CHAPTER II

THEORETICAL BACKGROUND AND LITERATURE REVIEW

2.1 Introduction

The consistent attention that has been paid to the issue of poverty over the last several decades clearly indicates that poverty is an issue that refuses to disappear despite different experiments of "development." Development is always in the center of debates between the contrasting perspectives of different actors within and between communities. In important ways a discourse of development can determine how a country, a people and their past are represented.

In particular, the relationship between knowledge and power in development is also crucial, and it is necessary to explore the constitution of socially important knowledge of development. The different ways of perceiving development create complexity and diversity of development. The definition and impact are various also among the ethnic, society, locations and generation. At the same time, the analysis of poverty, its meanings, causes and consequence has thrown up more complex aspects of the issue in development.

In most of the developing countries such as Sri Lanka, development policies were dominated by western ideology. However, within the variety of global and national development institutions each institution adopts its own myths of 'positive change.' In the last three decades, empowerment through participation and microfinance became a key concept in the methodologies that emerge during this period (even today) in reference to people's engagement with development, and poverty alleviation programs. Grassroots development is often termed 'participatory', but it is important to recognize what this means. In this section I will examine briefly, the theoretical background of these concepts and also how these concepts impact the country development and poverty alleviation in the context of Sri Lanka.

2.2 The Construction of Development

Development is a process by which the range of choices, economic as well as non-economic, become increasingly available to people. However, development means something different to different individuals, groups, and organizations. Throughout the twentieth century, Western governments sought to achieve 'development' not only in their own counties, but also in other regions of the world, particularly in Africa, Asia, Latin America and the Caribbean. Conversely, development has become an important concept in the last 50 years or so since the end of the Second World War. The meanings of development are hotly contested and indeed the very idea of development is under challenge.

In particular, I look at how 'development' has been defined, who has defined it, and at what scale 'development' has been examined. The main definitions of 'development' and 'development theory' are descriptive approaches to development that have changed over time. While some theorists view economic growth and increased economic wealth as the key definition of 'development,' others consider 'development' to encompass ideas of greater autonomy and choice about how individuals live their lives. These definitions reveal different viewpoints and focuses toward rural and urban development and hence are helpful for one to consider while dealing with development.

As Polanyi (1957) analyzed, the development of capitalism throughout the nineteenth century and the huge disruptions of the first part of the twentieth, the idea of 'globalization' has dominated thoughts about development. In the new era of globalization, the question of the appalling poverty of large numbers of the world's people, with continued inequities between the rich and the poor, remains as potent as ever. The studies by Wallman (1977) and others show how people's development goals may be very different from those of the planners. Development is not always a peaceful and effective process. Note that the idea of who the poor are is different in different societies, and is likely to depend on value systems as well as economic factors.

Friedmann (1992) outlines how the basic needs approach could have represented a real alternative to previous development approaches and policies, particularly with its focus on grassroots participation and wealth redistribution. According to Friedmann (1992) the politics of alternative development does not negate the need for continued growth in a dynamic world economy. He said that it would be absurd to attempt to substitute a people-centered development, or to reduce all development questions to the microstructures of household and locality. For Cowen and Shenton (1996) in their discussion of the history of the idea of development, the era of industrial capitalism has also been the period of the 'modern doctrine of development'. Cowen and Shenton (1996) also argue that development should be conceptually differentiated from progress.

The second half of the twentieth century has been called the era of development. Sachs (1992) mentions that the last 40 years can be called the age of development. Esteva (1992) defines development in terms of escaping from underdevelopment. Sachs and Esteva, the leading members of the 'post-development school', argue that development has always been unjust, never worked, and has clearly failed. However according to Sachs, "the idea of development stands like a ruin in the intellectual landscape," and "it is time to dismantle this mental structure" (Sachs, 1992 p.1).

Thomas (2000) points out that development has failed, or that it has always been a 'hoax' designed to cover up violent damage being done to the so-called 'developing' world and its people. Although Thomas (2000) claims that poverty means a lack of development, development may occur without poverty alleviation.

The centralized approach to development rarely provides the poor with sustainable solutions to the problem. These policies are designed by someone at the center and implemented by some others on a top-down channel which ends up producing unsatisfactory and sometimes undesirable results for the poor. In that development process, the poor are regarded as mere "recipients" of these policies. The failures of centralized large-scale policies have induced a search for new ways to undertake the problem of poverty via development. For others, however, the idea of development has been of leading importance over the past half century and remains salient today. While there have been recurrent disappointments, it can be claimed that there have also been successes (Thomas, 2000).

For many people, ideas of development are linked to concepts of modernity, and they also define development as modernity, while looking at development largely in economic term. In economic terms, 'modernity' encompasses industrialization, urbanization and increased use of technology within all sectors of the economy. 'Modernity' in its broadest sense means the condition of being modern, new or up-to-date, so 'the idea of 'modernity' situates people in time' (Ogborn, 1999).

However, within the variety of global and national development institutions each institution adopts its own myths of 'positive change' and in which the poor are represented and development becomes a material reality. The meaning of development built around humanitarian and emergency discourses raises all kinds of questions about the legacies of the past. Yet nowadays, this term is still a central discourse in developing countries, such as Sri Lanka.

However, Sri Lanka was a poor country with a remarkably highly developed welfare state, with this policy influenced from the British colonial time. These development policies were less supportive of economic growth (Perera and Fernando, 1980). Consequently, Sri Lanka's economic growth lagged behind when compared with East Asia. Most development policies were mainly focused welfare development. It may be one reason for lack of economic growth. Arai (2000) said that after independence Sri Lankan leaders were unable to present a clear-cut policy for nation building. Due to the spread of the education system, the labor market was supplied with highly educated school graduates every year, but the country failed to create a private labor market to absorb them.

Nevertheless, the year 1977 was a significant landmark in the history of Sri Lanka for the reason that in the late 1977 a series of policy reforms were introduced on the advice and direction of the International Monetary Fund (IMF) and World Bank (Lakshman, 2000). The government has been engaged in market-oriented economic reforms for over 25 years and has made considerable progress towards achieving a more liberal trade policy regime. Moreover, it has achieved a high level of human development due to the heavy investments by the successive governments in social infrastructure (Karunanayake, 2002). However, in the mid-1980s the World

Bank and the government renewed negotiations and in 1989 introduced a new set of structural adjustment initiatives, amid widespread social unrest arising partly from a public perception because, the economic liberalization had failed to generate the promised benefits for the poor (Shaw, 1999).

The Sri Lankan NGO sector played a significant role in the development process; wealthy people in urban areas managed these NGOs. After a hiatus during the mid-1980s the World Bank and the Sri Lankan government renewed negotiations and in 1989 introduced a new adjustment measures and an expensive poverty safety net known as the Janasaviya Program (JP). JP operated until 1994, when the new government changed the name of the project to the National Development Trust Fund (NDTF). Its mandate was to promote the role of intermediary organizations as welfare delivery agents by providing financial and technical support to local government agencies and NGOs to implement poverty reduction projects. But, before the 1990s, the NGO sector was not well-established. Many of the new NGOs scan the environment and flock to whatever sectors seem to offer the best opportunities for securing donor funds in the short term. Observers have noted the emergence of a large number of "brief-case NGOs" (i.e. agencies run by one or two persons and driven primarily by the opportunism of their leaders) (Kiriwandeniya *et al.*, 1997; World Bank, 1995. cited in Shaw, 1999).

Current estimates show that the number of NGOs in the country varies from around 300 to several thousand but only two, Sarvodaya and the SANASA movement, have nationwide coverage. These programs are not primarily a poverty reduction program but most of program members are low-income people. The small size, inexperience and financial weakness of many NGOs limit their ability to design and implement complex projects (Shaw, 1999).

