CHAPTER EIGHT

FINDINGS AND RECOMMENDATIONS

Despite the proliferation of research studies highlighting the benefits of economic reforms during the past two decades, evidence drawn from country studies barely support the contention that free-trade accelerates economic growth to bring about reduction of poverty and inequality in the third world.[1] One reason for this disconnect may be the flawed cross-country econometric analyses used extensively to arrive at conclusions on the benefits of free-trade. These studies are rendered flawed by time varying noise and specification errors in the regression models.

In this backdrop, there is a need for more country-specific case studies to ascertain how post-reform developing economies fared on poverty reduction. Such studies may establish whether the pace of growth has faltered in these economies and distributional outcomes worsened, on account of the failure of the export-led industrialization strategies. Sri Lanka completed 27 years of its post-reform experience in 2004. This thesis, therefore, was undertaken to critically evaluate the economic performance of post-reform Sri Lanka, to ascertain whether she was able to accelerate economic growth, create employment opportunities, ensure inclusive growth and reduce the incidence of poverty.

The following two major constraints affected this undertaking adversely. In a country where the liberalization orthodoxy was the dominant economic ideology for almost three decades, there is very little space for heterodox views among academia, research institutions and agencies responsible for policy formulation. The principal constraint for this work was finding a critical mass of researchers in Sri Lanka, where the topic could be discussed and tailored to suit the specific conditions of the country. Associated with this constraint was the paucity of consistent and comparable time series data on employment, growth, poverty and inequality for the period of reference. Moreover, in almost all of these

[1] For a review of the literature on the poverty-liberalization nexus see Winters, 2000; Banister and Thuggs, 2001; Bhagwati and Srinivasan. 2000; Berg and Krueger, 2003: UNCTAD, 2004; Hoekmann et al, 2002; Reimer. 2002; and Rodrik. 2001

cases, the definitions of national sampling surveys have changed making one set of data almost incompatible with the other. The national sampling surveys have been invariably irregular and did not cover large part of the country since the mid-1980s. The non-availability of annual surveys based on 'thin' samples, as in the case of India, made tracing poverty and inequality trends difficult.

Part One

The major findings

The study revealed that growth in post-reform Sri Lanka was sub-optimal in terms of its impact on employment generation and poverty reduction, making it exclusive in nature with outcomes that implied a widening of the economic divide.

The study has divided the economic history of Sri Lanka during the last three and a half decades into three sub-periods: pre-reform (1970-1978); the first phase of reforms (1979-1989); and the second phase of reforms (1990-2004). This periodization was based on the major policy shifts in the economy towards liberalization in 1977 and the subsequent intensification of liberalization and adoption of SAP in 1989.[2]

It has been found that the periodization used for this study was consistent with the changes in the policy paradigms and concomitant changes in the structure of the economy. The pre-reform era of 1970-1978 was characterized by a reduction of income inequality and incidence of poverty on account of the 'pro-poor' stance of economic development. The first phase of reforms (1979-1989) was marked by the adoption of liberalization policies in November 1977 which gave rise to the exacerbation of HC poverty and economic inequality. The second phase of 1990-2004 was characterized by the adverse effects of economic reforms cum structural adjustments that made the divide wider.

The liberalization package of 1977 included trade, exchange rate, fiscal, and financial reforms; these reforms were expected to deliver a combination of benefits to the economy by accelerating the pace of growth and making its pattern more inclusive, by creating

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[2] Outward looking strategy refers to policies. which are based on 'constant attention to' trade, technological and investment opportunities globally (Keesing 1967, p. 302).

employment opportunities, reducing inflationary pressures and improving the overall well being of the people. We examined the implications of reforms on the overall well being of the people of Sri Lanka, with special reference to the rural sector which is home to more than 90 per cent of the poor.

