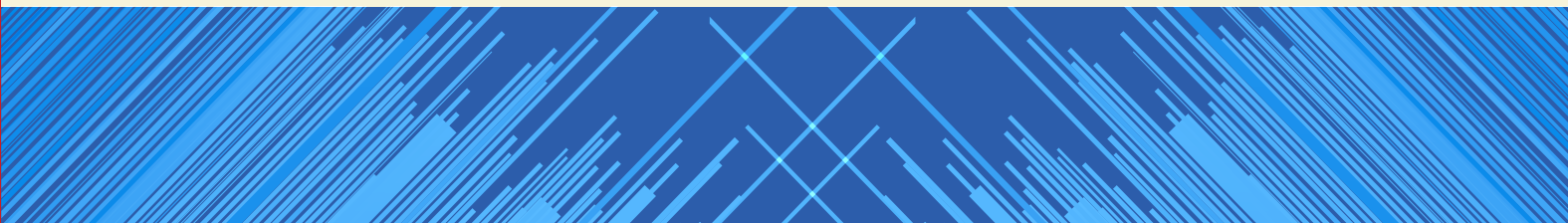




# Southern Voice

2015 On Post-MDG International Development Goals



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**UNPACKING THE MIDDLE**  
*A Class-based Analysis of the Labour Market in Sri Lanka*

*Southern Voice Occasional Paper 22*

*Vagisha Gunasekara*

Publisher

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First Published February 2015

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ISSN 2307-9827 (Online)

ISSN 2307-681X (Print)

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# Preface

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The *Southern Voice on Post-MDG International Development Goals* works as an open platform, and is a network of 48 think tanks from Africa, Latin America and Asia that seeks to contribute to the global post-2015 dialogue. Motivated by the spirit of wide academic inquiry, the initiative is committed to provide quality data, empirical evidence and policy analyses, derived from research in the countries of global South. Through strategic engagements, *Southern Voice* aspires to address the existing ‘knowledge asymmetry’ and ‘participation deficit’ afflicting the global discourse on post-2015 agenda.

With these goals in mind, *Southern Voice* launched a call for papers among its members to inform the global debate based on promoting original research on new issues that have emerged from various reports, structured conversations concerning the post-2015 agenda as well as from the discussions around them and beyond. Eleven research grants were offered during this phase.

In response to the call, we received numerous proposals which were reviewed by *Southern Voice* members. The research papers were also peer reviewed, and the revised drafts were later validated by the reviewer.

The resulting collection of papers highlights some of the most pressing concerns for the countries of the global South. In doing so, they explore a variety of topics including social, governance, economic and environmental concerns. Each paper demonstrates the challenges of building an international agenda which responds to the specificities of each country, while also being internationally relevant. It is by acknowledging and analysing these challenges that the research from the global South supports the objective of a meaningful post-2015 agenda.

In connection with the ongoing debates on post-2015 international development goals, **Unpacking the Middle: A Class-based Analysis of the Labour Market in Sri Lanka** by *Dr Vagisha Gunasekara*, a Senior Researcher at the Centre for Poverty Analysis (CEPA) in Sri Lanka explores the constraints to sustainable, inclusive growth with particular attention to the constraints that make it difficult for the poor and other excluded groups to engage in full, productive and decent employment in middle-income countries.

Contributions of *Ms Andrea Ordóñez*, Research Coordinator of the initiative and *Ms Mahenaw Ummul Wara* (Research Associate, Centre for Policy Dialogue (CPD) and Focal Point at the Southern Voice Secretariat) in managing and organising the smooth implementation of the research programme are gratefully acknowledged.

I would also like to thank *Mr Towfiqul Islam Khan*, Research Fellow, CPD, Dhaka for peer reviewing, and *Mr Michael Olender* for copy editing the paper. I would like to take this opportunity to recognise the support of Think Tank Initiative (TTI) towards *Southern Voice*, particularly that of *Dr Peter Taylor*, Programme Leader, TTI.

I hope the engaged readership will find the paper stimulating.

Dhaka, Bangladesh  
February 2015

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# Abstract

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The present study looks at the links between economic class and different labour market variables related to economic participation and employment in Sri Lanka. The findings indicate that: the extreme poor are significantly marginalised from labour markets; educational attainment is positively related to economic class; young people, particularly young females, face considerable obstacles to accessing employment; vulnerable employment is closely linked to low income; gender disparities in labour force participation and job quality are prevalent among all economic classes; and the currently accepted definition of vulnerable employment is insufficient to capture workers engaged in precarious work in both the formal and informal sectors. The policy recommendation that stems from this study is that policies that aim at achieving full, productive and decent employment must be central to poverty eradication measures in the post-2015 agenda.

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# Acronyms

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GDP	Gross Domestic Product
GNI	Gross National Income
HIES	Household Income and Expenditure Survey (Sri Lanka)
LICs	Low-Income Countries
MDG	Millennium Development Goal
MICs	Middle-Income Countries
US	United States
USD	United States Dollar

# Unpacking the Middle

## *A Class-based Analysis of the Labour Market in Sri Lanka*

Vagisha Gunasekara

### 1. Introduction

It is well known that the United States (US) Department of State, at the height of the Cold War, deployed the nation's brightest minds on propaganda missions to function as "good-will ambassadors" who market the American middle-class lifestyle – better known as the "American dream" – to people around the world. Several decades later, the world is characterised by the surge of consumerism, particularly during the last decade, which saw an increase in average incomes and a fall in levels of absolute poverty. The trends of the last decade indicate that an increasing proportion of the world's population is neither rich nor poor – a "global middle class" that is projected to include 3.2 billion people in 2020 and 4.9 billion in 2030 (Pezzini, 2012). Many middle-income countries (MICs)<sup>1</sup> are now home to this dramatically expanding "global middle," defined by expenditures of between USD 2 and USD 10 per capita per day (Sumner, 2012, 1). Estimates from 2012 indicate that more than one billion people living on between USD 2 and USD 4 per day *and* another billion living on between USD 4 and 10 per day, termed the "buoyant billions," reside in MICs (ibid). This is viewed as good news to many, particularly those who believe in the marvels of unlocking the spending power of the global middle class. Some argue that MICs like India and China have reached a tipping point where large numbers of people will enter the middle class and drive consumption (Kharas and Gertz, 2010). Other optimistic accounts suggest that being part of the middle class is associated with better access to jobs and regular wages and greater investment in health and education (Banerjee and Duflo, 2008).

However, there exists another different reality of this global middle class. MICs, the homes to these "buoyant billions" are also currently homes to two billion other people – 80 per cent of the world's poor who live on under USD 2 per day (World Bank, 2013). Two-thirds of the world's population who live on under USD 1.25 per day live in MICs. Although above the global poverty line (and even national poverty lines), many of the people who are classified as part of the new middle class may in fact hover just above the poverty line and remain vulnerable to poverty. Moreover, a significant proportion of this "middle" may engage in informal, precarious work that exacerbates multiple vulnerabilities. As such, many in the middle may face realities that are similar to those of their poor counterparts. It is too soon to celebrate the growth of this middle as the motor of growth and domestic demand. The fleeting gains made on one score, poverty reduction, often get lost on account of unabated or worsened unemployment and inequalities that token policies often fail to address in meaningful ways.

A lot has been written about the benefits of the middle class (Loyaza *et al.*, 2012; Kharas, 2010; Easterly, 2001; Chun, 2010; Birdsall, 2010; African Development Bank, 2011; Amoranto *et al.*, 2010). Many scholars have focused on estimates of the size of middle classes in various countries and others have examined trends in working poverty. Less is known about the specific job-related features of different economic classes and the extent that labour markets are inclusive of poor and near-poor

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<sup>1</sup>MICs are defined by the World Bank as countries whose gross national income (GNI) per capita in the 2014-2015 fiscal year lay in the range of USD 1,045 to USD 12,746. Lower middle-income and upper middle-income countries are separated at USD 4,125 GNI per capita (World Bank, 2014).



workers vis-à-vis middle-class workers (International Labour Organization, 2011; Kapsos, 2004). It is generally understood that ensuring adequate and secure livelihoods for each individual and inclusivity in the labour market is an important prerequisite for social mobility and the emergence of a stable middle class. However, country-level studies examining employment of workers from various economic classes are few. This paper presents new measurements of workers by economic class and their distinguishing employment characteristics in Sri Lanka, a brand-new entrant to the MIC category. Employing a class-based framework<sup>2</sup> to examine labour market characteristics in a new MIC will shed light on sustainable employment challenges that must be addressed in order to eradicate poverty, foster growth of the middle classes and promote inclusive labour markets.

## **2. Approach and Methodology**

The objective of this study is to understand the constraints to sustainable, inclusive growth with particular attention to the constraints that make it difficult for the poor and other excluded groups to engage in full, productive and decent employment. This paper takes a closer look at the links between economic class and different labour market variables related to economic participation and employment in Sri Lanka. It highlights the features that distinguish the poor from the middle class in terms of education, access to better quality jobs, working conditions and opportunities for young people.

This study examines workers based on their economic class. As such, it adopts the past practice of defining the working poor: a cross-tabulation of employment status and economic class status are presented as the estimates of employment by economic class. Employment status is defined at the individual level (whether or not an individual is employed), and economic class is determined by per capita household consumption of the household in which the individual lives. Total employment in a given class is equal to the number of individuals of working age who are employed and living in a household with per capita consumption or income between the upper and lower bounds of per capita consumption for a particular economic class.

The methodology adopted for this paper requires primary household-level data on Sri Lanka. The primary data source used in this paper is the Sri Lanka Household Income and Expenditure Survey (HIES) for 2009/10. This survey was conducted by the Department of Census and Statistics of Sri Lanka. The survey is cross-sectional in nature and adopts a two-stage stratified sampling frame (Department of Census and Statistics 2009/10). The HIES includes information on income and expenditure as well as the demographic and other socio-economic characteristics of household members. The 2009/10 survey covers 25,000 housing units. It is important to note that the analysis of economic class and employment as presented in this paper is primarily descriptive and does not examine longitudinal trends or assess causality. Therefore, inferences about whether higher economic class leads to better access to wage employment, or conversely if holding a salaried job leads to higher economic class status, are not attempted. In addition to academic and policy literature, supplementary data sources, such as desk reviews of surveys, evaluation studies and grey literature covering a wide range of low-income countries (LICs) and MICs, are utilised in this study.

### **2.1 Defining Economic Class**

There is little consensus in the literature on an absolute definition of economic “class.” This study adopts the economic class definitions established in Kapsos and Bourmpoula (2013) and Huynh and Kapsos (2013), which classify working individuals with incomes below USD 1.25 per day (at purchasing power parity) as the “extreme working poor” (Class 1), those living on between USD 1.25 and USD 2 per day as the “moderate working poor” (Class 2), and those living on between USD 2 and USD 4 per day as “near-poor workers” (Class 3). Given the relatively small cohort of workers with

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<sup>2</sup>The class-based framework utilised in this study is adopted from Kapsos and Bourmpoula (2013) and Huynh and Kapsos (2013).

incomes above USD 13 per day in Sri Lanka, the two “middle class” categories as stated in Kapsos and Bourmpoula (2013) – comprising of workers living on from USD 4 to USD 13 per day and USD 13 and above – have been combined to form the “developing middle class and above” (Class 4).

Class 1 is consistent with the definition of extreme poverty established by the Millennium Development Goals (MDGs), which was influenced by the work of Chen and Ravallion (2008). Class 2 follows the international measurement of moderate poverty. USD 2 is the upper bound for this class, which is equivalent to the median poverty line among a sample of national poverty lines for developing and transition economies (World Bank, 2009). Class 3 consists of individuals who are not poor but have a high vulnerability to poverty. The upper bound of USD 4 follows the findings of Banerjee and Duflo (2008) and Kapsos and Bourmpoula (2013) related to common demographic, health, education and labour market characteristics of individuals in this class. For a sample of 39 developing countries, Kapsos and Bourmpoula (2013) find that there is a substantially higher share of near-poor workers in wage employment (35.3 per cent) in comparison to the two working-poor classes. They observe that the middle classes have more than 60 per cent of workers in wage employment, in which case the near-poor class stands out as a group that is more likely to be in informal, vulnerable jobs.

Class 4, the “developing middle class and above,” consists of workers with per capita consumption or income of USD 4 and above. Given the 2005 poverty line of the United States, most workers in this class are poor based on developed world standards (Ravallion, 2009) but live above the thresholds of poverty or near poverty of the lower three classes. According to Kapsos and Bourmpoula (2013), workers in this class are an incipient consumer class as they are able to afford non-essential goods and services, including some international consumer goods. They are considered to be more educated than the lower economic classes and likely to have better access to good quality healthcare in comparison to the extreme, moderate and near poor. Workers who are near the upper bound of this class are able to afford a wide range of international consumer goods (ibid, 7).

