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Inclusive Growth in Sri Lanka

Saman Kelegama

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 a larger number of people below the poverty line than in any other region in the world. Sobhan has argued that persistent poverty in the region derives from the unjust nature of the social order which effectively excludes the poor from equitable opportunities for participating in the development process.[1] 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 being in place.

The central premises of Sobhan's work seek to move away from visualization of poverty as a measure of income deprivation. An attempt is made to redefine 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. Thus, it is argued that eradicating poverty should be measured through the change in opportunity structures for the excluded.

The inequitable distribution of opportunities across society and 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; rather it 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 financial resources to the excluded, nor the promotion of growth, are likely to resolve the problem of poverty. Sobhan (2010) also suggests 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 on poverty in South Asia goes on, it must be recognized that the ultimate objective of growth is to achieve 'development' in the region. In his pioneering work, Sen has shown that development, as an expression of freedom, encompasses all forms of freedom—economic, political, and social—and embraces all segments of society, not just a privileged few.[2] For widespread enjoyment of freedom to be possible, the growth process must be inclusive, in other words, the structures of production and employment associated with the growth process must be of a nature that offers opportunities to all segments of society to benefit from economic expansion. In the remaining sections of this essay, inclusive growth is further elaborated upon and the Sri Lankan scenario is examined.

What are the Policy Ingredients of Inclusive Growth?

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

High and Sustainable Growth

High and sustainable growth leads to the creation of productive and decent employment opportunities. Strategies for gaining high and sustainable growth vary from country to country, depending on a 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 is where opportunities for productivity growth have been located. One way of ensuring the sustainability of growth is integration with regional and global economies. This requires continued investments in physical infrastructure, human capital, improving the business environment, foreign trade, and foreign investment. The main role of the government in this regard is investing in physical infrastructure and human capital, building institutional capacities, maintaining macroeconomic stability, adopting market friendly policies, protecting property rights, and maintaining the rule of law. Such government intervention helps in sustaining market competition through minimizing market failures and thereby induces integration and sustainable economic growth.

Social Inclusion

The second strategy of inclusive growth is social inclusion. Public intervention on social inclusion is required in three broad areas: (1) expansion of human capacities, especially of the disadvantaged, through investments in education, health, and other social services; (2) improvement in social and economic justice through promotion of effective policies and sound institutions; and (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.

Expanding Human Capacities

Sustainable growth provides resources for developing 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 perhaps 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 increase labour productivity and thereby poor people's earning capacities. Moreover, improved health conditions of the poor may reduce expenses on medicines and increase savings. Better access to clean water and sanitation contributes to good health. The government has the main responsibility for providing education, health, and other social services as there are strong

externalities in these sectors. However, in developing countries, governments face financial problems in providing these services to citizens.

Effective Policies and Sound Institutions

As discussed earlier, promoting social inclusion requires effective policies and sound institutions. The expansion of human resources/capacities will 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.[4] In the presence of weak institutions and governance, social injustice will be more severe. Thus, the government has a key role to play in maintaining effective policies and building/consolidating institutions. Political, economic, cultural, and social freedoms ensure that members of society will 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.[5]

Social Safety Nets

The main role of social safety nets is mitigating the adverse impact of external shocks faced by the poor and fulfilling their basic needs. Risks faced by the poor are mainly related to ill health and other life cycle events, macroeconomic crises, 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 forms 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 wages in the labour market. Labour market policies attempt to enhance the quality and skills of labour through skill development and training. Effective labour market policies improve labour skills so that they can match global standards. Social insurance, such as pension schemes, mitigates 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/cash transfers to the most vulnerable groups. Child protection ensures the healthy and productive development of children.

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 in democratic polity. The policy agenda is premised on elevating the excluded from agents into principals through repositioning 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. This will impart to them the capacity to invest. Sobhan (2010) states that democratizing access to assets and markets should be backed by equitable access to education and healthcare.

Repositioning of the excluded should be built on strengthening their capacity for collective action, that is, strengthening their capacity to participate and to 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 their capacity to compete in the marketplace, (3) designing institutions for collective action by the excluded, (4) enhancing access to quality education, (5) redesigning the budgetary policy to reach the excluded, and (6) restructuring the financial policy to deliver credit and provide savings instruments to the excluded.

Is Inclusive Growth Visible in Sri Lanka?

