1. Introduction

Recently, a debate triggered consequent to a lecture by Jagdish Bhagwati on the need for high economic growth to combat poverty and this was documented in a blog managed by CUTS, India. In short, Bhagwati argued that high and rising growth in South Asia has helped poverty alleviation by (i) pulling the poor up into gainful employment; and (ii) providing larger volume of revenues without which social programmes could not be adequately financed.

Bhagwati also pointed out that social welfare programmes are not a novel idea but had always been a part of South Asia’s development agenda. However, they did not go very far principally because low incomes at independence and slow growth subsequently meant there were simply not enough revenues to carry out social programmes on a large enough scale. Bhagwati, argued that targeted social programmes are important because they supplement the favourable effect that the last two decades of reform-led high and rising growth in South Asia has demonstrably had on poverty, nutrition, etc.

In this debate on growth versus social-sector spending, one point that has been insufficiently emphasized is that additional social-sector spending may not lead to better human development outcomes. The empirical evidence (across countries and over time) shows a very weak connection at best.\(^1\) Despite such specific points that have been highlighted in the literature, there generally seems to be consensus among some economists in South Asia on this line of argument articulated by Bhagawati. But there are different views that have been articulated that have highlighted the ‘structural injustice’ of poverty that is not captured in Bhagwati’s line of argument.

South Asia has experimented with a number of poverty reduction strategies as advocated by the World Bank, donor agencies, and regional institutions over the last few decades. Yet poverty reduction has been slow and South Asia has the largest number of people under poverty than any other region in the world. Sobhan (2010) has argued that persistent poverty in the region derives from the unjust nature of social order which effectively exclude the poor from equitable opportunities for participating in the development process. He argues that unless the structural injustices which underlie poverty are removed, poverty will persist in South Asia despite both growth and existing poverty reduction strategies been in place.

\(^1\) There are at least three reasons according to Deverajan (2011). First, social-sector spending is often captured by the non-poor. In India, about 33 per cent of public spending on health accrues to the richest 20 per cent of the population, while less than 10 per cent goes to the poorest quintile. The reason is that the lion's share of this spending goes to hospitals (which are located in urban areas) rather than to primary clinics in rural areas (where the majority of the poor live). Second, even when spending is redirected towards primary clinics and schools, the doctor is absent 40 per cent of the time, and the teacher 25 per cent of the time. Finally, when present, qualified public sector doctors in Delhi have been found to provide worse service than unqualified private doctors. In short, the question is not whether government should emphasize growth or social sector spending, but how overall public spending—and public policy more generally, including regulations—could be made more pro-poor.
The central premises of Sobhan’s work seek to move away from visualization of poverty as a measure of income deprivation. Attempt is made to re-define poverty as a process which excludes significant segments of the population from opportunities to participate on equitable terms in opportunities for development and decision making in society. It is argued that eradicating poverty should thus be measured through the change in opportunity structures for the excluded.

The inequitable distribution of opportunities across society between the rich and the excluded is defined as ‘structural injustice’. The term ‘structural’ indicates that exclusion does not derive from the play of market forces but originates in the structural arrangements of society which determine the working of market forces, as well as the design and functioning of its institutions. The assumption underlying this structural perspective on poverty recognizes that neither targeting of development resources to the excluded, nor the promotion of growth, are likely to resolve the problem of poverty. Sobhan (2010) also shows that it is not enough to recognize the salience of structural issues in the poverty discourse, without addressing the political economy which underlies the structural features of a society.

While the debate goes on poverty in South Asia, the ultimate objective of growth is to achieve ‘development’ in the region. In his pioneering work, Sen (1999) has shown that development as an expression of freedom, encompassing all forms of freedom – economic, political, and social – and embracing all segments of the society, not just a privileged few. For widespread enjoyment of freedom to be possible, the growth process must be inclusive, in other words, the structures of production and employment that the growth process generates must be of a nature that offers opportunities to all segments of the society to benefit from expansion. Widespread expansion of opportunities is the demand for inclusive growth.

The rest of the paper is organized as follows: Section 2 discusses the policy ingredients of inclusive growth. Section 3 discusses the visibility of inclusive growth in Sri Lanka followed by Section 4 on challenges in the post conflict era. Section 5 details out the action that successive governments have taken to achieve inclusive growth. Section 6 attempts to identify the challenges ahead and the final section (7) has some concluding remarks.

2. What are the Policy Ingredients of Inclusive Growth?

Given that inclusive growth focuses on both creating economic opportunities and ensuring equal access to them, an effective inclusive growth strategy should have two anchors: (1) high and sustainable growth to create productive and decent employment opportunities, and (2) social inclusion to ensure equal access to opportunities by all (Ifzal Ali and Juzhong Zhuang, 2007), and (3) as per Sobhan (2010) four main areas of structural injustice, viz., unequal access to assets, unequal participation in the market, unequal access to human development, and unjust governance needs addressing.
2.1 **High and Sustainable Growth**

High and sustainable growth leads to creating productive and decent employment opportunities. Strategies for gaining high and sustaining growth are different from country to country depending on the country’s level of income and poverty. Ifzal Ali and Juzhong Zhuang (2007) highlight that the transformations associated with sustained fast growth often entail a shift of output from agriculture to industry and services. One reason for this is that industry has been where opportunities for productivity growth have been located. One way of ensuring the sustainability of growth is integration with the regional and global economy. This requires continued investment in physical infrastructure, human capital, improving business environment, foreign trade, and foreign investment. The main role of government in this regard is to invest in physical infrastructure and human capital, build institutional capacities, maintain macroeconomic stability, adopt market friendly policies, protect property rights, and maintain the rule of law. Such government intervention leads to sustain the market competition through minimizing market failures and thereby create integration and sustainable economic growth.

2.2 **Social Inclusion**

The second strategy of inclusive growth is social inclusion. The public intervention on social inclusion is required in three broad areas: (1) expansion of human capacities, especially of the disadvantaged through investment on education, health, and other social services, (2) improvement of social and economic justice through promotion of good policy and sound institutions, (3) prevention of extreme deprivation by formation of safety nets. The first two strategies equalize opportunities while the third strategy caters to the special needs of disadvantaged groups.

2.2.1 **Expanding Human Capacities**

Sustainable growth provides resources for development of human resources/capacities while, expanded human resources/capacities increase sustainable economic growth further. The best way of expanding human resources/capacities is to invest in education, health, and other social services such as water and sanitation. Education is the best way of moving out of poverty as it opens up paths for equal economic opportunities for the poor. On the other hand, improved health and nutrition will increase the labour productivity and thereby poors’ earning capacities. Also improved health conditions of the poor will reduce the expenses on medicine and increase their savings. Better access to clean water and sanitation are supports for increasing good health. The government has the main responsibility for the provision of education, health and other social services as there are strong externalities in these sectors. However, in developing countries, governments basically face financial problems in the provision of these services to their citizens. In addition to the financial resources, government should also provide sound physical infrastructure, strong institutional capacities, a sound policy framework and good governance to expand the human capacities of a country and thereby reach inclusive growth of a country.
2.2.2 Effective Policies and Sound Institutions

As discussed in the above section, promoting social inclusion requires good policy and sound institutions. The expansion of human resources/capacities would not ensure equal opportunities for all if some people do not have access to employment opportunities because of their circumstances, face unfair returns on those capacities, unequal protection of their rights and have unequal access to complementary factors of production (World Bank 2006, cited in Ali and Zhuang 2007). In the presence of weak institutions and governance, social injustice is more severe. Like in other strategies, the government has a key role to play in the promotion of policies and institutions. Political, economic, cultural, and social freedoms ensure that members of society would not be excluded from participating, contributing, and benefiting from the new economic opportunities because of their individual circumstances, or because they do not belong to certain power groups who control political and economic decision making (Rajan and Zingales, 2007 cited in Ali and Zhuang, 2007).

