

## A NEED OF HUMAN CAPITAL INVESTMENT IN INDIA

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### ABSTRACT

*In the Indian context, human capital investment has become a critical issue. Human capital investment challenges in India focuses on the Indian labour force and identifies why Government is finding it difficult to create human capital and is the investment in human capital adequate for Indian economy? There is a need to maintain a balance between the demand and supply of technical labour force. India has a very large population (over 1.39 billion) and the working age group (15-64) in the population has been increasing by seven million people each year in the country. India can take advantage of this demographic dividend by creating skilled manpower, employment opportunities and human capital investment. Overall investment in human capital has definitely long run impact on growth. Economists distinguish among three types of human capital investment: expenses for education and training; expenses for care of health; and expenses for mobility. Out of these investments, the investment on education and training has some peculiarities, which makes it different from other types of investment. The human capital investment plays crucial role in the economic development. Firstly, formation of human capital would tend to change the traditional society to modern society, which has higher scope for economic development. Secondly, human capital increases the productivity of the physical capital. Enhanced productivity would accelerate the growth. Thirdly, higher standard of life is possible only via development of human capital. Fourthly, human capital investment facilitates the use and growth of innovation. Innovation is the principal determinant of growth. Fifthly, human capital formation increases the rate of participation. Higher the rate of participation, greater is the degree of economic equality in the society. Finally, investment in human capital yields larger returns and the returns on this type of investment far outweigh its input costs.*

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**Keywords:** Human Capital, Human Capital Investment, Demographic Dividend, Economic Development, Inclusive Growth, Youth Population, Education and Training.

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### Introduction

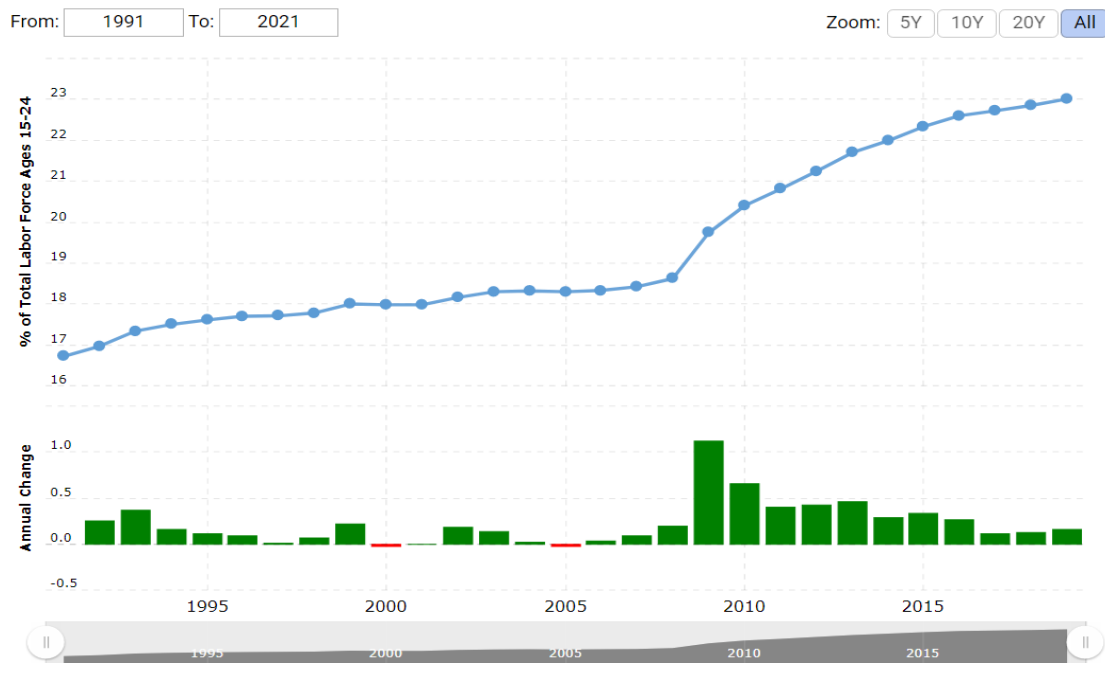
#### Human Capital Investment in India

A country's economic growth depends on many factors like Natural resources, human resources, physical capital, technological development, social and political factors. After attaining Independence India has developed in almost all spheres. After 30 years of economic reforms, India is recognized as one of the high growth economies with the potential to make a big leap from a developing to a developed nation. India has a large army of youth but this demographic dividend can be reaped only if this large army will be well prepared through investment in human capital. Delivering inclusive growth is possible only through the growth of our people. An equally important aspect of building human capital is creating the capacity for innovation. This can only be done when India embeds 'creativity' into the DNA of her education system and reward innovation. This will build the much-needed intellectual capital which is key to sustain long-term economic growth. However, this requires a large amount of investment in human capital.<sup>1</sup>

