CHAPTER II

URBAN LABOUR MARKET
THEORETICAL ANGLE
2.1. INTRODUCTION

In this chapter an attempt is made to briefly discuss the dynamics of urban labour market with reference to developing economies. It is attempted to trace the origin of the concept of dualism and its relationship with labour market issues such as Urban Labour market and migration, structure of sectoral earnings, labour absorption, access and mobility are also discussed.

2.2. CONCEPTUAL FRAMEWORK

2.2.1 DUALISM AND LABOUR MARKET

In the process of economic development in many developing countries, a modern commercialised industrial sector has developed alongside a traditional subsistence agricultural sector, resulting in a dual economy. In this context, it is aptly said that "in the controversial field of economic development, one of the few areas of agreement is over the existence of multiple labour markets in many developing countries. People who cross swords on the subject of the existence of surplus labour and disguised unemployment, nevertheless seem to agree on the prevalence of gap in wages (and labour costs) in different sectors of the underdeveloped economy.1 Despite such universal acceptance on the existence of multiple (or dual) labour markets, there is no such consensus regarding its nature and causes. Analogously, the development of these sectors and the associated labour transfers in the developing countries have been a subject of discussion amongst the development economists.

2.2.2 BOEKE'S CONCEPT OF DUALISM

Boeke2 has pioneered the Dualistic Theories with his classical explanation of the concept of dualism. According to him dualism refers
to the co-existence of an urban market economy, and the subsistence rural economy. He observed that the precapitalistic sector of the eastern economy in contrast to the 'homogeneous', western economy is characterised by backward sloping supply curves of effort and risk-taking. This behaviour is the result of a different value system of the 'eastern' or 'oriental' societies. He also held that dualism arising out of the penetration of a 'western' enclave into the traditional society is fundamental and permanent and is not amenable for change. Thus, Boeke stressed the need for a distinctive economic and social theory for underdeveloped countries.

2.2.3 Higgins on Dualism

As an alternative to Boeke's sociological theory of Dualism, Higgins has emphasised the theory of technological dualism. He observed that one of the most important effects of dualistic development is its influence on the pattern of employment. To him labour employment problems are the results of the existence of technological dualism - the use of different production functions in the advanced and the traditional sectors. Thus, Higgins pointed out that 'dualism' is associated with 'structural unemployment' or 'technological unemployment'.

2.2.4 The LFR Model

Another well-known Model of development that considered the process of rural-urban transfer was developed by Lewis⁵, and later modified by Fel and Ranis⁶,⁷. In sharp contrast to Boeke's formulation, they laid emphasis on the structural differences with a socio-economic basis, in explaining their model of traditional and modern sector dualism. They have used the concept of dualism to investigate how surplus labour can be transferred from the rural subsistence sector to the growing modern sector. The modern capitalist sector is considered
as a dynamic one whose growth is brought about by output expansion and reinvestment of profits that accrue to the capitalists. The speed with which labor transfer and employment growth takes place is determined by the capital accumulation rate in the modern industrial sector. It is also assumed that capitalists reinvest all their profits.

In the rural subsistence sector marginal productivity is assumed to be near zero or even negative. As a result wages would stagnate at lower level. On the other hand, in the urban industrial sector wages are assumed to be determined as a fixed premium over a constant subsistence wage in the traditional agricultural sector. At this ruling wage rate or supply price, the supply of labor force is considered to be perfectly elastic (due to the presence of disguised unemployment and underemployment) in the traditional sector. As modern industrial sector grows, perfectly elastic supply of labor comes forth at these constant real wages. Thus the increased capital formation and improved technology in the modern sector will not raise the wages but raise the share of profits which are reinvested in the growth of the industrial sector itself. Thus the process of growth of the Modern sector and expansion of employment will continue until the entire surplus rural labour is absorbed in the urban industrial sector. Afterwards, the labour supply curve becomes positively sloped and both urban wages and employment continue to grow. The following diagram illustrates the LFR Model of growth and employment in a dual labour surplus economy.

![Diagram 2.1: Quantities of Labour](image-url)
On the horizontal axis we have quantity of labour and on the vertical axis the real wage and marginal product of labour (assumed to be equalised in the competitive modern sector) OA represents the average level of real subsistence income in the traditional rural sector OW is the real wage in the urban industrial sector At this wage, the supply of labour is assumed to be perfectly elastic and is represented by WS In the initial stages of growth, with a given capital investment, declining marginal product is shown by Curve-D1 (k1).