However, these NGOs were with little experience in or commitment to participatory development and had a poor understanding of basic social mobilization concepts and approaches. Few had a convincing strategy for maintaining their programs after the termination of NDTF. However, In the case of Sri Lanka, those considerable spatial imbalances exist in rural and regional development, and also local and regional variation in its geography, economy and society. The Western

Province's total GDP in 1995 amounted to 43.3 percent. Its share in the manufacturing sector increased from 56.8 percent in 1981 to 72.4 percent in 1995. But in the same time, the Central Province contributed 9.7 percent to the GDP, and Uva and North Central Provinces were 5.1 and 6.4 percent respectively (see appendix C). However, infrastructure development in the Southern, Central and North Western Provinces is more developed than other regions in the periphery. The development problems and potentials of different regions are also not uniform, and even the same areas different society. This diversity makes most centrally-determined, uniform, and all-embracing general solutions to the problems not only inadequate, but also inappropriate (Gooneratne, 2001). The polarization of Colombo as the core area has become one of the major regional development issues in the country.

In 1977 more liberalized economic policy aimed to develop the whole country, but its benefits were limited to the Colombo Metropolitan Region, and do not appear to be spreading to other regions. More and more industrial and service centers are being developed in Colombo; people have migrated to the Western province from the remote rural areas. Because the rural development policy gives less support to the industrial-based production sector, rural people are suffering unemployment or underemployment. On the one hand, compared to other regions, Colombo is the more developed. But on the other hand half of the city population is living in the low-income settlements.

There are many Sri Lankan government development projects that aim to improve the living conditions of local people. These policies on socio economic development are to promote domestic production, industrialization, education, health services, and other service sectors. Among the attempts at social economic development one of the most significant has been the development of the major land settlement and large multipurpose irrigation schemes such as Mahaweli Development Scheme additionally, land reform has been aimed at benefiting the poor. Despite such progress in human development, Sri Lanka has continued to have a high incidence of poverty over the last decade, with about 30 per cent of its population living below the poverty line.

2.3 Perspectives of Poverty and Specific Context in Sri Lanka

Poverty has many dimensions and definitions. The most commonly used and probably the easiest to measure and understand is that of income poverty. Those not obtaining an adequate income for their needs are defined as the poor. However, poverty can be perceived, defined and analyzed in various ways. This definition was dominated by Western ideology for the model of development in the Third World. Also they are poverty is defined in accordance with economic growth, the urbanization process, social development and overpopulation in the Third World.

However, who are the poor? In different cultures and languages it is such that, all in all, everything and everyone under the sun could be labeled as poor, in one way or another (Rahnema, 1992). There may be as many poor and as many perceptions of poverty as there are human beings. Remenyi's (1994) study remains to date, the most detailed analysis available on poverty. This study identified that we all have a natural tendency to believe that we know what it means to be poor, and that most of the poor people, homeless refugees, vulnerable children, and families are bereft of assets, education, good health or opportunities for self-help. However, for the great majority of the poor people in the Third World, the everyday reality is quite different.

Following in the broad tradition of underdevelopment theory, Michael Lipton's theory of 'urban bias' and an explanation for distorted, uneven development in the "Third World", has generated considerable debate among writers on the left. Lipton believes that the main reason why development is held back in the Third World, and 'why poor people stay poor', is because of the existence of parasitical and corrupt urban elites (Lipton, 1977).

Sen (1981) has described this disjunction between supply and effective demand as the entitlement approach to poverty analysis. The people can starve in the midst of plenty of food as a result of a collapse in their means of command over food. Undue emphasis on aggregate food availability, Sen argues, diverts attention from the more fundamental issues of how particular individuals and groups of people gain access to and control over food. Thus scarcity is the characteristic of people not having enough..., it is not the characteristic of there not being enough.

While the latter can be the cause of the former, it is one of many causes (Sen, 1981. 1). Sen mentions that ownership relations are one kind of entitlement relation. It is necessary to understand the entitlement systems within which the problem of starvation is to be analyzed.

Moreover, this applies more generally to poverty as such and more specifically to famines as well. Absolute lack of resources may be only one of a number of reasons for people not gaining access to the resources they need for sustaining livelihoods. He also mentioned that "poverty implies the inadequacy of exchange entitlement" in respect to the affected social group (Sen, 1981). This would be primarily a case of lack of access to jobs and income-earning opportunities, and inability to generate the above-poverty-line income. These entitlement relations may be based on processes such as production, own-labor, trade, inheritance or transfer. His concern was therefore to examine how different people derive entitlements from their endowments and so improve their well-being or capabilities.

Chambers (1983) revealed that poor people have to struggle against five interlocking disadvantages, which trap them into deprivation. Those disadvantages are poverty itself, physical weakness, isolation, vulnerability and powerlessness. Poverty contributes to physical weakness through lack of food, small bodies, malnutrition, inability to pay the cost of schooling and the like. Physical weakness also contributes to poverty in several ways such as low productivity owing to weak labor, inability to cultivate larger areas or working longer hours. Due to physical weakness, the poor become isolated which results, for instance, in lack of education, and remoteness, being out of contact, etc. Powerlessness also contributes to poverty in many ways. These five disadvantages are the key problems interrelated with each other to which many face difficulty in finding solutions.

Income poverty itself has at least two dimensions: absolute and relative poverty. Webster (1990) explains that absolute poverty is then fairly easy to define in objective though gruesome terms. Absolute poverty describes a situation in which people barely exist, where the next meal may literally be a matter of life or death. For one fifth of the people in the world, absolute poverty is related to low levels of nutrition, health, housing, clothing and opportunity. The recognized nature of poverty led academics, development agencies, and some aid donors in the North to propose a different approach to the Third World development known as the 'basic needs strategy.' According to Webster (1990) the basic needs strategy seeks to do two things. First, is to relieve as quickly as is possible the absolute poverty through intensive direct assistance to those in desperate circumstances. Second, is to meet the basic needs of all in terms of material needs such as food, clothing, shelter and fuel, and social needs such as education, human rights and 'participation' in social life through employment and political involvement.

The subsistence concept of poverty is based on an estimate of the level of money necessary for buying food to satisfy the average nutritional needs of each family. This concept has dominated official policy in Western Europe and the United States since the turn of the 20^{th} century. Nevertheless a number of problems emerge in this approach. The critics of the subsistence approach challenge its simplistic assumption that the basic needs of an individual or family can be determined merely through an assessment of the biological and physiological demands of the human body (Webster, 1990).

Chambers (1997) suggests several criteria for understanding poverty. There are disabilities, lacking resources such as land, live-stock, farm equipment, being unable to send their children to schools, bad housing, children labor, access to only low-status work, food security for only a few months each year, and lacking social support, being single parents, and dependence on common property resources. These criteria give significant insight to characteristics of poor people, and seem to be a tragedy in a human life. Most of these characteristics are inter-related with the problem of low income due to low saving, low investment and low production. That is the cyclical process commonly known as the "vicious circle of poverty". Some criteria that signify characteristics of poor people are a tragedy in a human life, when describing the nature of poverty.

However, most of the development policies were formulated by international aid agencies in tandem with Third World government. In the 1950s and 1960s the more developed countries believed the main way of reducing world poverty was through economic growth. They assumed that rising GNP levels meant real growth whereby poverty would be eventually eradicated. While a number of countries' per capita income had improved, the population's standard of living did not improve. Indeed, over the period in question, more people joined the ranks of hundreds of millions already suffering from absolute poverty (Webster, 1990).

Economic growth is most often believed to be the pathway toward poverty reduction, but while in general and in the aggregate, growth goes together with poverty reduction, and it is not possible to say how this relationship works out in practice for any particular country, region or community (Krishna, 2004). It's noted that poverty applies to individuals and households, whereas development also refers to large-scale processes of change at the community level. The World Bank measures a person's income and establishes a poverty line which represents an income level below which a person is held to be in "extreme poverty."

Defining and measuring poverty is a difficult task. The global target for reducing poverty uses a single poverty line for the whole world, income less than US$ 1 per day. Poverty clearly does not only mean a lack of income, falling below a poverty line necessary for the purchase of a minimum basket of commodities for basic nutrition, or for the purchasing power parity at which local currency is standardized in 1985 dollars enough for a person to buy minimum commodities to sustain life–often set at $1 or $2 a day (Bush, 2004). The World Bank also measures the level of development of different countries with the gross national product (GNP) per capita to measure the average income based on market valuations. GNP per capita says nothing about the distribution of wealth between the rich and the poor and underestimates both subsistence and collective goods.