The study found that the poverty head count ratio had increased from about 22.7 per cent in 1980 to 40 per cent in 1985/86. Despite the ambitious poverty alleviation campaign launched in 1989, HC poverty during the second phase did not show any discernible sign of decline, except in the urban sector, where it fell from 16.3 percent in 1990 to 7.9 per cent in 2002. The incidence of rural poverty remained at around 24 per cent at the end of the second phase, while in the case of the estate sector it increased from 20.5 to 30 per cent.

The poverty trends became even more disturbing when poverty data in the provinces were compared. The HC poverty in the *Western province*, for instance, had declined by 41 per cent between 1990/91 and 2002, although in the provinces like *Uva, Sabaragamuwa* and *North Western* it had increased by 32 per cent, 23 per cent and 17 per cent respectively. The fact that about five districts were partially or completely excluded from the sampling process of the national surveys, made the poverty and inequality picture even more complicated.

Further, inequality trends measured in terms of both income data of CFSES and consumption data of HIES showed that the economic divide had worsened during the post-reform era.[3] The Gini ratio that was as low as 0.35 in 1973 increased to 0.46 by 1986/87, and continued to be at around 0.46 by the end of 2003/04. With regard to the expenditure data of HIES the relevant Gini coefficient estimate that stood at 0.32 in 1969/70 had increased to 0.41 by 2002. Provincial data on inequality show that the incidence of inequality was the highest in the Western province with a Gini ratio of 0.56 in 2002. The rural sector recorded a moderate ratio of inequality. Although the estate sector recorded the

[3] CFSES series of the CBSL has sample surveys for 1973, 1978/79, 1981/82, 1986/87, 1996/97, 2003/04 while the HIES series of the DCS has conducted sample surveys for 1969/70, 1980/81, 1985/86, known as LFSS and 1990/91, 1995/96 and 2002 designated as HIES.

lowest level of inequality until 1996/97, this position was reversed when its income inequality started worsening towards 2003/04.

A set of proxy indicators (covering educational, health and nutritional domains) used to ascertain human poverty revealed that access to educational and health opportunities, both in terms of quantity and quality, declined during the post-reform period. Further, nutritional standards of children have shown signs of degeneration in the 1990s. The post-reform development trajectory thus undermined Sri Lanka's outstanding position as a model developing country in terms of social indicators that she enjoyed in the 1970s.[4]

The study attempts to analyze the impact of liberalization on economic and social outcomes in Sri Lanka via a set of proximate determinants or transmission mechanisms including the pace of growth, patterns of growth, unemployment, inflation and the reduction of public expenditure. These determinants are ordered in terms of their impact on poverty reduction, measured in terms of the steepness of the trend curves presented in chapters four and five.

Accordingly, public expenditure emerged as the most powerful proximate determinant of poverty. To ascertain the impact of public expenditure on poverty, three year moving averages of public expenditure data were plotted against HC poverty. The shape of the curve was negative with a steep slope, the inference being that HC poverty is strongly associated with the reduction of public expenditure.

Public expenditure is important because of its overarching effects on growth, employment generation and inflation. The study showed that in the early 1980s the economic growth rate remained rather stable, on account of the massive public investment programme. Similarly, public expenses on social security during the pre-reform period and also during the early years of the poverty alleviation programme had positive effects in terms of poverty and inequality reduction. The effects of fiscal conservatism were overwhelmingly

[4] It was established that data on literacy, life expectancy and infant mortality for Sri Lanka in the 1970s were three standard deviations away from the world average for countries of similar per capita income. This reversal means that the adverse effects of reforms on capabilities and functioning have taken a long time to stabilize.

felt during the second phase of reforms when public investments meant for infrastructure development declined.

Fiscal conservatism reduced the flow and volume of social expenditure from 12.5 per cent of GDP in the early 1970s, to a very low level of 5 per cent by 2004. The long-established food subsidy scheme was abolished, and social expenditure on education fell in real terms. The poverty alleviation expenditure as a ratio of total government expenditure fell from about Rs 10 billion in 1990 to a meagre 2 billion in real terms by 2004. Consequently, by the middle of the 1990s, the number of children suffering from malnutrition and related manifestations of stunting, low birth weight, iron deficiency and anaemia increased substantially.

