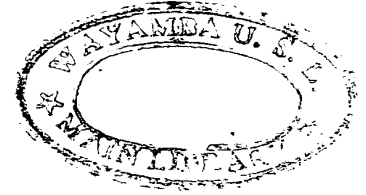


Analyzing the Unemployment of Sri Lanka; Theoretical Aspects and Recent Trends.

RAVINDRA DEYSHAPPRIYA

Uva Wellassa University
SRI LANKA

ravipdn@yahoo.com; ravindra@uwu.ac.lk



Abstract:-

Sri Lanka is an emerging economy in the Asian region with higher level of social development compared to the other Asian counterparts, in terms of health and education. Despite the social development, country has been suffering from two digits severe unemployment problem from several decades. On the other hand, it was affected by civil war nearly 30 years, increasing the level of unemployment and accounting for low economic growth to Asian neighbors. This paper clearly indicates the current trends in domestic unemployment and theoretical aspects as well. More specifically several hypotheses of unemployment have been analyzed in the context of Sri Lanka. It has been observed that, even if there is a decline pattern of overall unemployment, still educated youth are suffering from structural unemployment, which in spite of their relatively high level of education waits for a long time before entering the work force. Therefore appropriate policy changes are strongly recommended to reduce the level of unemployment, leading to steady economic growth as well.

Keyword: - Emerging economy, Social development, Structural unemployment, Economic growth

1. Introduction

1.1 Back ground of the study and definitions

Undoubtedly labor is a precious resource for every economy when they are trying to attain a steady economic growth and development. However a number of problems may be occurred, unless the government utilizes the labor force of a country for the process of production effectively. The major problem related to labor force is unemployment. It can cause for drastic economic and social problems which arise severe obstacles for economic growth and development. Currently problem of unemployment is a highly discussable title among the economists and policy makers as it is a global phenomenon in both developing and developed countries. According to the previous facts and figures in the context of Sri Lanka, It has been identified the timely

importance of analyzing the behavior of domestic unemployment. Therefore this article mainly focuses on explaining the unemployment of Sri Lanka emphasizing its definitions, types, theoretical concept, characteristics, causes and remedies as well. It is very hard to find a unique definition for unemployment, but I can get a common idea by gathering several definitions which were used by the different institutions. Basically, unemployment occurs when a person does not have a job even if he or she is willing to have a job. According to the census conducted in 1971, it had been taken unemployment in to account as the people who are searching a job at the time survey was being conducted. Apart from that in 1981, unemployment has been calculated by subtracting the extent of people who didn't have a job from the midyear labor force. Central bank of Sri Lanka have defined the unemployment as the people who didn't have a job during the particular period even

though they were willing to do a job and also waiting for a job. The Department of Census and Statistics (DCS), which is responsible for the Labor Force Survey (LFS), defines a person as unemployed based on if he or she is available for work, is actively looking for work and has worked less than one hour the preceding week (Bell et al, 1999:2) Furthermore the rate of unemployment is defined as the number of unemployed persons as a percentage of the total labor force (Central Bank of Sri Lanka, 1999:62). Generally this is the concept that is used to measure the level of unemployment in the country, is known as unemployment rate.

However generally, people who have some kind of job but he or she is temporarily absent from work due to vacation, illness, strike and bad weather is not counted as unemployment. Moreover these sources have mentioned three criteria to be satisfied by the people if they are counted as unemployed people. (Andre, 2004)

- 01) He or she must not have a job.
- 02) He or she must be qualified to take a job.
- 03) He or she has looked for a job in the preceding four week.

1.2 Characteristics of labor market in developing countries

The labor market is functioning in terms of demand and supply of labor. As stated by Kelly (1992): Labor market outcomes are conditioned by the quantity and quality of labor inputs (skills, participations rates) and by the internal operations of the markets, which themselves are constrained by market structures, the availability of information or signals of disequilibrium, and the transactions costs which govern the flexibility of market responses to those signals. (Kelly, 1992:1) In other words, the demand for labor depends on the functioning of the economy and the labor market. The supply side of educated labor is responding to the demand for labor in the labor market. This demand is strongly related to investments in human capital. It is important that the demand for and supply of labor is

strongly related to one other, otherwise, the chance for mismatch is big.

The labor market in developing countries is often characterized by a fast growing supply of labor. In most low-income countries, the supply of labor is increasing at 2.5% per year or more (Perkins et al, 2001:282). The labor force is determined by three factors: the size of the population, its composition in terms of age groups and sexes and the labor force participation rates of these groups, which reflects social factors such as educational patterns and the women's willingness to work outside the home (ibid: 292). The rise in the number of potential workers is then, of course, closely related to the growth of the population. Since the health conditions has been improved in many developing countries the population growth has increased, which in turn has resulted in a faster labor force growth. The largest share of the labor force in developing countries is occupied in the agricultural sector. Even though the significance of industry and service sector has increased, the agriculture is still the dominant sector (Lakshman, 1997:37).

Another well-known feature of developing countries is that the wages are generally low and that differences in wages between workers are big depending on different skills and education. It is usual that a skilled worker earn about 40-100% more than their unskilled counterparts (Perkins et al, 2001:284). A final characteristic of labor in developing countries is the underutilization of available labor supply. This underutilization means that people have some kind of jobs, and may even work for many hours, but their contribution to output is small (ibid). The labor markets in LDCs are usually seen as imperfect markets, since competitive forces do not determine wages. The structure of labor markets consists of an urban formal sector, an urban informal sector and rural employment (ibid: 286). The urban formal sector consists of the government and large-scale enterprises. This is the sector where almost everyone would like to work because of compensation for greater stability, attractive benefits and prestige and, principally the most important, they pay the highest wages (ibid: 287). The wages are higher in this sector

because it to a large extent hires people with secondary and university degree. Another reason is that the government pushes up the wages to a certain level, for instance through minimum wage laws. This minimum-wage legislation can improve the wages and working conditions for the workers if it is effectively used, but at the same time, it limits the possibility for firms to hire more workers since the costs of labor is rising. It also limits the creation of more enterprises. If we look at it in this way, minimum-wage laws harm the much larger group of labor that is either unemployed or work in the informal rural sectors (ibid:307).

