Chapter 4

PRICES, WAGES AND EMPLOYMENT

4.1 Overview

The overall developments in prices continued to be unfavourable during 2007, despite the tight monetary policy measures to curtail demand pressure, due to both domestic and external factors. As measured by the New Colombo Consumers' Price Index (CCPI(N)), the general price level moved on an upward trend, leading to an annual average increase of 15.8 per cent in 2007 compared with an increase of 10 per cent in 2006. This adverse development was a combined effect of several factors both of domestic and external origin. On the domestic front, the terrorist disturbances in major paddy producing areas in the North and East, bad weather conditions and higher demand for rice due to the substitution effect arising from higher wheat prices had an adverse impact on domestic rice prices. The supply shortages and high distribution cost also raised the prices of domestic agricultural commodities. On the external front, the continued escalation of global oil and gas prices led to upward adjustments in domestic prices of these items at several occasions during the year, exerting direct and indirect impact on the prices of consumer items at varying intensities. Equally, the adverse developments in the international commodity market coupled with both global supply shortages and increased demand, raised the prices of major imported food commodities such as wheat and milk foods, particularly towards the second half of the year. The real wage increases during the year also exerted some pressure on prices. These external developments and supply shocks had an overriding impact on prices, though the demand pressure was notably curtailed by implementing a tight monetary policy programme.

The nominal wages of all three sectors, namely public sector, formal private sector and informal sector increased in 2007. Real wage increases of public sector employees recorded a decelerating trend, while that of formal private sector recorded an increase in 2007, as against the real wage losses in 2006. The

increase in wages of the public sector employees was due to the payment of remaining 50 per cent of the salary revisions of last year and the upward adjustment of the cost of living allowance (COLA). The upward revision in the minimum wage for all workers earning a monthly salary, governed by the Wages Board Trades had a significant impact on the wage rate indices of the formal private sector. However, informal sector employees suffered real wage losses, as their wages did not increase sufficiently to compensate the increase in the price level.

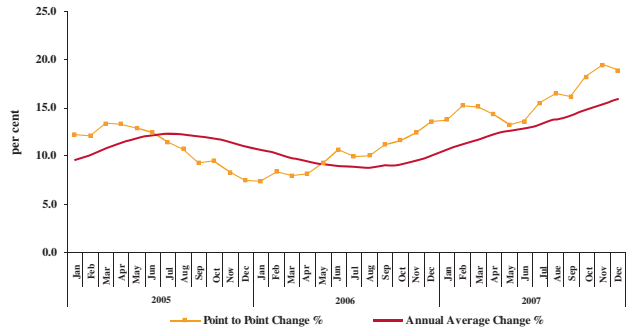
The rate of unemployment continued its declining trend observed over the past few years and dropped to its lowest annual rate of 6 per cent in 2007, while the quarterly unemployment also recorded its lowest ever level of 5.5 per cent during fourth quarter of 2007. Increased employment opportunities were seen in the personal services, construction, transport, storage and communication sectors during the year. However, the set-back in agriculture production, particularly paddy, resulted in a drop in agricultural employment. Meanwhile, the infrastructure development projects created more employment opportunities, especially for youth, contributing to reduce unemployment. Meanwhile, improvement in labour productivity witnessed over the years, especially in the industry and services sectors contributed to achieve high economic growth. At the same time, the improvement in the overseas job market, which accounts for around 18 per cent of the total employed, was significant in reducing unemployment in 2007.

4.2 Prices

Factors Contributing to Price Movements

The general price level increased in 2007 over 2006 consequential upon the build up of price pressure due to combined effects of domestic as well as external demand and supply factors. This was reflected by the annual average change of the

Chart 4.1 New Colombo Consumers' Price Index



CCPI(N), which registered a 15.8 per cent increase. The increase in wages of public sector employees in January, 2007 following the budget proposals presented in November 2006, exerted some pressure on consumer prices through increased demand. However, the tight monetary policy stance adopted by the Central Bank by keeping the reserve money well within the stringent targets in 2007 curtailed the demand pressure during the year.

Supply deficiencies in both the local and international markets resulted in higher prices of food commodities in 2007. This was exacerbated by the disturbances created for distribution of goods due to adverse security developments in the Northern and Eastern provinces and high cost of transportation arising from the escalation of fuel prices. In addition, prices of food imports rose sharply due to the high global agricultural prices, driven by the increased demand generated from high growth in Asian economies and lower supply that resulted from adverse weather conditions. However, the government's programme to stabilize the prices of ten essential food commodities from time to time during the year contributed to lower the pressure on food prices to some extent.

Table 4.1 Changes in Price Indices

Index	Average Index			Point to Point Percentage Change		Annual Average Percentage Change	
	2005	2006	2007 (a)	Dec.2006/ Dec.2005	Dec.2007/ Dec.2006(a)	2006/2005	2007/2006 (a)
CCPI(N)	128.0	140.8	163.1	13.5	18.8	10.0	15.8
WPI	2,105.9	2,351.5	2,924.4	17.3	32.1	11.7	24.4
GDP Deflator	202.1	224.9	256.3	-	-	11.3	14.0

(a) Provisional

Sources : Central Bank of Sri Lanka.
Department of Census and Statistics

Price increases of most domestic agriculture commodities were sharper in 2007 compared to 2006. The price of rice was on an escalation path since May, 2007 in response to the set-back in paddy production which dropped by 6.3 per cent in 2007. In addition, increased demand for rice resulting from the substitution effect of high bread and wheat flour prices, especially during the latter part of the year, too had an impact on sustaining the high price levels. As a result, retail prices of rice rose in a range of 18-35 per cent during 2007. The average price increases of vegetables during the year was also significant on account of low supply from main producing areas, aggravated by bad weather conditions, resulting in earth slips in up country areas and floods in the down south. There was an improvement in the coconut output in 2007 as compared with the last year. However, the increase in import duty on other edible oils during the year had a demand pressure on coconut oil, diverting more output for oil production. This resulted in a decrease in the number of nuts available for domestic consumption leading to higher coconut prices in the domestic market in 2007. Meanwhile, higher export prices helped to increase the wages of workers in the coconut industry in 2007. Consequently, the prices of coconut and coconut oil recorded increases of 21 per cent and 53 per cent, respectively. Similarly, the production of fresh fish recorded a growth of 15.8 per cent in 2007 with the full recovery of the fisheries sector aftermath of the tsunami devastation, but the increased fuel prices had an upward pressure on the prices.

Prices of major import commodities increased substantially, as a result of high international prices. World market prices of wheat grain and milk powder rose during the year as a result of low supply mainly due to the drought and dry weather conditions in Australia. The import price of milk powder, in US dollar terms, rose by around 20 per cent, while that of wheat grain rose by 47 per cent, on average, in 2007. Among other key food commodities, the increases in the import price of dhal (68 per cent) and dried chillies (31 per cent) were also significant. However, in contrast, average import price of sugar declined by 24 per cent in US dollar terms during the year with the increased global supply, especially from India and Brazil. Reflecting this, the domestic consumer prices also registered an annual average price decline of 8 per cent in 2007 over 2006.

The upsurge in crude oil prices was a major driving force in raising the overall cost structure in 2007. The average price of crude oil imported in 2007 rose by around 10 per cent from US dollars 64 per barrel in 2006 to US dollars 71 per barrel compelling the upward revision of domestic fuel prices. Similarly, the high international price of LP gas which rose to a peak of 1.2 US dollars per kg by December, 2007 compared to a price of 0.62 US dollars at the beginning of the year, led to raise the domestic prices at several occasions during the year. As a result, domestic price of LP gas increased by an average of 35 per cent. Import price of fertilizer too increased by 18 per cent during 2007 compared to a 3 per cent increase in 2006. In addition to higher international prices, price increases

Table 4.2 **Retail Prices of Key Imported and Domestically Produced Items**

	Item	Unit	CCPI (N) Weight %	Price - Rs.						Percentage Change			
				Annual Average			Dec.	Dec.	Dec.	Annual Average		Point to Point	
				2005	2006	2007 (a)	2005	2006	2007 (a)	2006/ 2005	2007/ 2006 (a)	Dec. 2006/ Dec. 2005	Dec. 2007/ Dec. 2006 (a)
Domestic	Rice - Samba	kg	2.8	41.80	41.15	50.98	44.46	45.40	63.71	-1.6	23.9	2.1	40.3
	Rice - Kekulu (Red)	kg	0.9	32.85	31.19	44.56	32.10	38.27	55.32	-5.1	42.9	19.2	44.6
	Rice - Kekulu (White)	kg	0.6	28.51	27.37	38.78	29.42	32.01	51.68	-4.0	41.7	8.8	61.4
	Rice - Nadu	kg	0.5	31.80	31.48	44.45	33.65	38.01	56.99	-1.0	41.2	13.0	49.9
	Coconut (medium)	Nut	5.4	16.65	15.65	21.83	16.39	18.62	27.83	-6.0	39.5	13.6	49.5
	Fish - Kelawalla	kg	1.1	264.75	308.14	407.10	275.60	333.81	414.72	16.4	32.1	21.1	24.2
	Beans	kg	0.5	69.36	75.99	83.51	73.64	102.10	82.93	9.6	9.9	38.6	-18.8
	Brinjal	kg	0.2	42.10	47.67	52.12	45.76	71.31	55.99	13.2	9.3	55.8	-21.5
	Eggs	One	0.4	7.26	7.06	9.31	6.71	9.09	11.64	-2.8	31.9	35.5	28.1
Imports	Sugar	kg	1.1	41.93	60.20	54.30	43.66	65.35	53.21	43.6	-9.8	49.7	-18.6
	Milk Powder - Anchor	400g	3.8	156.26	160.55	189.32	158.98	165.83	268.82	2.7	17.9	4.3	62.1
	Red Dhal	kg	0.8	76.51	75.49	103.80	75.87	81.94	117.64	-1.3	37.5	8.0	43.6
	Wheat Flour	kg	0.2	28.99	34.22	55.36	29.13	40.47	66.12	18.0	61.8	38.9	63.4

(a) Provisional

Source : Central Bank of Sri Lanka

of imported goods were affected by the increased freight charges in response to high fuel prices.