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Human capital investment (HCI) is the process country use to develop productivity of work force. In other words, the economic concept of developing human labor is commonly referred to as human capital investment. HCI focuses on value adding people management and attention to what needs to be done to make the best use of human capital. The added value that people can contribute to an organization is emphasized by human capital theory. It regards people as assets and stresses that investment by organizations in people will generate worthwhile returns. An approach to human capital management based on human capital theory analyses the impact of investment on economic growth. After the economic reform of 1991 public intervention and trend of public investment in human capital is continuously increasing. Youth population of India is increasing continuously after economic reforms (Figure).



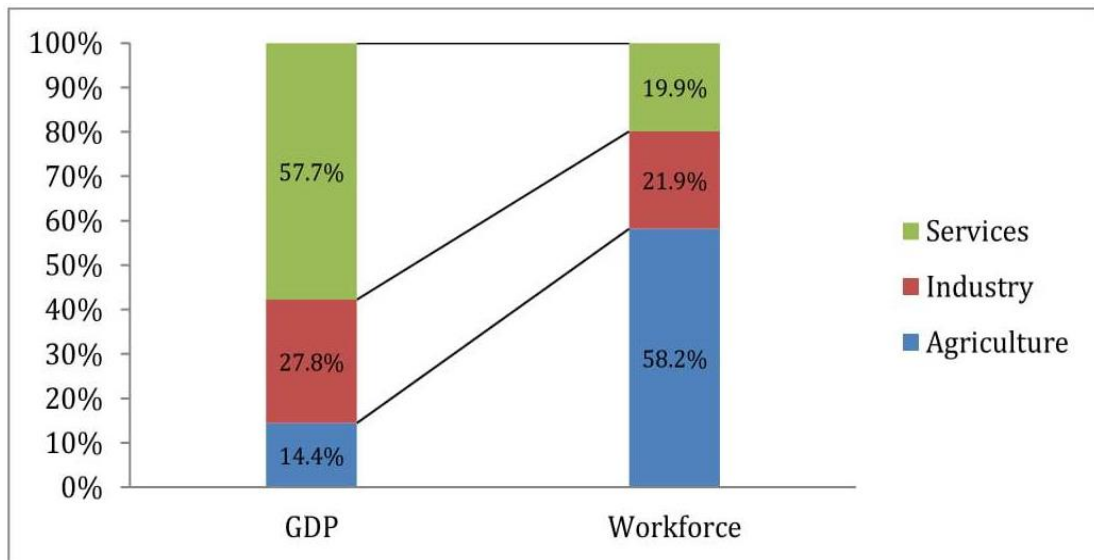
Data Source: World Bank

**Figure: Youth Population: India's Demographic Dividend**

**Current Workforce Scenario in India**

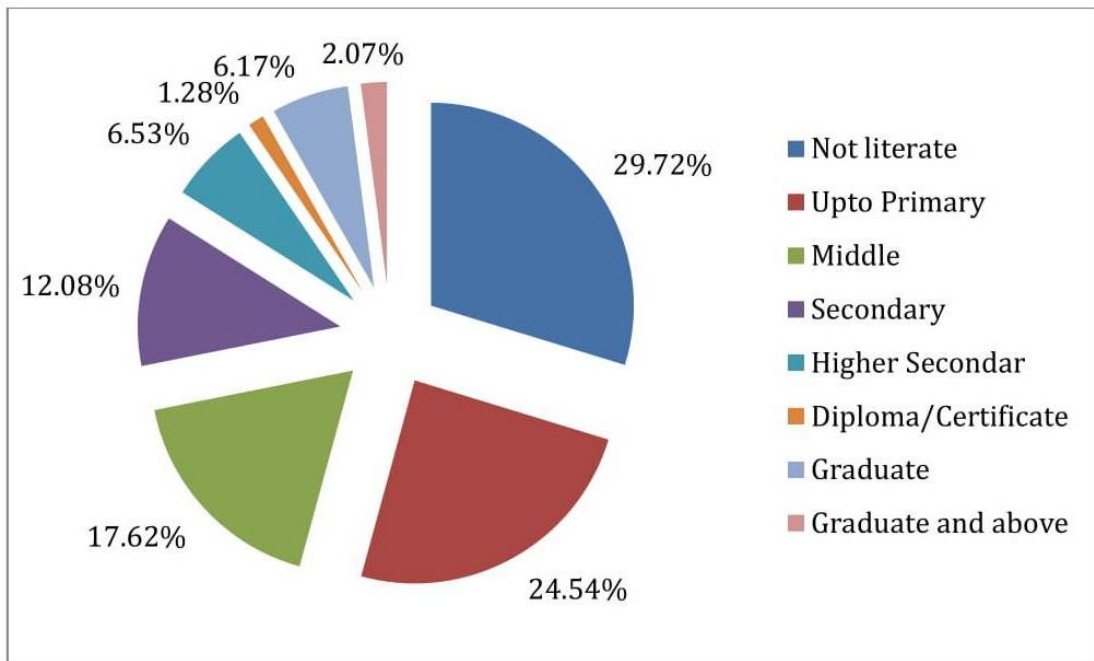
India has a very large population (over 1.39 billion) and the working age group (15-64) in the population has been increasing by seven million people each year in the country. India can take advantage of this demographic dividend by creating skilled manpower, employment opportunities, and human capital formation. This process can be achieved through the use of public health policies, education and training opportunities.