These simple poverty indicators such as income (see Table 2.1), while easy to record, tell us nothing about why people are poor or what they might do to overcome their poverty. The World Bank includes other factors, such as nutritional status, life expectancy, under-five mortality, and school enrollment rates in what are termed the Priority Poverty Indicators.

Table 2.1 Poverty Indicators

Dimension	Indicator
Economic	
Income	Number of people below poverty line
Social	
Nutrition	Calorie intake
Sanitation and water	Access to potable water
Energy	Access to electricity
Health	Access to primary health care and reproductive services, under 5s mortality
Education	Access to primary education
Enabling environment	
Access to means of production	Participation in decision making capital availability Access to technology and information
Vulnerability	Marginal areas (esp. Slums, hillsides) High environmental hazard Insecurity (intimidation, crime, conflict) Isolation and alienation
Isolation	Poor market and poor infrastructure

Source: Gunawardena (2005)

The Department for International Development's (UK-DFID) White Paper (1997) builds on these indicators to include gender equality in education, access to reproductive health services, democratic accountability, protection of human rights, and environmental sustainability. Ultimately, however, people's own perception of their poverty is most important and participatory poverty assessment is now gaining acceptance as a methodology. More recently, enabling environmental indicators such as access to means of production, vulnerability, and isolation are being considered (Henninger, 1998, cited in Jones, 1999).

However, poverty alleviation has re-emerged as an important item on the agenda of global development. Changes in the political and ideological climate during the last two decades pose major challenges to how anti-poverty strategies are conceptualized and implemented. The 1980s, an era of fiscal belt-tightening in both the South and the North, saw a shift in the approach of major multilateral agencies, away from redistribution and basic needs and towards structural adjustment and market-oriented economic reforms. By the 1990s, a new poverty agenda had surfaced (the World Bank's *World Development Report* 1990) as a counterpart of the so-called 'Washington Consensus' on structural reforms.

The basic principles of this policy have been endorsed by most development agencies, and widely adopted for the development of poverty reduction solutions (Moser, 1998). This new agenda stresses the importance of market-led growth itself as the most important method to address poverty. The role of the state, and of focused anti-poverty strategies, is viewed as secondary in this approach. The state's role is limited to policies in selected social sectors such as health, education, and to programs focusing on safety-net provisions for the vulnerable people. To the importance of understanding issues of opportunity, empowerment and security in the World Bank's *World Development Report* (2000) reported this new language is mostly concerned with efficiency of markets, economic liberalization, and the importance of social and human capital, where education and the knowledge economy are intended to provide the umbrella under which the forces of globalization operate.

Another recent trend that has been more positive, especially during the 1990s, is the greater visibility of gender concerns through the series of UN global conferences. These conferences have become an impetus that has strengthened networking and joint action. There are conceptual and institutional challenges to engendering poverty reduction strategies and programs. The challenges that institutions face operate at different levels, including global, national, and local depending on the level at which the institution itself functions, and the strategies it espouses.

According to these definitions, poverty could be identified as a multidimensional phenomenon, encompassing inability to satisfy basic needs, lack of control over resources, lack of education and skills, poor health, malnutrition, lack of shelter, poor access to water and sanitation, vulnerability to shocks, violence and crime, and lack of political freedom and voice.

Poverty is not a problem of the few in the tropics; it is a normal condition of the bulk of people hence, while the absolute poor must be targeted as beneficiaries of development, a further 40-50 percent of the population of the Third World can claim that development has not banished their poverty. They ought to be targeted as beneficiaries of successful development.

In the shopping list of policy reforms intended to improve income distribution and reduce poverty, very little is said about the people who are poor, how they are identified, how they express their grievances at being poor and how, under whatever circumstances by which poverty is to be reduced, the essential driver of such a strategy must be the women and men who are poor. They, moreover, must be seen as agents of social change rather than just victims of exclusion (Jordan, 1996).

Recently, in terms of the political and economic regime, poverty should be viewed from the perspective of a specific nation or region with its own development needs. Countries in South Asia have a long experience of being colonized, so the influence of the Western European ideology is more or less a matter of course. The process of development is imposed accompanied by modernization bringing about wealth, and economic and commercial growth in the city center. The state development policies and programs have been helping the poor, but poverty remains serious. The so-called modern cities contained all the advantages and extravagances of European urbanization together with the additional disadvantages of general poverty (Gilbert and Gugler, 1992).

However, many of the practices and policies in place have not been adequately impacting on poverty. The issue of poverty, and particularly of poverty alleviation, has been given much emphasis in various international and national arenas, since the declaration of the Millennium Goals by the United Nation in 2000. The declaration focused strongly on alleviating world poverty within the next decades. The World Bank has also supported this goal by taking up poverty as a key issue in their World Development Report (2000/2001), under the aggressive title of "Attacking Poverty." Indeed, the World Trade Center terrorist attack in 2001 has added yet another dimension to the issue of poverty, with some countries maintaining that sustainable and appropriate development could be a further strategy to prevent terrorism and violent conflict (Marcus and Wilkinson, 2002).

This means that how poverty is defined and understood is to be further debated. There is, without doubt, an increased acceptance nowadays, that poverty is not solely about economics and that one has to go well beyond purely economic terms in order to understand the processes and causes of poverty.

However, income and consumption based concepts are still widely used to identify the poor and to design poverty related project interventions. Marcus and Wilkinson (2002) also point out that most countries still apply a rather static measurement of poverty: while poverty statistics were sometimes disaggregated into poor and extremely poor..., the distinction between chronic and transient poverty was never mentioned, nor was the meaning of vulnerability in a particular country, region or social context spelt out.

Researchers within the poverty sector have to investigate such distinctions of poverty if they are to help governments and other national and local agencies to identify and use innovative and effective poverty alleviation strategies based on real understandings of poverty processes and experiences (Marcus, 2003). Whereas the concept of poverty has been expanded in many ways beyond solely economic considerations, new elements have been recognized as being crucial to sustained poverty alleviation at national levels. This has also contributed to significant changes in the ways poverty has been conceptualized by major donor agencies over the last years. Marcus (2003) show that discussion on "new" poverty concepts by agencies such as the World Bank, Asian Development Banks and UN circles more or less focus on three main key components: pro-poor growth, good governance, and social development. These components point towards many of the necessary factors for sustained poverty alleviation efforts; it is doubtful how far the above components actually improve the design and implementation of poverty alleviation strategies.

All these considerations hold for a Sri Lanka that has long been regarded as a model for successful welfare policies and government provided social security measures that have led to comparatively good social indicators of literacy, life expectancy, fertility decline and low infant mortality (Jayasuriya, 2000).

However, the validity of the current measurement of these indicators is being increasingly questioned, considering the confused political and socio-economic past of Sri Lanka over the last 2 decades. Globalization and the introduction of liberalization and open economic policies created new social and economic opportunities, but have also had various negative effects on local economics (Jayasuriya, 2000, and Kelagama, 2000). An intensifying violent conflict with the Tamil separatist movement in the north and east as well as youth unrest in the south would most certainly have jeopardized developmental achievements of the past (Arunatilake *et al.*, 2000).

Notwithstanding the long history of programs for poverty alleviation in Sri Lanka, the population below the poverty line remains significant. On the one hand, politicization of poverty alleviation programs has problems. This may lead to situations in which the genuinely poor are excluded while the non-poor are included. Although it is noted that some 2.1 million households benefit from the Samurdhi program (Central Bank, 2000), recent research finds that the program does not assist some 40 percent of the poorest income quintile at all. This suggests that the program both misses a large number of the poor and provides benefits to many non-poor households. On the other hand, lack of congruence between macro and micro development policies have surfaced from time to time (Karunanayaka, 2001).

At present the government is concerned with the adoption of a more inclusive strategy for poverty alleviation and this finds expression in the policy document titled 'Sri Lanka: A Framework for Poverty Reduction of the National Planning Department' (2002). It points out that the past efforts aimed at combating poverty have not altogether been successful and hence the need for a more inclusive approaches to alleviate poverty (Markus, 2003).