Sri Lanka has been experiencing an average economic growth of 6 per cent since 2003. A resurgent economic performance with GDP growth of 8 per cent was visible in 2010 after a dip to 3.5 per cent in 2009 consequent to the global economic crisis during 2008–09.[6] Sri Lanka's economic growth has been characterized by low total factor productivity and low average productivity of investment.[7] Even so, Sri Lanka was able to double its per capita income from US$ 1,241 to US$ 2,053 within a 5-year period from 2005 to 2010, although high inflation during this period did make a substantial contribution to this enhancement (Table 10.1). Consequent to a rapid increase in per capita income, Sri Lanka was categorized as a middle income country by the International Monetary Fund (IMF) in January 2010.

The poverty headcount ratio has been declining as a result of high growth and according to the Department of Census and Statistics, it was around 15.2 per cent in 2006–7 as compared to 26.1 per cent in 1990–1 (Table 10.1). However, this level of poverty, based on income

Table 10.1 Income Per Capita and Poverty Incidence in Sri Lanka

Year	GDP Per Capita, at Market Price US$	Average Annual Growth Rate	Headcount Ratio US$ 1 a day (%)
1990–91	473	6.2*	26.1
2006–07	1421	7.7**	15.2

Source: Central Bank *Annual Report* 2000–8 and Department of Census and Statistics.
Notes: * Data for 1990; ** data for 2007.

of less than US$ 1 a day becomes 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 shocks, ill health, or any other domestic shock.[8]

In Sri Lankan policy it has been a tradition to place poverty reduction efforts at the top of the government agenda.[9] 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. Notwithstanding these achievements, 15.2 per cent of the population remained under poverty in 2006–7, 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 1990–5 was not very impressive. Poverty in fact increased between 1991–2 and 1995–6: from 26.1 to 28.8 per cent of the population. Some have argued that the time span 1995–6 should be excluded from the 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.

Per capita GDP growth was 3 per cent per year between 1990 and 1995–6. According to various surveys, many of the poor experienced an increase in poverty. The increase in poverty during 1991–2 and 1995–6 is puzzling in the light of the following: (a) economic growth on an average of 5 per cent; (b) unemployment declining from 17 per cent in 1990 to 11 per cent in 1996; (c) private remittances doubling; and (d) maintaining expenditure on education and health despite escalation of defense outlays.

What explains the modest decline in poverty? Poverty has the highest prevalence (32 per cent) in households that derive their income from agriculture.[10] Slow growth in agriculture was perhaps the main determinant of increase in poverty during 1991–6. Agriculture grew by only 1 per cent during 1991–6. 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 have argued that poverty levels in the mid-1990s would have been higher if not for transfers to rural economies from overseas worker remittances, and transfers from workers in readymade garment factories and the armed forces.[11]

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 remained highly vulnerable to income shocks and were unable to take advantage of the opportunities generated by high growth in the early 1990s. The issue with regard to poverty reduction becomes clear when we compare the poverty reduction from 1990 to 2002, where the average annual reduction in the incidence of poverty was 0.28 percentage points (poverty declined from 26.1 per cent in 1990 to 22.7 per cent in 2002) as compared to GDP per capita increase of 3.1 per cent per annum. The implicit growth elasticity of poverty reduction was about 0.3 which is insignificant compared to other Asian countries.[12]

A more pressing issue is that this rapid growth has not trickled down to the key areas at 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 increased between 1990 and 2006 from 0.43 to 0.49. Sri Lanka's Gini coefficient increased more rapidly during the 1990s compared to countries such as Korea, Malaysia, Thailand, and Vietnam.[13]

The share of the poorest quintile (20 per cent) in national consumption declined from 8.9 per cent in 1990 to 7.1 per cent in 2006–7 which further confirms the rising inequality trend.[14] On the other hand, average per capita consumption during 1990–91 and 2002 grew by 50 per cent for the richest consumption quintile but by only 2 per cent for the poorest quintile.[15] 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 consumption patterns and lifestyles of the rich, are leading to a perceptible increase in social and political tensions, undermining social cohesiveness.

The favourable impact of economic growth on consumption-poverty may be reduced if there is a simultaneous 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.[16] 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 (Figure 10.1). Sri Lanka has not achieved high growth rates like China to compensate for the increase in income inequality. Also as Ravallion has argued, initial inequality matters and this could dampen the impact of economic growth on poverty alleviation.[17]

The World Bank undertook an exercise to decompose the change in poverty into parts that were a result of growth and of inequality respectively.[18] The results indicated that if inequality had not increased between 1990 and 2002, the observed growth in mean consumption would have

