CHAPTER III

INDUSTRIAL GROWTH OF SRI LANKA UNTIL 1977
Although overseas joint ventures include both manufacturing and non-manufacturing categories, yet the bulk of them are of industrial nature and the involvement of manufacturing is assumed in most of them. At least in the case of India, out of the total of 134 Indian joint ventures abroad in operation in July 1982, 87 units, accounting for 94 per cent of the total Indian investment, were engaged in manufacturing activities. In order to undertake an intensive study of the Indian joint ventures in Sri Lanka, it is essential to have an understanding of the growth and development of manufacturing industry in the island. Besides this the Sri Lanka Government's policy on foreign investment, the infrastructural base that has evolved in the country and the general political and economic backdrop have also to be studied.

**Early Years and Emphasis on Plantation:**

In the early years after independence the concept of industrialisation was not seriously pursued and there was very little change in the structure of the economy. The government continued to rely heavily on the plantation


Sector as the main source of income to continue financing several social welfare measures which it had initiated during the second world war. The United National Party (U.N.P.) government that was in power until 1956 could not pursue industrialisation for a variety of reasons. The ruling elite's faith in the plantation economy and their response to the economic challenge comes out vividly in the following words of Ivor Jennings "the present wealth of the country lies in its plantations; it is impossible to foresee and almost impossible to imagine the development of conditions in which this situation would be altered." Although in the first policy statement of independent Sri Lanka "the need to welcome foreign industrial investment for industrial development" was emphasised, in practice industrialisation was deliberately given a minor place and the government proclaimed that it could think of few prospectively efficient industries. Deriving its power base from the urban commercial and propertyed classes, the U.N.P. did not want to adopt a policy of import substitution with regard to manufactured goods since this would have


caused dislocation in the trade of the former and discomfort to the consumption of the latter. Further the Marxist politicians in the opposition were demanding a larger measure of industrialisation as the only panacea for the country's economic ills. The demand was construed by the U.N.P to be due to the leftist desire to consolidate its power among the industrial proletariat. The World Bank Mission of 1952 also recommended against capital intensive industrial ventures although it did suggest encouraging small scale industries. The mission felt that raising the resources necessary for industrialisation would entail increased taxation of foreign owned business and estate interest and might cause a flight of foreign capital. The emphasis, therefore, in national economic policy was to expand the prevalent agricultural economy by opening up new land for cultivation and revitalise the plantation industry


8. The economy had been plagued with wave after wave of strikes and slow-downs by organized labour. Leftist parties competed for the allegiance and control of trade unions and used them to intimidate the government. Gunnar Myrdal, Asian Drama, vol.1, (Middlesex, 1968), p.356.

9. Snodgrass, n.6, p.111.

10. The Central Bank of Ceylon was already apprehensive of the flight of foreign capital and had estimated that during the years 1950 and 1951 there was a net outward movement of private capital amounting to Rs.19 million and Rs.38 million respectively. Central Bank of Ceylon, Annual Report 1951 (Colombo, 1952), pp.60-1.
through replanting programme.

Manufacturing Sector - Small Beginning:

The manufacturing sector in Sri Lanka's economy at the beginning of the 1950s, as a result, was a small and relatively unimportant component. The Census of Industry held in 1952 enumerated approximately 700 manufacturing enterprises in the branches of industry other than the industrial processing of the three export crops - tea, rubber and coconut. These were small in nature, the typical initial industrial enterprises of a less developed country producing matches, shoes, beer and soft drinks. Table 9 in the Annexure gives details of the structure of industry in 1952. The government left the task of industrialisation to private enterprise. But domestic private capital was reluctant to enter the manufacturing field as there were opportunities to buy profitable foreign owned mercantile establishments and estates. Between 1930 and 1952, foreign company ownership of tea estates fell from 80 per cent to 50 per cent while Ceylonese ownership increased. Besides tea and rubber estates, a wide


variety of commercial establishments - newspapers, hotels and department stores - changed hands during these years.

Public Sector:

In the public sector, the only industrial venture of importance set up during this period was the Kankesanthurai government cement factory in the north of the country in 1950. Another field in which government policy did succeed in bringing about a significant change was in the generation of electric power. The U.N.P. government introduced the major hydro-electric power for the first time with the commissioning of the Luxpana station with a capacity of 25 megawatts. As for the sources of technology, the Report of the Commission on Government Commercial Undertaking states that projects were promoted with technology obtained through consultancy service which had to be paid at every stage of the project. These consultants were not infallible and their applying inappropriate technology, coupled with bad designs, led to frequent breakdowns. State investment in industries during this period resulted in a small state owned manufacturing sector which was inefficient and

14. Snodgrass, n.6, p.211.
unprofitable and consequently a burden on public revenue.

S.L.F.P. Rule and the Industrial Policy:

From 1956 to 1965, except for a brief spell, the Sri Lanka Freedom Party (S.L.F.P.) was in office and, therefore, its industrial policy had a significant impact on industrialisation. The government, soon after assuming power, made an industrial policy declaration to the effect that it would place high priority on industrial development with state ownership and control of basic industries. The planning body reiterated that industrialisation was the solution to the problem of Ceylon's increasing work force and to the country's economic growth in general. The stage was already set, it was felt, for initiating a process of industrialisation. Under the new industrial policy, the government defined the areas of public investment and what was to be left to the private sector. All industries were categorised into three schedules. Schedule 'A' consisting of basic and strategic industries like cement, fertilizers, steel and minerals, was reserved for the State. Schedule 'B' comprising of 23 light consumer goods industries like


electric bulbs, storage batteries, glass products and galvanised iron sheets took the organisational form of joint state and private sector and Schedule 'C' consisting of 82 small scale industries like soap, bicycle tyres, tubes, blades and safety pin were reserved exclusively for the private sector. A significant trend in the policies was the strong emphasis on the state sector and the private sector was not allowed to participate freely in industrial development. As can be seen, participation was allowed for the private sector only in light consumer goods industries. The decision of the previous government, under the Government Sponsored Corporations Act of 1955, to transfer to the private sector several state enterprises manufacturing ceramics, vegetable oil, paper, cement, leather and plywood was reversed.

Planning and Industrial Development:

In 1956, the government constituted a National Planning Council which was to function as a non-political organisation. In 1959, it presented a Ten Year Plan which was the first development plan that embraced the whole economy. A comprehensive document, the Ten Year Plan set out a long term strategy aimed at "providing a focal point around


which efforts of the nation should hereforth be centered".

The plan had high qualities as an intellectual exercise and
its architect placed relatively high priority on
industrial development.

