's LFPR rose to decadal high of 41.6% in 2020-21...

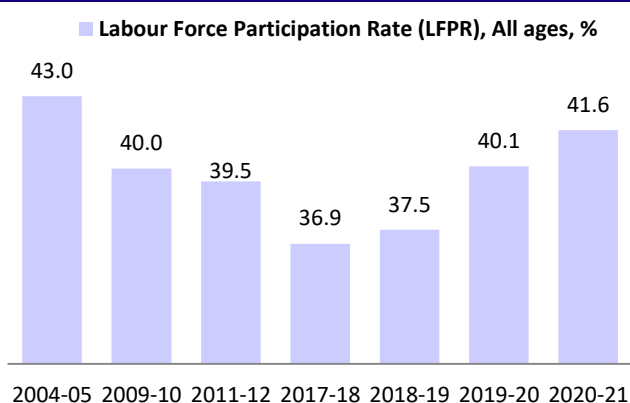
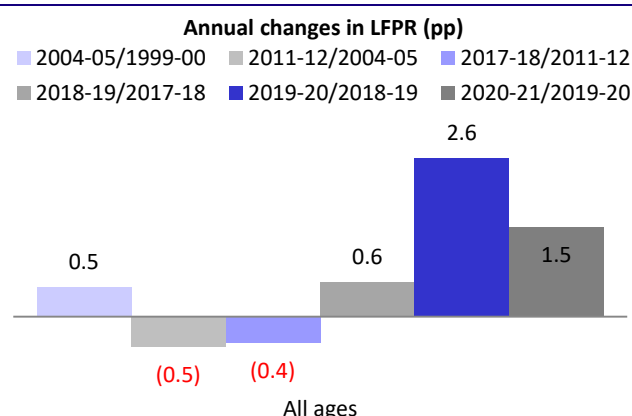
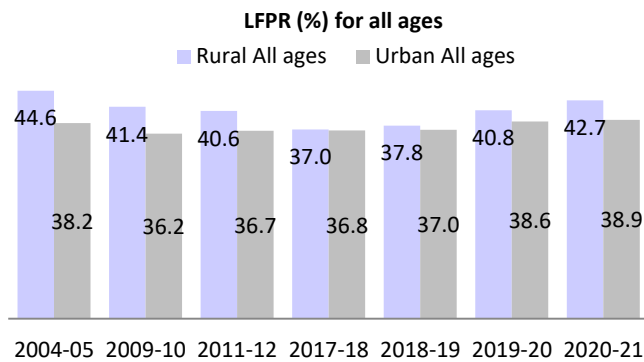
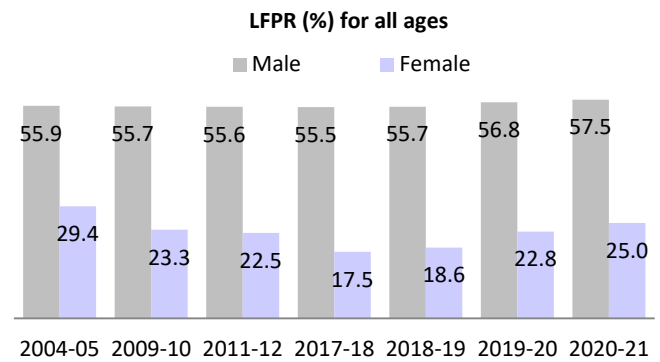