2.4 The Poor in the Formal and Informal Sectors

The distinction between formal and informal has become the standard way to characterize urban labor markets in developing countries (Soest and Pradhan, 1995). Commonly, the urban poor profile popular notion that the urban labor market may conveniently be separated into "formal" and "informal" sectors. These sectors are taken to be largely without linkage to each other and are thought to possess characteristics that, in stylized fashion (Linn, 1987), can be summarized as Table

2.2. It is shows that different and much more complex picture than the simple dichotomy between formal and informal labor markets.

Linn (1987) also noted that the concept of formal is based on the employment of waged labor within a framework of rules and regulations, usually devised and implemented by the state, based on working hours, minimum wages, health and safety at work, or the social security obligations of employers and employees. Jobs in the formal sector are relatively secure and in return for regular wages/salaries, individuals contribute to the public good via taxes on their earnings that are used to provide public services, such as health or education. However, the vast majority of the poor's labor force is self-employed and nearly 35 percent are engaged in casual wage work. In other words, the urban poor are mostly employed in self-managed low paid jobs in the informal urban sectors.

Table 2.2 The Conventional View of the Urban Labor Market

Formal Sector	**Informal Sector**
High and middle income	Poor and very poor
Low unemployment	High unemployment
Industry, business, government	Artisans, services, petty trade
Large-scale operations	Small-scale operations
Wage employment	Self-employment and family employment
High-skill employment	Low-skill employment
Restricted entry	Easy entry
Regulate	Unregulated
Taxed	Untaxed
Native population	Recent migrants
Productive employment	Residual (unproductive) employment
Mainstream	Marginal

Source: Linn, 1983

Gugler (1982) and Riddell (1978) widely accepted that informal sector is marginal and isolated, and a relatively nonproductive artifact of an old, traditional way of life. Workers in this type of employment are labeled as "under" or "misemployed" (Gugler, 1982). "Casual work" in temporary jobs, street vending, and work in family enterprises are characterized by "the underutilization of labor" and represent "underemployment," while "misemployment" is work done in socially useless jobs. According to Smith (1996) recent research on Third World cities suggest that viewing the formal sector as nonproductive is inaccurate.

The concept of an "informal" economy is possibly much easier to grasp than a definition, about which much divergence persists. There is agreement, however, that it incorporates legal and illegal activities and is a very significant part of the labor force in the mega-cities in the developing world. While the measurement problem is not insignificant, most observers agree that the informal economy is large and growing and it will be an enduring feature of the economy of mega-cities for some time (Los *et al.*, 2002).

However, the informal sector has emerged in the process of state development. The sector includes many kinds of job: petty traders, drivers of non-public and privatized public transport services, street vendors, domestic workers, small factory workers, self-employment and so on. In the major cities of the low-developed countries streets are cluttered with tens of thousands of workers in the informal sector who eke out marginal existences in jobs with long hours and no fringe benefits. Families barely manage to make ends meet by having all able-bodied members, including women and children, participating in such employment (Berenmann, K. *et al*, 2002).

There are a number of arguments on the reasons why the informal sector is important as a focus for development study. Hart (1973) emphasized the great variety of both legitimate and illegitimate income opportunities available for urban poor. Subsequently McGee (1976) explored various approaches towards what he called the 'proto-proletariat'. The response to Hart's statement that a historical, cross-cultural comparison of urban economies in the development process must grant a place to the analysis of 'informal' as well as 'formal' structures was nothing less than overwhelming. Linn (1983) argued that urban open unemployment is not the primary cause of the urban poverty.

The urban poor cannot afford to remain without some form of employment, since they do not have any alternative source of subsistence. Some younger members of family in both the poor and middle-income groups are relatively well educated, but they engage in low salary occupations or like training. In the last few years, there has been a return to the facilitator approach to the informal sector that characterized the approach of the International Labor Organization (ILO) in the early 1970s. The 'new right' perceives the informal and formal sectors as complementary, and distinguished by the institutional mechanisms which prevent informal-sector access to markets and resources. It places the problem of employment and wealth creation in the informal sector.

Gilbert and Gugler (1992) believes that the informal sector is "only functional to the needs of capital in specific circumstances", and describes the 'normalization' process as that which demands "a shift to a more flexible relationship between labor and capital, so that labor can be absorbed or discarded in a more sensitive response to economic market forces." Gilbert and Gugler (1992) characterized the informal sector in urban areas as a denial occupation from the government's viewpoint. They support Hart's argument in the notion that the informal sector provided a range of low-cost, labor-intensive, competitive goods and services. According to them, the informal activities are ease of entry, reliance on indigenous resources, small scales of operation, labor intensive and adapted technology, skills acquired outside the formal school system and unregulated and competitive markets. These informal activities are largely ignored, rarely supported, often regulated and sometimes actively discouraged by the government. The characteristics of formal sector activities are opposite compared to these informal sectors.

Many formal sector workers enjoy a measure of protection through legislation and collective bargaining. Their wages and benefits, working conditions, job security, and social security coverage as a rule, compare favorable with those of other workers. Most of the poor, low level, formal sector employment includes occupations such as cleaners, garment factory workers, municipal council and water supply board labor, state sector official aides. The informal sector provides the answer to the urban employment problem, which is reinforced by the notion that it receives little support from government.

However, these who work in the informal sector may face unemployment because of its insecurity from the government's protection in a competitive market economy in the urban sector. More generally, while formal-sector firms typically enjoy privileged access to credit, foreign exchange, and tax concessions, entrepreneurs in the informal sector can be seen to enjoy competitive advantage vis-à-vis large-scale industry in so far as they escape taxation, social security levies, and government regulation of wages, working conditions, and job security. Also the informal sector is usually against the law, in some cases by occupying roads or public spaces.

Many scholars have observed that informal sectors are playing a very important role in the urban economy, especially for low income people who obtain their main income from the informal sector. They show that the informal sector is a supplier of job opportunities to the urban poor and is a cheap supplier of services to the urban population. This means that these services are not simply the underemployment of poor unskilled people, but a necessity for society.

Moreover, income from the informal sector is important for poor households. Under rapid socio-economic change, people in rural society have diversified their economic activities, because it is so difficult to survive on only a farming income. In the case of a mining community in South Africa, income from mining, that is, men's earnings, was not enough to support the whole household (Batley, 1992, cited in Gilbert 1992). Other income sources, such as women's work, have been important in households. Their work in the informal sector was quite significant for the household economy in that mining community. When we focus on the issue of poverty, it is crucial to examine the several sources of income and its value in a household. Sometimes income from the informal sector may be very small, but it is important for household survival.

However, informal sectors are also difficult to maintain. On the one hand, there is insecurity of employment because of little protection under the law, and on the other hand, workers such as petty traders are unsure of their day-to-day earnings.

In commonly, most of the poor migrants move to urban areas for economic reasons. When people are asked why they moved, they usually cite the better prospects in the urban economy as their chief reason.

The informal sector is significant as a gender issue because many women work in this sector than men. Nelson's (1988) detailed study of the economic activities of women in a squatter settlement in Nairobi shows women to be much more restricted than men in their choice of economic activities (cited in Gilbert and Gugler, 1992). Women are easily involved in the informal sector because it needs skills which women use in their daily lives (Diem, 2003). Also those who live in urban communities have a low income and mostly work in the informal sector that needs little skill and capital.

However, in Sri Lanka a number of social, cultural, economic and religious prejudices prevent the full participation of women on equal terms with men United Nations, 1993). Since the manufacturing industry was established in Sri Lanka, many unmarried people (especially women) have been employed in factories which can be regarded as a formal occupation. But in the Free Trade Zone industries where women workers predominate, exploitation in forms of longer working hours, inadequate pay and rest periods, and lack of basic welfare amenities is evident (Kottegoda, 2000). More young men and women are now entering the labor market, attracted by the incentives of the modern sector. The lower grade occupations appear to be taken up mainly by the low-income groups from both the rural and urban sectors. Self-employment is a significant development among both employed males and females. However, most of the activities carried out by the urban poor represent "residual," "unproductive," or "superfluous" employment (Kottegoda, 2000). Many poor are employed in modern sector activities, although at low wages and with low productivity.

