

# The Labour Market in India: Where are MSMEs Placed?

*ISED Discussion Paper*

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by

ISED Small Enterprise Observatory

*jointly with*

ISED Centre for Social Development

**Institute of Small Enterprises & Development**

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## Preface

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Business start-up, in any economy is a powerful indicator of the growth of entrepreneurship resources. While employment is a central concern of today in most countries of the world, there are only limited options before the governments. Unlike this global trend, India as an emerging economy, has significant opportunities in expanding its base of self employment- induced job creation, which the country has neglected for long. Beyond a social goal, entrepreneurship is a critical resource in waiting for India. However, to tap this potential effectively, the country needs to move forward towards a concrete labour market policy.

The purpose of this Discussion Paper is to bring to light some of the least known aspects of the subject. It is also meant to initiate a wider discussion on the subject so that it may contribute to public policy and strategies.

This paper is the outcome of a project at the Institute of Small Enterprise and Development. The study was initiated by the ISED Center for Social Development, jointly with the ISED Small Enterprise Observatory. The support extended by the research team of the two Centers is gratefully acknowledged.

Cochin

February 23, 2017

P.M.Mathew

# The Labour Market in India: Where are MSMEs Placed ?

## *Abstract*

*Business start-up, in any economy, is a powerful indicator of the growth of entrepreneurship resources. While employment is a central concern of today in most countries of the world, there are only limited options before the governments; promotion of start-ups is one among them. Unlike this global trend, India as an emerging economy, has significant opportunities in expanding its base of self employment- induced job creation, which the country has neglected for long. Beyond a social goal, entrepreneurship is a critical resource in waiting for India. However, to tap this potential effectively, the country needs to move forward towards a concrete labour market policy. Though skill development and start-up promotion are keywords of the day, an integrated concept of entrepreneurship as a critical resource, and a policy approach that can fully harness the potential of this resource, are the imperatives of the times.*

*Key words: Start-up, entrepreneurship, labour market policy, skill development.*

## **1.0. Introduction**

The politics and the economics of micro, small, and medium enterprises, in any economy, converge at a particular point: start-up. It is the stage at which the orientation and achievement motivation of an individual get translated into action. This stage is also critical from the point of view of public policy, as the actions by the government at this stage act as a vital link between labour market policy and enterprise policy. The question as to why people start an enterprise, and why governments and promotional agencies make them start, are problematic questions that need closer examination and analysis. The purpose of the following pages is to analyze India's most recent experience, against the global developments in general, and of the experience of selected countries of interest to India.

## **2.0. Why Discuss the Labour Market?**

In any society, the supply of entrepreneurs is a critical factor that determines both economic growth and employment. Business start-up is essentially a labour market problem. However, supply of entrepreneurs, unlike creation of wage employment opportunities, is dependent on the individual decisions of entrepreneurs, on which the governments do not have much control. Therefore, an understanding of the basic nature of the labour market as also the specifics of policy, are crucial from the point of view of evolving effective strategies on start-ups, skills, and entrepreneurship. The shape of the labour market, thus, defines entrepreneurship potential as well.

While the labour market involves a two-way distinction on the basis of labour use, i.e., wage employment and self employment, the share of self employment is a reflection of two major forces: 1)the ecosystem under which

entrepreneurship gets groomed; and b) public policy, which facilitates or deters entrepreneurship to come up. An understanding of how these two major forces operates in the real world, necessitates a preliminary understanding of the labour market itself.

## **2.1. Basic Nature of the Labour Market**

Neoclassical economists view the labour market as similar to other markets, in that the forces of supply and demand jointly determine price (in this case the wage rate) and quantity (in this case the number of people employed). However, the labour market differs from other markets (like the markets for goods or the financial market) in several ways. Perhaps the most important of these differences is the function of supply and demand in setting price and quantity. In markets for goods, if the price is high, there is a tendency, in the long run, for more goods to be produced until the demand is satisfied. With labour, overall supply cannot effectively be manufactured because people have a limited amount of time in the day, and that people are not manufactured.

## **2.2. Social Marginality and Entrepreneurship**

In the USA for example, roughly 25 per cent of successful high-tech start-ups, over the last decade, were founded or co-founded by immigrants, where, Indians have played a key role. Studies by the Kauffman Foundation concludes that, if there is a happy coincidence of high-IQ risk-takers in government and a society that is biased toward high-IQ risk-takers, one gets an above-average returns as a country. What is common to Singapore, Israel and America, is that they were all built by high-IQ risk-takers and all thrived but only in the US, did it happen at a large scale and with global diversity.

Business is part of society and reflects its values. The very



Put another way, differences in compensation for labour arise only on the supply side.

