Critical Reasoning

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An unstated shift in Modi's economic direction

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"We are nudging industry to use less automation and more labour," said Finance Secretary T.V. Somanathan in a post-Budget interview. He was referring to the Narendra Modi government's Budget announcement of a new employment linked incentive (ELI) scheme for corporates. Under the scheme, companies will be provided a financial incentive for every new employee they hire. Dozens of commentators and experts have critiqued it and have questioned the assumption that a company will hire more people, merely for a financial incentive. This is a myopic and technocratic analysis that misses a fundamental shift in economic thought. The Finance Secretary's statement symbolises a significant and profound change in the economic policy direction of the Modi government. It signals a recognition of the misplaced faith in chasing GDP growth, the big capital-labour skew, and the need for course correction.

Initiatives that did not work well

For a decade, the Modi government's economic philosophy was the traditional Washington Consensus' trickle-down development model that emphasised the efficient production of goods and services, in the assumption that it would automatically lead to jobs, incomes and prosperity for people. When companies produce, GDP grows, and jobs are created, was the doctrine. 'Make in India', which was launched in 2014, was this quintessential example that aimed to spur manufacturing in the hope that it would make companies hire large numbers of workers. In 2019, the Modi government made a sudden off-Budget announcement of a big cut in corporate tax rates for companies, again in the hope that it would lure industry to invest more, which would then trickle down to more jobs. In 2020, the government announced a new production linked incentive (PLI) scheme of a whopping ₹2 lakh crore as financial incentives to be provided to companies based on the achieving of certain production targets. Once again, the intent was to incentivise companies financially to produce more, which would then lead to more jobs. Of course, we know now that none of these initiatives yielded the expected number of jobs. Companies either pocketed the tax cuts without investing or they invested more in equipment than in hiring people. Simply put, production incentives or tax cuts for corporates neither trickled nor dripped down to enough people through jobs and incomes.

ELI is a recognition of this failure and a change in course to provide direct incentives to corporates to employ people rather than through indirect trickle-down means. After all, if one agrees that production incentives can entice companies to produce more by lowering marginal production costs, then, by the same logic, employment incentives should propel companies to hire more people by lowering marginal labour costs. ELI must be viewed in the context of PLI and not as a standalone idea for job creation. PLI is an incentive for the economy to pour more into the top of a funnel. ELI is an incentive to collect more at the bottom of the funnel, which is the eventual objective anyway.

ELI is the first such policy of the Modi government that acknowledges the breakdown between GDP growth and jobs. If the ultimate goal of economic development is to improve the living standards of the median citizen, then the neo-liberal economic development paradigm of chasing GDP growth has run its course because it has stopped translating into jobs and prosperity for people. Which is why the bombastic rhetoric about India being the fastest growing economy in the world has no significance for the average Indian. The natural next step then is to call for direct policy interventions for jobs for people, rather than for economic output. And a PLI to ELI transition is the first attempt in this shift in economic direction.

The new ELI scheme for corporates is an acknowledgement by the Narendra Modi government of the breakdown between GDP growth and jobs

It can make a difference

ELI by itself may not incentivise corporates to create more jobs. But it can impact firm level decisions at the margin, of buying equipment versus hiring more people. Ceteris paribus, an ELI scheme encourages firms to hire people rather than use machines. When a million small, medium and large enterprises are 'ELI nudged' to choose labour over machines (capital), it can make a meaningful difference to overall job creation.

Neo-liberal economists, for whom technology-led productivity and efficiency are the cornerstones of economic development, would deem ELI blasphemous. Their argument is that it would render Indian companies less productive and, hence, less competitive globally. They are partially justified in their fears but the current model of development that prizes capital over labour and headline GDP over jobs is unsustainable in a democratic society.

Jobs deficit and ideas deficit

The shortage of jobs is the root cause of dangerous and foolhardy proposals such as the recent one in Karnataka to reserve all jobs for locals. When there are very few jobs generated overall in the economy, political compulsions in a democracy are bound to induce a mad rush to grab as many of the few available jobs for their voters. It is intellectually dishonest to merely criticise such proposals but not provide concrete ideas to create new jobs. India not only has a jobs deficit but also an ideas deficit to bridge the jobs deficit. The stock response by economists for creating more jobs is the much abused 'R' word – reforms. Their standard refrain is that a concoction of labour, education, skills and ease of doing business reforms is the magic pill to create more jobs, which is easier written than done.

ELI may or may not work to create additional jobs, but it is certainly a concrete new idea to alleviate the capital-labour imbalance and jobless growth woes of India's economy. More importantly, it marks a distinct shift in policy direction from trickle-down economics to bottom-up interventions. "India is ready for ELI, regardless of whose idea it is" was the last line in my article in a daily on the morning of Budget 2024. Just a few hours later, much to my utter surprise, Finance Minister Nirmala Sitharaman announced the ELI scheme in Parliament. ELI was proposed in the Congress's manifesto, and it is extremely laudable that the Finance Minister chose to keep politics aside to adopt this idea in the larger national interest.

Question -1) What is the underlying assumption in the Finance Secretary's statement about using less automation and more labour?

A. Automation is cheaper than hiring labour.

B. The current economic policies have successfully created jobs.

C. Financial incentives alone are enough to change company behaviors.

D. Increasing labour usage will lead to more job creation.

Question -2) Which of the following can be inferred from the passage about the Modi government's economic policies prior to the ELI scheme?

A. They were highly successful in job creation.

B. They focused primarily on GDP growth and production.

C. They were based on bottom-up economic interventions.

D. They led to significant improvements in living standards for all citizens.

Question -3) Which of the following, if true, would most strengthen the argument in favor of the ELI scheme?

A. Companies have historically responded positively to financial incentives.

B. Automation has led to a decrease in job opportunities.

C. The ELI scheme is similar to policies used successfully in other countries.

D. Companies are currently facing high marginal labour costs.

Question -4) Which of the following, if true, would weaken the argument that the ELI scheme will lead to significant job creation?

A. Companies find it cheaper to invest in automation than to hire new employees.

B. Previous incentive schemes did not yield the expected increase in jobs.

C. The global market favors companies with high levels of automation.

D. The scheme offers insufficient financial incentives to make a significant impact.

Question -5) What is the primary purpose of the passage?

A. To criticize the Modi government’s economic policies.

B. To highlight the success of the ELI scheme.

C. To discuss the shift in economic policy from production incentives to employment incentives.

D. To propose new economic reforms for job creation.

Question -6) Based on the passage, what is a potential drawback of the ELI scheme according to neo-liberal economists?

A. It might lead to increased unemployment.

B. It could reduce the productivity and global competitiveness of Indian companies.

C. It may result in higher operational costs for companies.

D. It might not be sufficient to counter the effects of automation.

Thank you for attempting!!!