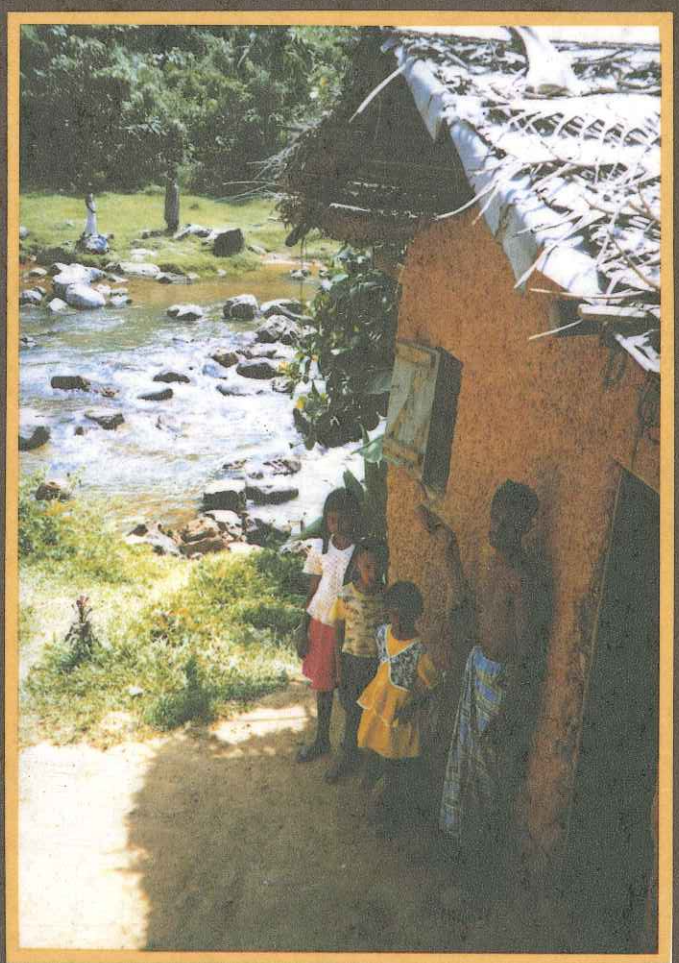
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Review of Literature Linking Macroeconomic Policies to Household Welfare in Sri Lanka



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The Micro Impacts of Macroeconomic and Adjustment Policies **(MIMAP)** program is an initiative of the IDRC, Canada with projects currently operational in several Asian and African countries. MIMAP is based on the idea that macroeconomic policies need to be guided by the final outcomes at the micro level. Hence, MIMAP program initiatives seek to increase the understanding of the links between macroeconomic policies and household income and wealth; and the 'feedback loop' that alters the efficacy of the original policy and its design.

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Section 1: Introduction

This review is an effort to explore the extent to which the existing literature on post 1977 Sri Lanka can contribute towards understanding of the process by which macroeconomic policies affect the welfare of households. Crucially, it will seek to understand the impact macro policies directed at economic variables, such as inflation rates, budgetary deficit and balance of payments, have on household welfare.

Considerable literature exists in relation to Sri Lanka's macro policy environment, poverty and welfare experience. Sri Lanka's early efforts and achievements in welfare and equity, and subsequent turnaround towards economic growth through market led adjustment policies has made it an obvious case study choice in developmental literature. Sri Lanka has been extensively used as a case study in the growth versus welfare debate of the 1980s and subsequently, in UNICEF's work on adjustment with a human face. Acute awareness and constant debate within Sri Lanka regarding the need for structural adjustment and its potential social costs have spawned extensive literature. However, most often the literature on macro economic and adjustment policies are separate from the literature on welfare impacts. The literature that does consider the links between the two are basically of two types; studies which connect macro policies to aggregate socio-economic welfare in an overall analysis, and those that look at specific sectors and aspects using descriptive or empirical methodology.

Given the vast area of interest - straddling as it does both the macro and the micro aspects of more or less the entire economy - and the equally vast coverage by literature, this review has not attempted to cover all literature relevant to every aspect. Instead it is limited to presenting the general direction taken by the body of literature at large and identifying the extent to which existing literature can form a knowledge base for subsequent research on macro-micro transmission channels, and to identify gaps in knowledge that need to be addressed.

The specific objectives of this study are:

1. To review the existing literature on policy reform in the post 1977 period and the literature on the welfare performance during the same period.
2. To assess the extent to which the existing literature facilitate the identification of channels of transmission between macro policy changes and welfare at the household level.

The structure of this review has been based on its objectives. Following the introduction is an assessment of the available literature and a brief descriptive presentation of what it says about macro economic and adjustment policies in the post 1977 period. Section 3 does the same for the poverty and social welfare situation brought about during this period. Section 4 attempts to identify channels of transmission between macro policy changes and welfare at the household level. Here the information generated by the literature reviewed in Section 2 and Section 3 are combined with the literature which specifically attempts to identify macro-micro links. The concluding section discusses the extent to which existing literature succeeds in providing a base for identifying channels of transmission between macroeconomic policy and micro welfare. It also identifies gaps in the existing body of literature in relation to understanding the process of transformation by which macroeconomic policies impact household welfare.

Section 2: Macroeconomic Policy

As most literature considers 1977 a watershed in Sri Lankan policy reform this review concentrates on the literature relating to the post 1977 period. The period prior to 1977 was characterised by economic management structured around economic planning, extensive government intervention, controls on trade and resource ownership with a limited role assigned to the private sector (Lakshman 1996). Though the policy reforms of the post 1977 period doubtless brought about liberalisation of the economy and a market orientation through radical changes, the prevailing policy environments of the two periods would be better represented by the terms 'predominantly closed / controlled' and 'predominately open / market' (Abeysekara 1993). The immediate policy changes of 1977 were more dramatic in their level of publicity and visibility than in actual structural changes. However, the continued and intensifying adherence to liberalisation and adjustment justifies considering 1977 as the beginning of a new macroeconomic policy era.

Two main phases of liberalisation can be discerned in the post 1977 period - the first phase from 1977-89 and the second since 1989. The change of government in 1994, inaugurated a sub period as the policy orientation towards adjustment and stabilisation continued with a few changes in emphasis.

A review of the existing literature[1] on macroeconomic policy shows that the initial phase is extensively documented and analysed. The second phase too has a substantial body of literature though not to the extent of the initial phase. However, there is a definite paucity of literature regarding the post 1994 period.

The methodologies used by most literature tend towards a descriptive style of analysis from a fundamentally technical economic base. The economic environment that necessitated or precipitated policy changes, the details of policy and the performance of the economy in terms of policy reform, are discussed extensively. Studies which follow a political economy approach to the analysis form the minority of the literature. Significantly, the bulk of the political economic analysis is of the post 1989 reforms (See Abeysekera *et al.* 1993; Dunham and Kelegama 1997).

This section does not consider in detail various policy changes. Instead it discusses briefly only those policies that the literature considers important in terms of its socio-economic impact.

2.1 The First Phase, 1977 – 1989

Briefly, the significant policy reforms initiated in 1977 consisted of:

- Liberalisation of trade and payments: Termination of state trading monopolies, the relaxation of price controls, elimination of import controls, export quotas and their replacement by tariffs.
- Exchange rate reform: Substantial devaluation of the Rupee, a change over to a managed float from the existing fixed, multiple exchange rate system.
- Rationalisation of public expenditure: Change in the consumer subsidy policy, gradual withdrawal of transfers to loss making public enterprises, closure of non-viable public sector ventures.
- De-control of prices and interest rates: Along with most commodity prices, interest rates were freed from control and market forces were allowed to operate.
- Reducing the role of the state in the economy: Growth was conceived to be private sector led and policy focus was to create an enabling environment for both local and foreign capital to fulfill such a role.