2.5 Livelihood of the Urban Poor

The livelihoods approach is a generalization of the more established literature on poverty and provides a way of thinking about the scope, objectives and priorities of development. Most commonly understood livelihoods approached as means of gaining a living. However, there are various debates on livelihood. Chambers and Conway (1991) argue that a livelihood comprises "the capabilities, assets and activities required for a living. According to Carnev (1998), a livelihood comprises the capabilities, assets (including both material and social resources) and activities required for a means of living. A livelihood is sustainable when it can cope with and recover from stresses and shocks and maintain or enhance its capabilities and assets both now and in the future, while not undermining the natural resources on which it is based (Carney, 1998, cited in Korf, 2003). However, according to a more recent definition, the term livelihood is not just what people do in order to make a living, but the resources that provide them with the capability to build a satisfactory living (Ellis and Freeman, 2005).

Chambers and Conway (1991) show that household livelihoods depend on household assets that include: tangible assets (resources and stores) and intangible assets (claims and access). Most poverty analysts increasingly seek to understand what the poor have, rather than what they lack, examining the nature of these assets. Moser (1998) points out that asset ownership is closely linked to vulnerability. Vulnerability in urban areas also appears to be diverse and highly complex (Moser 1998). The more assets people have, the less vulnerable they are, and the greater the erosion of people's assets, the greater their insecurity.

However, the asset ownership/vulnerability debate has mainly concerned the rural sector. Therefore, in the context of an urban study it is also important to identify any distinctive features of urban vulnerability deriving from the particular assets that the urban poor control (Moser, 1998).

In recent years, Sustainable Livelihood Analysis (SLA) has emerged as an alternative way of conceptualizing poverty alleviation, including its context, objectives and priorities. It focuses on one of the most fundamental aspects of life: the ability of people to support themselves, both now and into the future. SLA takes into account the range of tangible assets and largely invisible intangible assets necessary to build a livelihood, identifying five types of 'capital' or core assets (DFID, 2000).

According to the Department of international Development (2000) building a livelihood requires to some extent inclusion of all five. "Human capital" denotes skills, knowledge, good health and ability to work. Health status determines people's capacity to work, skills, and education, which determine the return to their labor. Human capital is a factor of the amount and quality of labor available. "Social capital" refers to formal and informal social relationships, including their degree of trust, social networks, membership of groups, and access to wider institutions of society upon which people draw in pursuit of livelihood. "Natural capital" consists of natural resources, including their flows and services. "Physical capital" refers to producer goods and physical infrastructure. "Financial capital" includes financial resources such as pensions, saving, supplies of credit or regular remittances or pensions, which provide them with different livelihood options.

Korf (2003) shows that the strength of the livelihood frame compared to earlier development frameworks is that it emphasizes people's potential in a holistic way rather than concentrating their problems, constraints and needs. However, there are close relationships between these assets and they constitute a system of livelihoods. Therefore, a livelihood itself is dynamic. Changing one factor in the system leads to changes of the whole system.

Moser (1998) indicate that the three generalized characteristic of urban life often identified as differentiating urban from rural areas are levels of commoditization, environmental hazard, and social fragmentation. The highly "commoditized" nature of the urban sector means that labor is the urban poor's most important asset, generating income either directly in terms of its monetary exchange value through wage employment, or indirectly through the production of goods and services which are sold though informal sector self-employment activities.

Also the urban households pay for their food and shelter rather than rely on their own production and more dependent upon purchasing services such as transportation and education. In the urban context housing is an important asset that generates income through, for instance, renting rooms and the use of its space for home-based production activities. While the urban poor may benefit from public sector services provision, poor quality housing and inadequate water supplies, sanitation, and solid waste disposal are all environmental risks that often have a particularly serious impact upon the urban poor's human capital, health and well-being (Hardoy *et all.*, 1990). Finally, the urban poor may be particularly vulnerable to social fragmentation. In the urban study, the extent to which economic crisis increases or eroded social capital may have important long-term consequences for a community's ability to create and sustain alternative delivery services if publicly provided services deteriorate (Moser, 1998).

Gender, age and other social differences may significantly affect access to livelihood assets within the household and other groups. When households become poorer, the common response was for more women to join the labor force. The urban study shows that household asset stocks are the net result of accumulation over time. The understanding and perception of livelihoods between men and women are quite different. Therefore, livelihood strategies are constructed differently by gender (Hart, 1986).

However, Livelihoods are not simply a localized phenomenon, but connected by environmental, economic, political and cultural processes to wider national, regional and global arenas. It is clear that livelihood strategies of local people are diverse and flexible. Livelihoods are not something that already exist, but they have been constructed and reconstructed in the ways local people synthesize their practical experiences by combining livelihood resources. Livelihoods strategies are what people perceive and know about the environment, ecology and society. The question of a livelihood's capacity for sustainability involves evaluating current circumstances and assessing future trends, as well as past conditions and patterns.

2.6 Participation, Empowerment and Gender in Poverty Alleviation Program

The concept of 'participation' in itself has various understandings and points of view. In recent years, many governments of the developing countries, international organizations, and NGOs have paid more attention to local people's roles in development projects and environmental management in which participation is a key word. Participation is usually used as an umbrella term to refer to the involvement of local people in development activities, often NGO-based. One of the key routes through which empowerment is meant to be achieved is through 'participation.' Grassroots development is often termed 'participatory, but it is important to recognize what this means. Participation can take place in a number of ways and at different stages in the setting up of development projects. NGO practitioners and researchers nave begun to use a range of different methods in order to find out more about the understandings local people have of a range of topics.

During the late 1980s and into the 1990s the discourse about community has been complimented by an increasingly ubiquitous discourse about 'people's participation' and 'empowerment'. When the concept of popular participation was initially advanced by its promoters as a key element in creating an alternative, human-centered development, it was intended to perform at least four functions: cognitive, social, instrumental and political function. Popular participation was to carve out a new meaning for a common search for popular knowledge (Polanyi, 1957). Most definitions are similar, in principle.

In the present context, to borrow from Polanyi's (1957) description of the modern economy, participation has come to be disembodied from the socio-cultural roots which had always kept it alive. It is now simply perceived as one of the many resources needed to keep the economy alive. Moreover, the concept is further refined as "popular participation" capable of saving the development from its present crisis and giving it new stamina to enable the grassroots population to regenerate their life.

According to Lele (1975) participation means that, in its broadest sense, to sensitize people and thus to increase the receptivity and ability of rural people to respond to development programs and to encourage local initiatives as well. The United Nations Research Institute of Social Development (UNRISD), point to "participation" as an actual social reality (UNRISD, 1980). In an earlier UNRISD report (1975), popular participation is defined as "a process of activities... comprising people's involvement and decision-making, contributing to the development efforts and sharing equitably in the benefits derived there from". However, several definitions of participation have been offered.

The concept of popular participation was broadly conceived, it is not only required the creation of opportunities for political involvement but the adoption of measures that would enable ordinary people to share fully in the development process Wolfe (1982). According to Rahnema (1992) the words 'participation' and 'participatory' appeared for the first time in the development jargon during the late 1950s. Recently, people's participation has become the more central issue and people are urged to participate in the events and processes that shape their lives. Facilitating 'people participation' is now on the agenda of most international development institutions. However, the increasingly widespread acceptance of the idea of participation suggests that it has been severely diluted and has lost some radical political potential. Government and development institutions are no longer scared by the outcome of people's participation…there is little evidence to indicate that the participatory approach, as it evolves, succeeds in bringing about new forms of people power (Rahnema, 1992).

However Rowlands (1998) has highlighted, 'empowerment' has become one of the key buzzwords in development policy since the early 1990s. The concept of 'empowerment' itself, as reflected in the focus of participatory action research, is rooted in the basic goal of social progress.

The approach of development that evolved in the 1970s slightly altered the concepts of development and participation and established a direct link between the two. Development was defined as economic growth with equitable distribution of the fruits of growth (World Bank, 1995); participation was to be the nexus where people and government met in the process of development. This nexus was to be located at the implementation stage of development projects. Decentralization was the new strategy introduced to ensure participation (Sawter, 1993).