While acknowledging the limitations posed by confining this study to an analysis of a single country, it should be noted that generalisability of findings is not an intended outcome of the study. However, the possibility that the findings and related policy recommendations produced by this study are transferable at the conceptual level to other developing countries is not ruled out. The class-based framework was employed solely to question the assumptions about MICs and the new middle class in the developing world, and thereby caution policymakers not to dilute the notion of inclusive growth by merely implementing the standard variety of poverty alleviation programmes. Failure to reform the processes that assure continued enrichment of the relatively small upper crust of society, enjoying both direct and indirect support and use of public exchequer as ordained by the logic of market-determined economic processes, will only worsen the social exclusion of billions of people.

### **3. Inclusive Growth, Poverty Reduction and Employment**

The close affinity between the problems of poverty, unemployment and inequalities bedevilling the existence of the poor in developing countries was the focus of an influential group of scholars for many decades. The common view of this group was that the most direct method of raising incomes is to “raise the zero incomes of the unemployed” and reduce inequality in developing countries (Tinbergen, 1979, 36-37; Seers, 1979; Mahalanobis, 1955). Put simply, neither poverty nor unemployment can be reduced if per capita incomes are falling. Increases in per capita income, therefore, are a necessary condition for poverty and unemployment reduction. This does not, however, mean that increases in per capita income are sufficient for poverty reduction or creating employment opportunities, as a rise in per capita incomes may be accompanied by, or even cause, growing unemployment (Seers, 1979, 4). Rapid poverty reduction will take place if economic growth is accompanied by a declining concentration of incomes (ibid). Thus, it is the pattern of development that is most crucial for people who have been economically and socially excluded because growth and accentuation of the existing pattern in tandem leave the majority excluded, which is clear when the direct and indirect costs caused by such exclusion are given proper attention.

### **3.1 The Nature of Growth Matters**

Early development economists were mainly engaged in theorising about models of growth, with the expectation that poverty and inequality may be addressed later. In the late 1990s, the increasingly widespread recognition that the relationship between growth and poverty is complex and determined by the level of and changes in inequality gave rise to the idea of “pro-poor growth.” While an exact definition has not yet been agreed upon, pro-poor growth refers broadly to economic growth that results in poverty reduction. In some ways, this concept is an attempt to move beyond the debate regarding the primacy of growth or equity in analysing development outcomes, an attempt to prove that both are important (Whitfield, 2008).

However, ongoing debates regarding the nature of poverty reduction have given rise to two often competing definitions of pro-poor growth. “Absolute pro-poor growth” is defined simply as growth that reduces poverty (Ravallion and Chen, 2003). The absolute measure looks only at average income among the poor and whether the economic conditions of the poor are improving. Any growth in mean income that benefits the poor falls within this definition. A more demanding measure is “relative pro-poor growth,” which occurs when the incomes of the poor rise faster than those of the well-off, changing the income distribution. In other words, poverty falls more than it would if all incomes grow at the same rate (Kakwani and Pernia, 2000). This definitional debate draws attention to the importance of income and employment effects (termed the growth effects) versus redistribution effects on poverty.

The concept of “inclusive growth” is an attempt to move beyond the debates regarding absolute and relative measures of pro-poor growth, as well as direct and indirect benefits of growth. Inclusive growth focuses both on the pace and pattern of growth. It refers to sustained growth, which is broad-based across sectors and inclusive of the majority of a country’s labour force (Ianchovichina and Lundstorm, 2009). The Commission on Growth and Development (2008) notes that inclusiveness, which encompasses equity, equality of opportunity and protection in market and employment transitions, is an essential component of any successful growth strategy. Inclusive growth evidently involves not just the poverty outcomes of growth, but also the nature of growth that provides equality of opportunity for productive employment.<sup>3</sup> This concept has recently been discussed in Asian policy circles. In policy statements and development plans, China has put forth the concept of “harmonious society” and Thailand that of “sufficient economy,” both of which echo the need to address the discontent about growth not benefitting everyone equally.

Writing about the post-financial crisis global economy, Rodrik (2011) observes that a strong basis for this discontent stems from the reality that there is a large divide between groups that perceive themselves as globally mobile and therefore view their opportunities and remuneration as determined by the global economy (i.e. highly skilled professionals and capitalists) and the vast majority of people who are not globally mobile and whose employment and livelihood opportunities are set by what happens in the domestic economy. Spence (2011) argues that this visible divide is fuelled by the demise of manufacturing and moderately skilled service sectors. Spence’s assertion reflects concerns about polarisation induced by technological change, which in turn reduces the number of jobs in the middle of the wage distribution. Intuitively and practically, this type of structural change widens the gap between workers with high-level skill sets and those who are low-skilled. These realities challenge the notion of inclusive growth as persistent unemployment and underemployment lead to economic and social exclusion and strip the basic citizenship rights of the vast majority of people in developing countries.

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<sup>3</sup>“Shared growth” is often used interchangeably with the term inclusive growth. According to the World Bank, however, the concept of shared growth can be misunderstood as implying a focus on income redistribution schemes and measures to reduce inequality, as opposed to productive employment (Ianchovichina and Lundstorm, 2009). This study follows the logic of the World Bank and refers only to inclusive growth.

### **3.2 Inclusive Growth and the Right to Full, Productive, and Decent Employment**

Work is one of the most defining aspects of a person's life. People participate in and contribute to society through their capacities to work. Having a job is not merely a means to receive a wage and survive – it provides a way to become a part of societal processes. As such, the notion of work is a conscious activity, purposive and fulfilling in that it allows human beings to be *someone*. Unemployment and underemployment have direct economic costs such as the loss of potential output and income, deterioration of labour skills and productivity, lower tax revenues and serious social costs such as poverty, inequality, malnutrition and injustice. According to Sen (1997), unemployment is an injustice since “the unemployed may feel deprived because of the lack of freedom in their lives, and this goes well beyond just the lowness of income.” For these reasons, it is important that governments design and implement policies to achieve full employment of the labour force as a way of ensuring inclusive growth. According to Felipe (2010), full employment refers to zero involuntary unemployment and zero involuntary part-time employment. The latter is particularly important in developing countries, where underemployment is a much more serious problem than open unemployment. As such, the goal of full employment in developing countries must include reducing underemployment in addition to reducing unemployment. Felipe and Hasan (2006) distinguish four types of underemployment: (i) working limited hours; (ii) high-skilled workers being forced to take up low-paying jobs; (iii) overstaffing; and (iv) workers carrying out their work with very little capital. These dimensions indicate that the objective of full employment must be accompanied by efforts to generate productive employment (*ibid*).

While policymakers often show interest in implementing policies that reduce unemployment, there is a general sense of ignorance about the actual places of individuals on the economic and social playing field, their relative and absolute positions, and the levels, growth and sustainability of their well-being and contributions to national-level economic variables, and hence to development (Kabra, 2012, 421). The stark reality in most developing countries is that large segments of their populations are forced to live without consistent or adequate means of income due to exclusion from mainstream market activities. Palliatives such as social protection schemes are not lasting solutions to fulfil the needs, rights and aspirations of people at the lower rungs of society. As such, the objective of policymaking must also be to generate decent employment that provides a living wage, employee benefits, reasonable job security and a sound work environment.

Although hardly any policymaker would protest policies that generate full, productive and decent employment – some would consider them obvious – there is reason to highlight special emphasis on such policies. An assumption made by mainstream proponents of economic growth is that rapid economic growth resulting from open markets and globalisation of market processes in turn creates employment in developing countries. But the realities in many developing countries falsify this assumption. In those countries, there is broad consensus that creating adequate and assured livelihood opportunities for all working-age individuals is one of the most daunting challenges. Contemporary theories of economic growth that stem from the experiences of Western industrialised democracies understand unemployment to be a cyclical issue, not an endemic structural problem as it is understood in developing countries (Kabra, 2012, 420). Thus, these theories do not assign the level of priority to employment as needed in the contexts of developing countries. Rather, employment occupies a secondary place and is regarded as a by-product of economic growth, capital accumulation, technological progress and macroeconomic balance (*ibid*). This is not to disregard the importance of economic growth, but to point out that it will not, by itself, deliver full, productive and decent employment for all.

The above discussion implies that inclusive growth requires a direct link between the macro and micro determinants of economic growth. Micro determinants capture the importance of structural transformation for economic diversification and competition. The extent to which growth can be inclusive depends on the amount of human capital that the poor possess, such as education, skills and good health (Bigsten and Levin, 2000). Hall and Jones (1999) show that per capita income levels



are indirectly determined by the amount of “social infrastructure” in a society. Social infrastructure refers to the institutions and government policies that determine the economic environment within which individuals accumulate skills, and firms accumulate capital and produce output. Drawing on the literature on inclusive growth and full employment, this paper argues that the post-2015 development goals, which strive to reduce inequality, must seriously advocate full employment.

#### **4. Employment in Neoliberalised Sri Lanka**

Given the emphasis of this paper on inclusive growth, it is important to assess the realities on the ground regarding employment in Sri Lanka, specifically in terms of understanding livelihood adequacy and security during the period of full-scale adoption of the neoliberal policy package. The structural adjustment process and internal and external liberalisation that began in 1977 in the country was expected to boost growth in labour-intensive sectors – agriculture, industry and services – by removing the barriers stipulated by protectionist policies (Jayasuriya, 2010). This policy package was expected to bring higher economic growth, a higher rate of employment growth and a higher growth rate of the incomes of workers engaged in labour-intensive sectors (Jayasuriya, 2010). Several stylised facts can be observed in examining employment and unemployment trends in the years following the initiation of neoliberal reforms in Sri Lanka.

Sri Lanka’s economic liberalisation paved the way for export-oriented economic growth. Liberalisation also transformed the composition of exports, with agricultural exports declining from 79 per cent of total export in 1977 to 23 per cent in 2008 and manufacturing exports increasing from 14 per cent of total exports in 1977 to 76 per cent in 2008 (Gunatilaka *et al.*, 2010, 3). Despite a civil war that spanned for nearly three decades, Sri Lanka has maintained a healthy rate of economic growth over time, registering an average annual growth rate of 6.53 per cent from 2003 to 2014 and recording an all-time high of 8.6 per cent in the fourth quarter of 2010 (Trading Economics, 2014). This favourable trend has been premised on structural transformation that steered the economy away from agricultural production to value-added service-oriented activities. In 1999, the agricultural sector accounted for 15 per cent of gross domestic product (GDP) and by 2013 its share had declined to 10.8 per cent (Department of Census and Statistics, 2013a). The share of industry has remained more or less stable at approximately 28 per cent, with a slight increase of two percentage points since 2009. The services sector has grown the fastest and contributes most to GDP (currently at 58 per cent) (*ibid*). Changes in the Sri Lankan labour market, however, have not been commensurate with the gains in economic growth.

In 1980, the agricultural sector absorbed 46 per cent of all employed persons, but by 2012, this share had dropped to 30 per cent. The manufacturing sector now accounts for one-fourth of all employed persons, while the services sector accounts for roughly half (Department of Census and Statistics, 2012). Unemployment rates declined to 3.9 per cent for males and 10.2 per cent for females in 2012, but the nature of available employment options remains a matter of concern. Job creation in the formal private sector is relatively low and roughly two-thirds of the Sri Lankan labour force is employed in the informal sector (Department of Census and Statistics, 2006). This is a particularly worrying observation since economic growth in recent years has not managed to create decent jobs for the growing and educated labour force (Gunatilaka, 2008).

Table 1 demonstrates that informal employment plays a significant role in Sri Lanka. Of those employed in the informal sector, 45 per cent were own-account workers, 29 per cent were employees in informal businesses, and 8 per cent worked in formal enterprises where they received wages but were not entitled to social security benefits (see Table 2). Only 6 per cent of employees working in informal businesses had permanent tenure, while the employment arrangement for the remaining workers was temporary and casual in nature. A large number of informal workers did not have a permanent job and 45 per cent of this group were in enterprises with fewer than five workers (*ibid*).

**Table 1: Labour Market Segmentation in Sri Lanka (2006)**

Category	Percentage
<b>Public employment</b>	
As a share of total employment	13.4
As a share of total formal employment	39.8
<b>Private formal employment</b>	
As a share of total employment	20.3
As a share of total formal employment	60.2
<b>Informal employment</b>	
As a share of total employment	66.3

**Source:** Gunatilaka (2008) based on the Sri Lanka Department of Census and Statistics' Quarterly Labour Force Survey Data, 2006.

Both young and older workers are overrepresented in informal sector jobs, as are ethnic Moors in comparison with the reference category, the majority Sinhala population. Educational attainment drives individuals away from informal jobs. Workers with tertiary education are 53 per cent less likely to engage in informal jobs compared to workers with primary or no education (ibid). Manufacturing and services sectors in urban areas are more likely to employ individuals in informal jobs in comparison to the agricultural sector in rural or estate settings (ibid).

**Table 2: Structure of Informal Employment**

Category	Percentage of Total Informal Employment
<b>Informal employment in formal sector</b>	
<b>8.2</b>	
Family worker in formal enterprise	0.7
Employee in informal job in formal enterprise	7.5
<b>Informal employment in informal sector</b>	
<b>91.8</b>	
Own-account worker in informal enterprise or household	44.7
Employer in informal enterprise	3.0
Family worker in informal enterprise	15.0
Employee in informal enterprise or household	29.1

**Source:** Gunatilaka (2008) based on the Sri Lanka Department of Census and Statistics' Quarterly Labour Force Survey Data, 2006.