[1] See Annotated Bibliography of Macroeconomic and Adjustment Policies in the Post 1977 Period, MIMAP-Sri Lanka Series No. 3.

- Foreign investment and export promotion: Primarily through infrastructure and institutional development, while some reliance was placed on incentive packages

The initial phase of the reform process focused on economic growth and did not have a high profile welfare strategy. Instead, it claimed to rely on economic efficiency 'trickling down' to create welfare, complemented by an efficiently targeted income transfer programme. The emphasis in the allocation of public sector expenditure during 1977-84 was on infrastructure development to support the contrasting sectors of the private sector and rural development. The idea was to address poverty issues through growth and employment generation. Growth and employment was also to be generated through the Government's public investment programme which centred on three lead projects largely financed by foreign aid: the Accelerated Mahaweli Development Programme (for irrigation and power development), infrastructure for the Free Trade Zone project and the Housing and Urban Development Programme.

However, it should be noted that the perennial welfare orientation of Sri Lanka's policy did not undergo as much a dramatic change as would be expected to run parallel to other liberalisation policies carried out. The socio-political forces which created Sri Lanka's historical bias towards welfare continued to exert its considerable influence (Bastian 1993; Gunathilaka 1998). Sri Lanka was also able to attract substantial foreign aid to support the adjustment package which enabled financing of growth oriented policies without substantial cuts in welfare expenditure – food subsides being a major exception. Furthermore, there were no major cuts in government expenditure in the education and health sectors: universal free provision was continued (Jayaweera et al. 1988; Edirisinghe 1990; Alailima 1997; World Bank 1998a). However, private sector participation in delivery of health care and technical and vocational education was encouraged. In the school and university education limited private sector participation has been through the manipulation of the Company's Act (World Bank 1998a).

The most significant change in welfare policy occurred when the consumer subsidy policy which had been in operation for over three decades was replaced by a means-tested, non-indexed Food Stamps Programme.[2] The Food Stamps Programme ended the distribution of free rice rations to non-tax payers. The post 1977 food policy was based on an increase in the availability of food through the liberalisation of imports and trade of

[2] The value of the food stamp was fixed in nominal terms. Consequently, its real value declined rapidly due to inflation. The food stamp scheme ceased to exist in 1996 and its functions are now the responsibility of the Samurdhi programme.

food items, rather than through price controls and subsidies. Henceforth, subsidies were used as a safety net and were targeted to families with an annual income below Rs. 3600 (Edirisinghe 1987, 1988; Basu 1991).

2.2 The Second Phase, 1989 – 1994

The more technically crucial changes to the structure of the Sri Lankan economy were made following the change in leadership in 1989 when the Government entered into a three year Structural Adjustment Facility (SAF) with the IMF and subsequently in 1991, when it entered into an Enhanced Structural Adjustment Facility (ESAF). A fair proportion of these reforms were fulfilled over the period 1989-94 in an accelerated process of structural reform (Lakshman 1996). The macro policy reforms undertaken have been in six broad areas:

- Financial sector and capital market reforms: Development of the Treasury Bill and stock markets, liberalisation of portfolio investments, relaxation of credit allocation guidelines.
- Fiscal reforms: Changes in the corporate tax system, further elimination of subsidies and price controls, public sector rationalisation, increased income transfers.
- Foreign exchange reforms: Devaluation and further relaxation of exchange controls, acceptance of Article VIII of IMF Charter.
- Trade policy reforms: Rationalisation of the tariff structure.
- Privatisation and private sector promotion measures.

In terms of the socio-economic impact of these reforms the following points should be noted. The second phase of adjustment and stabilisation, while having an in-depth stabilisation programme, also saw a much greater emphasis on poverty alleviation. The literature on the background to the second phase of policy reform identifies a number of factors that influenced the change in policy orientation. The socio-political tensions that had come to a head in 1989 were seen to be fuelled by the 'perceptions among... the rural poor and urban working classes that the dynamics of the early liberalisation phase had effectively by-passed them' (Dunham and Kelegama 1995, 8). The pro-poor bias of the new President[3] was a major complementary factor in the policy re-orientation towards direct intervention for poverty alleviation. This was backed up by the change in donor

[3] The General Election of 1989 retained the same party in government but with new leadership under President Premadasa.

perceptions regarding the need to protect the vulnerable during adjustment periods. The Adjustment with a Human Face literature[4] (Cornia *et al.* 1987), and Social Dimensions of Adjustment studies were gaining ground by this time.

Though there was a re-entry of welfare and poverty alleviation as high profile policies, the basic premise of targeted intervention was adhered to, at least in the design of the front runner Janasaviya Programme. The Janasaviya Programme combined a monthly cash transfer to poor households with incentives to embark on self-employment projects which were to ultimately move the household out of poverty (JTF 1994; Wanigaratne 1996; Shaw 1999). The Janasaviya was visualised as a programme in keeping with market reforms and was implemented as an appendage to the macro economic policies. Among other sub-programmes launched was the mid-day meal programme for school children which was intended to improve nutrition among children. An important new element that was added during this period was the change in the image projected by the government regarding provision of welfare and poverty alleviation assistance. With the rise in popularity of participatory methodology, community and non-governmental institutions, etc. the state sought to project it self in the role of facilitator of poverty alleviation rather than the direct provider of welfare (Dunham and Kelegama 1995; Gunathilaka 1998; Lakshman 1998).

2.3 1994 Onwards

The elections of 1994 brought about a complete political change in the government. However, there was no real major change in economic policy but rather a continuation of past policies with an even greater intensification of privatisation. The changes continued with fiscal reforms (continuation of corporate and investment tax reforms and the introduction of the Goods and Services Tax), trade policy reforms (continuation of tariff reform and elimination of quantitative restrictions on the import of several agricultural products), private sector development, and financial and capital market reforms (World Bank 1998b).

[4] The UNICEF sponsored study concluded that 'Growth oriented adjustment is necessary but not sufficient to protect the vulnerable groups. The lack of coherent and adequate effort to protect vulnerable groups during the adjustment process ...(has)...meant that some deterioration in human conditions was evident in (Sri Lanka and Brazil) despite sustained growth in resources' (Cornia *et al.* 1987, 125).

The new government was elected on a platform of 'a market economy with a human face'. This however, referred more to issues of human rights and political repression than poverty and welfare (Dunham 1997).

Considering social policy, health and education reform has been brought to the forefront since 1994. The quality of the provision of health and education is being questioned as the market becomes more segregated with the provision of private services, and the state allocation of recurrent and capital funds change. Education policy reforms which seek to give quality and relevance to the education system have been formulated and are in the process of staggered implementation. Health policy reforms which are still in the early stages of formulation have been deemed by the World Bank as 'go(ing) in the right direction, (but) would benefit greatly from a broadening of scope to address the fundamental problems of the health sector in a more comprehensive and sustainable way, in particular, the secondary and tertiary health care needs of the population' (World Bank 1998 a).

The Samurdhi Programme replaced the Janasaviya Programme as the lead poverty alleviation programme. Though fundamentally similar the Samurdhi Programme had certain fiscal consequences as it was on a much larger scale and the income transfer component consumed at least 80 per cent of the total programme budget. As with its predecessor, the Samurdhi Programme is documented by the implementing agency (Mithraratne [various]; Ratnayake 1997) as well as by external evaluators (see Gunathilaka *et al.* 1997; Gunathilaka and Salih 1999).

Section 3: Poverty and Social Welfare

This section reviews the existing literature on poverty and social welfare. The literature on poverty and welfare is vast and varied. For ease of review they can be sorted into two broad groups based on their primary objective:

1. Studies that seek to conceptualise poverty and welfare and estimate its occurrence – either at a given point in time or over a period of time.
2. Those that provide descriptive analysis of the trends and disaggregated characteristics of poverty and welfare – once again, either at a given point in time or over a period of time.