2.2.3 Social Safety Nets

The main role of social safety nets is to mitigate the adverse impact of external shocks faced by the poor and to fulfill their basic needs. Risks faced by the poor are mainly related to ill health and other life cycle events, macroeconomic crisis, and natural disasters. Public safety nets are more important in societies where insurance markets are rudimentary and cover only a small segment of the population. The form of social safety nets can be divided mainly into four groups: labour market policies, social insurance programmes, social assistance and welfare schemes, and child protection. Labour market policies reduce the risk of unemployment and underemployment. In addition, such policies can ensure minimum wage in the labour market. Labour market policies attempt to enhance the quality and skills of labour through skills development and training. Sound labour market policies improve the labour skills so that they could match with global standards. Social insurance such as pension schemes mitigate the impact of unforeseen risks such as ill health, disability, unemployment, and old age. Social assistance and welfare programmes provide social services or in-kind or cash transfers for the most vulnerable groups. Child protection ensures the healthy and productive development of children.

2.2.4 Removing Structural Injustice

The general recommendation is empowerment of the excluded by strengthening their capacity to participate on more equitable terms in a market economy and democratic polity. The policy agenda is premised on elevating the excluded from agents into principals through re-positioning them within the process of production, distribution, and governance. The intention is to graduate the excluded from wage earners and tenants to owners of productive assets by investing them with capacity. Sobhan (2010) states that democratizing access to assets and markets should be backed by equitable access to education and health care.
Re-positioning of the excluded should be built upon strengthening their capacity for collective action – this is, strengthening their capacity to participate and share the benefits. Sobhan (2010) proposes policy interventions in the following areas to empower the excluded: (1) expanding the ownership and control of the excluded over productive assets, (2) strengthening the capacity of the excluded to compete in the market place, (3) designing institutions for collective action by the excluded, (4) enhancing access to quality education, (5) re-designing budgetary policy to reach the excluded, and (6) restructuring financial policy to deliver credit and provide savings instruments to the excluded.

3. Is Inclusive Growth Visible in Sri Lanka?

Consequent to rapid increase in per capita income during the last five years, Sri Lanka was categorized as a middle income country by the IMF in January 2010. Poverty headcount ratio in Sri Lanka has been declining sharply as a result of high growth and according to the Department of Census and Statistics; it was around 15.2 per cent in 2006/07. However, this level of poverty based on income of less than US $ 1 a day will become more than double when poverty is estimated based on US $2 a day. Clearly, there are a large number of people just above the poverty line who are vulnerable to external shock or ill health or any other domestic shock.

In Sri Lankan policy, it has been a tradition to put efforts to reduce poverty at the top of the government agenda (Lakshman, 1997). It was one of the first developing countries, by accident or by design, to understand the multidimensional nature of poverty, and to strongly emphasize policies of free health and education as early as the 1930s. In addition to its achievements in social indicators, Sri Lanka managed to completely eradicate starvation and destitution. Despite these achievements, 15.2 per cent of the population remained under poverty in 2006/07, depending on the poverty line used.

Despite reducing poverty from 39.4 per cent of the population in the mid-1980s (as per Lakshman, 1997) to 26.1 per cent by the mid-1990s, the experience during 1990–1995 was not very impressive. Poverty in fact increased between 1991/92 and 1995/96: from 26.1 per cent to 28.8 percent of the population. Some have argued that the year 1995/1996 should be excluded from poverty trend analyses in Sri Lanka because it happened to be a drought year. However, the slow progress in consumption-poverty reduction was striking in the backdrop of relatively faster GDP growth (average 5 per cent) during the first half of the 1990s.

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Per capita GDP growth was on the order of 3.0 per cent per year between 1990 and 1995/96. According to various surveys, many of the poor experienced an increase in poverty. The increase in poverty during 1991/92–1995/96 is puzzling in the light of these facts: (a) economic growth recorded an average 5 per cent; (b) unemployment declined

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2 It may be noted that the North & East are excluded from all available data on poverty.
from 17 per cent in 1990 to 11 per cent in 1996; (c) private remittances doubled; and (d) expenditure on education and health was maintained despite escalation of defense outlays.

What explains the modest decline in poverty? Poverty is highest (32 per cent) in households that derive their income from agriculture: 38 per cent of the Sri Lankan labor force is still engaged in the agriculture sector. Slow growth in agriculture was perhaps the main determinant of increase in poverty during 1991–1996. Agriculture grew by only 1 per cent during 1991-1996. The restructuring of estates in the early stages of privatization, low paddy production, and other factors contributed to poverty in estates and rural areas. Dunham and Edwards (1997) argued that the poverty levels in the mid-1990s would have been higher if not for transfers to the rural economies from worker remittances from overseas, and transfers from ready-made garment factories, and armed forces.

Availability of two data points calls for caution in interpreting the trends. Even so, the increase in poverty during the first five years of the 1990s shows that the poor remain highly vulnerable to income shocks and are unable to take advantage of the opportunities generated by high growth in the early 1990s.

Although urban poverty declined rapidly, rural poverty declined slowly while estate poverty increased in the early 2000s. In the 2000s the poverty reduction has been far more rapid that in the 1990s and 1980s.

Sri Lanka is experiencing rapid economic growth from year 2003 except the global economic crisis induced drawback in 2009. GDP growth in 2009 was a low rate of 3.5 per cent due to two reasons: loss of demand from export markets and a lackluster domestic demand. However, a resurgent economic performance with GDP growth forecast at 7 per cent in 2010 (IPS, 2010). Sri Lanka was able to double the per capita income from US $1241 to US $ 2053 within a five year period from 2005 to 2010, partly enhanced by high inflation.

As can be seen in the Table 1, this rapid growth has led to a dramatic reduction in the level of extreme poverty. According to the US$ 1-a-day poverty line, the incidence of extreme income poverty declined from 26.1 per cent to 15.2 per cent between 1991/92 and 2006/07 (UNDP, 2008/09). If this trend continues the income poverty target of the Millennium Development Goals (MDGs) in Sri Lanka is on track.