Since profit maximising modern sector employers are assumed to hire labourers up to the real wage (i.e., the point F of intersection between the demand and supply curves of labour), total modern sector output is given by the area OD1 FL1. Out of this total wages, paid to the workers equal the area of rectangle OWFL1, the residual surplus output shown by the area WDF1 would form profits that accrue to the capitalists. Since it is assumed that all these profits are re-invested in the modern sector, the total capital stock in it will rise from K1 to K2. This causes the total product curve to rise from K1 to K2. This causes the total product curve to rise and induces the marginal product demand curve for labour to shift upwards to line D2 (K2). A new equilibrium urban employment level is established at point G with OL2 workers employed. This causes total output to rise to OD2 GL2 while total wages and profits increase to OWGL2 and WD2G respectively. If once again these profits are reinvested, capital stock will increase to K3 which in turn leads to a shift in the labour demand curve to D3(K3). This raises the level of employment in modern sector to L3.

Though this two-sector development model is based on the historical experiences of economic growth on the West, it has three key assumptions which are at variance with the available empirical evidence of the growth process in the developing countries. First, the model implicitly assumes that the rate of labour transfer and employment in
the urban Modern Sector is proportional to the rate of urban capital accumulation. The faster the rate of capital accumulation, the higher will be the rate of growth of the modern sector and the faster will be the rate of labour absorption. This may not hold good if profits are invested in more sophisticated labour saving capital equipment. Though Lewis has recognised the role of technical progress, he disregarded the possibility of any impact of it, regardless of whether the new knowledge in capital saving (and thus equivalent to an increase in capital) or labour saving (and thus equivalent to an increase in the marginal productivity of labour)\(^0\). Thus if additions to capital stock embody labour saving technical progress the new demand curve (D\(_2\)K\(_2\)) for labour will now have a greater negative slope than D\(_1\) (K\(_1\)) as can be seen from figure 2.2. Even if total output grows substantially (i.e., OD \(_{EL}\) is significantly greater than OD\(_{EFL_1}\)) total wages (OW\(_{EL_1}\)) and total employment (OL\(_1\)) remain unchanged when there is a labour-saving technological progress. Thus, the total benefits of economic development will accrue to the capitalists only when there is labour-saving technological progress. In contrast to the assumption made by the model.

![Diagram 2.2](image-url)
Secondly, the model implicitly assumes that surplus labour exists in rural areas whereas there is full employment on the urban areas. But contemporary research studies have established exactly the opposite in the case of most of the developing countries. These economists, by and large, agree that the assumption of urban surplus labour is empirically more valid than Lewis assumption of general rural surplus labour.

Another point on which economists differ is the notion of continued existence of constant real wages in the urban industrial sector until the supply of labour from the rural subsistence sector is totally exhausted. In many of the developing countries, urban wages tended to rise and have not remained constant over a period of time. In such cases, the profit share of the capitalists and their savings tend to decline over a period of time, thus affecting their investment rate. It appears that Lewis also visualised this possibility and identified four reasons which may lead to such a situation.

Despite these short-comings, Lewis model assumes significance in throwing some light on the composition of two sectors in an economy. The capitalist sector is defined as that part of the economy which uses reproducible capital, pays capitalists for the use thereof and employs wage-labour for profit-making purposes. The subsistence sector is that part of the economy which does not use reproducible capital and does not hire labour for profit. The capitalist sector is generally related to the industries which are established in towns and cities. The subsistence sector is equated to agriculture and therefore to rural areas. However, Lewis' conception of the latter is wider and includes the casual workers, petty retail trading, domestic services etc. It is quite clear that the latter part of the subsistence sector is not restricted to rural areas but is likely to be found in urban areas also. Thus, labour transfer to capitalist sector will occur from both these components of
the subsistence sector in a developing economy. However, in the case of rural subsistence sector rural-urban migration process is another important factor that affects sectoral labour transfers.

2.3 URBAN LABOUR MARKET AND MIGRATION

Since migrants come from the bulk of urban labour force in many developing countries, the supply of urban labour is mainly determined by the magnitude of rural urban migration. As such, before analysing the urban labour market, it is necessary to have an idea regarding the factors that influence rural-urban migration of labour force in a developing country. There is a widespread agreement among economists and non-economists alike that rural urban migration can be explained primarily by the influence of economic factors.

