



Industrial Policy & Development in Sri Lanka

Kithmina V. Hewage

Overview

- History of industrial policy in Sri Lanka
- Diagnostic of industrial sector
- Recent developments in industrial policy
- Path forward



History of Industrial Policy

1948 – 77: Import substitution industrialization

- Producing basic industrial products
- Mainly by state-run manufacturing companies
- High import tariff and protectionism

Failure, as industries became largely import-dependent, not saving any foreign exchange, and functioning below capacity



1977 – 90: Liberalization Period

- Export-oriented industrialization
- Trade policy as main instrument of industrial promotion
- High contribution of FDI

Notable rise in industrial output, however, industrialization was urban-biased and relatively undiversified.



Early 1990s: Second Wave of Liberalization

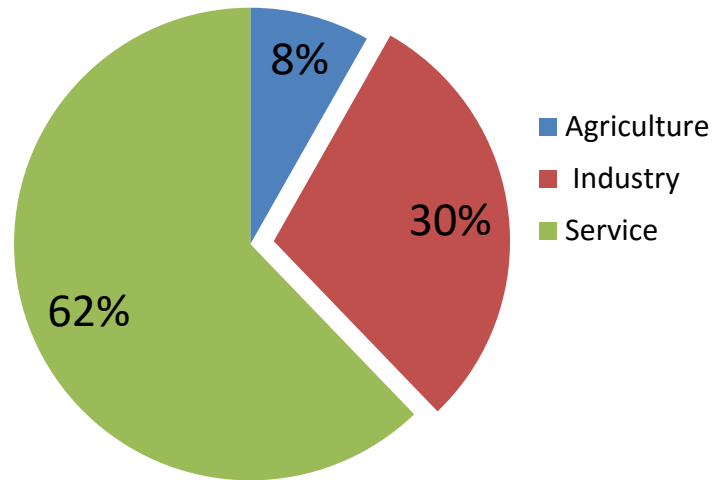
- Liberalizing FDI flows
- Reconstituted Board of Investment (BOI)
- Incentives for rural investment

Success was undermined by the lack of suitable infrastructure, limiting geographical spread. Manufactured goods were mainly of low value-added products utilizing low skill/low cost labour

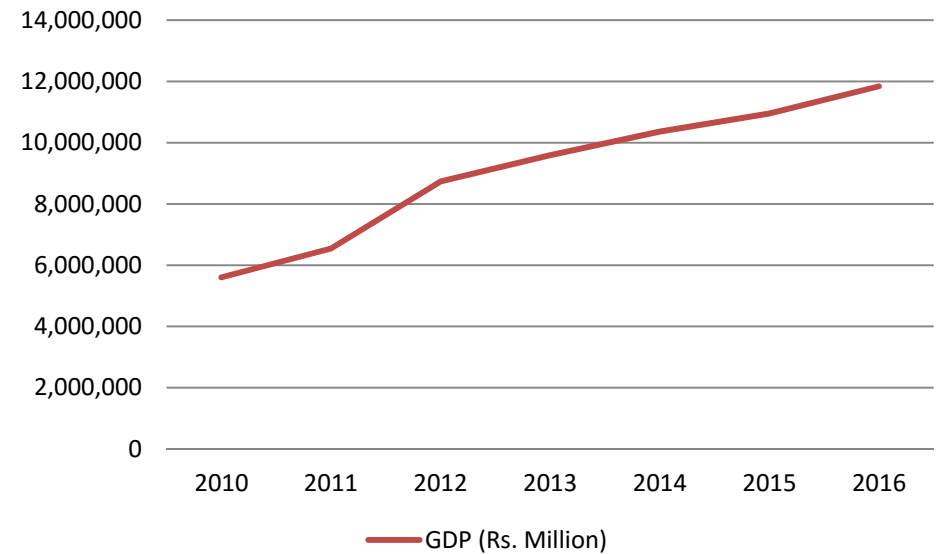


Economic Diagnostic

GDP Sector Breakdown (2016)