<table>
<thead>
<tr>
<th>Year</th>
<th>GDP Per Capita, at market price US$</th>
<th>Average Annual Growth Rate</th>
<th>Headcount Ratio $1-a-day (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1990/91</td>
<td>473</td>
<td>6.2*</td>
<td>26.1</td>
</tr>
<tr>
<td>2006/07</td>
<td>1421</td>
<td>7.7**</td>
<td>15.2</td>
</tr>
</tbody>
</table>

Source: Central Bank Annual Report 2000/2008 and Department of Census and Statistics
* Data for 1990.
** Data for 2007.
A more pressing issue is that this rapid growth has not trickled down to the key areas in the bottom level. As a result, there are two types of inequalities: income inequality between top and bottom income deciles, and regional disparities. According to the Gini coefficient, a commonly used measure of inequality, income inequality has increased between 1990 and 2006 from 0.43 to 0.49. The share of the poorest quintile (20 per cent) in national consumption has declined from 8.9 per cent in 1990 to 7.1 per cent in 2006/07 which further confirms rising inequality trend (UNDP, 2008/09). On the other hand, average per capita consumption during 1990/91-2002 grew by 50 per cent for the richest consumption quintile but by only 2 per cent for the poorest quintile (World Bank, 2007 cited in UNDP, 2008/9). What is more disturbing is the increase in absolute inequalities as measured by differences in mean consumption of the top quintile relative to the bottom quintile. These increases in the absolute gaps between the rich and poor and the very visible changes in the consumption patterns and lifestyles of the rich, are leading to a perceptible increase in social and political tensions, undermining social cohesiveness.

Figure 1: Recent Trend in Gini Coefficient in Sri Lanka

![Recent Trend in Gini Coefficient in Sri Lanka](chart)

Source: Department of Census and Statistics.

The favorable impact of economic growth on consumption-poverty may be reduced if there is a contemporaneous increase in income inequality. Some rise in inequality in the process of rapid economic growth is, however, unavoidable, as the classic Kuznets income-inequality relationship would imply (inverted-U hypothesis). A sharp rise in inequality in the early 1980s is thus understandable in the context of rapid economic growth and structural change (Kelegama, 1993). However, the Sri Lankan experience in the context of 5-per cent average growth during the 1990s shows little decline in inequality. Note that the Gini index of income (expenditure) distribution as a measure of relative income (expenditure) inequality did not vary much. Sri Lanka has not achieved high growth rates like China to compensate for the increase in income inequality. Also as Ravallion (1997)
has argued, initial inequality matters, and this could dampen the impact of economic growth on poverty alleviation.

Inequality has increased significantly in the 1990s and has remained rising thereafter. A decomposition analysis done by Gunatilaka (2011) shows that income flows associated with access to infrastructure, education, and the nature of occupation are the principle determinants of inequality and the main drivers of the change of income distribution. The contribution from income flows to education and infrastructure to the change in inequality appears to have increased over the years. In short, growing inequality is explained mainly by growing disparity in households’ access to education and infrastructure. The same variables were found to be the main drivers behind the rightward shift of the entire income distribution (Gunatileka, 2011). Clearly, the same policy variables that were responsible for widespread economic growth were also responsible for widespread inequality. In other words, the policies led to wider inequality as the middle class and lower middle class benefitted disproportionately more from the state provision of education and infrastructure.

Osmani (2008) shows that three components of income had exerted the most unequalizing influence on household distribution in both rural and urban areas in Bangladesh: self employment in non-farm enterprises, salaried wage employment, and remittances income from Bangladeshi’s abroad. These three components according to Osmani (2008) played a critical role in accelerating the pace of growth and poverty reduction in Bangladesh during the post-1990 period. Thus the experience in Sri Lanka in regard to worsening inequality is not a unique event.

The income disparity is more compounded across the different sectors and provinces. Even though Sri Lanka is on track to achieve many of the MDGs targets and has already achieved some of these targets, there are considerable regional disparities which need to be addressed. For example, according to the Department of Census and Statistics, the poverty headcount ratio has declined in all districts except Nuwara Eliya and Monaragala where the headcount ratio is double that of the national level (See Table 2). On the other hand, poverty indicators show that there is a decline in rural and urban sectors while there is an increase in the estate sector. Therefore, the discussion of inclusive growth in Sri Lanka needs to focus on regional disparities, in addition to inequality between the rich and poor income deciles.
### Table 2: Poverty Headcount Ratio by Sectors and Provinces

<table>
<thead>
<tr>
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<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Sri Lanka</td>
<td>19,886</td>
<td>100</td>
<td>26.1</td>
<td>28.8</td>
<td>22.7</td>
<td>15.2</td>
<td>100</td>
</tr>
<tr>
<td>Urban</td>
<td>24671</td>
<td>14.6</td>
<td>16.3</td>
<td>14</td>
<td>7.9</td>
<td>6.7</td>
<td>6.6</td>
</tr>
<tr>
<td>Rural</td>
<td>135481</td>
<td>80</td>
<td>29.4</td>
<td>30.9</td>
<td>24.7</td>
<td>15.7</td>
<td>82.2</td>
</tr>
<tr>
<td>Estate</td>
<td>9141</td>
<td>5.4</td>
<td>20.5</td>
<td>38.4</td>
<td>30</td>
<td>32</td>
<td>11.3</td>
</tr>
<tr>
<td>Western</td>
<td>5648</td>
<td>28.40</td>
<td>19</td>
<td>17</td>
<td>11</td>
<td>8.2</td>
<td>15.19</td>
</tr>
<tr>
<td>Central</td>
<td>2567</td>
<td>12.91</td>
<td>30</td>
<td>34</td>
<td>24</td>
<td>22.3</td>
<td>18.82</td>
</tr>
<tr>
<td>Southern</td>
<td>2391</td>
<td>12.02</td>
<td>29</td>
<td>32</td>
<td>28</td>
<td>13.8</td>
<td>10.92</td>
</tr>
<tr>
<td>Northern</td>
<td>1146</td>
<td>5.75</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Eastern</td>
<td>1578</td>
<td>7.94</td>
<td></td>
<td></td>
<td></td>
<td>10.82</td>
<td>4.23</td>
</tr>
<tr>
<td>North Western</td>
<td>2256</td>
<td>11.35</td>
<td>26</td>
<td>27</td>
<td>27</td>
<td>14.6</td>
<td>10.93</td>
</tr>
<tr>
<td>North Central</td>
<td>1173</td>
<td>5.90</td>
<td>24</td>
<td>25</td>
<td>21</td>
<td>14.2</td>
<td>5.51</td>
</tr>
<tr>
<td>Uva</td>
<td>1257</td>
<td>6.32</td>
<td>32</td>
<td>47</td>
<td>37</td>
<td>27</td>
<td>11.17</td>
</tr>
<tr>
<td>Sabaragamuwa</td>
<td>1870</td>
<td>9.41</td>
<td>31</td>
<td>42</td>
<td>33</td>
<td>24.2</td>
<td>15</td>
</tr>
</tbody>
</table>

Source: UNDP, 2008/09.

Inadequate infrastructure facilities, inadequate development of the agriculture sector where most of the labour force participants work, weak targeting in welfare programmes, inadequate employment opportunities in less developed regions, low level of employment growth, high level of employment in the informal sector, and differences in real wages, can be identified as possible reasons for this inequality. If the trend of the rising inequalities and non-income inequalities continue and is left without being addressed, there is a major risk to sustainable economic progress in Sri Lanka.