For purposes of identifying channels of transmission between macro policy and micro level welfare, it is the second block of literature that is more directly useful. However, as the literature which conceptualises and estimates poverty and welfare form the base for the more descriptive analysis and, more importantly, contributes to its quality and reliability, it also becomes a crucial block of literature (see Bhalla 1985; Gunaratne 1985a; Nanayakkara 1994; Datt & Gunewardena 1997).

There are a number of studies which have attempted to analyse and compare the findings of these conceptualisation and estimation studies (Alailima 1986; Hopkins and Jogaratnam 1990; Lakshman 1997,1998). This literature brings out the commonalties and differences in definitions and methodology and also discusses the problems created when attempting to compare the findings of the studies.

Some commonalties discussed are:

- Predominant concentration on absolute poverty. An exception was the group of studies by Gunaratne 1985a, Bhalla & Glewwe1985 and Anand & Harris 1985 which attempted to measure poverty using a hybrid indicator of absolute and relative poverty.
- Most use an expenditure/consumption base rather than income base for estimating the incidence of poverty.
- Most study time trends in poverty.

Some common problems which constrain inter-temporal and comparative analysis which are identified and discussed in varying detail are: different levels and criteria used for poverty thresholds, different definitions, assumptions and methodology, different benchmark years. The importance of being aware that a slight variation in the poverty threshold can produce significant variations in the result is frequently emphasised (see Hopkins and Jogaratnam 1990; Lakshman 1998).

These critical discussions become very helpful when using the conceptulisation and estimation studies as the base for further work. However, secondary literature which use information generated by poverty estimate literature tend to use the studies which best backup their argument (see World Bank 1995; Lakshman 1998).

However, if links between macro policy and welfare changes at levels beyond the national level are to be established, information regarding trends in various welfare and

poverty indicators in relation to different groups, regions, sectors, etc. are needed. If such information is available it becomes possible to identify which groups have been positively, negatively or negligibly affected and in which aspects of welfare.

3.1 Characteristics of Poverty and Welfare

Studies which deconstruct poverty and welfare into disaggregated segments most rigorously are those that focus on analysing national surveys. Examples of such work are Edirisinghe (1990) which is based on the Consumer Finances Survey 1986/87, Nanayakkara (1994) which is based on the Labour Force and Socio-Economic Surveys of 1980/81 and 1985/86 and the Income and Expenditure Survey of 1990/91, Datt and Gunawardane (1997) which is based on the two latter surveys.

These and other studies based on the data compiled by the Department of Census and Statistics and the Central Bank of Sri Lanka enable the exploration of questions such as where do the poor live? What are their sources of income? What is the profile of a poor household? To what extent are their basic needs such as nutrition met?

The main trends and disaggregations analysed in the literature are briefly summarised below.

3.1.1 Poverty and Income Distribution

With respect to the incidence of poverty in Sri Lanka the literature concludes that absolute poverty is highest in the rural sector and lowest in the estate sector. According to the 1990/91 Household Income and Expenditure Survey, the incidence of poverty in the rural sector was 24 per cent, followed by 18 per cent in the urban sector, and 13 per cent in the estate sector. However, when considering inter-temporal patterns of the incidence, depth and severity of poverty, it can be seen that while the conditions improved in the rural and estate sectors, a deterioration has occurred in the urban sector between the periods 1985/86 to 1990 /91.

With respect to the distribution of income between sectors, the urban sector seems to have been better equipped to reap the early benefits of liberalisation. The urban sector's share of total income rose from 28 per cent to 36 per cent during the period 1981/82 and 1985/86 while the share of the rural sector dropped from 67 per cent to 59 per cent.

However, income disparity within the urban sector increased markedly indicating that a very narrow spread of income had taken place: the Gini co-efficient has increased from 0.44 to 0.62 between 1980/81 and 1990/91 in the urban sector.

With regard to the occupational composition of the poor, agricultural and animal husbandry workers, farmers, construction workers, technical related workers, sales workers and labour not otherwise categorised made up 80 per cent of the poor in 1986/87 (Edirisinghe 1990). This trend seems to be continuing as Nanayakkara's (1994) analysis of 1990/91 data shows that manual labourers are the worst affected group in terms of incidence of poverty irrespective of whether they are in the agricultural or non-agricultural sector. Unlike most other studies Datt & Gunewardene's (1997) analysis of poverty by sector of employment attempts to reflect occupational diversity within the household as well as multiple occupations of individuals.

3.1.2 Human Development

Sri Lanka's achievements in human development are very well documented. However, the picture becomes more blurred once the literature moves away from the high achieving national aggregates such as literacy and life expectancy. At levels of greater disaggregation, quality of services becomes a vital issue. The clue to determining change in the quality of social services comes from disaggregating total public expenditure on these services. In the adjustment period, real per capita expenditure hardly increased for the social sector as declining recurrent expenditure set off increases in capital investment. There was also a disparity in the distribution of investment. For instance, although overall capital expenditure on health and education increased, expenditure in the sub-sectors of vocational and technical training and primary health care remained static. By the end of the 1990s, infrastructure development in health shifted from provincial and base hospitals to national hospitals.

The changes in public expenditure on social welfare services resulted in a change in the distribution of benefits accruing to different income groups. For example, the quality of education provided by schools in sparsely populated areas deteriorated rapidly (Alailima 1985). However, as this deterioration has been from a very high base, Datt and Gunawardena (1997) conclude that the variation between the literacy levels and average years of schooling between the national average and the poor groups are not that significant.

Malnutrition, (especially among young children), is an indicator that continued to throw a shadow on Sri Lanka's human development achievements. Disaggregated data show serious calorie deficiencies in the lower income groups. In 1986/87, approximately 90 per cent of the bottom most quintile of income earners had less than the recommended calorie intake. When considering the sectoral occurrence of malnutrition, the most serious problem lies in the lowest income quintile of urban sector households.

At a district level, dietary inadequacies (i.e. consuming less than 80 per cent of the requirement), stunting and wasting are most obvious in Kandy, Nuwara Eliya, Matale, Badulla, Trincomalee, Batticaloa and Ampara (Alailima 1984).

When disaggregated by employment type, nutrition standards are lowest among households where the main income earner is an agricultural or animal husbandry worker, labourer, cultivator or farmer (Shan 1984; Alailima 1988). In 1981/82 these households make up 61 per cent of those in the lowest expenditure quartile. However, Nanyakkara (1994) shows that there have been significant improvements in the nutrition levels between 1980/1 and 1990/1 in all three sectors. The improvement has been most significant in the estate sector.

Malnutrition has also been disaggregated by age to arrive at trends in child malnutrition. 36 per cent of all pre-school children were found to be suffering from chronic malnourishment in 1980/82. The rate had dropped only very marginally to 32 per cent by 1988/89 (Edirisinghe 1990). The trend traced by the World Bank's (1995) poverty assessment report points to an improving situation. The incidence of malnutrition among young children[5] has been decreasing since 1979/82.

The only digression has been in the 1987-89 period which has been explained away citing the social disturbances of the period. Nanayakkara's (1994) calculations complement these observations by concluding that there was an improvement in the national nutritional levels between 1985/86 and 1990/91. He also concludes that the percentage of households 'nutritionally at risk' is decreasing. There are a number of studies, however, which point to a progressive drop in calorie consumption (Alailima 1984, 1991).

[5] Measured in terms of wasting and stunting.

3.1.3 Employment

Employment merits special attention as it is a key means to increasing welfare as well as an indicator of welfare. Almost uniformly, the literature on employment base their studies on data from the Labour Force Surveys of the Department of Census and Statistics. However until 1990, the absence of time series data generated by consistent and regular surveys of employment has constrained analytical studies (Korale 1989; Rodrigo 1994; Kiribanda 1997).

