

# Constraints in Macroeconomic Policies in Raising Employment

MudaserAhad Bhat<sup>1</sup> and BinishQadri<sup>2</sup>

<sup>1&2</sup>Research Scholar, Department of Economics, Central University of Kashmir, Kashmir, India  
E-Mail: mudaserahadbhat1990@gmail.com qadribinish@ gmail.com

**Abstract** - Macroeconomic factors such as low inflation, export orientation and low labor taxes help to determine how much employment is created by growth. The relationship between growth and employment is strong and positive which gets enlightened when all macroeconomic policies work in harmony. Indian economy at the time of independence was mainly rural in nature and in a bad state. This was due to the anti-Indian policies of the British Government. The country was engulfed by the vicious circle of poverty and to break this vicious circle Government of India planned in a focused way. The emphasis shifted from agriculture to industry. Also emphasis was laid on increasing role of the state to generate employment and reduce poverty by appropriate macroeconomic policies. However, little was achieved till 1990's. So the path to long-run economic growth was ensured by introducing New Economic Policy in 1991, which aimed at reducing fiscal deficits, lowering inflation, maintaining exchange rate stability etc. One thing that was obvious was that under New Economic Policy, the public sector will have a diminished role and will be largely limited to social sectors and non-profit making activities unattractive to the private sector. These policy changes affected macroeconomic policies of the government. Despite these policy changes brought under the New Economic Policy, one feature that still remains an important feature of macroeconomic policies in India is that macroeconomic policies still continue to act more as the control devices rather than as development tools. As a result macroeconomic policies fail to generate additional employment. Macroeconomic policies need to be converted into tools for macroeconomic stabilization (Shah, 2008). There are various constraints in macroeconomic policies which refrain them to act as development tools and thereby increase unemployment levels in underdeveloped economies of the world. The present paper attempts to highlight such constraints and suggest remedial measures.

**Keywords:** Heterogeneity, formalism, overlapping, absence of equi-genetic change, accommodation with assimilation, stretching-the-existing function, leaving-the-one stretching function.

## I. INTRODUCTION

Economic growth of country depends upon many inter-related elements. One such an element is macroeconomic policy. Generally, macroeconomic policy is implemented through two sets of tools: fiscal and monetary policy. Both forms of policy are used to stabilize the economy, which can mean boosting the economy to the level of GDP consistent with full employment (Thomas, 2002). Macroeconomic policy focuses on limiting the effects of the business cycle to achieve the economic goals of price stability, full employment, and growth (reviewecon.com). "Macroeconomic policy denotes

carrying out a planned change in the economy with a view of achieving greater national growth and development. The essence of macroeconomic policy is holistic change undertaken through properly coordinated, integrated, organized and properly directed government action in those conditions in which there are usually wide and new demands and in which there are intense obstacles and typically low capacities in achieving them"(author's definition).

Macroeconomic policy is the identity and report card of the countries performance. Macroeconomic policies determine the pace and pattern of economic growth in a country. They are the tools which are used by the countries to achieve economic stability and secure greater justice. In addition, they are also used to create jobs which are productive. In our country the tragedy is that we have achieved the double-digit growth but unemployment along with poverty still continues to be the major problems. Now, the question arises why the macroeconomic policies in India have failed to achieve their desired objectives? The plausible answer is as follows: ours is a transitional economy in which the government is neither diffused nor narrowly specific but intermediate as to the degree of functional specialization. The government does not blend well with other institutions within the economic system and thus tend to fuel the forces of mal-integration. Developing economies of the world, like ours, thus suffer from a serious lack of balance between the rates of economic and governmental growth. Due to government hegemony, the government often encroaches upon the jurisdiction of the RBI and tries deliberately to affect the economic process. All this implies that our economy is differentiated but is differentiated by mal-integration which is a greatest hurdle/constraint in the working of macroeconomic policy. This has led to the lack of proper co-ordination between various constituents of macroeconomic policies and accordingly these policies have failed to achieve the desired objectives. That is to say that it has led to the bad interface among different macroeconomic policies in general and fiscal policy and monetary policy in particular.

This primary constraint has given rise to other secondary constraints. The present paper tries to analyze such constraints in order to suggest the way by which harmony can be secured between major agencies of formulating macroeconomic policies, namely, government and RBI, so that these policies may become vehicles for creating more

productive employment opportunities in India in particular and other developing countries in general.

## II. OBJECTIVES

1. To highlight the macroeconomic constraints in raising employment in India.
2. To highlight the consequences of macroeconomic constraints.

## III. METHODOLOGY

The present paper brings into limelight the key macroeconomic policy challenges faced by contemporary India. Many of the basic tenets of macroeconomic policy need to be redefined in the context of current global problems (Jonathan Harris, 2001). Almost all macroeconomic policies involve two types of measures viz. ex-ante and ex-post. The ex-ante (and ex-post) reasoning in economic topics was introduced mainly by Swedish economist Gunnar Myrdal in his 1927–39 work on monetary theory.

The term ex-ante is a phrase meaning “before the event” or “simply appraisal”. The opposite of ex-ante is ex-post (actual or simply evaluation). Both ex-ante and ex-post measures have been used to analyze the various constraints faced by the macroeconomic policies in underdeveloped countries in general and India in particular. While, analyzing the consequences of these macroeconomic policies, only ex-post measures have been used.