One explanation for the growth of informal employment is the slow pace of formal job creation in Sri Lanka. A 2005 assessment conducted by the World Bank and the Asian Development Bank noted that Sri Lanka has very low job flows relative to other countries (World Bank and Asian Development Bank, 2005). Moreover, firms at or below 14 workers are less likely to increase employment compared with firms above the threshold (Gunatilaka and Vodopivec, 2010, 63). These observations are largely attributed to Sri Lanka's restrictive labour regulations, particularly the Termination of Employment of Workers Act of 1971, which makes it very difficult for firms to fire or lay off employees (ibid). Interestingly, however, evidence from India questions whether slow job creation in the formal sector is entirely dependent on the nature of labour regulations (Kabra, 2012). In the absence of an equivalent to Sri Lanka's act, India faces similar challenges in the area of job growth in the formal sector. Thus, the changing nature of production (in favour of high-value consumption goods as opposed to mass consumption products) and lack of incentives for the growth of small and medium-sized enterprises (e.g. high unofficial "fees" and charges by public officials when obtaining permits, licenses and registrations, lack of information and knowledge on core business activities and a general lack of a business-friendly environment) may serve as plausible alternative explanations for the negative trends observed in both countries (ibid).

**Table 3: Determinants of Growth and Employment in Four Selected Districts in Sri Lanka**

District	Growth Elasticity of Poverty (Kakwani, 1993)	Growth Incidence Curve (Ravallion and Chen, 2003)	Determinants of Growth and Employment
Gampaha	High (-3.17) – suggestive of inclusive growth	Positive growth in consumption across all consumption percentiles	<ul style="list-style-type: none"> <li>• Educational attainment has contributed to upward mobility in the labour force</li> <li>• The most important sectors in terms of employment and earnings are manufacturing and other services; however, these sectors seem to be trapping the poor in poverty or attracting mainly poor workers for informal and low-return jobs in these sectors</li> <li>• Those employed in the transport, trade and farming sectors have experienced income growth at a higher rate</li> <li>• Access to infrastructure appears to be a key determinant in providing access to employment</li> </ul>
Puttalam	High (-2.3) – suggestive of inclusive growth	Positive growth in consumption across all consumption percentiles	<ul style="list-style-type: none"> <li>• The growth in the share of workers with secondary education seems to have contributed to earnings growth</li> <li>• Greater connectivity and integration of markets appear to be associated with a growth in consumption and employment</li> </ul>
Nuwara Eliya	Low (0.6)	Negative rate of consumption across all percentiles excluding only the highest consumption percentile	<ul style="list-style-type: none"> <li>• Farming is the most important sector in terms of both employment and earnings, but it has experienced the least growth with most households experiencing negative growth in earnings</li> <li>• Although construction, manufacturing and other services offer twice the median earnings, many workers are unable to access jobs in those sectors due to limited educational attainment</li> </ul>
Ratnapura	Low (-0.2)	Negative rate of consumption across all percentiles excluding only the highest consumption percentile	<ul style="list-style-type: none"> <li>• There have been few improvements in educational attainment of the workforce beyond secondary level</li> <li>• More workers engage in farming than before, but household shares of employees in mining, manufacturing and other services have contracted</li> </ul>

**Source:** Centre for Poverty Analysis (2011).

In 2011, Sri Lanka's Centre for Poverty Analysis (2011) conducted a study to assess district-level disparities in economic growth and poverty reduction in an attempt to understand the barriers to sustainable, inclusive growth, particularly for the poor and other excluded groups, and how these groups could contribute to and benefit from growth. Having observed (from the preliminary analysis that included all districts in Sri Lanka) that high rates of economic growth have been neither necessary nor sufficient for poverty reduction in Sri Lanka during the 2002-2007 period, the study carried out further analysis in four selected districts to better understand the nature and determinants of growth. The four districts were selected based on their positions in Kakwani's (1993) growth elasticity of poverty tool and the growth incidence curve (Ravallion and Chen, 2003). A summary of findings is presented in Table 3.

The results of this study show interesting similarities and variances in terms of growth patterns. For example, all four districts appear to indicate the importance of infrastructure growth. Much of the growth in all four districts is associated with improvements in infrastructure, specifically access to telephones. The study also finds that there is a link between growth and education, although the relationship is not the same in all districts. In Gampaha, for example, the proportion of employed persons with Advanced Level qualification and university degrees has increased, which explains as much as 9 per cent of the growth in the district. Neither this level of emphasis on higher education nor such high returns to higher education are seen in any of the other three districts, where either the proportion of employed with Advanced Level qualification or degrees has decreased or an increase has had a negative effect on growth. It could be that Gampaha, situated within close proximity to Colombo, is benefitting from its location. On the one hand, its proximity to Colombo allows its residents to travel to technical and professional works available in the commercial capital, while on the other hand economic activities may be spilling over from Colombo into Gampaha, which has excellent infrastructure. In other districts, higher education appears to be leading to out-migration in search of appropriate employment, which is not available within the district.

In Gampaha, Puttalam and Ratnapura, employment in agriculture is decreasing but returns from agriculture appear to be increasing. These patterns may indicate that the agricultural sector is consolidating and farmers are moving to higher value crops and using technology to increase output. They may also reflect the impacts of global trends such as high food prices, which are creating local demand pressures. While the sectoral changes appear to be benefitting self-employed farmers, including small holders, agricultural employees remain some of the lowest paid across all sectors in the districts. Manufacturing, on the other hand, is a growing sector in some districts, such as Puttalam, but not in others, such as Gampaha.

Overall, households that have reached a certain level of income find it much easier to further increase their income, while the richest households tend to be those that have a first-mover advantage – be it in vegetable farming or salt packaging. There is some social mobility and poor households enjoy a better quality of life than they did 10 years ago, some due to government- and project-funded programmes that improve basic infrastructure. Yet, approximately 10 per cent of the households studied have remained chronically poor, constrained by multiple issues such as lack of education, alcoholism, too many dependents, lack of basic infrastructure, ill health as well as economic structures that allow very low returns for unskilled wage labour. Economic growth in Puttalam during the past 10 years has had little or no impact on poor households, and in some cases has further marginalised them.

#### ***4.1 Employment and Economic Class: Distinguishing Class-based Characteristics of the Labour Market in Sri Lanka***

This section analyses the links between economic class and different labour market variables related to economic participation and employment with the intent of highlighting the features that distinguish the poor from the middle class in terms of education, access to better quality jobs, working conditions and opportunities for young people.

##### *4.1.1 Participation in the Labour Force*

Figure 1 presents the distribution of the working-age population (aged 15 and above) by labour force status<sup>4</sup> for the different economic classes in Sri Lanka. The proportion of the extremely poor who

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<sup>4</sup>Clarification note about definitions adopted in this paper (Department of Census and Statistics 2009/10):

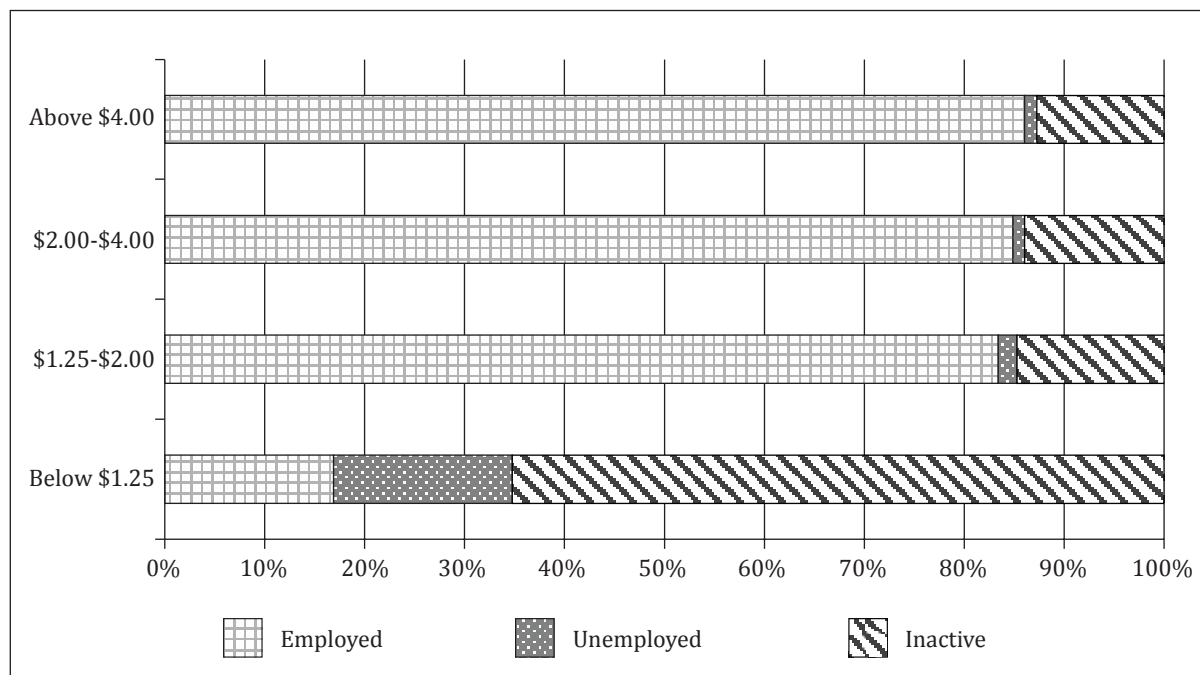
**Employed:** Persons who, during the reference period, worked as paid employees, employers, own-account workers (self-employed) or contributing family workers are said to be employed. Persons with a job but not working during the reference period were included.

**Unemployed:** Persons who are seeking and available for work, but had no employment during the reference period.

**Economically Inactive:** Persons who were neither working nor available/looking for work are classified as “not in the labour force.” Persons are not in the labour force for reasons such as full-time care of the household and being a full-time student, retired or old aged, infirmed or disabled, or uninterested in working for one reason or another.



**Figure 1: Distribution of Employed, Unemployed and Economically Inactive in Total Population Aged 15+ by Economic Class (%)**



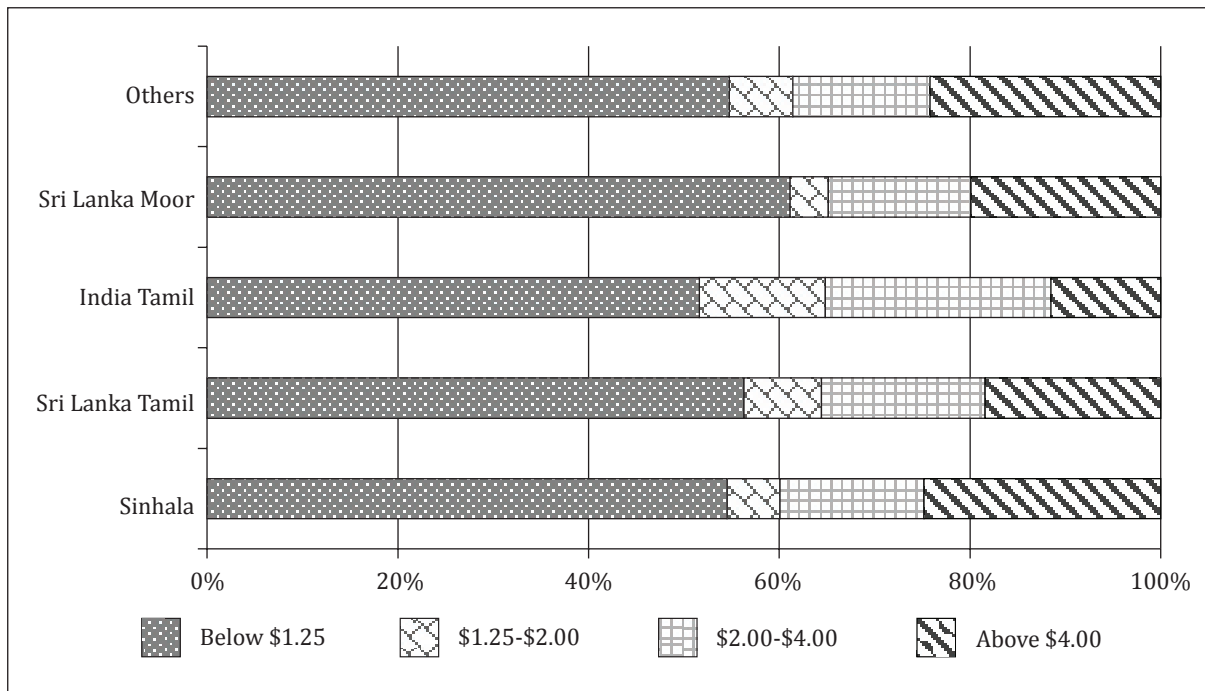
**Source:** Author’s calculations based on Department of Census and Statistics (2009/10).