The second most important proximate determinant is the pattern of growth. When the growth rates of the provinces were plotted against their respective HC poverty data, it was revealed that the slope of the curve was steeply negative. The implication of this finding is that the worsening of regional inequality contributes to higher HC poverty. These findings reveal that the benefits of growth by-passed the rural and estate sectors and certain geographic regions. The volatility in the pattern of growth during the second phase worsened this situation. This was because of the tendency of the rich to gain disproportionately during economic recovery, and the worsening of the conditions of the poor during economic downturns. The slow GDP growth in the predominantly agricultural-rural sector and the rapid expansion of the services sector in the urban metropolis compounded the problem of the widening divide. On the whole, it confirms the assumption that worsening of inequality reduced the poverty reduction impact of growth.

The third most proximate determinant of poverty is inflation. Two segments of the population appeared to have suffered greatly on account of creeping inflation. They were the wage workers and small holders. As for wage workers, falling real wages have aversely affected all wage-board categories while the small holders suffered on account of increasing costs of inputs and falling producer margins. The thesis agrees that deflationary policies are bad for the poor. It weakens the salutary effects of public investments thus contributing to HC poverty.

The fourth proximate determinant of poverty reduction is the pace of economic growth. The slope of the regression curve was negative; but the curve was almost horizontal. The negative slope means that a higher growth rate has a salutary effect on poverty reduction. However, its moderate slope showed that the pace of growth was less than optimal. The more discernible reduction of HC poverty in the urban sector, that recorded a much higher pace of growth, corroborates this view.

The mean growth rate of 4.78 percent per annum for the post-reform period lagged far behind the growth records of those countries cited as success stories of reforms. Secondly, contrary to the expectations of reforms, the process of export-led industrialization did not take place. Thirdly, economic fundamentals such as budget deficits and the balance of payments which the reforms promised to put right were far worse than they were during the pre-reform era. There was no sign of recovery in any of these fronts. Thus the growth dividend of the reforms was minimal.

The fifth proximate determinant of poverty was unemployment. The regression line of this relationship registered an insignificant positive slope. It implies that HC poverty increases when unemployment increases in the country. However, quite surprisingly, its slope was almost horizontal. This finding should be interpreted in the context of the following manifestations that hid the real picture of unemployment in the country during the post-reform era. First, the unemployment data of this period conceals the changes in the structure of the employment market, with regular jobs being replaced by jobs in the informal/unorganized sector accompanied by falling real wages. Second, the changes in the definition of employment blurred the extent of unemployment in the country thus contributing to the reduction of unemployment figures. Thirdly, the high incidence of underemployment seriously undermined income growth and poverty reduction in the rural sector.

In terms of the macro impact of liberalization on poverty, the five proximate determinants identified and examined above have been conclusive in a number of spheres. Firstly, poverty and income inequality in Sri Lanka have taken a turn for the worse after the reforms in 1977. Secondly, public expenditure stood out as the most powerful influence on the extent of poverty; this was followed by the skewed pattern of economic growth. Thirdly, the inflationary trends in the country have had a negative impact on poverty reduction. Fourthly, the export-led industrialization strategy did not have a strong positive effect on economic growth in Sri Lanka in the aftermath of reforms; consequently, the terms of trade and the exchange rate of the Sri Lankan rupee deteriorated unceasingly. Finally, growth and employment benefits of reforms were both sub-optimal and exclusive, and were inadequate to have an impact on poverty reduction.

The major findings pertaining to the sectoral effects of the proximate determinants of poverty are presented using a set of seven (7) indices. All these indices have deteriorated continuously during the post-reform period. However, the extent to which they contributed to poverty could not be ascertained on account of the paucity of comparable time series data on poverty by sectors.

