Economic Policy in Sri Lanka: Issues and Debates

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The essays contained in this volume discuss the historical evolution of Sri Lanka's social and economic policy and the ideology and debates governing it. The contributions in this volume are dedicated to Gamani Corea - one of the foremost Sri Lankan economists of national and international standing.

Corea played a key role in shaping Sri Lankan policy during 1950-72. In 1975 as Permanent Secretary of the newly created Ministry of Planning and Economic Affairs, Corea virtually became the sole architect of economic policies of the nation during 1965-70. In 1974 Corea was elected to the prestigious post of Secretary General of UNCTAD, a position he held for 11 years till 1984.

In an introduction to this volume, Saman Kelegama, editor of this volume, and Executive Director of the Institute for Policy Studies of Sri Lanka points out

> Under Corea's leadership UNCTAD became a hive of intellectual activity......The codes of restrictive business practices, multi-modal transport, liner conferences, the charter on rights and duties of states, the cancellation of debt by poor countries, the concept of generalized scheme of preferences, were all achievements of UNCTAD via a dialogue with developed countries. Corea was instrumental in introducing the Integrated Programme for Commodities- commonly known as the 'Corea Plan'- which was among the finest of his achievements.

The essays in this volume bring together contributions of 23 eminent economists and social scientists. The essays in this book have been grouped under six Parts, based on thematic issues.

Part I of the book deals with development strategy and policy. The implications of terms of trade deterioration for the development efforts of commodity dependent economies (in particular of Sri Lanka) has been a dominant theme of intellectual concern in Corea's long and highly influential career. Prema-Chandra Athukorala's analysis (Ch.1) of Sri Lanka's terms of trade from 1948-2002 makes an interesting departure from Corea's long-standing pessimism on this issue. He demonstrates that owing to changing composition of Sri Lanka's exports following reforms in 1978, the country's barter terms of trade has started improving, particularly since 1984. When income terms of trade are noted, factoring in increasing export volumes, the improvement is even more marked. Conventional analysis of income terms of trade factors is based only on export volumes but leaves out increase in import volumes, which in my view, is partial analysis. Perhaps such an analysis including both export and import volumes could be worth attempting.

One apparent paradox in Sri Lanka's development experience is how this country, having achieved remarkable strides in its human development indicators even prior to its independence, could not translate this to accelerate its economic growth similar to East Asian countries. Late Lal Jayawardena provides an explanation to this inconsistency (Ch.4). He laments that the root of Sri Lanka's problem lies in erroneous policies that widened the ethnic divide. The two major policies he refers to in this context are 'Sinhala only' language policy and introduction of 'standardization of marks' that made it extremely difficult for students in urban areas (by implication Jaffna Tamils) from entering the university. Failing to do so, they chose to become the leaders of the Tamil insurrectionary movement of Liberation Tigers of Tamil Eelam (LTTE). The financing of the resulting internal conflict had risen to the equivalent of 6 per cent of GDP, which in effect, replaced the food subsidy (p.99).

Dushni Weerakoon (Ch.2) points to the mixed results achieved during the decades of neo-liberal policies based on 'Washington Consensus.' In fact, perceptions of inequity in access to the benefits of market driven policies is argued to have been a contributing factor in heightening social and political tensions in Sri Lanka in the latter part of the 1980s. The search for new answers recognized the need for a broader set of reforms – referred to collectively as 'second generation' reforms- focused around the need to develop institutional capacity for reforms with added emphasis to private sector participation and poverty reduction. But this, the author believes, may not be easy to achieve given the complexity of the issues involved.

Late J.B. Kelegama (Ch. 5) laments the declining role of public investment in Sri Lanka's economy with the adoption of free market policies of deregulation, privatization and liberalization. Drawing lessons from the East Asian experience, he shows how private investment calls for public investment. The problem with Sri Lanka however is that of mobilsation of public revenue and is brought out in the section on macroeconomic issues.

Part II of the book relates to macroeconomic policy. In Chapter 6 D.D.M.Waidyasekera analyses the effectiveness and efficacy of the prevalent fiscal and taxation system and discusses the declining trend in government revenue in relation to gross domestic product (GDP) over time. The author critiques the effectiveness of regular amnesties granted. He suggests that careful attention must be paid to the economic and fiscal aspects of devolution to Provincial Councils from the very beginning. In the next chapter Nihal Kappagoda shows how government tax revenue to GDP declined between 1992-2001. He cautions that revenue constraints may cause problems in repaying both domestic and foreign debt.