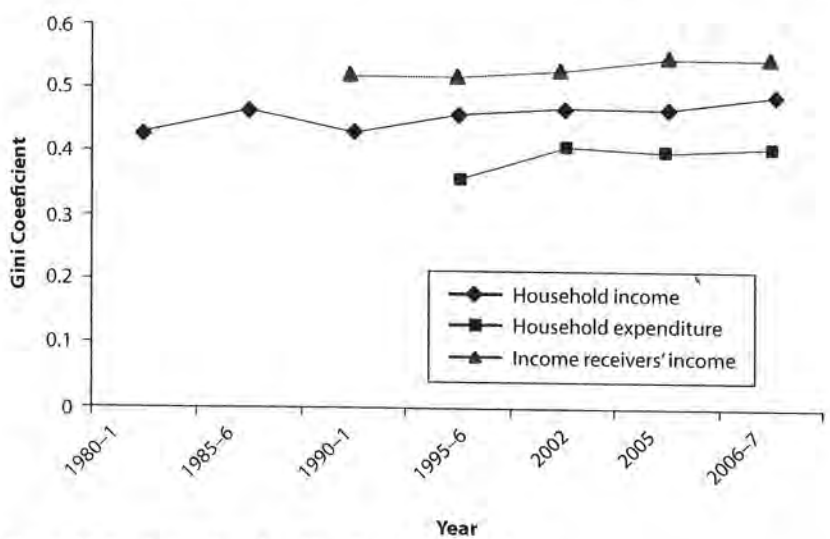

Figure 10.1 Recent Trend in Gini Coefficient in Sri Lanka
Source: Department of Census and Statistics.

been sufficient to reduce poverty by 15 percentage points. This would have brought the poverty level down to a single digit which is half of its actual level in 2002. In other words, the increase in inequality that took place during 1990–2002 prevented the decline in poverty headcount by over 15 percentage points. The World Bank (2007) goes on to argue that Sri Lanka is deeply entrapped in an 'inequality trap'.[19]

A decomposition analysis done by Gunatilaka (2011) shows that income flows associated with access to infrastructure, education, and the nature of occupation, are the principal determinants of inequality and the main drivers of the change in income distribution. The inequality in the provision of education and infrastructure as factors underlying the overall income inequality has increased over time. 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.[20] 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 benefited disproportionately more from state provision of education and infrastructure.

Osmani shows that three components of income exerted the most unequal 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 Bangladeshis abroad. These three components, according to Osmani, played a critical role in accelerating the pace of growth and poverty reduction in Bangladesh during the post-1990 period. Thus, the Sri Lankan experience with regard to worsening inequality is not a unique event.[21]

Income disparity is more compounded across different sectors and provinces. Even though Sri Lanka is on track to achieve many of the MDG targets and has already achieved some of them, there are considerable regional disparities which need to be addressed. For example, according to the Department of Census and Statistics, the poverty headcount ratio declined in all districts except Nuwara Eliya and Monaragala where the headcount ratio was double the national level (see Table 10.2). On the other hand, poverty indicators show that there has been a decline in rural and urban sectors while there has been an increase in the estate sector. Therefore, a 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 10.2 Poverty Headcount Ratio by Sectors and Provinces

Sector and Province	Population Estimate, '000 (2006)	Population as Percentage of Toral Population	Poverty Headcount Ratio (1991–2)	Poverty Headcount Ratio (1995–6)	Poverty Headcount Ratio (2002)	Poverty Headcount Ratio (2006–7)	Poor as Percentage of Total Poor in 2006–7
Sri Lanka	19,886	100.00	26.10	28.80	22.70	15.20	100.00
Urban	24,671	14.60	16.30	14.00	7.90	6.70	6.60
Rural	135,481	80.00	29.40	30.90	24.70	15.70	82.20
Estate	9,141	5.40	20.50	38.40	30.00	32.00	11.30
Western	5,648	28.40	19.00	17.00	11.00	8.20	15.19
Central	2,567	12.91	30.00	34.00	24.00	22.30	18.82
Southern	2,391	12.02	29.00	32.00	28.00	13.80	10.92
Northern	1,146	5.75					
Eastern	1,578	7.94				10.82	4.23
North Western	2,256	11.35	26.00	27.00	27.00	14.60	10.93
North Central	1,173	5.90	24.00	25.00	21.00	14.20	5.51
Uva	1,257	6.32	32.00	47.00	37.00	27.00	11.17
Sabaragamuwa	1,870	9.41	31.00	42.00	33.00	24.20	15.00

Source: UNDP (2008–09).