The Sri Lanka Rupee depreciated by 6.0 per cent on average against the US dollar in 2007 over 2006, but on year-on-year basis depreciation was less than 1.0 per cent, due to the sharp appreciation of the currency during the latter part of the year. The impact of currency depreciation was reflected by the higher increase in import prices in terms of Sri Lankan rupee than that, in US dollar terms. However, the impact of increased import prices of key essential food items on consumers was mitigated to some extent by removing or lowering customs duty.

Several administrative price revisions took place during 2007. This had both direct and indirect impact on rising price levels of domestically produced as well as imported goods. The adjustments to fuel prices resulted in petrol, diesel and kerosene prices rising by 20 per cent, 18 per cent and 43 per cent, respectively during the year. Consequent upon these revisions, transport charges were increased, including a 16.5 per cent increase in bus fares. The electricity charges of both domestic and industrial users were also revised upward during the year. Although these price revisions had a cascading effect through increased transport expenditure and input costs, in the long run, the removal of subsidies is beneficial to contain inflation through reduced pressure on budget deficit.

Consumer prices showed volatility due to seasonal factors and natural disasters. Agricultural prices showed more volatility than industrial prices responding to the two main agricultural seasons of Yala and Maha along with the natural vagaries viz., floods, droughts and pests. In addition, prices creeped up due to the increased demand generated from the two main festive seasons in April and December.

Movement of Price Indices

New Colombo Consumers' Price Index - CCPI(N)

The consumer price behaviour during the year 2007 was analysed on the newly introduced CCPI(N). The CCPI(N) was introduced to measure general movements of consumer prices. The index constructed by the DCS on the basis of the consumption patterns revealed in the Household Income and Expenditure Survey of 2002 was accepted as the official measure of inflation in Sri Lanka in November 2007, replacing the outdated Colombo Consumers' Price Index (CCPI)[1]. Further, in order to have a single standard measure of inflation in the

[1] For more details please refer Box 10 in page 77.

Table 4.3 Administered Price Revisions in 2006 and 2007

Item	Unit	Price (Dec.) - Rs.			Percentage Change	
		2005	2006	2007	2006/2005	2007/2006
Cigarettes (Gold-leaf)	Each	10.50	11.00	14.00	4.8	27.3
Cigarettes (Bristol/ Viceroy)	Each	9.00	9.50	12.00	5.6	26.3
Coconut Arrack	750 ml	365.00	410.00	525.00	12.3	28.0
Extra Special Arrack	750 ml	335.00	360.00	450.00	7.5	25.0
Diesel	1 ltr.	50.00	60.00	75.00	20.0	25.0
Kerosene	1 ltr.	30.00	48.00	68.00	60.0	41.7
Petrol	1 ltr.	80.00	92.00	117.00	15.0	27.2
Furnace Oil (1000)	1 ltr.	24.70	44.40	52.70	79.8	18.7
Furnace Oil (1500)	1 ltr.	30.30	43.30	51.70	42.9	19.4
Furnace Oil (3500)	1 ltr.	28.00	41.00	46.65	46.4	13.8
Electricity - Fixed charges Tariff Block						
first 30 units		30.00	60.00	60.00	100.0	0.0
31-60 units		30.00	90.00	90.00	200.0	0.0
61-90 units		30.00	120.00	120.00	300.0	0.0
91-180 units		30.00	180.00	180.00	500.0	0.0
Above 180 units		30.00	240.00	240.00	700.0	0.0
Electricity - Unit charges Tariff Block						
first 30 units		3.00	3.00	3.00	0.0	0.0
31-60 units		3.70	4.70	4.70	27.0	0.0
61-90 units		4.10	5.10	7.50	24.4	47.1
91-180 units		10.60	12.10	14.00	14.2	15.7
Above 180 units		15.80	17.30	19.80	9.5	14.5
Bus Fare		-	-	-	16.0	16.5

Source: Central Bank of Sri Lanka

Box 10

New Colombo Consumers' Price Index

A reliable, accurate and timely available measure of inflation is needed to assess inflationary pressure in a country and for policy formulation to achieve price stability, the key objective of monetary policy. In many countries, a consumer price index (CPI) is used for this purpose. A CPI measures the cost of a basket of goods and services consumed by a representative group of consumers and thereby indicates the average level of prices of items in the basket. In Sri Lanka, the widely used index for this purpose for more than 5 decades was the Colombo Consumers' Price Index (CCPI), computed by the Department of Census and Statistics (DCS).

CCPI had been used as the official CPI of Sri Lanka, since 1953. Though it served as a representative price index at the time it was introduced with many structural changes that had occurred since then, its applicability has been of little relevance today. It suffers from many inherent weaknesses, mainly stemming from its more than five and a half decade old base. The soundness of a CPI depends on the extent to which it had captured the current consumption behaviour of an average household in the reference population. The items to be chosen for computing a CPI as well as the relative weights assigned to them need be based on findings of a contemporaneous survey on consumption patterns of the targeted group. The relative importance of each item consumed by the consumer is represented by the weight assigned to each item in the index, derived normally through periodically conducted household expenditure surveys. CCPI, the oldest index in Sri Lanka, was based on the monthly spending patterns of 455 working class households, that lived in the Colombo Municipal area in 1949/50. Accordingly, CCPI is indisputably outdated.

According to the latest Household Income and Expenditure Survey (HIES) conducted by DCS in 2002, the household consumption patterns have undergone substantial changes during the last 50 years, with the improvement in income levels and also the changes in tastes and consumer preferences over time with the availability of new goods and services. These changes have substantially altered the size, content and composition of the basket of goods and services, the price movement of which is measured by CCPI. CCPI basket does not contain some of the current main expenditure items such as LP gas, water, telephone, private tuition and some popular items like mosquito coils. Food items are notably over-represented in the CCPI basket because in 1949/50 food constituted the major item in consumer budgets. Although some revisions have been made to the index from time to time, those changes have been ad hoc and limited in scope. The index is highly sensitive to price changes of several items, the significance of which has declined substantially as better substitutes have emerged over the years. Unlike in many other countries,

Table B 10.1

Salient Features of CCPI and CCPI(N)

Basic Component	CCPI			CCPI(N)		
Base Period	Outdated	:	1952	More Recent	:	2002
Reference Population	Limited	:	Working Class	Increased	:	All Urban
Geographical Coverage	Narrow	:	Colombo City	Wider	:	Colombo District
Sample Size	Lower	:	455 Households	Higher	:	1300 Households
Price Collection Centres[1]	Few	:	07	More	:	12
No. of Items	Low	:	213	High	:	334
Total Basket Value (Rs.)	202.24			17,996.38		

Source: Department of Census and Statistics

[1] The 7 centres in the CCPI are Pettah, Maradana, Wellawatte, Dematagoda, Grandpass, Borella, and Kirulapone while 12 price collection centres for CCPI(N) are Pettah, Maradana, Wellawatte, Dematagoda, Grandpass, Borella, Kirulapone, Dehiwela, Kotte, Nugegoda, Kolonnawa and Ratmalana.

Table B 10.2
Expenditure Weights of CCPI and CCPI(N)

Group	CCPI[2] Base: 1952=100 (%)	CCPI(N) Base: 2002=100 (%)
1. Food and Non Alcoholic Beverages	68.32	46.71
2. Alcoholic Beverages, Tobacco and Narcotics	7.85	-
3. Clothing and Footwear	5.44	3.08
4. Housing, Water, Electricity, Gas and other Fuels	9.54	18.29
5. Furnishing, Household Equipment and Routine Household Maintenance	-	3.22
6. Health	0.43	4.18
7. Transport	1.76	9.47
8. Communication	0.16	4.42
9. Recreation and Culture	6.50	2.18
10. Education		5.79
11. Miscellaneous Goods and Services		2.65
Total	100.00	100.00

Source: Department of Census and Statistics

reweighting and rebasing were not done to CCPI for many years, which made the index outdated and non-representative of the goods and services consumed by the people.

Hence, the need for a more representative consumer price index had been repeatedly highlighted by many for decades. In view of this long felt need, DCS constructed a more comprehensive CPI called the New Colombo Consumers' Price Index, abbreviated as CCPI(N), in November, 2007 addressing many of the deficiencies of the old index. It is based on the most recent consumer expenditure pattern as reflected by the HIES of 2002 conducted by DCS and it has a wider representation than CCPI in scope and geographical coverage. The salient features of CCPI(N) vis-a-vis CCPI are highlighted in Table B 10.1, while comparable weights in two indices are shown in Table B 10.2. More detailed weights of CCPI(N) are given in Annex B 10.I.