Sisira Jayasurya in his discussion on the exchange rate in Chapter 8, brings out the 'worst case' scenario. He cautions that if the deficit is monetized and the currency continues to float freely, the resulting pressure on the current account deficit will lead to continuous decline in the nominal exchange rate. But what if the Sri Lankan currency is allowed to remain overvalued? What is the 'fundamental change in policy' he has in mind is not spelt out explicitly.

Part III of the book deals with sectoral analysis of the Sri Lankan economy. Nimal Sanderatne in his paper (Ch. 9) on agricultural development states that debates regarding agricultural policy issues have been rather limited except in academic circles. However, more recently there have been controversies regarding the liberalization of trade in agricultural produce, the removal of production subsidies and the imposition of water tax. In this context the author needs to highlight how the binding of agricultural tariff under WTO at a low level of around 50 per cent caused distress to high cost Sri Lankan farmers.

Sarath Rajapatirana in his paper states that industrial policy (Ch. 10) is not a proper response to market distortion. In his view, it is better to

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formulate specific interventions through appropriate institutional arrangements, not through trade policies. He suggests that targeted domestic subsidy be administered by a public commission in a transparent manner over a predetermined period. What Rajapatirana misses is that a neutral policy that uses selective interventions in the market is also a component of industrial policy and does not connote the absence of a policy.

In **Part IV** relating to employment and labour, Ravindra Yatawara's paper on labour productivity and growth establishes a direct relationship between the two. The study is unable to establish total productivity growth owing to unreliability of Sri Lanka's capital stock data. However it is difficult to accept that its omission 'does prevent making misleading pronouncements'. Could not its omission be the cause of this problem?

The problem of youth unemployment is one of the very destabilizing factors in the Sri Lankan economy. W.D.Lakshman in Chapter 13 brings this out very cogently and persuasively. The author's data reveals a marginal decline in Sri Lanka's unemployment rate since 1990s. But even so, as many as 11.5 per cent youth were unemployed in 1996-07 in spite of a declining trend in Sri Lanka's labour force growth. An ILO Mission in 1971 had laid strong emphasis on the structural mismatches between the quality of available manpower and their employability. Currently, emphasis is being given to low levels of capital accumulation and sluggish growth. The two kinds of arguments are however not mutually inconsistent. But the fact remains that even today Sri Lanka produces far too many graduates in the liberal arts as compared to science, engineering and medicine.

Part V of the book deals with institutions and governance issues. In Chapter 15 David Dunham examines the alternative views in the discussion of institutional reforms and economic liberalization in Sri Lanka. He states that reform is located in the broader political agenda of particular governments, adopted and implemented selectively to serve its ends. Malathy Knight-John (Ch 17) too argues that better results could have been achieved in a more efficient institutional setting.

The last part of the book **(Part VI)** deals with social welfare. Laksiri Jayasuriya's paper deals with the colonial lineages of a welfare state. Amala de Silva presents an overview of the health sector (Ch. 20). She examines how with the introduction of universal franchise in 1931, politicians determined the supply of health care in line with the electorate's demand for services. Harsha Aturupane (Ch. 21) shows how education investment appears to have a strong impact on economic welfare and poverty reduction in Sri Lanka. Buddhadasa Hewavitharana in his paper on poverty alleviation calls for revitalization of rural development by commercialization of farming and raising of investment and returns in agriculture by means of more stable market based trade and price policy, focusing of research and extension on competitiveness, liberalization of land market and fostering rural non-farm activities.

The editor of this volume needs to be complimented for having brought together such a comprehensive collection of essays covering almost all facets of the Sri Lankan economy from very renowned scholars from both within the country and abroad. The collection of essays tells us that high social development is an enabling factor in economic development. It needs to serve a social purpose to permit sustainable economic development. In Sri Lanka, growth rates have improved during periods of peace. But the peace dividend has so far proved to be illusory. Until such times this is realized, the country has to be content with growth rates that are much below its potential.