However, the concept of empowerment created important change in the current thinking of rural and urban development, namely a shift from top down planning and bureaucratic implementation to a participatory approach.

Empowerment is the process and the way through which the powerless empower themselves or the powerful enable the powerless. Empowered people have freedom of choice and action. However, the meanings of "being empowered" vary across time, culture and domains of a person's life. Empowerment is a cross-cutting issue ranging from education and health care to governance and economic policy, or all activities which seek to empower poor people to increase development opportunities, development outcomes and people's quality of life (Friedmann, 1992).

In practice, most development program policy is made and implemented by men. 'Empowerment' is a phrase, which is beginning to be used by development agencies. Though, by simply drafting women, for example, programs will do little to empower women. The term 'empowerment' is now used regularly by the World Bank and other sections of the 'development industry' (Ferguson, 1990) to showcase their commitment to popular participation in decision-making for development.

Escobar (1995) also seems disillusioned with the development concept of participation and empowerment, pointing out that development planners and politicians have often tried to manipulate the experience of participation to suit their own ends. Giving full voice to the disempowered sectors of the population tends to follow a certain sequence. Political empowerment would seem to require a prior process of social empowerment through which effective participation in politics becomes possible. For instance, social empowerment, especially when oriented to women, can lead to the release from household drudgeries, and the time thus won, like any surplus resource, can now be variously applied, including to political practice.

As pointed out by Batliwala (1993) the most conspicuous feature of the term empowerment is that it contains within it the word "power". Empowerment is about power and about changing the balance of power. In every society, there are powerful and powerless groups. Power is exercised in social, economic and political relations between individuals and groups. Participatory development takes place when people are empowered with the knowledge and means to decide their own priorities, to improve their own skills, to meet their needs and find their own fulfillment. Therefore, participatory process basically represents the initiative of people seeking life improvements through a process of awareness built up and organized through group actions directed towards self-reliance.

However, Participation is a problematic concept (Stiefel and Wolfe, 1994). They said this is partly because it is contrary to the dominant individualist, consumer basis of society, and contradicts the socialization of many people. Another problem with participation is the problem of tokenism (Ife, 1995). The history of community participation projects is riddled with examples of tokenism, and people have rightly learned to look on exhortations to community participation with extreme skepticism, as most people have better things to do with their time than to spend it in token participatory exercises. This will inevitably take time, and it must be achieved quickly; it is a slow, development process. Despite the difficulties of achieving genuine participation, here are a number of ways in which participation can be encouraged. It is important to emphasize that non-participation is not natural, nor is it necessarily inevitable that people will participate in community structures, under the right conditions (Ife, 1995).

Cooke and Kothari (2001) talk about participation being the 'new tyranny' in development work. What they mean by this is that development policy and 'participation' and participatory approaches' are encouraged by multilateral organizations such as the World Bank. But, Francis (2001) suggests that these are ideas which have been taken on board, and the dimensions of participation that could challenge existing practices and power relations are not engaged with (Willis, 2005). When individual projects are examined, the limitations of the participation discourse become apparent.

In the present context, Willis (2005) shows that far too often this form of participation is not achieved. Instead local people are involved in meetings or contributing labor, but this is not participation in the wider sense which can be linked to empowerment. Willis (2005) also shows that truly participatory development projects come from the pressures of the so-called 'development industry.' This means that many projects are more likely to react to the requirements and favorite topics of the potential donor not local people needs, because NGOs depend on donor funding.

During the late 1980s and into the 1990s in Sri Lanka, the discourse about community has been complemented by an increasingly ubiquitous discourse about "people's participation" and "empowerment". While community has by no means completely disappeared from public and private discourses on development, everyone, from farmers to international donors, has begun to speak the language of "participation" and "empowerment" (Woost, 1997). But Woost goes on to argue, 'the mainstream use of participatory rhetoric in Sri Lanka offers little in the way of alternative development.

Although using the rhetoric of participation and empowerment, the way in which development has been constructed in Sri Lanka 'sets definite limits on people's participation. It does not give them the power to define development for themselves (Grillo, 1997). The problem lies in how the grassroots can empower themselves through participation. Empowerment emerged from unequal power relations in society, and from the conflicts between class and state or the rich and the poor. Some state agencies and government propose a "top-down" approach that views the marginalized people as the powerless; but NGOs and some development agencies insist on the "bottom up" approach that sees the poor as not completely powerless. The poor have their own potential and capability in the form of local knowledge and local wisdom.

However, in Sri Lanka the poverty alleviation strategies so far have failed to integrate their outcomes or to eliminate the causes of poverty, which keep reinforcing the conditions that result in impoverishment. The participatory development programs are mainly aimed at sustaining the poor by granting cash transfer until they are able to rise out of poverty through compulsory saving components of the program. To enable the poor to become entrepreneurs the credit facilities are made available, which are in inaccessible to the ultra poor through the market (Wickramasinghe, 2004).

The problem remains, however, that participatory processes are often undertaken ritualistically by development agencies and NGOs and that those processes have turned out to be manipulative, or even harmful to 'those who were supposed to be empowered' (Cornwall, 2003). These 'new forms of people power' relate, in part, to local experiences of governance and development and the politics of everyday challenges to the establishment (Power, 2003).

In recent decades, the issues of gender equality and empowerment of women have been given increasing attention in national and regional development efforts. By the end of the twentieth century, all approaches to development involving a focus on women had been amalgamated into a Gender and Development (GAD) approach (Young, 1987). Based on the concept of gender (the socially acquired ideas of masculinity and femininity) and gender relation (the socially constructed pattern of relations between men and women) they analyzed how development reshapes these power relations. Drawing on feminist activism, gender analysts explicitly see women as agents of change. Gender relations are those socially, culturally and psychologically constituted relations between men and women which are shaped and sanctioned by the norms and values held by members of the society concerned (Showalter, 1989).

However, the development process affects women and men in different ways. The penetration of capitalism, leading to the modernization and restructuring of subsistence and centrally planned economies, often increases the gender-based disadvantages. Nevertheless, gender is a widely used and often misunderstood term. It is sometimes conflated with sex or used to refer only to women because women are more marginalized in our society than men (Kabeer, 1994). For example, although a majority of the better-paid jobs involving new technology go to men, male income is less likely to be spent on the family. Women often lose control over resource such as land and houses. By comparison, men tended to be more concerned with political risks such as terrorist activities and harassment by government and city council officials. These factors include women's limited roles in household decision-making (including decisions regarding the use of their own income), limited access to and control over household resources (physical and financial assets), and women's low level of individual assets.

Kabeer (1994) also highlights gender differences among microfinance clients that suggest women clients may be more vulnerable than men. Women are burdened with heavy domestic workloads and suffer from limited mobility, knowledge, and skills. Low self-confidence and self-esteem are related factors. However, women experience different risks than men. Women tend to perceive more risks associated with domestic factors than men.

GAD considers WID's view that women's marginalization from the development process was, because of the unequal access to new technologies and skills, as an over-simplification. It points out that capital accumulation separated direct producers from men and women from means of production. Although women had been integrated into the development process, they were integrated only at the bottom of an inherently hierarchical and contradictory structure of production and accumulation. The outcome of this structural process is seen as the formation of different classes and gender relations in society (Amarasinghe, 1999).

They also criticize the Women in Development (WID) approach for treating women as a homogenous category and they emphasize the important influence of differences of class, age, marital status, religion and ethnicity or race on development outcomes. Also, participatory development has generally, like WID, pursued the liberal project of inserting participatory practices of various kinds into conventional development activities, mostly talking implementation (Cornwall, 2000). However, within various approaches have been distinguished such as welfare approach, equity and antipoverty approach and efficiency and empowerment approach, in respect to women they broadly fall.

Development specialist in gender and development recognized that women and men have different needs because they have different roles in society. The development programs aimed at improving socio-economic status of both rural and urban women and currently recognize the necessity of identifying the strategic needs of women that result from the changing gender relations in the society. Most of the poverty alleviation programs designed to grant basic needs to the poor have consciously and frequently tended to provide for practical needs of women. However, the question of who participates and who benefits raises awkward questions for participatory development.