India's labor market can be characterized by three related and distinguishable megatrends. Firstly, the labor intensity in the agricultural sector in India is very high, compared to other sectors. This space is characterized by 'disguised unemployment' as it absorbs 58 percent of our labor while contributing only 14 percent to national GDP. This sector experiences low wages, under-productivity and poor competitiveness due to over-employment and under-skilled workforce (Bar chart). Secondly, informalization extends to other industrialized sectors also within our economy. The share of informal employment in the organized sector has increased by 45 percent from 2005 to 2010. This is consistent with the studies that have shown a strong positive correlation between the level of formalization and the level of skill required to perform tasks. India's labor force possesses low education levels, though the scenario has been improving in the recent past with initiatives like Right to Education. About 29 percent of the workforce is not even literate and 24 percent had education up to primary level (Pie chart).<sup>2</sup>



**Bar Chart: Sector-wise workforce distribution**

Source: Planning Commission, XII Five Year Plan, Employment and Skill Development



**Pie Chart: Education levels of the workforce**

Source: Planning Commission, XII Five Year Plan, Employment and Skill Development

**Reaping Demographic Dividend through Skill Development**

India is not alone in facing a serious shortage of skilled workforce. This issue afflicts many Asian economies which have risen fast in recent years, leading to increasing demand for scarce human capital. Our primary, secondary and tertiary education has produced some of the best talents but to a large extent, we face a mismatch between school education and the skills required in the economy. For bridging the skill gap, India needs trained and skilled people to operate efficiently and professionally, so as to benefit not only the institution concern but also the whole economy.<sup>3</sup>

Thus, human capital formation is associated with investment in human resources and their development as creative and productive resources. Educated and trained people have stronger incentives to invest in developing their skills, which increases workforce productivity by reducing incapacity and debility. Overall investment in human capital has definitely long-run impact on growth.<sup>4</sup>

Economists distinguish among three types of human capital investment:

- Expenses for education and training;
- Expenses for the care of health;
- Expenses for mobility.

Out of these investments, the investment in education and training has some peculiarities, which makes it different from other types of investment.<sup>5</sup>

In its broader sense, investment in human capital usually means spending on health, education and social services; and in its narrow sense, it means spending on education and training. It has become customary to talk about investment in human resources in the narrow sense of spending on education and training as measurable against social services.<sup>6</sup>

### **Human Capital Investment in Education and Training**

The concept of human capital arose from the recognition that an economy's decision to invest in human capital (financing education and training) is similar to decisions about other types of investments undertaken by Government. Human capital investments involve an initial cost (investment in education and training) which the economy hopes to gain a return on it in the future (increased earnings or higher productivity). As with investments in physical capital, this human capital investment will only be undertaken by the wealth-maximising economy if the expected return from the investment is greater than the market rate of interest. In the competitive global market where wages reflect the marginal product of workers, to be able to command higher earnings, the better-educated or more-trained workers must be sufficiently more productive in employment than their less-skilled counterparts.

Two common types of human capital investment include education and training. Education often includes reimbursing employees for traditional college degrees or paying for seminars or trade schools. Education is often used to develop an employee's technical skills in areas such as accounting, finance, or production. Training is most often conducted by supervisors working on the job with employees, showing them how to complete specific functions.