A net expansion of employment opportunities created by policy reform has been reflected in the aggregate employment trends. Unemployment which was 25 per cent in 1977, fell to 14 per cent in 1984 and to 11.7 per cent by 1996 (CBSL 1998). The employment growth rates followed the GDP growth very closely in the first decade after reform. The post -1977 period was one of high employment growth. Between 1981 and 1985/86 employment grew at a phenomenal 5.1 per cent. Though the growth rate reduced to around 3.2 per cent during the latter part of the 1980s it was still positive and much higher than the pre reform years. 1991 and 1992 saw a negative growth rate for the first time but 1994 saw an escalation to 4.8 per cent before settling to a more sustainable rate of around 1 per cent (Korale 1992; Kiribanda 1997).

Employment can be disaggregated by regional concentration, sectoral change, occupational type, gender and age distribution and quality (based on the level in the occupational ladder).

Regionally, economic opportunities have concentrated in metropolitan and regional growth centres. Considering the growth of employment opportunities in the manufacturing sector, industrial growth especially in the early phase of reform has been predominantly in the Western Province (Samarasinghe 1989; Dassanayake 1998).
In terms of sectors, the fastest growing sectors have been construction, services and wearing apparel, all of which are highly labour intensive. This had a positive impact on employment. However, the construction boom financed by deficit financing and foreign aid was not sustainable in the long-run. Furthermore, it should be noted that significant structural changes have occurred in the manufacturing sector as a result of policy changes. The 'some gain, some lose' issue is very visible when employment in the manufacturing sector is disaggregated. The most famous losers of the first phase were the workers in the handloom industry (Waidyanatha 1980; Osmani 1987).

With respect to age, between 1980/1 and 1985/6 employment rates have increased in the first 3 groups - i.e. 10 years to 29 years. The 'most prominent increase has been in the 10-14 age group, hinting at a substantial increase in child employment particularly among females (Jayaweera 1988 *et al.*).

Disaggregating by gender, most literature reviewed agrees with the idea that the generation of employment in the post reform period has been biased towards women[6] (Rodrigo 1994; Lakshman 1998b). Female unemployment rates decreased faster than those of males. In 1985/86 female employment grew at a rate of 13.3 per cent while male employment grew at a steady average of 2.5 per cent except in the negative years of 1991 and 1992 (Kiribanda 1997). Female labour is also significant in overseas employment rates. They make up over 70 per cent of the overseas migrants (Rodrigo 1994). However, this aggregate picture needs to be analyzed in its structural dimensions since each group of female workers was affected differently by adjustment policies.

Increased female labour force participation was also visible in the agricultural sector, especially paddy. This was particularly visible in the first phase of reform. Community and social services also absorbed a considerable share of female labour (Jayaweera *et al.* 1988a; Rodrigo 1994).

In terms of the quality of employment generated, a number of disturbing trends has been discerned in the literature (Jayaweera *et al.* 1988a; Rodrigo 1994). The increase in employment in the manufacturing sector has been primarily in the low paid, low skilled strata. Examples include low-skilled workers in the garment industry (Rodrigo 1994; Lakshman 1998). The conditions under which most women have secured employment are very low. Women have been hired in such large numbers because of the very nature of the jobs available and because women take up employment even under adverse labour and welfare conditions. Furthermore, the disproportionate rise of females in unpaid family labour and casual employment is seen as evidence of strain and stress in the labour market, rather than a signal of prosperity and stability (Rodrigo 1994).

A further development is what Rodrigo (1994) terms the trend towards 'informalisation' - the expansion of the informal sector. The expanding informal sector, especially in the

[6] Contrastingly, the rapid expansion of the security and defence sector has been the growth area for male employment (Rodrigo 1994).

manufacturing sector, has the implications of reversals in the social security coverage and facilitates the evasion of protective labour legislation by employers.

The literature also identifies a trend in the deterioration of the real wage rate of fixed income earners in the organised sector as against those in the unorganised sector. Sandaratne (1984) [7] concludes that wages in the unorganised sector appear to have responded to price increases though not adequately in all sub-sectors: the most responsive has been the paddy sector and the construction sector while the least responsive has been the female rubber sector and male tea sector. In the organised sector real wage rates dropped most in the middle and low wage categories. Given that low income groups derive more than 70 per cent of their income from wages the behaviour of real wages has a strong impact on the welfare of these groups (Alailima 1985; Edirisinghe 1990).

3.2 Empirical Studies

Another group of literature exists which is of particular interest to the study of micro impacts of macro policy due to its emphasis on the household level. These studies are slightly removed from the mainstream economic literature and do not rely on the conventional sources for data. While the level of disaggregation and the type of analysis attained by the literature discussed so far is constrained by data availability, these studies go a long way in overcoming this weakness. They frequently combine quantitative and qualitative data with impressionistic evidence and follow a case study approach in methodology. Analytical methods are heavily influenced by those used in sociology, anthropology and political science and the concept of vulnerability is defined not only in terms of income, but also in terms of other socio-political criteria (See ARTI [various], CENWOR 1987, 1995; Jayaweera *et al.* 1988b; Samarasinghe 1989; Jayaweera and Sunmugam 1993; Lakshman *et al.* 1995; Malalgoda and Hidellage 1995; de Soysa 1996; Jayatilaka 1998).

While this literature provides essential insights into the micro level it is important to be aware of its weaknesses.

[7] Sanderate (1984) divides the organised sector into 3 sub-sectors - the government, school teachers & those trades in the private sector and corporations which are governed by Wages Boards. He includes small-holding cultivators of tea, rubber, coconut, paddy and building construction activities in the unorganised sector.

As a block of literature its main weakness lies in the coverage of vulnerable groups and aspects of welfare. Certain groups – such as women, small-producers, urban slum dwellers, irrigation scheme settlers, plantation workers - are extensively researched while others are largely neglected. It is possible to hypothesise that these areas have received attention due to the perceptions that they are particularly vulnerable to change and also due to the trends in international research. At a methodological level, the main weakness arises from the limited sample size and the tendency to reach speculative conclusions when linking impacts to policy.

Studies that concentrate on women form a large block of this literature. The vulnerability of poor women to economic reform and social pressures, and the entry of women into the labour force through employment opportunities created by policy reform has spawned numerous micro level empirical studies.

Most of the literature concentrates on employment as a source of change. Though employment opportunities grew for women in agriculture (mainly in paddy), and community and social services, it is the impact of employment in the export industries and overseas migration that has received the greatest attention. In addition to studying the quality of employment, conditions of work and pay, and living conditions of labour, some studies also look into the influence on the status and position of women, the impact on the family structure, child rearing, intra-household power relations, etc. which affects the overall wellbeing of the household (See Voice of Women 1983; Abeywardena *et al.* 1994; Jayatilake 1998; CENWOR [various]).

In a detailed study of two villages in the Southern Province, Jayatilaka (1998) finds that women have taken advantage of new opportunities created by the export industries, tourism and overseas migration, to move out of traditional economic activities which were mainly home based, unremunerated or poorly remunerated. She concludes that in such families the woman has become the main income earner and thereby reduced her dependence on her husband and extended family and has gained more confidence and assertiveness in decision making within the family. Despite these gains however, policy reform has had little impact on general gender ideology. There continues to be unequal division of labour within the household and, even if unemployed, the man rarely takes on the role of 'home maker'.

At the village level, a blurring of class boundaries has occurred due to the rising affluence of some families and their lessened dependence on the richer / elite classes. On the adverse side, as economic mobility occurs only to certain households there is a rise of intra-class jealousies and rivalries and a deterioration of solidarity. Each group – women in traditional occupations, migrant women, factory workers – thought adversely of the other, both in social and economic terms (Jayatilaka 1998).

