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## Rise of the Indian Middle Class and Its Impact on the Labor Market

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## ABSTRACT

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# Rise of the Indian Middle Class and Its Impact on the Labor Market

The world is changing its socio-economic landscape. By doing so, the phenomenon of a growing middle-class appears. Both household surveys and growth projections suggest that only about one-third of the global middle class is based in Asia. However, between 2009 and 2017, the global middle-class has increased from 1.8 billion to 3.5 billion, whereas 40 percent are located in Asia. The key contributors to this trend are China and India. Between 2011 and 2019, GDP per capita has surged by 66 percent in China and 53 percent in India. Forecasts by the OECD predict that between 2030 and 2035, India will overtake China in terms of middle-class population in absolute terms. Against this background, the article seeks to outline the implications that are associated with the rise of a growing middle class on India's labor market.

**JEL Classification:** E24, J21, J31

**Keywords:** middle class, India, labor market, employment, liberalization

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## **1. Introduction**

The world is changing its socio-economic landscape. By doing so, the phenomenon of a growing middle-class appears. In 2010, Kharas (2010) argues that a large part of the global middle class is located in the rich OECD countries. However, both household surveys and growth projections suggest that only about one-third of the global middle class is based in Asia. At the same time, he points out that this share could double by 2020 and that by then the percentage of the global middle class could amount to around 40 percent.

These projections have been proven to be correct. Between 2009 and 2017, the global middle-class has increased from 1.8 billion to 3.5 billion, whereas 40 percent are located in Asia (European Commission, 2016). The key contributors to this trend are China and India. Between 2011 and 2019, GDP per capita has surged by 66 percent in China and 53 percent in India (World Bank, n.d.-b). Forecasts by the OECD predict that between 2030 and 2035, India will overtake China in terms of middle-class population in absolute terms (OECD, n.d.).

Against this background, the article seeks to outline the implications that are associated with the rise of a growing middle class in an emerging country with regard to its labor market.

## **2. Theoretical Evidence**

A wide range of definitions concerning the Indian middle class exists. Like the global middle class, the Indian middle class comprises an income group, a social class, a potential political interest group, and a consumer market (Saxena, 2010). The definition of the Indian middle class is controversial because the indicators to measure them are subject to constant change (Javalgi & Grossman, 2016). That being said, Table 1 includes various definitions and estimates around the size of the middle class in India:

**Table 1: India's Middle Class: Sizes and Definitions**

Source	Size	Year	Definition
<b>Beinhocker et al. (2007)</b>	around 55 million	2005	Households with disposable income between INR 200,000-INR 1,000,000 per year (approx. \$11-\$55/day and \$4,200-\$21,000/year)
<b>Sankhe et al. (2010)</b>	32 million households	2008	Households with disposable income between INR 200,000 - INR 1'000'000 per year
<b>Meyer and Birdsall (2012)</b>	70 million	2009-2010	\$10 - \$50 / day (2005 PPP)
<b>CNN-IBN (2007)</b>	Around 200 million	2005	Consumption criterion / specific goods in a household: car, scooter, color TV, telephone
<b>Indian Ministry of Finance (2017)</b>	36 million	FY 2013-2014	Taxpayers who filed tax returns
<b>Indian Census (2013)</b>	Around 68 million	2011	Share of a population with a higher education

According to Meyer and Birdsall (2012), the number of people considered middle class is lower than projected by Beinhocker et al. (2005). Based on India's National Sample Survey, they estimated that the Indian middle class constitutes 70 million people, less than 10 percent of the population. They further suggest that the Indian middle class is reasonably secure in material terms. Meyer and Birdsall assume that the varying results are mainly driven by different definitions of what constitutes middle-class consumers or households and differences in the underlying survey data.

CNN-IBN applied another method and looked at the specific consumption criterion. In a survey, they asked households if they owned specific goods. One would only attribute the included goods to a middle class like a TV, scooter, a color TV, or a telephone. It was found that about 20 percent of the total population met these criteria. By the standards of the time, that would have been over 200 million people.

Nonetheless, due to rising incomes and falling prices, some consumer goods can no longer be classified as specific middle-class goods. Telephones, TVs, or scooters were considered typical higher middle-class goods until the 1980s. Today, these goods are so common that they are at most associated with the lowest middle class (Kapur, 2010). Therefore, this definition results in a much higher number for the Indian middle class.