The present paper develops a subjective definition of macroeconomic policy. The purpose is to understand the various theoretical challenges and constraints faced by macroeconomic policies in underdeveloped countries like India comprehensively. In this context, we are addressing ex-post (actual) proposals mainly from the employment point of view. An important limitation of the subsequent analysis is that the ex-ante proposals may be announced but not implemented or implemented but not effective, which actually happens in the real world.

## IV. LITERATURE REVIEW

In order to fulfill the objectives of our study, the literature review is divided in two parts. The first part is examining the interaction or interface of fiscal and monetary policy in order to understand it comprehensively so as to highlight the macroeconomic constraints while the second part of the literature review is examining the existing literature which deals with the debate of sustainability and environment which is very important for macroeconomic stabilization and understanding the macroeconomic challenges and constraints. Many of the basic canons or principles of macroeconomic policy need to be redefined in the context of current global problems of which sustainability is at the top level.

## V. FISCAL AND MONETARY INTERFACE

Fiscal and monetary policies are two pillars of macroeconomic policy, both for accelerating growth and ensuring stability (Sixth Dr. Raja J.Chelliah Memorial Lecture, 2017; Nayyar, 2011). Interdependence of economic policies necessarily results in overlapping and coordinating the policies between different levels of government is a major challenge faced in all multilevel fiscal systems. While much of the debate on economic reforms in India has focused on economic liberalization at the central level, there is relatively less attention on the reforms at the sub-national level which can be labelled as the macroeconomic constraint (Rao & Sen, 2011). According to Duvvuri Subbarao (London, 13 March 2013) we can accelerate growth and improve welfare only if we effectively implement wide ranging economic and governance reforms. The Government has to be at the center of this and lead the process of economic revival. In his fifth I.G.Patel lecture at LSE, he discussed some important macroeconomic challenges and constraints from the Reserve Bank’s (Monetary Policy) perspective.

1. Managing growth-inflation dynamic
2. Mitigating the vulnerability of external sector
3. Managing the political economy of fiscal consolidation

While talking about the vulnerability of the external sector which is one of the biggest macroeconomic constraint post 1990’s Duvvuri Subbarao (London, 13 March 2013) refer to large and increasing current account deficit (CAD) and the three concerns pertaining to it viz quantum, quality and financing of CAD. The large fiscal deficit of the government remains India’s biggest macroeconomic challenge. Therefore need of the hour is to manage the political economy of fiscal consolidation. There is evidence regarding the exogenous and policy-related factors which greatly affect the success of fiscal consolidation efforts (Price, 2010).

While discussing the macroeconomic constraints he illustrated the dilemmas that we face in managing the growth-inflation trade-off (Phillips curve). Monetary policy tightening is inappropriate to combat supply shock driven inflation.

Investment is a matter of functions two: the generation of income and increasing the productive capacity of economy (Harrod, 1939; Domar, 1946). Today’s investment is tomorrow’s production capacity. Private investment is significantly and negatively influenced by uncertainty and macroeconomic instability (Ramey and Ramey, 1995). Macroeconomic stability is the cornerstone of any successful attempt to increase private investment and economic growth (Ramey and Ramey, 1995; Easterly and Kraay, 1999). India needs to not only reverse the investment downturn but also increase it significantly to raise production to match the growing consumption demand.

Increase in investment is necessary also to raise production for exports and thereby create jobs at home. Making this happen requires a supply response from the government by way of providing public goods and creating a conducive environment for private investment. Meanwhile, the Reserve Bank has to ensure that inflation is brought down to the threshold level and is maintained there. The macroeconomic challenge is to keep inflation in check over long periods of time, allowing the economy to grow at its potential rate with minimal breaks, dispersions and deviations. This is the best way in which the macroeconomic environment can contribute to a positive business climate. (Keynote Address by Dr. Subir Gokarn, Deputy Governor, Reserve Bank of India on October 5, 2010 at The Private Equity International India Forum).

Policies cannot be understood or explained without reference to geographical location, historical context and overall environment (Kanagasabapathy, 2001).

Sixth Raja Chelliah Memorial Lecture (24<sup>th</sup> March, 2017) by Y.V. Reddy discussed how the interface between fiscal and monetary policy evolved in our country. It discusses how the stressful interface between 2008 and 2015 has been replaced by an entirely new framework in 2016 which is closer to theory than before and is closer to the practice being followed in advanced economies. Post 1990's saw a paradigm shift in the interface. At a very broad level, the paradigm shift occurred through a series of acts of abnegation of power by the Government to RBI and the markets. The concluding remarks emphasized upon the good interface between fiscal and monetary policy. Acharya (2008) too felt the need for a better coordination of monetary and fiscal policies for managing the macroeconomic situation by highlighting the need for structural reforms. Noah Smith and Paul Krugman both argue that support for difficult economic conditions created by government measures to reduce public expenditure in the slump is at least partially a product of desire for structural reforms. Smith notes: "I conjecture that "austerians" are concerned that anti-recessionary macro policy will allow a country to "muddle through" a crisis without improving its institutions. In other words, they fear that a successful stimulus would be wasting a good crisis. In the broadest sense "structural reforms" simply mean changes to the economy-polity structure (John Aziz, 2013).