As explained by Lewis theory of labour transfer, overall economic development in the developing countries is characterised by the gradual reallocation of labour from agriculture to industry through rural urban migration. Lewis model has also stated that the labour supply from the rural subsistence sector is perfectly elastic and will be absorbed by continuously growing industrial sector at a constant wage rate. However, this model failed to pay attention to the problems that may crop up in the urban labour-market.

During 1970s and 1980s, many of the developing countries have experienced massive rural to urban migration despite rising levels of urban unemployment and under employment. This migration was labelled as 'excessive' and was explained with the help of 'experted' income framework by Harris and Todaro. Their model postulates that labourers will migrate from rural to urban areas if their expected income in the urban areas exceeds their expected income in the rural areas. The model also states that migration to the urban areas
is a positive function of the urban-rural expected wage differential. A worker may accept a period of unemployment or a short stay in the urban subsistence sector before he gets an entry into the formal sector. This hypothesis has been verified in the light of the experience of many developing countries. Guy standing in his study on Kingston (Jamaica) observed that the persistence of high rate of urban unemployment has coincided with a high rate of internal migration to the urban areas of Jamaica (notably to the capital). On the other hand, God Fray in his study on Ghana has drawn an opposite conclusion i.e., this hypothesis failed to coincide with the experience of Ghana. It is also observed that the 'expected earnings framework' has failed to take note of the behavioural aspects of the workers in the following ways:

1. The migrant is not likely to risk his entire economic existence on mere probability of getting a modern sector job, where he may draw a blank.

2. The migrant is not likely to weigh the modern sector wage by the probability of getting a job, independent of time.

3. Workers subjective perception of the probability of employment irrespective of the ratio of the employed to the labour force influence his decision to migrate. Thus the length of time for which an individual migrant is willing to accept to a loss and the associated stream of earnings have become very important variables in affecting his decisions. Despite these limitations, the real contribution of Harris-Todaro Model lies in explaining rural urban migration with reference to the urban labour market.

To explain the determinants of migration in detail, Bicoa model, an intertemporal linear programming model, constructed for the economy of Ecuador by Gaude, J and Peck, P in their study on "the economic effects of rural-urban migration". International Labour
introduced into Harris-Todaro framework, the concept of reservation wage. The reservation wage has been defined as the expected rural income plus the opportunity cost of moving which includes transportation costs involved in looking for a job and also the "Psychic" ones associated with changing ones social environment. This model, in contrast with Harris-Todaro model, states that an individual will not necessarily move when the expected rural-urban wage differential is positive unless the expected urban income exceeds the reservation wage. According to this, the propensity to migrate depends on rural and urban levels of income and employment. However, more convenient way of explaining the motives of migration is in terms of urban pull factors and rural push factors.

It is argued that the migration affects and in turn is affected by the structure of sectoral earnings, labour absorption and mobility in different sectors of an economy.

2.4 STRUCTURE OF SECTORAL EARNINGS

The models discussed above have explained the process of migration from traditional to modern sectors in a developing economy. Interestingly both modern and traditional sectors are found to be existing in the urban labour market. Contrary to Lewis hypothesis, wages in the modern sector are comparatively much higher than those in the traditional sector and are found to be rising in real terms also. These wage earning differentials which constitute an important challenge to the orthodox neoclassical theory of labour market are explained by the four major strands of thought viz institutional explanation, labour heterogeneity, labour quality and tertiary sector.
Wage earnings differentials in the labour market have been traditionally attributed to the institutional factors. It is often contended that earnings in the modern (formal) sector are pushed upwards to an artificially higher level by factors such as trade unionism and minimum-wage legislation. The trade unions often attempt to influence wages in the modern sector through political lobbying, besides collective bargaining. On the other hand, low wages (earnings) in both the urban and rural traditional (informal) sectors are the result of lack of bargaining power and effective legislation for these sectors. Low earnings in these sectors are also attributed to the existence of competitive conditions which are also aggravated by unrestricted entry of labour.

Sectoral location of the worker is considered to be another institutional factor that explains earning differentials among labourers. Low earnings, in other words, are not to be explained solely in terms of factor supplies affecting the earning capacity of the worker but an essential element in the story in his location in an institutionally determined part of the labour market. In terms of analysis this has two possible interpretations:

1. Is that a difference in earnings can be attributed to 'institutional' factors after we have allowed for variations in measurable human quality factors like education and experience. Thus the location in the labour market decisively shifts the earnings function for labour of similar quality.