According to the efficiency wage theory, workers' productivity is a positive function of the wage paid. In other words, better-paid workers may be more productive. At the same time, if the wages are not competitive, the labor tends to produce at a lower rate. The high wages contribute to the fact that most people would like to work in the formal sector. Not everyone can find a job there though, and this leads to a queue of workers that rather stay unemployed than taking a job outside the formal sector (ibid: 289). However, such behavior can be pursued only by those who can afford to remain unemployed while they search/wait for a job in the urban formal sector. The poor people cannot afford this type of behavior and therefore have to take the less preferred jobs that are offered. Alongside with the urban formal sector is the urban informal sector. This sector is characterized by a large number of small enterprises and service activities. These tend to operate like monopolistically competitive firms with ease of entry, excess capacity and competition that drives the profits down to the average supply price (Todaro, Smith, 2003:325). Because it is easy to enter, the urban informal sector market tends to be in equilibrium (Perkins et al, 2001:290). However, the wage level is considerably lower than in the formal sector. The last sector is the rural labor market. Rural employment in LDCs means work by family members for a share in the output of a family enterprise, that is, not for wages. Even if they work primarily in the agriculture, they often need to rely on small-scale non-agricultural

activities in order to provide supplements to agriculture income (ibid: 291). In this sector the wages are very low, even lower than the one paid in the urban informal sector. In the developing countries the main cause of the employment problem has been the rapid population growth and labor force relative to the natural resources. But problems also have occurred on the demand side of the labor market. Even when, for instance, the capital stock has increased faster than the labor force, the capital stock has been developed in ways that has kept labor absorption below its potential. However, in order to address the employment problem, little can be done on the supply-side. Of course the government can reduce the growth of labor by limiting population growth, but that will be in a long run perspective. In order to solve the problems in a shorter term, the policy makers must therefore concentrate on the demand side. There are many different kinds of policy that affect the economy's ability to create jobs for a growing labor force. The demand curve for labor shifts for example outwards due to industrial policy, foreign trade and educational policies. It is also possible to increase the demand for labor by moving down, along the demand curve for labor. This is kind of labor creating policy is therefore to adjust the wage rate. Once it was widely believed that by increasing the supply of skilled labor, the employment would expand, generally through an increased absorption of complementary unskilled labor. The effect on the general employment is hard to determine, but for the skilled labor force, there is a risk for unemployment since there might be too many of them in relation to the production structure in the country (ibid: 306). As stated before, the demand for educated labor is dependent upon economic growth and the overall demand for labor, whereas the supply side for educated labor is responding to the demand for labor in the labor market.

1.3 Types of Unemployment

Frictional unemployment

Frictional unemployment occurs due to the imperfect information in the job market. When

the information in the job market is imperfect it takes time for unemployed workers and employers with jobs to meet each other and as a result of that people have to suffer from unemployment until meet them each other. If the information in the job market is perfect and costless then frictional unemployment will not take place. Currently world has globalized and information technology has marked a tremendous improvement globally. Therefore frictional unemployment exists relatively short duration because when the both parties meet each other frictional unemployment will clear. Even though this kind of unemployment affects relatively large number of people. Moreover Frictional unemployment will result severe economic costs, but some economic benefits as well. For example, time period of frictional unemployment may help to select the better job for unemployed people and also find a better worker for employers according to their preferences.

Structural Unemployment

Most of the time economy has different kinds of jobs even though people do not like to accept those jobs due to the mismatch with their expectation as a result of that structural unemployment arises in the economy. This mismatch may be related to skill, education, age or any other factor. With the spread of free education system people become more erudite and they always eager to have a employment which is match with their qualification and skills. For example most of the Sri Lankan arts graduates suffering from structural unemployment because even if they have educationally qualified, most of them not professionally qualified enough to hold a better job in the current society. Not like Frictional unemployment, structural unemployment will exist long term in the economy. However both Structural and Frictional unemployment related with the job search, but the main difference is the speed which the job search process is completed. That means the process of job search end up relatively quickly with Frictional unemployment than the Structural unemployment.

Cyclical Unemployment

This kind of unemployment arises due to the insufficient aggregate demand in the economy. As a result of that, economy doesn't have fair situation to generate enough jobs for job seekers. Therefore cyclical unemployment is also called "demand deficient unemployment". Cyclical unemployment is related with the business cycle and it implies that at the upswing of the cycle, unemployment decrease due to growth of production. On the other hand in the recession, firms cut down the production and don't willing to hire new workers due to less demand for goods and whole these things results to increase the unemployment in the economy. Firstly low skill workers and non educated workers suffer from cyclical unemployment and after that the effect spread up to high skilled and educated workers also unless the prevention action will not be taken.

2. Literature Review

Before we start the discussion about previous research, we want to make one thing clear: The word "mismatch" is used frequently in earlier research about the Sri Lankan unemployment problem, and we believe that it is important to explain the different contexts in which this term exists. We do this since we had some troubles to make a distinction between them. In fact, there exists a mismatch on the labor market where the demand for educated labor is less than the supply of it. This is an empirical fact, since this mismatch is reflected in the high rate of unemployed educated youth. In other words, there are fewer jobs with educational requirements than the supply of educated workers. The logical outcome of this is unemployment. There are, however different kinds of hypotheses developed to explain this kind of mismatch and one of them is called the Mismatch theory. We will try to give a brief summary of the different explanations below.

