Box 1.2

Extent of skill mismatch in the local labour market

In Q1 2006, there still existed a visible gap between the unemployment rates for lower-skilled and higher-skilled workers, notwithstanding the significant narrowing over the past couple of years. This is oft-cited as a sign of high structural unemployment in Hong Kong.

However, the issue of structural unemployment may also be analysed by way of a Beveridge curve. The curve depicts the relationship between job vacancies and unemployment, which in turn reflects the underlying process of job matching between employers and job seekers. Generally speaking, movements along a given, convex Beveridge curve are associated with cyclical shocks, while shifts in the curve itself are associated with changes in parameters underlying the efficiency of the job matching process, including changes in demographic structure, regional labour mobility and skill mismatch, advancement in information technology, etc. Specifically, an outward shift in the curve is usually interpreted as a sign of increasing skill mismatch and higher structural/frictional unemployment, and vice versa.

The Beveridge curve for the Hong Kong economy between 1986 and Q1 2006 is shown in the diagram below. Apparently, there has been a fairly stable and negative relationship between the unemployment rate and vacancy rate since 1986, yet with no clear evidence of any major outward shift of the curve itself. Analytically, the Beveridge curve can be separated into two main parts, with the Asian financial crisis serving as the dividing line. At the upper part of the curve are the pre-crisis years, mostly involving a combination of higher vacancy rate and lower unemployment rate. The post-crisis years characterised by higher unemployment rate and lower vacancy rate are however found mostly at the lower part. Yet thanks to the latest economic revival, there has been an ease-back in unemployment rate and a concurrent rise in the vacancy rate since mid-2003, thereby contributing to a ‘V’ turn of the curve.

Beveridge curve for the entire economy, 1986 - 2006 Q1
Box 1.2 (cont’d)

The Beveridge curve can be further analysed by a breakdown of workers into different skill levels. However, owing to the lack of data for the years before 1996, it is not possible to analyse the unemployment-vacancy relationship over a longer time frame, which makes it difficult to delineate the shifts in the Beveridge curve caused by structural factors from those caused by cyclical factors and external shocks. Nevertheless, the fact that there still exists a considerable proportion of unemployment in the construction, retail and restaurants sectors, which is to no small degree cyclical in nature, goes a long way in explaining why the unemployment rate for the lower-skilled workers has been relatively higher.

(*) Excluding the construction sector, owing to the lack of respective vacancy data.

Another way to gauge the extent of skill mismatch is to examine the manpower resource balance\(^{(1)}\) in different occupations and industries. The statistics show that the manpower resource balances in various occupations, though generally improving, have remained negative (i.e. in surplus) in recent years. For professionals and managerial staff, there is a much smaller surplus in labour supply, as a larger proportion of them have already been absorbed into employment. On the other hand, workers at the lower segment face a much looser manpower resource balance. Analysed by industry, except the financing sector comprising mainly banks and investment companies, the manpower resource balance has remained negative virtually across-the-board.

\(^{(1)}\) Manpower resource balance is defined as the difference between total labour demand and supply (expressed as a ratio to labour supply). Total labour demand is measured by the sum of employment and vacancies which represents the overall job opportunities, whereas total labour supply is equivalent to total labour force (employment + unemployment). As such, manpower resource balance essentially refers to the gap between vacancies and unemployment.
Two factors mainly of cyclical nature are thought to have held back the improvement in unemployment in recent period. *First*, despite the strong GDP growth since mid-2003, construction investment has been mostly on the decrease, and this is the sector where a large proportion of unemployment can be found (around 20% of the total). Excluding the construction sector, the unemployment rate (not seasonally adjusted) is reckoned to be only around 4.3% for Q2 2006, 0.7 of a percentage point lower than the overall average of 5.0%. Thus, it can be expected that as and when construction investment turns around, there will be room for unemployment to fall further.

*Secondly*, the weak consumption amidst the property market doldrums of 1997 – 2003 has also been aggravating unemployment. Over the period 1997-2005, private consumption expenditure has grown only mildly by an annual average of 1.4%. This explains why the unemployment rates in the consumption-related sectors, such as the retail trade, restaurants and hotels, are still substantially above the economy-wide average and also higher than their corresponding levels back in the 1990s.
In conclusion, the above studies suggest that structural unemployment does exist in the economy, but the problem may be somewhat less severe than commonly perceived. A not-insignificant proportion of the current unemployment appears to be cyclical rather than structural in nature. The developments over the past few years also suggest that in order to generate a wide spectrum of jobs at the lower-skilled segment, it is imperative for the economy to attain a more balanced growth. Of no less importance is the need to enhance further the quality of the local workforce through education and job training and retraining for better coping with the changing work requirements in a knowledge-based economy.