Small producers are another group frequently identified as being strongly affected by the policy reform and adjustment process. The literature considers the impact on small producers in terms of increased competition, change in the incentive structure and policy orientation away from small producers, issues relating to cost and access to raw material and tools, employment and income generation (see Ariyabandu and Hidellage 1994; Lakshamn *et al.* 1994; Siriwardene 1994).

Ariyabandu and Hidellage (1994) studying small producers in the non-traditional agricultural exports and manufacturing sector conclude that small producers in the manufacturing sector are increasingly being reduced to the level of wage labourers. In the non-traditional export sector, the cases of gherkin growers and cashew nut producers lead to the conclusion that the education of children and the health of workers can be affected. The labour intensive nature of gherkins has at times had a adverse effect on the rate of schooling of children as they are called upon to cultivate. In the cashew nut industry, deterioration in the health of persons involved in cleaning and processing was constantly observed. The stagnation of the income earning capacity is identified as the considerable dependence on middlemen and exporting companies have an adverse impact on the profitability of the enterprise. The greater propensity for men to increase their income is observed as they are involved in marketing of produce, as against the women who are primarily involved in processing.

Ariyabandu and Hidellage (1994) identifies the access to information and other resources (such as education, skill, capital) as being of crucial importance to small producers – both manufacturing and agricultural – ability to survive competition and take advantage of the changed policy and economic environment.

In a detailed case study of small producers who are part of self-employment and social mobilisation programmes, Lakshman *et al.* (1994) conclude that they are characterised by the lack of dynamism, under capitalisation, and use of very low level traditional know-

how. Further they occupy the lowest end of the continuum of small producers. Most have become small producers as an income generating activity of last resort. They view it as a temporary activity until they are absorbed into more remunerative employment in the market.

However, Lakshman *et al.* (1994) point out that due to the very small scale of enterprises and their interaction with the immediate economy only, they are not very sensitive to changes in macro policy relating to industry.

There are a number of other areas which micro level studies provide substantial insight to household welfare changes precipitated by macro policies. Studies of landless small farmers, farming families on irrigation settlement schemes, etc. have been extensively carried out by institutes such as the Agrarian Research Institute (HARTI) and the Mahaweli Authority. These socio-anthropological studies are particularly important as the social context of low income farming communities have an important impact on the sensitivity to policy changes.

Studies that have gained ground more recently are those that look at self destructive and anti-social behaviour patterns of primarily the youth of the country. Studies point to increases in suicides, alcoholism, drug addiction, prostitution, and availability of pornography. Most studies attempt to explore the prevalence of these problems among different age groups, income groups, and regions and possible causes for the trends. At a societal level, these studies have explored political violence, youth unrest and crime as possible violent expressions of economic and political dissatisfaction (See Hettige 1992, 1998).

Section 4: Linking Macro Policy to Poverty and Welfare

As discussed in the introduction to this review, Sri Lanka's continuing concern and debate over the potential social costs and benefits of adjustment, and its use as a 'test case' in the growth versus welfare debate of the 1980s[8] has generated considerable research interest regarding the impact policy reform has had on poverty and social welfare.

[8] See among others Isenman 1980; Sen 1981; Bhalla & Glewwe 1986, 1987; Glewwe 1986; Anand & Kanbur 1991; Osmani 1994.

It is clear from the review of existing literature that channels of transmission between macro policy changes and household level welfare can be identified through two methods:

1. By linking the literature on macro policy reform with literature on welfare and poverty. Here the existing literature supplies the information at the two ends of the issue and indicates the links between them.

2. Using literature which itself attempts to link policy reform and welfare in a cause and effect relationship. Broadly, these are of two types:
   i) those that analyse the impact of policies to the general structure of poverty and welfare at a macro level[9], and
   ii) those that focus on specific groups and sectors at a more disaggregated level[10].

While the former takes policy changes as the point of entry to the analysis, the latter frequently starts with the group affected. However, few studies rigorously attempt to identify channels of transmission. Exceptions are Shan (1988), Edirisinghe (1987) and Gulde (1991) which use an econometric and statistical base specifically to identify channels of transmission through which price changes impact primarily on food consumption and nutrition. Gutkin (1988) attempts to establish links by modeling the impact of different macro policies on specific aspects of household welfare. However, the majority of the links drawn in this section between macro policies and welfare impacts are based on literature reviewed in the previous section which looks primarily at one aspect or draws broad links between the two.

However, prior to attempting to identify cause and effect links between macro adjustment and household welfare, problems inherent to the process must be understood. The review of literature and initial attempts at isolating impacts brings out strongly the constraints in establishing causal relationships within an acceptable level of clarity and reliability. Killick's (1995) study on structural adjustment and poverty alleviation has a comprehensive discussion on the issue of obscurities being too large to permit simple

[9] See among others Kurukulasuriya 1984; Lakshman 1986,1994, 1996; Shan 1987; Alailima 1988; Indraratne 1992; World Bank 1992; Jayasuriya 1995.

[10] See among others Athokorale 1986; Gunasinghe 1986; ILO 1986; Osmani 1987; Rodrigo 1994; Dunham and Edwards 1997.

generalisations of links between macro policy and poverty.[11] He highlights the difficulty of disentangling the effects of policy from the effects of other exogenous factors, and the difficulty of isolating the effect of a single adjustment policy on a household when structural adjustment programmes are designed and implemented as a package of interrelated policies. Further, the effect of badly designed and implemented policies and the timing and sequencing of policy reform can distort the impact on welfare and poverty in a way that makes identification of links more or less futile.

In attempting to identify the channels of transmission between macro policy and micro impact, this section will approach it from the macro policy end. The process by which some selected policies impact welfare at the micro level is explored. These are policies which appear most frequently in the literature as those that have a direct or indirect impact on the living standards of the lower income segments of the population. Notwithstanding the above discussion on constraints to identifying isolated links, the policies have been considered separately to enable ease of analysis. However, an effort has been made to identify other connecting policies.

4.1 Devaluation

Based on literature on monetary policy and welfare, and literature that deals specifically with price changes it can be concluded that the impact of devaluation is translated into welfare impacts by both direct and indirect channels.

Considering the direct channels, low income groups are affected both in their role as consumers as well as producers. Low income consumers are adversely affected through the increase in prices i.e. drop in real wages. Low income producers are affected positively through change in prices of export products and negatively through imported raw material and tools.

In the case of price changes caused by devaluation, the change in the prices of basic commodities such as rice, wheat, sugar have an impact on the consumption and nutrition levels of all types of low income groups. Shan (1988) concludes that due to the low price elasticity of rice and its high share in the budget of a low income household, changes in the price of rice cause reductions in the consumption of all other commodities. In the case of price changes of other imported goods, the impact differs based on the

[11] See also Goldstein and Monteil 1986; White and Luttik 1994.

consumption patterns of the household. The impact on urban consumers is greater than the impact on rural and estate consumers due to the significance of imported goods in their consumption patterns (Lakshman, 1994).

The impact of inflation caused by devaluation on different groups depended on the movement of the real wage rate. Considering sector wise, the greater sensitivity of the unorganised sector wages to inflation caused by devaluation has meant that it has not acted strongly as a source of deteriorating welfare. The changes in real wages caused by devaluation were felt far more strongly by the fixed wage receivers (see Sandaratne 1985; Rodrigo 1994).

Linking in with other adjustment policies, the devaluation effect on consumption and nutrition was aggravated by the policies which caused the removal of control prices and the virtual abolition of food and kerosene subsidies (Lakshman 1994).