**Notes:** Since the HIES of 2009/10 offers income figures in rupees, an exchange rate of 113 rupees per US dollar is used for 2010. Then, four economic classes were created using daily income ranges: below USD 1.25, USD 1.25 to USD 2, USD 2 to USD 4, and above USD 4.

are employed is significantly less in comparison to the participation of the moderately poor in the labour market (83 per cent) and the economic activity of Class 3 (84 per cent) and Class 4 (85 per cent). While it could be argued that many of the workers may have advanced to the next economic class (USD 1.25 to USD 2), the observation that nearly 65 per cent in the poorest economic class are economically inactive is a cause for concern. It is also worrying that Class 1 has the highest number of unemployed persons. This finding raises further questions about the reasons why this segment is not included in the formal or informal sectors, and has implications for social protection needs and coverage provided by the government (i.e. for the older and the disabled members of the population). The widely accepted notion is that the extremely poor are more likely to seek income-generating opportunities in the labour market due to insufficient household disposable income, few if any material assets and patchy provision of formal social protection in developing countries (Huynh and Kapsos 2013). The case of Sri Lanka shows that the proportion of employed persons increases with advancements in economic class. As a result, those who earn over USD 4 per day comprise the largest representation of the employed and the smallest representation of the economically inactive. The pattern observed in Sri Lanka suggests that working-age individuals who are extremely poor may be marginalised from both the formal and informal sectors (other reasons, such as the lack of motivation to work or the incapability of engaging in the labour market, could also be salient), which in turn perpetuates their poverty and vulnerability.

Figure 2 presents the class breakdown of each ethnic category in Sri Lanka. The data indicate that over 60 per cent of Sri Lankan Moors are extremely poor and 60 per cent of individuals in almost all ethnic groups are extremely or moderately poor. The ethnic group with the highest proportion of people in the middle class appears to be the majority Sinhala population (22 per cent), while the group with the smallest middle class appears to be the Indian Tamils (10 per cent). This latter trend is rooted in the historical and ongoing marginalisation and disenfranchisement of Indian Tamils in Sri Lanka, indicating that barriers to economic mobility still exist for this group and need to be addressed.

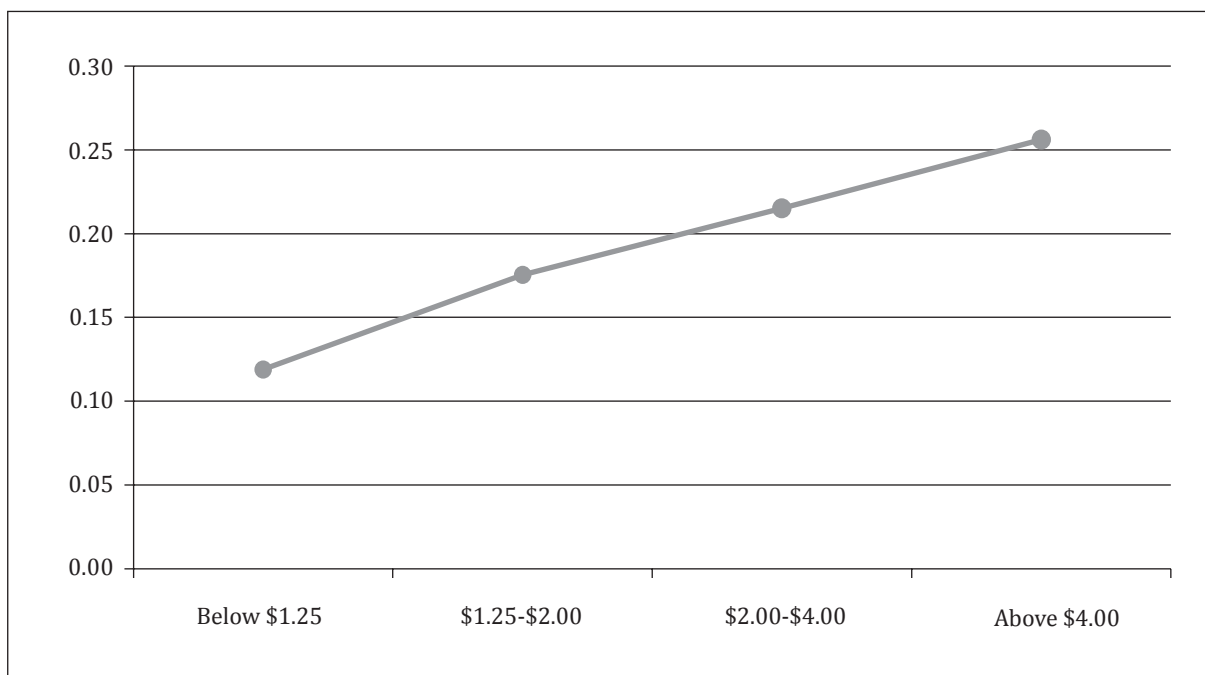
**Figure 2: Ethnicity and Economic Class (%)**



**Source:** Author's calculations based on Department of Census and Statistics (2009/10).

Figure 3 presents gender differences in the overall economic activity rates regardless of economic class. The deficit in female labour force participation increases with advancement in economic class. The extremely poor have a relatively lower gender gap in labour force participation (12 per cent) compared to the developing middle class and above (26 per cent).

**Figure 3: Male-Female Gap in Labour Force Participation Rates Aged 15+ by Economic Class (percentage points)**



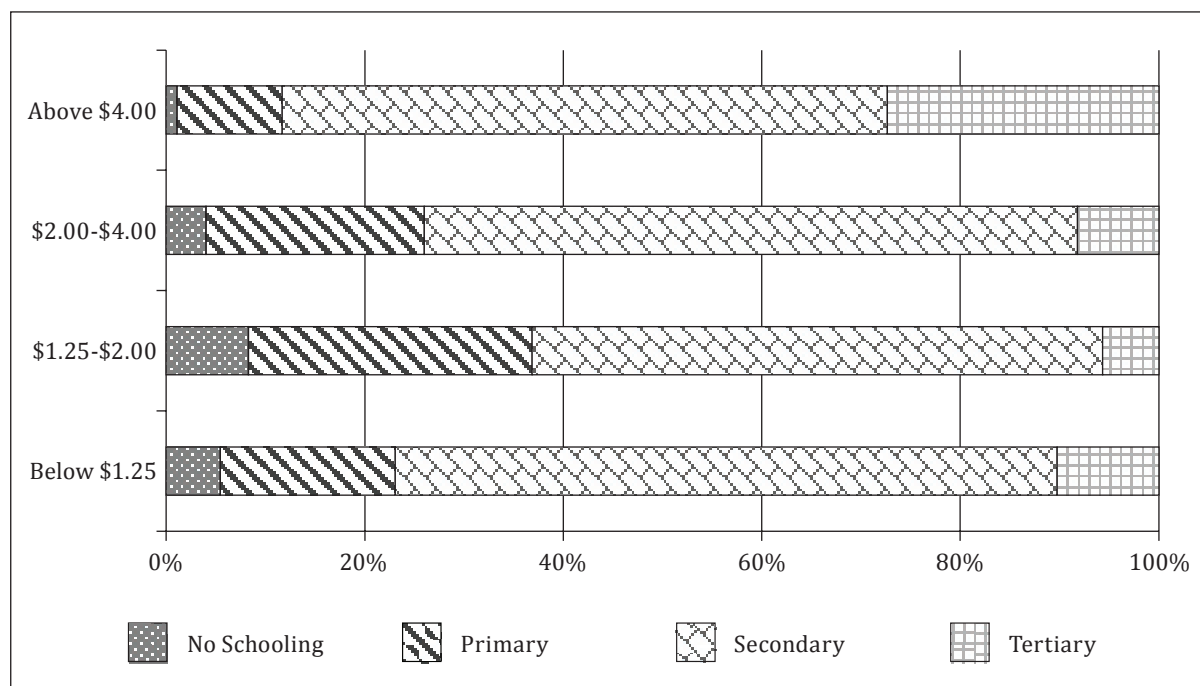
**Source:** Author's calculations based on Department of Census and Statistics (2009/10).

In most developing countries, more and more women participate in the labour force as their incomes improve. In India, for example, the trend is the reverse of what is observed in Sri Lanka, which is attributed to relatively more egalitarian sharing of household responsibilities between men and women in middle class families or the luxury of domestic help that can be afforded by affluent families, which allows middle class women the option to pursue career opportunities (Huynh and Kapsos, 2013). Although the trend in India corroborates the notion that a growing middle class can promote women’s economic participation, the reversal of the trend in Sri Lanka challenges that a growing middle class has positive implications for gender equality in terms of engagement in paid work. The unemployment rate for women is also much higher in comparison to that of men in Sri Lanka. In 2003, the women’s unemployment rate was 12.3 per cent, compared to the men’s unemployment rate of 6 per cent, and 6.3 per cent, compared to men’s 2.7 per cent, in 2012 (Department of Census and Statistics, 2012). In 2012, 70 per cent of the female labour force was economically inactive compared to 33.2 per cent of the male labour force (ibid). The trend in Sri Lanka requires further investigation into why fewer females engage in the labour market. Institutionalised discrimination against women, which poses barriers to women’s advancement in the labour force, may explain the higher deficit of females in the “developing middle class and above” category, which has important implications for policies such as affirmative action for higher-level managerial and decision-making positions in the public and private sectors.

#### 4.1.2 Education Gaps and Middle Class Opportunities

While there is general consensus on the conceptual link between education and poverty reduction, an examination of the class-based education gap and stylised facts that emerge from comparison of the extremely poor, moderately poor, near-poor and middle class workforces is worthwhile. The general expectation is that higher economic classes have higher levels of educational attainment (see Figure 4).<sup>5</sup> The Figure demonstrates that the largest shares of the population across all four economic classes have completed secondary education, given that Sri Lanka has progressive education policies

**Figure 4: Distribution of Labour Force Aged 15+ by Education and Economic Class (%)**



Source: Author’s calculations based on Department of Census and Statistics (2009/10).

<sup>5</sup>Primary education includes Grades 1 through 5, secondary education includes Grades 6 through 13, and tertiary education includes undergraduate or graduate degree programmes.

that encourage even the poorest to attend school. Consistent with the generally accepted association between educational attainment and poverty reduction, the highest economic class records the highest proportion of individuals with tertiary education. Sri Lanka's labour force trends from 1998 to 2012 indicate an increasing trend in the level of education of the employed population as a whole (ibid, 17), signalling the likelihood of sharpened class disparity in the labour market in the future.

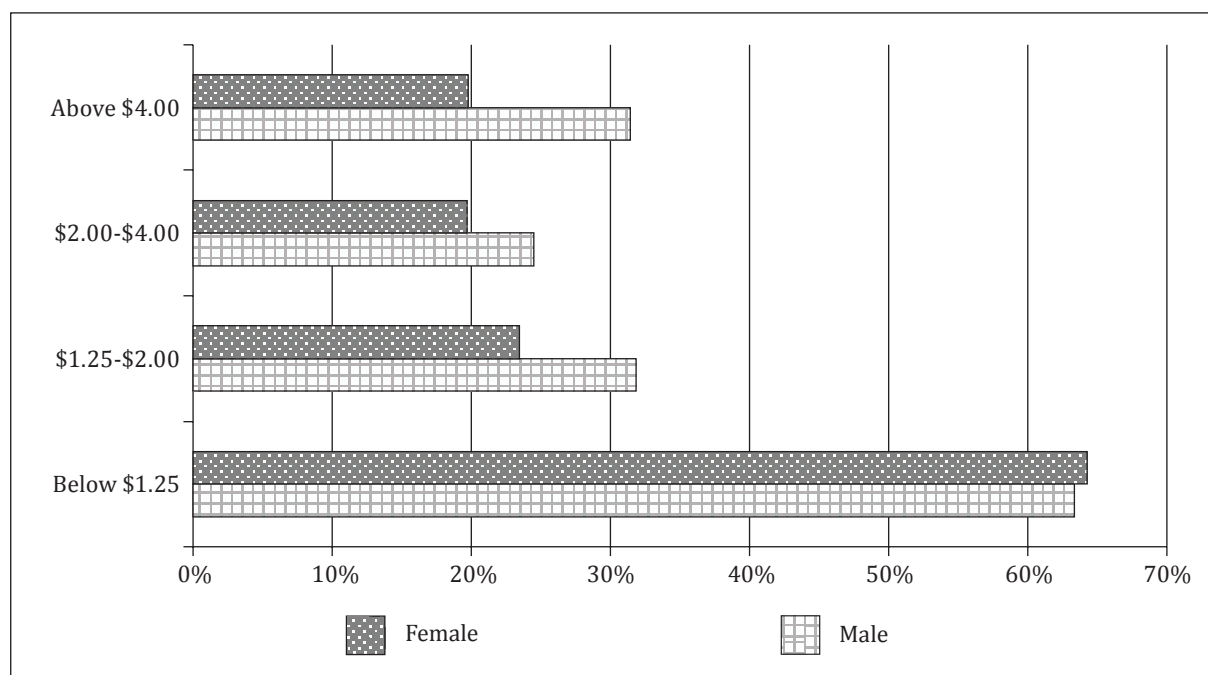
This evidence further strengthens the claim that the educational attainment of the labour force is strongly tied to economic class, with higher levels of education consistently associated with higher economic classes. Relatedly, there is a strong link between educational attainment and employment in both the formal and informal sectors. In 2011, 81 per cent of the labour force with only primary education and 73 per cent also completing secondary education worked in the informal sector, while 77 per cent of workers with tertiary education were employed in the formal sector (Department of Census and Statistics, 2012).

