

Labor Market Regulations and Jobs: Nepalese Experience

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Introduction

- Job most crucial for
 - Boosting living standards, raising productivity and fostering social cohesion (WB, 2013).
 - Labor often an only asset of a poor.
- However, the design and appropriateness of labor market laws and policies for jobs and productivity still debatable
 - Arguments in favor of flexible and deregulated labor market laws
 - Protective labor legislations distort markets, raise transaction costs, prevent adjustment in wages and other resources and hence spoil both investment and employment.
 - Protecting of insiders interest hurt chances of new entrances into the labor market resulting into social divide and upholding of inequality.
 - Regulation by lowering employment and productivity often hurts intended beneficiaries.
 - Labor market flexibility and deregulation, on the other hand, enhances both efficiency and equity.
 - Arguments in favor of labor market regulation
 - Competing firms often reduce their unit costs by lowering wages and labor standards with adverse effect on workers conditions.
 - Productivity through substitution of labor by capital makes very adverse effect on job creation
 - Mitigating market failures
 - Guarantying of minimum wages
 - Ensuring job security particularly to the most vulnerable.

Introduction

- The findings of empirical results are mixed and less conclusive.
 - Neither higher wages (Blanchflower and Oswald, 1995) nor stronger trade union rights reduce employment or hinder trade competitiveness (Kucera and Sarna, 2004).
 - Negative effect of rigid labor regulation on employment and productivity (Botero et al., 2004, Besley and Burgess, 2004 and Amin, 2009).
 - Job protection takes place at the expense of workers seeking job and prevents natural flow of workers between firms needed from adjusting to external shocks. On the other hand, flexible regulation increases net employment (Kaplan, 2009).
 - A study exclusively devoted to low income countries (LICs) finds more broadly a negative effect of regulations on formal employment but a compensating positive effect on informal employment. The study concludes that effect on the overall employment rates and unemployment is broadly ambiguous (Nataraj et al, 2012).
- In these backgrounds, based on earlier study findings, recent data and information, labor market regulatory rules and practices affecting jobs/employment is presented and discussed below in the Nepalese context.

Key features of labor market regulations in Nepal

- In Nepal labor market regulation is governed by the Labor Act of 1992 and Trade Union Act of 1993.
- The Labor Law 1992, however, covers only those firms and enterprises that employ 10 and above workers and hence leaves out the predominant informal labor market.
- More broadly, the Labor Law 1992 deals with
 - Matters relating to employment and security of employment.
 - Working hours and minimum wages.
 - Welfare of employees.
 - Employer employee relations and the settlement of labor disputes.
 - Labor Regulation, 1993 further clarifies issues associated with security of profession and service, remuneration and welfare provision, health, cleanliness and safety, etc.
- Some of the specific provisions related to labor market regulation and worker's rights include
 - Right to unionization and collective bargaining.
 - Right against gender discrimination and labor court.
 - Minimum wage fixation through tripartite agreement.
 - Permanent worker status after six months of employment.
 - Dispute settlement bilaterally or on a tripartite basis depending on the nature of dispute .
 - Some welfare, health, cleanliness and safety provisions.
- The Bonus Act of 1974, as amended subsequently, provides a legal basis for the payment of bonus to the workers and employees of factories and commercial establishments.
- A social insurance scheme in the form of Social Security Fund has been recently introduced which is yet to be implemented.
- There is no unemployment insurance as such.

Demographic and labor market characteristics

Main demographic characteristics include

- Reduced population growth rate to 1.35 % (2001-2011) from 2.3 % (1981-2001) but a higher labor force growth at about 2.3 % per annum.
- The overall labor force participation rate at 80.1 % including female participation rate at 79.4% .
- A higher share of youth population at 40.43 % (15-39).
- Rate of urbanization one of the highest in South Asia at 5 % per annum.
- Very high rate of migration in general and external migration in particular. Almost 53 percent families have at least one absentee member in a family with more than 33 percent out migration.

Main labor market features include

- Unemployment rate at 2.2 % but the underutilized rate at 30 % with 49.9 and 26.9 % urban and rural share respectively.
- Paid employee constitute 39.7 % followed by 36.5 % self-employed without regular employees and 19.8 % contributing family members (self employment almost 60.3 percent).

Demographic..

- Skill composition-only 1.7 % and 2 % are in professional and associate professional category and rest are in medium/low and elementary category.
- Never attended school workers constitute almost half in 'elementary occupation' and 'subsistence agriculture'. Such a ratio of female workers in such occupation is more than two-thirds.
- Exclusionary practices is high in the labour market with female employment ratio at 3.5 % in non-agriculture sector formal employment.
- More strikingly, the share of informal employment is about 96.2 % without job security.
- A positive development in the labor market , however, is in the wage front. During 1995 to 2010 compared to 2.9 fold increase in consumer prices (NRB, 2103), wages in the agriculture rose by 4.25 times as against 3.55 times increase in the non-agricultural sector wages (CBS, 2011). A rise from very low base is partly due to higher level of outmigration.
- Narrowing of wage gap between the urban and rural areas is another phenomenon. Data show that wage rate in the rural areas is higher by only 8 per cent in the agricultural sector and by 28 percent in the non-agricultural sector.
- A larger gap, however, is persistent between the male and female wage rate with male wage rate being higher by almost 37 percent in the agricultural sector and by 51 percent in the non-agricultural sector (CBS, 2011).