### 4. Challenges in Post-Conflict Sri Lanka

Although successive governments have taken several steps for inclusive growth, the effects of those policies have been concealed by the North/East war in the country. Conflicts affect poverty through entitlement failures, in direct and indirect ways, and war is a barrier for poverty reduction and thus for inclusive growth. According to Draman (2003), entitlement failures can be divided into four main groups: loss of public entitlements, loss of market/livelihood entitlements, loss of civil/social entitlements, and reverse entitlements. Such failures tend to create new forms of social inequalities.

#### 4.1 Loss of Public Entitlement

Loss of public entitlement has direct as well as indirect effects. Breakdown of public order and public infrastructure can be identified as direct outcomes of loss of public entitlement.
while, growing macro-insecurity of states and regimes can be identified as indirect effects of loss of public entitlement. The internal war situation in Sri Lanka more or less destroyed such infrastructure of the North and to some extent in the East (IPS, 2010). For example, the entire road transport network and railway lines in the Northern and Eastern Provinces were severely damaged as well as the main road connecting the Jaffna District to the southern parts of the country.

4.2 Loss of Livelihood Entitlements

The destruction to physical capital, communication infrastructure, and withdrawal of land and labour force from production which leads to loss of markets/livelihood entitlements can be identified as a direct impact of the loss of livelihood entitlements. Closure of the A9 road which connects North and South, and the consequent war affected region disconnected from the rest of the country, created a negative impact on livelihood of the war affected people through loss of markets. According to IPS (2010), the extent of land under agriculture in the North and East has been reduced to 25 per cent by 2002, than the amount in 1982. In addition, destruction of assets, migration, loss of family members especially bread-winners, destruction of financial markets also have had a negative impact on the livelihood of the people in the conflict affected areas.

4.3 Loss of Civil/ Social Entitlements

The direct impact of loss of civil/social entitlement is the destruction of social capital and social networks through the displacement. Indirect impacts of loss of social entitlement are failure of institutions, and competition for resources. For instance, the Samurdhi poverty alleviation programme was not operational in Kilinochchi, Mannar, and Mullativu districts before the liberation of those areas due to the collapse of the administrative structure.

4.4 Reverse Entitlements/ New Forms of Inequality

Population displacement together with assets transfer leads to a new form of social inequality. This will create another series of issues such as insecurity, rent-seeking by those who have power, exploitation of vulnerable groups, and emergence of new groups formerly dependent on the war.

The major challenge for inclusive growth in the post-conflict situation is to address this new form of social inequality which is in addition to the existing inequality in the country. In this context, social protection becomes an essential basic service for the poor. Social protection is highly needed in the conflict affected areas as the loss of livelihood entitlement had made the households more vulnerable. However, it is difficult for the existing social protection programmes to absorb such a large number of people due to the financial constraints. The best way of getting the displaced people out from the hunger trap

3 Census of Agriculture 1982 and 2002, DCS.
is provision of food in exchange for work. The government is planning to expand the Samurdhi income transfer programme which is the main social protection programme / poverty alleviation programme of Sri Lanka into the directly affected areas. The programme has to be implemented with modifications to the existing programmes, along with other social protection schemes. The measurements which the current government has taken to overcome this new form of inequality are discussed in the next section.

5 Policies that Successive Governments have Implemented for Inclusive Growth in Sri Lanka

Successive governments of Sri Lanka have taken many measures for economic growth to become inclusive growth. As described in Section 3, these actions can be categorized mainly into two sub-divisions: (i) sustainable growth, and (ii) social inclusion.

5.1 Sustainable Growth

The most recent development plan in Sri Lanka is the ‘Mahinda Chinthana Idiri Dakam’ – the Ten year (2006-16) horizontal development plan (MCID). It tries to integrate the positive attributes of the market oriented economic policies while safeguarding the domestic aspirations by providing necessary support to domestic enterprises while encouraging foreign investment (IPS, 2008). Priority has been given to the regional development in the MCID. In addition, education, health, livelihood development, social protection, disaster management, and water supply are covered by the social development plan of the MCID. What is clear is that at a general level the current development policies focus on sustainable growth and social inclusion. For achieving these broader objectives, focus is mainly on physical infrastructure development and promotion of a business friendly environment suitable for a market oriented economy.

5.1.1 Physical Infrastructure

The current government under the MCID has taken steps to uplift the investment in physical infrastructure. These infrastructure projects are implemented at both national level as well as regional level. National level infrastructure development projects are operating under the ‘Randora’ Programme while, regional level programmes are operating through ‘Gama Neguma’ (development of villages) and ‘Maga Neguma’ (developments of roads) programmes.4

4 Randora Programme covers the areas of economic infrastructure, irrigation, education and health, industries, urban development, and development of townships. Huge infrastructure programmes such as Upper Kothmale Hydro Power Project, Puttalam Coal Power Plant, Colombo Port Expansion Project, Hambantota Sea Port Development Project, Galle Port Development Project, Oluvil Port Development Project, Southern Expressway, and the Colombo-Katunayaka Expressway are covered by the Randora Programme.
The overall objective of ‘Gama Neguma’ and ‘Maga Neguma’ is to improve small scale infrastructure facilities in all regions and these two programmes are working in the areas of road development, energy, water supply and sanitation, reconstruction of canals, construction of small-scale rural buildings, small-scale infrastructure development, ports and aviation, transport and rural infrastructure at regional level. ‘Gama Neguma’ and ‘Maga Neguma’ programmes are following the participatory development methods for comprehensive rural development. Since its initiation, ‘Maga Neguma’ has involved the rehabilitation of around 1,350 km of rural roads in 2008/09, with most roads being concreted to ensure durability (IPS, 2010).

**Table 3: Government Investment in Infrastructure**

<table>
<thead>
<tr>
<th>Year</th>
<th>Economic Services</th>
<th>Social Services</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Rs. Bn</td>
<td>% of GDP</td>
<td>Rs. Bn</td>
</tr>
<tr>
<td>2006</td>
<td>106.8</td>
<td>3.6</td>
<td>48.4</td>
</tr>
<tr>
<td>2007</td>
<td>141.2</td>
<td>3.9</td>
<td>55</td>
</tr>
<tr>
<td>2008</td>
<td>168.9</td>
<td>3.8</td>
<td>60.2</td>
</tr>
<tr>
<td>2009</td>
<td>256.4</td>
<td>5.8</td>
<td>53.9</td>
</tr>
</tbody>
</table>


Infrastructure development is particularly important in the context of post-conflict development in Sri Lanka to reduce the gap between the Northern and Eastern provinces and the rest of the country. With this broader objective, the government has introduced two separate development programmes for the Eastern Province and Northern Province, namely: ‘Negenahira Navodaya’ and ‘Uthuru Wasanthaya’. In addition to the reduction of the gap between the conflict affected area and the rest of the country, these two programmes aim to compensate the loss of public entitlements and livelihood entitlements of citizens in the conflict affected areas (IPS, 2010, Kelegama, 2010, and others).