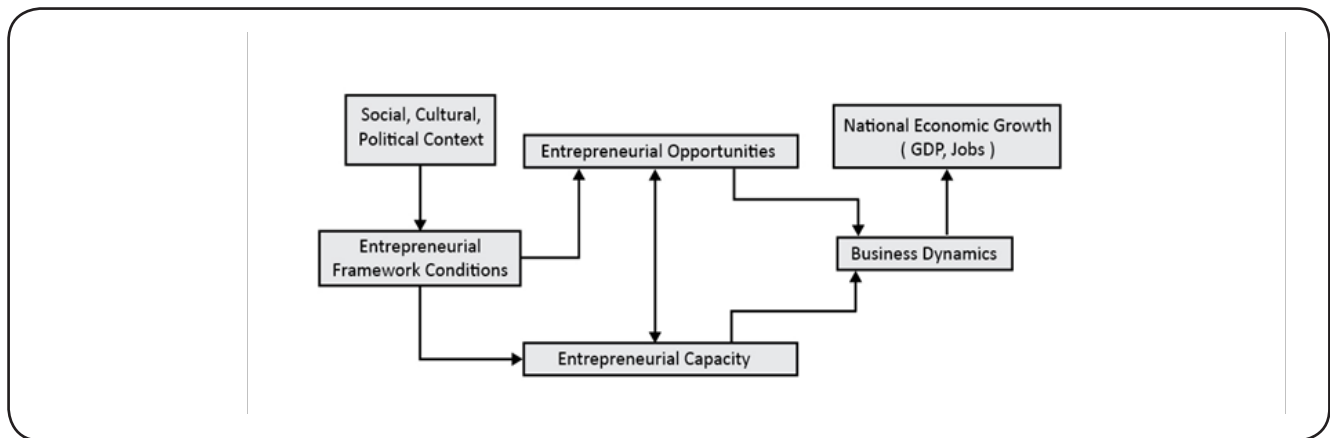
In the theory of labour market segmentation, there exists important differences on the demand side which imply differences in compensation and the like that are not explained by individual workers' characteristics. Since labour markets are far from perfect, non-market institutions such as craft unions and professional associations play a role, as do the different strategies employed by employers, in producing different results for workers with similar characteristics. Labour market segmentation splits the aggregate labour market between the primary sector and the secondary sector. In a primary sector, the workforce as a whole is motivated to serve their employer because of wages, health benefit, and pension and job security. Job market consists of majority blue collar jobs. The primary sector generally contains the higher-grade, higher-status,

and better-paid jobs, with employers who offer the best terms and conditions.

### 2.3. Employability

Having full employment as a goal, is understandable at the policy stage. But, it is important that the policy be translated into strategies. 'Employability' is a key item in the tool of analysts and policy makers today. The term, 'employability', is used in a variety of contexts, with a range of meanings. Hence, it can lack clarity and precision as an operational concept. In simple terms, employability is about being capable of getting and keeping fulfilling work. More comprehensively, employability is the capability to move self-sufficiently within the labour market to realise its potential through sustainable employment. For the individual, employability depends on the knowledge, skills and attitudes they possess, the way they use those assets, and present them to employers and the context (e.g.

**Figure 1: Model of Entrepreneurial Processes Affecting National Economic Growth**



Source: Reynolds P.D, M.Hay, S.M.Camp, *Global Entrepreneurship Monitor, 1999 Executive Report*, p.10

ordinariness of entrepreneurship in American commerce suggests that society prizes originality and improvement, and the human traits that enable both. Thus, entrepreneurship transcends business practice. It's a distinctive kind of human agency that derives from business but can operate in any realm of human endeavour. Entrepreneurship also is a basic exercise in social responsibility. To suppress or constrain innovation and improvement— and their implementation—ignores a society's needs and wants, holds it back, and diminishes its future.

The labour market also acts as a non-clearing market. While, according to neoclassical theory, most markets have a point of equilibrium without excess surplus or demand, this may not be true of the labour market: it may have a persistent level of unemployment. Contrasting the labour market to other markets also reveals persistent compensating differentials among similar workers.

A labour market is seen as segmented, if it "consists of

various sub-groups with little or no crossover capability". Segmentation can result in different groups, for example men and women, receiving different wages. A similar, almost synonymous concept is that of a **dual labour market (DLM)**. However, as the word "dual" implies, a DLM usually refers to two parallel markets, whilst segmentation in the broadest sense may involve several labour market Business and Value System. The theory of labour market segmentation contrasts with the view of neo-classical economic theory, which posits the existence of a unified market for labour, consisting of buyers and sellers in open competition with each other. The labour market is seen as functioning in the same way as other markets. In this model, the only difference between different workers' wages and conditions arise from individual differences in their human capital (skills, experience, or formal education) or tastes. On the latter, as part of the theory of compensating wage differentials those who prefer risky or dirty jobs receive higher wages.