

## Total factor productivity dynamics of manufacturing industries in Sri Lanka in the post-trade liberalization period

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Export competitiveness of Sri Lanka's Manufacturing Industries can no longer be dependent on low cost labour particularly in the presence of change in export market environment that include entrance of new competitors, expiration of Multi-Fibre Arrangement (MFA) by 2005, and new Free Trade Agreements. Hence, Sri Lanka's competitive edge of manufacturing exports is to be realised by improvements in productivity in the sector.

Total Factor Productivity (TFP) is the widely discussed measure of productivity, where as the growth accounting methodology or the Solow residual approach is the widely used technique to estimate TFP growth.

This paper uses a recently developed Stochastic Frontier (varying coefficient) Production Function approach to estimate TFP growth, based on a balanced panel data set covering 27 industries over 21 years.

The paper provides new policy insights to productivity debate in Sri Lanka by (i) pointing out the serious limitations of the current interpretation of the TFP measure and (ii) decomposing TFP into Technical Efficiency (TE) and Technological Progress (TP). The paper also finds that manufacturing industries in Sri Lanka have not gained sufficient productivity improvements in the post-trade liberalization period. In general what these industries lack most is TE is rather than TP. Further, the case of Sri Lanka's manufacturing industries does not provide sufficient evidence to negate the 'input driven growth' proposition conjectured by Krugman (1994).

Key words: Total factor productivity; Manufacturing industries; Trade liberalization; Export competitiveness; Export market environment