The most powerful variable under the sectoral category was the expenditure on poverty reduction. The trends of these allocations were examined in terms of the budgetary allocations for poverty reduction in constant rupee terms for the period 1990-2004. It is shown that the slopes of the trend lines were steeply negative. It was the cumulative effects of this decrease in poverty assistance in real terms coupled with targeting errors and problems of coverage that made poverty reduction programmes in the mid-1990s futile. This finding should be compared with the successful programme of public action in the pre-reform period which improved literacy, life expectancy and mortality rates. The income generation and self-employment component of the poverty alleviation programme too suffered from a multitude of weaknesses, pertaining to the choice of ventures, lack of capital, poor quality of technology used and market constraints. The goods and services produced by the small ventures resembled a 'distress adaptation strategy'.

The second proximate determinant, under the sectoral category, was rural credit and micro finance (MF) arrangements which reflected the adverse effects of financial reforms on poverty and inequality. The drawbacks of the MF arrangements was demonstrated by the outward transfer of surplus-deposit funds of the Cooperative Rural Banks, which showed the extent to which rural deposits were siphoned off to finance projects in the urban areas despite the shortage of capital in the rural areas. With regard to the inflow of finances under the Comprehensive Rural Credit Scheme (CRCS) into the rural sector, the trend line yielded a negative slope. The MF operations failed to fill the void created by the reduction of formal credit. The poor capital base, weaknesses in the institutional machinery, failure to target credit to the poor, usurious interest rates on small loans, refusal to accept new technology and siphoning of deposit funds to the urban sector despite the severe scarcity of capital within the rural sector worsened the situation.

The last set of sectoral determinants dealt with the negative growth trends of the priority sectors, i.e., the agricultural and industrial sectors. The falling real wages of industrial workers were added to illustrate the effects of the failure of these sectors on poverty. All three indices have shown declining trends as reflected in the negative slopes of the trend lines. This indicates the failure of the export-led industrialization strategy to trigger inclusive growth on the one hand, and the vulnerability of the peasantry to the falling producer margins on the other. These three processes, *inter alia,* exacerbated the poverty scenario in the rural and the estate sectors.

It was revealed that the campaign for commercialization of crops by the multinational donors eventually led to dispossession of assets that worsened the problems of poverty and inequality. The expansion of the high valued crop sector, sans adequate arrangements to provide capital, know-how, extension services, market arrangements and information has made banana cultivation largely an exclusive strategy. In the early years of reform the labour intensive industries in the secondary sector suffered virtual ruination. The revival of the manufacturing sector during the second phase of reforms was attributed to the expansion in the textile and garment sub-sector with extremely high import content. The unplanned location of industrial ventures and business outlets in the metropolitan areas during the second phase exacerbated the regional divide.

In sum, the Sri Lankan case shows that market reforms during the past 27 years failed to generate rapid growth to reduce mass structural poverty while income transfer programmes also failed to achieve their assumed objectives of alleviating the problem of private destitution.

Part Two

Consistency of findings with the framework of analysis

This thesis was based on the premise that 'context specific' evidence was more important than the findings of cross-country studies in ascertaining the impact of trade liberalization. The Sri Lankan case provides sufficient evidence to show that economic reforms of 1977 were not 'crisis driven'. On the contrary, this thesis argues that the politico-economic crisis of the late 1980s in Sri Lanka was a direct outcome of economic reforms. The thesis reveals that free trade does not automatically generate growth as is often contended. Economic reforms cannot, after all, change climatic conditions, the socio-political ambience of the country and the terms of trade effects. The structure and composition of exports in Sri Lanka did not, therefore, change to deliver the maximum mileage out of trade expansion.[5] The long-term growth trends of the post-reform industrial and agricultural GDP were negative; the country's terms of trade also deteriorated continuously during the same period.

