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Workfare programs and Private Sector wages: lessons from India

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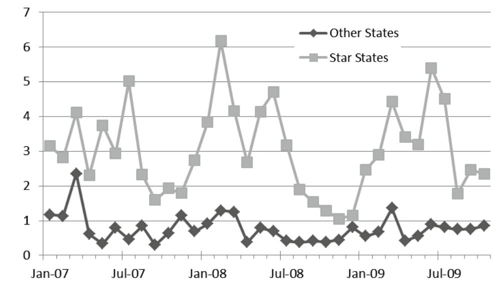
Many countries throughout the developing world have implemented workfare programs, i.e. social safety nets whose beneficiaries are hired on public infrastructures projects. Beyond their direct benefits to participants, these programs are likely to have indirect effects, through their impact on labor markets. We study India's National Rural Employment Guarantee Scheme, which is **the largest workfare program in the world today**. Using the gradual roll-out of the program to identify its impact, we show that it crowds out private sector work and increases wages for unskilled laborers. Our estimates suggest that the welfare gains from increases in equilibrium wages for the poor are large in absolute terms and large relative to the gains received solely by program participants.

THE NATIONAL RURAL EMPLOYMENT GUARANTEE ACT (NREGA)

In 2005, the Indian Parliament passed the National Rural Employment Guarantee Act (NREGA), which **entitled each rural household to 100 days of employment on public works per year**. There is no eligibility condition, and workers are paid according to each state's minimum wage legislation. The NREGA was described by the Prime Minister Manmohan Singh (Congress) as "the most significant legislation of our times." The program was introduced gradually across Indian districts from 2006 to 2009 and rapidly reached a massive scale; in 2012, official sources reported 51 million beneficiary households.

The quality of NREGA implementation varies considerably across states: as the figure shows, virtually all public employment is provided by five states (out of 28). The lack of administrative capacity constrains employment generation in some of the poorest states of India, where households need it the most (see Dutta et al. 2012). In the five "star" states however, the administration is able to respond to the demand for work. Employment provision in these states is highly seasonal, with more employment provided during the lean season of agriculture, between January and July, when work opportunities are scarce.

Figure 1: Seasonality of NREGA employment provision in star states and other states

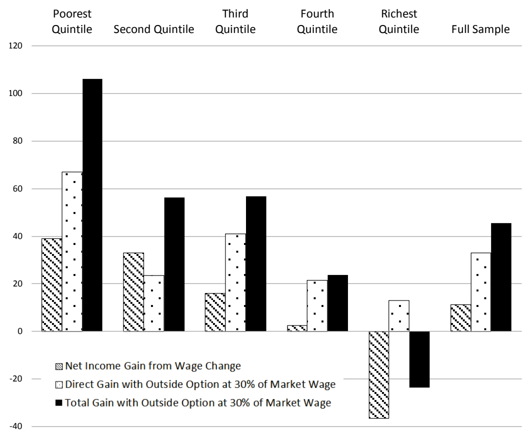


Source: Official reports on NREGA expenditures (monthly progress report). Star states are the five best performing states in NREGA implementation: Andhra Pradesh, Chhattisgarh, Madhy Pradesh, Rajasthan and Tamil Nadu

THE EFFECTS ON LABOR MARKETS

Comparing districts in which NREGA was introduced first to districts where it came into force later allows us to estimate **the impact of the program on rural employment.** We show that the introduction of the program is correlated with an increase in public employment, and an equivalent fall in private sector employment of about 1%. As a standard model of competitive labor markets would predict, we also find that the daily wage for casual work in the private sector increased by 5.5%. These effects are concentrated during the first half of the year and driven entirely by the "star" states. We use these estimates to compute the welfare impact of NREGA in each consumption quintile. We first consider gains from participation in the program and find that the poorest quintiles are more likely to benefit from public employment provision. We also consider the impact of a rise in private sector wages, which may affect all households, and show that it generates substantial welfare gains to the poor (30 to 60% of total welfare gains) and implies a welfare loss for the rich, who are net buyers of labor.

Figure 2: Welfare effect by Consumption Quintile



Note: Welfare gains are expressed in Indian Rupees, per household per month. See Imbert and Papp (2012) for more details.

IMPLICATIONS

Our research has important implications for the understanding of social programs in the developing world. This study is **one of the first to present direct evidence that the effect of a common social program on labor markets may be large**.

Our results suggest that workfare programs redistribute income to the poor directly through program participation and also indirectly through a rise in private sector wages. Hence, labor market effects should be taken into account while evaluating workfare programs' impact on poverty and inequality.

Picture: a Rajhastan NREGA working site, with the courtesy of Clement Imbert

Our findings also indicate that richer households are made worse off by the increase in labor costs. This explains why in some states, like Andhra Pradesh, farmers lobbied to keep public works closed during the peak season of agriculture. Manmohan Singh, who is also a Keynesian economist, hoped that in the end even private sector employers would benefit from positive externalities of public infrastructures. Unfortunately, field reports suggest the quality of NREGA infrastructures is quite poor and these effects have yet to be demonstrated.

Références

- Clément Imbert & John Papp, 2012. *"Equilibrium Distributional Impacts of Government. Employment Programs: Evidence from India's Employment Guarantee"*, PSE Working Papers

- Puja Dutta and Rinku Murgai and Martin Ravallion and Dominique van de Walle 2012 *"Does India's employment guarantee scheme guarantee employment?"* World Bank Policy Research working paper No 6003