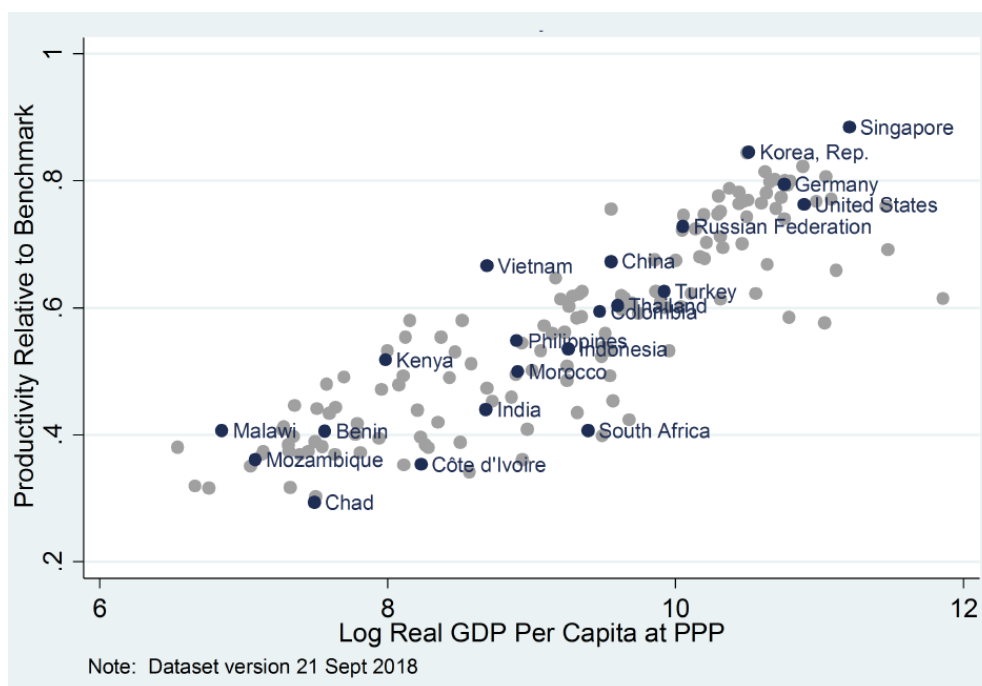
The same author sheds light on the number of income taxpayers in India that filed a tax return. Following this approach, for the fiscal year from 2013 to 2014, this figure amounts to 36 million, comparable to Sankhe et al.'s estimate from 2008. Further, he emphasizes value orientation rather than income or consumption measures. Subsequently, the number of people with a higher education degree shall be considered middle-class.

According to the survey data of the Indian census in 2011, 26.17 million females and 42.12 million males graduated from a tertiary educational institution or have higher educational qualifications. Overall, the Indian population amounted to 1.25 billion people in the same year (The World Bank, n.d.-a). As a result, around 68 million people would be considered middle-class.

Regardless of what definition and measurement one uses to determine the middle class, it is essential to recognize a growing middle class's relevance to an economy. For many scholars, the middle class constitutes a crucial driver for economic development through human capital development, consumption, and savings (López-Calva et al., 2014).

Nancy Birdsall et al. (2000) even argued that the middle class can be seen as the backbone of the economy and democracy in a market-driven economy. It can also be linked to reduced corruption, lower tariffs on international trade, and increased educational spending relative to GDP (Loayza et al., 2012). Another study Chun et al. (2011) analyzed the cross-country data of 105 developing countries using different middle-class measures spanning the period of 1985 and 2013. Accordingly, the middle class positively impacts economic development through human capital factor inputs. In this sense, the secondary school enrollment rate might be crucial and correlates positively with a rising middle class.

**Figure 1:** The human capital index



**Source:** Collin & Weil (2018); Kraay (2018).

A broad middle class requires economic growth and better jobs that generate higher incomes. Merotto et al. (2019) show that both the labor force participation and employment rate account for only 20 percent of income per capita growth. However, more critical is labor productivity growth, which explains 80 percent of the increase in per capita income.

Consequently, not the general employment rate but the quality and value-added labor force activities that determine economic growth per capita. Usually, the employment rate in low- and middle-income countries is relatively high. The problem is that workers in low-quality and low-productive jobs are rather underemployed. That is, the vast majority of the workforce tends to have irregular working hours.

40 percent of workers work less than 35 hours per week and about one-third work more than 45 hours (Merotto et al., 2019). Following this, workers in these low-quality and low-productive jobs work long hours, but their productivity per hour is relatively low.

80 percent of labor productivity growth is associated with a shift from low-productivity agriculture to relatively higher productivity in the manufacturing and service sectors. This shift is also referred to as economic transformation and is the primary driver of productivity growth in low-income countries.



