

# CHAPTER 1

## INTRODUCTION

Poverty alleviation has been one of the guiding principles of the planning process in India. A significant share of public resources is spent on programs targeted at the poorest sections of the population. Such programs transfer assets and skills to people for self-employment, provide employment during times of distress and reduce the adverse effects of high food prices, and these programs have played a crucial role in reducing poverty and improving health and educational outcomes of the population.

Agricultural labourers, small and marginal farmers, and casual workers engaged in non-agricultural activities in rural areas constitute the bulk of the poor in the country. Small land holdings and their low productivity are one of the main causes of poverty in the country. Further, due to poor physical and human capital base, a large share of the population are forced to seek employment in sectors with extremely low levels of productivity and wages. The creation of employment opportunities for the unskilled workforce has been a major challenge for policy makers in India. We begin with a discussion on trends in poverty and inequality in India before coming to the main focus of the thesis, and towards this end the findings of an important paper are presented in the next few paragraphs.

Mahendra Dev and Ravi (2007) have examined changes in poverty and inequality during the pre (1983-94) and post reform (1993-2005) periods, and their findings provide a good basis to understand the dynamics of poverty and inequality in India. According to the study the rate of decline in total (rural and urban) poverty is not higher in the post-reform period as compared to the pre-reform period. This is also true for rural poverty. On the other hand, the rate of decline in urban

poverty was slower in the post-reform period. Further, inequality in consumption has increased significantly for both rural and urban areas in the post-reform period – the rate of increase being much higher for urban as compared to rural areas. The authors' estimates of decomposition of poverty into growth and distribution show that the increase in inequality has reduced the rate of decline in poverty in the post-reform period. Poverty declined in almost all the states in the pre- and post-reform periods. In spite of the reduction in poverty some of the states have very high poverty ratios. Estimates reveal increasing concentration of poor in a few states. A group of four states comprising Bihar, MP, Orissa and UP had a share of 49.8 percent in the rural poor of the country in 1983. This share increased to 55 per cent in 1993-94 and further to 61 per cent in 2004-05. Growth rates in Gini coefficient for the total (rural and urban) shows that inequality either increased or the rate of decline was slower in 13 out of 17 states in the post reform period as compared to the pre-reform period. Gini coefficient in urban areas increased in 15 states during the same period. The study finds widening disparities between rural and urban areas in the post reform period. Rural monthly per capita consumption expenditure (MPCE) as per cent of urban MPCE declined from 66 per cent in 1983 to 61 per cent in 1993-94 and to 56 per cent in 2004-05 at the all-India level. This percentage declined for majority of the states over time. The study finds a positive relationship between the rate of decline in poverty and rate of growth in MPCE. In the urban areas the positive relationship between growth in MPCE and decline in poverty seems to be weaker than that for rural poverty. States which have low poverty ratios had high income and Gini elasticities, implying that growth alone would not be sufficient for reduction in poverty and policies that reduce inequality are also important in these states. On the other hand, states such as Bihar, Orissa, UP and MP which have high poverty ratios show low income and Gini elasticities implying the need for higher growth in these states. Thus, the main conclusion that emerges from the study is inclusive growth that increases agriculture and non-farm sector growth, and leads to reduction in regional, rural-urban and social disparities is important for poverty reduction. Human development is equally important

for poverty alleviation, and therefore, policies that have positive effects on growth and equity have to be followed.

India spends significant amount of resources on rural development. The total budgetary allocation for all rural development programs in 2009-10 was Rs 74,270 crore (1.1 percent of GDP), which accounted for 31 per cent of the total Central Budget Plan provision. Rural development programs cover employment programs, such as the Mahatma Gandhi National Rural Employment Guarantee Act (MGNREGA) and the Swarnjayanti Gram SwarozgarYojana (SGSY), housing via the Indira AwaasYojana (IAY), sanitation via the Total Sanitation Campaign (TSC), provision of drinking water via the National Rural Drinking Water Program, watershed development via the Integrated Watershed Management Program, road connectivity via the Pradhan Mantri Gram Sadak Yojana, electrification via the Rajiv Gandhi Grameen Vidyutikaran Yojana , and social security via the National Social Assistance Program, the Indira Gandhi National Widow Pension Scheme (IGNWPS), and the Indira Gandhi National Disability Pension Scheme (IGNDPS).