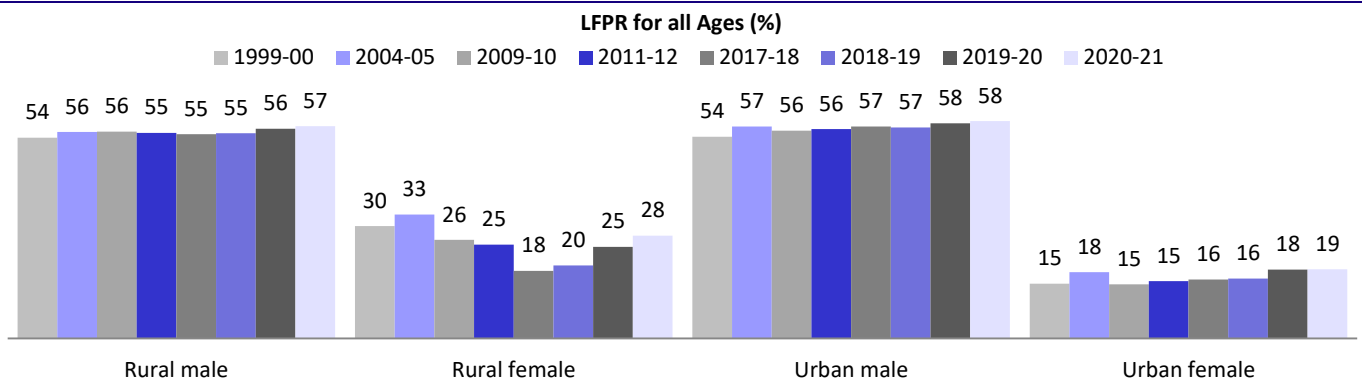
Exhibit 2: ...and the annual changes have been very high during the past two years



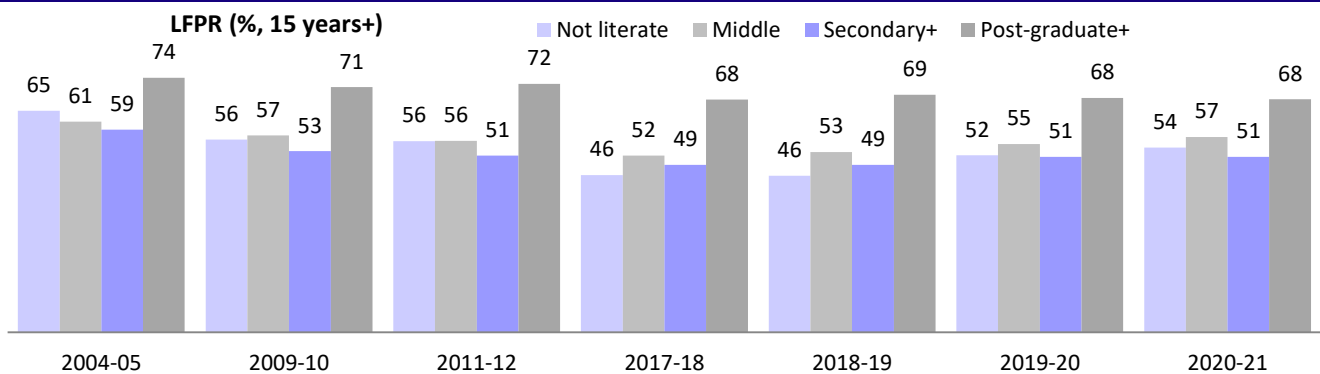
Source: PLFS, MOFSL

Exhibit 3: Rural LFPR rose faster than urban LFPR...**Exhibit 4: ...and female LFPR rose faster than male LFPR**