Educated and trained manpower is the human capital like other tangible forms of capital. Schooling, a computer training course, and lectures on the virtues of punctuality and honesty are also a capital. This is because they increase earnings, or increase a person's good habits for most of their life. Economists therefore view education, training and similar expenditures as investments in human capital. They are called human capital because people cannot be separated from their knowledge, skills or values in the same way that they can be separated from their financial and physical assets. Since India will have a large youth population in the age group of 20-35 years, it will be a great opportunity for India to have a large skilled population and allow the country to fully reap the benefits of the demographic dividend. There is a need to provide quality education. Not only does it need to be scaled up, but quality issues also need to be addressed," the Economic Survey said, adding that skill development is essential not only to benefit from the demographic dividend but also for more inclusive growth.

- **Investment in Education and Economic Growth**

*"Education is the most powerful weapon you can use to change the world" - Nelson Mandela.*

The above famous quote sums up the cardinal importance of education and it is all the truer as far as our country is concerned. As a young democracy, India is growing by leaps and bounds on the education front. After Independence, the policymakers worked hard to transform the elitist system of education created by the British into a mass-based system, built on principles of equality and social justice. With the formulation of Right to Education in 2009, the right to education was made a fundamental right and the National Education Policy was also announced.

Many studies show that a high school and college education in the United States significantly increases a person's income, even after accounting for the direct and indirect costs of schooling, and even that after adjusting for the fact that people with more education earn more. Similar evidence spanning many years is now available from more than a hundred countries with different cultures and economic systems. Earnings of the more educated are almost always higher than average, although less developed countries generally have higher earnings.<sup>7</sup>

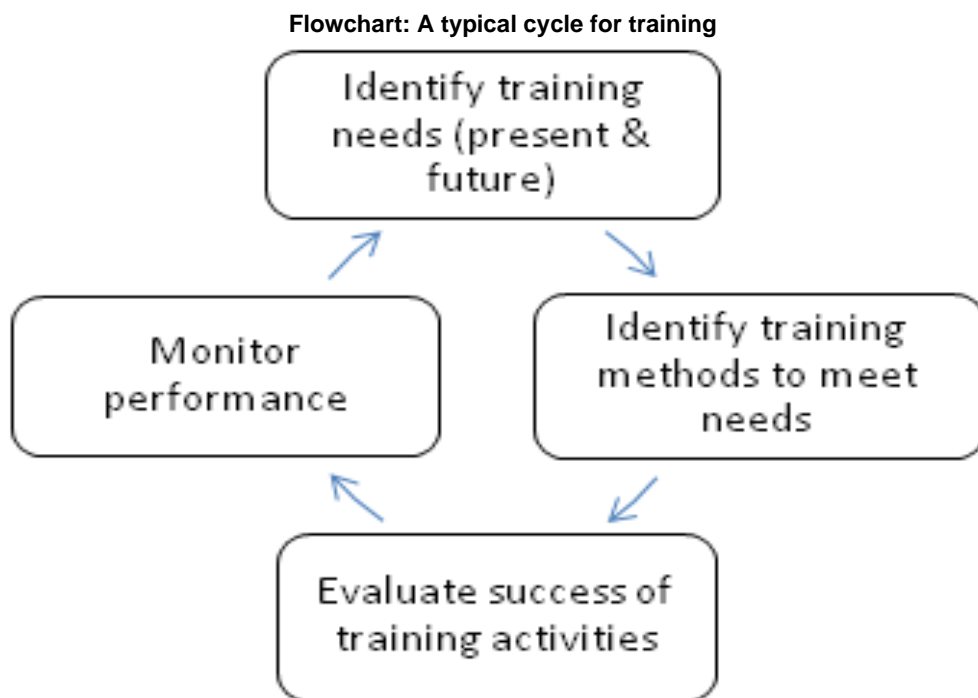
Apparently, the opportunities provided by the modern economy, along with the extensive provision of education and charitable support, enable the majority of those from low-income backgrounds to do reasonably well in the labor market. The same opportunities that promote upward mobility for the poor create an equal amount of downward mobility for those higher up the income ladder. New technological advances are obviously of little value to countries with few skilled workers who know how to use them. Economic growth depends on the synergy between new knowledge and human capital, which is why large increases in education have been accompanied by large advances in technological knowledge in all countries that have achieved significant economic growth.