2.7 Defining Micro-finance as a Concept

Microfinance and credit two terms are closely related to each other. Poor people need micro credit for these various and different purposes. It may be to meet the major household expenses; emergency needs or even basic livelihood support. The poor lack the ability to accumulate necessary capital, because they are constantly struggling to fulfill their basic needs (Singh, 2002).

There are two main systems of microfinance, one is formal and the other is informal. Both of the systems have their own positive and negative aspects. The positive of the formal financial system is that loans are available at low rates of interest with easy and periodical repayments and with moratorium periods. Also the most important aspect of this type of credit is that it is available for income generating activities. But at the same time micro-credit from the formal financial system is not easily available. Because the system requires collateral or security, it has complex legal and operational procedures, involving a lot of paper work. The credit is not available in time. Moreover, there is a stigma attached to the poor people so that the bankers do not think they are credit worth and feel that the recovery rate is unsatisfactory.

The positive aspect of the informal system of micro-credit is that the credit disbursement is easy and relatively quick. No collateral is required and there is less paper work. Credit can be given for any activity, especially for consumption and emergency purposes. Credit is generally given for non-productive purposes as well. But the negative aspect of this system is its very high interest rates. Exploitation is also attached with this system. Moneylenders take repayment at one time only.

However, microfinance was created to somehow combine the positive aspects of both financial systems like low rate of interest, easy process of disbursement, no collateral or security and less paper work etc. In the recent past, microfinance has become a critical component of community development and poverty reduction strategies. In this special issue of the development official statement the advantages and difficulties of implementing effective microfinance programs are explored from a number of different perspectives.

Mayoux (1995:2) has identified two broad models of microfinance: the market model, and the empowerment model. According to him, the market model is a credit-driven model, which has a reduced emphasis on client savings, except as security deposits against loans. The empowerment model is based on a mutual or self-help approach and high levels of group ownership, control and management. It involves small groups of women who collect their own savings and revolve them as credit among their members. These savings are often supplemented by external credit injections from banks or other institutions. This model has lower transaction costs than either the market approaches or those which provide loans to individuals (Puhazhendi, 1995). But Mayoux (1995) argues that the very process of making decisions within the group is an empowering process and so can lead to broader development outcomes, such as the greater participation of women in local government processes. In terms of poverty outreach, the mutual model provides greater opportunities. However, it is not conducive to rapid expansion, as it is savings rather than credit driven, and it has high institutional costs in start-up that in effect are a cost to the donor, which to many would be seen as a subsidy. Also, these models because they are less disciplined and more decentralized, are harder to regulate and monitor, and so represent a greater risk to the donor (Mayoux, 1995).

The Asian Development Bank (ADB) defined it, as "the provision of a broad range of financial services such as deposit, loans, payment services, money transfers, and insurance to poor and low-income households and their micro-enterprises." Most of the microfinance systems are run by NGOs or are using NGO characters by government programs, and recently commercial banks. However these systems practice not only financial intermediation for the poor, but also accomplish much for the poor in terms of economic, social and individual development (Gunatilaka, 1997)

The Declaration of the Micro-Credit Summit held in Washington, D. C. in 1997 defined micro-credit programs as those that "extend small loans to poor people for self-employment projects that generate income, allowing them to care for themselves and their families" (Microcredit Summit, 1997). The Taskforce on Microfinance established by National Bank for Agriculture and Rural Development

(NABARD) in India defines microfinance as the "provision of thrift, credit and other financial services and products of very small amounts to the poor in rural, semi urban or urban areas for enabling them to raise their income levels and improve living standards" (NABARD, 1999). While these definitions essentially seek to foreground the purpose of microfinance programs for the "income generation" through self-employment, the sizes of the financial services offered are "very small amounts" and the target clientele of such programs are "the poor."

The current consensus, aggressively propagated by some of the leading development organizations including the World Bank, the United States Agency for International Development (USAID) and the Department for International Development (DFID), that microfinance based programs constitute the single most effective development intervention that can be universally adapted and may be attributed to the close association of microfinance (Ledgerwood, 1999).

Nevertheless, the Microfinance Handbook produced by the World Bank's Sustainable Banking with the Poor Project states that while the term microfinance refers to the provision of financial services to low-income clients, including the self-employed, many Microfinance Institutions (MFIs) provide social intermediation services comprising group formation, training in financial literacy and management capabilities and therefore the definition of microfinance encompasses both financial and social intermediation. It notes that microfinance activities typically involve small loans, usually for working capital, informal appraisal of borrowers and investments, collateral substitutes such as group guarantees or compulsory savings, access to repeat and larger loans, secure savings products and streamlined loan disbursement and monitoring (Ledgerwood, 1999).

The terms "microfinance" and "microcredit" have, in the course of popular usage. It is not only the goal of reaching financial assistance to a designated target population, but also to encompass a particular set of lending methodologies and transactional technologies with a particular set of lending technologies that primarily comprise lending to neighborhood based "primary groups", "self help groups", or "solidarity groups", so as to reduce transaction costs to the borrower and the lending institution. It is important to note that the organizational structure of the equal group based channel of delivery of microfinancial services is remarkably heterogeneous, assumes diverse forms across the globe and ranges across a spectrum including the Grameen type groups of Bangladesh, the Indian self help groups, and the village banking model prominent in Latin America etc. (Nair, 2001).

As the Microfinance Handbook of the World Bank points out, the MFIs in turn, could be nongovernmental organizations, credit unions, savings and loan cooperatives, government banks, commercial banks, and non-bank financial institutions. Although microfinance and microcredit are often used as interchangeable terms in the literature, it is generally agreed that microcredit or small loans for income-generation or consumption purposes refer to one component of a larger array of microfinance services that could include savings, insurance and other related business development services as well.

The core of microfinance programs goes beyond mere access and distribution of money, to deeper issues of how money is utilized and invested by low-income individuals. It helps in fostering and developing a micro, community-based environment where existing networks and interlinks are strengthened. It is important therefore to understand that microfinance doesn't stand alone, but overlaps on existing developmental activities and helps in their implementation. Micro-finance has brought the poor in large numbers into extensive organizational networks, has promoted savings and provided credit without collateral, and has shown that the poor are bankable.

2.7.1 Micro-finance in the Financial System of Sri Lanka

There are two main financial systems in Sri Lanka; one is formal and the other is informal. According to Berensmann *et al.*, (2002) there are three systems, including the formal, informal and semiformal. The Central Bank of Sri Lanka (CBSL) regulates formal financial institutions. These institutions are made up of a number of commercial banks, savings and development banks and regional development banks, deposit institutions, contractual savings institutions including insurance companies and other specialized financial institutions, including leasing companies, merchant banks, venture capital companies and finance companies. The main actors in the informal financial sector are moneylenders and self-help groups.

A recent study shows that one of the main actors in the formal financial sector is in the field of microfinance. In the formal financial sector, lending activities are focused on large individual sums provided to private and government-owned enterprises in the modern industrial sector. The formal financial sector has undertaken some efforts to become active in microfinance. Among the institutions regulated by the central bank, only banks play a relevant role in microfinance. Mainly, there are two types of banks, which are involved in the micro-finance sector in Sri Lanka: Regional Development Banks (RDBs) and commercial banks.

Regional Rural Development Banks (RRDBs) were set up in 1985 as government institutions with the objective of improving financial services for the rural poor. Legislation in 1997 provided for the creation of RDBs by combining the previously operating Regional Rural Development Banks (RRDBs). One reason for doing this was to conform to provincial boundaries, in line with political decentralization, but the other purpose was to professionalize RDB management, achieve economics of scale, and to reduce Central Bank influence over the operation of RDB's. RDBs in Sri Lanka focus their activities on rural areas. Both commercial banks and RRDBs have been used as conduits for government poverty alleviation programs involving elements of credit. Thus, the Janasaviya program, which operated from 1989 to 1994, included micro-credit disbursed through the state commercial banks and RRDBs, among other conduits (Berensmann *et al.*, 2002).