In 1957 legislation was enacted for nationalisation of
regular and occasional omnibus services and hiring car
services. In the same year, the State Industrial
Corporation Act was passed and three state corporations were
established for the production of ilmenite, sugar and salt.
Between 1957 and 1959, more number of industrial
corporations were set up to produce shoes, leather goods,
caustic soda and chlorine, cotton yarn, sugar, bricks and
tiles and hardboard. Together these corporations
represented an investment of about Rs. 20,000,000.

Foreign Exchange Constraint and Import Restrictions:

An important phase in the industrial development of the
country began largely as a result of the stringent import

24. Ibid.
25. Gamani Corea who was the Secretary of the National-
Council was also the Director of the Planning
Secretariat which produced the plan.
26. Unfortunately the targets of this plan were never
realised. The political instability that followed
within a few months of the publication of the plan and
the increasing balance of payments difficulties doomed
its timely implementation. Myrdal, n.8, p.358.
29. Central Bank of Ceylon, Annual Reports of the Monetary
Board to the Ministry of Finance, 1961 and 1962 as
quoted in Snodgrass, n.6.
restrictions introduced by the government in response to the country's deteriorating balance of payments. In 1955, Sri Lanka's export earnings reached a peak level of Rs. 1,893 million. Thereafter, there was a gradual decline in these earnings. This decline, despite increases in the volume of the two major exports, tea and rubber, was due to poor export prices. As against these developments, there was a rapid increase in imports from 1956 to 1960 because of the 'consumer boom' resulting in heavy demand for imports. The government budget, which was largely financed by the borrowings from the banking system, was the major factor in creating excessive purchasing power in the economy. The country's tariff policy during this period was very liberal. Import duties were levied only for revenue purposes and, therefore, in the case of most imports the duties were nominal. There was no deliberate use of tariff policy to regulate imports through the system. In fact, during the period 1955-60, a large part of the lending capacity of the commercial banks was absorbed by imports. This resulted in a continuous downward trend in the country's external assets which fell from an all time record of Rs.1,276 million in


32. Dahanayake, n.22, pp.72-3.
1956 to Rs.541 million in 1960. Thus, the country was plunged into a continuing foreign exchange crisis. Perceiving an acute insufficiency of domestic savings and capital inflow, the government resorted to heavy restrictions on imports and naturally, when the question of industrialisation came up, it had to look in the direction of import substitution. The government was forced to introduce a greater degree of nationalisation, especially through a more systematic and strict allocation of foreign exchange for the import of raw materials and other inputs. With production almost entirely oriented towards the home market, the manufacturing sector became heavily dependent on imported inputs.

State Control to Ensure Equitable Distribution:

The government’s emphasis on state control and public sector oriented industrialisation was a result of the exaggerated hopes of redistribution of wealth and the assumption that structural changes such as nationalisation would automatically generate additional revenue. In most of the developing countries state ownership and operation of enterprise prevail to some extent irrespective of political ideologies of governments. The increasing and active participation of the state through public enterprises and

the regulation of the functioning of private enterprise could be explained as the outcome of the urgent desire of the governments of the developing countries and the ever-rising expectations of their increasing population to achieve a higher standard of life as compared with the developed countries.

Communist Countries' Help to Public Sector:

The establishment of industries in the public sector was further assisted by several factors. One of them was the availability of assistance by way of technology and capital goods from the centrally planned economies of East Europe with whom the new government established diplomatic relations. These countries provided economic assistance, showing a natural preference for state enterprises. U.S.S.R and East European countries thus supported the development of public sector enterprise in Sri Lanka. In addition, there was a measure of reluctance on the part of local private enterprise to raise the extent of capital required or to accept risks involved in entering the field of large-scale industry, particularly in the context of a marked political antipathy on the part of the ruling party towards the establishment of privately owned industrial sector.

36. Karandawala, n.11, p.32.

37. Ponnambalam, n.7, p.47.

38. For Instance, the controls on the import of automobile tyres led to a state tyre factory which was set up with the collaboration of Soviet Union. Nawaz Dawood, n.13, p.133.

Inefficiency in Public Sector:

But the Industrial scene in the public sector presented a dismal picture. A number of the state industrial corporations showed very poor financial results. They were plagued by unutilised capacity, mismanagement, overstaffing, technical deficiencies in planning and defective policies. Their output was characterised by high prices, inferior products and shortages. The natural consequence was considerable loss in many of these enterprises. These corporations imposed heavy burden on the government budget. No efforts were made until the mid-1960's to improve the performance of these state industrial undertakings. Greater efficiency in management, higher rates of capacity utilisation and the adoption of more appropriate pricing policies were sadly lacking.

Private Sector Industries:

Conscious of the limitation of the public sector operation, the government revised its industrial policy and tried to promote private sector industries. Foreign collaboration was also encouraged. In order to attract private capital in the early sixties, a great deal of prodding was done by the government to make private enterprise start consumer goods manufacture. Protection by

40. Balakrishnan, n.30, p.117.
41. Ibid.
42. Karanadawala, n.11, p.55.
43. Balakrishnan, n.30, p.117.
tariff and incentives were offered to entrepreneurs.

To dispel fear of nationalisation the government assured that it would not, for the ensuing ten years, consider the question of nationalising of any private foreign investments in the country. To provide further incentives for industries in the private sector an Industrial Estate Corporation was set up in 1959. The corporation established an industrial estate at Ekala occupying a land area of approximately 70 acres. The estate provided basic amenities such as buildings, water, power, communications and sewerage to all occupants.

Aids to Industrialisation:

In order to give a fillip to industrialisation the government also established during this period the Ceylon Institute of Scientific and Industrial Research (C.I.S.I.R.) the Development Finance Corporation of Ceylon and the Bureau of Standards. Further, fiscal concessions were granted to industries by the Inland Revenue Act no.3 of 1963. This provided for: (1) a development rebate on expenditure incurred in the purchase and installation of plant and


46. Nawaz Dawood, n.13, p.133.

machinery in the new approved undertakings. (2) Tax relief on investments in approved industries and concessionary rates of all customs duties were given on import of raw materials, machinery, equipments and components in the case of approved industries that did not enjoy a protected market. (3) Exemption was given from Income Tax on profits from the export of articles approved by the government. Government also adopted encouraging measures to promote export of industrial products. Tax holidays on export profits, refund of duties, deduction of advertising costs abroad, rebate on Income-Tax equal to 5 per cent of the value exported, waiver of excise duty and turnover-tax on industrial goods exported were some of the measures adopted by the government to encourage investment. With these efforts, a measure of industrialisation was achieved. Between 1960 and 1963, over 1,000 new industrial units were

49. Ibid.
50. Ibid.
51. "But the level of company taxation rose considerably. By 1948 the rates of tax on non-resident companies was 36.8 percent and by 1956 it had risen to 57 percent in profit tax plus 16 percent dividend tax based on total net profits. By the early 1960s the total tax rose to 74 percent. Thus in a short period Ceylon had changed from being a country with low corporate rates of taxation to one with exceptionally high taxes". D.K. Fieldhouse, Unilever Overseas (London, 1978), pp.316-8.
approved in the private sector against about 500 set up during the 15 years since 1945.