The study showed that even the beneficial outcomes of 'trade' are not sustained unless the initial conditions are set for inclusive development.[6] These initial conditions include a disciplined bureaucracy, egalitarian land reforms, an informed leadership and public, which, for example, were instrumental for economic progress in South Korea and Taiwan in the 1970s (Rodrik, 1997). On the other hand, the country suffered on account of the presence of a disruptive and self-seeking bureaucracy and undisciplined entrepreneurial class that hindered the growth process as in the case of India in the 1980s (Chandrasekhar and Ghosh, 2002; Haris-white, 1999). These two settings were extremely important in

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[5] This is in comparison with the performance pertaining to export-led industrialization in the East and South East Asian countries.

[6] Trade is not necessarily bad although free-trade can be harmful (UNCTAD, 2004).

explaining why Sri Lanka could not do better during the pre-reform era and its conditions worsened during the post-reform era.

The adverse effects of fiscal conservatism during the second phase of reforms permeated all sectors. Social security, education, health, and farm credit formed the soft targets that were affected, while rural infrastructure, power and energy signified the 'not-so-soft' targets that were weakened. Not only did they eliminate the initial advantages of the country in social welfare but also exacerbated the economic divide.

The inequality trends in Sri Lanka clearly disproved the contention that free trade produces income equality in the long run as espoused in the archetypical Kuznets hypothesis. In fact income inequality worsened despite 27 years of unbroken history of free trade. Thus, the convergence hypothesis of Sachs and Warner did not work in Sri Lanka. Although Sri Lanka's poverty reduction strategy showed some positive results in the early 1990s, its design and implementation failures leading to large-scale leakages, curtailment of fiscal allocations and faulty targeting made it ineffective by the latter part of 1990s.

In this context 'wage for work' type of experimentation, as conducted in India and Bangladesh, could provide useful means to minimize targeting errors while helping to improve the overall welfare of the poor at a comparable cost. Unlike a mere cash grant scheme, wage for work programmes increase the capital stock in poverty-stricken sectors and also raise effective demand when part of the assistance is channelled to purchase domestically produced cereals, pulses and other essentials.

Further, the empirical evidence from Sri Lanka has refuted the conjecture that free trade contributes to increase employment opportunities to unskilled labour. However, the argument that inequality stifles economic development was very much in evidence during the post-reform Sri Lanka. The worsening political crisis in the Northern and Eastern provinces nullified the contribution of the two provinces in the spheres of fisheries, tourism, paddy production and commercial agriculture.

The dominant view that the market produces miracles of accelerated growth while ensuring equity through the 'trickle down' effect has proved to be a chimera as twenty-seven years of economic liberalization have not resulted in any trickling down of growth dividends in Sri Lanka. Therefore, a shift from the current dependence on market fetishism to a strategy where the state plays a more active role in regulating growth priorities, targets of export promotion, and incentives for agricultural and industrial growth has become absolutely necessary. The type of strategy visualized here blends elements of market and state-mediated action in a holistic manner. The growth strategies of Taiwan and South Korea in the 1970s provide plenty of lessons for carrying out such a paradigm shift.

Part Three

General recommendations

For a country where one out of every four person was identified as income poor and more than 46 per cent of the population receives poverty assistance, the first policy priority unquestionably should be poverty reduction. Trade integration and economic reforms are secondary to these fundamental development priorities as neither is feasible given that socio-economic and political tensions have made 'trade orientation' and 'openness'-related priorities unworkable.

The realization of the development objectives of the country depends on its ability to increase public expenditure which emerged as the most important proximate determinant of poverty. It is linked with the development of productive capacities, employment generation and technological progress along with raising of the welfare standards. Its impact permeates improvement of physical infrastructure such as roads and transportation, market, electricity and telecommunication networks along with the provision of social security. All these changes imply a deviation from the current agenda of fiscal conservatism.

The country's existing market structures have made economic activities in the rural sector artificially depressed, on account of faulty input and output pricing mechanisms put in place by marketing monopolies and monopsonist agents. The revival of the rural and estate sectors will also depend on the extent to which the state is able reinvigorate the market structure. Similarly, the re-introduction of formal credit to redress indebtedness, insurance mechanisms to hedge against crop damage and revitalizing the public distribution system are areas that require special attention.