The high rate of unemployment in Sri Lanka have concerned researchers, policymakers and the international community for a long time

which has resulted in a lot of research and literature in the topic. Several explanations have been proposed and the most accepted explanation though is the Skills Mismatch hypothesis. It was first articulated by the International Labor Organization (ILO) in the 1970s and was further researched by Glewwe (1987) and Dickens and Lang (1996) (ref in Bell et al 1999:3). This theory suggests that the educational system of Sri Lanka does not produce the skills that are valued by the employers. At the same time it raises the expectations of those who acquire them. This means that the unemployed are not interested in the available jobs. At the same time the employers will not hire them since they lack the skills needed. This hypothesis argues that the reason for the high rate of unemployment among the first job seekers is that this group has just finished school, and has therefore not developed the skills needed out of earlier work experiences. This theory suggests that in order to defeat the unemployment problem, the educational system needs to be reformed through skills development and vocational training with more connection to the labor market (ibid). However, Bell et al is questioning the Skills Mismatch Hypothesis because none of the analyses have any empirical evidence that education attainment raises the expectations of income even more than the actual income, which they mean are a critical foundation for the Skills Mismatch Hypothesis. Aturupane (1997) showed in a study that the private returns to schooling are high, especially at the highest rates of education, which goes in the opposite direction of the skills mismatch theory and shows that the educational system is well geared towards the labor market. (Ref in Rama 1999:4). Still, Bell et al argues, that conclusion does not object the fact that some of the unemployed do not have the skills most commonly required by currently available jobs. They call this a 'functional' mismatch that exists because of structural obstacles like wage rigidities and governments employment and pay policies (Bell et al, 1999:ii).

Another explanation to the unemployment problem is the Queuing hypothesis linked to public sector employment and wage policies.

This theory is also suggested by Glewwe (1987), and was developed by Bowen (1990) and Dickens and Lang (1996). They argue that public sector workers have a lower wage than those in the private sector in a well functioning labor market. This is so because of compensation for greater stability, attractive benefits and prestige and lower work efforts that exists in the public sector. This is not the case in Sri Lanka though, were the public servants both get all the mentioned benefits and a higher pay. As a consequence, the fresh graduates prefer to wait for the jobs in the public sector and thereby choose to stay unemployed for a while instead of taking jobs outside the public sector (Bell et al, 1999:3). This hypothesis can therefore be seen as a mismatch between expectations and available jobs. The solution to this type of problem is to reform the way the public sector recruits their staff and establish wage policies to stop this queuing behavior (ref in Bell et al, 1999:3). Even this part is questioned. Rama claims that there is no hard evidence to support the claim that public sector jobs are more attractive than the private sector ones. He claims that Glewwe compared average earnings across sectors and skills, to show that the government pays more. This comparison was for broad groups of workers though, and not for individuals with similar characteristics.

The data were from 1969 and Rama claims that the relative earnings might have changed (Rama 1999:5). Bell et al on the other hand, argues that strong job preferences partly explain the unemployment problem since they found that when using a narrow definition of unemployment where only those who reported as willing to take any job are considered as unemployed, the overall unemployment rate fall dramatically. (Bell et al, 1999:ii). They also find that there is substantial evidence of labor market segmentation which provides a rationale for the unemployed to wait for so-called "good" jobs. The third explanation is that the labor market regulations create a wedge. This explanation is connected with Rama (1994) and suggests that the labor market regulations discourage employers to hire new staff in their enterprises since they make it very hard to terminate unwanted

workers. The Termination of Workmen Act (TEWA) is regulating enterprises with at least 15 employees and provides life long tenure. Small firms with less than 15 workers have on the other hand no job security at all. The same goes for the Export Processing Zones (EPZs). This is a duality that means that the unemployed prefer to wait for the regulated jobs. The solution would be to reduce the wedge between TEWA protected and the unprotected jobs (ibid). As the reader probably have noticed, the theories “be or not to be” is depending on the data used, and how to interpret it. Since we have not made any surveys ourselves it is hard to know what data to rely on. The conclusions are hard to isolate between the different explanations. They are all connected and the outcomes influence each other. We have been using some of the outcomes from most of the different surveys discussed above.

3. Problem Statement and Objectives of the Study

In economists point of view unemployment may cause to sever economic and social problems, especially in long term. In the context of Sri Lanka, most of the people have been suffering from unemployment even if they are well educated. Furthermore it can be identified age specific pattern of unemployment in the current society. According to the literature, there are several studies have touched this issue in the context of Sri Lanka and globally as well. However the trend of unemployment can differ with the time, political states and the economic transition. Therefore dated studies are highly needed to analyze the recent trend in unemployment. I completed this study with the aim of filling this gap and to put forward updated analysis.

Main two objectives have been engaged with this study.

01. Identify the theoretical aspects of unemployment
02. Identify the recent trends in unemployment in Sri Lanka.

4. Methodology

Throughout this study I didn't employ much complex quantitative methods to analyze the data, since the problem should be investigated in a qualitative manner as which gives more realistic outcome. Data were collected by using secondary sources, especially annual reports of Central Bank of Sri Lanka. Firstly I presented few theories about unemployment and finally used descriptive methods to identify the trend in unemployment during the period of 1990 – 2009.

5. Theories of Unemployment

In this section, two main theories of unemployment and three important hypotheses are considered to be explained.

Classical Theory of Unemployment

According to F.A. Hayek and his colléauges, classical theory of unemployment can be occurred due to the increase of real wages and the Labor demand and supply always related with the changes of real wages. The intervention of trade union and government wage regulations cause to increase the money wages and also it will results to rise the real wages if the price level remain constant.