**Private Sector's Instinct for Survival:**

Governmental efforts were not the only reason for the growth of industries in the private sector. It could also be said that the private sector had entered the manufacturing field due to an instinct for survival. In August 1960 several import restrictions were imposed. In January 1961 they were expanded and strengthened. Further restriction on imports followed in rapid succession till October 1962 when all imports excepting foodstuffs, petroleum, fuel, fertilizers, and medical drugs were brought under individual licencing. In 1963 and 1964, some more items from the above categories were brought under individual licencing and in December 1964, the system of Open General Licence ceased to operate altogether.

With these substantial restrictions on imports the response of several interested parties converged to produce a sizeable lump of industrial investment during this period. The local trading interests which had organised profitable commercial activities on the import of industrial and other goods found their source of profit threatened by the new import policies.

---

52. Soyasa, n.17, p.133.


55. Gunatilleke, n.12, p.17.
Foreign firms which were selling goods to the local market suddenly found themselves cut off from a lucrative, though small, export market. These firms were motivated to establish subsidiaries in Sri Lanka and thereby retain their markets. They were also persuaded to enter into joint ventures with local partners for the production of goods within the country. The prevailing pattern of trade and the commercial links that were already established had a decisive influence in the selection of foreign partners.

These industries were given heavy protection not only against competition from abroad but also from within the country through a strict system of granting approval for setting up of industries and allocation of foreign exchange for materials and capital goods. Thus by 1964, the coverage of individual import licensing amounted to 61 per cent of the total import bill.

Success Stories and Failures:

The result of this neo-merrantilist regulation of the country's foreign trade combined with industrial regulation proved a windfall for many new local consumer goods industries, manufacturing perfumes and toilet goods, canned fruits and jams, pickles, chocolates, detergents, razor blades, pharmaceuticals, radios and electrical goods. Since these companies worked under near monopoly conditions they began to exploit the captive consumer market and made

56. Ibid.

unconscionable profits.

The generous tax concessions further contributed to consolidate their gains. The foreign partners could make large remittances in the form of dividends which enabled them to write off their investment over a very short period of time. In certain instances, the average annual dividend was being consistently maintained at a level as high as 44-60 per cent.

But there was also the other side of the picture. Not all industries were successful; some of them were operating below capacity because of the import restrictions on intermediate and capital goods. Raw materials, spares and other capital equipments became scarce. Due to the high import content of industrial production, cuts in this import group had an adverse impact on industrial output.

Absence of Export Orientation in Industrial Growth:

Because of the balance of payment crisis, the government policies had a major slant on conservance of

58. Ponnambalam, n.7, p.47.

59. D.K.Fieldhouse presents a different view when he writes, "But from about 1960 onwards although tariffs and import restrictions tended to favour the concern as a local manufacturer, government control on imports, particularly of raw materials and intermediaries, together with increasingly severe company taxation, were likely eventually to affect profitability. One would therefore expect the best years for local manufacturing to last from about 1939 to the mid or later 1950s with a subsequent decline in profitability and prospects as high taxation and adverse government policies began to affect." Fieldhouse, n.51, p.317.

foreign exchange and this had largely been the influencing factor in creating the import substitution industries. The outcome was an almost complete absence of export oriented industrialisation. This had been a major weakness in the country's industrial policy and structure. Non-traditional exports remained at a very low level. Both the over-valued exchange rate and the government industrial policy favoured production for the home market as against the export market. The over-valued exchange rate which is a concomitant characteristic of an inward-looking strategy has a discouraging effect on the inflow of foreign private investment. At a time, when the country most needed foreign capital, these policies discouraged inflow of foreign private capital.

The experience of Sri Lanka during these years perhaps strengthens the view that import substitution as a strategy of industrialisation will not help in the lessening of the balance of payments constraint. The strategy makes the country become increasingly dependent on inflows of foreign capital (private and public) to maintain the real capacity to produce. Import substitution industrialisation may successfully create income and employment but the redistribution of income towards sectors and groups with high marginal propensities to import, results in the establishment of highly import intensive industries which eventually will have a detrimental effect on the balance of

Reason for Slow Pace in Private Sector:

The manner in which the industrial policies were implemented towards greater state participation in industry had a demoralising effect on the entrepreneurial enthusiasm of the private sector. Also, the uncertainty about the future and the fear of nationalisation (despite the assurance) discouraged large scale investment in industrial ventures by the private sector. It was during this period that the distribution of a wide range of consumer articles was taken over by the government through a network of government sponsored co-operatives and through the state controlled Co-operative Wholesale Establishments. Between 1961 and 1963 life insurance and general insurance were nationalised through the establishment and expansion of the Insurance Corporation of Ceylon. State control over banking was extended with nationalisation in 1963 of the Bank of Ceylon, which was the only locally owned bank in the island. Distribution of petroleum and kerosene was also nationalised and the assets of all foreign oil companies operating in Sri Lanka were taken over by the state. Under these circumstances, foreign capital could not be expected to flow into the country. The ultimate result was that Sri Lanka's industrial progress, especially during the early sixties, was moving at a snail's pace.

Other factors also contributed to the slow pace of industrialisation. Sri Lanka lacked almost all raw-material inputs including steel and petroleum products needed for modern industry. Starting industries with fully imported raw materials was out of the question in view of the serious foreign exchange crisis. The dearth of trained manpower and the lack of technological talents also contributed to industrial sluggishness. Perhaps the most important barrier to industrialisation was the smallness of the national market. The relatively small population and the low per capita income level placed a definite limit on the number of articles which could be produced in Sri Lanka purely for the local market without enormous sacrifice of efficiency.

The limited internal demand soon exhausted the potential for import substitution and the economies of scale was not available for expansion of large scale industries like paper, steel, cement, fertilizer, unless part of the output found markets abroad. "All in all" concludes Snodgrass, "the obstacles to full scale industrial development in Ceylon was formidable, though certainly not altogether insurmountable".

63. This was one of the reasons why Indian companies never thought of Sri Lanka for setting up joint ventures although there was a spurt in the growth of Indian overseas joint ventures elsewhere in the mid 1960s.

64. Snodgrass, n.6, pp.234-5.
The infrastructural growth in the island was too minimal. Except for power, other facilities had not grown enough to warrant smooth industrial development. Transport outside Colombo was still underdeveloped. Even the lack of adequate statistical data and other vital information essential for planning exercise and policy making had been the subject matter of adverse comments. The World Bank Mission highlighted the major discrepancies and methodological weakness in the national accounts.