Increasing agricultural productivity constitutes a critical driver of growth and economic transformation in low- and middle-income countries. Often, however, the modern and more productive sectors in developing countries tend to be underdeveloped. Hence, not all workers from agriculture who could switch to the manufacturing or service industry can be integrated into the labor market. As a result, they have to return to the agricultural sector. Consequently, productivity there drops again and with it economic growth.

Another significant influence on the economic transformation process shows the type of employment of the working population. According to Merotto et al. (2019), the richer a country is and the higher the per capita income, the greater the share of wage work. Nevertheless, many people employed in agriculture are either self-employed or are being considered as unpaid family workers. Yet, as soon as these workers make the transition to the industrial or service sector, they are engaged in wage work.

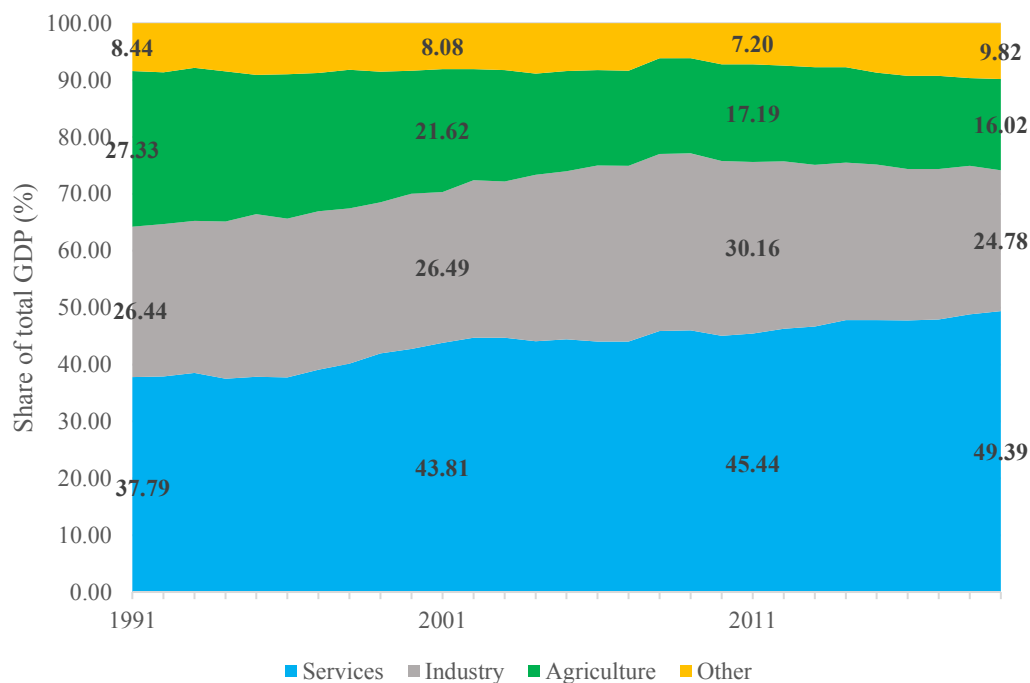
The share of wage labor in countries with a per capita income of less than \$600 is only 20 percent, while in countries with a middle-class income, the share rises to 63 percent (Merotto et al., 2019). Public sector wage employment accounts for about 40 percent of wage work in low- and middle-income countries on average.

### 3. Findings

Figure 2 shows the changes in the sectoral contributions to total GDP in India between 1991 and 2019. It shows that India has undergone a structural transformation since its reforms. While the share of the primary sector, mainly driven by agriculture, has decreased from 27.3 to 16.02 percent, the share of the tertiary sector, driven by the service sector, has increased from 37.8 to 49.4 percent.

The fact that the secondary sector, dominated by the industry sector, has increased only marginally is not surprising because India has already been industrialized before the economic reforms in 1991.