Fiscal policy can hurt prospects for economic growth if, for example, profligate Government machinery runs up successively high budget deficits and crowds out productive private investment (Raghbendra, 2004). This is what we find in Indian economy for past many decades. Corrective measures on the fiscal front initiated at the beginning of the 1990s produced some promising output during the first half of the decade. However, the fiscal consolidation even during the first half of the 1990s was brought about primarily through curtailment in capital expenditure. From 1997-98, expenditure started rising once again, and by the year 2001-02, all the major fiscal indicators, viz, revenue

deficit, fiscal deficit, and public debt rose to levels higher than those prevalent at the beginning of the reform process. And some improvement again being witnessed since 2002-03 which was accelerated by the enactment of the Fiscal Responsibility and Budget Management (FRBM) Act, 2003.

The Fiscal Responsibility and Budget Management Act, 2003 (FRBMA) is an Act of the Parliament of India to institutionalize financial discipline, reduce India's fiscal deficit, improve macroeconomic management and the overall management of the public funds by moving towards a balanced budget and strengthen fiscal prudence. The main purpose was to eliminate revenue deficit of the country and bring down the fiscal deficit to a manageable 3% of the GDP by March 2008. There is need for fiscal consolidations in a serious manner.

Laurens & de Piedra (1998) analyses interaction between two main macroeconomic policies viz fiscal and monetary policy. Stress is being given on policy coordination at two different levels; fulfillment of overall policy objectives, and institutional and operational procedures. The efficient pursuit of the objectives of the macroeconomic policy requires a good interface of financial policies. Both policy mix and individual policy must be set on a sustainable and credible lines. A necessary condition for efficient coordination of monetary and fiscal policies is that each policy must be sustainable and credible. Moreover, joint determination of objectives and policies by the fiscal and monetary authorities is equally important.

## VI. SUSTAINABILITY AND ENVIRONMENT

The most popular view of sustainability comes from Brundtland Report of 1987 according to which development which meet the needs of present generation without compromising the needs of future generation is said to be sustainable. Sustainability perspective implies that radical and proactive government policies are required to achieve economic development that is both socially just and ecologically sound. Sustained growth and development arguably depend more on the social and political institutions of a nation (Basu, 2012). Many of the basic tenets of macroeconomic policy need to be redefined in the context of current global problems. The objectives of macroeconomic policy should include economic stabilization, distributional equity, broad social goals such as income security, education, and universal health care, and the management of economic growth. There is an increasing recognition that the achievement of social goals is essential to environmental sustainability. Regarding growth, while earlier macroeconomic theorists generally assumed that growth was good, ecological economists such as Herman Daly (1991) have suggested that growth should be limited and that a sustainable economic scale, rather than exponential growth, should be the goal of macroeconomic policy. The theorists and practitioners of a new macroeconomics should insist on a broad perspective that

asks what macroeconomic policy can achieve in the areas of distribution, social equity, and ecological sustainability. The goal should be to provide a theoretical basis for the reorientation of macro policy at the national and international levels, linking efforts to promote local-level sustainability and equity with “greening” and restructuring of multilateral institutions (Jonathan Harris, 2001).

“Much of our corruption control policy goes wrong when it comes to implementation because of one fundamental error, a propensity to treat the enforcers of the law—the policemen, the bureaucrats and administrators—as robotic agents, who will carry out the task they are supposed to do mechanically and flawlessly” says Basu (2012). According to him whatever system we suggest must have the property of being a ‘self-enforcing equilibrium’. “The social and political ethos that prevails in a society can reinforce or weaken the innate propensity of human beings to be other-regarding. Social norms are like in-built restraints, which ensure that certain actions that may be physically feasible are, nevertheless, considered out of bounds. All dogs can bite but only some do. Similar propensities are also true about human beings. In designing policies we must take realistic stock of the interests and propensities of the enforcers. These can differ across societies. So to design these policies right we cannot be mechanistic but must have knowledge of the society we are dealing with and the propensities of the people of this society.” quotes further.

A report from McKinsey Global Institute noted that CEE countries have stable macro-economic environment. Success mantras from such countries can be taken and implemented in order to boost the macroeconomic environment in India.

## VII. SUMMARY OF LITERATURE REVIEW

While the existing literature lays more emphasis on sustainability (Herman Daly, 1991; Harris, 2001; Goodwin, Nelson & Harris, 2008; Basu, 2012) but the need for the unique principles in macroeconomic policy formulations and implementations are neglected at large. Present study recognizes the need for unique principles in macroeconomic policy formulations and implementations. But these unique principles should depend upon the needs of the society rather than upon the choice of political structures, governance reforms and directions of the political heads (Subbarao, 2013). Also the existing literature does not recognize the need of process of observation and experimentation in macroeconomic policy formulations and implementations but the present study recognizes that the macroeconomic policies should use, to a certain extent, the process of observation and experimentation keeping in view the changes taking place in the society so that certain predictions on the part of the policy making institutions can become possible. Existing literature characterizes macroeconomic policies solely as pragmatic and problem-solving tools and has totally neglected the need of lending social scientific status to macroeconomic policies. Since,

macroeconomic policies touch almost all aspects of life in the contemporary world, how these policies are planned and organized and how they are implemented and operated in practice should naturally attract our attention.