Change of Government and Ideological Giant:

The heavy external dependence of the economy was a definite disadvantage because the behaviour of the economies of the rest of the world set limits to the country's capacity for action. Further, the change in government brought about changes in the emphasis on the different components of the plan, resulting in infructuous pursuits and wasteful expenditure. The U.N.P. government laid strong emphasis on food production and agricultural development in contrast with the S.L.F.P. government's view that the way to economic development and the effective measure of solving unemployment problem was industrialisation.

Successive governments in Sri Lanka laid great emphasis on social welfare and redistribution of income rather than on building an industrial base. While these objectives are


laudable, the consequence was that an unusually large share of the national product was devoted to social welfare expenditure, leaving very little for industrialisation. Table 10 in the Annexure brings out the over emphasis laid on welfare expenditure. As H.N.G. Karunatileke put it,

"economic planners in Sri Lanka have the view that the increase in G.N.P. alone is not a sufficient indicator of economic progress because even with a relatively high annual growth the G.N.P. could be unequally distributed resulting in serious income disparities. In view of this, there has been a great deal of emphasis on redistributing existing income and wealth."

No doubt by the record of poverty alleviation Sri Lanka's performance is creditable, but this was accomplished at the cost of growth.

**Transfer of Technology**

While analysing the growth of industry in Sri Lanka the types of transfer of technology that took place over the years should also be examined. In the early stages of industrialisation until 1955, the technology requirements of the country was less complex. As mentioned earlier, the transfer of technology meant obtaining technical information from foreign consultants and also from corporate bodies and industrial houses. As in the cases of Ceylon Ceramics Corporation, Ceylon Cement Corporation and Paranathan Chemicals the choice of technology was unsuitable and caused

---

serious operational problems. The investment by the state sector during this period was not also very large because of meagre resources. As a result, most of the industrial units were inefficient and unprofitable.

From 1956 Sri Lanka entered another phase in transfer of technology when the Government began to look to Socialist countries for assistance for some of the major industrial projects. The transfer of technology that was offered by the Socialist countries was in a package consisting of the following elements: (a) the pre-investment and feasibility studies; (b) the sale of the complete plant which was largely produced in their own capital goods sector; (c) the offer of the technology that went with it to enable the local enterprises to operate the plant efficiently; (d) the training of local personnel for this purpose and (e) the assignment of their own experts and technical personnel for the formulation of the project, procurement of plant and machinery, commissioning of plant and operation of the plant for a limited period.


70. Gunatilleke, n.12, p.12.
This type of technology transfer was naturally quite different from that of the private sector as there was no foreign ownership involvement or royalty payment for the technology. Due to constraint imposed by foreign exchange shortage, the state sector placed heavy reliance on technical aid from the Socialist countries on a 'turnkey' basis.

In the case of the private sector, industrialisation took place by importing technology from multinational corporate bodies which started their operation as foreign owned subsidiaries or as joint ventures or through local enterprises by handing over the process technologies, supply of machinery and equipment and the training of local personnel.

71. A list of major projects set up with assistance from Socialist countries is given below:

<table>
<thead>
<tr>
<th>Project</th>
<th>Country</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tyre and Tube</td>
<td>U.S.S.R.</td>
</tr>
<tr>
<td>Steel</td>
<td>U.S.S.R.</td>
</tr>
<tr>
<td>Flour Milling</td>
<td>U.S.S.R.</td>
</tr>
<tr>
<td>Fertilizer</td>
<td>U.S.S.R.</td>
</tr>
<tr>
<td>Hardboard</td>
<td>Romania</td>
</tr>
<tr>
<td>Hardware</td>
<td>Poland</td>
</tr>
<tr>
<td>Sugar</td>
<td>Czechoslovakia,</td>
</tr>
<tr>
<td></td>
<td>German Democratic Republic</td>
</tr>
<tr>
<td>Textiles(3 projects)</td>
<td>Poland and China</td>
</tr>
</tbody>
</table>

Gunatilleke, n.12, p.16.
personnel without equity participation in the firm.

72. A sample list of firms in each of the three categories, that had started during this period is given below:

**Foreign Owned Subsidiaries:**

1. Ceylon Oxygen Ltd. - Oxygen
2. Union Carbide - Drycell batteries
3. Warner Hudnut (Lanka) Ltd. - Pharmaceuticals
5. Singer Industries (Ceylon) - Sewing Machines Limited

**Joint Ventures:**

1. Ceylon Bulbs and Electricals Limited. (Tokyo Shibara and Mitsui of Japan) - Electrical Bulbs
2. Ceylon Glass Company (Mitsui and Co. of Japan) - Glass products, Bicycle tyres and tubes
3. Vythialingam and Co. (Kawasaki Steel Corporation and Marubeni Corporation of Japan) - Galvanised Iron Sheets
5. Usha Limited (Jay Engineering, India) - Sewing Machines

**Local Enterprises:**

1. Elephant Life Corporation - Dry Cell Batteries
2. Colombo Paints - Paints.

Gunatilleke, n.12, pp.19-22.
But the quantum of technology transfer to these enterprises was minimal and designed merely to enable them to be efficient production units. Innovative adaptations were not promoted in any significant way. There was no sustained efforts to build up research and development capability within the country.

To sum up, during the period between 1956 and 1965 Sri Lanka embarked on a programme of import substituting industrialisation. This strategy had only limited success and did not result in any transformation of the industrial base. The nature of import substitution at that time was such that production was confined largely to assembly and compounding of finished and semi-finished components and, compared to needs, frequently concentrated in 'luxury' items such as chocolates and refrigerators. To sustain this sector, large imports of foreign technology and raw materials became necessary, siphoning off even more foreign exchange.

The value of imported raw materials in 1965 formed 56 per cent of the total value of raw materials used in the organised manufacturing sector. Foreign exchange scarcity thus remained a critical factor in determining the pace of growth in this sector.


Dudley Senanayake Government and the Changes in Industrial Policy:

With the change of government in 1965 and Dudley Senanayake assuming charge as Prime Minister, the inward looking policies to cope with the balance of payments difficulties were revised. The new government was more favourable to free enterprise. During its term, several steps were taken towards liberalising restrictions on imports, promotion of exports and encouraging both foreign and local private investments. The new government attempted to generate major development efforts which incorporated a substantial investment programme in both agriculture and industry. The government naturally was in favour of market oriented policies unlike its predecessors.