Considering low income producers, the impact of devaluation can be transmitted to household welfare through the earning capacity of low income producers. Gulde's (1991)[12] analysis of the short term net effects of structural adjustment on poor sections of the population brings out the cushioning impact devaluation has had on small holders of export crops. Small holders, primarily in the export crops of rubber and coconut, were shielded from the adverse effects of falling world prices due to the devaluation of the Rupee. Devaluation prevented the full pass-through of the international price decline in rubber and coconut. Gulde (1991) also hypothesises that these groups engaged in the tradable goods sector will benefit in the medium and long term from the relative price changes originating from the devaluation.

A primary reason for devaluation was to create economic growth. Hence, low income groups will be indirectly affected through the change in employment opportunities and the structure of the labour market as the economy grows. This rationale is the base for the 'trickle down' argument.

[12] Gulde (1991) makes a rigorous analysis of how the structural adjustment programme of 1989 affected the poorer segments of the society in the short term. The income impact and expenditure impact is used critically to arrive at conclusions regarding the net impact of adjustment.

4.2 Foreign Investment and Export Promotion

The lack of linkages between export oriented ventures and the local economy has been extensively discussed in the literature. The impact of foreign investment and export promotion was transmitted to the lower income groups primarily through the generation of employment and to a lesser extent through the expansion of other satellite income generating opportunities.

Rodrigo (1994) identifies export and foreign investment oriented policies along with trade liberalisation as being the key causes of increasing employment in the manufacturing sector. However, there seems to be considerable concern in the literature about the quality of the employment provided. The working conditions and living environment of urban export factory workers have been identified as being of a particularly low standard.

The distributional impact of this policy can also be traced. During the first phase of policy reform, promotion of the export sector was concentrated in the trade zones which were mostly in the Western Province. Employment created by these zones created a definite urban bias along with a bias towards low skilled female labour. In response, the 200 garment factory scheme sought specifically to combine the export promotion policy with income distribution by locating in the more rural areas.

Aside from the impact through the manufacturing sector, export promotion has had an impact on low income groups through the expansion of the non-traditional agricultural exports. In the agricultural sector greater linkages with the local economy have caused the growth of small commercial farmers. Increased income has been the positive outcome, though lack of income security exists.

If the employment opportunities created through foreign investment and export promotion policies were compared with the loss of opportunities due to the contraction of state enterprises, it can be seen that a change in the structure of employment opportunities was created. Low or semi skilled labour, and in the case of the textile and garment sector predominantly young female labour, was in demand for the new employment opportunities created. This is fundamentally different to the labour that would have been absorbed into state enterprises. The worst affected were young educated rural labour that

would have been absorbed into white-collar jobs by the state sector but now form a crucial segment of the unemployed.

4.3 Trade Liberalisation

Most literature which considers the impact of reform on the poor, dwells to some extent on the impact of trade liberalisation.

The impact of trade liberalisation moves through a number of channels. The product market acts as a channel through which household consumption is affected. Theoretically, household consumption is directly affected as a positive impact filters through decreased prices of goods due to increased availability. However, the impact of devaluation on the prices of imported goods frequently means that in fact the prices of goods increase. The net impact would differ depending on the particular good under consideration, and the basket of goods consumed by the household.

The impact of trade liberalisation is transmitted not just through product market channels but also through indirect impacts on the market structure. Alailima (1984) identifies the impact of trade liberalisation on the health status of the lower income groups through the affect on the availability and costs of medical drugs. Liberalisation of imports in 1977 terminated the State Pharmaceutical Corporation's monopoly to import drugs. While this increased the availability of drugs it also pushed up the prices. With the expansion of the private sector, and the decreases in the budgetary allocations for recurrent expenses, the private sector soon became the main importer of medical drugs. Lack of control within the system created a trend among medical practitioners to prescribe higher price drugs which were promoted by pharmaceutical trading companies.

The main channel through which trade liberalisation affected household welfare was through changes in employment opportunities. Though the net impact was an increase in employment opportunities, as discussed in the previous section, the disaggregated impact on employment has been twofold. Both positive and negative changes occurred. Whether a household gained or lost through trade liberalisation depended on the features of the labour available within the household and the access to employment opportunities.

On the negative side, employment opportunities and sources of income contracted as trade reforms contributed directly to the removal of protection for 'infant' and other

'strategic' industries. As part of the policy of non-intervention with the market state support in marketing, raw material procurement, subsidies on inputs, and preferential access to public resources were withdrawn. The most documented has been the experience of the handloom industry (Osmani 1987; Waidyanatha 1980). Other areas identified as having suffered due to liberalisation were pottery, agro-based industries such as treacle, crude sugar, and minor food crops (Jayaweera *et al.* 1988a). Those employed in these sectors were predominantly from the low income groups. However, a contrary view is put forward by Lakshman *et al.*' s (1994) study on very small scale producers. Here it is observed that increased competition caused by trade liberalisation has not affected these producers as their market is very localised and products border on Giffen goods.

The positive impact has occurred through a number of channels. Rodrigo (1994) identifies trade reform along with export promotion as the main source of employment generation in the manufacturing sector. She further highlights the positive impact on employment which has occurred through the expansion and better capacity utilisation of industries due to greater availability of raw materials, equipment, etc. Significantly, this positive impact has also been observed by Lakshman *et al.*' s (1994) micro level study of the very small-scale producers.

Another sector identified by literature as rapidly expanding due to trade liberalisation is the retail and wholesale trade sector. The employment opportunities generated in large numbers in the small private sector enterprises of this sector had the greatest impact on low income groups. However, the contribution of these sectors are frequently not reflected in the official statistics (Sanadarante 1984; Rodrigo 1994).

Liberalisation of domestic trade and the corresponding removal of administered price for agricultural products link to the welfare levels of small farmers. Dunham and Edwards (1997) argue that expected increases in earning capacity of rice farmers due to higher paddy prices do not always accrue to small holders. The capacity to benefit from price changes is linked to the structure of production. Small farming households are net consumers in the market – they consume most of their production at home. Consequently, their earning will not be affected significantly by increased rice prices. This is the position in the short term. Whether the higher prices will change the behaviuor of small farmers in the future is an area that needs exploration.

4.4 Fiscal Contraction

The high sensitivity of the wellbeing of lower income groups in Sri Lanka to changes in fiscal policy is widely acknowledged (see Edirisinghe 1987,1988; Shan 1987, 1988; Cornia *et al.* 1987; Alailima 1997). This relationship can be traced to the dependence of the lower income groups in Sri Lanka on public services to maintain their standards of living. Changes in budgetary allocations translate to changes in household standards of living which is maintained through subsidised food, health, education, transport, etc.

The greatest and most direct impact has been through the change in the food subsidy programme. Much of the literature surveyed maintain that Sri Lanka's policy on subsidising food has been the major cause of better nutrition and greater equality (Sen 1981; Edirisinghe 1987, 1988; Shan 1987; Basu 1988). The removal and reduction of subsidies and the phasing off of administered prices has had a direct and adverse impact on the consumption levels of the poor households. A primary cause has been the structure of the food stamp scheme which combined with rapid inflation to create a sharp deterioration in the real value of the food stamps (see Edirisinghe 1987; Shan 1988; Gulde 1991).

Considering the groups most affected by the reduction in public spending on food subsidies, Shan (1988) concludes that strongest impact is felt by urban and landless labour. This is backed up by Gulde's (1991) analysis of the relationship between price changes and the welfare of the poor. She estimates the adjustment induced changes of real spending power disaggregated by employment type[13] and concludes that while the changes have a negative impact on all three disaggregated groups, the urban informal sector is worst affected and the small-holders least. However, Gulde's estimations hold that some of the negative impact will be mitigated by positive effects on income.

Looking at intra-household impact, Edirisinghe (1987) maintains that nutritional distribution between economically productive adults and dependents will depend on the intra-household food allocation practices. More equitable distribution occurs between the two groups when about 80 per cent of the calorie requirement of the economically active members are met.