Macroeconomic policies operate in the context of society, of which they are part. Hence just as society is concerned with goals and values, so should be the, macroeconomic policies. Therefore, we notice two way relationship: macroeconomic policy exist in society and the pattern of macroeconomic policy theoretically is determined by society and accordingly the goals of the society and that of the macroeconomic policies should be consistent with each other. But in the current world or in the 21<sup>st</sup> century macroeconomic world, we see a trade-off between the goals of the society and that of the macroeconomic policies. All economic policies have trade-offs that benefit some groups more than others, and it should be up to the political processes within the countries to make the difficult choices amongst serious alternative policies (Shari Spiegel,2006). Macroeconomic instability hurts the weaker sections of society (Ames, Brown, Devarajan & Izquierd, 2001). Macroeconomic Society at large wants development while the macroeconomic policies also aim at development but they want to achieve it through short-cuts by largely focusing on containing fiscal deficits and inflation rates without keeping in view poverty, unemployment and other socio-economic problems. As a result, the nature and orientation of the macroeconomic policies has changed from the development tools to control devices. Poverty is a multidimensional problem that goes beyond economics to include, among other things, social, political, and cultural issue. Therefore, solutions to poverty cannot be based exclusively on economic policies, but require a comprehensive set of well-coordinated measures (Ames, Brown, Devarajan & Izquierd, 2001).

### *A. Constraints in macroeconomic policies in raising employment*

It is very important to rethink and redefine macroeconomic policies which cannot simply be used for the eradication of macroeconomic imbalances and inflationary management tool, since fiscal and monetary policies are potent and versatile instruments in the pursuit of development goals. In doing so, it is essential to the overcome the constraints embedded in orthodox economic thinking and recognize the constraints implicit in the politics of ideology and interests (Nayyar, 2011).

1. Heterogeneity: Generally two institutions are involved in formulating and implementing macroeconomic policies, namely government itself and the central bank of the country (Thomas, 2002). A situation in which there is simultaneous presence of quite different kinds of practices and view-points in fiscal and monetary and external policies of the government and the central bank respectively is called heterogeneity. This has become an important feature of modern

macroeconomic policies just like modern macroeconomics where heterogeneity has become main protagonist in empirical strategies (Chari, 2007). Due to the parallel co-existence of diametrical opposite view-points and practices in fiscal policy of the government and monetary and external policies of the central bank to achieve the same objective(s), two agencies of formulating and implementing macroeconomic policies have become complementary to each other rather being supplementary to each other and the result is that the macroeconomic policies of the modern times have become inconsistent, incomplete and irresponsive. This intermingling of diametrical opposite view-points and practices, followed by government in its fiscal policy and by the central bank in its monetary policy, introduce numerous complexities and difficulties in formulating and implementing macroeconomic policies.

The cause of heterogeneity is two-fold. Firstly, while the central bank as the policy making institution is essential for formulating and carrying out monetary policy operations, it suffers from many deficiencies in its framework in developing countries. Often the major part of policy making personnel of the central bank aligns with the government in power leading to factional politics and rivalry between the departments. Factionalism is a concept in political anthropology used to describe groups of people formed around a political leader who reject the status quo and actively work against established order or authority within a society, such as state institutions, political parties, or economic interests (Hill, 2013). Some administrators of the central bank also show a tendency towards acquiring independent power positions to increase their group interests and as a result their energies and capacities are more often spent in preparing their self-interest than in the pursuit of development goals. This is how heterogeneity creeps in macroeconomic policies on the part of the central bank.

Secondly, the central bank as the policy making institution is getting increasingly politicized. The political leaders tend to control the central bank excessively, interfere with its policy formulation and implementation process and bring unjust pressures and demands on it. This excessive political control and interference with the policy making process of the central bank makes the policy making personnel of the central bank frustrated and power less and thereby reduces their independence and effectiveness. This is how heterogeneity creeps in on the part of the government.

It follows that in developing countries, both the government and the central bank as the policy making institutions seek to exchange their power. This gives rise to tensions and conflicts in their interaction and does not permit them to collaborate in national-building

and development goals which they try to achieve through their respective policies.

Existing body of literature talks about heterogeneity but in modern macroeconomics especially in relation to household heterogeneity (Krueger, Mitman & Perri, 2016), latent heterogeneity in econometrics (Arellano, 2003), economic models with heterogeneous agents (Krusell & Smith, 1998; Algan, Allais & Haan, 2008; Reiter, 2009; Mertens & Judd, 2012) and not in relation to macroeconomic policy. The present study therefore attempted to highlight heterogeneity in macroeconomic policies as the main macroeconomic constraint.

2. **Formalism:** Formalism may be defined in two senses. In one sense. It means the degree of discrepancy between the formally prescribed procedures and methods in formulation of macroeconomic policies and effectively practiced procedures and methods in implementation of macro economies. This implies that procedures and methods announced during formulation of macroeconomic policies are not strictly followed during their implementation process. In short, formalism refers to gap between theory and practice (Dow, 1998; Hilbert, 1913). In another sense, formalism refers to the existence of gap between the stated objectives and the real performance. The broad reason for emergence of formalism is the lack of ability of the policy making institutions to guide the performance of the social and economic institutions and therefore, all attempts to bring about a policy reform has only a superficial impact. Also, due to this formalism macroeconomic fail policies to adjust their behavior gradually to the demanding situations.
3. **Overlapping:** Fiscal and monetary policy affect each other (Sargent and Wallace, 1981). Clash and interference in the functions between the two for sure leads to overlapping. Overlapping refers to condition in which a function is demarcated for say monetary policy but fiscal policy or external policy also performs that function and vice-versa. Due this overlapping, it becomes difficult to observe precisely the behavior of macroeconomic policy over time. And due to it, policy makers feel that macroeconomic policy does not require any reform over time as it appears that macroeconomic is working smoothly. But in real practice, a major or minor reform is actually always needed by a macroeconomic policy to realize its objectives. This prevents unification of goal and creates a situation of confusion. As a result, decision making becomes difficult. However, if in a situation of overlapping, policy makers try to reform the macroeconomic policy, such a reform leads to "reform indeterminacy" i.e. reforms keep changing after a very short period of time without serving their objectives. Nature of the reform depends upon the relationship among various constituents of macroeconomic policy and this relationship is blurred by overlapping and the result is

