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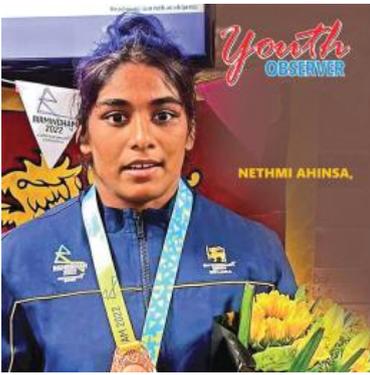
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IPS proposals for Interim Budget

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Business (/business)

7 August, 2022



There are certain products in which Sri Lanka enjoys a comparative advantage in global markets, requiring low imported raw materials in production such as tea, spices and mineral products like graphite

Ahead of the presentation of the Interim Budget, the Institute of Policy Studies of Sri Lanka (IPS) has recommended policy proposals for inclusion in the forthcoming Budget. Some key policy issues and recommendations:

Trade policy

Despite strict import controls, Sri Lanka's trade deficit in merchandise goods widened in 2021. The slight increase was mainly due to the sharp price movements in the world market, with the import reduction patterns across categories being consistent with the post-pandemic controls. As consumer goods imports are prioritised, including food imports, it generates two key undesirable impacts. First, it impacts food security and nutrition needs. Second, high food prices will incentivise a further resource shift – such as labour – to agriculture, raise wage costs for sectors like manufacturing and impact their competitiveness. In this context, two key recommendations are:

1. Prioritise imports for industrial expansion and food security needs: IPS research shows that about 88% of food imports are now subject to quantitative or price restrictions. The Special Commodity Levy (SCL) on items such as canned fish, green/black gram, cowpea, palm oil, and black gram flour should be removed to ensure that food security and caloric needs are met. Licensing restriction on maize imports which feeds poultry production costs must also be revisited. Sri Lanka must prioritise fertiliser imports and reintroduce fertiliser subsidies to paddy and vegetable farmers to raise productivity and prevent a resource shift that will impact overall economic efficiency.

2. Focus on increasing exports in sectors that use minimum foreign raw materials: There are certain products in which Sri Lanka enjoys a comparative advantage in global markets, requiring low imported raw materials in production such as tea, spices and mineral products like graphite. To meet immediate needs, bottlenecks such as fertiliser shortages should be addressed to raise productivity and export earnings while mineral resources can be auctioned to increase revenues.

Education Policy

The Covid-19 pandemic and the economic crisis have severely affected the education sector. Health concerns, union action, social unrest and transport issues have resulted in frequent school closures. Inadequate budget allocations and improper recruitment of teachers have deteriorated the quality of education. Recent news items have highlighted difficulties faced by schools due to shortages of paper and other materials necessary for the functioning of schools. Further, deterioration of school facilities has affected the effective functioning of schools. Interruptions to school-based relief measures such as the school meal programs can also increase school dropouts and malnutrition. Data from the Ministry of Finance reveals that public investment in education has remained just above 1%. Of this minuscule allocation, a large share is spent on teacher salaries. Frequent absorptions to the teaching cadre to provide jobs to unemployed graduates has worsened this situation crowding out funds from other necessary education inputs.

The government has recommended online lessons as a solution to difficulties in conducting on-site school classes. But IPS research shows that the access to online lessons is not equitable due to poor access to the internet, lack of necessary devices and high cost of data. In this context, two key recommendations are:

1. Increase public investment in education: Public investment in education should be increased and an adequate share of such investments should be dedicated to increasing the quality of education delivery such as the maintenance of school facilities, paper, and maintenance of school-centred relief programs (e.g. school meals). This can be done by putting a cap on the share of government spending on salaries and wages of total expenditure in education. Given the lower enrolment rates for A-Levels, the government should consider introducing targeted financial assistance programs for deserving children from poorer families to continue their studies.

2. Minimise school closures due to transport issues: Increase the existing fleet of school buses and provide adequate fuel for school buses to limit school closures due to transport issues. Measures should also be taken to ensure that children do not travel long distances to attend schools so that schools can function uninterrupted even in times of crisis.

Food security and nutrition policy

IPS research shows that long-term environmental, social, and economic trends heightened by domestic and international challenges have eroded the resilience of Sri Lanka's agri-food systems. On the global front, the COVID-19 pandemic and the Russia-Ukraine conflict are generating a global recession with high world market prices of food, oil, and fertiliser. At the local level, crop failures have resulted from poor government policies such as the chemical fertiliser import ban. Inflationary pressures arising from a combination of factors including excessive money printing and the sudden free float of the exchange rate have also taken a toll on domestic food prices and food supply. All these have resulted in low farm incomes, high food prices, food shortages and hunger and malnutrition. In this context, two key recommendations are:

1. Introduce a targeted food ration scheme for the poor and strengthen nutritional assistance: As an immediate measure to help the poor and marginalised who are the most vulnerable, introduce a targeted food ration scheme covering essentials like rice, wheat flour and dhal. Strengthen nutritional assistance programmes such as the School Meals programme, 'Thripasha' and 'Poshana Malla'. Support from the World Food Programme (WFP), Food and Agriculture Organization (FAO) and regional (SAARC) and bilateral sources can be sought for this purpose.