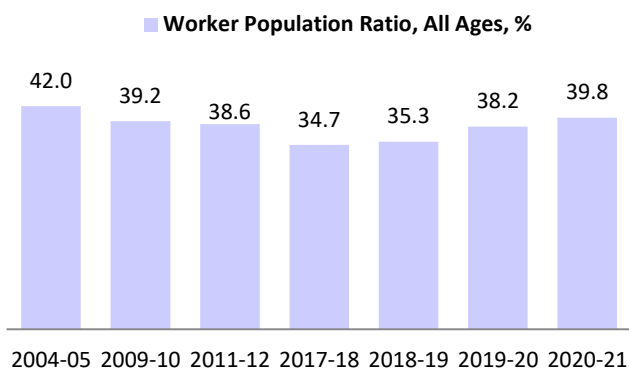
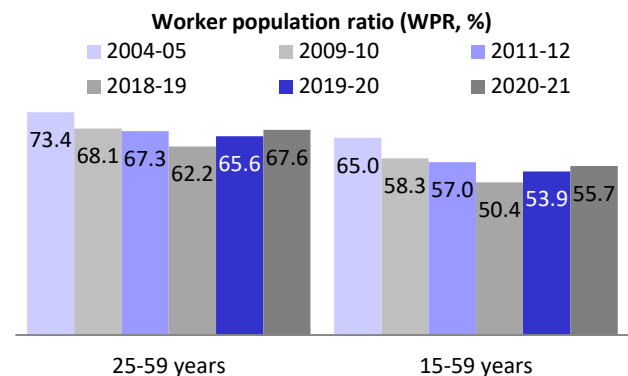
Source: PLFS, MOFSL

Exhibit 5: Most of the rise in all-India LFPR is attributable to females in India (both in rural and urban areas)

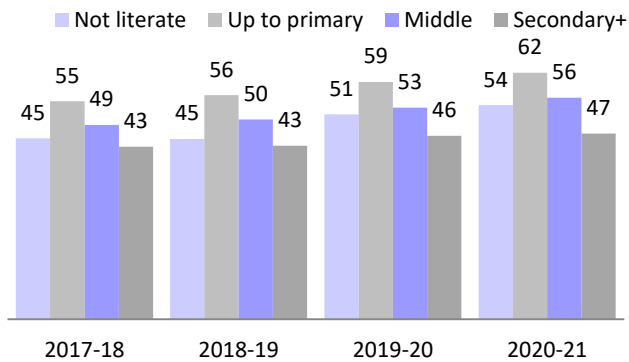
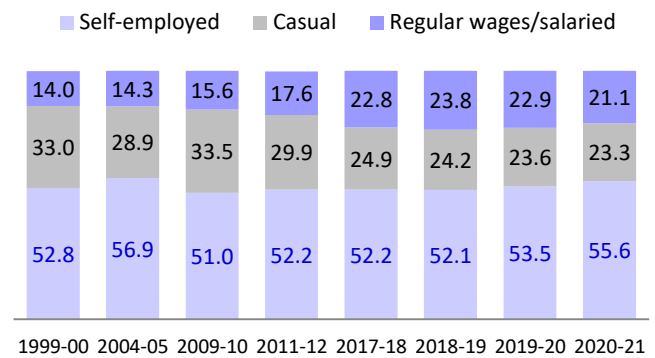
Source: RBI, MOFSL

Exhibit 6: LFPR among the higher educated class (post graduate+) of people actually declined in 2020-21

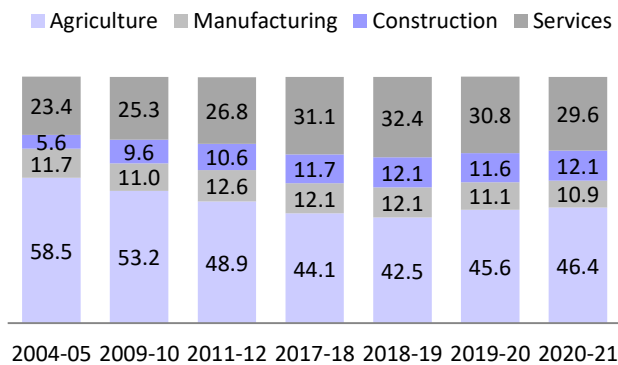
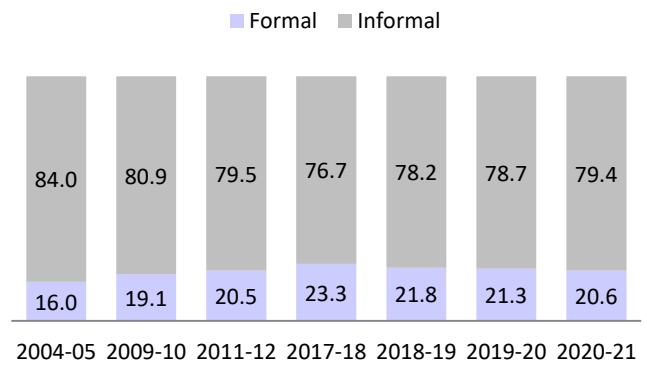
Source: RBI, MOFSL