GDP



Sectoral Composition of GDP

Year	1975	1980	1985	1990	1995	2000	2004	2010	2015
Agriculture	30.4%	27.6%	27.7%	26.3%	23%	19.9%	12.7%	8%	8.2%
Industry	26.4%	29.6%	26.2%	26%	26.5%	27.3%	30.2%	26.6%	27.3%
Services	43.2%	42.8%	46.1%	47.7%	50.5%	52.8%	57.3%	54.6%	57.3%
Manufacturing	13.1%	18.3%	18.2%	17.4%	20.4%	15.8%	16.3%	17.3%	15.4%

Source: Central Bank, Annual Report, Various Issues

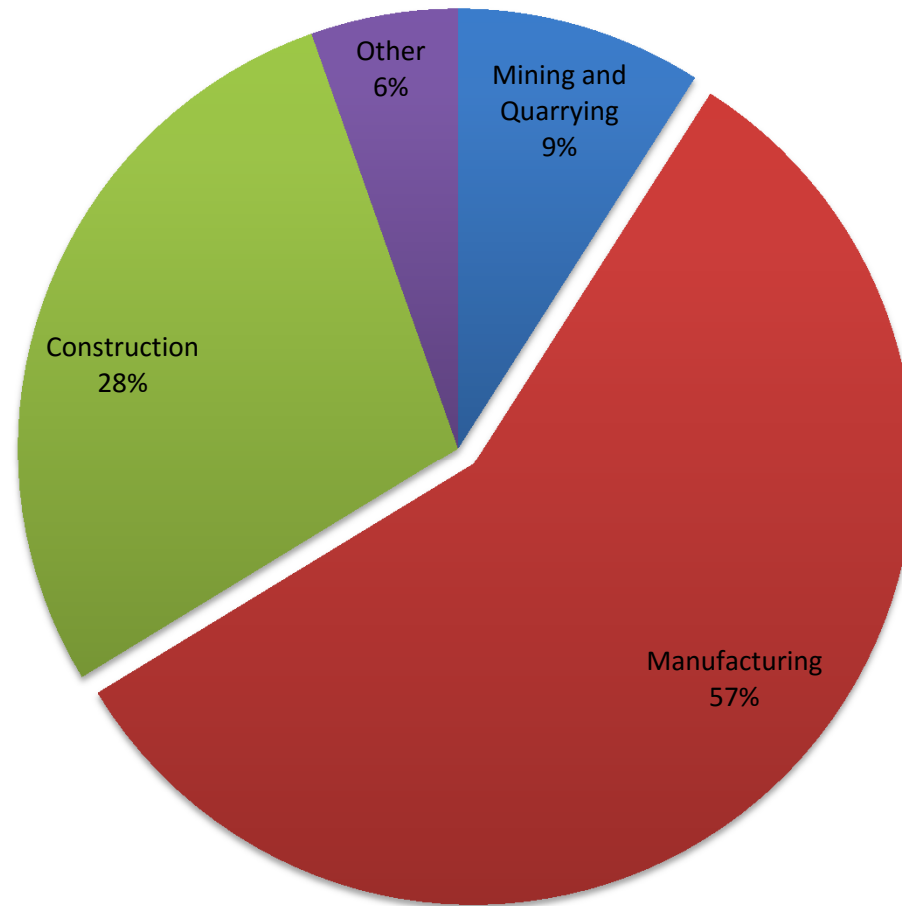
- Sri Lanka's industrial component – including manufacturing – has been effectively leapfrogged by the services sector
- However, services sector growth has been in domestic non-tradeables like wholesale and retail trade (25% of GDP), transport, storage and communication services – that are not export revenue generating



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Composition of Industry Sector (2016)