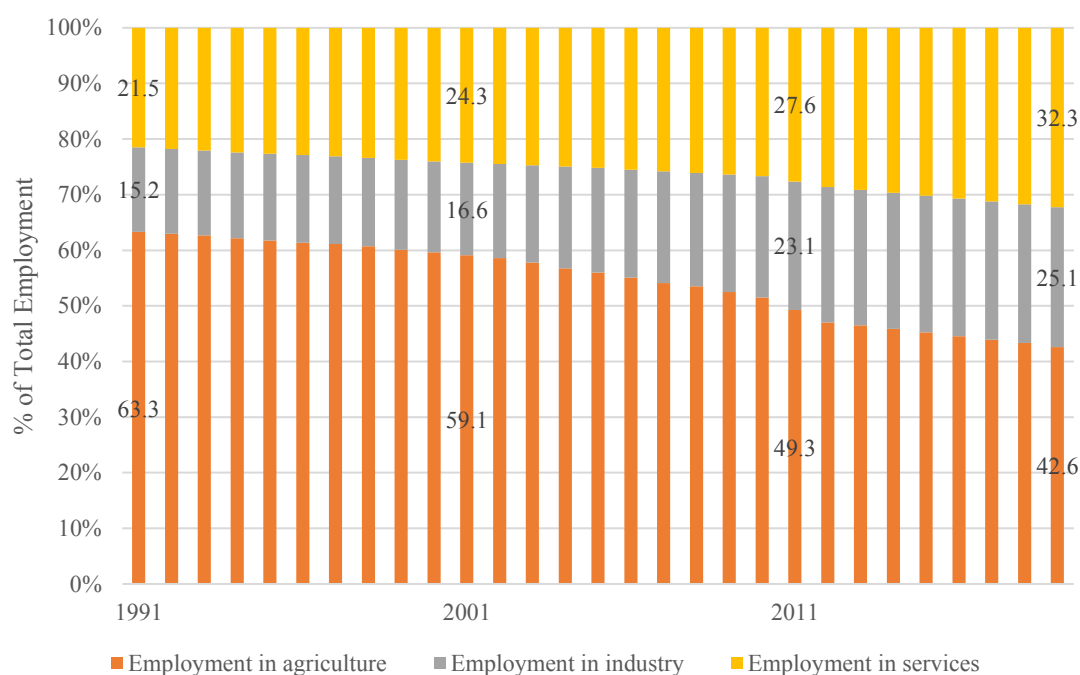
**Figure 2:** Value Added by Sector in % of GDP from 1991 to 2019



**Source:** World Bank (n.d.-b).

The sectoral change of the whole economy impacted the labor force distribution across all sectors. Figure 3 shows the distribution of the workforce across all economic sectors from 1991 to 2019. The share of employment in agriculture has fallen significantly from 63.3 to 42.6 percent. The consequent rise in the share of the industry and service sector has been more or less equal. Both the industry sector increased from 15.2 to 25.1 percent, and in the service sector from 21.5 to 32.3 percent.

**Figure 3:** Distribution of the Workforce Across all Economic Sectors;



**Source:** The World Bank (n.d.-b).

Millions of workers have shifted from farming to non-farming jobs. Yet, the non-agriculture job creation took place in only a few sectors (Bhattacharya, 2018).

**Table 2:** Top Ten job-generating sectors

Sectors	Share of new-non-farming jobs created between			Productivity per worker (INR 1000/worker, in 2015-16)
	1980-81 and 1990-91 (in%)	1990-91 and 2015-16 (in%)	Share of total work-force in 2015-16 (in%)	
<b>Construction</b>	<b>20.13</b>	<b>35.74</b>	<b>14.4</b>	<b>126.56</b>
Trade	24.84	14.56	10.04	235.78
Miscellaneous Service (including Real Estate Brokerage)	7.38	8.43	5.02	415.53
Transport & Storage	9.78	7.44	4.29	255.39
Education	3.13	6.26	3.22	22.13
<b>Business Services</b>	<b>1.47</b>	<b>5.99</b>	<b>2.18</b>	<b>811.68</b>
Hotels and Restaurants	2.49	3.75	1.89	123.53
Gems, Jewellery and Misc. Manufacturing	3.02	2.46	1.43	87.19
Food Products, Beverages, and Tobacco	4.92	2.28	2.42	158.72
<b>Financial Services</b>	<b>2.42</b>	<b>2.26</b>	<b>1.11</b>	<b>1259.52</b>
Health & Social Work	0.81	2.07	1.08	290.04