Challenges in Post-conflict Sri Lanka

Although successive governments have taken several steps for inclusive growth, the effects of these policies have been concealed by the North–East war in the country. Conflicts affect poverty through entitlement failures in direct and indirect ways. War is a barrier for poverty reduction and thus for inclusive growth. According to Draman, 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.[22]

Loss of Public Entitlements

Loss of public entitlements has direct as well as indirect effects. Breakdown of public order and public infrastructure can be identified as direct outcomes of loss of public entitlements, while growing macro-insecurity of states and regimes can be identified as indirect effects. Public infrastructure in the North, and to some extent in the East, was more or less destroyed due to the internal war situation.[23] 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 Jaffna district to the southern parts of the country.

Loss of Livelihood Entitlements

The destruction of 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 the North and South, and the consequent disconnection of the war affected region from the rest of the country, created a negative impact on the livelihoods of war affected people through loss of markets. The extent of land under agriculture in the North and East in 2002, had been reduced by 25 per cent as compared to 1982.[24] In addition, destruction of assets and financial markets, migration and loss of family members, especially bread winners, had a negative impact on the livelihoods of people in conflict affected areas.

Loss of Civil/ Social Entitlements

The direct impact of the loss of civil/social entitlements is the destruction of social capital and social networks through displacement. Indirect

impacts of the loss of social entitlements are failure of institutions, and competition for resources. For instance, the Samurdhi Poverty Alleviation programme was not operational in Killinochchi, Mannar, and Mullativu districts before the liberation of those areas due to the collapse of the administrative structure.

Reverse Entitlements/New Forms of Inequality

Population displacement together with assets transfer leads to a new form of social inequality. This creates 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 addressing 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 since the loss of livelihood entitlements has made the households more vulnerable. However, it is difficult for existing social protection programmes to absorb such a large number of people due to financial constraints. The best way of getting displaced people out from the hunger trap is providing food in exchange for work. The government is planning to expand the Samurdhi Income Transfer programme, which is the main social protection/poverty alleviation programme in Sri Lanka, into directly affected areas. The programme has to be implemented with modifications to existing programmes, along with other social protection schemes. The measures which the current government has taken to overcome this new form of inequality are discussed in the next section.

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

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

Sustainable Growth

The most recent development plan in Sri Lanka is the Mahinda Chinthana Idiri Dakma—the 10-year (2006–16) horizontal development

plan (MCID). It tries to integrate the positive attributes of market oriented economic policies while safeguarding the domestic aspirations by providing necessary support to domestic enterprises.[25] Priority has been given to regional development. In addition, education, health, livelihood development, social protection, disaster management, and water supply are covered by MCID's social development plan. 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, the focus is mainly on developing physical infrastructure, promoting a business friendly environment for a market oriented economy, and investing in social services (Table 10.3).

Physical Infrastructure

The current government has recognized that the low productivity of investment is partly due to weak infrastructure and has taken steps (under MCID) to uplift investment in physical infrastructure. These infrastructure projects are implemented at both the national and regional levels. 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 (development of roads) programmes.[26]

The overall objective of Gama Neguma and Maga Neguma is improving 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, and transport and rural infrastructure at the regional level. These programmes are following the participatory development methods

Table 10.3 Government Investment in Infrastructure

	Economic Services		Social Services		Total	
Year	Rs (bn)	Percentage of GDP	Rs (bn)	Percentage of GDP	Rs (bn)	Percentage of GDP
2006	106.8	3.6	48.4	1.6	155.2	5.2
2007	141.2	3.9	55.0	1.5	196.2	5.4
2008	168.9	3.8	60.2	1.4	229.1	5.2
2009	256.4	5.8	53.9	1.2	310.3	7.0

Source: CBSL Annual Report (2009).

for rural development. Maga Neguma was involved in the rehabilitation of around 1,350 km of rural roads in 2008–9, with most roads being concreted to ensure durability (IPS 2010).

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 and northern provinces—Negenahira Navodaya and Uthuru Wasanthaya. Moreover these two programmes aim to compensate citizens in the conflict affected areas for the loss of public entitlements of citizens.[27]

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 promoting the export–import sector as it is an effective driving force for growth. The other features of tax reforms include incentives for the promotion of domestic production, tourism, and service industries like finance, Information and communications technology (ICT), and telecommunications.

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 successive governments in the past laid a good foundation for achieving social inclusion in Sri Lanka and invested a significant percentage of its GDP on social development. Social policy in Sri Lanka has mainly focused on expanding human development and safety nets.

Expanding Human Capacity

After its independence from British rule, Sri Lankan governments introduced free education and free health facilities for its citizens. These health and education policies are universal in nature.