Raising agricultural productivity is linked to yield improvements through adoption of better technology and extension services, and upholding the producer margins through better internal terms of trade. The scope for diversification of the predominantly agricultural rural economy to generate productive non-farm employment opportunities also is high. The relocation of garment factories in the early 1990s is proof of the feasibility of this proposal. Besides, a faster growth of the secondary sector to absorb the labour surpluses in the agricultural sector is crucial for sustainable income and employment growth in the economy.

There is a case for revisiting the process of land and agrarian reforms to ensure equity and income opportunities. The paucity of land and water are the two main evils that had undermined the productive capacities of the rural economy; this could still be addressed by implementing a proper programme of 'land to tiller'. Although, the scope for land-based expansion of opportunities is not unlimited, agrarian reforms can make agricultural development more inclusive so as to narrow the economic divide. Agricultural research and development to identify drought-resistant food crops and perennial crops can help upgrade farm income.

The thesis has shown that the effects of the concentration of economic activities in the urban metropolis occurred partly on account of the urban-centric growth strategy. Industrial location has been excessively biased towards the *Western province* which received more than 90 per cent of new industrial ventures. A programme to devolve power will, therefore, be helpful in redressing this problem of regional disparity and the vexed problem of ethnic divide.

There is a need for paying adequate attention to the poor state of statistical databases in the country. Without consistent, reliable and comparable data, policy formulation and monitoring becomes tenuous, and will be based on counterfactual assumptions. The current approach to 'market driven' research and procedures of prioritising and funding research, based on market principles by data gathering institutions, have made independent research impossible.

Another serious concern is the mounting defence expenditure, which is at around 4 per cent of the GDP; it has reduced the country's capacity to invest in the much-needed social and economic sectors.[7] Unless a political solution is worked out for the perplexed national question that has caused a huge gulf between segments of its own people, the undesirable situation will persist. At the political leadership level, what the country needs is patience and a vision to resolve the problems of disarticulation and the ethnic divide.

Almost all policy alternatives presented above require financial resources, and Sri Lanka can no longer expect concessionary loans and aid as its GDP per capita has exceeded the US$1000 mark by 2004.[8] Therefore, she has to mobilize resources within the country by widening the structure of the country's tax base and improving the tax collection machinery. The current strategy of taxing the losers by imposing turnover/value added taxes should be reversed by expanding the tax base by introducing direct taxes to cover those who gained from the reforms.

Part Four

Specific recommendations

The assessments made in this thesis, showed that there is a growing disparity in the country by income groups, sectors and regions. Therefore, 'one-size fits-all' types of formulae, as envisaged by the liberalization orthodoxy, may not help solve the problems of poverty and inequality in the country. Therefore we propose the following specific recommendations.

[7] A reduction of defence expenditure to the regional average of 1.5 per cent would have unleashed fiscal surplus of Rs35.2 billion (US$338 million) which compares with the total poverty alleviation budget of around US$80 million for the year 2004.
[8] It was US$1031 per capita for 2004.

1. Revamp the public purchase mechanism that was made dormant during the post-reform period, to reduce the volatility of farm-gate prices of agricultural produce and to stabilize the prices of wage goods. It is proposed to amalgamate existing institutional structures of farmer organizations, multi-purpose cooperative societies and the apex cooperative structures including the CWE, to minimize the overhead costs of this machinery. Further, forward buying arrangements successfully implemented in certain parts of the country during 1996-2002 will help reduce price fluctuations at farm-gate levels.[9]

2. Import of food grains, canned food and other substitutes that pose a direct threat to domestic production should be subjected to a high tax regime, to protect domestic production and income levels of the poor, whose livelihoods depend on the production of these commodities. This will offset the unfair practices of monopolist importers who build up stock-piles with imported food grains just before harvest to keep the domestic prices down.[10]