Exhibit 7: India's WPR also rose to 39.8% in 2020-21...**Exhibit 8: ...and it increased in all age groups**

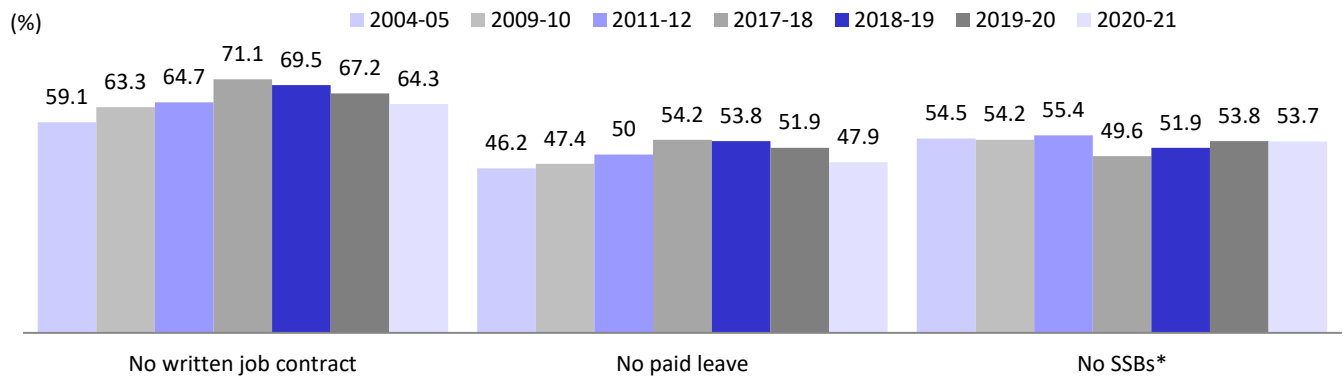
Source: PLFS, MOFSL

Exhibit 9: WPR high among illiterate and low educated**Exhibit 10: Share of self-employed has increased**

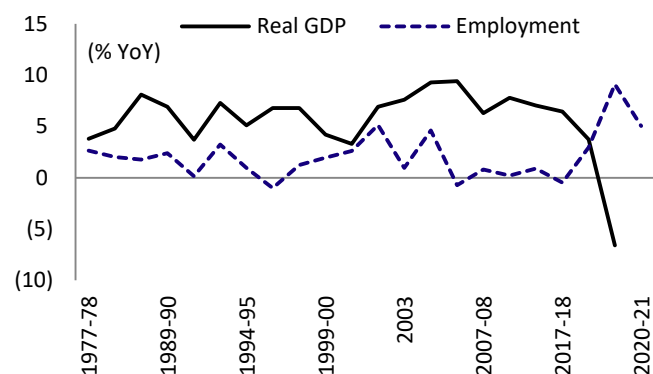
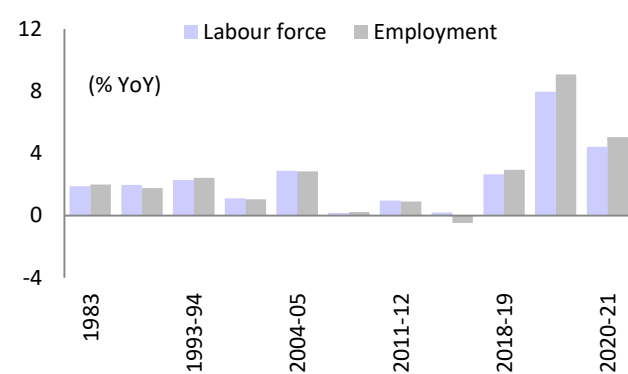
Source: PLFS, MOFSL

