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**THE RELATIONSHIP BETWEEN SOCIAL EXPENDITURE
AND ECONOMIC GROWTH IN SRI LANKA:
AN EMPIRICAL INVESTIGATION**

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The issue of economic growth versus the social welfare trade-off has received serious attention from economists and policy makers. However, the relationship between these two factors seems to be complex. The Sri Lankan experience would suggest that the government's spending on social development resulted in a positive impact on human development in the country. There is also an argument that the trickle-town effect on economic growth was not experienced. This issue justifies a study to find the statistical relationship between social expenditures and economic growth that can impact correct policy decisions on social spending. Thus, the objective of this study is to examine the relationship between public spending on education, health and social welfare (since these are major components of social expenditure); and economic growth in the long run for Sri Lanka.

Endogenous growth theory provides a basis to define the theoretical model that is used in this study, i.e., Economic Growth (EG) is a function of various components of the social expenditure; expenditure on education, expenditure on health and expenditure on social welfare. Augmented Dicky-Fuller (ADF) - Unit Root Test and Co-integrations Test were conducted to find out the order of integration of all time series variables and to establish long run relationships between the variables.

ADF-Unit Root Test confirms that all variables considered are stationary at first order difference at 1% level. The co-integration test confirms long-run dynamic relationship between independent variables and economic growth. Expenditure on education and health has a positive relationship with economic growth and these are statistically significant at 1% level while expenditure on social welfare is not significant.

Thus, this study confirms that the public expenditures on education and health have a positive impact on economic growth in Sri Lanka. If the social development of the country is neglected, it could be a constraint for sustainable economic growth in the future. Hence, the government should improve the social sector through increased funding. In addition, the Government should also ensure that the resources reach the target populations. The government should promote efficiency in the allocation of social development resources by promoting private sector and beneficiary participation.