For the first time in Sri Lanka's history the government made planning a serious business and established a new Ministry of Planning and Economic Affairs. The Ministry was under the direct charge of the Prime Minister. With the view to advising and making recommendations on the techno-economic problems of the various industrial sectors, the Ministry of Industries directed the Industrial Development Board to set up industrial panels for different groups and sectors. The Planning Ministry acquired specific functions of resource

---

75. Sharma, n.47.
76. Myrdal, n.8, p.359.
allocation through the control of the foreign exchange budget and the government capital budget. The planning role was transformed from one of plan formulation which was essentially advisory in character to one of economic management.

But these panels could not make much headway. They were only able to prepare a number of sectoral programmes of action on an annual basis mainly for agriculture and public sector industry. Private sector was looked after through the allocation of further foreign exchange by the Foreign Exchange Budget Committee which also functioned in close association with the Ministry of Planning.

In order to dispel the fears of foreign investors and encourage flow of foreign capital, the government agreed to be more generous in giving compensations. The threat to nationalise foreign plantations was quietly but definitely shelved. The government also strived to restore friendly relations not only with the World Bank and the International Monetary Fund but also with the United States, United Kingdom and other aid giving countries.

In early 1966, the government issued a new policy statement on private foreign investments in Sri Lanka. The statement highlighted a large and steady inflow of foreign capital and technological and managerial skills that were

77. Dahanayake, n.22, p.18.
78. Myrdal, n.8, p.359.
79. Ibid.
vital for the country's development efforts. The government offered certain facilities and concessions to private foreign investments and invited them into all areas of industrial production except certain essential and basic industries in which the previous administration had established public corporations. These basic industries, which were declared to be exclusive responsibility of the state, included cement, ceramics, paper, mineral sands, caustic soda and chlorine, plywood, steel, tyres and tubes, fertilizer and petroleum.

Industrialisation was expected to stimulate agricultural development based on local raw materials. Import substituting essential consumer goods and specific fields like textiles, construction materials and light engineering industries with export potential, were sought to be encouraged. Large state ventures were discouraged and new tax concessions and other facilities were offered.

Response:

In 1967, 29 applications from foreign investors were approved. These applications covered investments in motor car and jeep assembly, frozen sea foods for export, glass and glass products, aluminium, iron sheets, textiles and agro-chemicals. The foreign component of these investments

---


81. Ibid.
was reported to be about Rs.34 million.

Although foreign investments could not be attracted much, the impact of the concessions and facilities on industrial production by the existing units were encouraging. In the two years 1967 and 1968, the value of industrial production rose by 12.3 per cent and 46.6 per cent respectively. This was a tremendous progress compared with the pitifully low increase of 0.4 per cent in 1966 over the previous year.

**Exchange Crisis and Devaluation**:

Ever since 1960, the par value of the Ceylon Rupee had been maintained only by increasingly stringent control on foreign payments. In 1966, the export receipts declined sharply but the import bill increased considerably causing a large deficit in the trade balance. In 1967 the balance of payments position continued to worsen. Sri Lanka had to draw heavily on its external assets which reduced its gross external assets to the lowest level since 1940. The devaluation of the pound sterling in 1967 by the U.K., Sri Lanka's largest trade partner, and the cumulative effects of the almost continuous deterioration in the balance of payments in the preceding years, ultimately led to the


85. Ibid.
The Sri Lankan rupee was devalued by 20 percent on November 22, 1967. This decision created more favourable effect in the case of exports originating from industrial production. Upto 1967 exports did not belong to industrial category. But the few that were existing and a couple of others that came into being in the year following the devaluation showed considerable improvement. Not only the volume of exports increased after the devaluation but also their foreign exchange earnings; the latter increased by 33.0 percent in 1968 over the previous year. The overall increase in the value of minor exports was greater than that of their volume.

A new scheme known as Foreign Exchange Entitlement Certificate (F.E.E.C.) scheme was introduced in 1968 under which import liberalisation in a gradual and selective manner was introduced. For the first time since 1961, attempts were made to relax restrictions on import of machinery and raw materials on a more realistic basis. These increased imports had a striking impact on the level of industrial development. An upsurge in industrial production was observed immediately after the introduction of F.E.E.C. scheme. There was hardly any lag in the production response to the import liberalisation.

86. Ibid.
Growth of Manufacturing Sector:

In 1968 the value of total industrial production increased by 46.6 percent over the previous year and in 1969 and 1970 it increased by 16.3 percent and 19.6 percent respectively. The remarkable growth in 1968 was probably due to the immediate release of stocks of imported intermediate and investment goods, built up earlier by traders due to uncertainty about the future. With clear indications of gradual liberalisation under the F.E.E.C. Scheme these stocks no longer had to be piled up. As imported inputs began to flow freely into various sectors of the economy, the volume imported was determined not by speculative demand but by effective demand. In fact, the volume of imports of intermediate goods in the years 1969 and 1970 fell slightly. This was probably because of the release of stocks built up earlier.

By the year 1970 the value of private foreign investment in manufacturing amounted to Rs.100 million of which Rs.54 million was in the cigarette and tobacco sector. Apart from these, local manufacturers without foreign collaboration established a brewery, synthetic textile factory and manufactured motor spares, rubber goods.

---

90. Dahanayake, n.22, p.130.
91. Ibid.
ball-point pens, transistor radios and watches.

The manufacturing sector grew at 12.6 percent per year between 1966 and 1969 which was at a much accelerated rate compared with the 9.8 percent for the entire period from 1960 to 1969. But these were the industries which came into existence for the purpose of producing substitutes for the semi-essential or luxury imports in those years. Their relevance to the social and economic needs of the country was marginal. As the economic problems increased they proved to be the source of much of these misallocation of the scarce resources.

Since the Senanayake government made agriculture the 'spear-head' of the developmental effort, it could not ensure a 'balanced growth' between agriculture and industry. Industrial development and agricultural development have too often been viewed as conflicting objectives, and simultaneous efforts in both directions is difficult in many countries owing to resource constraint. There could perhaps have been a bigger push to industrial growth in Sri Lanka during this period but for these circumstances.

95. Dahanayake, n.22, p.131.
But as though to offset this growth in agriculture the price of tea fell and fell down in nominal terms from 1954 when it fetched Rs.2.61 a pound until 1969 when it reached a low of only Rs.1.53 per pound. The declining prices of tea led to lower incomes throughout the country, the amount people were left with to spend on manufactured goods fell and the country started to de-industrialise. Employment in industry declined by one-third, the labour force grew faster than jobs and unemployment reached the million mark in the early 1970s.

Although the planning concept was introduced into the economy, the crucial social and political factors were ignored in making the plans, thus leading to failure of logically impeccable projects. Ceylon needed higher rate of development to bring about a progressive transformation of living standards but political compulsions stood in the way of effective reversal of priorities and significant reallocation of resources in favour of development. Development as a step to further development in the race to "catch up" with advanced countries was ruled out because

postponement of gratification of immediate wants in order to enrich posterity is unacceptable to the masses of countries which have the freedom of choice between these alternatives.