[13] Urban informal sector, rural landless labourers and smallholders.

The literature also explores coping strategies employed by the low income groups in the face of deteriorating welfare due to reduction in public spending on food subsidies. Gulde (1991) and Shan (1988) show the importance of consumption and expenditure patterns of the poor in their ability to cope with the deteriorating real values of food stamps and wages. Their levels of consumption are most sensitive to price changes in staple food (rice) due to the low price elasticity of rice and its large budget share.[14] The price of rice has a major impact on the consumption of other commodities even though there are efficient substitutes for most other commodities (Alailima 1984; Shan 1988; Gulde 1991).

The extent to which the falling values of the food stamps affected a given group also depended on their capacity to generate an income by taking advantage of the new economic opportunities. Literature identifies the fixed income earners in the organised sector as a group adversely affected by the subsidy withdrawal and price de-regulation components of policy reform (Sandaratne 1987; Rodrigo 1994). A compensatory factor created by the policy changes has been the increase in employment opportunities. This has meant that households which find their real income falling has increased the number of earners as a coping strategy (Rodrigo 1994).

Yet another channel by which reductions in public expenditure affects welfare is through the change in public services. Though public spending in education and health has not decreased, its composition has changed. A shift in emphasis from recurrent to capital expenditure has translated into deterioration in the quality of the service, especially at the primary level. The quality of service has also deteriorated due to the low morale of the staff caused by differential wages in the private sector and public sector as the private sector expanded and the real value of public wages failed to keep up (Cornia *et al.* 1987).

The impact of changes in fertilizer subsidies is another area covered quite frequently in the literature. Small holder farmers are the most important group in the 'self-employed' category of the poor. Theoretically, the removal of fertilizer subsidies and administered prices of other inputs would have a negative impact on their earning capacity. However, as Gulde (1991) points out, the actual impact would depend on the usage of fertilizer by this group. World Bank (1988) casts considerable doubt as to the use of fertilizer by the

[14] Share of food in the budget of a household in the lower income decile: Urban 63 %, Rural 69%, Estate 76% all Island 70%. Of this the greater percentage is spent on rice (Gulde 1991, 5).

poorer small holder farmers. If this is so, the actual negative impact would be smaller than the potential impact due to bad implementation of past policy.

4.5 Public Sector Reform and Private Sector Expansion

Structural adjustment of the economy by reforming the public sector and increasing private sector participation was undertaken in an effort to create economic growth through reduction in the financial burden of the government, improved industrial growth through more efficient use of the assets and factors of production, and by accruing efficiency gains to the economy from enhanced competition (Kelegama 1994). According to the conventional rationale, economic growth thus created translates into increased welfare of the lower income groups through increased employment opportunities, a more rational state, etc.

Kelegama (1994) identifies two channels through which impacts have been transmitted to the lower income groups more directly in the short term: through the loss of socially desirable services and through the immediate impact on employment.

Hence, as emphasised by Kelegama (1994), the issue of short term and long term impact is particularly relevant in exploring the effect of these policy reforms on the welfare of lower income groups.

The primary role of state owned enterprises (SOEs) was to shield the public from the adverse impacts of the market forces and provide them with goods and services at reasonable, and frequently subsidised, prices (Kelegama 1994). The primary beneficiaries of this system were expected to be those most vulnerable to the market forces: the poor segments of the population. With the contraction of the SOEs and the spread of the private sector this orientation has undergone a change. This, naturally, has been a primary channel of impact.

Considering the potential impact of privatisation of SOEs, Kelegama (1994, 1997) stresses the importance of the conditions of divestiture in enabling a beneficial outcome to be transmitted to employees and service receivers. The policy framework and structure of the privatisation agreement affects the distribution of benefits between labour and profit and the impact on service receivers. In the case of labour, the compensation package for those retrenched, the conditions of employment for those retained and in the

case of the service receivers, the minimum levels of service provision are affected by the conditions of divestiture.

Transport has been widely identified in the literature (Jayaweera 1988; Knight 1993; Kelegama 1994, 1997) as a socially desirable service which has been adversely affected by the private sector participation and subsequent divestiture of the state transport system. Rather than improving, the service has deteriorated due to increase in bus fares and the disruption of services to socially desirable but financially non-viable routes. Loss of affordable and accessible transport translates into lower standards of living of low income groups through weakened access to education, health, employment, markets, etc. Transport is a vital link to low income groups benefiting from state services as well as taking advantage of economic opportunities arising from adjustment induced growth. The worst affected are the low income groups in outlying areas and school children.

Considering the direct impact on delivery of health and education, in addition to the fiscal contraction impact, the increase of private sector participation has had a qualitative impact on the services provided. As the private sector expands, the higher income earners are moving out of the state sector provision and into the higher priced private supplier segment such as international schools, foreign or private universities, and private hospitals. A segmented market is developing with the state offering services at a different standard of efficiency and quality to the lower income groups. This impact has been felt strongly in the health and education services and has translated into an equity issue. It can be expected that these changes will have serious consequences for basic standards of living of the future generations (see Alailima 1985, Cornia *et al.* 1987; Jayaweera *et al.* 1988a; Rodrigo 1994).

However, on the positive side, Alailima (1985) identifies how liberalisation of medical practice has translated into greater access to doctors by the more marginalised communities. Lucrative private practice in the suburban and regional areas lured doctors to peripheral units and district hospitals in remote and previously unattractive areas.

In terms of employment, a direct short run impact has been through redundancies in the divesting SOEs. However, in the long run the private sector expansion in manufacturing sector is likely to fill the employment gap. Yet, the change in the employment structure created a crucial mechanism by which differential impact is transmitted to households. The contraction of the state sector has created a contraction of opportunities for educated

rural youth aspiring for service jobs. The private sector jobs created were either urban based low or semi-skilled jobs, as in the case of manufacturing and passenger transport, or more lucrative white-collar jobs which recruited primary from the urban middle-class background (Rodrigo 1994; Dunham 1997). This change in employment opportunities has a particular relevance given that the most severe unemployment problem remains with the rural educated youth.

Labour welfare is yet another channel through which household welfare is affected. Rodrigo (1994) observes that the contracting share of the public sector with its established norms of job security, employee welfare, etc. and the expansion of the less formalised private sector cannot be without repercussions to labour. The situation of labour was further aggravated by the fact that the transition was taking place at a time when the trade union movement was rather weak in its bargaining power (Rodrigo 1994; Devendra 1996). In contrast, successful negotiations by the politically powerful trade union has been the main reason for the significant improvements in minimum wages and benefits of the estate sector (Ratnayake 1998).

An indirect source of impoverishment of retrenched public sector workers has been their lack of ability to invest compensation fruitfully. Compensation was overwhelmingly (over 80 per cent) used to pay off debts. Few who invested did so in bank deposits which were low risk and low returns. The policy framework made no provision for the state or the private sector to provide investment advice (Kelegama 1994). Though SOE employees do not fall into the lowest income group, many lower level workers slid down the scales following redundancy.

Rodrigo (1994) also points to the need to investigate whether the impact of intensified competition under restructuring was leading to a decrease of labour intensive small scale production units. If, as the evidence seems to suggest, liberalisation strategy was more favourable to the expansion of bigger units, and the growth of labour intensive industries are slow, the retrenched labour will join the ranks of the unemployed (Kelegama 1994; Rodrigo 1994).

4.6 Liberalisation of Travel and Overseas Employment

The impact of liberalisation of overseas travel and employment is analyzed predominantly in the gender orientated literature, and is available in a cross section of

macro level and household level studies (CENWOR 1987, 1995; Jayaweera *et al.* 1988a; Jayathileke 1998; Jayasundera 1998).