2. Alternatively, the returns to human capital variables may be quite different in the different sector of the urban labour market.
LABOUR HETEROGENEITY

The neo-classical as well as Harris-Todaro models treat labour supplies as homogenous. However, the supply of labour to the urban labour market constitutes heterogenous group. This is attributed to two important factors viz:

1. Standard human capital variables like, education, experience, skill, etc. and

2. Personal attributes or background variables like caste, family background, etc.

Mazumdar (1975) observes that much of the differential between formal and traditional (informal) sector earnings can be explained by the age, sex and educational characteristics of workers in the two sectors.

It is further pointed out that heterogeneity of labour may affect the absorption of different quality labour in different sectors. Then it is likely that inter-sectoral differences in effect reflect differential returns to different quality labour. These differentials in earnings caused by the background variables related to labour heterogeneity may indicate segmentation of labour market into higher-wage sector and low-wage sector. These differentials independent of human capital variables are the consequence of institutional factors such as discrimination. As pointed out by Mazumdar and Ahmed at times "even the magnitude of returns to education and experience may also reflect some institutional influences rather than by fully accounted for by productivity differences". Though it is difficult to interpret these differences, the significant institutional and heterogeneity variables are to be taken into account in explaining wage differentials.
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In addition to education and experience, there are other aspects that affect the quality of labour. Mazumdar\(^2^4\) identifies the difference in the type of migrants as one such important characteristic. According to him, there are different types or rural to urban migrants—'visitors' who came to the urban labour market for a short stay without any commitment and 'regulars' who aspire for a more permanent job in the city, preferably in organised sector. Differences in quality of labour is also reflected in the different family compositions in the urban area during their urban residence\(^2^5\). It is argued that single migrants are less committed to the urban labour market compared to the family type.

As such stable workers who are assumed to be more productive are often preferred by the modern sector employers in the urban labour market. It is also argued that the supply price of different types of migrants will also be different. The family type of migrants will have a higher supply price compared to the single migrants. Mazumdar puts forth three probable reasons for this:

(a) The substantially higher housing costs for family migrant in town

(b) The lower earning strength of the family in town as women and children may not easily form part of the urban labour forces unlike in rural areas

(c) The existence of disguised unemployment on family farms which could make the marginal contribution of an individual worker low relative to the average income per earner of the family\(^2^6\).
Another explanation for the intersectoral earning differentials generally rests on the absorptive role of the urban tertiary sector in developing countries. The urban traditional sector is often equated with the tertiary sector which includes those activities producing non-material output. It is also assumed that urban tertiary sector provides an outlet for the under-employed in rural areas. The empirical evidence for this is provided by the faster growth of tertiary sector relative to manufacturing. The theoretical justification is given by the assumption that the model of monopolistic competition with easy entry is generally applicable in tertiary activity. The market structure associated with this model enables additional productive units to enter the industry even though its total output is not growing significantly. There is redistribution of total income generated among large number of workers and a fall in average income for workers. Mogee called this process as 'involution'. To him this happens because the basis of 'Bazaar' (traditional) economy is the family and the head of the house is committed to ensuring members of his family entrance into the system. Moreover, the type of goods and services are such that they often move in circles and allow the introduction of more labour. Thus the absorptive and involuting character of the tertiary sector pulls down the earnings in the urban traditional sector and causes intersectoral earnings differentials.

The above explanations for the intersectoral earnings differentials are not necessarily exclusive and may be exerting their influence simultaneously also. In the long run with perfect labour mobility these differences in earnings may disappear. However, the labour absorption and mobility are influenced by other considerations.
2.5. LABOUR ABSORPTION ACCESS AND MOBILITY

It is found that labour in the urban areas of developing countries is non-homogenous in character. As such labour absorption in different activities with different levels of average earnings may be considered both from the supply and demand sides and other institutional factors like recruitment processes and levels of information in the labour market. One approach to understanding, the labour absorption is to simply look at the results of the actions of labour as reflected in variables like participation rates, rates of unemployment and/or underemployment indices of direction and mobility etc. In spite of certain problems of measurement these indices could indicate the nature of absorption. Further, to explain these patterns, we need to study the preferences and constraints of the suppliers of labour. The first part 'involves grouping' together the behaviour and the character of individuals and identifying various regular statistical features between the two series. The explanation consists in saying why labour suppliers with this or that characteristic act in a particular way.\(^{29}\)

There are different factors that are likely to affect the preferences of workers. The first significant factor may be related to the nature of assets and other sources of income for the workers household. As explained by Sen\(^{30}\) this is based partly on 'indivisibilities of labour supply.' A farmer may not like to leave his farm for factory job. Given the choice, he would like to pursue both at a rather low supply price. Even in urban areas these considerations are not unlikely.