The 1970 Elections:

Despite the improved performance in the various sectors of the economy during the late 1960's, reflecting in the improved annual growth rate and the achievement of an impressive welfare record, the U.N.P. was badly defeated at the polls in 1970 and the United Front led by S.L.F.P. was given an unprecedented two-thirds majority in the Parliament.

In the previous elections, the economic problems of the country were relegated to the background and the socio-cultural palliatives of language and religion and the projection of Sinhala Buddhist national identity were presented as the main issues of the contest. However, in the 1970 election, the economic issues were brought to the forefront. It was, therefore, initially expected that the new government would devote itself more to solving the economic problems facing the country.

The Five Year Plan and the New Policy:

In 1970 the manufacturing sector as a whole accounted


103. Ponnambalam, n.7, p.95.
for 16.94 per cent of the total production in Sri Lanka's economy. The Five Year Plan, 1972-76, made provision for the establishment of several large scale basic industries in the public sector as well as the expansion of small scale industries in the private sector, envisaging an annual growth rate of 8.6 per cent.

The industrial policy of the new government represented a radical departure. It was largely influenced by the government's commitment to a socialist model of economic development. The following statement by the Minister of Industries summarises the government's industrial policy:

We are definitely committed to a socialist policy. Socialism means that industry, basic industry - those that are most essential to society - would be either state owned or to a certain extent controlled by the state to meet the needs of the people.

Based on this premise the new industrial policy declared that heavy basic and essential industries would be under state ownership or under state control and those industries, ownership of which should not vest with the private sector for reasons of technology, scale or size or public interest, would be left to private enterprise.

Emphasis on Public Sector:

The public sector industries had begun to proliferate from the time of the S.W.R.D. Bandaranaike government in

---

1956 and the number of public manufacturing corporations increased between 1958 and 1970. The government considered the growth of public sector economic activity as the key instrument for the achievement of socialism that it had promised voters at the time of 1970 elections. The maiden speech from the Throne stated:

The heavy and capital goods industries and other suitable basic industries will be state owned. Other industries will be assigned to the co-operative and to private enterprises". 108

And the Five Year Plan stated:

A necessary corollary of the country's commitment to the building of a socialist society is the expansion of the public sector economic activity. A socialist economy must rely heavily on the surpluses of profits generated by public sector enterprises for the savings necessary for further investment. This clear lesson emerges from the experience of all countries which have taken the socialist road to development". 109

The speech from the Throne further reiterated state control and participation in its plans for development.

The import trade in all essential commodities will be handled by the state. The share of the state in export trade will be progressively expanded in order to ensure that bilateral trade agreements with other countries are properly carried out to promote new market for our traditional and non-traditional exports and to rescur our export trade in domestic produce from the doldrum of falling prices. Appropriate state enterprises will be set up for this purpose. The central wholesale trade


in all import of essential commodities and in such local commodities as might be necessary will be handled by various state and co-operative organisations. 110

Several measures were taken to strengthen the public sector and also to make the private sector fall in line with the development plans of the government. The period from 1970 witnessed a rapid expansion in the role of the public sector indirect production and distribution. The island's graphite mines were taken over from the private sector; a large public sector project for manufacturing urea fertilizer, at an estimated cost Rs.340 million was in the implementation stage. The big Mineriya Textile Mill was also planned and started with Chinese help during this period. Work on a paper mill at Embillipitiya at a cost of Rs.10 million was started in 1972.

The second cement factory of the island was commissioned in 1972 at Puttalam followed by a third at Galle. All these were public sector projects intended to boost the participation of state sector in industrial production and to favour the growth and development of industry through state monopoly venture.

110. Throne Speech, n.108.
112. Ibid.
113. Ibid.
Unutilised Capacity and Inefficiency:

The most serious problem faced by the government was unutilised capacity of major industrial undertakings. Because of the nature of the imported machinery and technology, installed capacities were much in excess of immediate demand. Despite all efforts to correct the problem, 60 per cent of the installed industrial capacity remained unutilized in 1974. For example, the National Textile Corporation had an installed capacity ranging from 19.4 million pounds in 1972 to 22.4 million pounds in 1976. As against this, the actual production in 1972 was 8.8 million pounds and 4.6 million pounds in the first half of 1977. Similar situations prevailed in the National Milk Board, the Sugar Corporation and the Cement and the Steel Corporations. In 1976-77 alone over Rs.150 million had to be spent on textile imports, after having invested over Rs.600 million in the textile industry.

Another intractable problem was the management of these public corporations. From the beginning, the tradition was to appoint political protégés and relatives as Directors. With the United Front Government, it became worse as many politicians got appointed to the Boards of Directors of these Corporations. Utilising the public

115. Central Bank of Ceylon, Review of the Economy 1981 (Colombo), Table 2.5.
116. de Mel n.111, p.17.
117. Ibid.
enterprises sector for distribution of political patronage, caused serious adverse effects on the efficiency and integrity of public enterprises.

Between 1970 and 1975, capital investment in public sector enterprises more than doubled. The bulk of new investment in the industrial sector went into new capacity in cement, textiles, plywood, paper, caustic soda and chlorine. A sum of Rs.90 million was spent on an oil exploration project in Pesalai and Mannar with no positive results whatsoever in a vain attempt at petroleum prospecting. On an investment of Rs.2,964 million as on 1975, the state industrial corporations returned a total profit of only Rs.69 million. The four corporations which had persistently been running at a loss were the National Milk Board, Oils and Fats Corporation, Fisheries Corporation and the State Hardware Corporation.

The 1971 Insurrection:

The Janata Vimukti Peramuna (J.V.P.) insurrection in April 1971 affected the political and economic development in the island. The insurrection could be said to be the major cause of the complete economic stagnation in the year 1971 and the low growth during the next two years, besides

118. Karandawala, n.11, p.63.
120. de Mel, n.111.
weakening the country's capacity to adjust to external economic shocks. The stagnation in capital expenditure in 1971, despite the provision in the budget and the failure to shift resources in the subsequent years, by a sufficient scale towards investment, were all the after effects of the insurgency.

Private Sector:

As for the private sector, the government tried to follow an industrial strategy aimed at encouraging those industries that were manufacturing goods for export. Inducements were provided in the form of a five year tax holiday for firms already established and an eight year holiday for new firms. Further, incentives included the F.E.E.C. rate of exchange, Convertible Rupee Accounts, tax exemption on shareholder's dividends, customs duty rebates and special foreign exchange allocations for raw materials and machinery imports. In consequence, a shift towards the export market became evident in the 1970's.