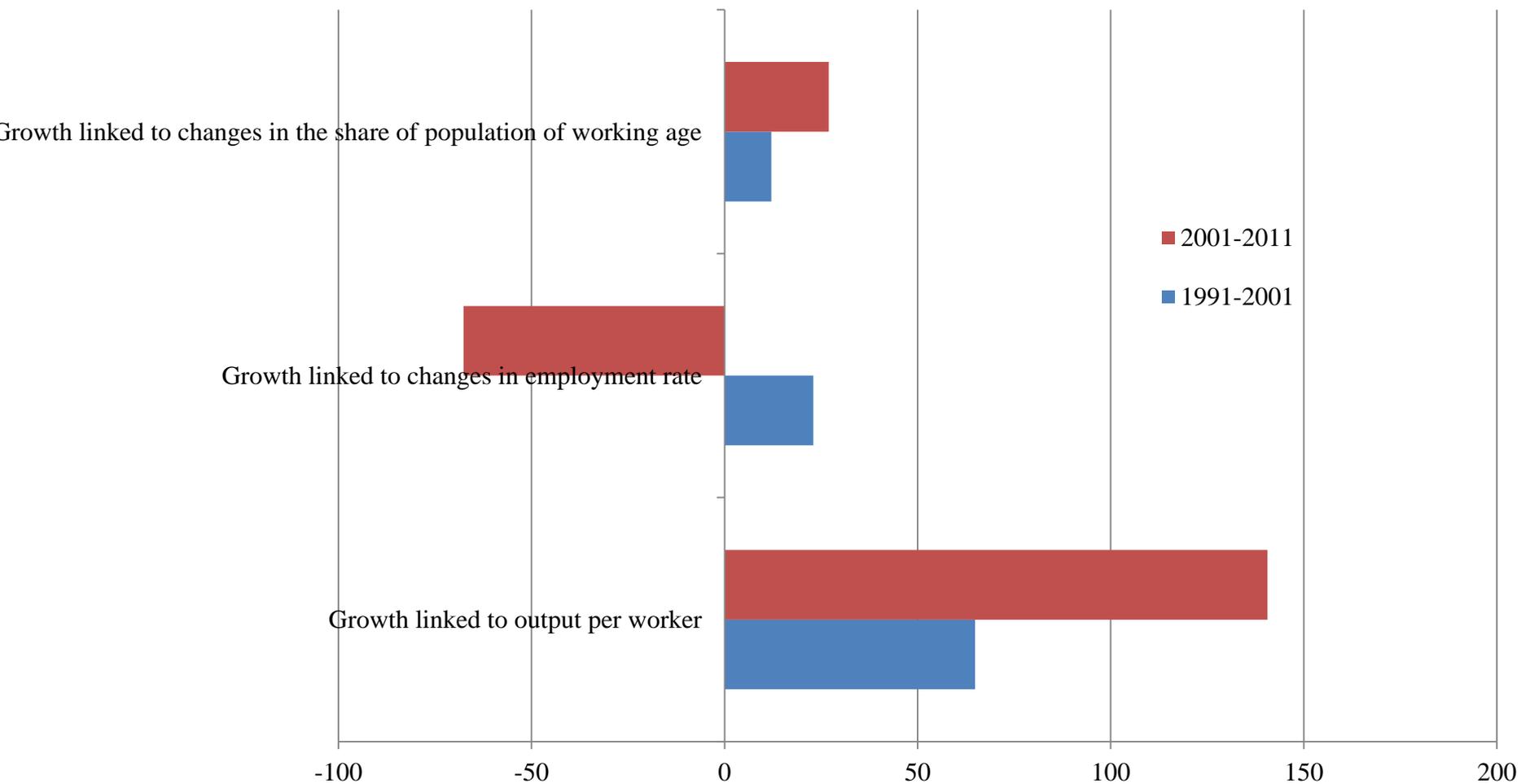
Trends in jobs and employment pattern

- A miserable job performance amidst long term growth rate of about 4 % on the average with a tendency of sharp fall in growth in the aftermath of earthquake followed by fuel and other supplies disruptions more recently.
- Growth and structure of employment (1991-2001 and 2001-2011)
 - Share of agricultural sector employment indeed increased to 66.67 % during 2001-2011 from 65.7 % during 1991-2001.
 - Contrarily, share of manufacturing and trade declined to 5.5 % and 8.1% from 8.8 and 9.9 % during the same period. Only in community and social services there was some jump from 8.6 to 12.8%.
 - On the other hand, employment grew at a rate of 2.7 % during 1991-2001 but reduced to just 0.6 % during 2001-2011.
 - During 2001-2011 employment growth in electricity, manufacturing and trade sector reduced by 16.0, 3.7 and 1.3 % respectively.
 - A modest growth in transportation and community sectors at 4.3 and 4.2 % per annum was recorded.