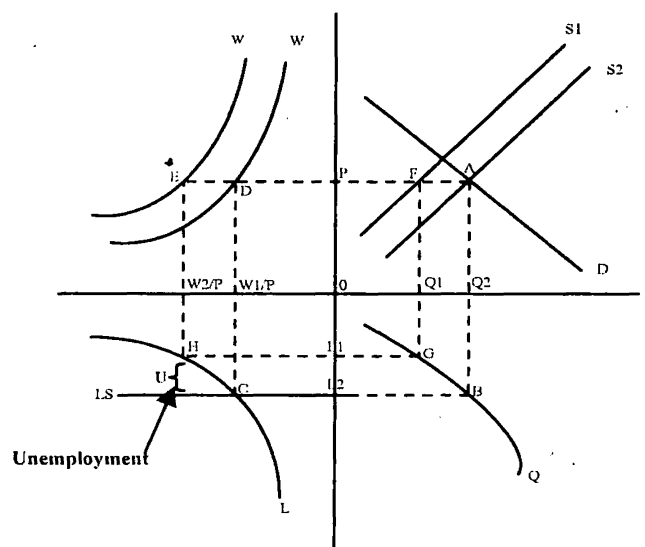


Figure – 01: Classical Unemployment

The initial equilibrium is shown by points A, B, C and D related to W money wage level and after that we will assume that money wages

were increased by the government due to the trade union influence or due to the government wage regulation. As a result of that wage curve shifts upward and real wages also increase automatically while price level remains the same. Then the product market comes out from the equilibrium and excess demand has taken place from the extent of Q_1 - Q_2 , because producers reduce their production as the cost of labor has been increases and also they hire only L_1 level of labor instead of L_2 in the initial equilibrium. Therefore it is apparent that the extent of labor L_1 - L_2 was fired by the firm because of increasing the real wage. In fact the extent of L_1 - L_2 is the unemployment introduced by the classical economists which is occurred due to the increase of real wages. Classical economists pointed out that this unemployment will clear if government keeps labor market more competitively by controlling trade union power and minimizing the regulations on money wages.

Keynesian Theory of unemployment

In the classical theory of unemployment, they assume that price level is unchanged while money wages increases. But according to the Keynesian theory unemployment will take place not due to the increase of real wages but it associates with the deficient demand due to the increase of the price level.

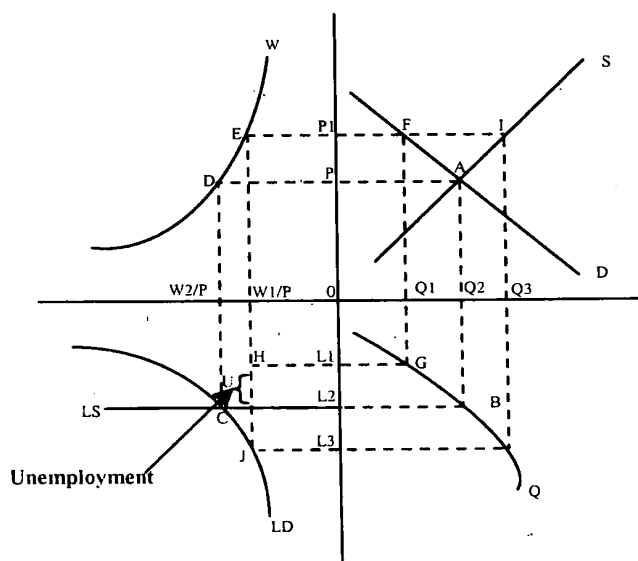


Figure – 02: Keynesian Unemployment

According to the above graphical illustration the initial equilibrium is shown by the points

A, B, C and D and as price level increases firms tend to produce more although consumers demand less. Therefore excess supply takes place equal to the extent of Q_3 - Q_1 associates with the points F and I. In this situation, they have used L_3 level of labor to produce Q_3 level of output. Immediately producers realize that it is not efficient producing Q_3 level of output as consumers demand only Q_1 . Therefore they reduce the production up to Q_1 which is used only L_1 level of labor. As mentioned above, even if firms used L_2 level of labor in the initial equilibrium ABCD, finally they decrease the level of labor up to L_1 which is utilized for their production. As a result of that, from L_1 to L_2 shows the extent of unemployment explained by the Keynesian theory.

In addition to this main two theories of unemployment, there are three crucial hypotheses can be identified. The most important hypothesis developed is the prevalence of a skills mismatch where the education system is not providing what the labor market needs. Another explanation is that the public sector employment and wage policies operating in the country lead to a queuing behavior among the population for the attractive jobs. The third hypothesis is that the existence of stringent labor market regulations prevents employment creation. The previous empirical researchs regarding these explanations are considered to analyze in the next section.

6. Analyzing the Unemployment of Sri Lanka

Not only the past few decades, currently also is Sri Lanka suffering from high level of unemployment problem. Therefore it is timely important to analyze the behavior of Sri Lanka unemployment and discover the main causes of it. In that sense this section is used to reveal causes of domestic unemployment and identify the trends of unemployment. The appearance of high unemployment rates and low economic growth in Sri Lanka can be looked upon with some degree of surprise. There are several advantages that would attract foreign investors to the country, which would generate

economic growth and employment opportunities. For example, Sri Lanka is a country where the wage levels are among the lowest in the world, comparable with Bangladesh and China. The labor force has an unusually good educational level for a low-income country and it has a strategic location between the Western and South-East Asian markets. In relation to other developing countries the infrastructure is well functioning. Concerning the tourism, one could argue that Sri Lanka has a stronger comparative advantage with its use of English, nice beaches and the variety of the nature in the island in comparison with its neighbors (Catterson, Lindahl, 1997:24). So, with all these advantages, why is the unemployment still persistent?