#### 4.1.3 Moving from Quantity to Quality: Vulnerable and Casual Employment

Examining the conditions and security attached to jobs is generally useful in providing insight into the quality of employment. This study adopts the international definition of vulnerable employment as the proportion of own-account and contributing family workers in total employment. Individuals in these categories are less likely to have formal work arrangements, consistent income and access to benefits or social protection as well as relatively more vulnerable to poverty in times of crises and shocks (International Labour Office, 2013). Figure 5 shows male and female participation rates in vulnerable employment by economic class. Male and female participation in vulnerable employment among those parts of the poorest economic class is more or less equal, with a slightly higher proportion of female workers being in vulnerable employment. However, in higher economic classes, shares of males in vulnerable employment are much higher than those of females.

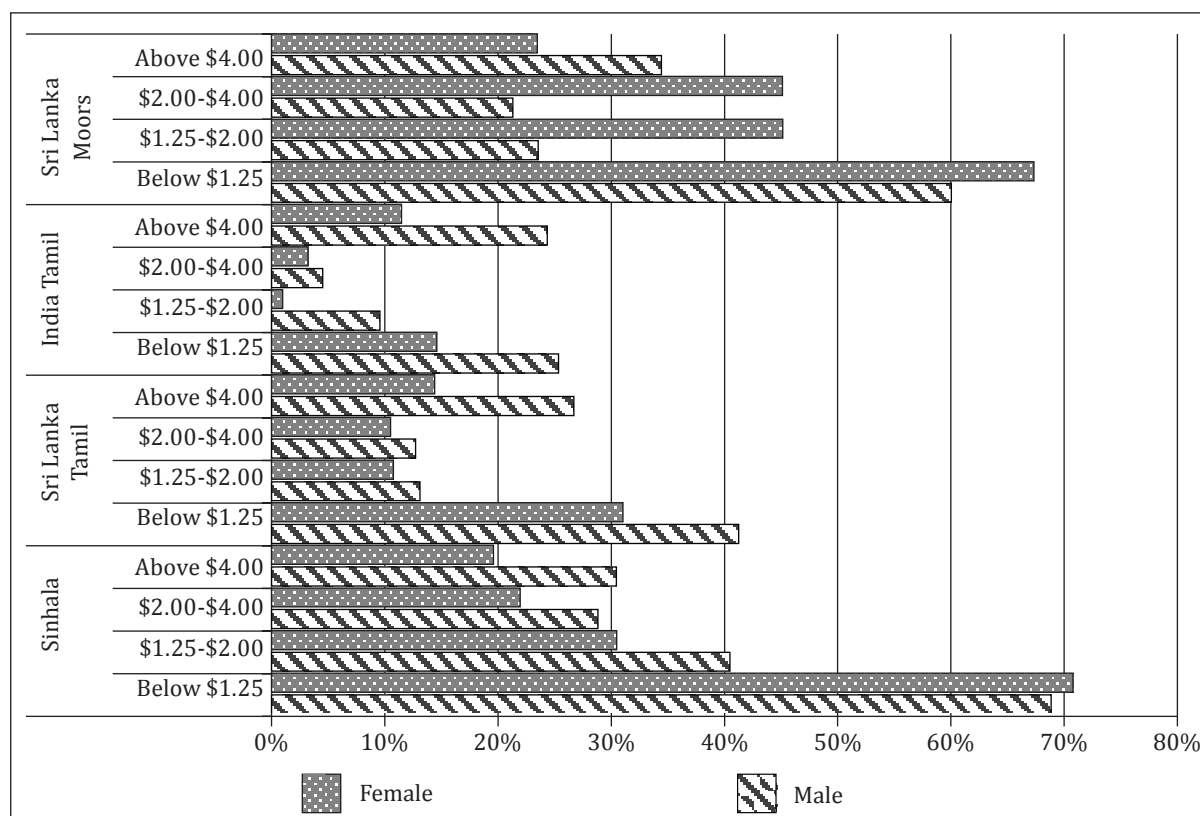
When the shares of the population in vulnerable employment are further disaggregated by ethnicity, significant proportions of extremely poor women among Sri Lankan Moors and the Sinhala population (70 per cent and 73 per cent, respectively) appear to be engaged in vulnerable employment, as

**Figure 5: Vulnerable Employment by Sex and Economic Class (%)**



Source: Author's calculations based on Department of Census and Statistics (2009/10).

**Figure 6: Vulnerable Employment by Ethnicity, Economic Class and Sex (%)**



Source: Author’s calculations based on Department of Census and Statistics (2009/10).

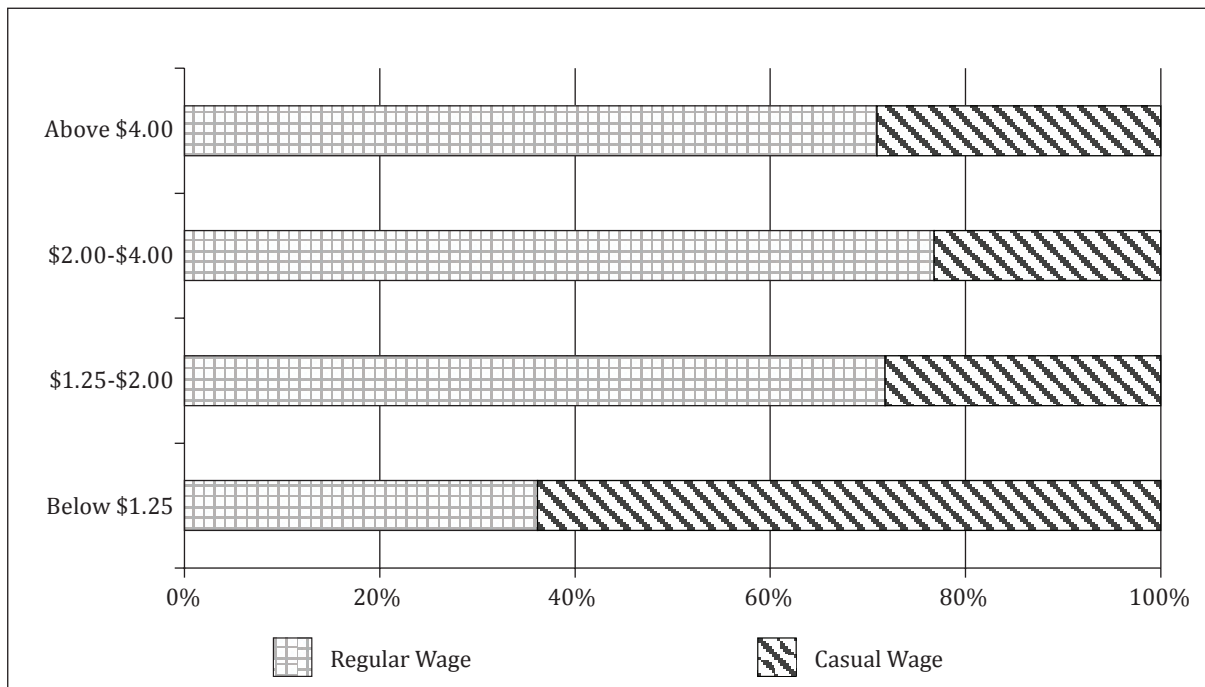
shown in Figure 6. It is important to highlight that Indian Tamils, one of the most marginalised ethnic groups in Sri Lanka, do not appear to be highly engaged in vulnerable employment. The Indian Tamil population in Sri Lanka who mainly work on tea plantations<sup>6</sup> is among the poorest, 61 per cent of estate sector households falling into the poorest category in terms of socio-economic status (Jayawardena, 2012). Although considered “formal employment,” the jobs of estate workers are far from decent – their remuneration is insufficient to cover basic expenditures, hence these workers are among the country’s poorest in terms of nutrition (ibid). The fact that the Indian Tamil population’s engagement in the estate sector is not captured by the definition of “vulnerable employment” suggests that the concept of vulnerable employment should be extended to include precarious and informal work arrangements within the formal sector.

Vulnerabilities faced by own-account and contributing family workers are often shared by casual wage employees. While regular wage employment is commonly associated with better job quality, casual wage work is linked to sub-par working conditions and job insecurity. Figure 7 shows the proportions of regular wage employees and casual wage employees in the total working population.<sup>7</sup> Evidently, the poorest economic classes are largely comprised of casual wage employees. But with advancement in economic class, the share of casual wage employees in the total working-age population remains between 20 per cent and 30 per cent. Although there is a trend of decreasing

<sup>6</sup>The labour force on tea estates consists of Tamil immigrants from India who were brought over by the British as indentured labour. They were deprived of citizenship rights for a long time and were thus neglected by many of the country’s economic development programmes. Both men and women engage in various jobs on tea plantations and estate workers and their families live on plantation premises.

<sup>7</sup>Regular wage employees are government workers, semi-government workers (semi-government institutions are partly owned by the government and partly by private enterprises or individuals), private sector workers and employers. Casual wage employees are own-account and contributing family workers.

**Figure 7: Regular Wage and Casual Wage Employment**



**Source:** Author’s calculations based on Department of Census and Statistics (2009/10).

shares of casual wage employees in higher economic classes up to the “near-poor workers” category, this trend does not carry over to the developing middle class and above.

#### 4.1.4 Escaping the Agricultural Poverty Trap

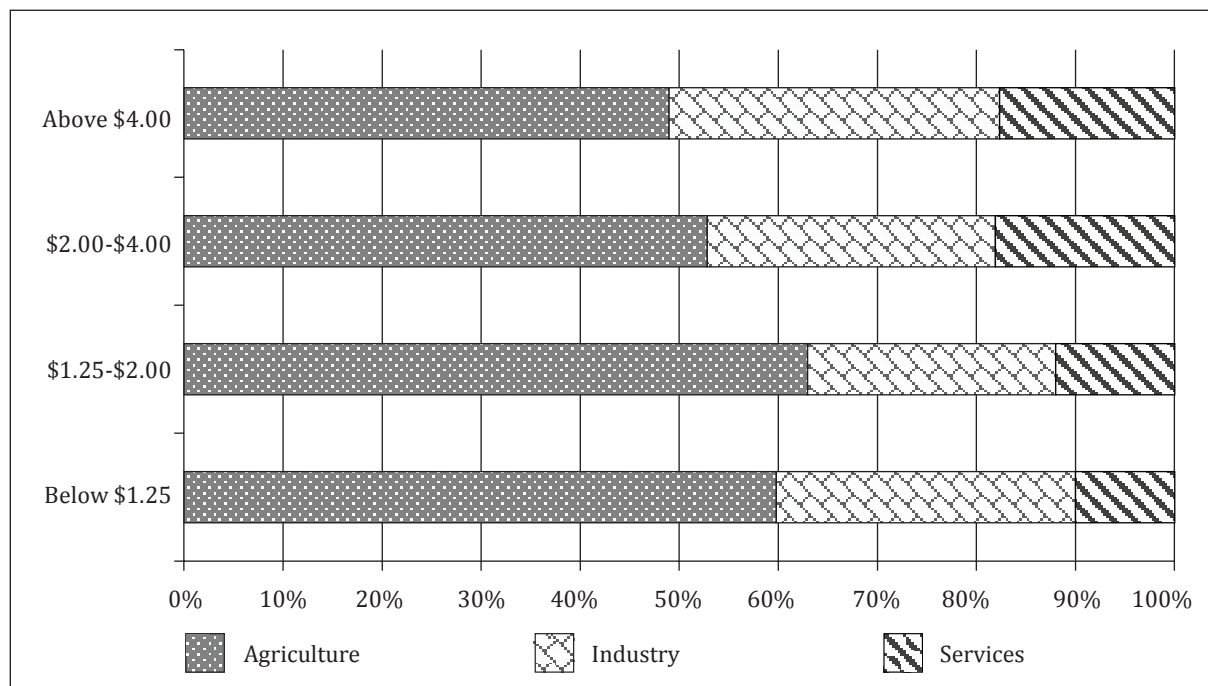
Given that the majority of the world’s poor engage in the agricultural sector, it is important to examine whether workers part of a particular economic class are concentrated in a certain economic sector. Figure 8 indicates that the vast majority of the extremely poor and moderately poor engage in agriculture.

Conversely, with advancement in economic class, the chances of being employed in the services or industrial sectors increased significantly. These observations bolster the argument that rural workers must be supported to increase their agricultural productivity while also encouraging the transition of workers out of agriculture into value-added services. The majority of extremely poor and moderately poor workers are employed in the agricultural sector, and nearly 55 per cent of the developing middle class and above are in the services sector. The share of employment in the industrial sector is generally consistent across all economic classes, indicating that employment within this sector is less likely to be tied to a worker’s economic class.

Manufacturing is an important sector worthy of further examination given its instrumental role in driving export-oriented growth, salaried jobs and higher living standards in developing countries. Figure 9 shows the distribution of workers in the manufacturing sector by sex and economic class. The figure demonstrates that the majority of females engaged in manufacturing are part of the poorest economic class while over 50 per cent of males within the sector are part of the highest economic class.