Trends...

- Employment elasticity (Khanal, 2015)
 - Overall 0.18 during 2001-2011 from 0.64 during 1991-2001.
 - Negative elasticity in electricity, manufacturing and trade at -4.85 , -1.83 and -1.43 respectively during 2001-2011 from 3.93, 2.15 and 2.58 during 1991-2001.
 - In sectors like transport, community services and construction a moderate elasticity at 0.74, 0.63 and 0.43 respectively during 2001-2011.
 - In agriculture and finance, 0.25 and 0.05 respectively during 2001-2011.
- A decomposition analysis examining the association of per capita GDP growth with changes in productivity, employment rate and demography corroborates that during 2001-2011, there was a "job- less growth" (Khanal, 2015).
- One additional phenomenon revealed is that the inter-sectoral shift of 2001-2011 had some adverse effect on productivity growth indicating that labor moved out from more productive non-agricultural sectors to agriculture or remained unemployed and largely opted for foreign employment (Khanal, 2015).

Aggregate Employment, Productivity and Demographic Profile of Growth (1991-2011)



Main aspects of labor market regulatory constraints in creating job and employment

- Despite counter arguments on social security and job safety grounds, the Labor Law 1992 governing labor regulation is quite rigid with net adverse effect on both job and productivity. This is corroborated by a number of studies.
 - Findings of the World Bank survey (WB, 2012) on leveraging the private sector for job creation and growth finds
 - Rigid regulations and unionization reducing incentives to hire workers through formal contracts is leading to high level of underemployment including higher migration abroad.
 - Minimum wages provisions with little differentiation across skill levels is adversely affecting labor productivity and investments in human capital.
 - ADB study (ADB, 2009) focused on development constraints finds
 - Rigid regulations induced multi-unionism is creating serious problems especially to the large scale manufacturing industries.
 - Like unions, employers' associations are equally politicized in Nepal.
 - A study examining industrial relations (Nepal et al, 2012) indicates
 - Political issues precedence over workers issues, limited dialogue, inter-union rivalry, difficult to establish an official trade union for collective bargaining , weak labor institutions and implementation problems are major hurdles in the areas of industrial relations.
 - Key findings of two related studies (Khanal, 2012 and 2015) include
 - Weak institutional framework and arrangements enforcing the law are very problematic amidst labor rigidity or flexibility centered debate.
 - Like the multi-unions, active employer's associations in key sectors like transport and retail trade practicing strong syndicate or cartel system are affecting firm's efficiency and productivity-a symptom of market failures.

Main aspects ...

- To avoid labor law compliance, there is an increased tendency of labor contract even in the organized sector.
- Predominance of informal labor market without social security and minimum wage guarantee amidst increased shift to the services sector employment is adversely affecting productivity growth potentials with additional constraints to job creation.
- Macro economic policy environment inducing capital intensive investment in unproductive areas including non-tradable activities is also a constraining factor from both sustainable growth and employment point of view. An input reallocation exercise further corroborated this.
- The World Bank doing business indices of the World Bank further depict that problems like enforcing contracts (152), getting credit (133), getting electricity (131) and paying taxes (124) are major constraining factors (World Bank, 2016). Noticeably, out of 189 countries, Nepal is ranked at 99 which is lower than other South Asian countries except Bhutan.

Some policy implications

- Need of more flexible labor market regulation by bringing about changes in existing act, regulation and related policies. But such a change needs serious consideration in several related fronts simultaneously.
 - Measures to enhance employable capacity of the unskilled workers for raising labor productivity and preventing labor market vulnerability.
 - Provision of unemployment insurance to support displaced workers which also would have positive effect on social protection.
 - Measures to discourage informalization practices through simplifying business complexities and minimizing cost of compliance.
 - Introduction of committed minimum wage floor as a fundamental principles and rights at work which covers all workers, regardless of whether they are in the formal or informal economy
 - More broadly social security to informal sector workers and explicit policy for transition to formality simultaneously.
 - Enough care on ways to strengthen institutional capability and enforcement mechanism that addresses problems of market failures and other market distortion practices.
 - System of regular information flow, dissemination and monitoring of labor market conditions.
- Make labor market policy as a part of macroeconomic policy including better macroeconomic policy environment for raising firm's efficiency and productivity through incentive environment to attract investment in labor intensive productive sectors.
- Simultaneous considering to other adverse factors affecting business environment that are hindering both growth and employment.