Education: According to the Education Act of 1945, education in Sri Lanka is free from Grade 1 to degree level and is universal. The government expanded the school network to fulfil educational demand and changed the medium of instruction from English to local languages to meet 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 educational opportunities for the poor, and increasing the quality of education, successive governments introduced different policies in different years. Establishing central colleges in the 1940s, implementing the common curriculum in the 1970s, introducing intervention strategies to compensate for socioeconomic differences, introducing the Grade 5 scholarship programme, district based university enrolment system in 1979, free school textbook programme in 1980,[28] free mid-day meal programme, free uniform material programme in 1993, and subsidized transport facilities, are among the steps taken (see Box 10.1).

Public expenditure on education was increased with the introduction of free education in the early 1950s to the end of the mid-1960s; this reached its peak in early 1970s. As can be seen in Figure 10.2, the government was able to spend more than 4 per cent of the GDP on education and the favourable economic climate in the country after independence supported such an allocation. However, the economic downturn together with structural changes in 1977, curtailed expenditure on social services including that on education. This reduction led to a decline in the quality of education and regional disparities in the educational sector. The current 2.5 per cent of GDP average expenditure on education is below that in many developing countries such as India (3.7 per cent of GDP), South Korea (4.2 per cent of GDP), Thailand (4.1 per cent of GDP), Malaysia (4.1 per cent of GDP), and Vietnam (5.3 per cent of GDP).

Challenges in the Post-conflict Era: Due to the conflict in the northern and eastern provinces during the post-1983 period, education for most students in these areas was disrupted due to displacement, loss of family members, psychological impact, loss of school material, and destruction of school buildings and infrastructure. UNICEF estimates that more than 48,000 school-going children had returned to their home towns by February 2010 (IPS 2010). However, there are a number of children who still live in camps and consequently there are several issues which need to be considered in providing basic educational services for the conflict affected groups: reintegrating with the school curriculum,

Box 10.1 Education Welfare Programmes in Sri Lanka

Free School Textbook Programme

This programme was initiated in 1980 with the aim of improving the quality of education. School textbooks are provided free to all students in Grades 1–11 in all state and state-aided schools. Currently, the programme 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. Government funds together with donor funds are the main source of funding for this programme.

Free School Uniform Material Programme

This programme was introduced in 1993. Under this programme all students in all the government and temple schools are provided free uniform material. The type of material and the quantity received by students depends on the gender and the grade in school. This programme is entirely funded by 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 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 group is school children in difficult areas, in marginalized families, and in identified schools where at least 30 per cent of the students are malnourished.

dealing with ex-child-combatants, providing educational infrastructure, ensuring adequate human resources, and psycho-social support. In addition, there are issues with educational infrastructure such as lack of essential material, 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. According to the Northern Province Department of

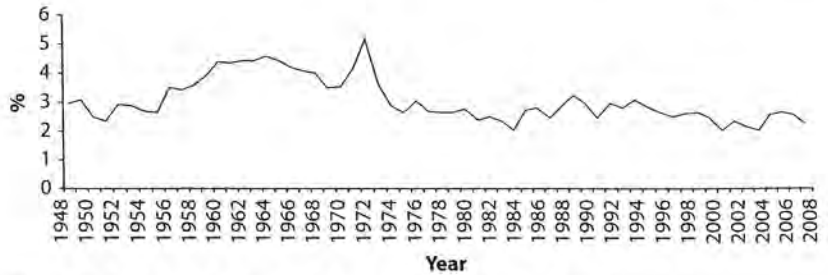

Figure 10.2 Education Expenditure as a Percentage of GDP
Source: Central Bank annual reports (various years).

Education, it is estimated that 115 out of the 326 existing schools had been reopened by the end of March 2010 (IPS 2010). Temporary learning centres (TLCs) and the catch up education system are two main steps. TLCs provide educational services for those living in camps. For instance, in Vavuniya and Mannar districts, 21 TLCs are providing continual educational services for IDP students. The catch up education programme reintegrates students with regular school curriculum.

Health: The pattern of public expenditure on health is somewhat similar to that on education. Public health expenditure was relatively high during the 1950s; 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 increased as a result of high demand for health services after the tsunami (Figure 10.3).

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

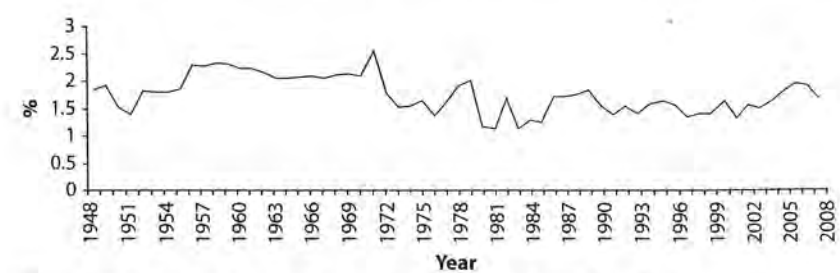

Figure 10.3 Health Expenditure as a Percentage of GDP in Sri Lanka
Source: Central Bank annual reports (various years).