Terms of Trade and Import Restriction:

With import prices increasing faster than in the previous years, the rate of deterioration of the terms of

trade started sharply. Since the foreign reserves were getting depleted, the external resource gap was financed mainly by increasing the level of foreign borrowings. This had created a new dimension to the balance of payments problem, namely, increasing foreign debt servicing needs. In 1972 the total debt servicing cost constituted a substantial per cent of the total foreign exchange earnings of the year.

As a natural reaction to this development, the government started tightening the import programme causing heavy reductions in the import of intermediate and investment goods. The allocations of foreign exchange to private sector industries was drastically reduced. The growth rate of industrial production, dropped from 19.6 per cent in 1970 to 13.5 per cent in 1971; 10.6 per cent in 1972 and 8.5 per cent in 1973. Thus, the tempo of industrialisation stimulated by the liberal policies of the late sixties was greatly reduced.

Radical Legislative Measures:

One important development in the industrial policy was the enactment in December 1970 of the Business Undertaking (Acquisition) Act. This Act provided necessary powers for the government to take over any business undertaking that

employed more than 100 persons. A compulsory savings levy and capital levy were also introduced, and a ceiling on incomes at Rs.2,000 per month was introduced. The compulsory savings levy was such that it had the effect of planning a ceiling on individual incomes at Rs.3,500 (per month) and a ceiling on all company dividends at 12 per cent.

Consequent upon the passing of the Land Reforms Law in 1972, British tea estates were taken over and the number of tea planters dropped from 100 to 30 by the spring of 1972. The Land Reforms Law set the maximum as 50 acres per family unit. The Land Reforms Commission took over 20 per cent of the coconut estate land, 14.7 per cent of the rubber estate land and 24.7 per cent of the tea estate land. About 5,000 land owners were affected by this legislation. The Rent Registration Act froze rents at 1969


levels and the ceiling by Housing Property Act limited the number of houses a person could own. Such marked leftist propensities were due to the influence of the L.G.S.P. and C.P. elements in the coalition.

Tight State Control:

Import of raw materials for the private sector was routed through the public sector corporations such as the Ceylon Steel Corporation, Ceylon Ceramics Corporations and National Paper Corporation. Some of these Corporations also maintained controls on the quality and price at which raw materials were imported by the private sector. This trend of exercising tight control was extended eventually to acquisition of certain private sector industries for management by the public sector.

These measures created certain amount of misgivings in the private sector. With the government starting to use the Business Acquisition Act to take over industries by the sectoral development corporations, there emerged a gloomy prospect for the future of the private sector in Sri Lanka. There could be nothing more frustrating to the private sector than the uncertainty about the future.

136. The nationalising trend continued even later in the S.L.F.P. period when the Wellawatte Spinning and Weaving Mills and the J.D. Textiles were taken over by the State. Tissa Balasuriya, ed., Towards A Socialist Society in Sri Lanka (Centre for Society and Religion Colombo, 1977), p.6.
Foreign Investment:

In the matter of foreign capital, the government did not follow a consistent policy. Under its industrial policy, foreign capital had only a marginal role to play, the economic growth of the country to be achieved mainly by government efforts. The contribution that foreign capital can make can be only marginal. But in 1972, the government issued a White Paper on Foreign Investment which stated that foreign capital had an important role to play in the economic development of the country. But the policy declaration did not contain any guarantees regarding repatriation of capital or interest or against expropriation without compensation. The U.F. which during the elections had severely criticised the previous government's dependence on foreign financing, committed a volte face and provided a blueprint for the entry of foreign private capital into the country thus shifting the emphasis from inward orientation to outward orientation in industrial growth. The report of the Special Committee of the Export Promotion Secretariat concretely expressed the idea of a

---

137. The Budget Speech of 1971 mentions, "The economic growth of this country can be achieved mainly by our efforts. The contribution that foreign capital can make can be only marginal", Budget Speech 1971 (Colombo), p.5.


Free Trade Zone. As regards foreign investments the significant development in the 1970s was the laying down of the principle of participation with local capital as a rule, thus promoting the concept of joint ventures. The Five Year Plan mentions,

if the proposal is for investment in the private sector the undertaking should be in collaboration with local enterprise. The general rule will be that Ceylonese collaboration should hold the greater part of the shares and retain effective control. Relaxation of this requirement may be considered in exceptional circumstances.141

The White Paper of 1972 relaxed this slightly saying,

if the proposal is for investment in the private sector, the undertakings should generally be in collaboration with local enterprise. The general rule will be that local collaborators should hold greater part of the shares and retain effective control. Relaxation of this requirement may be considered in exceptional circumstances so that the major shares or even the entirety of the investment could be foreign, where the benefits to Sri Lanka will be substantial.142

Thus the government started taking a more pragmatic stand on foreign investment in its anxiety to secure more foreign participation.

Yet the response was disappointing. Despite the White Paper, no foreign private capital in fact entered the country and four years later the Finance Minister had to


propose a Foreign Investment Guarantee Law with specific guarantees to foreign investors. No such law, however, was enacted during the extended lifetime of the government.

Concentration of Wealth:

Another lopsided development was the disproportionate growth of wealth of a few families and the high degree of concentration of ownership. The process of economic development in Sri Lanka had so far tended to give stimulus to capital accumulation in the hands of a few wealthy families who have, in the main, been the beneficiaries of the tax holidays and reliefs granted. Out of a total investment of Rs.275 million, as much as Rs.205 million was held by 11 family groups. The concentration of ownership in manufacturing was also evident in the fact that in 1974, 89 per cent of output was produced by 140 firms, just 9 per cent of the total number of firms in the manufacturing sector.

Efforts to Use Local Raw-Materials:

Two main criteria adopted by the government in encouraging new manufacturing industries were the extent to which they would utilise local raw materials and whether

143. Wijesinghe, n.147.
144. Ponnambalam, n.7, p.125.
they could be located away from Colombo. However, a substantial portion of raw material inputs in private sector industries in 1974 were still imported and the total value of foreign raw-materials in that year amounted to Rs.1,635 million. Thus the first objective of the government's industrial policy was clearly not achieved.

The objective of locating industries away from Colombo was also not achieved. The geographical distribution of private sector industries hardly changed. Nearly 70 per cent of the registered manufacturing establishments in 1974 were still located in and around Colombo and they accounted for 90 per cent of the total value of industrial output. Moreover, 76 per cent of industries producing 96 per cent of output were located in the Western province.