reform indeterminacy. Reform indeterminacy further deteriorates the economic conditions, as it encourages black marketing, hoarding, low investment etc. leading to higher level of inflation and unemployment. An overlapping generations approach is widely used in macroeconomics to judge the effects of various macroeconomic policies (Blanchard & Stanley, 1989; Barro & Xavier, 2004) but no existing body of literature talks about overlapping as a macroeconomic constraint.

4. Absence of Equi-Genetic Change: Change is difficult (Krasner, 1984). The pressure for change in macroeconomic policy comes from both internal and external sources. If the pressure for change is primarily external source(s), it may be called “exogenous change” and if the pressure for change is mainly internal source(s), then it may be called “endogenous change”. However, if the pressure for change is caused by both external and internal sources, then it is called “equi-genetic change”. Generally, both external and internal sources call for change in macroeconomic policies. But in our country, the tradition is that macroeconomic policies are changed either due to internal factors or due to external factors of change and both internal and external factors of change are never taken into account simultaneously while formulating macroeconomic policies. In the presence of equi-genetic change, behavior predictions of macroeconomic policies become correct to a large extent and such correct behavior predictions are not possible either in endogenous change or in exogenous change alone. In a given environment of endogenous and exogenous factors, the institutions and the behavioral patterns they generate and create equilibrium and stability (Greif, 2003). The reason is that in an equi-genetic change, future impacts of a macroeconomic policy become unanticipated on the part of the public and anticipated on the part of the policy formulating and implementing agency. Further, the presence of equi-genetic change makes a macroeconomic policy able to absorb the externally induced change as well as internally induced change in the shortest possible time. This lends a macroeconomic policy a homogeneous, connective and a realistic character. But in under developed countries like India, the macroeconomic policies fail to absorb either endogenous change or exogenous change or both types of changes and as a result, they face greater problems of greater heterogeneity, formalism and overlapping and which in turn induce macroeconomic instability (Joya, 2011). The endogenous growth theory primarily holds that the long run growth rate of an economy depends on policy measures (Arrow, 1962, Romer, 1994; Lucas, 1988; Barro & Martin, 2004). Economic growth primarily results from endogenous forces. Neglecting such changes would mean deviation from the long run growth path. Exogenous growth theorists lay thrust on exogenous factors (Harrod, 1939; Domar, 1946). Like death and taxes the exogenous

drivers are inevitable (Downes & Stoeckel, 2006). Many studies highlight that the structural change in the economy is caused by endogenous and exogenous changes. (Downes & Stoeckel, 2006; Florensa, 2004) but no study has given equal weightage to endogenous and exogenous changes in macroeconomic policies. Moreover, no study has described the equi- change as a constraint in macroeconomic policy.

5. Accommodation with Assimilation: The notion *accommodation without assimilation* has been the key feature of Indian civilization. India has accommodated different elements of society without letting them lose their separate identity. We have got enough freedom to practice our own way of life. This feature of Indian society is good on cultural side. As far as macroeconomic policies are concerned ‘*accommodation without assimilation*’ doesn’t find any place. Rather it is ‘*accommodation with assimilation*’ that is seen in our macroeconomic policies. The system is such that it has accommodated various macroeconomic policies but the blunder is that it has assimilated them leading to overlapping, clashes and malfunctioning. Interdependence of economic policies necessarily results in overlapping (Govinda Rao & Tapas Sen, 2011). We must realize the fact that it is ‘*accommodation with assimilation*’ which is the root cause of all macroeconomic problems. ‘*Accommodation without assimilation*’ should be the mantra for the success of macroeconomic policies and will definitely help in raising income, output and employment levels in the economy.

#### B. Consequences of the macroeconomic constraints

The above mentioned constraints of macroeconomic policies have following consequences on overall performance of the economy particularly from the employment point of view:

1. Stretching-The-Existingfunction/Phenomenon  
Consequence: Our macroeconomic policies try to enhance the growth by utilizing more fully parts of the already employed labor-force trapped in low-productivity but these policies pay no or little attention towards creating new additional employment opportunities. This behavior of macroeconomic policies may be rightly called as “stretching-the-existing function/phenomenon”. This approach to increasing the growth rate of an economy is no doubt a positive approach but it increases the unemployment rate in the economy and thereby leads to jobless growth. If productivity growth is not being accompanied by employment growth we need to place greater weight on employment in economic policies. Policies need to address the quality of employment in addition to simply increasing employment (Junankar, 2013). This approach to increase the growth rate of an economy

should be used along with paying sufficient emphasis on the creation of additional and productive employment opportunities. The blending of these two approaches would not only raise the growth rate of an economy to higher levels by increasing both the production and employment in same direction but will also reduce the poverty and will improve the quality of employment in the country.