Chart B 10.1 **Weight Distribution of CCPI**

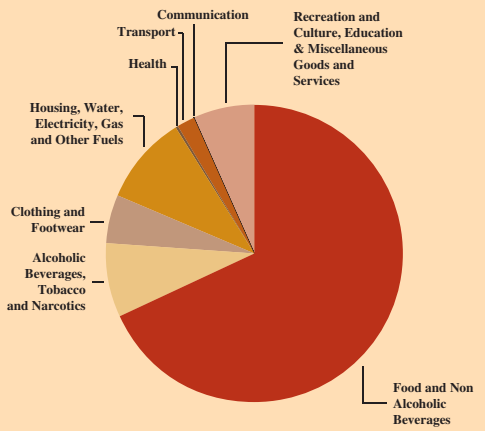
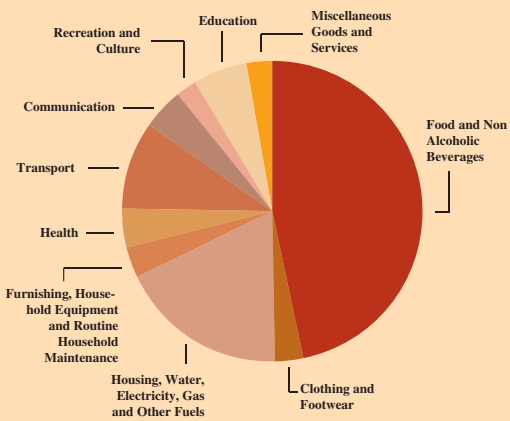


Chart B 10.2 **Weight Distribution of CCPI(N)**



[2] The five sub groups of the CCPI were reclassified according to the Classification of Individual Consumption by Purpose (COICOP) for comparison purposes.

The most notable change in the household consumption has been the sharp decline in the share of expenditure on food from 68 per cent in the CCPI to 47 per cent in the CCPI(N). The CCPI also had relatively higher weights for kerosene, firewood, vegetables and coconut while it did not include petrol, diesel, cooking gas, telephone charges and tuition fees in the basket. The 'Housing, Water, Electricity, Gas and Other Fuels' sub group was inadequately represented in the old index. For example, it did not contain Liquefied Petroleum Gas (LP Gas) at all, and the weight for electricity too was insignificant. The shares of expenditure on utilities and other services such as communication and education were comparatively low as well. CCPI(N) is more representative in terms of consumer habits and covers a wider spectrum of goods and services, and hence, is a more reliable indicator of overall movement in consumer prices. Therefore, CCPI(N) is now being used as the official index for measuring inflation in Sri Lanka. The index would be revised at regular intervals of five years to capture the changing consumption patterns.

The movements of year on year inflation (Point to point change) and the Annual average inflation of CCPI and CCPI(N) for the period 2002-2007 are given in Table B 10.3, Charts B 10.3 and B 10.4 below.

Table B 10.3
Movements of the CCPI and CCPI(N)

Year	Index Number		Rate of Inflation (% Change)			
			Year on Year (Pt. to Pt.)		Annual Average	
	CCPI (1952=100)	CCPI (N) (2002=100)	CCPI	CCPI (N)	CCPI	CCPI (N)
2002	3,176.4	100.0	11.3		9.6	
2003	3,377.0	105.8	5.0		6.3	
2004	3,632.8	115.3	13.8	13.0	7.6	9.0
2005	4,055.5	128.0	8.0	7.4	11.6	11.0
2006	4,610.8	140.8	19.3	13.5	13.7	10.0
2007	5,416.1	163.1	16.4	18.8	17.5	15.8

Source: Department of Census and Statistics

Chart B 10.3 Year on Year (Point to Point) Change of CCPI and CCPI(N)

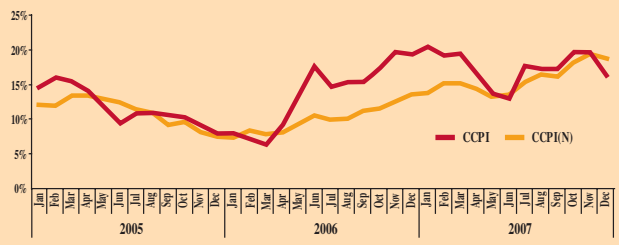
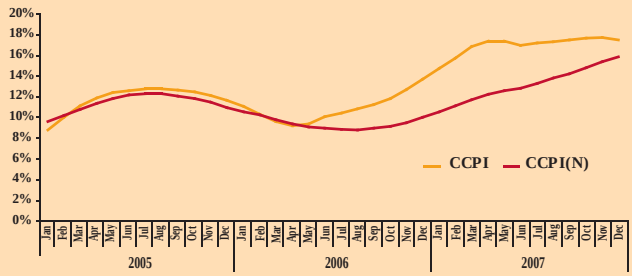


Chart B 10.4 Annual Average Change of CCPI and CCPI(N)



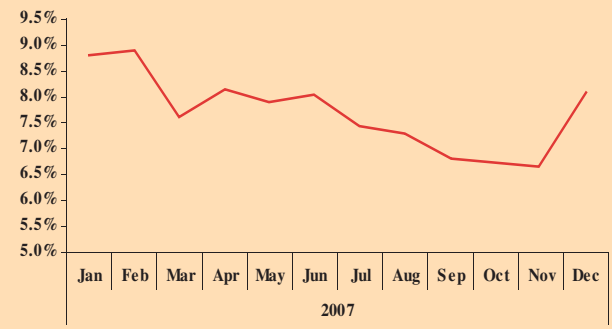
In addition to headline inflation, many countries publish a measure of core inflation and many Central Banks at present monitor core inflation for monetary policy purposes. Table B 10.4 summarises the measures adopted by certain countries, both industrialised as well as emerging economies for compilation of core inflation.

Table B 10.4
Core Inflation Measures Adopted by Selected Countries

Country	Official Core Inflation	Other Core Inflation Measures
Industrialised Countries		
Canada	CPI excluding food, energy and indirect taxes	CPI excluding 8 most volatile items (16% of total basket) Weighted median Trimmed mean (15%)
UK	Retail Price Index excluding mortgage interest rates (RPIX)	Weighted median Trimmed Mean
US	CPI excluding food and energy	
Japan	CPI excluding fresh food	CPI excluding food (without alcoholic beverages) and energy
Emerging Market Countries		
Philippines	CPI excluding food and energy	Trimmed mean (30%) Weighted median CPI excluding volatile items
Pakistan	CPI excluding food and six energy items	Trimmed mean (20%)
China	CPI excluding food and energy	
Thailand	CPI excluding fresh food and energy	Trimmed mean (10%)

Sri Lanka too is planning to adopt a similar core inflation measure based on the CCPI(N) in the near future, in line with the international best practices. Core inflation numbers computed by excluding food and energy items from the CCPI(N) for the year 2007 are given in Chart B 10.5.

Chart B 10.5 **Core Inflation - 2007**



Annex B10.I

Base Weights for CCPI(N)
(Group/Sub Class; Base-2002 = 100)

COICOP Code	Group/Sub Class	Group Total (Rs.)	%
	Total	**17,996.38**	**100.00**
1	**Food and Non Alcoholic Beverages**	**8,405.65**	**46.71**
1.1	**Food**	**8,188.70**	**45.50**
1.1.1	Bread and Cereals	3,086.56	17.15
1.1.2	Meat	534.75	2.97
1.1.3	Fish and Sea Food	1,011.07	5.62
1.1.4	Milk, Cheese and Eggs	1,359.96	7.56
1.1.5	Oils and Fats	273.28	1.52
1.1.6	Fruits	392.98	2.18
1.1.7	Vegetables	579.35	3.22
1.1.8	Sugar, Jam, Honey, Chocolate and Confectionary	302.57	1.68
1.1.9	Food Products n.e.c.	648.17	3.60
1.2	**Non - Alcoholic Beverages**	**216.95**	**1.21**
1.2.1	Coffee, Tea and Cocoa	216.95	1.21
3	**Clothing and Footwear**	**554.86**	**3.08**
3.1	**Clothing**	**469.49**	**2.61**
3.1.1	Clothing materials	32.12	0.18
3.1.2	Garments	424.55	2.36
3.1.4	Cleaning, repair and hire of clothing	12.81	0.07
3.2	**Footwear**	**85.38**	**0.47**
3.2.1	Shoes and other Footwear	85.38	0.47
4	**Housing, Water, Electricity, Gas and other Fuels**	**3,291.30**	**18.29**
4.1	**Actual rentals for housing**	**1,537.24**	**8.54**
4.1.1	Actuals rentals paid by tenants	1,537.24	8.54
4.3	**Maintenance and repair of the dwelling**	**375.55**	**2.09**
4.3.1	Materials for the maintenance and repair of the dwellings	375.55	2.09
4.4	**Water supply and miscellaneous services relating to the dwellings**	**186.16**	**1.03**
4.4.1	Water supply	186.16	1.03
4.5	**Electricity, Gas and other fuels**	**1,192.35**	**6.63**
4.5.1	Electricity	735.51	4.09
4.5.2	Gas	287.28	1.60
4.5.3	Liquid Fuels	134.18	0.75
4.5.4	Solid Fuels	35.38	0.20
5	**Furnishing, household equipment and routine household maintenance**	**580.16**	**3.22**
5.1	**Furniture and furnishings, carpets and other floor coverings**	**156.78**	**0.87**
5.1.1	Furniture and furnishings	156.78	0.87
5.2	**Household Textiles**	**16.03**	**0.09**
5.2.0	Household Textiles	16.03	0.09
5.3	**Household appliances**	**71.06**	**0.39**
5.3.1	Major household appliances, whether electric or not	71.06	0.39
5.4	**Glassware, tableware and household utensils**	**82.03**	**0.46**