4.1 Causes of Unemployment of Sri Lanka

The Ethnical Conflict

One logical explanation is the existence of the ethnical conflict that has plagued the country since the beginning of the 1980s. The ethnical conflict has kept the country's development far below potential and it has absorbed a large amount of the Government's budget, which has created a persistent budget deficit. The armed conflict has also made foreign direct investment less attractive and delayed the development of the tourism (Catterson, Lindahl, 1997:20). Catterson and Lindahl claim that in the absence of this conflict, the tourist industry in Sri Lanka would have been the leading one in the world today. This kind of industry would have had multiplier effects on the construction, service industries etc., which could have contributed considerably to employment creation and economic growth (ibid: 24). However, some studies have implied that the worsening in the labor climate is more deterrent for foreign investors than the political problems in Sri Lanka (Lall et al, 1996:122).

Universal Free Education and Population Growth

Another troublesome feature in Sri Lanka is the population growth in relation to the

educational system. In order to give poor people a chance for upward social mobility, the independence socialist regimes expanded the state sector through state institutions and public enterprises such as factories, banks and infrastructure projects. This gave poor people the opportunity to change their situation of life through formal education. As the education became free, it did not take long before the demand for such employment far outstripped the supply (Hettige, 2000). This behaviour is in line with the theories about the demand for education, referred to in the second section. As the labor market gets tight, people demand more education in order to secure a modern formal sector employment. School enrolment increased rapidly in Sri Lanka and in combination with improved health and social conditions, the population grew very fast from the mid-1940s. The economy was not capable of keeping up with the high rate of population growth, especially in the 1960s and 70s. This resulted in a huge expansion of the young population and with that, a substantial rise in the proportion of a school going group in the country, and also, an increasing number of people with paper qualifications from school. The competition for public sector jobs was hard and in order to secure employment like that, one needed special contacts with the employers. Politicians often used this situation in order to gain political support, which led to kinship behaviour in the political life (ibid).

The Skills Mismatch Hypothesis

Even if the ethnical conflict and the population growth have been contributing factors to the unemployment problem, the most widely accepted explanation is the Skills Mismatch hypothesis. This theory suggests that there exists a skills mismatch between the educational system and the skills demanded by the employers. Even though this theory has been questioned, on grounds based on the inventor of the theory's methods and choice of data all of our sources agree that the educational system does not equip the population with the skills needed in the country. This is also stated by domestic sources, for instance, in a thesis written by the Sri Lankan government in 2003 (Government

of Sri Lanka, 2003:73) and the Central Bank (Central Bank Annual Report 2003:156). Since more than 70% of the Sri Lankan population have enrolled in secondary education, the labor market has problems with absorbing all the job seekers with more than basic education.

Therefore it has been argued that there is a need for job market oriented training, a so-called vocational training. The main problem is that the linkages between the education and training system in Sri Lanka and the employing sectors are weak. However, studies have shown that the vocational training provided in the country has not gone through any proper needs analysis and, as a consequence, the return on investment in vocational training has been less than expected. The employers do not know what to expect from the trainees since the programs over the country have different standards on the same skill area (Master Plan for Rural Development, 1999:12-5) Training and education rise the expectations of the population of securing a so-called "good" job. But as the labor market cannot absorb all the educated, frustration emerges, which is reflected in the several riots, strikes and the decline in work ethics that has plagued the country since the 1960s (Hettige, 2000). In order to create more jobs for the educated, the links need to be strengthened and the system needs to be reoriented from supply- to demand side objectives. Kelly suggested this already in 1992 and claimed that there seems to be a believe that training creates job opportunities in Sri Lanka.

However, this is not the case, since the training has not favoured the skills in technical subjects, which is what is needed in Sri Lanka. Training should be provided for first job entry instead for some skill upgrading for the employed since this is ineffective. Skills should not be valued in and of themselves, but rather for what they produce (Kelly, 1992:15). Even at the university level of education the mismatch of skills demanded and supplied is obvious. For instance, a huge amount of graduates are in civil engineering rather than in disciplines that are appropriate for industrial technology. Textile engineers are the most

relevant to the country's main export, but in 1996 less than 1 percent of the university graduates had these skills (Lall et al, 1996:116). The problems with the skills mismatch are exacerbated by the governmental education policies. Traditionally, the education has mainly been provided by the government since private schools has been forbidden and considered as elitist. At the university level, the governmental monopoly has not worked well since it has not been able to keep up with international innovations. Regarding the vocational level, the monopoly has led to a centralized training system that has not taken local conditions into account. Therefore, the training should be managed by the private sector and the local industry in order to be more demand based and create a stronger linkage between the training system and the labor market. The private firms, on the other hand, might be reluctant to invest in human capital as they cannot be sure that the skilled worker will not leave for another company with higher wages. This externality problem might be solved by letting the government be the financier rather than the manager and that firms should be encouraged to provide training linked to the labor market (Kelly 1992:16).

In short, we can state that the Sri Lankan educational system leads to expectations among the graduates of securing First World employment while the labor market still mainly offers Third World employment opportunities in the rural agriculture and in the labor intensive, low value product industries.