This stretching-the-existing phenomenon tends to produce much stronger effect on production than on employment. Accordingly, this phenomenon may also be termed as “stretching-the-existing employment phenomenon”. There may be other reasons responsible for the growth of this phenomenon but it is pertinent to mention here that “employment generation is an outcome of the overall macroeconomic policy direction and decision of the government”.

2. **Leaving-The-One Stretching Function Consequence:** Besides being defined as the sustained increase in GDP or GNP (Kuznets & Murphy, 1966), economic development is also being defined as the change in the occupational structure of an economy (i.e. falling share of the agricultural sector and rising share of the non-agricultural sectors such as of industry and service sectors). In the normal course of development, countries first shift their employment and output from agriculture sector to manufacturing sector and then to service sector but in India, this shift is taking place directly from the agriculture sector to the service sector and therefore, manufacturing sector remains out of development process at large. In China, this shift is taking place from agriculture sector to manufacturing sector and final to service sector thereby all the leading sectors of the China’s economy are involved in employment creation and poverty reduction. This behavior of the development process in the Indian economy may be rightly called as “leaving-the-one stretching function” i.e. development is taking place but without the development of manufacturing sector at large. This behavior of the development leads to lopsided of the economy and the major cause behind such behavior of the development process are the macroeconomic policies of the country. This type of development behavior adversely affects the employment elasticity in the country as for example; negative employment elasticity was reported from manufacturing sector of the Indian economy recently. Further, this behavior of macroeconomic policies caused high rate of interest, low gross capital formation, infrastructural bottlenecks and low domestic and external demand thereby lead to low growth in the manufacturing sector.

At least one reason may be held responsible for creating this leaving-the-one stretching phenomenon through macroeconomic policy; viz. , macroeconomic policies are always formulated and implemented with the aim of

increasing the supply of modern technology from developed countries to our country. This is essentially a good feature of our macroeconomic policies but the way in which these policies try to achieve such a technology transfer is essentially a bad feature of our macroeconomic policies. Modern technology is essentially capital-intensive and labor saving and our economy (Indian economy) is essentially labor-intensive. The introduction of a capital-intensive technology in a labor-intensive economy tends to produce a much stronger effect on production than on employment. If the ultimate aim of our macroeconomic policies happens to increase only the production, then this increase in production could have also been made possible by increasing the productivity of the labor force as well by employing extra labor force. Then what is the logic behind the import of technology? Industrialization of developing countries, particularly south-Asian countries was principally dependent on imported technology from advanced capitalistic countries, which has less employment elasticity (Mehrotra, 2007). Instead of placing blind faith in technological progress and economic growth, society should adopt a precautionary principle. This principle says that we should err on the cautious side, preferring to cooperate with natural systems rather than assuming we can safely replace them( Goodwin, Nelson & Harris, 2008).The cost-effective advantage of capital-intensive technology has come to end due to its unlimited use. The high inflation rates in the world sufficiently reflect that cost-effectiveness no longer remains monopoly advantage of the capital-intensive technology. This has happened because infinite use of capital-intensive technology, due to incentives effect, has raised the costs of inputs used to run a capital-intensive technology as well as the costs of inputs used for producing outputs proportionately more than the cost of employment which is being sacrificed for the use of these capital-intensive technologies. This has not only raised unemployment rates but also inflation rates. Our macroeconomic policies do not take in to account this demerit of modern technology and try to reap the benefits of the technological transfer in one go without bothering about its adverse impacts on employment elasticity, fiscal deficits and price level. Importing and employing modern technology is not bad in itself but only its poor management creates problems in the economy. Strategy for importing and employing capital-intensive technology should be such that employment elasticity should remain positive by employing it. To maintain positive employment elasticity, every time macroeconomic policies should facilitate limited technology transfer according to the needs of the economy.

Further, capital-intensive technology should be evenly distributed among the leading sectors of the economy. Use of it should not remain confined to one sector only,

for at least in one sector the spread effects of the technology may be greater than its backwash effects.

Poor modern technology management is one the broad reasons responsible for in-formalization of labor in our country. It has led to increase in casual labor because employers feel that they can be retrenched at will. Modern macroeconomic policies have created a trade-off between the informal employment in the unorganized sector and the informal employment in the organized sector (Ghose, 2017 ), i.e., the movement from informal unorganized sector employment to informal organized sector employment is taking place but the formal employment in the organized sector continued to remain stagnant. The constraints discussed above lie at the root that cause poor management of the modern technology by the macroeconomic policies.

## VII. CONCLUSION

Macroeconomic factors such as low inflation, export orientation and low labor taxes help to determine how much employment is created by growth. The relationship between growth and employment is strong and positive which gets enlightened when all macroeconomic policies work in harmony. It is very necessary to return to a developmental approach to macroeconomic policies, which is based on an integration of short-term fiscal and monetary policy goals with long term development objectives (Nayyar, 2011). The essence of macroeconomic policy is holistic change undertaken through properly coordinated, integrated, organized and properly directed government action in those conditions in which there are usually wide and new demands and in which there intense obstacles and typically low capacities in achieving them. Usually our macroeconomic policies ignore these new demands, intense obstacles and typically low capacities. With the result macroeconomic policies face various constraints like heterogeneity, formalism, overlapping, absence of equi-genetic change and accommodation with assimilation which refrain them to act as development tools and thereby increase unemployment levels in underdeveloped economies of the world. Attainment of high employment rather than aversion to high unemployment should now become the goal of our macroeconomic policies. Macroeconomic policy is incomplete unless more and more structural, societal, institutional, and behavioral characteristics are incorporated to depict a modern welfare economy.