COICOP Code	Group/Sub Class	Group Total (Rs.)	%
5.4.0	Glassware, tableware and household utensils	82.03	0.46
5.5	**Tools and equipment for house and garden**	**20.52**	**0.11**
5.5.2	Small tools and miscellaneous accessories	20.52	0.11
5.6	**Goods and services for routine household maintenance**	**233.74**	**1.30**
5.6.1	Non - durable household goods	225.09	1.25
5.6.2	Domestic services and household services	8.65	0.05
6	**Health**	**752.01**	**4.18**
6.1	**Medical products, appliances and equipment**	**250.48**	**1.39**
6.1.1	Pharmaceutical products	210.93	1.17
6.1.3	Therapeutic appliances and equipment	39.55	0.22
6.2	**Outpatient services**	**501.53**	**2.79**
6.2.1	Medical services	412.81	2.29
6.2.3	Paramedical services	88.72	0.49
7	**Transport**	**1,703.83**	**9.47**
7.1	**Purchase of vehicles**	**178.55**	**0.99**
7.1.2	Motor cycles	178.55	0.99
7.2	**Operation of personal transport equipment**	**922.35**	**5.13**
7.2.1	Spare parts and accessories for personal transport equipment	87.97	0.49
7.2.2	Fuels and lubricants for personal transport equipment	466.44	2.59
7.2.3	Maintenance and repair of personal transport equipment	206.88	1.15
7.2.4	Other services in respect of personal transport equipment	161.06	0.89
7.3	**Transport services**	**602.93**	**3.35**
7.3.1	Passenger transport by railway	299.84	1.67
7.3.2	Passenger transport by road	130.83	0.73
7.3.6	Other purchased transport services	172.26	0.96
8	**Communication**	**796.06**	**4.42**
8.1	**Postal services**	**32.74**	**0.18**
8.1.0	Postal services	32.74	0.18
8.2	**Telephone and telefax equipment**	**60.14**	**0.33**
8.2.0	Telephone and telefax equipment	60.14	0.33
8.3	**Telephone and telefax services**	**703.18**	**3.91**
8.3.0	Telephone and telefax services	703.18	3.91
9	**Recreation and culture**	**393.21**	**2.18**
9.1	**Audio - Visual, photographic and information processing unit**	**93.05**	**0.52**
9.1.1	Equipment for the reception, recording and reproduction of sound and pictures	56.28	0.31
9.1.3	Information processing equipment	29.16	0.16
9.1.5	Repair of audio - visual, photographic and information processing equipment	7.61	0.04
9.3	**Other recreational items and equipment, gardens and pets**	**16.51**	**0.09**
9.3.1	Games, toys and hobbies	16.51	0.09
9.4	**Recreational and cultural services**	**65.33**	**0.36**
9.4.1	Recreational and sporting services	14.98	0.08
9.4.2	Cultural services	15.16	0.08
9.4.3	Games of chance	35.19	0.20
9.5	**Newspapers, books and stationery**	**79.13**	**0.44**
9.5.2	Newspapers and periodicals	79.13	0.44

COICOP Code	Group/Sub Class	Group Total (Rs.)	%
9.6	**Package holidays**	**139.19**	**0.77**
9.6.0	Package holidays	139.19	0.77
10	**Education**	**1,041.67**	**5.79**
10.2	**Secondary education**	**812.34**	**4.51**
10.2.0	Secondary education	812.34	4.51
10.3	**Post - secondary non - tertiary education**	**131.71**	**0.73**
10.3.0	Post - secondary non - tertiary education	131.71	0.73
10.5	**Education not definable by level**	**97.62**	**0.54**
10.5.0	Education not definable by level	97.62	0.54
12	**Miscellaneous goods and services**	**477.64**	**2.65**
12.1	**Personal care**	**323.92**	**1.80**
12.1.1	Hairdressing salons and personal grooming establishments	82.98	0.46
12.1.3	Other appliances, articles and products for personal care	240.94	1.34
12.3	**Personal effects n.e.c**	**50.71**	**0.28**
12.3.1	Jewellery, Clocks and watches	39.27	0.22
12.3.2	Other personal effects	11.44	0.06
12.5	**Insurance**	**82.71**	**0.46**
12.5.3	Insurance connected with health	82.71	0.46
12.6	**Financial services**	**20.31**	**0.11**
12.6.2	Other financial services n.e.c.	20.31	0.11

Source: Department of Census and Statistics

country, a policy decision was taken to discontinue with the compilation of the five regional indices compiled by the CBSL and the Sri Lanka Consumers' Price Index (SLCPI) compiled by the Department of Census and Statistics (DCS) during the year.

There were signs of deceleration in the inflationary pressure which was on an upward movement since mid 2006, as indicated by the point to point change in CCPI(N), during early 2007. However, the trend reversed and inflation accelerated mainly during the second half of 2007. The rising inflation, as indicated by point to point increases, declined from 15.2 per cent in February, 2007 to 13.2 per cent by May, 2007. However, it increased gradually since then and accelerated over the fourth quarter, registering 18.8 per cent in December, 2007 compared to 13.5 per cent in December 2006, culminating in an annual average increase of 15.8 per cent for the year 2007, as against a 10.0 per cent increase in 2006.

Price increases of both imported and domestically produced goods contributed to the overall inflation. The overriding influence on inflation was dominated by domestically produced goods, which account for around 74 per cent of total consumption expenditure. However, the contribution from the imported items to the overall inflation increased during the year rising from 28.7 per cent in January, 2007 to 39.7 per cent by December, 2007 influenced by high import prices of both food and non-food items.

When different sub indices of the index are considered, the major contribution to the overall index came from food sub index, which has the highest weight in the CCPI(N). The food sub index recorded a 25 per cent increase on a point to point basis in December, 2007 recording an annual average increase of 20 per cent by the year end. This sub index was responsible for more than 60 per cent of the overall point to point increase. The price increases of rice, bread, meals bought from outside, milk powder, coconut

and coconut oil in 2007 were the key food items which impacted heavily on the index. The price increase of LP gas by 14 per cent in 2007 over 2006 had a substantial indirect impact on the prices of meals purchased outside.

The other sub indices with significant contributions were Housing, water, electricity, gas and other fuels, and Transport, which contributed around 20 per cent and 8 per cent, respectively to the overall increase in 2007. The contributions from these two sub groups were significant compared to other sub groups owing to their high weights of around 18.3 per cent and 9.5 per cent, respectively in the CCPI(N) basket. Except for the Communication sub index, which registered a decline in the cost, all other sub indices recorded increases (ranging from 2.1 per cent to 20.3 per cent) during 2007. However, their individual contributions to the overall increase in the index were less than 2 per cent as weights attached to them were relatively low.

Wholesale Price Index (WPI)

Prices at the primary market level rose at a higher intensity than the retail prices, as reflected by the WPI. WPI measures overall movements of prices, at producer level, of a wide range of goods covering consumer, intermediate and investment as well as those imported and those produced for export and for local uses. However, it suffers from a somewhat outdated weight structure which is based on the composition of goods produced and imported in 1974. The WPI commenced with an accelerating path continuing from the previous year, but showed signs of deceleration towards the beginning of the second quarter. This was due to the arrival of the domestic agriculture production into the market. However, with the price developments thereafter, WPI increased steadily to record a point to point increase of 26.8 per cent by December, 2007 compared to 17.3 per cent in 2006. Consequently, the annual average increase was 24.4 per cent for the year as against 11.7 per cent in the last year.

The main contributor to the rise in the index was the food category, which has a weight of around 68 per cent. On average, the food sub index contributed for around 72 per cent of the overall increase during the year. This was mainly due to the sharp increase in food prices, both domestic and imported, particularly during the second half of the year. When total increase in the food sub index is considered, exports based food commodities contributed for around 64 per cent, while imported food items added around 16 per cent. The annual average increase of 26.5 per cent in Petroleum sub index, having the second highest weight, was a result of the upward revision in domestic fuel prices several times during the year. The contribution to the overall increase from this sector was around 14 per cent. Similarly, Transport and Electrical items sub groups recorded increases of 21 per cent and 24 per cent, respectively. This was mainly due to the increase in raw materials, local rubber and international metal prices. Alcoholic drinks sub sector also had an average increase of 11.7 per cent due to the increase in excise duty (12.5%) and BTT (3%) on alcoholic drinks during the first quarter and the revision of excise duty (2.1%) in November, 2007.

On the basis of origin of goods, Exports sub sector was largely responsible for the overall increase in the index. The Exports group increased at a steady pace during the year, registering an annual average increase of 36.1 per cent for the year. It contributed 51 per cent to the overall increase in the index. This was largely due to high international prices driven by increased global demand for rubber and tea, mainly arising from global supply shortages coupled with the increased crude oil prices. Imports sub sector increased by around 25 per cent mainly due to the price increase in imported items such as petroleum, wheat grain, imported rice and milk powder. This sector accounted for around 26 per cent of the overall increase. Domestic sector had a relatively lower growth of around 13.9 per cent, influenced mainly by the price increase in local food items such as paddy, coconut, fish and vegetables, transport equipment, machinery such as water pumps and sewing machines, cement and liquor.