**Negenahira Navodaya**

Negenahira Navodaya was implemented in 2007 with the aim of developing the Eastern Province after three decades of conflict. In the short run, its main objectives were de-mining, livelihood recovery, reconstruction of damaged infrastructure, and industrial development. The focus of the economic infrastructure is on electricity supply, roads, transport, ports, water and sanitation, and rural infrastructure. Most of the infrastructure programmes which have been operating in the rest of the country have now been moved to the Eastern Province.
Uthuru Wasanthaya

Uthuru Wasanthaya Programme which was introduced by the government with the purpose of developing the Northern Province at the end of the conflict is being implemented in two stages:

1. a 180 day programme (currently operating)

The focus of the first phase is on de-mining, resettlement of IDPs, reconstruction of damaged economic and social infrastructure, livelihood recovery, and employment generation. The second phase covers the areas of infrastructure development, electricity, water supply and sanitation, health, solid waste disposal, education, sports, cultural affairs, and transportation together with livelihood development programmes. The overall target of this programme is to provide public entitlements which were damaged during the conflict and it is operating in all five districts in the Northern Province.

5.1.2 Business Friendly Environment through Tax Reform

With the aim of creating a favourable environment for the business community and thereby achieving sustainable growth, the Sri Lankan government has proposed to restructure the current tax system as it is complex and narrowly based. One of the main objectives of this restructuring is to promote the export-import sector as it is an effective driving force for growth. One of the specific objectives of this promotion is to increase the exports of value added products. Many Sri Lankan exports are without sufficient value addition. Therefore, a CESS (Commodity Export Subsidy Scheme) is imposed on all exports of raw and semi-processed items while, finished products are free from CESS. In addition, taxes on import of machinery and equipment have been reduced with the objective of improving the accessibility to world class technology. At the same time, income tax for industries with value addition has been reduced from 15 per cent to 10 per cent. In addition to the reduction of tax on value addition, government has reduced tax on all exports from 15 per cent to 12 per cent to promote general exports of the country. With the objective of promoting domestic production, government has reduced income tax on the profits of domestic industries from 35 per cent to 28 per cent. Special focus has been drawn to the apparel sector by the budget 2011. Machinery and equipment to manufacture textile, leather, footwear and bags are exempted from import duties and VAT.

The other objective of the tax re-structure is to promote the tourism sector as it is one of the main income sources. Therefore, the government has imposed a levy of US$ 20 per bed on all five star hotels which charge a room rate that is less than US$ 125 per night from January 2011 in order to compel all hotels to charge better rates. Like in the domestic production sector, income tax of the tourism sector has also been reduced from 15 per cent to 12 per cent. On the other hand, government has reduced taxes on passenger transport as it is important for the promotion of tourism indirectly.
Promotion of other services like finance, ICT and telecommunication is also important for high and sustainable growth of a country. To improve these sectors, the government has taken several steps to re-structure the tax system. VAT on the financial sector has been reduced from 20 per cent to 12 per cent and tax on profits has been reduced from 35 per cent to 28 per cent. The government has made concerted effort to promote the ICT sector through tax reforms in addition to the other steps that have been taken such as establishing IT centres such as: ‘Nanasala’ and ‘Vidatha’.

### 5.2 Social Inclusion

Sri Lanka stands well above its peer countries and very close to developed countries in terms of social indicators such as literacy and infant mortality rate. Moreover, Sri Lanka has achieved many of the MDGs and is on track to achieve the rest. This indicates that past successive governments have laid a good foundation to achieve social inclusion in Sri Lanka and have invested a significant percentage of its GDP on social development. Social policy in Sri Lanka has mainly focused on expansion of human development and safety nets.

#### 5.2.1 Expanding Human Capacity

After its independence from British rule, the Sri Lankan governments have introduced free education and free health facilities to its citizens. These health and education policies are universal policies.

**Education**

According the Education Act of 1945, education in Sri Lanka is free from Grade 1 to degree level and it is universal. The government expanded the school network to fulfill the educational demand and changed the medium of instruction from English to local languages to meet the social demand. In the initial stages, there was a bias in the allocation of resources and as a result, there were regional disparities in the education sector. With the purpose of overcoming these imbalances, increasing the educational opportunities for the poor and increasing the quality of education, successive governments have introduced different policies in different years. Establishment of central colleges in 1940s, the implementation of the common-curriculum in the 1970s, introduction of intervention strategies to compensate for socio-economic differences, introduction of the Grade 5 scholarship programme, district based university enrolment system in 1979, the free school textbook programme initiated in 1980\(^5\), the free midday meal programme, free uniform material programme introduced in 1993, and subsidized transport facilities, are among them (see Box 1)

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\(^5\) Textbooks free-of-charge to all students in Grades 1-11
Box 1: Education Welfare Programmes in Sri Lanka

Free School Text Book Programme
This programme was initiated in 1980 with the aim of improving the quality of education. School textbooks are provided freely to all students in Grades 1-11 in all the state and state-aided schools. Currently, it covers all students from over 10,000 schools in all the districts in the country. Further, over 30 million copies covering more than 300 different subjects/titles in the three basic languages of Sinhalese, Tamil and English are distributed annually under this programme. The government fund together with donor funds are the main sources of funding for this programme.

Free School Uniform Materials Programme
This programme was introduced in 1993. Under this programme all students in all the government schools and temple schools are provided with free uniform material. The type of material and the quantity received by students depends on the gender and the grade in School (Table 19). This programme is entirely funded by the national treasury funds.

School Mid-Day Meal Programme
This programme was introduced in 1989 with the aim of providing one meal to all children enrolled in primary and secondary schools across the country. Initially, a student received a stamp of Rs.3 and was expected to bring a home prepared lunch to school. Due to budgetary constraints, this programme had to shift from its universalism to a targeted programme and was finally absorbed into the Samurdhi poverty alleviation programme in 1995. The target groups are the school children in difficult areas, in marginalized families and identified schools where at least 30 per cent of the students are malnourished.

Public expenditure on education has been increased with the introduction of free education in early 1950s to the end of mid 1960s and reached its peak in early 1970s. As can be seen in Figure 2, the government was able to spend more than 4 per cent of the GDP on education and favorable economic climate in the country after independence supported such allocation. However, the economic downturn together with structural changes in 1977 curtailed expenditure on social services including education. This reduction led to a decline in the quality of education and regional disparities in the educational sector.
**Figure 2 : Education Expenditure as a Percentage of GDP**

![Education Expenditure as a Percentage of GDP](image)

Source: Central Bank *Annual Reports*, various years.

**Challenges in the Post-Conflict Situation**

Due to the post-1983 conflict in the Northern and Eastern provinces, education of the most students of these areas were disrupted due to displacement, loss of family members, psychological impact, loss of school materials, and the destruction of school buildings and infrastructure. In this context, reintegration into the regular curriculum is necessary in addition to the provision of basic education services. The UNICEF estimates that more than 48,000 school going children have returned to their home towns by February 2010 (IPS, 2010). But there are a number of children who still live at camps and consequently there are several issues which need to be considered in providing basic educational services for the conflict affected groups: reintegrating to school curriculum, dealing with ex-child-combatants, providing educational infrastructure, ensuring adequate human resources, and psycho social support. In addition there are issues with the educational infrastructure such as lack of essential materials -- furniture, and teaching and learning aids. In the Northern Province, 392 schools and 10 Divisional and Zonal Education Offices are estimated to be in need of fairly extensive repairs and rehabilitation (IPS, 2010).