## VIII. LIMITATIONS AND FUTURE DIRECTIONS

The present paper highlighted the various constraints faced by the macroeconomic policies in underdeveloped countries but it discussed the consequences of these constraints only from the employment point of view. While as growth-inflation dynamics, the vulnerability of external sector, fiscal constraints etc. have not been discussed in length. Therefore, to highlight all the possible consequences of

macroeconomic policies from all possible angles forms a future Research Gap.

## REFERENCES

- [1] D. Hilbert., "Grundlagen der Geometrie", (Foundation of Geometry), Springer, 1913.
- [2] Harrod, Roy F., "An Essay in Dynamic Theory", *The Economic Journal*. Vol. 49, No. 193, pp. 14–33, 1939. doi:10.2307/2225181.
- [3] Domar, Evsey, "Capital Expansion, Rate of Growth, and Employment", *Econometrica*, vol. 14, No. 2, pp. 137–147, 1946. doi: 10.2307/1905364.
- [4] Muth, J.F., "Rational Expectations and the Theory of Price Movements", *Econometrica*, vol. 29, No. 3, pp. 315-335, 1961. Retrieved from <http://www.jstor.org/stable/1909635>.
- [5] Arrow, J. K., "*Economic welfare and the allocation of resources for invention*", National Bureau of Economic, Research Princeton University Press. ISBN: 0-87014-304-2, pp. 609 – 626, 1962. Retrieved from <http://www.nber.org/chapters/c2144.pdf>
- [6] Sargent, Thomas J., and Neil Wallace., "Some Unpleasant Monetarist Arithmetic", *Federal Reserve Bank of Minneapolis Quarterly Review*. Vol. 5, No. 1, pp. 1–17, 1981.
- [7] Krasner, S.D., "Approaches to the State: Alternative Concepts and Historical Dynamics", *Comparative Politics*, vol. 16, No. 2, pp. 223-46, 1984.
- [8] Lucas, R.E., "On the mechanics of Economic Development", *Journal of Monetary Economics*. Vol. 22 , No.1, 1988.
- [9] World Bank, "World Development Report", Washington D.C, 1988.
- [10] Government of India, "Report on the Current Economic Situation and Priority Areas for Action, Ministry of Finance, New Delhi", 1989.
- [11] Blanchard, Olivier Jean; Fischer, Stanley, "The Overlapping Generations Model. Lectures on Macroeconomics", Cambridge: MIT Press. pp. 91–152, 1989. ISBN 0-262-02283-4.
- [12] Daly, Herman., "Elements of Environmental Macroeconomics. Chapter 3 in Costanza ed. Ecological", Economics: The Science and Management of Sustainability. New York: Columbia University Press, 1991.
- [13] Romer, P.M., "The Origins of Endogenous Growth", *The Journal of Economic Perspectives*, Vol. 8, No. 1, pp. 3–22, 1994. Doi:10.1257/jep.8.1.3.
- [14] Ramey, Garey, and Valerie A. Ramey, "Cross-Country Evidence on the Link between Volatility and Growth", *American Economic Review*, Vol. 85 (December), pp. 1138–51, 1995.
- [15] Bagchi, Amaresh, "India's Fiscal Reform: Some Signposts", Vol. 28, No. 1, 1998, January-March, Indian Institute of Management, Ahmedabad.
- [16] Dow, S. C., "Editorial Introduction to the Formalism in Economics Controversy", *Economic Journal*, Vol. 108, No. 451, 1998.
- [17] Krusell P, Smith AA., "Income and wealth heterogeneity in the macro economy", *Journal of Political Economy*, vol. 106, No. 5, pp. 867–96, 1998.
- [18] Easterly, William, and Aart Kraay, "Small States, Small Problems?" Policy Research Working Paper No. 2139, 1999, Development Research Group (Washington: World Bank).
- [19] Ames, B., Brown, W., Devarajan, S., & Izquierdo, A., "Macroeconomic Policy and Poverty Reduction. Washington, DC: International Monetary Fund", 2001. Retrieved from <https://www.imf.org/external/pubs/ft/exrp/macropol/eng/#ref>.
- [20] Harris., "Macroeconomic Policy and Sustainability. Global Development And Environment Institute (G-DAE)", 2001. Working Paper No. 01-09. Retrieved from <https://ageconsearch.umn.edu/bitstream/15573/1/wp010009.pdf>.
- [21] Mayer, Thomas, "Monetary policy: role of". In Snow don, Brian; Vane, Howard R. An Encyclopedia of Macroeconomics", Northampton, Massachusetts: Edward Elgar Publishing. pp. 495–99, 2002. ISBN 978-1-84542-180-9. Retrieved from <http://www.Reviewecon.com/outside-resources.html>.
- [22] Greif, A., "Institutions. Theory and History", Forthcoming Cambridge University Press. Chapter 1, 5 and 9. Gokarn, 2003. Keynote Address. The Private Equity International India Forum.
- [23] M. Arellano., "*Panel Data Econometrics. Chapter 2. Unobserved heterogeneity*", pp. 7-31, 2003. Oxford University Press.