Exhibit 11: Most of the rise in WPR was in farm sector...**Exhibit 12: ...and thus, in the informal sector**

Source: PLFS, MOFSL

Exhibit 13: Working conditions of workers in India broadly improved in 2020-21

Source: PLFS, MOFSL L

Exhibit 14: Inverse relationship between real GDP and employment growth in India...**Exhibit 15: ...and the employment growth has exceeded labor force growth during most of the periods**

Source: PLFS, MOFSL

Exhibit 16: India's LFPR rose in both age groups (15-24 and 25-59)...

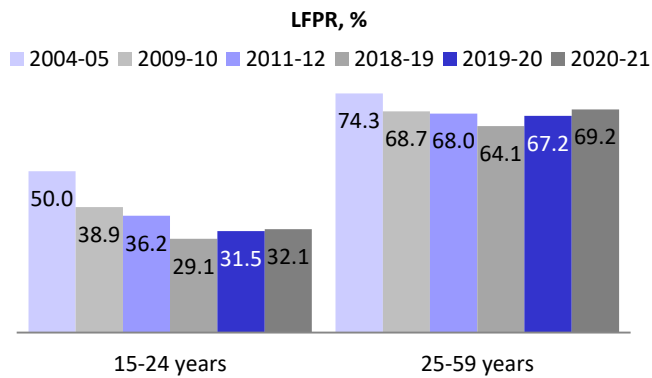
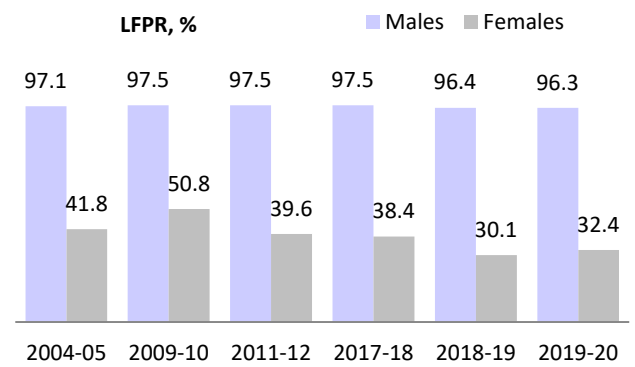


Exhibit 17: ...and the rise was seen majorly in females rather than males

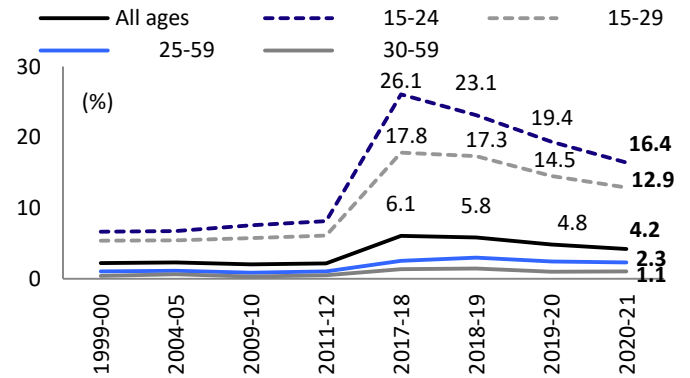


Source: PLFS, MOFSL

Exhibit 18: All-India unemployment rate across all ages declined to 4.2% in 2020-21 from 4.8% a year ago...



Exhibit 19: ...and the unemployment rate fell across all age-groups except 30-59 years



Source: PLFS, MOFSL

NOTES

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