#### **Present Scenario and need for Education in India**

The present education system in India has come a long way and the age-old traditions have undergone a new makeover. The government of India is doing lots of efforts in this field so that the objective of inclusive growth can be achieved very soon. A great achievement of the Indian government is a big jump in the literacy rate from 18.3 percent in 1950-51 to 74.04 percent in 2010-11. Kerala with 93.91 and Mizoram with 91.58 percent lead and inspire other states to achieve further heights. Such an achievement is the result of a lot of efforts by the Indian government in the education sector. The government is improving the educational status of the country to raise the standard of living of the people and achieve other goals like poverty and unemployment, social inequality, unequal distribution of income etc. As the overall development of the country. Education is not only a means of increasing efficiency but also an effective means of broadening and enhancing democratic participation and upgrading the overall quality of individual and societal life (Goel, 2008). Thus, the importance of education can't be ignored. <sup>8</sup>

- **Investment in Training and Economic Growth**

Human capital is a vital factor for an individual, firm and national economic growth. Whereas education provides positive economic returns, training appears to offer further benefits in terms of higher employment stability and is quite portable among jobs. In fact, a strong complementarity is found between the various types of human capital investments: early achievement and qualifications are important determinants of future educational attainment, individuals with higher educational attainment, in turn, undertake more training on the job, and those who have undertaken training in a previous period - with the current, but even with a former, employer - are more likely to participate in further training. There is some indication that workers and employers tend to share the returns from training - and thus possibly its costs.



Source: Training and Development - Issues in the Indian Context

In the present era of globalization, there is an imperative need for an employee with extraordinary skills which adds the potential to perform better. Human beings are naturally gifted with the potential to learn. It is up to us to leverage this inherent potential and achieve what we are destined to. There has also been a rapid transformation in organization structure and work practices. These changes are sure to have a significant impact on workplace training and development.<sup>9</sup>

#### **Present Scenario and need for Training in India**

In most empirical studies, training is distinguished from formal school and post-school qualifications (which are viewed as education) and is generally defined in terms of courses designed to help individuals develop skills that might be of use in their job. Training is a planned and systematic effort to change or develop knowledge/skills, behavior through learning experience, so as to achieve effective performance in an activity or range of activities. It is a very important aspect of any economy.

In India, different aspects of training are as follows:

- **Vocational Education and Training:** Vocational Education refers to vocational courses being offered in school for grades 11 and 12 students under a centrally sponsored scheme 'Vocationalisation of Secondary Education' and Ministry of Human Resources Development (MHRD) has its overall responsibility.
- **Modern Training Practices in Various Organization:** There are several kinds of training methods used by trainers in organizations. The training program designer needs to identify each of these in order to determine the best way to meet the training objectives. Some of the methods are lecture method, case study method, conference, in-basket method, T-group training, role play exercise, induction training, cross-functional training, creativity training, diversity training, refresher training, and safety training etc.
- **Corporate Training Initiatives in India:** In the last 10 years, business organizations in India have made outstanding progress in terms of their training initiatives. This is mainly due to the boost in competition and because of the entry of multinational companies in India, which has required them to look for various alternatives to develop organizational effectiveness.

Therefore, the training system in the Indian economy has been reformed to create a smarter workforce and produce better results. The optimum human capital is the goal of any economy and training is a means to enhance outcomes.<sup>10</sup>

#### **Conclusion**

Without a proper education system, a country can't develop. The educated citizens can bring the real development in a country. That is why all the developed countries spend a major proportion of the GDP on the education & training sector.

In conclusion, emphasis on human capital will have a spillover effect on every sector of the Indian economy, lead to increased output and ultimately reduction in poverty. India is the second most populous country in the world, with the largest school-age population in the world. The combined public expenditure of central and state governments on education has been around three to four percent of GDP since 2001. The government spends less than one percent of GDP on higher education. Expenditure on education needs to be increased to more than six percent of GDP.

Despite all such problems, Indian education scenario embracing all sectors is one of great and gigantic expansion and it is certainly on the upward swing. The steps taken by various agencies such as the UGC, the AICTE, the IMC, etc., and the various educational bodies such as NCERT, SCERT, CBSE and the private professional bodies and management associations will certainly bear fruit in the long run and make India a Knowledge Society and an attractive educational destination for today's globalized world.

We need to impart skills, training and education at all levels to match the needs of a changing India. Human capital is the pivot around which the long-term transformation of our economy has to be shaped. We need to enhance public-private partnership to further strengthen our systems and standard of education so that it serves all classes of society. A close partnership between government, educational institutions and industry can change the entire ecosystem and drive it towards uplifting the skills and capabilities of the nation and achieve this with a scale that is required for our growth ambition.<sup>11</sup>

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