However, most of the commercial bank were limited to involvement in the microfinance sector, due to the fact that they are unable to assess a clients risk in an appropriate manner. And also the transaction costs involved in processing small and short term loans are relatively high. The other reason is it is difficult for most banks to build up a sound relationship with their small-scale enterprises (SSE) and the poor. For these reasons, the overall commitment to small scale enterprises is generally weak. In addition, lack of personal relationships and high administrative requirements often keep SSE clients from borrowing from banks.

In Sri Lanka, there are 26 commercial banks, two of which are run by the state, six privately organized and 18 owned by foreign institutions. In the commercial bank sector, four institutions play a major role in SSE financing: the two state banks (the People's Bank and Bank of Ceylon) and two private banks (Hatton National Bank and Seylan Bank).

However the Hatton National Bank (HNB) started its microfinance program in 1989, which was called Gami Pubuduwa Upadeshaka (GPU). This has been the subject of a study by the World Bank. The bank wanted to reach three major objectives: social mobilization, improvement of rural savings opportunities, particularly for women and children, and promotion of growing micro-enterprises to enable them to develop into small or even medium-size enterprises. The GPU program is targeted small and micro-savers and the borrowers in rural and semi-urban areas. However, according to figures the performance of the HNB program is better than other commercial banks lending in rural areas (Gallardo, *et al.*, 1997; cited in Conroy, 2000).

One popular form of credit in Sri Lanka is pawnbroking. There are two types of pawnbroker in Sri Lanka, private and public. It is considered the oldest form of lending, and it plays a very important role in the micro-finance sector. Most pawnbrokers are registered and even commercial banks (both government and private) offer pawnbroking services to their clients. Pawnbrokers offer loans against collateral. This collateral can have various forms: household articles, machines or, a means very popular in Sri Lanka, gold. Registered pawnbrokers and banks usually accept only gold as pawned items. The interest rate is below 2 percent (monthly) at banks and 5 percent at licensed pawnbrokers. This rate is much lower than informal moneylenders. The main advantage of pawnbroking is the fact that it is extremely fast. The informal suppliers of micro-credit, however, play an important role in the country. According to Sanderatne and Senanayake (1989) the informal financial sector accounts for an estimated 30 percent of all financial transactions in Sri Lanka.

The term "semiformal" is commonly used as a label for the grey area between formality and informality. Semiformal actors are financial institutions that are not subject to banking laws, though they do not operate within a country's legal system. The most common semiformal financial actors are NGOs and credit co-operatives. These sectors have been a broad outreach and as a rule provided the largest share of small loans. NGOs are usually classified as semiformal MFIs, and operate between the formal level of bank and the often-informal level of micro-credit-demanding micro-entrepreneurs or poor individuals. However, NGOs are sometimes referred to as informal credit suppliers, mainly when the term "NGO" is used to include local, more grassroots-oriented collective organizations. Historically, many NGOs have engaged in distributing subsidized money as "loans." This kind of micro-credit program however, has suffered from inefficiency and low repayment rates (Berensmann *et al.*, 2002).

There are several semiformal microfinance institutions that have been operating in Sri Lanka. The most important financial NGO is the Sarvodaya Economic Enterprises Development Service (SEEDS). It is the economic development arm of the Sarvodaya movement, which mainly works in the field of participatory rural development. This is developed on the foundation of an existing network of "village banks" of which some 250 were operating in mid 1999, with a further 2200 societies altogether serving some 294,000 people.

Nevertheless, Credit cooperatives (CCs) also play a significant role in the provision of finances to poor individuals or entrepreneurs. CCs are organized according to basic co-operative principles, and the members of a credit cooperative provide capital to the CC, mainly equal shares. At the same time, the members can deposit savings. Part of this accumulated, self-generated capital can then be disbursed as loans to members. In country there are two types of cooperatives which play an outstanding role in microfinance; Cooperative Rural Bank (CRBs) and Thrift and Credit Co-operatives (TCCs). Both are regulated by the Department of Co-operatives, not by the central bank. According to Attanayake (1997), CRBs have been an important source of mobilizing savings but have some difficulties in lending money effectively. However, today networks of cooperative rural banking unions operate 1418 CRBs in the country.

The TCCs in Sri Lanka are organized in a national federation, which is known as the SANASA movement. It was founded in 1906 in order to increase financial services in rural areas. Today, SANASA provides a large number of products, e.g. microfinance schemes, insurance, and training facilities, and also more than 8400 primary co-operative societies, which operate 1418 rural bank, mobilize savings and provide loans for income generating activities and consumption (Kiriwandeniya, 1998). However, SANASA is an effective financial institution serving rural communities, including some of the poor, with the potential to increase its outreach to the disadvantaged.

There are a number of substantial and well-performing NGOs providing microfinance in the county. These NGOs are creation for the mainly for religious or social welfare objectives, for example, SEEDS and Janashakthi. In addition, the government has given of the resources for microfinance from the 1989 under official poverty alleviation schemes, such as Janasaviya, the National Development Trust Fund, and the Small Farmer and Landless Credit (SFLC) project. In some cases, official programs have also engendered community-based organizations of a quasi-independent nature which provide microfinance services at field level. Samurdhi is one such organization, which is not strictly an NGO, though sharing some NGO characteristics, and also in previous program experience was based to the Samurdhi Program. The major objective of Samurdhi Bank Union microfinance lending is stated as reducing the "income vulnerability" of the poor.

2.7.2 Relationship of Microfinance and Poverty

Poverty is in many dimensions and it is perceive to be in developing counties. These dimensions of poverty can be broadly classified into three: (1) economic dimension, often measured by the level of income and expenditure, ownership of assets, and employment; (2) vulnerability to risks and income failures; and (3) powerlessness and low social status (Tilakaratna *et al*, 2005).

In the case that microfinance has the potential to impact directly or indirectly on each of the dimension of poverty, it is claimed that microfinance can be an effective instrument to raise income, production and employment of the poor households. Lack of access to credit has been considered as a major obstacle for them to raise their income and production levels.

On the one hand the poor suffer not only from low incomes but also from various vulnerability and risks. They often lack reserves to fall back upon in times of need or buffers to absorb the shocks of income losses. On the other hand it is claimed that microfinance programs facilitate savings among the poorer and provide credit, and insurance services that help the poor to accumulate assets and strengthen their capacity to deal with risks. Moreover, these programs help the poor, particularly the poor women to gain economic and social empowerment such as improving income, assets and employment opportunities, and social networks. Participation in microfinance programs can also help to improve self-reliance, social recognition and social status of the poor.

2.8 Summary

Over the last century, Western conceptions of the world and history have been largely characterized by notions of progress, evolution, and development. Since the Second World War "development" has become the most widely used term. From the time of independence, in the context of development on poverty alleviation in Sri Lanka, the local people have received special concern from the government, and development workers as well as researchers inside and outside the country. They all know well that the country has a high level of human development but low levels of per capita income. Many of the practices and policies in place have not been adequately impacting poverty. This means that how poverty is defined and understood is to be further debated. However, all contemporary poverty discourse in Sri Lanka, be it conservative, liberal or radical, believers that there is a distinct, bounded poverty sector in the economy whose problems can be eradicate throughout economic development but that poverty cannot be eradicated through economic alone.

Nevertheless, by 1990 in the arena of the notion of development, community and people's participation became incorporated into the discourse of mainstream development and poverty alleviation. Many governments and NGOs with a focus on community-based programs and microfinance were able to access donor funding and the state facilitated an environment conducive to implementing income-generating programs and saving and credit schemes at the village level, even today. However, one could find that many people have escaped from poverty while many others people have fallen into poverty. In cause, why some communities and households benefit more from national economic growth, and even less is known about why some others fall into poverty at the same time. The consequences of national policy cannot be traced without a more accurate picture of how people respond and adapt to national policies.

However, in urban context, poverty is different than in rural context. Looking at urban poverty from a national point of view provides a very favorable picture. According to some figures most of the urban population lives in very poor quality housing and in crowded, unsanitary and insecure conditions with a severe lack of infrastructure and access to basic services. Money is the primary variable in all aspects of livelihood. But the culture of poverty view of poverty persists to this day among many low-income groups. However, poverty is beyond their control.