- [24] Barro Robert J & Sala-i-Martin, Xavier, "Overlapping Generations Model", *Economic Growth* (Second ed.). New York: McGraw-Hill. pp. 190–200, 2004. ISBN 0-262-02553-1.
- [25] Chakravarty, Shomit, "Reform of Tax Administration in India \_ A Quiet Revolution", in ADB India Economic Bulletin, October, New Delhi, 2004.
- [26] Florensa, C. M., "Institutional Stability and Change. A Logic Sequence for Studying Institutional Dynamics", Presented at Tenth Biennial Conference of the International Association for the Study of Common Property (IASCP). "The Commons in an Age of Global Transition: Challenges, Risks and Opportunities". Oaxaca, México, 9-13 August, 2004.
- [27] Jha, R., "Innovative sources of development finance", *The World Economy*. Vol. 27, No. 2, pp. 193-214, 2004.
- [28] Downes, P & Stoeckel, A., "Drivers of structural change in the Australian Economy". Centre for International Economics Canberra & Sydney, 2006. Retrieved from <http://www.theicie.com.au/wp-content/uploads/2014/06/MASTER-DITR-26-Feb.pdf>.
- [29] Spiegel, S., "Macroeconomic and Growth Policies", New York, 2006. United Nations DESA/UNDP. Retrieved from <https://www.g24.org/wpcontent/uploads/2016/01/MACROECONOMIC-and-growth-policies.pdf>.
- [30] Biggeri, M., "Children's valued capabilities", In M. Walker & E. Unterhalter (Eds.), *Amartya Sen's capability approach and social justice in education*, Chapter 10 , pp. 197–214, 2007. New York: Palgrave.
- [31] Chari, V.V. & Kehoe, J.P., "The Heterogeneous State of Modern Macroeconomics: A Reply to Solow", Federal Reserve Bank of Minneapolis Research Department Staff Report 399, 2007. Retrieved from <https://www.minneapolisfed.org/research/sr/sr399.pdf>.
- [32] Algan, Y., O. Allais & W. J. Den Haan, "Solving Heterogeneous-Agent Models with Parameterized Cross-Sectional Distributions", *Journal of Economic Dynamics and Control*, vol. 32, pp. 875 -908, 2008.
- [33] Stefano Eusepi & Bruce Preston, "Stabilizing Expectations under Monetary and Fiscal Policy Coordination", Federal Reserve Bank of New York Staff Reports. Staff Report No. 343, September 2008.
- [34] Goodwin, N., Nelson, A.J., & Harris, M.J. "Macroeconomic Activity in Context. First edition. Global Development and Environment Institute Tufts University Medford", MA 02155, 2008. M.E.Sharpe. Retrieved from [http://www.ase.tufts.edu/gdae/education\\_materials/modules/Macroeconomic\\_Activity\\_in\\_Context.pdf](http://www.ase.tufts.edu/gdae/education_materials/modules/Macroeconomic_Activity_in_Context.pdf).
- [35] Shah, A., "New issues in Indian macro policy", Working Paper 2008-51, 2008. Retrieved from [citeseerx.ist.psu.edu/viewdoc/download?doi=10.1.1.380.1832&rep=rep1&type=pdf](http://citeseerx.ist.psu.edu/viewdoc/download?doi=10.1.1.380.1832&rep=rep1&type=pdf)
- [36] Reiter, M., "Solving Heterogeneous-Agent Models by Projection and Perturbation", *Journal of Economic Dynamics and Control*, Vol. 33, pp. 649 – 665, 2009.
- [37] Price, R., "The Political Economy of Fiscal Consolidation", OECD Economics Department Working Papers, No. 776, 2010, OECD Publishing, Paris. <http://dx.doi.org/10.1787/5kmdq798lls-en>
- [38] Joya, O., "Macroeconomic Instability in Afghanistan: Causes and Solutions", Masters dissertation (memoire), 2011.
- [39] Nayyar, D., "Rethinking macroeconomic policies for development", *Brazilian Journal of Political Economy*. Vol. 31, No. 3 (123), pp. 339-351, 2011.
- [40] Mertens, T. M. and K. L. Judd, "Equilibrium existence and approximation for incomplete market models with substantial heterogeneity", Working Paper, 2012.
- [41] Hill, L. Version 1. Factionalism. ANTH 423, Dr. Maximilian Forte, Dept. of Sociology & Anthropology, Concordia University, 2013. Retrieved from <https://politicalanthro.wordpress.com/factionalism/>
- [42] Junankar, N.P., "Is there Trade-off between Employment and Productivity?", IZA Discussion Paper No. 7717, 2013.
- [43] Aziz, J., "What Are Structural Reforms?", 2013. Retrieved from [http://www.pieria.co.uk/articles/what\\_are\\_structural\\_reforms](http://www.pieria.co.uk/articles/what_are_structural_reforms).
- [44] Krueger, D., K. Mitman and F. Perri, "On the Distribution of the Welfare Losses of Large Recessions", *Proceedings of the Econometric Society World Congress*, 2016.
- [45] Ghose, K.A., "Globalization, Growth and Employment in India", *Indian Journal of Human Development*. Vol. 10, No. 2, pp. 127-156, 2017.