The government has taken initial steps to address these issues in the education sector of these areas. According to the Northern Province Department of Education, 115 out of the 326 existing schools are estimated to have been reopened as of end of March 2010 (IPS, 2010). Temporary Learning Centres (TLCs) and Catch up education system are two such main steps. TLCs provide educational services for those who are living in camps. For instance, in Vavuniya and Mannar districts, a total of 21 TLCs are providing continual educational services for IDP students. The Catch up education programme reintegrates students into the regular school curriculum.
Health
The pattern of public expenditure on health is somewhat similar to public expenditure on education. Public health expenditure was relatively high during 1950s and it recorded a peak in 1971 reaching 2.5 per cent of GDP (IPS, 2008). After 1971, it was cut back to 2 per cent of GDP and even more closer to 1 per cent. However, again in 2005, health expenditure has increased as a result of high demand for health services after the Tsunami.

Figure 3: Health Expenditure as a Percentage of GDP in Sri Lanka

![Health Expenditure as a Percentage of GDP in Sri Lanka](image)

Source: Central Bank Annual Report, various years.

However, economic liberalization opened the door for the private sector to invest in the health sector in Sri Lanka and allowed medical officers to practice in the private sector after duty hours. In 2004, public funds accounted for 49 per cent while private financing accounted to 51 per cent of the total health financing (IPS, 2008).

Challenges in Post-Conflict Situation
Sri Lanka has been able to maintain overall health indicators at a satisfactory level despite economic downturns over time. However, like in other MDG indicators explained earlier, there are regional disparities in these health indicators and this is compounded in the conflict affected districts. As can be seen in Table 4, maternal mortality rate is five times higher than those at national level and this incidence is even worse at some district levels. With the liberation from the LTTE, returned refugees may make a greater demand for health services. Therefore, the major challenge for the government is to reduce the gap between conflict affected areas and the rest of the country in health facilities and to meet the increasing demand from the conflict affected areas.
Table 4: Selected Health Indicators for North and East

<table>
<thead>
<tr>
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<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Sri Lanka</td>
<td>11.2*</td>
<td>14*</td>
<td>16.7</td>
<td>29.4</td>
<td>4</td>
<td>72.6</td>
</tr>
<tr>
<td>North and East</td>
<td>14.7</td>
<td>81</td>
<td>25.7</td>
<td>46.2</td>
<td>19.4</td>
<td>48.2</td>
</tr>
<tr>
<td>Ampara</td>
<td>10.3</td>
<td>24</td>
<td>22.7</td>
<td>44.1</td>
<td>19.8</td>
<td>58.2</td>
</tr>
<tr>
<td>Batticaloa</td>
<td>15.8</td>
<td>117</td>
<td>24.3</td>
<td>53.2</td>
<td>31.4</td>
<td>28.4</td>
</tr>
<tr>
<td>Trincomalee</td>
<td>4.6</td>
<td>57</td>
<td>30.5</td>
<td>44.7</td>
<td>13.6</td>
<td>25.6</td>
</tr>
<tr>
<td>Jaffna</td>
<td>22.3</td>
<td>62</td>
<td>30.5</td>
<td>43.1</td>
<td>4.4</td>
<td>79</td>
</tr>
<tr>
<td>Killinochchi</td>
<td>27.8</td>
<td>158</td>
<td>NA</td>
<td>NA</td>
<td>NA</td>
<td>NA</td>
</tr>
<tr>
<td>Mannar</td>
<td>22.3</td>
<td>97</td>
<td>12.7</td>
<td>38.3</td>
<td>39.4</td>
<td>70.9</td>
</tr>
<tr>
<td>Multhivu</td>
<td>20.3</td>
<td>123</td>
<td>NA</td>
<td>NA</td>
<td>NA</td>
<td>NA</td>
</tr>
<tr>
<td>Vavuniya</td>
<td>8.8</td>
<td>76</td>
<td>38.8</td>
<td>50.6</td>
<td>2.3</td>
<td>71</td>
</tr>
</tbody>
</table>

* data for 2002.

The current government of Sri Lanka has taken many steps to overcome these issues in the health sector in the conflict affected areas. For instance, the Ministry of Health has taken several steps in recent months to develop the main hospitals in the Jaffna district (IPS, 2010). Further, the government has allocated Rs. 350 million to uplift health care facilities in the Jaffna district. According to the Ministry of Rehabilitation and Reconstruction, the government has allocated Rs. 460 million under the ‘Uthuru Wasanthaya’ programme to improve health felicities in the Jaffna peninsula (IPS, 2010).

5.2.2 Social Safety Nets

Social safety nets in Sri Lanka can be divided mainly into three segments: (i) social assistance and welfare, and (ii) labour market policies, and (iii) social insurance schemes.

Social Assistance, Welfare and Insurance Schemes

The Samurdhi programme is the largest poverty alleviation programme in Sri Lanka and it provides social assistance, social welfare and social insurance for the poor in Sri Lanka. The Samurdhi programme was introduced in 1995 by an Act of Parliament. According to the Central Bank Annual Report 2008, 1.6 million households of the country are covered by the programme by end 2008. The objectives of the Samurdhi Act of 1995 are: to integrate youth, women and disadvantaged groups into economic and social development activities, to promote social stability, and alleviate poverty. It adopts both short-term strategies reducing vulnerability of the poor and long-term strategies assisting them to eventually move out of poverty. The short-term strategies are based on poverty cushioning methodologies such as income support, social insurance and social development.
programmes. Under long-term strategies it aims to address the core issues of poverty alleviation by using methods such as empowerment, social mobilization, and integrated rural development.

This programme is structured under two main components: (i) relief programme, and (ii) empowerment programme. Relief programme encompasses three sub-components namely, cash transfer programme, social security fund, and nutrition programme. The objective of the cash transfer programme is to provide financial assistance to low income families in order to enhance their standard of living. The benefits of the relief programme are based on the size of the household. The social security fund provides coverage against risks and life cycle events such as death, marriage, child birth, and illness. The nutritional programme is implemented in collaboration with the Ministry of Health and Nutrition. It provides an allowance of LKR 200 per month and it is valid for one year from the childbirth. The main objective of this programme is to enhance the nutritional level of pregnant and lactating mothers of poor families. There are five sub-programmes coming under the empowerment programme: rural infrastructure programmes, livelihood programmes, social development programmes, Samurdhi housing programme and Samurdhi Bank Societies (SBS).

Overall, the percentage of the beneficiary households has declined from 1995 to 2007. There is a sharp decline from 39.1 per cent to 26.7 per cent during 1995-2002. However, it has slightly increased from 2002 to 2007. Figure 4 shows the change in the government expenditure on the Samurdhi relief programme and nutrition programme over the years.

**Figure 4: Government Expenditure on Samurdhi Programme**

![Government Expenditure on Samurdhi Programme](http://dcgs.samurdhi.org/finance.html)

Source: http://dcgs.samurdhi.org/finance.html

As can be seen in Figure 4, overall budget for the Samurdhi programme has increased over time. In 2002, the maximum budget had been allocated for the Samurdhi programme

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6 Source does not specify whether this is the total cost of the Samurdhi programme or whether it is only the cost of the cash transfer component.
and gradually it has declined. Year 2006 again records an increase in the allocation as Samurdhi benefits were increased by 50 per cent for all the beneficiary groups.