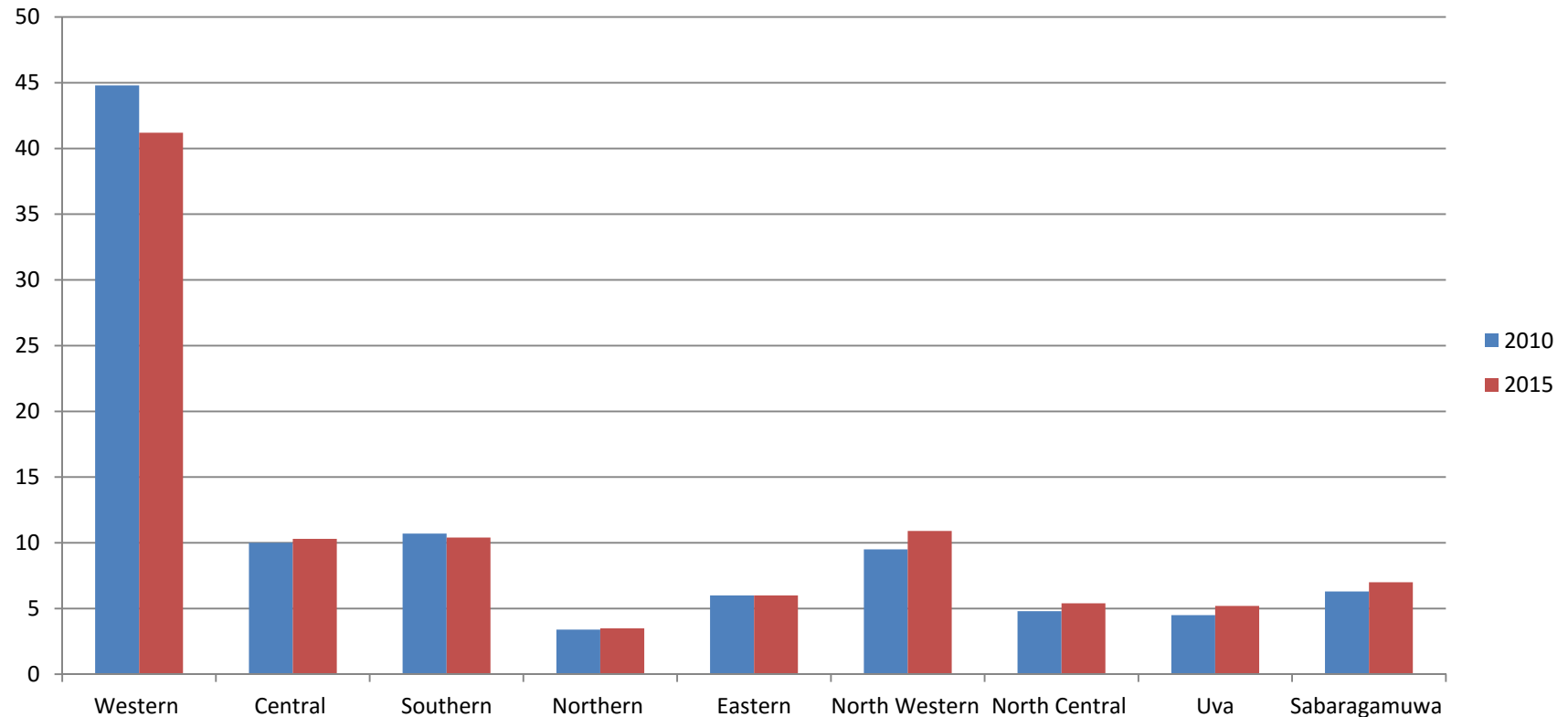


Key Challenges

- Lack of infrastructure connectivity between ports and rural areas
- High energy and transport costs
- Large industrial production concentrated in the Western Province
- Alternative has been to create Export Processing Zones and Industrial Estates
- Emergence of highways and post conflict infrastructure development drive is an important step towards improving connectivity



Provincial breakdown of GDP



- In addition to infrastructure gap, skills constraints have also restricted the expansion of industrial undertakings beyond Western Province



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New Age Industrial Policy

- Asian economies (with some exceptions) have been terrible at picking winners. New industrial policy should be market-oriented, rather than state-focussed
- Currently, Sri Lanka is looking at establishing a trifecta of free trade and investment agreements to leverage the trade-investment nexus (China, India, Singapore)
- Potentially significant role for OBOR: move beyond infrastructure projects and facilitate FDI flows





Institute of Policy Studies of Sri Lanka

100/2 Independence Avenue,
Colombo 7, Sri Lanka

T: +94 11 2143100

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