Sri Lanka’s “Employer of Last Resort” Policy: A Cautionary Tale

Sanjay DeSilva
Department of Economics
Bard College
desilva@bard.edu
Summary of ELS policy

• Not a well defined program, a series of *ad hoc* policies.

• Pre-liberalization, government was the dominant employer in the formal sector.

• Post-liberalization, government has taken up the more limited role as ELS of
  – Unemployed, university (and sometimes high school) graduates.
# Public Sector as Employer of the Educated

## Education Profile by Sector - Male Yr

<table>
<thead>
<tr>
<th>Sector</th>
<th>none</th>
<th>&lt;=5</th>
<th>6-10</th>
<th>O/L</th>
<th>A/L</th>
<th>degree</th>
</tr>
</thead>
<tbody>
<tr>
<td>Salaried Public</td>
<td>0</td>
<td>1.77</td>
<td>31.26</td>
<td>38.17</td>
<td>26.78</td>
<td>2.02</td>
</tr>
<tr>
<td>Salaried Private</td>
<td>0.31</td>
<td>1.49</td>
<td>33.7</td>
<td>41.84</td>
<td>21.86</td>
<td>0.8</td>
</tr>
<tr>
<td>Business</td>
<td>1.05</td>
<td>5.61</td>
<td>44.32</td>
<td>36.02</td>
<td>11.32</td>
<td>1.68</td>
</tr>
<tr>
<td>Farm/Fishing</td>
<td>1.85</td>
<td>11.63</td>
<td>58.05</td>
<td>25.18</td>
<td>3.21</td>
<td>0.09</td>
</tr>
<tr>
<td>Casual Non-Farm</td>
<td>3.57</td>
<td>14.89</td>
<td>62</td>
<td>18.29</td>
<td>1.26</td>
<td>0</td>
</tr>
<tr>
<td>Casual Farm/Estate</td>
<td>6.58</td>
<td>24.76</td>
<td>56.27</td>
<td>10.92</td>
<td>1.47</td>
<td>0</td>
</tr>
</tbody>
</table>

## Sector Profile by Education - Male Yr

<table>
<thead>
<tr>
<th>Sector</th>
<th>none</th>
<th>&lt;=5</th>
<th>6-10</th>
<th>O/L</th>
<th>A/L</th>
<th>degree</th>
</tr>
</thead>
<tbody>
<tr>
<td>Salaried Public</td>
<td>0</td>
<td>2.77</td>
<td>9.78</td>
<td>20.72</td>
<td>38.75</td>
<td>47.92</td>
</tr>
<tr>
<td>Salaried Private</td>
<td>2.85</td>
<td>3.03</td>
<td>13.69</td>
<td>29.47</td>
<td>41.04</td>
<td>24.48</td>
</tr>
<tr>
<td>Business</td>
<td>4.77</td>
<td>5.59</td>
<td>8.83</td>
<td>12.45</td>
<td>10.43</td>
<td>25.4</td>
</tr>
<tr>
<td>Farm/Fishing</td>
<td>14.02</td>
<td>19.41</td>
<td>19.36</td>
<td>14.56</td>
<td>4.95</td>
<td>2.2</td>
</tr>
<tr>
<td>Casual Non-Farm</td>
<td>48.86</td>
<td>44.79</td>
<td>37.26</td>
<td>19.06</td>
<td>3.49</td>
<td>0</td>
</tr>
<tr>
<td>Casual Farm/Estate</td>
<td>29.5</td>
<td>24.4</td>
<td>11.07</td>
<td>3.73</td>
<td>1.34</td>
<td>0</td>
</tr>
</tbody>
</table>
Features of the ELS policy

• Target: Unemployed, educated youth.

• Permanent Public Sector Employment

• “White Collar” jobs
  – Clerical, teaching, state banks
  – Village level ag extension, poverty programs.

• Higher (or at least comparable) wages with private sector
Rationale

• Reduce chronic unemployment among educated, youth.

