



STAGNANT REAL WAGE GROWTH - ECONOMY

NEWS: A recent report by India Ratings Agency says that in UP and Haryana real wages have been growing at a mere 0.1 per cent.

WHAT'S IN THE NEWS?

- **Real Wages Growth:** In UP and Haryana, real wages are growing at a mere **0.1%**, indicating negligible or even negative growth.
- **Implication:** This signals a **stagnant economic environment**, leading to potential immiserization of workers.

Theoretical Framework: Terms of Trade

- **Prebisch-Singer Hypothesis:**
 - **Hans Singer** and **Raul Prebisch** independently argued that **commodity-exporting regions** face adverse terms of trade against **manufacturing regions**.
 - These regions sell commodities at low prices but buy manufactured goods at higher prices, leading to a **secular decline in income**.
- **Application to Indian States:**
 - Non-industrial states like UP and Haryana function like commodity-exporting countries within India.
 - They face **adverse terms of trade** when dealing with more industrialized states such as Maharashtra, Gujarat, and southern states.

Causes of Low Wage Growth

A. Poor Quality of Skills

- **Low Investment in Human Capital:**
 - Prolonged underinvestment in **nutrition, health, and education** results in a poorly skilled workforce.
 - Many individuals in these states are considered **unemployable** due to lack of relevant skills.
- **Potential Workforce:**
 - Even if **5% of the population is skilled**, large populations (e.g., 30 crore in UP) could provide a substantial workforce (~1.5 crore people).

B. Paucity of Capital Investment

- **Inadequate Capital Flow:**



- Limited capital investment leads to fewer opportunities for skilled labor, resulting in underemployment or out-migration to other states.
- **Example:** UP and Haryana send a significant portion of their skilled and semi-skilled workforce to other regions.

Importance of Attracting Capital

A. Capital as a Key Driver of Wage Growth

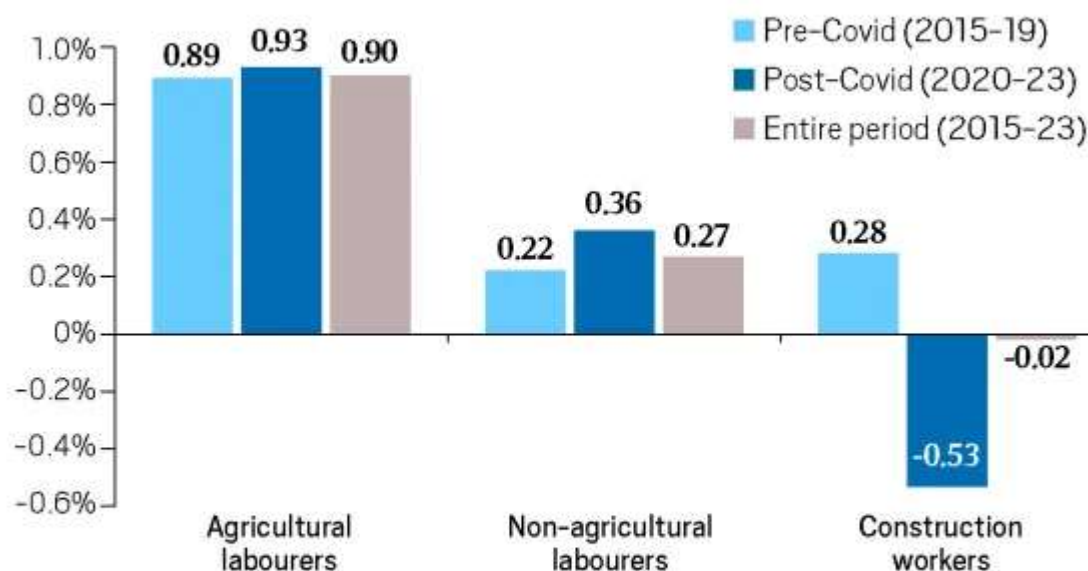
- States that attract higher **capital investment** experience better **wage growth**.
- Capital investment is more critical than merely improving **infrastructure or tax policies**.

B. Political Structure and Investment

- **Two-Party Systems Perform Better:**
 - States with **two dominant political parties** (e.g., Maharashtra, Gujarat, Tamil Nadu) are better at attracting capital and promoting manufacturing growth.
 - **Exceptions:** Madhya Pradesh and Rajasthan, despite having two-party systems, lag in manufacturing.
- **Multi-Party Competition:**
 - States like **UP, Bihar, Haryana, and West Bengal**, with intense political competition, struggle to attract investment due to **political instability**.



AVERAGE YEAR-ON-YEAR GROWTH OF REAL WAGES (% per year)



Source: Calculated from Labour Bureau data. Real wage = money wage deflated by CPIAL. Calendar years should be read as financial years (e.g. 2015-16 for 2015). Since 2014-15 is the baseline, estimates start in 2015-16.

Political Factors Influencing Investment

A. Unrealistic Minimum Wages

- **High Minimum Wages:**
 - Haryana sets **high minimum wages**, which deter potential investors despite good infrastructure.
 - Similarly, UP and other states suffer from distorted economic incentives due to political overreach.

B. Excessive Political Competition

- **Hyper-Competitive Environment:**
 - Over-competition among political parties leads to **policy distortions**.
 - **Outcome:** Misguided economic policies that hinder wage growth and discourage capital investment.

Conclusion

- **Capital Investment Crucial:** States with better policies to attract capital and investments experience higher wage growth and better economic outcomes.



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- **Balanced Political Competition Needed:** While political competition fosters democracy, **excessive competition** disrupts economic incentives, leading to adverse economic outcomes for citizens.



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