In addition to the Samurdhi programme, there are several other welfare programmes introduced by successive governments with the aim of improving the living standards of the citizens of the country. The Public Assistance Programme is one such programme and it targets vulnerable groups such as the poor among the elderly and disabled, families without breadwinners, destitute women and orphans. It provides an average monthly grant of Rs. 135 which is less than the Samurdhi Grant but the amount is not sufficient for cope up with the living cost. The Thriposha nutrition supplement programme is another programme which is implemented with the purpose of enhancing the nutritional level of children less than 5 years, and pregnant and lactating mothers. There were 580,000 such beneficiary families in 2005 (IPS, 2008). Budget 2011 has allocated Rs. 1500 million for the Thriposha programme to reach deserving mothers.

In addition to the social insurance provided by the Samurdhi programme, microinsurance programmes are also playing a significant role in the social security of the poor people. In Sri Lanka, microinsurance programmes are mainly provided by the microfinance institutions and still they are in the initial stage. The Sarvodaya Economic Enterprises Development Sector (SEEDS), Women’s Development Bank, Yasiru Mutual Provident Fund, and Sanasa Insurance Company are some of the institutions which play a significant role in the microinsurance market. In addition to the microfinance institutions, commercial insurance companies such as Ceylineco Insurance Company are also involved in microinsurance field. However, there are many barriers for the development of the microinsurance sector such as lack of reinsurance facilities and lack of human resources, among others.

**Labour Market Policies**

Retirement Schemes are the major labour market policies which provide safety nets for the working population, especially in old age. Sri Lanka is maintaining several such retirement schemes.

*Employees’ Provident Fund (EPF)*

The EPF is the largest retirement scheme in terms of coverage and it was introduced in 1958 by the Employees’ Provident Fund Act, No. 15 of 1958. Formal private sector workers are eligible for this scheme and the employers and the workers have to make joint contributions at the rates of 12 per cent and 8 per cent of earnings, respectively. The worker can withdraw the accumulated amount as a lump sum at the age of retirement. The principal custodian and investment manager of the fund is the Central Bank. By the end of 2001, the EPF had coverage of about 65 per cent of the eligible population, which represents about 1.9 million active accounts out of 2.9 million eligible formal private sector workers (IPS, 2008).
Public Service Pension Scheme (PSPS)
All the public sector workers are eligible for this retirement scheme. This is a mandatory and non-contributory scheme which is financed through government budget. The benefits are calculated based on the final salary and the years of service. For a person to qualify for the pension, a 10 year minimum service is required, which will bring in an entitlement of 40 per cent of the final salary.

Voluntary Schemes (Farmers, Fishermen and Self-Employed Scheme)
As the above mentioned retirement schemes are entirely for formal sector workers, Sri Lanka has introduced pension schemes by Acts of Parliament in 1987, 1990 and 1996 for the workers outside the formal sector. The main two such retirement schemes are the Farmers’ Pension and Social Security Benefit Scheme and the Fishermen’s Pension and Social Security Benefit Scheme. These schemes are administered by the Agricultural and Agrarian Insurance Board (AAIB). The eligibility for the farmers’ pension scheme depends on the type of the crops cultivated, age and non-entitlement to other retirement schemes. Eligibility criteria for the Fishermen’s Pension Scheme are also the same as for the farmer’s pension scheme except the crop type. However, to be a member of the Fishermen’s scheme, a fisherman should be an owner of certain assets. In addition to the income component, benefits of these two retirement schemes have social security benefits such as disability, disablement gratuity, and death gratuity.

In addition to those two main voluntary retirement schemes, Sri Lanka has introduced another pension and social security scheme for the self-employed named Self-Employed Pension Scheme. This is under the purview of the Sri Lanka Social Security Board. Only certain types of workers are eligible for the scheme depending on the age, income, and non-entitlement to other similar pension schemes. This scheme also provides social security benefits in addition to the income benefits.

Old age security of the beneficiary depends on how they are going to invest and utilize the retirement package. The largest retirement scheme operating in the public sector in Sri Lanka provides a lump-sum amount at time of retirement. Retirement benefits have become a concern in the selection of employment of the younger generation and they prefer to select government job rather than go for private sector jobs which are readily available compared to public sector jobs. Taking this into account, the current government has proposed a pension scheme for the workers in the private sector and corporate sector. According to this new proposal, a 2 per cent contribution from employees and a 2 per cent contribution from employers would go into this scheme.

On the other hand, old age social security of migrant workers are not ensured by any of these retirement schemes as they are not eligible for any of these retirement schemes. Considering the old age security of the migrant workers, who substantially contribute to foreign earnings of the country, the current government has proposed to set up an Overseas
Employees’ Pension Fund (OEPF). According to this new scheme, each migrant worker has to contribute at least Rs. 12,000 per annum for a minimum of two years.

Current senior citizens who have not contributed to any of the retirement schemes mentioned earlier are in a unsecured situation and according to the existing structure, they cannot participate in any of the above mentioned retirement schemes. Therefore the current government has proposed to set up a Citizens’ Pension and Insurance Fund (CPIF). Senior citizens have to contribute a minimum of Rs. 5,000 per year as and when they have money.

6 Challenges
As explained, successive governments have taken many steps to achieve inclusive growth in Sri Lanka; however there are high inequalities between income deciles as well as between regions and districts. This section highlights the shortcomings of some of the existing programmes to reduce inequality and achieve inclusive growth.

Inadequate Development of the Agricultures Sector
More than 30 per cent of total employment is in the agriculture sector and the majority of people in Sri Lanka directly or indirectly depend on the sector for their livelihoods. However, productivity of this sector is very low while the cost of production is very high. As a result, income of the people who are in the sector is also low and this is more severe as the size of the land holding is small. In addition to the small size of the average land holding, the less developed irrigation system and poor technology also negatively affects productivity of the agriculture sector. Like in the other production sectors in Sri Lanka, poor institutional, market conditions and less developed infrastructure are also reasons for the poor performance of the sector. Poor performance leads to low income and this low income of one sector compared to the other sectors leads to inequality in Sri Lanka.

Weak Targeting in Welfare Programmes
Samurdhi Programme
While the restructuring of the taxation system addresses the revenue concerns there is an urgent need to take actions to curtail expenditures. Time and again the need to curtail expenditures have been highlighted by the local economic institutions and the international lending agencies. In recent years, the Sri Lankan government has been spending around 4 per cent of GDP on transfer and subsidy programmes – key components of its poverty reduction strategy (Jayaweera, 2010). Some of these programmes involve direct cash and/or in-kind transfers to the poor. The Samurdhi programme is considered to be a major transfer programme dealing with poverty reduction and equity objectives, accounting for 0.2 per cent of GDP.
Table 5: Expenditure on Transfer Payments to Households (2009)

<table>
<thead>
<tr>
<th>Expenditure (Rs. Mil)</th>
<th>% of total expenditure</th>
<th>% of GDP</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pensions</td>
<td>85139</td>
<td>10</td>
</tr>
<tr>
<td>Fertilizer subsidy</td>
<td>26935</td>
<td>3</td>
</tr>
<tr>
<td>Other</td>
<td>27652</td>
<td>3</td>
</tr>
<tr>
<td>Samurdhi</td>
<td>9267</td>
<td>1</td>
</tr>
</tbody>
</table>


However, the Samurdhi programme is criticized due to the targeting errors incurred in it and as a result, it leads to greater inequality as the benefits shared are disproportionate to the income level of families. According to Jayaweera (2010), simply reducing the number of Samurdhi beneficiaries is not a solution to the targeting errors inherent in the Samurdhi programme. She further explains that from 1996 to 2006/7, there was a greater decline, around 9 per cent, in the number of Samurdhi beneficiaries, however, this decline is same in both richest and poorest deciles. But the number of Samurdhi beneficiaries is greater than the number of poor households in each district. Aryaratna and Ravisingha (2009) identified the bias at grassroots level officers, Samurdhi Development Officers (SDOs) as the major reasons for targeting errors in Samurdhi programmes. Ranathunga (2006) states that beneficiary selection was not successful due to political and other personal interventions though the selection criteria itself was sound (Jayaweera, 2010).