3. Poverty among the small holders engaged in paddy, minor food crops and other cash crops may be redressed by introducing a guaranteed price scheme (GP), which may be administered by the farmer organizations. The formulae for computing the guaranteed prices ought to cover the cost of production and provide a reasonable return.[11]

4. The recommendations mentioned above may involve a producer subsidy that can increase the financial burden on the exchequer. This will necessitate proposals to augment revenue collection. Assuming that the proposals to revamp the GPS cost less than Rs.1.5 Billions (US$14 millions), it will only demand an imposition of a cess of less than 3% on imported food-stuffs which are mostly consumed by the 'new rich'.[12]

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[9] This arrangement was initiated by the RRDB programme which was made ineffective by wrong trade policies which encouraged import of these products just before the harvesting of local crops.

[10] Currently, Sri Lanka has the lowest import tariff structure in the region and, therefore, upward revision of these tariffs is feasible. The average tariff rate for Sri Lanka in 2004 was around 20 per cent.

[11] ((Marketable surplus * GP)-cost of production) / (poverty threshold * 12 months) > 1 to ensure economic mobility beyond poverty threshold.

[12] For the year 2004, the total import bill of food and drinks amounts to Rs 60.5 billion (US$596 million). A cess of 2 per cent on this bill will provide the seed money (Rs1.2 billion) to launch this programme and its recurrent cost can be generated by maintaining half the present marketing margins of the private buyers (60 per cent).

5. There is a need to expand the formal credit net to cover small farmers and rural artisans, to liberate them from the clutches of money lenders. It was revealed that a portfolio target of 2 per cent of the total short-term loans of the commercial banks will be sufficient to make a five-fold increase in the current flow of CRCS loans to the rural sector.[13]

6. The current programme of cash-grants under *Samurdhi* programme, which has failed in a number of respects, may be gradually replaced by a better targeted 'wage for work' programme that could ensure poverty reduction while also improving the stock of national wealth. It will help to minimise targeting errors through self-selection procedures.

7. In the rural and estate sectors the incidence of poverty was found to be a function of the number of days worked per month (year) and their real wage rates. Therefore, poverty alleviation strategies should introduce a mechanism that can increase the hours/days of work available to reduce underemployment. The determination of wage rates under this scheme may eventually be linked to poverty threshold.[14]

8. In the plantation sector, additional work can be created in the areas of soil conservation and re-plantation, which are essentially labour intensive as well as productive in terms of the sustainability of the industry threatened by low yield levels of ageing tea bushes.

8. In the urban sector poverty rates have fallen despite worsening income inequality. Here again a combination of strategies aimed at increasing income levels by enhancing the rates of real wages of the workers of the organized private and public sectors by indexing them to cost of living is warranted. It is important to extend this facility to those workers who are in the informal sector through regulating their minimum wages.

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[13] The total rural credit flow under the CRCS scheme for the year 2004 was Rs1.5 billion (US$13.59 million) which was a meagre 0.45 per cent of the total short-term lending of US$3.1 billions for 2004. Even a five-fold increase of this amount will not hinder the present profitability levels of the commercial banks.
[14] (wage rate * number of days work) / poverty threshold > 1

Conclusion

If the liberalization of the Sri Lankan economy is policy induced, so are the implications of liberalization for the incidence of poverty and widening of the economic divide. The incidence of both income poverty and human poverty in the country was found to be widespread while economic inequality was persistently on the rise. The experience of economic liberalization has proved that it cannot address these two issues effectively. In fact, this thesis argues that the current situation is an outcome of the very policies of economic reforms the country faithfully carried out during the past few decades. Therefore, the solutions to the policy-induced problems of poverty and inequality should emerge from a carefully-designed package of policies that has the right combination of state mediation and the positive elements of trade promotion. The failure to do so will be very costly for a country already shaken by political, social and economic upheavals of unmanageable magnitude. It is hoped that the findings and recommendation of the thesis outlined above will broaden the insights of those debating, discussing, designing and implementing polices pertaining to the economic development of Sri Lanka.