Wage employment programs, an important component of anti-poverty policies, have sought to achieve multiple objectives. They not only provide employment opportunities during lean agricultural seasons but also in times of floods, droughts and other natural calamities. They create rural infrastructure which supports further economic activity. These programs also put an upward pressure on market wage rates by attracting people to public works programs. While public works programs to provide employment in times of distress have a long history, major thrust to wage employment programs in India was provided only after the attainment of self-sufficiency in food grains in the 1970s. The National Rural Employment Program (NREP) and the Rural Landless Employment Guarantee Program (RLEGP) are examples of early wage employment programs.

The MGNREGA is the world's largest rights based public works program. The program started in February 2006, after the National Rural Employment Guarantee Act was passed in 2005, in the 200 most backward districts of India. It was extended to an additional 130 districts in the first year of the Eleventh Plan (2007-08) and to the entire country in 2008-09. MGNREGA entitles each rural household to seek 100 days of employment every year. A brief overview of the performance of MGNREGA is given in Table 1.1. As Table 1.1 shows on average more than 3 crore rural households were provided employment per year under the scheme between 2006-07 and 2009-10. It is estimated that in 2009-10 nearly 5 crore families would be provided around 300 crore man-days of work under the program. This is more than three times the employment created by the rural employment program in 2006-07. From its inception in 2006 till September 2009, the program has provided nearly 600 crore man-days of work at a total expenditure of around Rs 70,000 crore. There has also been an increasing trend in the average program wage rate during this period. MGNREGA has a strong mandate that the shares of labour and other costs should not exceed 60 and 40 percent of total program costs, respectively. The program explicitly prohibits contractors to ensure high employment intensity. The works undertaken through MGNREGA like water harvesting, groundwater recharge, drought-proofing have the potential to increase land productivity and thus rural incomes.

**Table 1.1: Performance of MGNREGA (2006-07 to 2009-10)**

	2006-07 (200 districts)	2007-08 (330 districts)	2008-09 (615 districts)	2009-10 (619 districts till Sep. 2009)
Households employed (crore)	2.10	3.39	4.51	3.26
Man-days of employment generated (crore)	90.50	143.59	216.32	128.24
Work provided per year to households who worked (days)	43.00	42.00	48.00	39.00
Central release (Rscore)	8,640.85	12,610.39	29,939.60	16,006.23
Total funds available (including opening balance) (Rscore)	12,073.55	19,305.81	37,397.06	28,664.31
Budget outlay (Rscore)	11,300.00	12,000.00	30,000.00	39,100.00
Expenditure (Rscore)	8,823.35 (0.21)	15,856.89 (0.32)	27,250.10 (0.48)	15,737.40 (0.24)
Average wage per day (Rs)	65.00	75.00	84.00	88.00
Total works taken up (lakh)	8.35	17.88	27.75	25.21
Works completed (lakh)	3.87	8.22	12.14	6.39

Source: Mid term appraisal of the Eleventh Five Year Plan, Planning Commission; figures in parentheses are percentages of current GDP

A salient feature of the program is that it has benefitted socially disadvantaged groups, rural women and differently-abled workers, although some states have performed better than others in this respect. The share of Scheduled Caste (SC) and Scheduled Tribe (ST) families in the work provided under MGNREGA has ranged between 51-56 percent, while 41-50 percent of the workers were women. As many as 8.50 lakh differently-abled workers have so far registered for work. The program has led to financial inclusion in rural areas. Nearly 9 crore bank/post office accounts of the poorest people have been opened for MGNREGA payments and around 85 per cent of MGNREGA payments are made through this route. The program has however not been able to meet its objective of providing 100 days of employment. The number of days provided work under the program varies across states. The national average was 48 days in 2008-09 and as many as 15 states fall below the national average (see Table 1.1). Only 14 per cent of worker households completed 100 days of work.