This trend in literature is due to the fact that the low-skilled female labour form the majority of migrants. Considering the profile of migrant workers in order to identify the sub groups which are affected, a typical migrant worker is from the low income sector whether from the rural or urban sector, and has had less than 8 years of schooling, is low skilled, is between the age of 18 and 40, and is married with children. There does not seem to be a regional concentration regarding the origin of these workers (CENWOR 1995). Through this information, it can be concluded that the most affected are low income young families.

Reviewing the existing literature, two channels through which household welfare is affected can be identified. The first is through income generated through overseas employment, and the second is through the social and psychological impact on the family and social structure.

In terms of the impact on welfare through income generation, at a national level there has doubtless been a positive impact on national savings and foreign remittances. However, at the household level the impact is less clear. A major issue is the sustainability and usage of income generated. Over 80 per cent of the households use the income generated for consumption expenditure. The high level of consumption spending is a reflection of the low income status of most households. Though the standard of living increases, at times quite dramatically, due to migrant remittances, the tendency to fall back into lower levels following the return of the migrant worker is very prevalent (Jayasundera 1998). A repercussion has been repeated migration by women in an attempt to maintain the standard of living.

The sustainability of income generation occurring through migration would be facilitated through productive investment of income. From the studies available it can be concluded that most capital investments have been in the form of housing, land, bank savings, and business ventures. Of these, it is only business ventures that have some propensity to provide a sustainable income. In this regard Jayatilaka (1998) identifies the crucial role of the husband in investing wisely and maintaining an income generating source.

The social and psychological impact through migration on the workers, their families and society in general has been frequently identified in the literature. Most information is found in the micro level socio-anthropological studies (see Samarasinghe 1989; Jayatilaka 1998; CENWOR [various]). Regarding the migrant workers themselves, issues of emotional stress, victimisation, low working conditions are identified as adverse impacts. In relation to the families, tensions created between spouses and children are a prime contributor. UNICEF (1985) concludes that inadequate child and adolescent care has resulted in insecurity leading to disruption of education, drug addiction, begging and prostitution. However, Jayatilaka (1998) also identifies positive effects such as increased confidence, assertiveness in decision making, and social independence among women.

There seem to be a consensus in the literature that policy intervention can quite dramatically increase the positive impact on welfare occurring through migration (see Jayasundera 1998; Weerakoon 1998). The policy incentives for migrant labour has been a neglected area. Once restriction on travel and overseas employment was lifted the operation of market forces created the outflow of labour, with little other policy intervention.

A much less studied impact of liberalisation of travel and employment has been its impact on the quality of health provision. The combined effect of liberalisation of travel, the removal of compulsory minimum service requirements, and the ability to command much higher remuneration overseas has created an exodus of doctors and other medical support staff (laboratory technicians, radiographers, nurses, midwives, etc.). A major shortfall in cadre requirements has been a result (Alailima 1984; Cornia *et al.* 1987).

Section 5: Conclusion

As expressed in the introduction to this literature review, given the vast area of interest and the equally extensive literature, this review cannot be viewed as exhaustive. Nevertheless, it serves to give an idea of the existing literature and it is possible to arrive at some conclusions regarding the extent to which existing literature can form a knowledge base for subsequent research relating to linking macroeconomic policy to household welfare. The review also helps to identify gaps in knowledge that need to be addressed.

The literature on macroeconomic reform, and structural adjustment and stabilisation programmes is extensive, though there is considerable concentration of literature on the first phase of reform, and a definite scarcity of literature on the post 1994 period. The majority of the literature follows a descriptive analytical style from a fundamentally economic base. The political economy of policy reform and implantation is rather neglected, except to some degree in the literature that looks at the second phase of adjustment. When exploring the impact of macro policies on welfare, the implementation of policy is as crucial as the policy itself. This crucial area is quite neglected by the existing literature.

When considering the literature on the welfare impact, a considerable verity and differentiation regarding the orientation of the studies could be seen. At the macro level, though there are unresolved issues regarding conceptualisation and methodology, trends in poverty and welfare are extensively researched and critiqued. Nevertheless, relative poverty and different perceptions of poverty are areas that can benefit from further study.

As the review moved on to disaggregated characteristics of the poor, a few more problems arose. Though here too there is extensive literature, including studies which look at the characteristics of low income groups based on disaggregated data of specific survey years, issues with the available data constrain the usefulness of the literature. While data on gender, age, agro-climatic and socio-economic sectors, occupational categories, etc. are available the small size of some categories can create distorting trends. A further problem exists with the indicators used. Most indicators are too aggregated to be sufficiently sensitive to meso and micro level changes, especially if they start from a high base, as many do. However, the existing literature does succeed to a great extent in building a profile of the poor, based on the available criteria of disaggregation.

The literature which considers the welfare at a micro level form a very important strand of literature, which goes a long way towards giving depth to the profile of the poor. These studies provide insightful information regarding household level welfare using qualitative as well as quantitative indicators which consider non-economic aspects of welfare as well. However, the main weakness arises from the fragmented nature of the studies and the limited coverage in terms of geographic dispersion.

When considering the extent to which the existing literature facilitate the identification of channels of transmission between macro policy changes and welfare at the household level, it can be concluded that the existing literature does provide - albeit with numerous limitations - an initial base of knowledge. A few studies attempt specifically to identify a causal relationship between policy and impact using a rigorous methodology. The impacts of price policy on nutrition and consumption patterns appear to be the most extensively studied. However, the majority of the studies draw links from, at best a theoretical, and at worst, a speculative base. Nevertheless, based on this literature, basic transmission channels that can be identified are government expenditure, factor market (mainly through employment) and the product or commodity market (mainly due to food).

As a body of literature, the main problem that exists is that it is fragmented, and does not fit into a general structure which could help develop links between macro policy and micro level welfare. The literature seems to build upon its strengths and little attempt has been made to venture into unresearched areas. The existence of a strong literature base regarding macro policy change has meant that most studies - with the exception of micro level empirical studies - commence the analysis from the policy level. Similarly, the existence of published data of acceptable quality has meant that many studies restrict themselves to levels of disaggregation facilitated by this data.

Considering specific gaps in the literature; there is very little discussion of the impact being a two way process. Rodrigo's (1994) work on employment and wages was an isolated example where specific attention was drawn to the two way influence; structural adjustment has repercussions on the labour market while the labour market plays a crucial role in the success or failure of adjustment policies. Household aspirations have a crucial influence on policy primarily through the electoral process. This is particularly important given the observation by World Bank (1992) that poverty and unemployment have traditionally been key factors in shaping economic policies in Sri Lanka. However, literature on this aspect is almost non-existent, except in limited political-economy literature.

Another gap can be seen in the lack of literature regarding meso and micro level policy. Though the emphasis in this review has been on macro economic policy, it has been observed that macro policy changes do not always impact the poorest segments of the population. For example, the poorest small producers of the type studied by Lakshman

(1994) are unlikely to feel any significant effect directly from macroeconomic policy changes. More relevant to such segments would be the micro policies on credit, training, etc. provided by meso level development policies.

With regard to macro policy, an area that has been discussed only extremely briefly is the impact of the 13th Amendment which devolves state service provision of education and health to provincial councils.

The overall conclusion is that while the existing literature provides a very sound base there are important gaps that need to be filled, mainly in the area of identifying links. Potential areas for research can be considered as two types: work that takes a holistic view and those that consider particular sub areas. When considering the whole picture, attempts to develop a framework which will facilitate the identification of the primary links would be helpful as a point of reference for other work. As mentioned often, identifying channels of transmission covers a vast area. Hence, holistic conceptualisation becomes important. When considering particular sub areas, two options are open; either further develop areas where some knowledge already exists, or venture out into areas which have been neglected. Either way, to optimise effort and productivity, it is important that individual studies feed into an overall framework.

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