The Queuing Hypothesis

The queuing behaviour for "good" jobs is another contributing factor to the unemployment problem in Sri Lanka. We have found it a bit hard to distinguish this hypothesis with the skills mismatch, since this queuing behaviour also can be seen as a reflection of a mismatch between expectations of securing a so-called "good" job and the actual supply of those kinds of jobs. In Sri Lanka the problem of unemployment is not that there is a shortage of jobs, rather that there is segmentation between jobs that are of great demand ("good" jobs) and those which are not

in demand ("bad" jobs). In other words, the jobs supplied do not correspond to the preferences of the educated (Bell et al 1999:11). One factor to explain the queuing behaviour is that there exists a divide between the public sector and the rest of the economy. This has its origin from the British ruling. After the independence a public sector job became a part of the political patronage that developed. In those days a public sector job was associated with modern society, security, attractive benefits, pensions and limited working hours. Today public sectors jobs are still characterized as "good" jobs in Sri Lanka since they offer more stability, lower work effort, attractive benefits and higher pay than the private sector (Catterson, Lindahl, 1997:35). Another factor for the queuing behaviour comes from the fact that some jobs enjoy a much higher security with the TEWA regulation (Bell et al, 1999:11). The few jobs (15%) that are covered by TEWA are highly demanded by the workers because they enjoy higher protection, wages and better benefits than other jobs in the private sector. (ibid: 11).

Consequences of these factors are that the educated unemployed prefer to wait or queue for the "good" jobs rather than taking a job that is below their dignity. Many researchers claim that parents' supports of the unemployed reinforce the queuing behaviour. While the graduated wait to be offered "good" jobs, they rely on their parents. This means that the queuing behaviour is a phenomenon for well off families, since the poor cannot afford to wait for the preferred jobs (Ahmad, 1999:38). Ironically it is a luxury to be unemployed since only the privileged can afford it. Therefore, one can state that the private return to education is higher for the graduates with a rich background. A proposed solution to these problems is to reform public sector recruitment and wage policies since it would discourage this "queuing" attitude (Bell et al, 1999:3). Efforts should also aim at removing all the benefits that are associated with the "good" jobs, and also improve the protection of the so-called "bad" jobs (Rama, 1999:24).

Stringent Labor Market Regulations

The third explanation is closely linked to the above mentioned hypotheses. It regards the labor market regulation, of which TEWA is considered to be the most important. As stated before the jobs covered by TEWA are seen as "good" private sector jobs by the employees since it offers a high security in relation to the other jobs in the sector. However, for the employers, the situation is the opposite. It hinders the creation of new jobs and it has a negative impact on productivity. Workers do not have to be afraid of getting fired due to bad performance, incompetence or inadequate skills. There is a stronger tendency of organizing labor union action or demand higher wages under circumstances of high job security. Because of this, the employers try to circumvent TEWA, through hiring short-term and subcontracted workers and creating smaller firms with less than 15 employees. This is also bad for the productivity since small enterprises are stated to suffer from lower productivity because they cannot achieve economies of scale (Bell et al, 1999:18).

The labor costs in the TEWA-regulated enterprises are expensive since the severance pay is generous and the wages are high in relation to the jobs outside of the protected sector. The wages are set by some minimum level standards (Rama, 1999:21). As stated in the second section, minimum wages are, if efficiently used, good for the worker in terms of higher wage and better working conditions, but at the same time, it limits the possibility for the enterprises to hire more workers since the costs of labor is rising. It thereby limits the creation of more firms and as a consequence, these laws harm a larger group than they benefit. One way to reform the labor market regulations is to reduce the gap in protection of jobs, and remove the benefits that associate with the "good" jobs and instead improve the quality of bad jobs. Doing so, the income security to workers will not burden employers and support the private sectors capability to create "good" jobs. In other words, as the regulations are less stringent, the employers

will be encouraged to create bigger firms and thereby increase the productivity. From a worker's perspective, the supply of "good" private sector jobs will rise to a certain extent and the queuing behaviour will be reduced.

4.2 Trend and Characteristics of Sri Lankan Unemployment

Overall and sex based unemployment

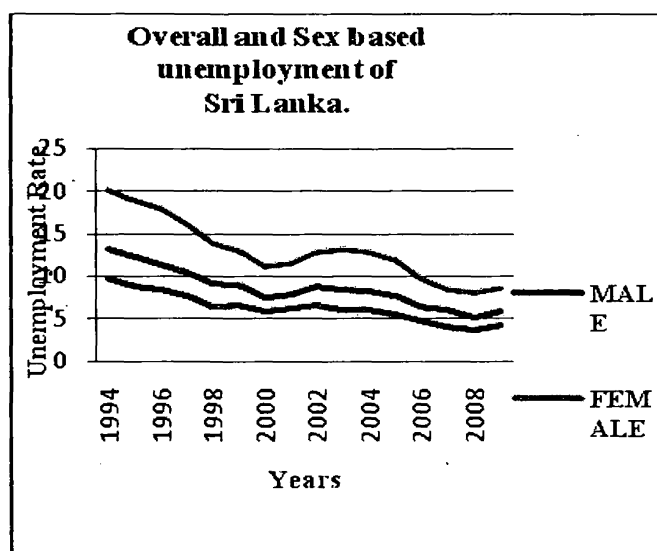
Unemployment has historically been a very sensitive issue in Sri Lanka. This is mainly due to that the high levels of unemployment have predominantly been concentrated among educated youth. According to LFS the unemployment rate is estimated to be 7.6% (excluding Eastern province) in the fourth quarter of 2003. This means that of all economically active persons in the country 7.6% are unemployed. It is the lowest rate that has been reported after the year 2000. The official unemployment rate has shown a declining trend since the 1970s, from 24 % in 1973 (Lakshman, 1997:241), to 7.6% in 2003 (Labor force survey Fourth quarter, 2003). A contributing factor to this decline is that fewer women are unemployed now, while the male unemployment has been static. Since the 1980s, employment opportunities have grown much faster for women than for men (Lakshman, 1997:241). Following graph clearly indicates that there is a decreasing pattern of unemployment during the past two decades and it can be seen the unemployment rate among the female is quite high compared to the male counterpart during the same time duration. However in 2009, overall unemployment as well as sex based unemployment also has increased compared to the previous two years.