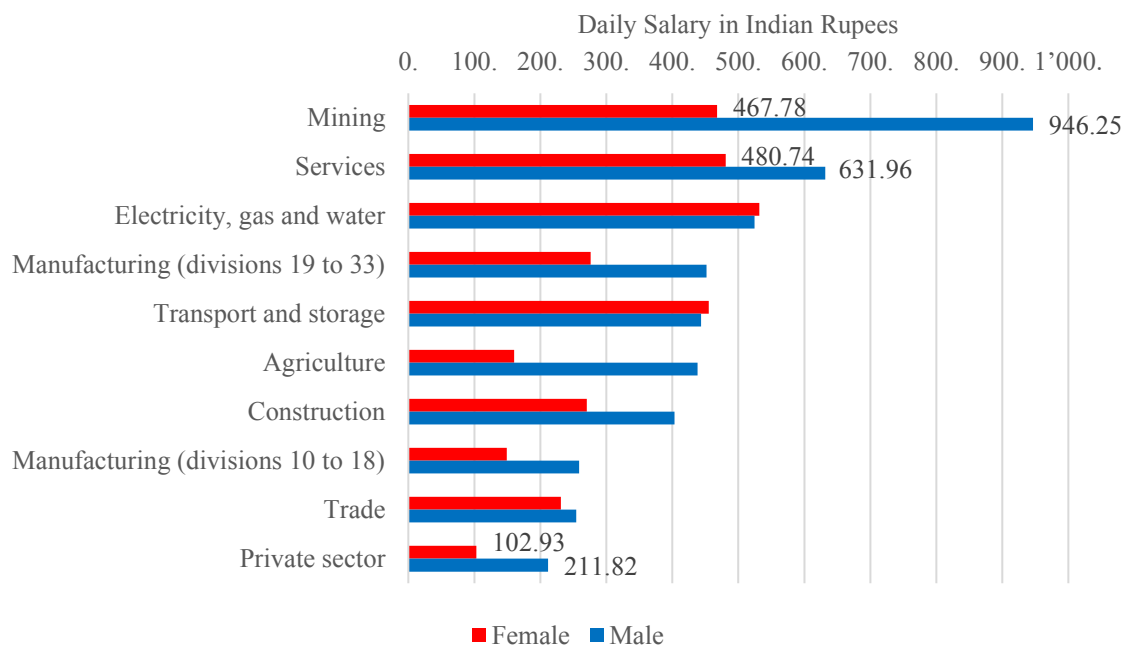
**Source:** Bhattacharya (2018).

Table 2 shows the top ten job-generating sectors in post-liberalization India. With 35.7 percent of all new non-farming jobs created between 1991 and 2016, the construction sector has contributed the most in absorbing workers from farming jobs. Even though the productivity level of the construction sector is 58 percent higher than in agriculture, it is still low at 126.56 and has even declined in recent years (Bhattacharya, 2018).

It shows that by no means did all workers benefit equally from the sectoral change. In this context, the decisive factor poses the productivity level because this also affects the income of the workers. As indicated in Table 2, it is predominantly service jobs, such as business services or financial services, that reveals high productivity levels per employee. (Eurostat, 2016).

The mining sector experienced a high labor productivity growth of 20.3 percent in 2019 (Ghosh, 2020). Nonetheless, it is the labor productivity that determines the income of the employee. Figure 4 discloses the average daily salary of urban male and female workers in India from 2011 to 12. Besides the gender salary gap, it indicates that the average salary in the mining sector was even higher than in services.

**Figure 4:** Value of daily average salary of an urban Indian worker in 2011-12

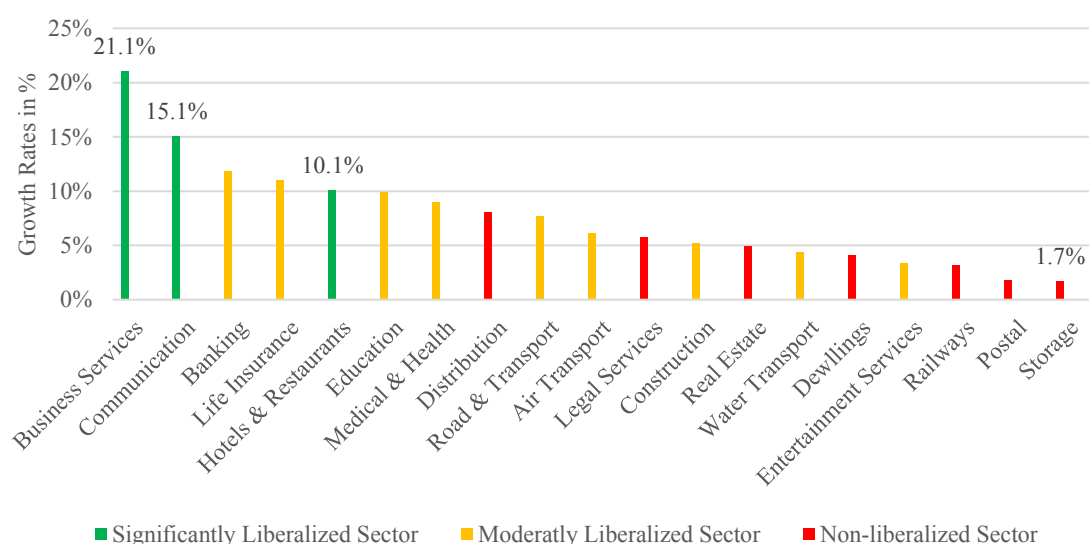


**Source:** Government of India (2016)

The expansion of the service sector created new job opportunities, especially in the middle-class segment. Additionally, FDI inflows in the post-liberalization period formed a crucial strategic investment component and contributor to economic development in general. The strong growth of the service sector is linked not only to domestic liberalization but also to the interconnection with external markets (Devajit, 2012).