Table 10.4 Selected Health Indicators for North and East

	Infant Mortality Rate Per 1,000 Live Births in 2000	Maternal Mortality Rate Per 1,000 Live Births in 2000	Low Birth Weight in 2001	Underweight in 2002	Home Deliveries in 2001	Safe Sanitation in 2001
Sri Lanka	11.2*	14*	16.7	29.4	4.0	72.6
North and East	14.7	81	25.7	46.2	19.4	48.2
Ampara	10.3	24	22.7	44.1	19.8	52.7
Batticaloa	15.8	117	24.3	53.2	31.4	28.4
Trincomalee	4.6	57	30.5	44.7	13.6	25.6
Jaffna	22.3	62	30.5	43.1	4.4	79.0
Killinochchi	27.8	158	NA	NA	NA	NA
Mannar	22.3	97	12.7	38.3	39.4	70.9
Mullativu	20.3	123	NA	NA	NA	NA
Vavuniya	8.8	76	38.8	50.6	2.3	71.0

Source: IPS (2010).
Note: * data for 2002.

funds accounted for 49 per cent, while private financing accounted for 51 per cent of the total health financing (IPS 2008).

Challenges in the Post-conflict Era: Sri Lanka has been able to maintain overall health indicators at a satisfactory level despite economic downturns over time. However, like in the case of other MDG indicators explained earlier, there are regional disparities in health indicators which are compounded in the conflict affected districts. As seen in Table 10.4, the maternal mortality rate is five times higher in the conflict affected North and East than it is at the national level and this incidence is even worse at the district level. With the end of the conflict, returned internally displaced people (IDPs) may make a greater demand for health services. The major challenge for the government is reducing the gap in health facilities between the conflict affected areas and the rest of the country and meeting the increasing demand from the former areas.

The Government of Sri Lanka has taken many steps to overcome issues in the health sector in conflict affected areas. For instance, the Ministry of Health has taken several steps to develop main hospitals in Jaffna district (IPS 2010). Further, the government has allocated US$ 3.2 million to uplift healthcare facilities and according to the Ministry of Rehabilitation and Reconstruction, the government has allocated US$ 4.2 million under the Uthuru Wasanthaya programme to improve health facilities in the Jaffna peninsula (IPS 2010).

Social Safety Nets

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

Social Assistance, Welfare, and Insurance Schemes: Samurdhi is the largest poverty alleviation programme in Sri Lanka which provides social assistance, social welfare, and social insurance to the poor. The Samurdhi programme was introduced in 1995 by an act of Parliament and according to the Central Bank of Sri Lanka (2008), 1.6 million households in the country had been covered by the programme by the end of 2008. The objectives of the Samurdhi Act of 1995 are: integrating youth, women, and disadvantaged groups into economic and social development activities, promoting social stability, and alleviating 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. On the other hand, long term strategies aim to address the core issues of poverty alleviation by using methods such as empowerment, social mobilization, and integrated rural development.

This Samurdhi programme is structured under two main components: (i) relief programme, and (ii) empowerment programme. The relief programme encompasses three sub-components—cash transfer, social security fund, and nutrition. 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 social security fund provides coverage against risks and lifecycle events such as death, marriage, childbirth, and illness. The nutritional programme is implemented in collaboration with the Ministry of Health and Nutrition. It provides an allowance of US$ 1.9 per month and it is valid for one year from a child's birth. The main objective of this programme is enhancing the nutritional level of pregnant and lactating mothers in poor families. The benefits of the relief programme are based on the size of the household. There are five sub-programmes under the empowerment programme: rural infrastructure, livelihood, social development, Samurdhi housing, and Samurdhi Bank Societies (SBS).

In addition to the Samurdhi programme, several other welfare programmes were 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 which targets vulnerable groups like the poor among the elderly and disabled, families without breadwinners, and destitute women and orphans. It provides an average monthly grant of Rs 135 which is less than the Samurdhi grant and the amount is not sufficient to meet living costs. The Thriposha Nutrition Supplement programme is another programme which is implemented with the purpose of enhancing nutritional levels of children less than 5 years of age, and pregnant and lactating mothers. There were 580,000 beneficiary families in 2005 (IPS 2008).