Wage employment programs provide only short-term relief to the poor. Long term sustainable poverty reduction in underdeveloped regions can come about only if other sectors of the economy grow rapidly. It is imperative therefore to ensure that the growth process is inclusive and pro-poor. Agricultural growth still holds the key to poverty alleviation in India. The ultimate potential of MGNREGA lies in improving the productivity of agriculture. Millions of small and marginal farmers are forced to work under MGNREGA because the productivity of their own farms is no longer enough to make ends meet. MGNREGA can become a really powerful policy tool if it helps to rebuild the decimated productivity of small farms and allows small and marginal farmers to return to full-time farming, thereby also reducing the load on MGNREGA. The First Annual Report of the National Consortium of Civil Society Organizations on MGNREGA (2009) has reported that earthen dams on common land have recharged wells of thousands of poor farmers who earlier

worked as labourers to build these dams. These farmers are now busy making investments to improve their own farms.

In brief the potential of MGNREGA to lower poverty is enormous despite daunting challenges, including the quality of the assets it creates. However, Dreze and Kerah (2008) after acknowledging problems with the quality of the assets suggest that the return on MGNREGA investments might not be inferior to the return on many other investments elsewhere in the economy. Moreover, they argue that it is not necessary to change MGNREGA rules for asset creation and that the quality of assets can greatly be enhanced with affordable, well directed research and development.

India and MGNREGA need to create the necessary capacities and institutions to effectively guarantee employment and efficiently build productive assets. Administrative, managerial, technical capacities need to be strengthened. Institutions for community participation, democratic decision making, transparency and anti-corruption need to be created and reinforced. If the benefits of an employment guarantee scheme were short term poverty alleviation one could look for an alternative lower cost program such as conditional cash transfer. However, if the scheme can reduce long term poverty by creating productive assets then it is worthwhile to bear the higher costs.

The above discussion thus points to the different roles MGNREGA could play in the economy. Specifically, MGNREGA could reduce poverty and inequality, reduce the rural-urban divide in income/consumption, boost growth by creating productive assets in rural areas, and provide an alternate source of employment for the rural poor during the agricultural off season. At the same time investments in MGNREGA are associated with large opportunity costs for the economy. Keeping in view the above the main objective of this study is to analyze the efficiency and equity

implications of MGNREGA using an economy-wide framework. A static multi sectoral computable general equilibrium (CGE) model will be used for conducting the analysis. A CGE model is an ideal tool for estimating aggregate economic impacts of specific policies, and the intention of this study is to find answers to the following research questions –

1. What are the efficiency and equity implications of MGNREGA? Can MGNREGA lower disparities between rural and urban income/consumption levels?
2. How do alternate ways of funding MGNREGA affect the efficiency and equity implications?
3. What are the efficiency and equity implications if MGNREGA is accompanied by the creation of productive assets in rural areas?
4. What is the potential of MGNREGA as a hedging tool against adverse agricultural productivity shocks?
5. How do investments in MGNREGA compare with investments in other sectors of the economy?

There are relatively few studies that have analyzed MGNREGA in an economy-wide framework, and it is hoped that the answers to the above research questions will give us an indication of the true potential of MGNREGA as a tool to alleviate poverty and inequality in India.

The rest of the thesis proceeds as follows. The next chapter (Chapter 2) provides an overview of employment guarantee programs in India and abroad. Chapter 3 discusses the relevant literature. Chapter 4 is devoted to model and data. Chapter 5 presents and discusses the findings of the study, and finally Chapter 6 mentions the conclusions and policy implications.