Under the end user classification, Consumer goods had the dominant influence of more than 75 per cent on the overall increase for the year. This sub index, with a share of 75 per cent, mainly comprising of food items behaved very similar to the food sub index and grew by 28.3 per cent. The increase in Intermediate group by 20 per cent was as a result of price increases in transport equipment (tyres and automotive batteries), fertilizer, footwear, electrical items (dry battery cells, fans, switches, insulated wires, refrigerators) and minor agricultural export items such as tobacco and cocoa. Meanwhile, Investment goods which has the lowest share among the three groups, had a marginal impact on the index. The slow growth in the prices of building material items such as cement, bricks, asbestos sheets, wall paint, s-lon pipes and tor steel during the year contributed largely to this development. Scarcity of cement during the year was

Table 4.4 Sectoral Deflators and GDP Deflator

Sector	Index			Percentage Change	
	2005	2006	2007 (a)	2006/2005	2007/2006 (a)
Agriculture	198.7	214.8	261.1	8.1	21.6
Industry	214.1	240.8	266.1	12.5	10.5
Services	195.8	217.9	249.1	11.3	14.3
GDP	202.1	224.9	256.3	11.3	14.0

(a) Provisional

Source : Department of Census and Statistics

evident due to a regional scarcity of cement and clinker coupled with the massive growth in the construction industry in ASEAN region. However, due to the government policy of declaring cement as an essential good, the increase in cement price was contained during the year.

GDP Deflator

Overall price change in the economy, as measured by the GDP deflator, rose by 14 per cent in 2007 compared with 11.3 per cent recorded in 2006. Agriculture sector recorded a relatively higher inflation rate of 21.6 per cent during the year, compared to the low growth of last year. The inflation in the services sector continued its increasing trend, which rose further from 11.3 per cent in 2006 to 14.3 per cent in 2007, the main contributors being trade and transport sectors. The lowest rate of inflation of 10.5 per cent during the year was in the industry sector, which decelerated from 12.5 per cent in 2006, mainly driven by the slow growth in the manufacturing sector prices.

4.3 Wages

According to the employment status of labour, there are two types of income earners, namely, wage earners and non-wage earners in the labour market. Developments in wages have a significant bearing on consumer prices. Hence, assessing developments in wages is a vital input for effective policy making. Movements in wages are monitored through Wage Rate Indices.

Wages in Sri Lanka can be analysed under two main categories of employment, namely, public sector and private sector. The public sector consists of government and the semi-government sectors while the private sector comprises of formal and informal sectors. Wage developments in the public sector are monitored through the wage indices computed by the Central Bank, covering non-executive grades and minor employees in the central government, and the government school teachers while those in the formal private sector are based on wage rate indices computed by the Department of Labour for agriculture, industry and commerce, and services sectors. The movements of wages in the informal sector are based on the wage information collected from the Country Wide Data Collection System (CWDCS) of the Central Bank.

Public Sector Wages [2]

The public sector employees enjoyed a significant wage increase in 2007, following the 2006 Budget proposals of the government. This increase was mainly due to the payment of remaining 50 per cent of the new salary scale (which was based on the difference between the new salary scales implemented with effect from January 1, 2006 and the salaries paid in December, 2005 inclusive of all allowances) and the increase in the cost of living allowance (COLA). According to this revision, public

[2] The public sector consists of two sub sectors, namely, the government (central government, local governments and provincial governments) and the semi-government (state corporations, statutory boards and state authorities).

Table 4.5 Wage Rate Indices

(December 1978=100)

Employment Category	Index						Percentage Change					
	Nominal			Real			Nominal			Real		
	2005	2006	2007(a)	2005	2006	2007(a)	2005	2006	2007(a)	2005	2006	2007(a)
1. Government employees												
Central government employees	2,417.5	3,150.8	3,828.4	142.7	164.0	169.5	29.1	30.3	21.5	15.8	14.9	3.4
Non-executives	2,178.4	2,853.8	3,493.4	128.6	148.5	154.7	27.5	31.0	22.4	14.3	15.5	4.1
Minor employees	2,672.4	3,463.0	4,172.7	157.8	180.2	184.8	31.0	29.6	20.5	17.5	14.2	2.5
Government school teachers	1,818.6	2,304.2	2,740.0	107.4	119.9	121.4	27.3	26.7	18.9	14.1	11.7	1.2
2. Workers in wages board trades												
All wages board trades	1,329.7	1,358.2	1,648.8	78.5	70.7	72.7	7.8	2.1	21.4	-3.5	-9.9	2.7
Workers in agriculture	1,527.4	1,567.1	1,821.4	90.2	81.6	80.3	9.3	2.6	16.2	-2.3	-9.5	-1.6
Workers in industry and commerce	1,078.4	1,090.7	1,522.4	63.7	56.8	67.0	3.3	1.1	39.6	-7.6	-10.8	18.0
Workers in services	779.7	779.7	1,057.1	46.0	40.6	46.5	3.8	0.0	35.6	-7.0	-11.8	14.5

(a) Provisional

Sources : Department of Labour
Central Bank of Sri Lanka

sector employees were initially granted a COLA of Rs. 1,000/- per month in January, 2006, subject to a maximum upward revision of Rs.375/- every six months. Accordingly, this has risen up to Rs. 2,125/- by July 01, 2007 from Rs. 1,750/- in January, 2007. This increase had a positive impact on both the nominal and real wage rate indices of all categories of public sector employees, as reflected in the wage rate indices for non-executive employees, minor employees and government school teachers. However, both nominal and real wage increases of public sector employees were lower in 2007 than in 2006.

In addition to above salary revisions, the government further decided to amend the salary scales of government officers other than those of the senior level groups, with effect from June 01, 2007, on the recommendations of the National Salaries and Cadre Commission (Public Administration circular No.06/2006(IV) of August 24, 2006). Consequent to all these revisions, Nominal Wage Rate Index (NWRI) of central government employees for the year 2007 recorded an increase of 21.5 per cent compared with the previous year, which was the combined outcome of the rise in the nominal wage rate indices of non-executive officers (by 22.4 per cent) and minor employees (by 20.5 per cent) in 2007. The NWRI of government school teachers too recorded an increase of 18.9 per cent over the previous year. These increases when adjusted for inflation, led to increases in the real wages within a range of 1-4 per cent for different categories. This gain has been on top of the real wage increases in a range of 12-16 per cent enjoyed by public sector employees in the previous year.

Formal Private Sector Wages [3]

Wages of the formal private sector employees are governed by regulations under the Wages Board Trades, which are tripartite bodies representing employers, workers and the government. As such, the wage increases in the formal private sector were influenced by the wage increases of individual contracts, collective agreements, unilateral decisions by employers and minimum wage decisions of Wages Boards. Movements of their wages are monitored through the minimum wage rate indices that cover only the minimum wage categories of employees governed by these Boards.

[3] The Formal Private Sector is defined as the sector consisting of private sector institutions that contribute to the Employees' Provident Fund (EPF) or maintain their own funds (any such contributory retirement benefit scheme) with the approval of the Commissioner of Labour.

Nominal wages in the three major employment categories of the formal private sector, namely agriculture, industry and commerce, and services, as reflected by the minimum wage rate indices, rose by 16 per cent, 40 per cent and 36 per cent, respectively in 2007 while the overall index for the whole sector recorded a nominal increase of 21 per cent, which was a significant improvement as compared with a marginal increase of 2 per cent in the previous year. As a result, these employees, on average, enjoyed a real wage increase of 2.7 per cent in 2007, in contrast to a real wage loss of 10 per cent suffered in 2006. However, the agriculture sector employees continued to suffer a further marginal loss in real wage by 1.6 per cent during 2007. The employees in the industry and commerce sector and service sector enjoyed real wage increases of 18 per cent and 16 per cent, respectively as against the losses of 11-12 per cent experienced in 2006. In general, situation could be different from what is reflected in these minimum wage rate indices as they do not cover wages earned by executives and professional classes in these sectors.

The rise in the nominal wages in 2007 was mainly due to the raise in the minimum wages for workers (who earn monthly salary and are governed by the Wages Board Trades), up to Rs. 5,000/- with effect from May 01, 2007 and the extending of the Collective Agreement entered into between the Plantation Companies and Trade Unions on December 19, 2006 to cover all employees engaged in Tea and Rubber Growing and Manufacturing Trades governed by the Wages Board Trades. This enabled such employees in Tea and Rubber Growing and Manufacturing Trades too to receive the Rs. 260/- daily remuneration package as those in Plantation Companies, with effect from June 01, 2007. As a result, the Minimum Wage Rate Indices of workers in Wages Board Trades increased in May and June, 2007.

Informal Private Sector Wages

The informal private sector comprises all employees who fall outside the public sector and formal private sector. They are not registered with the Labour Commissioner and therefore, not covered by any formal retirement benefit scheme. Nominal wages in the informal private sector are determined in a more free market environment. The wage information in this sector pertaining to agriculture and building construction, is collected under the Country Wide Data Collection System (CWDCS) of the Central Bank.

Table 4.6 **Informal Private Sector Daily Wages by Sector and Gender (a)**

Sector	Annual Average (Rs.)			Percentage Change			
				Nominal		Real	
	2005	2006	2007 (b)	2006	2007 (b)	2006	2007 (b)
1. **Agriculture Sector**							
Tea							
Male	300	333	378	10.9	13.8	-2.8	-3.7
Female	217	234	261	7.9	11.5	-5.8	-6.0
Rubber							
Male	305	335	384	9.7	14.6	-4.0	-2.9
Female	230	249	279	8.5	12.1	-5.2	-5.4
Coconut (c)							
Male	387	421	490	8.6	16.4	-5.1	-1.1
Paddy							
Male	361	391	453	8.4	15.8	-5.3	-1.7
Female	261	293	331	12.3	13.1	-1.4	-4.4
2. **Construction Sector (c,d)**							
Carpentry							
Master Carpenter - Male	556	633	732	13.9	15.6	-0.2	-1.9
Skilled and Unskilled Helper- Male	368	415	479	12.9	15.2	-0.8	-2.3
Masonry							
Master Mason - Male	553	628	727	13.6	15.8	-0.1	-1.7
Skilled and Unskilled Helper- Male	369	413	474	12.1	14.6	-1.6	-2.9

(a) Wage information were based on monthly wages from 93 centres.