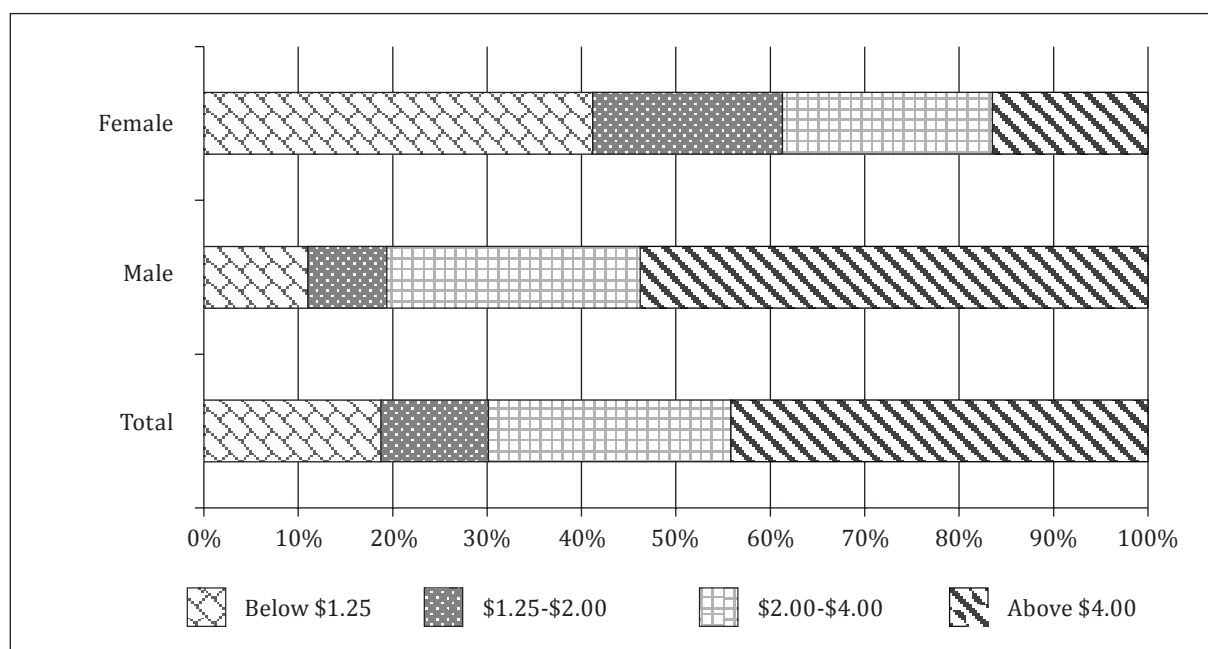
It should be noted that Sri Lanka has a larger proportion of male manufacturing workers from the developing middle class and above, indicating gender disparity in employment in better-paid or highly skilled manufacturing jobs.

**Figure 8: Distribution of Employed Population by Economic Sector and Economic Class (%)**



Source: Author's calculations based on Department of Census and Statistics (2009/10).

**Figure 9: Employment in Manufacturing by Sex and Economic Class (%)**



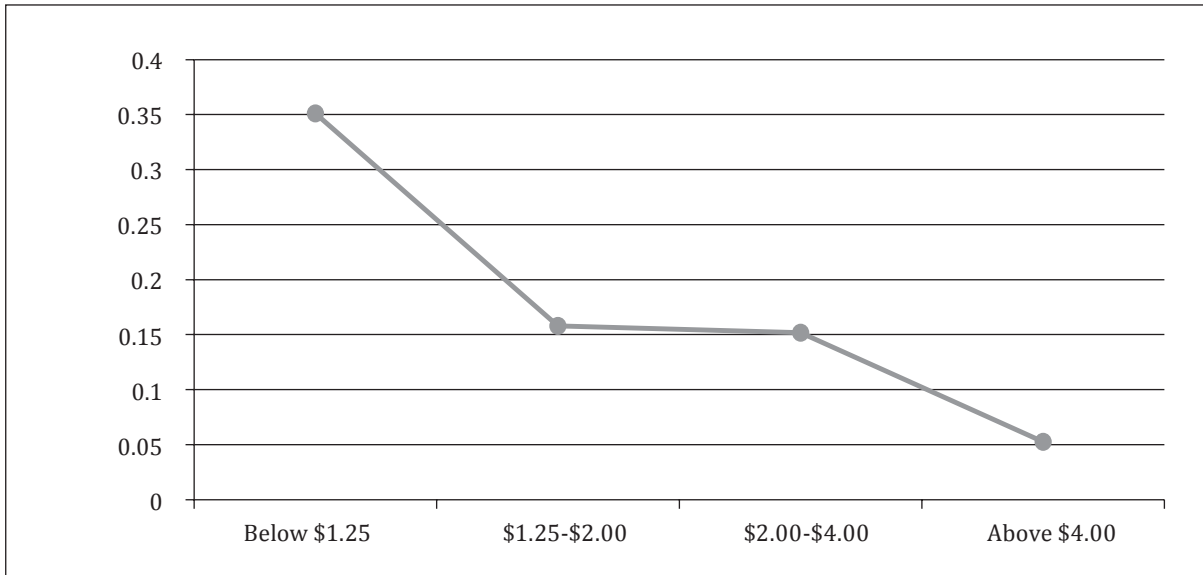
Source: Author's calculations based on Department of Census and Statistics (2009/10).

#### 4.1.5 Youth, Labour Markets and Economic Class

Aged 15-24 are considered to be the formative years of skill development of an individual. Generally, youth within this age range from wealthy families tend to invest in education during these years, whereas their extremely poor counterparts are left without a choice but to participate in income-generating activities. In Sri Lanka, the rich-poor gap in labour force participation by youth between the extremely poor and the developing middle class and above is nearly 30 percentage points

(see Figure 10). The lower rate of labour force participation among youth part of the developing middle class and above, 5 per cent, could also reflect better access to higher education and training opportunities available to middle-class youth in comparison to poorer youth.

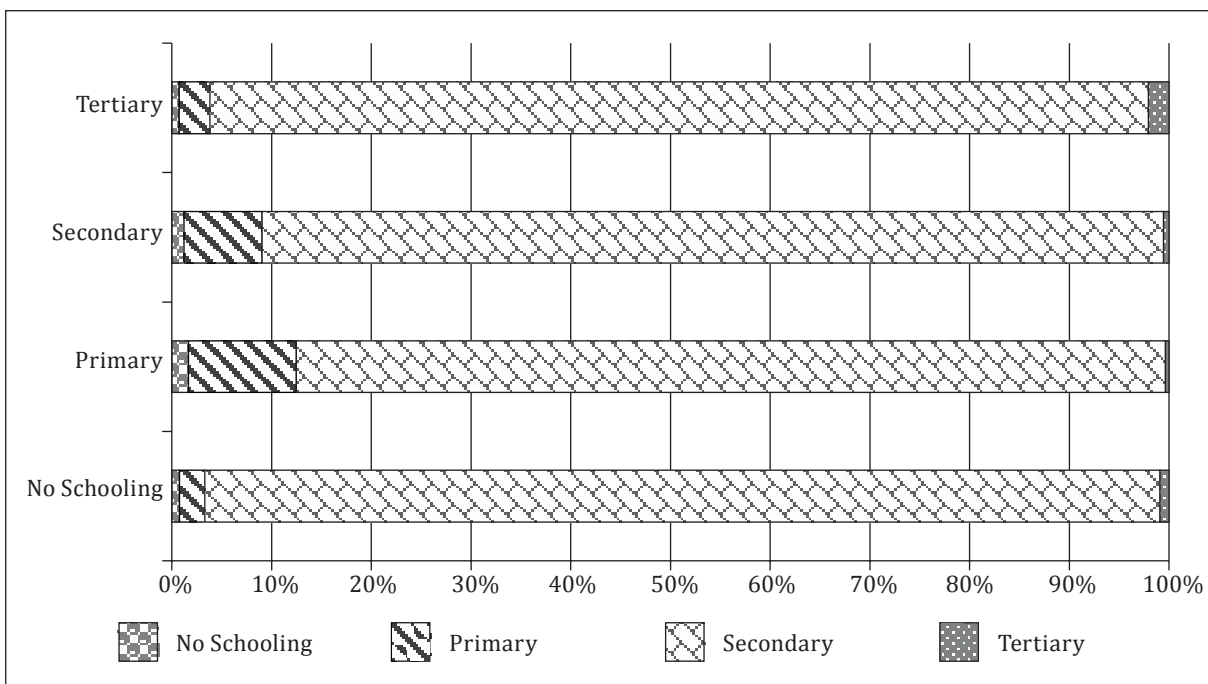
**Figure 10: Labour Force Participation Rate of Youth by Economic Class (%)**



Source: Author's calculations based on Department of Census and Statistics (2009/10).

Youth unemployment in Asia is often linked to the phenomenon of highly educated youth from affluent families spending time seeking ideal jobs that fit their aspirations and careers that fulfill the social expectations of their economic class. Figure 11 illustrates youth unemployment by economic class and sex. It demonstrates that there is a higher unemployment rate among female youth than male youth across all economic groups. This disparity could be a result of discrimination of women by employers within the labour market. The large share of unemployment

**Figure 11: Youth Unemployment by Economic Class in Sri Lanka (%)**



Source: Author's calculations based on Department of Census and Statistics (2009/10).

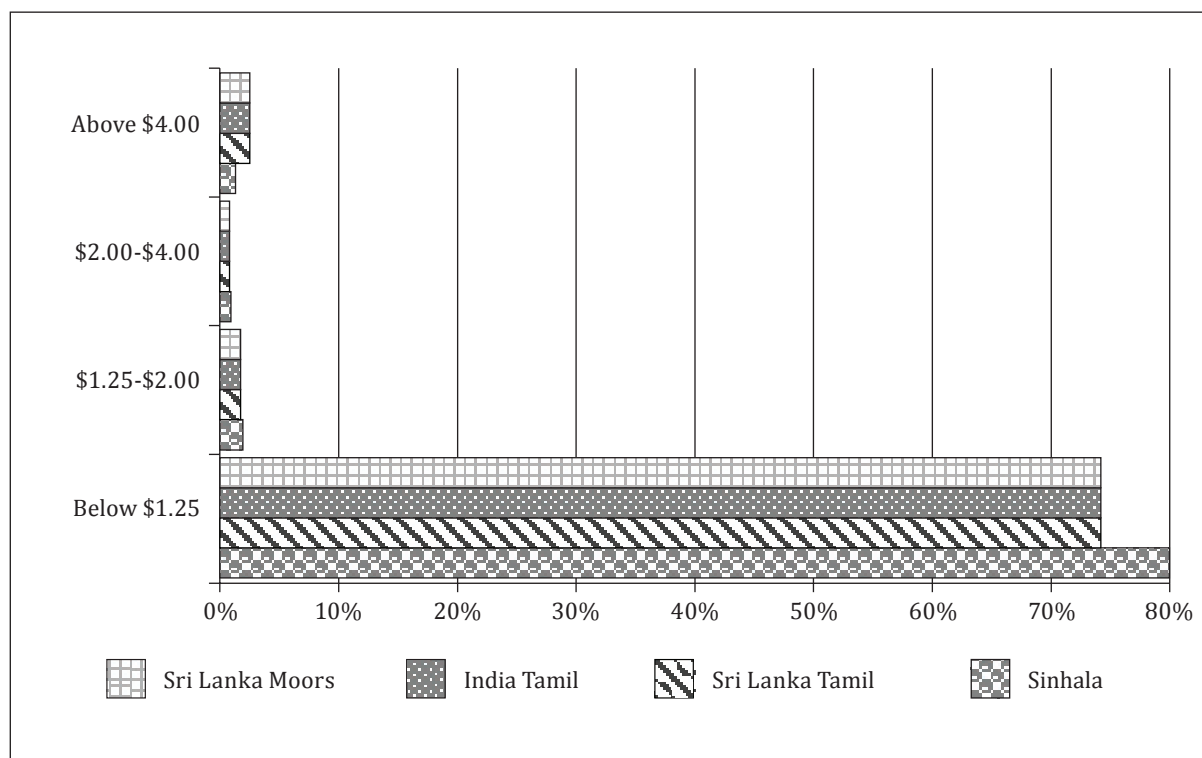


in the poorest economic class indicates that a large proportion of youth live without an income and often remain dependents.

Sri Lanka’s trend is a matter of concern since the poorest of the youth population appear to be excluded from the labour market. Their situation is worsened by the lack of higher education opportunities and training that is required for employment and social mobility in the country. This observation also may imply that the pace of job creation in some developing countries that have reached middle-income status is slow.

A breakdown of youth unemployment by ethnicity (see Figure 12) indicates that Sinhala youth from extremely poor households, as a proportion of total unemployed Sinhala youth, have the highest rate of unemployment at 80 per cent, although youth belonging to the remaining ethnic groups that are part of the same economic class also have alarmingly high unemployment rates. Left unchecked and unaddressed, this situation could have grave implications for social and political stability in Sri Lanka.