In addition to the social insurance provided by the Samurdhi programme, micro-insurance programmes are also playing a significant role in the social security of poor people. Micro-insurance programmes are mainly provided by micro-finance institutions but they are in their initial stages still. The Sarvodaya Economic Enterprises Development Sector (SEEDS), Women's Development Bank, Yasiru Mutual Provident Fund,

and the Sanasa insurance company are some of the institutions which play a significant role in the micro-insurance market. In addition to micro-finance institutions, commercial insurance companies such as the Ceylinco insurance company are also involved in the micro-insurance field. However, there are many barriers to the development of the micro-insurance sector such as lack of reinsurance facilities and lack of human resources, among others.[29]

Labour Market Policies: Most legislations governing the Sri Lankan labour market are outdated as they are legacies from the colonial and the closed economy era. Changes in labour legislations to suit the needs of the open economy are slow to come about. There were some radical attempts in the late 1970s and 2002–3 period to bring about some changes in labour legislations but there was only some partial success. The current government takes the view that since around 60 per cent of labour work is in the informal market, radical labour market reforms are not going to produce the desired impact. Hence, there are hardly any reforms taking place in the labour market other than some reforms for pension schemes. Retirement schemes are major labour market policies of the current government in the context of the rapidly ageing population. Sri Lanka is currently maintaining several retirement schemes. These include the Employees' Provident Fund (EPF) and the Public Sector Pension Scheme.

Voluntary Schemes (Farmers, Fishermen, and the Self-employed Scheme): As these retirement schemes are entirely for formal sector workers, Sri Lanka introduced pension schemes by acts of Parliament in 1987, 1990, and 1996 for workers outside the formal sector. The two main 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. The eligibility for the farmers' pension scheme depends on the type of crops cultivated, age, and non-entitlement to other retirement schemes. Eligibility criteria for the Fishermen's Pension Scheme is the same as that for the Farmers' 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, the two retirement schemes have social security benefits like disability, disablement gratuity, and death gratuity.

In addition to these two main voluntary retirement schemes, another pension and social security scheme for self-employed—the Self-employed

Pension Scheme—is also in operation. The Sri Lanka Social Security Board stipulates that only certain types of workers are eligible for the scheme depending on age, income, and non-entitlement to other similar pension schemes. Along with income benefits, this scheme also provides social security benefits.

Old age security of a beneficiary depends on the investment and utilization strategy of the retirement package. The largest retirement scheme operating in the public sector provides a single payment at the time of retirement. Retirement benefits have become a concern among the younger generation in the selection of employment and this generation prefers to select scarce government jobs rather than go for private sector jobs which are readily available. Taking this into account, the current government has proposed a pension scheme for workers in the private and corporate sectors. According to this new proposal, a 2 per cent contribution from employees and a 2 per cent contribution from employers would go to this scheme.[30]

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

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

Challenges

As explained earlier, successive governments took 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 for reducing inequality and achieving inclusive growth.

Poor Response of the Agricultures Sector

More than 30 per cent of the total employment is in the agriculture sector and a majority of the people in Sri Lanka directly or indirectly depend on this sector for their livelihood. However, the productivity of this sector is low while the cost of production is high. As a result, income of the people in the sector is also low and this is more severe due to the fact that average landholdings are relatively small. In addition, the less developed irrigation system and poor technology also negatively affect the productivity of the agriculture sector. Like in other production sectors, poor institutional market conditions and less developed infrastructure are also reasons for the poor performance of the sector. Poor performance leads to low incomes and these low incomes in 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 action to curtail expenditure. The need to curtail expenditure has been highlighted time and again by local economic institutions and 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.[31] Some of these programmes involve direct cash and/or in-kind transfers to the poor. The Samurdhi programme is considered a major transfer programme dealing with poverty reduction and equity objectives, accounting for 0.2 per cent of GDP.

Fertilizer Subsidy

In 2009, the fertilizer subsidy accounted for 3 per cent of the total government expenditure and 0.6 per cent of GDP.[32] Since this is a blanket programme, it incurs targeting errors and due to its universalism, there are over-applications of fertilizers. Most often small scale farmers are inefficient as compared to large scale 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, involving a wide range of fertilizer importers in the input voucher scheme, correct identification of poor

farmers, addressing infrastructure problems and input supply constraints, and strengthening farmers' effective demand for fertilizers 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 declining, the percentage of total employed people in the informal sector remains high. According to the Labour Force Survey 2009, 61.3 per cent of the total employed people were in the informal sector. High informal sector employment contributes to inequality as there is a large wage gap between the informal and formal sectors. As seen in Table 10.5, there was a large wage gap between the formal and informal sectors in all three industry groups. Looking at the mean monthly salary distribution of the monthly and daily earners by major industry groups, it is evident that in the services sector there was a large gap between those who were paid on a monthly basis and those who were paid daily wages. This gap was much larger compared to the other two sectors. As a result, income disparity still exists in the Sri Lankan economy.