Age-Specific Unemployment

According to the latest report of LFS, and annual reports of central bank unemployment is highest among the people between 15 -19 years. As table - 1 below indicates, nearly 80% of all unemployed are under 29 years of age. This rate is to a very high degree related to the

first time job seeker's entrance into the labor force (Catterson, Lindahl, 1997:27). In the age group 15-19 and 20-24 the male unemployment rate during the last years has exceeded the female rate. Nevertheless, the female unemployment rate is dominant in the age group 25-29 and 30+. A comparison of the unemployed in the late 1960s with those in the beginning of the 2000s reveals an improvement in some spheres and worsening in others. Unemployment related to the all age group has increased 2009 by little amount compared to the previous year, even though unemployment rate has shown a decreasing pattern in generally during the considered period.

Figure - 03 Overall and Sex based unemployment of Sri Lanka.



Source: Annual Rapports of Central Bank of Sri Lanka

Education and Unemployment

Sri Lanka's policy of universal free education has led to a relatively educated population in comparison of its low level of income. In spite of this, surveys indicate that the rate of unemployment is concentrated among the educated youth. A quotation from the ILO describes the situation in Sri Lanka well "The more a young person had been educated, the greater the likelihood that he or she may be unemployed" (ILO, 1971:28, Ref in Lakshman, 1997:244). In LFS 2003 (second quarter) 56% of the unemployed were with

qualifications of GCE O/L and GCE A/L, while it was 27% in the late of 1960s (Lakshman, 1997:244). This might depend on the fact that a bigger share of the population is acquiring secondary schooling today than in the 1960s since the education is free.

Table – 01: Age Specific Unemployment

Year	Age groups(Years)			
	15-19	20-29	30-39	40 and above
1990	40.1	30.3	8.4	4
1991	37.6	27.5	9.1	3.6
1992	39.1	27.5	7.8	3.5
1993	38.4	25.2	8.4	3.3
1994	40.7	24.5	7.6	2.5
1995	60.5	31.7	8	2.9
1996	36.5	22	6	1.9
1997	34	21.9	5.2	1.7
1998	27.3	19.3	4.9	2
1999	28.4	18.9	4.4	1.6
2000	27.2	19.7	3.9	1.4
2001	29.2	20.2	3.8	1.5
2002	30.1	20.1	4	1.6
2003	30.3	19.4	3.9	1.1
2004	28.3	19.2	4	1.3
2005	30.8	17.2	3.8	1.2
2006	23.1	15.9	3.3	1.4
2007	21.6	15	3.1	1.2
2008	20.6	13.2	3.1	1.2
2009	20.9	15.4	3.7	1.4

Source: Annual Reports of Central Bank

Educational attainment plays a major role in both employment and unemployment the key feature of that is unemployment among more educated people has recorded an all time high related to other educational group. When people are rich with educational attainment, they prefer to find higher level job according to their qualification and sometimes they reject jobs which are mismatch with their qualification. As we mentioned before this mismatch can cause for structural unemployment suffering the more educated people. According to the above empirical statistics in Sri Lanka, we can see people with G.C.E. (A/L) and above educational qualification suffering from unemployment

higher than the people with low educational attainment. Even if, after 2004 their unemployment has decreased dramatically, the major reason for that is the government tactics on graduate and other government recruitments.

Table – 02: Educational attainment and Unemployment

Year	Educational Attainments			
	Year 1-5	Year 6-10	O/L	A/L above
1990	3.3	5.1	23.9	29.4
1991	3.9	4.9	25	24.6
1992	3	4.7	22.2	22.4
1993	3.1	4.9	21.3	23.3
1994	2.6	5	19.6	23.7
1995	1.8	3.4	18.4	20
1996	2.8	3.4	16.4	19
1997	2	2.4	15.9	19.3
1998	1	2.4	13.7	17.5
1999	0.4	1.9	13.6	17.9
2000	1.2	1	12	16.2
2001	1.5	7.2	13	16.5
2002	1.8	7.9	13.3	16.8
2003	1.7	7.4	13	16.5
2004	2	6.9	12.3	16.8
2005	1.8	6.3	11.5	13.8
2006	1.4	5.8	9.9	11.6
2007	1.3	5.2	8.2	11.8
2008	1.1	4.5	7.4	9.9
2009	-	5	8.5	11.2

Source: Annual Reports of Central Bank

7. Conclusion

We have reviewed different kinds of hypotheses developed in previous research in order to explain the mismatch between the demand for and supply of educated workers. In this section we will discuss our conclusions. The high rate of unemployment is to a large extent voluntary. This is so because most of the unemployed prefer to wait for “good” jobs instead of taking jobs below their preferences. Such behaviour can be pursued only by people with wealthy backgrounds. Clearly, there is a mismatch between the educational system and the skills demanded by the employers. A contributing factor to this is that the linkages between the labor market and the educational

system are weak. The level of educational attainment of the population can be considered as too high to be economically justified in a country where a large amount of the labor force is occupied in the agriculture and labor-intensive industries.

At the same time, the high educational level of the people raises the expectations of securing modern sector jobs. Since the country is not capable of absorbing all with paper qualifications, frustration emerges, which is reflected in strikes, social unrest and high suicide rates among the people. It is important to keep in mind that education improves the quality of people's lives and an educated population is never bad for a country. The problem is that the education in Sri Lanka has not been based on industrial demand. The government is thus trying to create 2 million new jobs mainly in the private sector to facilitate the transition to capital-intensive production. The highly educated tend to be absorbed by the public sector because of its higher wages and benefits. In order to take advantage of the human capital though, it is important to address the educational programs towards the areas that are relevant for the country's production. This is important since it is the private, and not the public sector, that mainly generates economic growth. In other words, Sri Lanka needs to make the private sector more attractive for the employees through reducing the gap between the sectors. It is also important to equalize the different jobs in the private sector by lowering the security in TEWA and raising it in the non-protected jobs of today. Doing so, the income security to workers will not burden employers and support the private sectors capability to create "good" jobs. The unemployment in Sri Lanka has puzzled researchers and policy makers for several decades.