**Figure 12: Unemployment Rate by Ethnicity and Economic Class (%)**



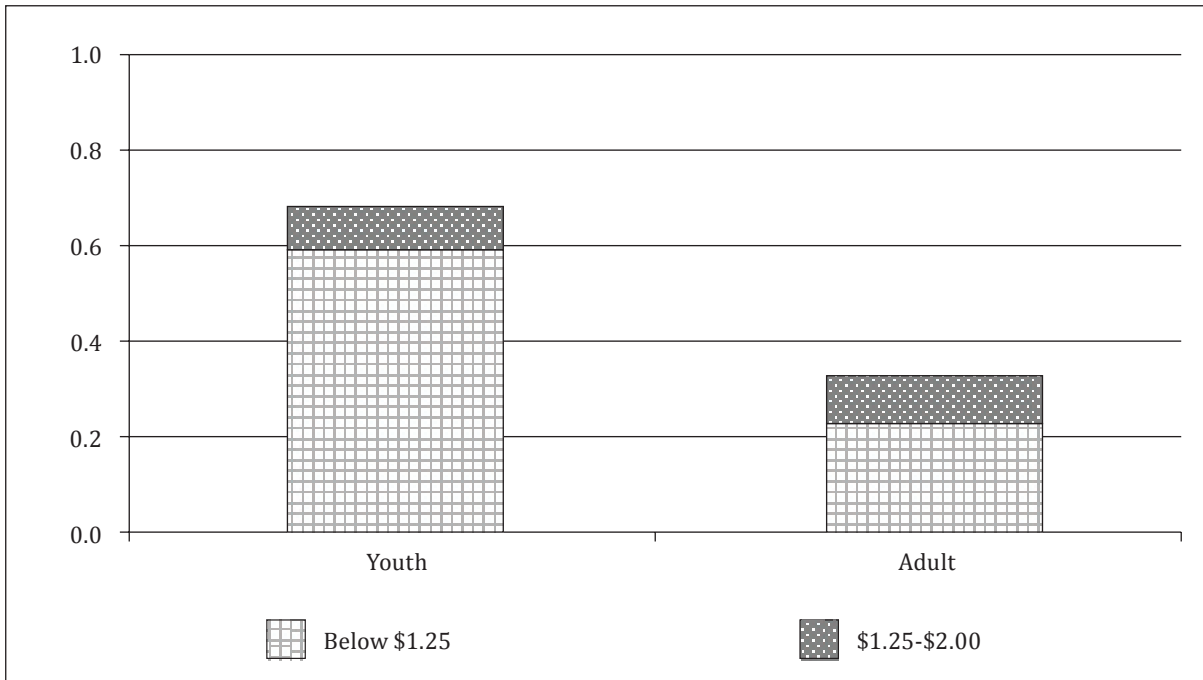
Source: Author’s calculations based on Department of Census and Statistics (2009/10).

#### 4.1.6 Youth Workers’ Quality of Work

A defining characteristic of employed youth in developing countries is that they tend to belong to the “extreme working poor” category. In Sri Lanka, over 60 per cent of youth workers live in extremely poor households (Figure 13).

Another stylised fact is that young workers are predominantly engaged in vulnerable employment (Figure 14). Vulnerable employment, defined as own-account work or work that contributes to family activities, is not only precarious and insecure but also offers insufficient earnings that perpetuate the cycle of poverty among young people. A comparatively smaller proportion of young workers in

**Figure 13: Share of Workers from Poor Households by Age Group (%)**



Source: Author's calculations based on Department of Census and Statistics (2009/10).

**Figure 14: Vulnerable Employment among Young Workers (%)**



Source: Author's calculations based on Department of Census and Statistics (2009/10).

middle-income groups engage in vulnerable employment, which indicates that job quality increases with advancement in economic class.

Although the vulnerable employment rate of adults was higher than that of young people, it should not be assumed that young workers have better quality jobs in comparison to adults. Further examination reveals that young workers often serve as contributing family workers who do not

receive any remuneration. This observation demonstrates the need to implement measures that enable youth to access gainful employment including sustainable entrepreneurship opportunities. Measures to improve the working conditions of youth must be supplemented with targeted actions to facilitate better access to education and financing options.

#### *4.1.7 Discussion of Findings*

This study employs an absolute definition of poverty at USD 1.25 and four economic class definitions with the intent of gaining a disaggregated picture of the labour market characteristics of the extreme working poor, the moderate working poor, near-poor workers, and the developing middle class and above in Sri Lanka. The application of a class-based framework, albeit rigid (and arguably arbitrary),<sup>8</sup> provides a nuanced understanding of full, productive and decent employment challenges that must be addressed in the post-2015 agenda. Further disaggregation by sex and age helps emphasise key concerns for poor women and youth and policy measures that can improve their positions in the labour force.

The above analysis presents a number of key findings that warrant further discussion. First, as demonstrated, individuals from higher economic classes have higher labour force participation rates in comparison to those from lower classes. This finding corroborates that of the recent study by Sri Lanka's Centre for Poverty Analysis (2011) that individuals from relatively higher income groups have a first-mover advantage in accessing the opportunities created by improvements in infrastructure or the expansion of markets. Despite reaching MIC status, Sri Lanka has a disproportionately high proportion of economically inactive and unemployed individuals among the extremely poor. As mentioned, economic inactivity could be due to old age, physical or mental disabilities that make it difficult for individuals to gain employment in a country that offers limited options for the differently abled, or a lack of motivation to participate in the labour force. Aside from the old aged, the economic inactivity of these other two groups is a matter of concern because it suggests labour market exclusion. What this means is that Sri Lanka's economy has not grown on a sufficient scale to absorb the expanding labour force, which in turn has resulted in adverse employment outcomes. This situation is inherently tied to the pattern of economic growth in the recent past. As such, achieving desired employment outcomes for the lower classes will be contingent upon reversing some aspects of the prevailing pattern of production that enables retrenched workers to get back into the labour force and simultaneously benefit from social assistance.

Second, this study finds that educational attainment is positively related to economic class with tertiary education being elusive for many living under or just above the poverty line. Additionally, young extremely poor, moderately poor and near-poor workers have significant difficulties in accessing higher education opportunities and gainful employment options. In the Sri Lankan context, access to primary and secondary education is less of an obstacle than access to higher education, particularly for low-income groups, although it is the quality of public education that is the matter of greater concern.<sup>9</sup> The diminishing quality of public education is invariably associated

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<sup>8</sup>When factoring in the cost of survival in Sri Lanka, even USD 4 a day cannot be considered a living wage. According to the Department of Census and Statistics (2012/13), the monthly average household expenditure of an urban household is estimated to be LKR 59,001 (relative to USD 15 per day per household or roughly USD 4 per day per person) and the monthly average expenditure of a rural household is estimated to be LKR 37,561 (relative to USD 9.5 per day or roughly USD 2.5 per day per person). The 2014 national poverty line is LKR 3,924 per person per month, which is almost USD 1 a day.

<sup>9</sup>Arunatilake (2006) examined the factors that determine unequitable rates of education participation among students aged 5-14 years, finding that demand-side problems such as poverty, direct and indirect costs of schooling, and cultural factors as well as supply-side shortcomings, such as the quality of education, affect the schooling of the observed group.

with the marketisation of education and the lack of government spending on higher education.<sup>10</sup> The sharp rise of “private tuition” by teachers (who are part of the public school system) and increasing competition for university admission push students to “purchase” market-offered education as a ticket to higher education (Aturupane *et al.*, 2013; de Silva *et al.*, 1991; de Silva, 1994; Gunawardena, 1994; Nanayakkara and Ranaweera, 1994). This trend leaves behind students from low-income groups who are unable to afford the extra help that is offered by the market. Moreover, the emergence of private higher education institutions, which boast affiliations with prestigious foreign universities, charge exorbitant fees for degree programmes but offer alternatives to individuals from wealthier families who are either unable or unwilling to attend local universities. Given the wide assortment of education options at their disposal and social networks that open avenues for employment, youth from relatively affluent families get a head start in the labour force, whereas their poor counterparts are gradually robbed of their rights to education and work. Thus, targeted measures that improve the quality of education and access to higher education and skills training for the poor and near poor must be supplemented with structural reforms concerning the marketisation of education.

Youth, particularly young females, face considerable obstacles in accessing employment. Sri Lanka’s national labour force participation rates for youth aged 20-24 years and 25-29 years are 56 per cent and 65.9 per cent, respectively, compared to around 70 per cent for older age groups (United Nations Development Programme Sri Lanka, 2014, 34). Among youth are the currently unemployed and the 40 million estimated first entrants into the job market (*ibid.*). The latest Youth and Development report (National Human Development Report 2014) finds that around 19 per cent of young workers are unsatisfied with their current jobs and a further 15.5 per cent engage exclusively in unpaid household work. Prior studies find a mismatch between the supply of job seekers with higher education levels and job aspirations and the demand for workers with those levels of educational attainment (Arunatilake and Jayawardena, 2010). Evidence points to the inability of the Sri Lankan education system to teach general skills (e.g. command over the English language and computer skills) essential for securing “good” jobs (*ibid.*), which is a reflection of the quality of education highlighted earlier in this discussion. The lack of formal employment opportunities for youth is generally explained by the slow rate of job creation, skills mismatch and queuing<sup>11</sup> (*ibid.*). There is intense competition for a limited number of desirable jobs and most vacancies are in low-skill occupational categories. Available jobs that require few skills may not meet the expectations of many young workers with higher education who aspire to sophisticated white-collar jobs, which in turn results in high levels of underemployment.

However, fixating on supply-side interventions – higher education, vocational training and enhancement of skills – all of which increase an individual’s “employability,” is only one part of the solution. The presence of a sizable population of unemployed educated youth in Sri Lanka indicates that the benefits of supply-side interventions are unlikely to be commensurate with the outlays. While the importance of long-term policy focus on improving the quality of education is crucial for MICs, recalibrating economic growth models to become inclusive and create decent jobs that can absorb the growing labour force is equally important. There is an urgent need to create jobs at the higher end of the occupational hierarchy and improve working conditions of low-skill occupations so that the job market appeals to job-seekers with diverse skill sets.

Third, vulnerable employment – jobs in the agricultural sector, casual wage labour, own-account work and contributions to family activities – is significantly linked to lower economic classes. In

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<sup>10</sup>Sri Lanka’s public spending on education has remained at 2-3 per cent of GDP during the past decade and a half, compared to a 3.5 per cent average across the rest of South Asia. General education, which includes primary and secondary levels, absorbs the largest share of total education expenditure. In 2005, higher education received a meager 14 per cent of the education budget, whereas technical training was granted an abysmal 3 per cent (World Bank, 2008).

<sup>11</sup>The idea of a labour/employment queue refers to the sets of individuals that compete for job openings at the same time, and are rank ordered by the employer. Understanding the rank orderings that employers impose on candidates for job vacancies becomes a high priority for accounts of the determinants of inequality.

South Asia, the poor and the near poor vis-à-vis middle-class workers face notable disadvantages in accessing better quality jobs. The above analysis describes the difficulties faced by the vulnerable segments of society, particularly agricultural workers, in gaining access to employment opportunities. Although the size of the services sector has increased at the expense of the agricultural sector, this change cannot be viewed as “employment-friendly.” While this situation may be viewed by mainstream proponents of economic growth as “normal,” the vulnerable population will be denied full, productive and decent employment if the nature of the underlying economic growth model is left unaddressed. Moreover, whether low-quality informal and irregular employment or own-account work with harsh conditions, low productivity and low and uncertain remuneration can even be considered “employment” in an inclusive growth model is a matter that requires further discussion and reflection. This situation must be addressed in a systematic manner with investment in infrastructure and by striking a balance during sectoral transition from agriculture to the production of value-added goods and services (in a way that maintains agricultural output and consistent food production).

Finally, gender disparities in labour force participation and job quality are prevalent across all economic classes in Sri Lanka. Higher household affluence is associated with relatively widening gender gaps in economic activity, which signal institutional discrimination that is sharpened by the patriarchal biases of employers, or reflect women’s choices not to engage in paid labour. This finding questions the generally accepted positive association between education and employment as Sri Lanka boasts high educational attainment levels for women relative to their male counterparts. The narrow range of skills typically acquired by women, gender segregation by occupation, demand for low-cost female labour, and the dual/multiple roles of women – paid work and unpaid reproductive and family responsibilities – are considered obstacles to women’s participation in paid employment (Wijayaweera, 2012). The finding from Sri Lanka also challenges the widely accepted notion that “middle-class values” facilitate the removal of barriers faced by women in entering the labour force, suggesting that affirmative action measures, family-friendly employment benefits and gender sensitisation of employees in both public and private sectors should be adopted to encourage women’s participation in the labour force regardless of their economic class.