Further, the nature of job selected by a worker is likely to be highly related to his personal characteristics like age, sex, caste group, marital status, and skill levels. However, in this type of analysis interpretation may be difficult due to the fact that the kind of association is being influenced by socio-economic environment where in
the worker is placed. Thus supply of labour cannot be isolated from its social context. Radhakrishna and others\textsuperscript{31} observe that "strong social prejudices exist for certain type of jobs even among the poorer sections." Sen\textsuperscript{32} points out that it would be foolish to attribute all such preferences to 'irrationality' of some kind or other. However, these tastes and preferences are not to be considered always as static. These are obviously the result of one's past experience and these may change from time to time. Obviously then, "the wage rate at which they would offer their unutilised labour may vary with their socio-economic classes and the place of work\textsuperscript{33} Further these considerations are likely to be related to the family variables also. In their study on the slum-workers in Ahmedabad, Radhakrishna and others found that the Adivasis (tribals) refrained from joining the Harijan (low caste) dominated construction work even though they could earn substantially more in that activity. Even within the Harijans, different subcastes did not like to work together despite economic losses. Self-employed cobblers, in spite of lower earnings, attached significance to family occupation and independence to a great extent Thus labour absorption and mobility have explanations rooted in the socio-economic background of workers as much as the purely economic explanations.

Another important aspect which influences workers' preference for a particular job and mobility later on is the relationship between the different phases in workers' life. This approach, though not tested empirically, relates successive 'states of the worker' in his working and domestic life, factors like age at entry in the labour force, father's employment status at this stage, his marital status, the type of job held as the first job, are all likely to be quite important in determining his ultimate behaviour Thus with the same socio-economic group the differentials can be explained by these considerations.
In addition to these preferences, workers' mobility is also affected by a number of constraints in the labour market. These constraints which are also interrelated with the preferences in the market are grouped into three categories. The first set relates to the possibility of the workers learning about the nature of opportunities. Lack of adequate information regarding the available opportunities and the necessary procedures to avail them are the likely constraints faced by the workers. This is more likely when the recruitment procedures operate mainly through social network through relations, family members and friends.

Even if the worker does have the necessary information, the second set of constraints faced by him relates to the cost and effort of search for a job, on the one hand, and his qualification and/or skill level compared to the job requirements. The possibility of search depends on several factors like, whether he is new entrant or already in job, the likely time and money he is able to devote to his search. These are determined by his present job and/or his capacity to remain unemployed while searching for a job. Once a worker is engaged in a particular activity, due to generally long hours of work, he is likely to be left with very little time for any effective job search. This throws most of the workers into the unorganised/informal sector. Even if these workers aspire for achieving necessary skills and assets, the likelihood for this is almost nil. It is possible only in the organised sector wherein on-the-job-training enables workers to achieve necessary skills. Thus workers' background is the main factor that affects the possibility of achieving skills qualifications and assets. This results in a peculiar vicious circle wherein a worker with low skills has low earnings and low opportunities for achieving new skills and the circle is complete.

The final set of constraints relates to the external environment and economic circumstances which determine the overall opportunities.
available in a market. As Breman pointed all that there is no question of equal chances for all in search of work in terms of employment. This is mainly attributed to the social system in India. Even the modern sector for appointments for jobs in factories considers of kinship caste and religion are relevant. However, Breman argues that the reason for this kind of discrimination is due to the situation of scarcity of work and not due to the force of tradition.

Thus these preferences, constraints and access or entry for different opportunities may lead to segmentation of labour market. This segmentation is further strengthened by the economic and social factors which provide very unequal opportunities for training (and access to information). Then according to Cain the empirical question is to what extent are workers according "to some pre-labour market group characteristics confined to one segment of the occupational spectrum." Further, the segmented labour market is one of the possible causes for earning differentials among workers.
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