Structural Injustice

A study on the subject by Tilekeratna et al. (2009) points out some important facts with 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 ongoing structural changes in the rural economy indicate that households increasingly depend on non-farm sources

Table 10.5 Mean and Median Monthly Gross Salary by Major Industry Group (2009)

Measurement	Agriculture	Industry	Service
Monthly Wage/Salary Earners			
Mean	8,541	13,135	17,797
Median	6,500	10,000	16,450
Daily Wage/Salary Earners			
Mean	6,803	9,549	8,582
Median	6,000	9,000	7,800

Source: Annual Report: Sri Lanka Labour Force Survey (2009).

of livelihood. Second, significant disparity still prevails in the quality of education available to the urban elites as 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 prevails, in Sri Lanka it is disparities in quality within the public education system which perpetuate 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, with regard to credit distribution among the poor, the study finds that in a large proportion of the households with access to micro-credit, progress in poverty reduction has been rather modest. Micro-credit has done little to change the position of poor households in the value addition chain. Households provided with micro-loans still have to compete on unequal terms in the market, and thus remain 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 structural sources of poverty related to unequal access to land, knowledge, and capital'.

All in all, it can be said that while many programmes are in place to address poverty and inequality, no concrete attempt has been made to address the specific problems of growth induced inequalities, inequality traps, low income elasticity of poverty reduction etc. and also to promote an integrated approach for making all these programmes more effective in addressing poverty and inequality.

* * *

Sri Lanka has experienced reasonably high economic growth during the last few years. However, the effect of this growth on reducing poverty has been uneven due to two types of inequalities: income inequality and regional disparities.

The war 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. The major challenge for inclusive growth in the post-conflict era is addressing this new form of social inequality which is in addition to the existing inequalities in the country.

With the objective of providing equal opportunities to the poor as well as to 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 reducing poverty are also responsible for widening economic inequalities. This is because people had different access to endowments that would enable them to integrate into the more dynamic sectors. Growth was not inclusive enough, poverty declined but inequality increased. It will be a challenge for policymakers to find alternative forms of growth that reduce both poverty and inequality.

The essay highlighted the reasons for the high inequality and a number of weaknesses in the existing packages for addressing inequality that need 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.

Notes

1. Sobhan (2010).
2. Sen (1999).
3. Ali and Zhuang (2007).
4. The World Bank (2006) cited in Ali and Zhuang (2007).
5. Rajan and Zingales (2007) cited in Ali and Zhuang (2007).
6. Central Bank of Sri Lanka (2010).
7. Ahmed and Ranjan (1995).
8. It may be noted that the North and East are excluded from all available data on poverty.
9. Lakshman (1997).
10. 38 per cent of the Sri Lankan labour force was still engaged in the agriculture sector in the early 1990s.
11. Dunham and Edwards (1997).
12. Ishii (2007).
13. Ibid.
14. UNDP (2008–9).
15. The World Bank (2007) cited in UNDP (2008–9).
16. Kelegama (1993).

17. Ravallion (1997).
18. The World Bank (2007).
19. For a definition of 'inequality trap' see the World Bank (2006).
20. Gunatileka (2011).
21. Osmani (2008).
22. Draman (2003).
23. IPS (2010).
24. Census of Agriculture 1982 and 2002 (DCS).
25. IPS (2008).
26. The Randora programme covers the areas of economic infrastructure, irrigation, education and health, industries, urban development, and development of townships. Huge infrastructure programmes such as the Upper Kothmale Hydro Power Project, Puttalam Coal Power Plant, the Colombo Port Expansion Project, the Hambantota Sea Port Development Project, the Galle Port Development Project, the Oluvil Port Development Project, Southern Expressway, and the Colombo–Katunayaka Expressway are covered by the programme.
27. IPS (2010), Kelegama (2010).
28. Textbooks became free of charge for all students in Grades 1–11.
29. Tilekeratne et al. (2011).
30. For the current debate on the subject, see http://www.island.lk/index.php?page_cat=article-details&page=article-details&code_title=25406.
31. Jayaweera (2010).
32. Thibbotuwawa (2010).

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