With the purpose of reducing the targeting error in the Samurdhi programme, the government has introduced a new participatory methodology named Family Classification Methodology (FCM) to the beneficiary selection procedure. Under this new methodology, villagers are free to rank themselves as destitute, chronically poor, poor, medium income, and non-poor, based on the selection criteria. As most of the villagers are familiar with the assets ownership of their neighbours, the beneficiary selection procedure is transparent and the problem of asymmetric information will be minimized. The Samurdhi Disaster Management Household Survey showed that the FCM has excellent potential to reach the neediest households and a systematic implementation of the FCM can provide large dividends by significantly improving the targeting performance and thus cost effectiveness of Samurdhi transfers (Jayaweera, 2010).

**Fertilizer Subsidy**

In 2009, the fertilizer subsidy accounted for 3 per cent of total government expenditure and 0.6 per cent of GDP (Thibbotuwawa, 2010). Since this is a blanket programme, it incurs targeting errors and due to its universalism, it is evident that there are over-applications of fertilizer. Most often small-scale farmers are inefficient compared to the large-scale

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farmers and as a result, it is necessary to correct the targeting errors in the fertilizer programme. Use of vouchers that can be redeemed at local retail stores, involvement of a wide range of fertilizer importers in the input voucher scheme, correct identification of poor farmers, addressing the infrastructure problems and input supply constraints, and strengthening farmers’ effective demand for fertilizer by making fertilizer use profitable, are some of the measures that can be taken as solutions for remedying the issues in fertilizer subsidies in Sri Lanka.

Inadequate Employment Opportunities in Less Developed Regions
Even though unemployment is dramatically declining in Sri Lanka, the percentage of the total employed people in the informal sector remains high. According to the Labour Force Survey 2009, 61.3 per cent of total employed people are in the informal sector. High informal sector employment contributes to inequality in Sri Lanka as there is a high wage gap between the informal and formal sectors. As can be seen in the Table 6, there is a high gap between formal and informal sectors in all three industry groups. Looking at the mean monthly salary distribution of monthly earners and the daily earners by major industry groups, it is evident that, in the services sector there is a high gap between those who are paid on a monthly basis and those who are paid daily wages. This gap is much higher compared to the other two sectors. As a result, income disparity still exists in the Sri Lankan economy.

Table 6: Mean & Median Monthly Gross Salary by Major Industry Group - 2009

<table>
<thead>
<tr>
<th>Measurement</th>
<th>Agriculture</th>
<th>Industry</th>
<th>Service</th>
</tr>
</thead>
<tbody>
<tr>
<td>Monthly wage/salary earners</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Mean</td>
<td>8,541</td>
<td>13,135</td>
<td>17,797</td>
</tr>
<tr>
<td>Median</td>
<td>6,500</td>
<td>10,000</td>
<td>16,450</td>
</tr>
<tr>
<td>Daily wage/salary earners</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Mean</td>
<td>6,803</td>
<td>9,549</td>
<td>8,582</td>
</tr>
<tr>
<td>Median</td>
<td>6,000</td>
<td>9,000</td>
<td>7,800</td>
</tr>
</tbody>
</table>


Structural Injustice
A study on the subject by Tilekeratna et al. (2009) points out some very important facts in regard to ownership of assets by the poor. First, the ownership of land has become less important as a source of both poverty and income distribution. The on-going structural changes in the rural economy indicate that households increasingly depend on non-farm sources of livelihood. Second, that significant disparity still prevails in the quality of education available to the urban elites compared to those who come from less privileged backgrounds or live in less developed areas. In contrast to other South Asian countries where disparity in quality between private and public education prevail, in Sri Lanka it is disparities in quality within the public education system which perpetuates inequality. The study goes on to state that “.. there is no evidence to suggest that the relative deprivation
of the resource poor to superior quality education will be substantially corrected, any time soon in Sri Lanka” (p. ix).

Third, in regard to credit distribution among the poor the study finds that a large proportion of households, with access to microcredit, progress in poverty reduction has been rather modest. Microcredit has indeed done little to change the position of the poor household in the value addition chain. Households provided with micro loans still have to compete on unequal terms in the market, thus, remains vulnerable to the vagaries of the market. Access to micro credit is no guarantee that individual micro entrepreneurs can grow out of poverty on a sustainable basis.

The conclusion of the said study is that “… interventions in all these key sectors do not necessarily add up to the sum of their parts, so as to end poverty. Little attempt appears to have been made by Sri Lankan policy makers to integrate these unique interventions in order to address the problem of poverty within a holistic framework. Nor have these programmes taken into account of structural sources of poverty related to unequal access to land, knowledge, and capital.

7 Concluding Remarks

Sri Lanka experienced reasonably high economic growth during the last few years. However, the effects of this fast growth while reducing poverty most of the time have resulted in two types of inequalities: income inequality and regional disparity.

The war which occurred in the Northern and Eastern Provinces has created a new form of inequality. Entitlement failures such as loss of public entitlements, loss of market/livelihood entitlements, loss of civil/social entitlements, and reversal of entitlements have created new forms of social inequalities. Moreover, destruction of assets, migration, loss of family members especially bread-winners, destruction of financial markets have had a negative impact on the livelihood of the people in the conflict affected areas and led to a new form of social inequality. The major challenge for inclusive growth in the post-conflict era is to address this new form of social inequality which is in addition to the existing inequalities in the country.

With the objective of providing equal opportunities for the poor as well as for the people from remote areas, successive governments have taken many measures. The current regime has also implemented a special growth and welfare package for North/East reconstruction/rehabilitation.

The story that emerges is that the same forces that contributed to increasing growth and reduction of poverty are responsible for widening economic inequality. This is because people had different access to endowments that would enable them to integrate them into more dynamic sectors. Growth was not inclusive enough, poverty declined but inequality increased. It will be a challenge for policy makers to find alternative forms of growth that
reduces both poverty and inequality. In regard to the Northern and Eastern Provinces, not much could be said about the effectiveness of the existing government programmes as it is still too early to obtain comparable accurate data.

The paper highlighted the reasons for the high inequality and a number of weaknesses in the existing packages to address inequality that needs to be addressed. While rectifying them, serious attention is required to integrate the war affected provinces to the rest of the economic system in Sri Lanka.

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