(b) Provisional

(c) Female participation is minimal in the Coconut and Construction sectors.

(d) Revised data

Source : Central Bank of Sri Lanka

The information on the daily wages of these sectors revealed an upward movement at different rates in nominal terms while recording a decline in real terms. Accordingly, nominal daily wages for the coconut sector showed the highest increase of 16.4 per cent, while those for tea, rubber and paddy sectors increased in a range of 11-16 per cent. Within the Agricultural sector, the rates of increase in daily wages of most of the sub categories varied partly due to the diversity among different activities. The increase in daily wages in the coconut sector was mainly driven by the demand for higher wages by workers in line with higher prices for coconut during the year. Rubber sector daily wages increased due to higher production and favourable prices in the domestic and global markets. Despite a drop in tea production, tea workers were also paid higher wages due to favourable prices in the global market.

Daily wages for masonry and carpentry in the construction sector recorded increases of 14-16 per cent consequent to the continued demand for workers for construction activities coupled with the shortages of such workers due to migration for foreign employment. However, when adjusted for inflation, their real wages dropped within a range of 1.5-3.0 per cent during the year. Accordingly, as experienced in the previous year, both the agriculture and construction sector employees suffered losses in their real wages in 2007 as compared with the previous year.

4.4 Population, Labour Force and Employment

Population

The mid year population is estimated at 20.0 million in 2007, an increase of 0.6 per cent compared with 1.1 per cent growth in 2006. All districts contributed to the expansion in population, except Ampara, Batticaloa and Trincomalee, which recorded declines due to displacements resulting from security operations conducted in these districts. High increases in population in Colombo, Kandy and Gampaha districts contributed 56 per cent to the overall growth.

Labour Force

The labour force is composed of the economically active population 10 years of age and over. This is measured by the Quarterly Labour Force Surveys (QLFS) conducted by the DCS since 1990. Since the labour force data collected from Northern and Eastern provinces in 2006 and 2007 were not reliable and sufficient, data for 2005, 2006 and 2007 are presented excluding those provinces for proper comparison purposes.

Table 4.7 **Districtwise Population**

'000 Persons

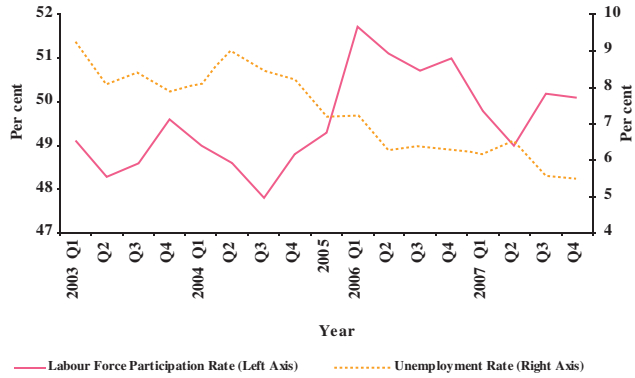
District	2006	2007(a)	Change (a)	Percentage Change (a)
Colombo	2,421	2,456	35	1.4
Kandy	1,361	1,380	19	1.4
Ratnapura	1,073	1,086	13	1.2
Badulla	837	850	13	1.6
Kurunegala	1,511	1,524	13	0.9
Gampaha	2,125	2,140	15	0.7
Galle	1,040	1,052	12	1.2
Anuradhapura	791	801	10	1.3
Kalutara	1,102	1,111	9	0.8
Matara	804	813	9	1.1
Nuwara Eliya	735	742	7	1.0
Ampara	627	615	-12	-1.9
Batticaloa	556	523	-33	-5.9
Puttalam	745	752	7	0.9
Jaffna	595	599	4	0.7
Matale	471	477	6	1.3
Trincomalee	395	355	-40	-10.1
Hambantota	547	552	5	0.9
Moneragala	420	425	5	1.2
Polonnnaruwa	382	395	13	3.4
Mullaitivu	145	147	2	1.4
Kilinochchi	142	146	4	2.8
Vavuniya	164	166	2	1.2
Kegalle	797	802	5	0.6
Mannar	100	101	1	1.0
Total	19,886	20,010	124	0.6

(a) Provisional

Source: Registrar General's Department

The annual average labour force declined by 1 per cent from 7.6 million in 2006 to 7.5 million in 2007. This annual decline was mainly due to the drop in labour force in second quarter of 2007. However, it recovered afterwards and the labour force increased up to 7.6 million by the fourth quarter of 2007. The labour force participation rate (LFPR), which is the ratio of the labour force to the total population aged 10 years and above, decreased to 49.8 per cent in 2007 from 51.2 per cent in 2006. The LFPRs for male and female were 68 per cent and 33 per cent, respectively for 2007.

Chart 4.2 **Trends in Labour Force and Unemployment 2003-2007**



Employment

According to the QLFS, number of employed persons, on average, stood at 7.0 million during 2007 compared to 7.1 million in 2006, showing a marginal decline. This was driven by the drop in employment during the first two quarters of 2007, which however picked up towards the latter part of the year, recording 7.2 million by the fourth quarter of 2007. Persons, who worked as paid employees, employers, own account workers (self employed) or unpaid family workers during the survey period are said to be employed persons in the QLFS. This includes persons with a job but not at work during the survey period. Employees temporarily absent from the work due to illness, bad weather or labour disputes are also considered as employed.

The drop in annual employment was seen in the agriculture and industry sectors. However, this

TABLE 4.8 **Household Population, Labour Force and Labour Force Participation (a)**

Item	2005(b)	2006	2007				
			Q1	Q2	Q3	Q4	Annual
Household Population (c) '000 Persons	14,838	14,834	15,007	15,029	15,006	15,150	15,048
Labour Force '000 Persons	7,312	7,599	7,471	7,362	7,526	7,598	7,489
Employed	6,788	7,105	7,008	6,880	7,102	7,177	7,042
Unemployed	524	493	462	482	423	421	447
Labour Force Participation Rate (d) per cent	49.3	51.2	49.8	49.0	50.2	50.1	49.8
Male	67.3	68.1	68.1	66.5	68.4	68.2	67.8
Female	32.6	35.7	33.2	32.7	33.8	33.7	33.4

(a) Data exclude both Northern and Eastern Provinces.
(b) QLFS was conducted as a one off survey in August 2005.
(c) Age 10 years and above.
(d) Labour force as a Percentage of household population aged 10 years and above.

Source: Department of Census and Statistics

Table 4.9 Employment by Economic Activity (a)

Sector	'000 Persons							Percentage of Total Employment		
	2005(b)	2006	2007					2005	2006	2007
			Q1	Q2	Q3	Q4	Annual			
Agriculture	**2,059**	**2,287**	**2,234**	**2,079**	**2,129**	**2,366**	**2,202**	**30.3**	**32.2**	**31.3**
Industry	**1,787**	**1890**	**1,890**	**1,851**	**1,920**	**1,835**	**1,874**	**26.3**	**26.6**	**26.6**
Manufacturing	1,293	1,363	1,300	1,323	1,333	1,369	1,331	19.0	19.2	18.9
Construction (c)	494	527	589	527	587	466	543	7.3	7.4	7.7
Services	**2,941**	**2,928**	**2,884**	**2,950**	**3,053**	**2,976**	**2,966**	**43.3**	**41.2**	**42.1**
Trade and hotels, etc.	932	1,084	1,002	1,074	1,056	1,070	1,051	13.7	15.3	14.9
Transport, storage and communication	448	430	459	447	471	450	457	6.6	6.1	6.5
Finance, insurance and real estate	226	221	243	206	212	200	215	3.3	3.1	3.1
Personal services and other	1,335	1,192	1,180	1,223	1,314	1,256	1,243	19.7	16.8	17.7
Total employment	**6,788**	**7,105**	**7,008**	**6,880**	**7,102**	**7,177**	**7,042**	**100.0**	**100.0**	**100.0**
Percentage of labour force	92.8	93.5	93.8	93.5	94.4	94.5	94.0			

(a) Data exclude both Northern and Eastern provinces.
(b) QLFS was conducted as a one-off survey in August 2005.
(c) Mining and quarrying, electricity, gas and water categorised under construction.

Source: Department of Census and Statistics

decline was mainly reflected in the first half of the year, recovering thereafter towards the third and fourth quarters of the year. The decreased employment in industrial sector by 0.8 per cent was mainly due to the lower employment in the manufacturing sub sector by 2.3 per cent, despite higher value addition in the sector reflecting significant productivity improvements. Meanwhile, the decline of employment in the Agriculture sector by 3.7 per cent was due to lower output in the paddy production during the second quarter 2007. These declines more than offset the positive impact of increased employment by 1.3 per cent in Services sector.

According to the QLFS, the share of public sector employment increased from 13.4 per cent in 2006 to 13.8 per cent in 2007, mainly due to the expansion in the forces and police service while the share of employment of private sector recorded an increase from 42.1 per cent in 2006 to 42.7 per cent in 2007. The expansion in the public sector employment during the reference period was also reflected in the Annual Public Sector Employment Survey (APSES) conducted by the Central Bank.