The skills mismatch hypothesis for example was first articulated by the ILO in 1970s. All of our sources, both domestic and independent, ranging from the beginning of the 1990s and forward, are in general prescribing the same kinds of reforms. The unemployment rate has only decreased marginally though, which gives us a hint that it is not only the educational

policies and the labor market to blame, rather, it is the economy as a whole that is not functioning well. One contributing factor might be that, in spite of the liberalization reforms in 1977, Sri Lanka is still considered to be relatively closed and caught in low-value production. Last but not least, the ethnical conflict prevailing in the country since the 1980s is an important constraint, since it has absorbed a huge amount of the government's budget and hindered foreign investors to operate in Sri Lanka. Reforms to correct the unemployment problem will in other words not have any substantial impact on the economy unless the environment of the country is peaceful.

References

- Ahmad, Alia, 1999. *Sri Lanka: Institutions, Economic Policies and Economic Growth*. Country Economic Report:1, Sida, Stockholm.
- Asian Development Bank, 2001. *Sri Lanka: Country Economic Review*. Asian Development Bank, 2000. *Asian Development Outlook 2000*. First Edition, Oxford University Press.
- Aturupane, Harsha, 1999. *Poverty in Sri Lanka: Achievements, Issues and Challenge*, World Bank Poverty Alleviation Study in Sri Lanka, Colombo.
- Aturupane, Harsha (Team Leader) – Rasanayagam, Yoga – Siddhisena, K.A.P. – Perera, Sasanka – Gunawardena, Dileni – Perera, Susantha, 1998. *Sri Lanka: National Human Development Report*. Colombo.
- Bell, Eric (Team Leader) – Goonesekere, Rapti – Rama, Martin, 1999. *Sri Lanka: A Fresh Look at Unemployment*. Report No. 19609-CE, Document of the World Bank
- Catterson, Julie – Lindahl, Claes, 1997. *Expectations and Reality: Challenges on Sri Lanka's Path of Development*. Management Perspectives International, Sida, Solna.
- Central Bank of Sri Lanka Annual Report, 2000, 2009. Colombo.

- Department of Census and Statistics, 2003. *Sri Lanka Labor Force Survey, Fourth Quarter 2003*. Colombo.
- Department of Census and Statistics, 2003. *Sri Lanka Labor Force Survey, Second Quarter*
- Government of Sri Lanka, 2002, *Regaining Sri Lanka: Vision and Strategy for Accelerated Development*. Sri Lanka: Poverty Reduction Strategy Paper 2003.
- Hettige, S.T, 2000. "Economic Liberalisation, Qualifications and Livelihoods in Sri Lanka" *Magazine: Assessment in Education: Principles, Policy and Practice*; November 1, 2000. Colombo
- Jayaweera, Swarna, 1993. *Women, Education and Training*. Centre for Women's Research – Sri Lanka. Working Paper No. 7, Colombo.
- Kelly, F. Terence, 1993. *Labor and the Numbers Racket: An Assessment of Labor Market Information in Sri Lanka*. Research Studies, Employment Studies No. 12, Institute of Policy Studies, Colombo.
- Kelly, F. Terence, 1992. *A Strategy for Skills-Development and Employment Policy in Sri Lanka*. Research Studies, Employment Studies No. 12, Institute of Policy Studies, Colombo.
- Lakshman, W.D., 1997. *Dilemmas of Development: Fifty Years of Economic Change in Sri Lanka*. Sri Lanka Association of Economists, Colombo.
- Lall, Sanjaya – Rao, Kishore – Wignaraja, Ganeshan – Addario, Di Sabrina – Akinci,
- Gokhan, 1996. "Building Sri Lankan Competitiveness: A Strategy for Manufactured Export Growth". Report for the National Development Council, Government of Sri Lanka.
- López, Ramón – Thomas, Vinod – Wang, Yan, 1998. *Addressing the Education Puzzle: The Distribution of Education and Economic Reform*. Policy Research Working Paper 2031, The World Bank Economic Development Institute Office of the Director and Macroeconomics and Policy Division, December 1998
- Perkins, H. Dwight – Radelet, Steven – Snodgrass, R. Donald – Gillis, Malcolm – Roemer, Michael, 2001. *Economics of Development*. Fifth Edition, New York.
- Rajapatirana, Sarath – Yatawara, A. Ravindra, 1997. "Sri Lanka in the Post-Uruguay Round Trading Environment" *Upanathi: The Journal of the Sri Lanka Association of Economists Volume 8 No. 1*. Colombo.
- Rama, Martin, 1999. *The Sri Lankan Unemployment Problem Revisited*. Policy Research Working Paper 2227, The World Bank Development Research Group Poverty and Human Resources, November 1999.
- Teams, Consultants in Development, 1999. *Master Plan for Rural Industrial Development in Sri Lanka*. Volume 1, Colombo.
- Tilak, B.G. Jandhyala, 2001. *Education and Poverty*. National Institute of Educational Planning and Administration, New Delhi.
- Todaro, P. Michael – Smith, C. Stephen, 2003. *Economic Development*. Eighth Edition, Pearson Education Limited, Essex.
- Zylberberg, A., 2004 *Labour Economics*. Third Edition, MIT Press.