Global Inflation Affects Sri Lanka:

Because of the high content of imported raw materials in Sri Lankan industry (about 73 per cent on an average over 1972 - 74) global inflation had a direct and serious impact on production costs. The output decline in 1974 was due mainly to the rise in the price of raw materials which not only caused the volume of inputs to be reduced but also reduced consumer demand for certain items on account of the cost induced price increases. The private sector industries received low priority in the allocation of imports and the

147. Ibid.
149. Ibid.
overall capacity utilisation fell to 40 per cent and at much lower levels in certain sub-groups.

**Policies being Reversed:**

Realising the gravity of the situation, the government relaxed the hold on imports and larger allocations were made for industries. With the exit of the Trotskyite Finance Minister N.M. Perera from the Cabinet, perceptible changes in the policy were brought in. Increased supplies of agricultural commodities for processing, after the good 1974 harvest, permitted significant growth in manufacturing output.

The new Finance Minister Felix Dias Bandaranaike departed drastically from the policies of his predecessor. Free market in paddy and rice was restored and the government's role in this sphere was reduced from that of monopoly purchaser to a competitor with private traders. Compulsory savings and the ceiling on incomes were removed; taxes were reduced substantially from the levels they had reached through the budgets of N.M. Perera. Perera's proposals for heavier taxes on wealth were jettisoned.

The Prime Minister moved along with powerful sections of government distinctly to the right and even accepted U.S. food aid. Later, with the Sri Lanka Communist Party leaving the coalition government in protest over its

---


151. De Silva, n. 35, p. 553.
Handling of a general strike at the end of 1976, the swing to the right became even more pronounced.

**Lack of Systematic Efforts at Industrialisation:**

For many politicians and planners in the less developed countries, industrialisation and development are synonymous with one another. The industrialisation of basically agricultural, primary export-oriented economy was seen as the means by which the chains of dependence forged during the colonial period would be broken, matching the newly acquired political independence with economic independence. Sri Lanka's politicians also did believe in such concepts but were slow in implementing the idea of industrialisation.

Unlike India, Sri Lanka's industrialisation efforts have been less planned and prompted by frequent necessity to meet economic crisis in the country. Only when the foreign exchange crunch was experienced did they think of industrialisation as a measure to conserve foreign exchange through import substitution. Historically import substitution has always accompanied economic growth in the less developed countries. Perhaps 50 per cent of industrial growth in a large number of countries was due to import substitution industrialisation, observes an analyst.

---


The lack of coherent industrial policy based on practical, pragmatic and realistic lines was a fundamental drawback during this period. Entrusting the work of building up and running large industries with the Communist bloc of countries is often blamed as one reason for the slow growth of industrial development. The steel mill at Uruwela built by the Russians made little headway. Again, the oil exploration work with Russian technology at Mannar became a very expensive experiment with no positive results whatsoever. The Tulhiriya Textile Mills (built with Chinese know-how) was working at not even 60 per cent of the installed capacity. These were some of the instances of the public sector ventures proving to be a dead weight on the economy. Thus, at a time when the country needed all the fillip and encouragement to push ahead with its industrial expansion, such frustrating experiences retarded the growth.

To illustrate further, while the capital expenditure of the government rose from Rs.1,026 million in 1969/70 to Rs.3,363 million in 1976, an increasing proportion of it was given in the form of capital contributions to public corporations. Such capital contributions to public sector at the end of 1975 stood at nearly Rs.4,600 million.

155. de Mel, n.111.
156. Ibid.
157. Ibid., p.17.
158. Ibid., p.24.
but the contributions of these corporations to the consolidated fund in 1976 amounted to only Rs.162 million or about 3 per cent.

Unemployment:

During the S.L.F.P. rule, it looked as though no breakthrough could be achieved. The government was principally concerned with crisis management and emergencies. Stagnation and deterioration were obvious, unemployment was mounting and queues and controls were everywhere. Sri Lanka was in a state of emergency throughout most of Srimavo Bandaranaike regime of 1970-77. When the leftist parties went out of the alliance, the government had to concentrate more on preserving its existence and there could be no time for any planned activity.

The failure of the economic policies resulted in massive unemployment. The people were disgusted with the infighting within the ruling coalition. The racial minorities were alienated by the government's intransigence. The youth and students were frustrated at the absence of a creative opportunity for employment and education. Even the workers were feeling the weight of the repression.

159. Ibid.
161. Balasuriya, n.102.
Economic Stagnation:

There was complete stagnation in every sector of the economy. The balance of payments had reached a stage of economic deterioration. External reserves were run down to critical levels and the debt service burden was fast approaching unmanageable proportions. With an emergency in force from April 1971 to February 1977, political activities were severely curbed and citizen's liberties circumscribed and judicial independence substantially abridged. These developments brought into the 1977 election campaign a set of new issues, guarantees of personal liberties, freedom from arbitrary arrests and detention, control of police excesses, the rule of law, independence of judiciary and the repeal of the ex post facto penal laws.

Reluctance of Foreign Capital:

This chapter is intended to acquaint the reader with the formative stages of industrialisation in Sri Lanka. Although Indian joint ventures had started moving into various countries in a big way during this period Indian entrepreneurs did not take any interest in Sri Lanka. The reasons are quite obvious. The country was fighting shy of receiving foreign capital during the S.L.R.P. period from

---


164. Ponnambalam, n.7, p.147.
1956 to 1965 and (inspite of feeble efforts) also from 1970 to 1977 which constitutes nearly three quarters of the period we have covered.

The socialist policies pursued by the government resulting in nationalisation of foreign interests largely distorted the image of the country in the eyes of foreign investors including Indian. The efforts to achieve greater economic interaction with the Communist bloc of countries encouraged public sector industrialisation in Sri Lanka. This had partly closed the doors for Indian investment in the context of India promoting joint ventures only by private entrepreneurs.

The pace of growth of industrial development was so sluggish that inspite of promotional efforts, foreign investors did not choose to invest in the island. Whatever new industries came up were mostly from countries like Britain with whom Sri Lanka had long traditional ties. The lack of private capital and of sizeable number of businessmen with industrial experience were also responsible for the slow growth.

The Indian Joint Ventures:

Inspite of these discouraging factors, an Indian joint venture was set up in 1961 for the manufacture of sewing machines and electric fans. Its slow growth in the early years could be attributed to the shortage of raw materials in Sri Lanka. Most of the raw materials had to be imported leaving the industry totally dependent upon import licences and allocations.
The Indian joint ventures that were established abroad in the middle of 1960s mostly belonged to textile and engineering industries. With the total non-availability of cotton and the big Chinese presence in the Sri Lankan textile industry, Indian textile mill owners naturally did not prefer to go in for collaboration with Sri Lanka. The total absence of metal based inputs and the acute import constraints had perhaps discouraged Indian collaborators to think of engineering joint ventures.

The only other Indian joint venture that was established in Sri Lanka in 1968 for the manufacturing of P.V.C. cloth again had to depend upon imported raw materials. Indian industrialists who were already experiencing shortage of imported inputs in India could not be expected to entangle themselves in joint ventures on a foreign land which was passing through foreign exchange crisis.