

AN ANALYSIS OF SECTORAL LINKAGES IN SRI LANKA

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The three major sectors of the Sri Lankan economy have been undergoing structural changes over the last few decades. This structural change and the uneven pattern of sectoral growth is likely to cause substantial changes in the production and demand linkages among various sectors, which in turn, could have significant implication for the overall growth of the economy. Therefore, an in-depth understanding of sectoral growth dynamics becomes very important for policy formulation in designing a structured and balanced growth in the economy. Hence, the main purpose of this research is to do a comprehensive analysis of inter-sectoral linkages among the major three sectors in the Sri Lankan economy. We used annual time series data covering the period between 1960-2018 for this study. All the series were extracted from annual reports of the Central Bank of Sri Lanka. The data of GDP of Agriculture (GDPA), GDP of Industry (GDPIND) and GDP of Services (GDP SER) are used as proxy for sectoral growth. All data were transformed into natural log form. ADF, and PPunit root test methods were conducted to test the order of integration. Lag length selection criteria such as AIC, SIC, LR, FPE and HQIC are utilized to select the optimum lag length that can be included in the model. Engle Granger (1987) co-integration test was used to determine the long run relationship between the variables. The Error Correction Model (ECM) was employed to identify the short run relationship as well as long-run adjustment among the variables. Moreover, Granger causality test was performed to investigate the causal relationship between the variables. Engle-Granger (EG) co-integration test using fully modified OLS estimation provides evidence of long run equilibrium relationship between sectors. The results from ECM show that the coefficient of error correction terms are statistically significant and had expected sign (negative) for all models, All sectors are positively related significantly even in the Short run. The investigation of causality analysis among sectors show that service and agriculture sectors have a two-way Granger causal relationship while industrial sector Granger affect the agricultural sector significantly. In the long run, Granger causality result (ECT) shows that Industrial and Agriculture sector have a two-way causal relationship. Moreover, agriculture sector Granger affect service sector while service sector Granger affect industrial sector significantly. Our empirical results indicate that all sectors are interlinked. Therefore, the government should promote all sectors in effective and stable ways.

Keywords: Inter-sectoral linkages, Co-integration, Causality