Table 4.10 Status of Employment (a)

Per cent

Period	Public Sector Employees	Private Sector Employees	Empl-oyers	Self-Employed	Unpaid Family Workers	Total
2005 (b)	13.2	46.2	2.8	29.7	8.1	100.0
2006	13.4	42.1	3.1	30.8	10.5	100.0
2007 (Annual)	13.8	42.7	2.8	30.4	10.3	100.0
1st Quarter	12.6	44.1	3.0	30.2	10.1	100.0
2nd Quarter	13.5	42.6	3.3	30.3	10.3	100.0
3rd Quarter	15.0	41.5	2.6	30.9	10.0	100.0
4th Quarter	13.8	42.7	2.5	30.2	10.8	100.0

Source: Department of Census and Statistics

(a) Data exclude both Northern and Eastern prvinces.
(b) QLFS was conducted as a one-off survey in August 2005.

Unemployment

According to the DCS, the unemployment rate has dropped to the lowest ever of 5.5 per cent during the fourth quarter, recording a continued decline in the annual rate from 6.5 per cent in 2006 to 6.0 per cent in 2007. This decline was associated with the healthy growth experienced in all three sectors of the economy during 2007. The implementation of several programmes for job creation in both government and private sector, dissemination of labour market information and career guidance programmes continued to lessen the rate of unemployment.

However, the unemployment among young age groups was relatively higher. Youth unemployment,

TABLE 4.11 Public Sector Employment

Sector	2005	2006	2007 (a)	Percentage Change	
				2006/ 2005	2007/ 2006(a)
Government (b)	850,321	887,674	937,494	4.4	5.6
Semi-Government (c)	253,922	258,049	259,116	1.6	0.4
Public Sector	**1,104,243**	**1,145,723**	**1,196,610**	**3.8**	4.4

(a) Provisional
(b) Central Government, Local Government and Provincial Councils
(c) State Corporations, Statutory Boards and State Authorities

Source: Central Bank of Sri Lanka

TABLE 4.12 Unemployment Rate (Unemployed as a Percentage of Labour Force) (a)

Category	2005(b)	2006	2007				
			Q1	Q2	Q3	Q4	Annual
All	7.2	6.5	6.2	6.5	5.6	5.5	6.0
By Gender							
Male	5.3	4.7	4.4	4.6	4.1	4.2	4.3
Female	10.7	9.7	9.5	10.3	8.5	8.0	9.0
By Age Group							
15 - 19	33.2	23.1	18.9	24.6	25.4	17.0	21.6
20 - 29	16.0	15.9	15.2	16.2	14.0	14.8	15.0
30 - 39	3.5	3.3	3.6	3.7	2.7	3.4	3.3
40 and above	2.4	1.4	1.6	1.3	0.9	1.3	1.3
By Education Level							
Grade 4/Year 5 and below	...	...	1.4	1.6	...	....	1.3
Grade 5-9/Year 6-10	6.1	5.8	5.6	5.3	5.2	4.5	5.2
GCE(O/L)/NCGE	10.6	9.9	8.3	9.5	7.1	8.1	8.2
GCE(A/L)/HNCE and above	12.2	11.6	12.3	13.0	10.5	11.3	11.8

(a) Data exclude both Northern and Eastern provinces.
(b) QLFS was conducted as a one-off survey in August 2005.

Source : Department of Census and Statistics

especially among the age groups of 15-19 years has dropped to 21.6 per cent in 2007 from 23.1 per cent in 2006, while the unemployment among the rest of the age groups recorded marginal declines, when compared with 2006. Further, the unemployment rate among those with GCE/OL had declined to 8.2 per cent from 9.9 per cent, while among those with GCE/AL and higher qualifications had risen to 11.8 per cent from 11.6 per cent.

Foreign Employment

Overseas job opportunities for the Sri Lankan labour force continued to be a vital source of employment in 2007, which recovered well from the temporary set-back in 2006. The total departures during the year 2007 at 217,306 compared with 201,948 in 2006, recorded a growth of 7.6 per cent. Accordingly, the total stock of foreign employment stood at 1.6 million as at end 2007 based on the estimates of the Sri Lanka Bureau of Foreign Employment (SLBFE). The total remittances for the year, which amounted to US dollars 2,502 million recorded an increase of around 15 per cent compared to 2006. This was predominantly a result of the increase in skilled and unskilled labour migrants during this period. The Middle Eastern region continued to contribute to more than 90 per cent of total foreign employment opportunities. However, job placements in Malaysia and South Korea recorded decreases, due to non-payment of agreed salaries for workers in Malaysia and the recruitment to South Korea was being done only through SLBFE from this year.

Table 4.13 Foreign Employment

Employment	2005		2006		2007(a)	
	Number	Per cent	Number	Per cent	Number	Per cent
Total Placements	231,290	100.0	201,948	100.0	217,306	100.0
By Source						
Licensed Agents	165,707	71.6	141,177	69.9	146,031	67.2
Other	65,583	28.4	60,771	30.1	71,275	32.8
By Gender						
Male	93,896	40.6	90,170	44.7	102,629	47.2
Female	137,394	59.4	111,778	55.3	114,677	52.8
By Manpower Category						
Housemaid	125,493	54.3	99,659	49.3	102,176	47.0
Other						
Skilled Labour	46,688	20.2	45,063	22.3	49,609	22.8
Unskilled Labour	41,904	18.1	40,705	20.2	52,191	24.0
Other	17,205	7.4	16,521	8.2	13,330	6.2

(a) Provisional

Source: Sri Lanka Bureau of Foreign Employment

Table 4.14 Foreign Employment Departures by Destination

Country	2006		2007 (a)		Change (a)	
	Number	Share	Number	Share	Number	Per cent
Qatar	31,458	15.6	38,728	17.8	7,270	23.1
Saudi Arabia	61,423	30.4	60,218	27.7	-1,205	-2.0
U A E	33,600	16.6	38,315	17.6	4,715	14.0
Kuwait	34,697	17.2	40,883	18.8	6,186	17.8
Other	40,770	20.2	39,162	18.0	-1,608	-3.9
Total	**201,948**	**100.0**	**217,306**	**100.0**	**15,358**	**7.6**

(a) Provisional

Source : Sri Lanka Bureau of Foreign Employment

The male contribution to foreign employment had been persistently increasing over the years. The share of male workers had further risen to 47 per cent in 2007 from that of 44 per cent in 2006. This increase was due to high demand for skilled and unskilled jobs for males in Qatar, Saudi Arabia, UAE and Jordan, particularly in construction and manufacturing sectors. On the other hand, the total departures for Saudi Arabia and Oman, suffered a set-back, mainly due to inadequate remuneration for certain categories of employment, including housemaids. The growth in departures of females, particularly housemaids had been slow over the recent years, mainly due to availability of job opportunities in Sri Lanka.

Unskilled workers continue to account for a significant share of overseas employment dominated by housemaids. However, this dominance has become weaker over the years, with the share of housemaids in foreign employment falling further from 49 per cent in 2006 to 47 per cent in 2007. At the same time, Sri Lanka has begun to explore the opportunities in various other areas of employment in the recent past. An apprenticeship training programme in the construction sector leading to an internationally accepted certification and similar training in hospitality trade were undertaken with a view to cater to these sectors in the global market. Consequently, the migrant workforce in the categories of skilled and unskilled labour, other than the housemaids, increased from 42 per cent in 2006 to 47 per cent in 2007.

Labour Productivity

Overall labour productivity continued to improve in 2007, following the trend experienced during the last few years. In terms of value addition based on GDP at constant (2002) prices, it increased by around 7.7 per cent over the previous year, to Rs.317,000 per employee, based on the employment numbers adjusted for Northern and Eastern provinces. The considerable increase in productivity in the Agricultural, Industrial and Services sectors contributed to the increase in overall productivity in 2007. It is noteworthy to mention that the agriculture sector recorded an increase of 7.3 per cent in productivity compared with a 4.3 per cent drop in 2006. The continuous increase in labour productivity is a favourable development in order to achieve higher economic growth while reducing unemployment. This will also help contain inflationary pressures arising from other factors.

Labour Relations and Labour Market Reforms

The steady decline in the number of strikes since 2004 continued in 2007 and recorded only 25 strikes in 2007 compared to 53 strikes in 2006. The number of strikes in the plantation sector industries decreased to 9 in 2007 compared with 19 in 2006. The total man-days lost and workers involved too dropped significantly. The number of strikes in the rest of the private sector also declined to 16 in 2007 from 34 in 2006. However, the total man-days lost increased by 36 per cent though the number of workers involved declined dramatically by more than 55 per cent in this category. This was mainly due to a stoppage of work at Sevenagala Sugar Company for twenty days and strikes launched by workers in some garment factories.

The private sector continued to emphasise further reforms in the labour market to create a good working environment in order to improve productivity. Necessity for the new labour market reforms did not arise in 2007 because industrial harmony prevailed throughout the year as steps have been taken to strengthen tripartite partners (Employers, Employees and the Government) to participate in the development and implementation of labour reforms made in the recent years.

