Is Financial Sector Evolution Pivotal in Poverty Alleviation in Sri Lanka?

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The studies in the field of financial sector development have gradually flourished, drawing increased attention from scholars globally. The rich literature posits that financial development is a core requirement in achieving the economic growth of a country. World Bank postulates that the evolution in a country's financial sector ensures capital accumulation via savings growth, mobilization of funds, risk management, and continuous flow of foreign direct investments whilst reinforcing efficient capital allocations leading to economic development. Albeit efficient credit allocations and increased investments correspond to financial development, inequalities in income distribution are often visible in society. Raising the savings rate, mobilising and pooling funds, producing investment information, facilitating and encouraging foreign capital inflows, optimising capital allocation, economic growth through capital accumulation, and technical advancement is essential to the financial sector development in poverty alleviation. The study investigates the impact of financial sector development on poverty alleviation in Sri Lanka. The study adopts a quantitative approach where secondary data are manually collected from 1960-2020. Financial sector evolution was proxied through broad money stock (M3) to nominal GDP ratio and domestic bank credit to the private sector to GDP ratio, whereas poverty alleviation was measured using the per capita consumption expenditure. The study employs Auto Regressive Distributed Lag (ARDL) technique to analyze the relationship between the variables. The co-integration test results of the study depict a long-run relationship between financial development and poverty alleviation in Sri Lanka. The ARDL test results posit that financial development coupled with economic growth lessens poverty in both the long and short run. Further, the Causality test corroborates an optimistic and unidirectional causality from financial development to poverty reduction in the Sri Lankan context. The study results reflect the importance of continuous developments in the financial sector by improving financial accessibility and diversifying financial products while reinforcing the financial institutions of the country aiming at the underserved market segments.

Keywords: *Financial Development, Poverty Alleviation, Sri Lanka*

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Background

The field of financial sector development have gradually flourished drawing increased attention from scholars globally. The rich literature posits that financial development is a core requirement in achieving the economic growth of a country. World Bank postulates the evolution in the financial sector of a country ensures accumulation of capital via savings growth, mobilization of funds, risk management, and continuous flow of foreign direct investments whilst reinforcing efficient capital allocations leading to economic development.

Problem statement

Albeit efficient credit allocations and increased investments correspond to financial development, inequalities in income distribution are often visible in society.

Purpose

To investigate the impact of financial sector development on poverty alleviation in Sri Lanka.

Research question

What is the impact of financial sector development on poverty alleviation in Sri Lanka?

1 NO POVERTY

Conceptual framework

Financial Development → Poverty

(CREDIT/GDP) → Per capita consumption expenditure

(M3/GDP) → Per capita consumption expenditure

Conclusion

The study findings depict the importance of developing government economic policies to implement positive NPV-generating projects to maximize the benefit for the vulnerable parties in society.

Findings

The co-integration test results depict a long-run relationship between infrastructure development and poverty alleviation. The ARDL test results posit that infrastructure development and economic growth lessen poverty in both the long run and short run. the Causality test corroborates a positive and unidirectional causality running from infrastructure development to poverty reduction in the Sri Lankan context.

Methodology

Design22	Quantitative design
Duration	1960-2020
Analysis technique	Auto Regressive Distributed Lag (ARDL) technique
Data collection method	Secondary data
Time horizon	Time series