Previous studies that examine the gender wage differential for Sri Lanka find that discrimination in the labour market, rather than differences in productive characteristics, account for a large fraction of the gender wage gap (Aturupane, 1993; Ajwad and Kurukulasuriya, 2002). Gunewardena (2003) finds that although the rates of return to education in employment are higher for women, occupational segregation of men and women has a negative impact on women’s wages since wages are depressed in the predominantly female professions of teaching and nursing (Gunewardena, 2003). Moreover, while the high levels of educational attainment by females indicate a rational response to the higher rates of return to education in employment, a bias against women still persists at the level of unskilled labour (ibid). In addition to gender wage gaps, there are also noticeable differences in wages along ethnic lines, particularly among young workers. Young Tamil men living outside the North and East are underpaid in comparison to Sinhala men in the same regions (Gunewardena, 2010). Larger unexplained wage differentials in the public sector relative to the private or agricultural sectors may reflect language constraints or patronage politics. Ethnic wage gaps among young females are largely explained by productive characteristics (i.e. low levels of education among minority women). This observation indicates a need for policymakers to redress gender bias in the labour market, especially for young and unskilled women, while continuing investment in the education of both women and men.

## **5. Conclusions and Recommendations for the Post-2015 Agenda**

This paper has offered a class-based analysis of labour market characteristics in Sri Lanka. It has discussed characteristics that distinguish the poor from the middle class in terms of education, access to better quality jobs, working conditions and opportunities for young people and women. Presented below is a summary of its findings.

First, individuals from relatively higher economic classes have higher labour force participation rates in comparison to those from lower classes. The highest level of unemployment is recorded for those living on under USD 1.25 per day, indicating the “extreme working poor” economic class experiences labour market exclusion. Second, there is a trend of increasing gender disparity in labour force participation and job quality across all economic classes. The gap between males and females in labour force participation increases as household incomes improve. More women than men among households living on under USD 1.25 per day engage in vulnerable employment. In the manufacturing sector, there are significantly more men than women in better-paid or highly skilled jobs. Third, educational attainment is positively related to economic class. The majority of individuals living on under USD 4 per day have only completed secondary education, while there has been a dramatic increase in the number of workers with tertiary education from households living above USD 4 per day. A low level of educational attainment has a strong link to employment in the informal sector in Sri Lanka. Fourth, a disproportionate number of those individuals living on under USD 1.25 per day engage in employment that provides casual wages (as opposed to regular wages) in comparison to those from other economic classes. Fifth, workers from higher economic classes are employed in the services sector at relatively higher rates than their poor counterparts (the vast majority of poor workers are employed in the agricultural sector). Sixth, significantly more young workers living on under USD 1.25 per day participate in the labour force in comparison to their better-off counterparts. Unemployment among youth living on under USD 1.25 per day is nearly 80 per cent. Finally, the historically marginalised Indian Tamil population’s engagement in the estate sector is not captured by the definition of “vulnerable employment” employed in this study, suggesting that the concept of vulnerable employment should be extended to include precarious and informal work arrangements within the formal sector.

Since “ending poverty” ranks high among the proposed goals for the post-2015 development agenda, it is important to reinforce the well-established link between poverty reduction and gainful employment and push for development goals and targets that foster inclusive growth in a meaningful way. Despite its immense individual and social benefits, policymakers throughout the world have moved away from attempting to achieve full employment. Despite the lack of political will, there are strong reasons to argue the case for full employment if poverty reduction is to remain at the heart of the post-2015 agenda. Felipe (2012) provides six reasons to directly advocate for full employment in developing countries: (i) full employment creates high overall purchasing power, which in turn leads to more buoyant markets, successful businesses, investment and growth; (ii) full employment delivers immense individual and social benefits; (iii) every individual has an inalienable right to employment and full employment is stated as a clear objective in many international legal instruments<sup>12</sup>; (iv) since 2006, decent work has been a target under the MDG 1 (to eradicate extreme poverty and hunger); (v) full employment contributes to political stability since the peace and prosperity of any country depends on the well-being of all segments of the population; and (vi) achieving full employment has an ethical basis given that its benefits outweigh its costs.

The proposed goals and targets of the post-2015 agenda tackle the issues of employment in proposed Goal 8: “promote sustained, inclusive and sustainable economic growth, full and productive employment and decent work for all” (United Nations, 2014). The above analysis suggests that the economic growth models of developing countries need to be recalibrated in a way that enables individuals from lower economic classes to access gainful employment, which in turn will facilitate poverty reduction and social mobility of low-income groups. While target 8.2 under the proposed goal advocates to “achieve higher levels of economic productivity of economies through diversification, technological upgrading and innovation, including through a focus on high value added and labour-intensive sectors” (ibid), the evidence from Sri Lanka suggests that the lower classes need an extra boost during their participation in this transition. What are some policy recommendations that

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<sup>12</sup>These instruments include the International Covenant on Economic, Social and Cultural Rights, the International Covenant on Civil and Political Rights, the International Labour Organization’s conventions, the Charter of the United Nations (see Articles 55 and 56), and the United Nations Universal Declaration of Human Rights (see Article 23).



could lead to the realisation of this target? Felipe (2012) suggests a strategy of careful approaching for a transition to value-added production without compromising the well-established importance of a thriving agricultural sector. The policy recommendation, then, is to redress the neglect of agriculture.

From time immemorial, agriculture has been considered the most important pursuit of Sri Lankan people. It has greatly conditioned the socio-economic environment of the country and continues to dominate every sphere of the economy. Although agriculture's contribution to GDP has declined over the decades, it must be noted that more than 30 per cent of the labour force still make their livelihoods directly or indirectly based on this sector (Department of Census and Statistics, 2013a). However, for decades, agriculture has been neglected in Sri Lanka as well as in many other developing countries, which have been attempting to emulate the growth track of East Asian countries. While the prospect of achieving fast economic growth via export orientation is attractive, the neglect of agriculture in favour of industrialisation may lead to food crises that are otherwise preventable. If growth in Sri Lanka is to be inclusive, then agriculture will have to be made a policy priority. Sri Lanka's labour productivity correlates roughly to an average income of USD 737 (in 2005 US dollars), while in Thailand, it correlates to about USD 1,650 and in the United States, about USD 40,000 (Felipe 2012, 47). If Sri Lanka upgrades its agricultural practices only to reach the level of labour productivity in Thailand, there is no doubt that tens of thousands would be lifted out of poverty. Although it could be argued that a better strategy might be to reallocate the agricultural labour force (mostly low-paid workers) from the agricultural sector to more productive sectors such as construction, manufacturing and services, an increase in employment outside of agriculture without a concomitant increase in food production may cause real wages to decrease. For this reason, reviving the agricultural sector, creating productive and decent employment opportunities in this sector, alongside stimulating sectoral transformation is a careful balancing act that policymakers should aim to strike. Relatedly, developing countries must increase public investment in basic infrastructure – energy, transport and urban facilities and services – targeted at high-employment projects and supply-side interventions (i.e. higher education, skills training, health, etc.) that would enable the labour market to be more inclusive.

As the discussion above suggests, production choices must be reconsidered in tandem with the design of more employment-friendly policies. Such changes challenge the neoliberal model of economic growth and the choice of production that is associated with comparative advantage. The growth-employment link will likely get eroded owing to the policy of opening up the domestic market to imports. In 2007-08, for every one rupee of domestic manufactured goods, India imported Rs. 1.38 worth of foreign manufactured goods. The corresponding ratio for Sri Lanka is 1.94 (Sri Lanka Department of Commerce, 2012). This is a classic scenario in which imports disrupt the domestic economy in terms of production output, employment and their inter-linkages. In order to address this likely scenario, macro-level changes must be supplemented by support mechanisms that allow the growth of micro, small and medium-sized enterprises (e.g. credit opportunities, investment, business development, training, etc.) that tend to get overlooked in the current paradigm of economic growth. Maintaining demand to be filled by enterprises by means of stimulation packages seem crucial for many MICs that have employment challenges owing to labour market exclusion.

In a series of papers, Rodrik (2004; 2006) argues that a country's structural transformation requires "strategic collaboration" between the public and private sectors to arrive at areas in which the country has a comparative advantage. The reason for such collaboration is that governments and entrepreneurs may have different sets of information and there may be a lack of communication between them. As such, the process of structural transformation, which is integral to the industrialisation of a country, should be a joint initiative between the public and private sectors to determine new economic activities. The question then is not whether to protect, but *how* to protect and promote industry in order to guarantee technological progress leading to higher labour productivity. These efforts require a private sector that is ready to invest in mutually agreed upon initiatives.

Also required are a sound macroeconomic environment and an enabling environment at the national, regional and international levels. Governments, more often than not, are obsessed with deficits. “Deficit fetishism” does not allow governments to address the difference between the saving desire of the private sector and the required government expenditure on an economy to run at full employment (Stiglitz *et al.*, 2006). However, when analysing deficits, whether or not a country is operating at full employment should be factored in (Felipe 2012, 53). For instance, if a country is at full employment, deficits are likely to crowd out private investment given high interest rates accompanied by high inflation. If the country is not at full employment, the aforementioned adverse effects may not arise. As such, governments should exogenously increase aggregated demand (i.e. increase expenditure) when private sector spending falls short of the full-employment level of effective demand, but reduce aggregate demand (i.e. increase taxation) if this spending exceeds the full-employment level (*ibid*). The balancing act of maintaining government expenditure at a level that neither induces inflation nor deflation is a difficult though achievable feat.

Target 8.5 under proposed Goal 8 for the post-2015 agenda, “by 2030 achieving full and productive employment and decent work for all women and men, including for young people and persons with disabilities, and equal pay for work of equal value” (United Nations, 2014), is supported by the evidence in this study. The findings in this study advocate targeted assistance to retrenched workers in lower economic classes that allows them to access gainful employment. The analysis above highlights the indispensable function played by the informal economy in Sri Lanka, providing means of livelihood to those who are excluded from the formal sector. Although precarious in nature, accessing informal employment serves as a survival and coping strategy for the majority of workers in developing countries who are cut off from regular wage employment due to a lack of productive characteristics and discriminatory social and institutional norms. This situation requires action – public, private or mixed – that enables informal workers to acquire secure and adequate livelihoods that provide a level of reward for work consistent with a minimum standard of basic needs. This minimum standard should be reevaluated periodically to reflect realistic and current standards of living.

Target 4.4 under proposed Goal 4 for the post-2015 agenda, which advocates the provision of “relevant skills, including technical and vocational skills, for employment, decent jobs and entrepreneurship” (United Nations, 2014), is also supported by the evidence in this study. In the context of MICs, this target must be further qualified to specifically target excluded low-income groups within the population who lack access to good quality education that provides general and specialised skills required in the evolving labour market. Without targeting excluded groups, governments will only give lip service to the blanket priority of “improving access to education,” rather than have real and effective impacts on the ground.

Finally, the findings of this study suggest that there is a need for high-quality and timely disaggregated data on employment. While most developing countries currently collect data according to internationally accepted standards and definitions, diverse labour market realities need to be captured as well. For example, most South Asian countries have informal economies that are proportionally larger than their formal economies. However, data on the informal sector lack contextual depth. Labour in both the formal and informal sectors is not captured in consistent and robust ways. Additionally, relevant authorities in countries must revisit their definitions of employment in order to ensure accurate representation of the total labour force. For instance, while the official unemployment rate in Sri Lanka was only 4.4 per cent in 2013, the official definition of employment is very broad. It includes those individuals working a minimum of one hour during the reference week, indicating that there is a strong possibility that widespread underemployment could be undermining prospects for many workers (Department of Census and Statistics, 2013b). Apparently, more than 20 per cent of employed individuals who are willing to work 35 hours or more in a week do not have the opportunity to do so (Karunatilake, 2006). The availability of high-quality, context-sensitive data that provide an accurate picture of unemployment and underemployment will



assist in the process of restructuring required in most labour markets in developing countries to achieve full employment.

The recommendations proposed here based on the evidence in this study are either superficially or substantially related to the United Nation's *Open Working Group Proposal for Sustainable Development Goals* (see United Nations, 2014), which will be presented and debated during negotiations on the post-2015 agenda later in 2015. While this is a positive sign, the architects and power brokers of the post-2015 process still must meaningfully reflect on the urgency of achieving full, productive and decent employment as a way to eradicate poverty. The various proposals for the post-2015 agenda must respond adequately to the accumulated evidence for and increasing challenge of immense livelihood insecurity in MICs. The time has come for governments to finally address the reality that achieving full, productive and decent employment must be deliberately and unequivocally integrated into the economic growth models of developing countries.

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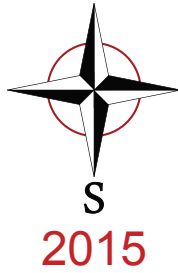
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**Southern Voice on Post-MDG International Development Goals** (*Southern Voice*) is a network of 48 think tanks from Africa, Latin America and South Asia, that has identified a unique space and scope for itself to contribute to the post-MDG dialogue. By providing quality data, evidence and analyses that derive from research in the countries of the South, these institutions seek to inform the discussion on the post-2015 framework, goals and targets, and to help give shape to the debate itself. In the process, *Southern Voice* aims to enhance the quality of international development policy analysis, strengthen the global outreach capacity of Southern think tanks, and facilitate professional linkages between these institutions and their respective governments. *Southern Voice* operates as an open platform where concerned institutions and individuals from both South and North interact with the network members. *Southern Voice Occasional Papers* are based on research undertaken by the members of the network as well as inputs received at various platforms of the initiative. *Centre for Policy Dialogue (CPD)*, Dhaka works as the Secretariat of the *Southern Voice*.



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