• Help alleviate associated social and political problems.
  – Psychological problems, frustration, suicide
  – Unrest, violence, conflict
Evidence

• Unemployed are disproportionately
  – Female (12.5%: Male 6%)
  – Young (27.3% for 20-24 age group)
  – Educated (High School and above 23.3% female, 11.1% male)

• A large proportion of the unemployed
  – Have never had a job (86%)
  – Have been unemployed for more than one year (71%)
Unemployment and Education

![Graph showing unemployment rates for different levels of education and genders over years 1996 to 2002.](image)

**Axes:**
- Y-axis: Percentage
- X-axis: Years (1996 to 2002)

**Legend:**
- High School and Above - Male
- High School and Above - Female
- Overall
Unemployment – by Gender

[Graph showing unemployment rates by gender from 1993 to 2002. The graph indicates a decrease in unemployment for both males and females, with females generally having higher unemployment rates than males.]
My Thesis

• Agree that the chronic unemployment problem is associated with a difficult and prolonged transition from “school to work”

• However, the ELS policy is not a solution but a cause of this problem.
The “hidden” rationale of the ELS policy

• Support the free education system that is politically committed to providing economic mobility.

• Mobility: Higher Education -> Higher Wages and Better Employment Prospects

• Increased mobility comes at the expense of increased unemployment.
The Free Education System

1945 Education Reforms:
Single most important policy document in Sri Lanka’s postcolonial history.

Education is

– a universal right.
– a pre-requisite of a democratic society.
– an agent of upward socio-economic mobility.

“Providing every child an opportunity to fulfill his/he potential without regard to his/her economic and social circumstances”.
The Problem with Delivering the Free Education Promise

• Large quality differentials in the school system.

• Dilemma: How do you provide equal opportunity with unequal schools?

• Reduce quality differentials?

• Government’s ingenious solution:
  – Reduce correlation between family background and educational performance.
    • Affirmative Action
    • Resistance to quality improvement in curricula – appeal to “least common denominator”.

Labor Market Response

• School system is highly competitive and perceived to be “fair”, but fails to produce skills demanded by the liberalized labor market.

• Diploma becomes weak signal of “employable” skills
  – English, IT
  – Higher order cognitive skills
  – Affective abilities (social capital)

• The Skill Mismatch Problem
  – The top of a highly selective educational pyramid don’t have marketable skills. Only 2% reached the college degree, but they are more likely to be unemployed than any other group.

• Ironically, economic mobility has decreased as private sector employer replace the weak “diploma” signal with others.
Weakness of the A/L certificate as a Signal

Distribution of Economic Activity by Family Background - A/L Qualified Employed Youth

Casual Far
Casual Non-Far
Salaried Public
Military
Large Private
Small Private
Business
Farm
Foreign

<=5
6-10
O/L
>=A/L
The government’s response

Support Free Education system by absorbing youth that are

– College graduates
– Unemployed

to the permanent cadre of the public sector.
Consequence: Private Returns to Schooling has remained high and increasing.

Contradicts “Skill Mismatch” prediction
Incentive Distortions of the Household

• Education
  – Over-investment in schooling
  – Over-investment in “wasteful” forms of learning.
    • Cramming and rote learning
    • Expenditure on Private tuition, test preps etc.

• Employment
  – Wait for good “public sector” jobs (Queuing)
  – Over-education and unemployment are rewarded.
  – Refusal of private sector employment esp. by females (crowding out).
Why did the government adopt ELR over school quality improvement?

1. Cost-efficient?
   - Can neglect educational investment.
   - Focused only on the top 2-5% to create “illusion” of mobility. Can neglect the “forgotten” youth who fail the competitive exams.

2. Political incentives
   - When an “unemployable” cohort exists, can’t divert resources to educational investments.
   - ELR policies are more visible in the short run, compared to school quality improvements that bring disaggregated results after 15-20 years.

Short time horizons of a populist democracy.
Conclusions: The Problem with the Sri Lankan ELR system

• The goal is socio-economic mobility, not poverty reduction or counter-cyclical insurance.

• Targeted at the highest education levels.

• Employment created in “white-collar” clerical and teaching occupations.

• Permanent (not counter-cyclical or temporary) employment.

• Public sector wages are too high. In fact, they should be lower to compensate for greater job security and social status.

• Ignores the incentive distortions at the household level. Every job handed out to an “unemployable” youth creates another youth that joins the queue with a “unemployable” diploma!
Lessons for Research

• Analyze the micro-impact (incentive distortions) of public employment policies (e.g. household work and schooling decisions).

• Incorporate political economy factors to the analysis (e.g. credibility of temporary programs).

• Analyze policies with their institutional context in mind (e.g. Free Education Reforms, Electoral Democracy).