Those sub-sectors that have been significantly liberalized and were subject to FDI investments experienced a higher growth rate and created most new employment opportunities during the 1990s. Figure 5 shows the most relevant service, categorized by their level of liberalization and the respective growth rate during the 1990s.

**Figure 5:** Liberalization and Growth Linkages in India's Service Sector in the 1990s



**Source:** World Bank (2004).

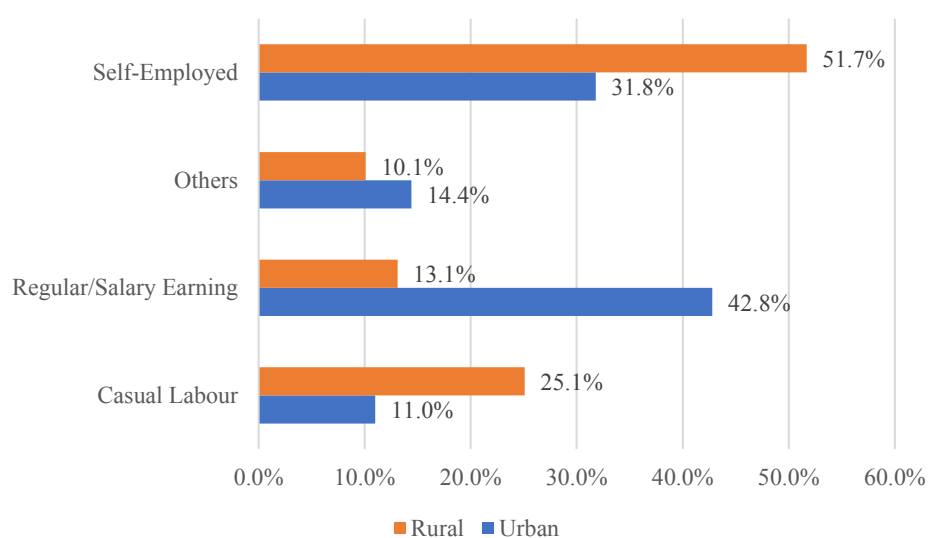
Most notably both the business services sector and the communication sector experienced the highest growth rates with 21.1 and 15.1 percent. The internationalization of white-collar employment mainly explains the growth of the business service sector in India (Fernandes, 2006). Many multinational companies, mainly from the US and the UK, began to relocate certain operations, such as customer service, to the suburban areas in India. As a result, many IT parks emerged in several tier cities like Bangalore, Delhi, Chennai, Hyderabad, Kolkata, and Pune, whereas Mumbai became a financial center.

To understand the employment of the Indian middle class, one must keep in mind that the Indian economy is fundamentally dualistic in terms of employment *and* enterprises (ILO, 2018). Dualism in this sense refers to a segmentation of the labor market and the enterprise landscape. In terms of the labor market, this means that the Indian government distinguishes between regular/salaried workers (formal, if they are covered by social security) and self-employed and casual workers (informal). In 2017-18 the total share of the formal sector was 47.6 percent, whereas the share of the informal sector was 52.4 percent (Murthy, 2015).

In terms of enterprises, a distinction is made between the organized and the unorganized sector. The organized sector includes all public establishments and non-agricultural businesses with more than ten employees and is therefore registered with the authorities. The unorganized sector includes all other private businesses that have no legal entity and fewer than ten employees.

Before the economic liberalization, the organized sector was always considered the same as regular/salaried work. However, ever since, the organized private sector has started to employ people on a casual or fixed-term-contractual basis, which prevents them from accessing social security or other benefits (ILO, 2018). Figure 6 shows the distribution of the income categorization in rural and urban households:

**Figure 6:** Distribution of households by type of work 2018 – 2019

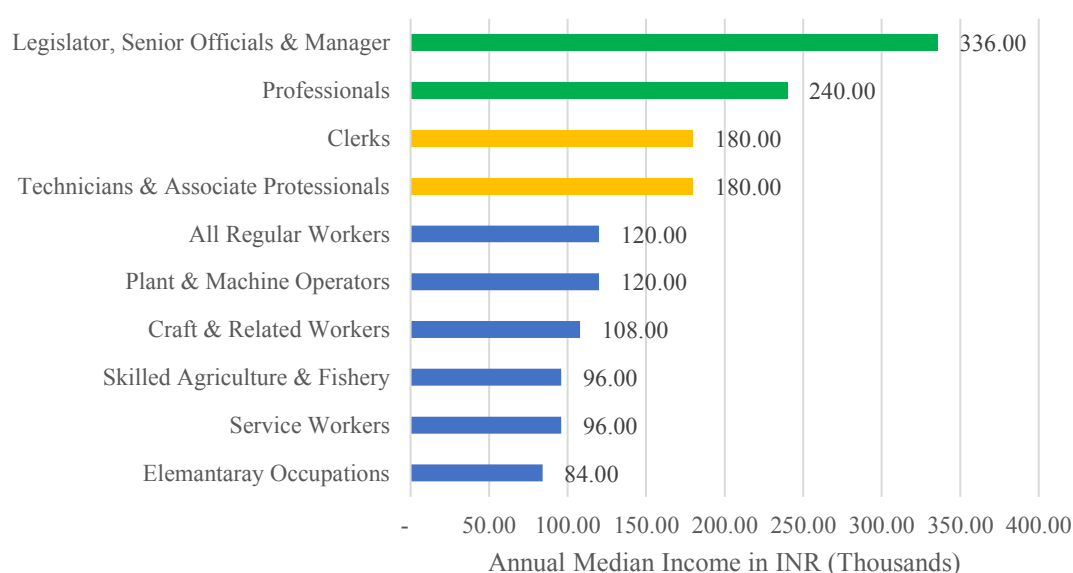


**Source:** MOSPI (2019).

As displayed in Figure 6, there exist significant differences between urban and rural areas. In rural areas, most households are self-employed (farmers in most cases), whereas in urban areas most households are engaged in regular/salary earning.

Regarding employment patterns and income, the lower middle class is predominantly in clerical or customer service occupations. Furthermore, they are also engaged in the technical areas where specialized knowledge is required. The upper-middle class is in the highest professional level of the natural sciences, such as engineering or medicine. The high earners occupy legislator, corporate manager or general manager positions in the private sector. Figure 7 shows the median income across different occupational classes.

**Figure 7:** Distribution of Median Income by Occupational Class 2017-18



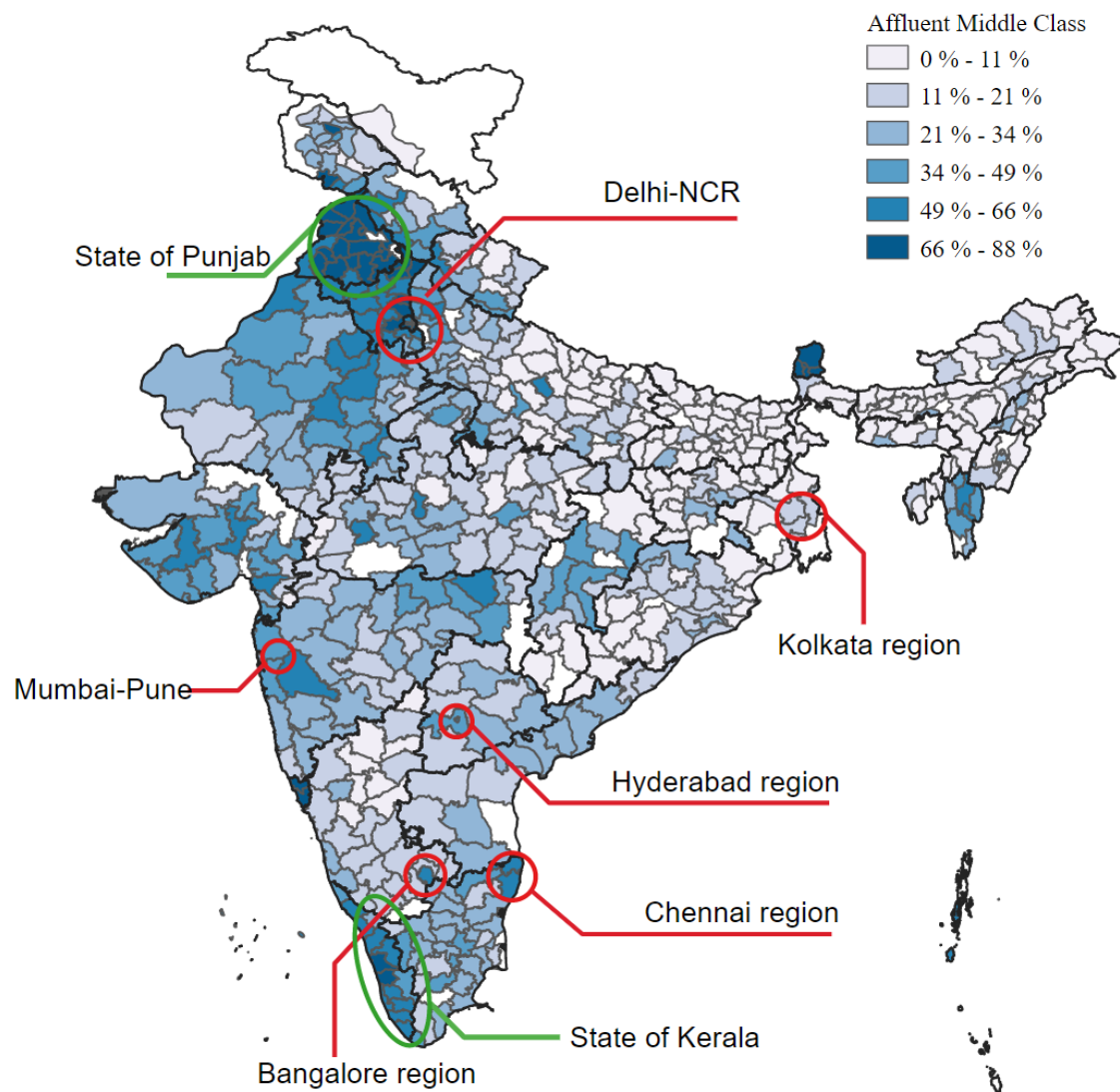
**Source:** MOSPI (2018).