Table 4.15 Labour Productivity by Major Economic Sector

	2005	2006	2007(a)
GDP at Constant (2002) Prices,Rs.Million	1,941,671	2,090,548	2,232,387
Agriculture	241,851	257,131	265,586
Industry	545,981	590,298	635,199
Services	1,153,839	1,243,119	1,331,602
Labour Productivity,Rs.'000 Per Person	286.0	294.2	317.0
Agriculture	117.5	112.4	120.6
Industry	305.5	312.3	339.0
Services	392.3	424.6	449.0

(a) Provisional

Sources : Department of Census and Statistics
Central Bank of Sri Lanka

Table 4.16

Strikes in Private Sector Industries

Year	Plantation			Other(a)			Total		
	No. of Strikes	Workers Involved	Man Days Lost	No. of Strikes	Workers Involved	Man Days Lost	No. of Strikes	Workers Involved	Man Days Lost
2004	**44**	**15,832**	**40,779**	**46**	**17,514**	**40,321**	**90**	**33,346**	**81,100**
2005	**17**	**4,283**	**8,370**	**40**	**49,282**	**149,982**	**57**	**53,565**	**158,352**
2006	**19**	**196,520**	**4,821,394**	**34**	**13,283**	**72,513**	**53**	**209,803**	**4,893,907**
1st Quarter	8	1,973	4,360	9	3,726	46,368	17	5,699	50,728
2nd Quarter	3	1,463	2,593	7	4,166	10,932	10	5,629	13,525
3rd Quarter	6	1,805	7,645	8	1,719	7,949	14	3,524	15,594
4th Quarter	2	191,279	4,806,796	10	3,672	7,264	12	194,951	4,814,060
2007 (b)	**9**	**1,468**	**6,089**	**16**	**5,948**	**98,417**	**25**	**7,416**	**104,506**
1st Quarter	**1**	**52**	**260**	**5**	**1,485**	**1,945**	**6**	**1,537**	**2,205**
2nd Quarter	**1**	**233**	**233**	**5**	**2,267**	**20,384**	**6**	**2,500**	**20,617**
3rd Quarter	**2**	**323**	**969**	**3**	**1,549**	**73,318**	**5**	**1,872**	**74,287**
4th Quarter	**5**	**860**	**4,627**	**3**	**647**	**2,770**	**8**	**1,507**	**7,397**

(a) Includes semigovernment instituttions and all other private institutions.
(b) Provisional

Source: Department of Labour

4.5 Policies and Issues

Continuation of relatively high rates of unemployment among the educated youth and short supply of IT qualified personnel with proficiency in English and interpersonal skills indicate a mismatch between the supply and demand for skilled labour categories. Therefore, the deficiencies in the education system need to be further rectified. Though the need for educational reforms accompanied by effective national level programmes for skills developments to meet the changing conditions in both domestic and international labour markets have been widely discussed and agreed, the implementation is still lagging behind.

Remittances from expatriate Sri Lankans continued to help improve the balance of payments in Sri Lanka with employment of more skilled workers in Qatar, Saudi Arabia, UAE and Kuwait. Though Sri Lanka still caters mostly to the low demand unskilled labour in the Middle East, the rising demand for professional and skilled labour in those countries is expected to create more employment opportunities for construction workers such as for quantity surveyors, carpenters and masons. Further, increasing opportunities are available in other countries such as Canada and Japan for nurses and care-givers and hence, training of personnel to cater to these markets should be increased. This would reduce the dependency on the Middle East for foreign employment leading to more foreign employment and foreign exchange remittances.

Box 11

The Establishment of Commodity Exchange and Its Benefits

The volatility of prices of agricultural commodities is a problem encountered not only by the farmers but also agro processors and other entrepreneurs involved in agriculture value addition. In particular, farmers who do not have holding capacity often have to dispose of their harvest at depressed prices that prevail during the harvest season. Forward Sales Contracts(FSC) in agricultural commodities were introduced by the Central Bank in 1999, as a solution to a chronic problem of widely fluctuating prices of agricultural commodities between the seasons and off seasons. In an FSC, a producer and buyer agree to purchase or sell, respectively a specified quantity of a commodity on a predetermined future date at a predetermined price. In such a contract, terms like quantity, quality, delivery date, and price are agreed upon between the buyer and seller, making each contract unique.

Even if FSCs are signed however, when the prices agreed upon by the buyers or sellers deviate substantially from the open market price that prevails at the time the transaction takes place, it is inevitable that there would be a reluctance on the part of one of the parties to contract at the agreed price. It has been observed that in such instances in Sri Lanka, the parties to the contract often arrive at a compromise price on which the transaction takes place[1].

In many countries price risk management is achieved by trading in **futures contracts** in a Commodity Exchange. **A commodity futures contract** is a standardized transferable forward contract (i.e., the quantity, quality and delivery date of the underlying asset are standardized). Unlike in the case of forward contracts, delivery is not mandatory in futures contracts and no counter-party risk is involved, as the Exchange which adopts various risk mitigation schemes assumes all risks. Persons with no involvement in the physical commodity market also can participate in trading in a Commodity Exchange with the hope of profiting through their predictive power on price movements in the physical market and resultant price changes. Such participants, called speculators, constitute the drivers of Commodity Exchanges.

Price risk management can be achieved by trading futures contracts in Commodity Exchanges. A hedger facing a risk in the physical market can mitigate such risks by taking a position in the futures market, so that any loss in the physical market would be set off by a gain in the futures market.

Eg: A farmer who sows paddy in December expecting a harvest in March faces a price risk as prices could drop drastically at harvest time. In the circumstances, any forward contract he enters into may not be honoured and he may be forced to agree to a compromise price. If a Commodity Exchange exists, it is possible for the farmer to sell March paddy futures at the price prevailing in the Exchange in December(say Rs. 20,000 per mt) . If paddy prices drop sharply in the physical market, the price in the futures market would also drop as prices in the two markets move in tandem with each other. Therefore, the farmer is in a position to make a profit by squaring his position in the futures market, as he could buy March paddy futures at a low price (say Rs. 17, 000 per mt). Hence, the loss sustained in the physical market will be offset by the profit made in the futures market.

In practice, however, only very large farmers would be in a position to trade directly in a Commodity Exchange. As such, farmer cooperatives and other farm produce associations with sufficient capital can trade directly in the Exchange. Even small farmers would benefit as produce buyers would be able to hedge their price risk and would, therefore, be willing to offer the farmers a better price.

Commodity Exchanges bring a number of benefits. For example, as the ability to hedge prices would make agriculture and agro processing industries less risky, access to credit by these sectors would improve bringing widespread benefits for different sectors in the economy including consumers. Further, as buyers and sellers in a Commodity Exchange undertake trading based on a host of factors such as the prevailing market information, expert opinion, demand and supply conditions, government policies, inflation rates, weather forecasts, market dynamics and hopes and fears, all of these transform into a continuous price discovery mechanism. All new information gets transformed into a single benchmark figure which is the market price agreed upon by the buyer and a seller. As this price is disseminated, markets become more integrated. Thus by watching the futures prices determined in the Exchange the parties involved could gauge the price developments at

[1]It is theoretically possible to take recourse to the law to enforce the contract, but this is not a realistic option, given the time and cost involved in litigation in the country.

practically zero search costs. An informed decision on the crops to be sown can be made by farmers as the futures prices prevailing in the Commodity Exchange are good indicators of the price that is likely to prevail in the future.

Export competitiveness could also be improved by trading in a Commodity Exchange. Exporters often need to contract in advance and, as such, are exposed to risk, if prices of supplies to be exported go up in the physical market at the time of the execution of the contract. If this risk is to be avoided by purchasing supplies in advance, capital would be tied up and a storage cost has to be incurred. These costs will have to be factored into the prices quoted by the exporter. By substituting a futures market transaction(future purchase) for a physical market transaction, price risk could be mitigated and a more competitive price could be quoted to the overseas buyer. (It should be noted that to take a position in the futures market, a hedger needs to put up only a small margin of the value of the contract and, therefore only a small segment capital will be tied up). Further, it has been found that the quality of commodities in the physical market improves over time if trading in contracts of such commodities take place in the Commodity Exchange. This is because trading of contracts of standardized quality of the underlying commodity takes place in a Commodity Exchange creating greater awareness on quality standards among stakeholders. Further, for more efficient price hedging it is necessary for the quality of commodities traded in the physical market to be benchmarked against the standardized quality of commodities in contracts traded at the Commodity Exchange. Such a situation will inevitably raise the demand for commodities with quality corresponding to the standardized quality/qualities in contracts traded in the Commodity Exchange, bringing about an all round improvement in quality of commodities.

The extent of benefits that can accrue from a Commodity Exchange will necessarily depend on the structure of markets, the critical mass of commodities traded in a country's commodity markets and the regulatory regime in existence. India, for example, is a country that produces several commodities as a major producer. Further, its commodity markets were dislocated and were subject to market distorting trade regulations, while the value chain pertaining to agri-products in the country was very long. In these circumstances, widespread benefits were derived from the establishment of Commodity Exchanges, including integration of markets, robust price discovery, compression of the value chain leading to a better margin for the farmer. The volume of commodities traded in Sri Lanka on the other hand, is relatively small and, as notable volumes of several major commodities are imported, price discovery for these commodities takes place abroad. Further, the value chain relating to most commodities tends to be relatively compressed in Sri Lanka.

An important pre-requisite for establishing a Commodity Exchange in Sri Lanka is the setting up of an enabling legal framework with proper regulatory mechanism in place. A regulatory regime is indispensable as the economic consequences of any manipulation or undesirable speculation in the Commodity Exchange will have much graver political and economic consequences than would arise, for instance, if fraud occurred in the stock exchange. The credibility of the Commodity Exchange is crucial, if it is to attract large scale participation and it should be set up by persons and entities of unimpeachable integrity. Therefore, either credible trading associations or institutions such as banks etc., should come forward for this purpose. The Commodity Exchange should be staffed by skilled personnel who, in addition to other skills, should have specific skills and knowledge to facilitate and regulate physical deliveries of commodities. It is also important to have the other marketing infrastructure, such as an organized warehouse structure and grading and assaying facilities in place, before establishing a Commodity Exchange.