2. Promote community gardens in the short term: Promote community gardens that include neighbourhood community gardens and school gardens. The way a community garden is set up and maintained can vary greatly from one to the other. These can be established in an empty land and the neighbours can look after it. It can be even in private land where the neighbours can share the harvest in exchange for labour. Some examples of community gardens include Virginia Avenue Community Garden, Washington, D.C., and Community Gardens Australia.

Health policy

Sri Lanka's health system is recognised as an efficient, low-cost model. However, changing demographic and disease patterns along with domestic finance issues threaten the sustainability of the health sector. Inadequate service provision in the public sector and shortages of medicine and equipment are driving people towards the private sector causing inequities in access to healthcare, as not all can afford private sector healthcare.

Over half of the budget is allocated for wages leaving very little resources for all other health inputs. As a result, investments in this vital sector have been curtailed over the past few years. Further, changing lifestyles have exacerbated the risk factors for non-communicable diseases (NCDs). Four major behavioural risk factors directly contribute to the escalating NCDs in the country: tobacco use, physical inactivity, alcohol misuse, and unhealthy dietary patterns. In this context, two key recommendations are:

1. Introduce a system to ensure proper financial planning for the health sector: This includes rationalising expenditure on the health sector, increasing efficiency of health expenditure, and introducing mechanisms for mobilising private sector resources for the health sector. Rationalising health expenditure involves prioritising public health spending to focus on essential health services and ensuring that sufficient funds are available for financing such essential needs. A system to limit recruitments to the health sector to maximise spending efficiency is also needed.
2. Design fiscal policies to increase government revenue and lower health-related costs: Taxes aimed at curbing NCD risk factors can both help to increase government revenue and decrease health expenditure. Even though an inflation-adjusted tax system is the best option in the long run, for the interim budget, an increase of LKR 20 for all types of cigarettes is recommended. Such an increase is estimated to increase government revenue by LKR 5 billion. Expanding and increasing the tax on sugar-sweetened beverages (SSB) can also help to increase revenue and decrease health costs. Emerging findings from an IPS study show that the tax imposed in 2017 had contributed to decreasing the demand for SSBs.

Labour migration policy

In the first half of 2022, total departures for foreign employment were 138,789 which records a 351% growth relative to the first half of 2021. Despite the high departure statistics, the below-par performance of worker remittances is a concern. IPS research indicates that a major component of remittances to Sri Lanka are sent through informal channels.

Many migrants avoid using formal channels due to their cumbersome rules and regulations. In recent times, some have boycotted using formal channels to show their dissatisfaction with the government's ad hoc policies and related economic mismanagement that led to a foreign exchange crisis. In this context, two key recommendations are:

1. Increase departures to increase remittances: Loans can be offered to migrants to bear the cost of migration with the promise to repay the loan via remittances. The budget can allocate a sum of money for this purpose to give banks credit guarantees to provide loans to potential migrants. The migrants can be encouraged to pay back such loans with remittances. This will facilitate migration and also increase formal remittances.
2. Attract remittances through formal channels. Allow remitters to negotiate higher exchange rates (on par with informal remittance channels) for remittances sent via formal channels. Part of the reason for the lower exchange rate is the higher transaction costs involved when sending money through formal channels. The government can subsidise this cost so that banks can offer a better exchange rate to the remitters.

Social protection policy

Rising food and non-food prices and fuel shortages have serious consequences, particularly for low and lower-middle-income households with declining household earnings affecting consumption pattern.

Given the extent of the present crisis, the existing social protection schemes will not be sufficient to cover those falling below the poverty line due to the economic downturn. Hence rapid assessments are needed to identify the poor and those affected by the crisis using village-level administrators/committees.

This can be done efficiently by using the existing lists compiled during the pandemic as a basis but improving them to rectify any targeting errors. Given the level of targeting errors in the Samurdhi program, beneficiaries should not necessarily include Samurdhi recipients (families) if they are neither poor nor their earnings affected by the crisis. In this context, two key recommendations are:

1. Provide a monthly cash allowance to poor households: An allowance of LKR 5,000 per family/ household should be provided for three consecutive months to well-identified groups. This should be on top of any other cash assistance they receive from the government. The program should aim to include poor/deserving families including those who are currently not beneficiaries of the Samurdhi program but deemed eligible and any other families in the informal sector whose income has been heavily affected by the economic crisis.
2. Extend the coverage of the elderly assistance program: The coverage of the elderly assistance program should be extended to all eligible people above 70 years from low-income households to ensure their financial security. This is particularly important to ensure the financial security of senior citizens at this time given the rising prices of food, medicine, and difficulty in obtaining medicine free from government hospitals. This will first require a systematic assessment of their eligibility based on the defined set of eligibility criteria for the program (which can be done at the divisional level).

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