To determine the proportion of an affluent middle class, the households that had at least six of the following items or amenities were investigated: pucca house<sup>1</sup>, electricity connection, phone (landline/mobile), television, A.C./cooler, refrigerator, washing machine, and motorized vehicles such as a car, motorcycle, tractor or truck. Figure 8 shows the share of affluent middle-class households on a district level. Accordingly, around 25 per cent of the total population fulfill this criterion.

<sup>1</sup> A pucca house has walls and a roof made of the following material: Burnt bricks, stones (packed with lime or cement), cement concrete, timber, etc. (MOSPI, 2015).

The share of urban middle-class Indians in tier cities (red circles) is the highest in the Chennai region, including Chennai, Kancheepuram, and Thiruvallur, with almost 61.8 percent of the population being affluent middle class. Delhi-NCR follows with 54.67 percent. With 17 percent, the share of the affluent middle-class around a tier city is the smallest in the Kolkata region.

**Figure 8:** Spatial Distribution of the Wealthier Population by District



**Source:** Kundu & Bhattacharya (2018).

When comparing the migration flows to cities with the spatial distribution of the affluent middle-class, a similar settlement pattern emerges, indicating that migration flows correlate positively with middle-class population density.



This spatial distribution shows that the affluent middle class is mainly located in and around the mega-metropolises (except Kolkata), where the quality jobs are, and the western feeling of a globalized city is present. However, it also shows that if the definition of the middle class is based on ownership instead of income, some rural districts, especially in the states of Kerala and Punjab (green circles), also show a significant proportion of affluent middle-class households.

## **4. Discussion**

It is no coincidence that the economic liberalization reforms resulted in the rise of a *new* middle class. However, only a minority of the Indian population has benefited from that development in terms of the employment. Although the economy has grown substantially, the labor market in the formal sector has only grown by 2 percent.

80 percent of the Indian workforce is employed in the informal sector (Hedrick-Wong & Bhardwaj, 2017). This means that they have neither job security, a regular salary, nor social security. As shown in the sectoral compositions of the economy, nearly half of the Indian workforce is still employed in the primary sector, which is informal in almost all cases.

Therefore, inclusive growth in the Indian labor market is also an issue. Only a minority, predominantly those with access to appropriate education, could be employed in the better-paid formal service sectors. Therefore, the ultimate goal of all Indians, regardless of their caste or social position, is that their children can complete a quality education to have an opportunity in the labor market (Kundu, 2021).

## **5. Conclusion**

India has gone through a remarkable economic transition. Since India's independence from Great Britain, it has been rebuilt under a socialist government. Economic growth stagnated at 3.5% per year between 1950 and 1991. At that time, there was no sign of a broad middle class. The middle class at that time consisted exclusively of members of the higher castes and government officials. The households belonging to this group were often referred to as *post-colonial* middle-class.

It was not until the economic liberalization reforms and the associated opening of markets that the country took a step toward a mixed market economy. Economic growth increased dramatically, new employment opportunities emerged, and cities became the epicenter of globalization, privatization, and entrepreneurship. At the same time, a new consumer-driven class, often referred to as the *new* middle-class, emerged around these urban areas.

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