

## FINANCING NON-SUBSIDISED MASS EMPLOYMENT

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Former Secretary-General founding the Colombo Stock Exchange and a former Member of the GCEC Board, current head of Wiros Loh Institute, an academic institute doing autochthonous studies in Economics. It also does some policy research. The subject matter of this paper was initially presented to the Government (Alleviation of Poverty) by the author in December 1987. A paper presented at the December 1988 SLAAS sessions by the author and Kosala Jayasinghe provided an elaboration of that original scheme. A prominent banker and several others who wish to remain anonymous contributed greatly to the development of the main idea. The author remains responsible solely for this article.

The Socio-Economic survey of 1985/86 by the Department of Census places unemployment at 840,252 in its preliminary figures. The employed population was estimated at 5.1 million of which 2.99 million were employees. There has been much discussion on the interpretation of these figures. It has been confused by the fact that the number of active accounts at the EPF stood at only 1,173,000 at December 1987. However it is clear that there is widespread under-employment and unemployment in Sri Lanka. Officials involved in this subject have stressed that the situation is acute in the South of the island where, apparently, there has been less investment by the public and private sectors.

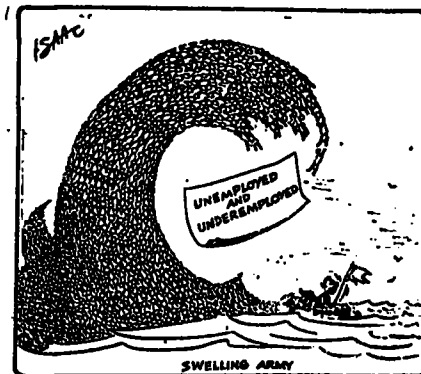
It appears that this problem is a general one in developing countries and solutions are currently associated with the generic term "alleviation of poverty program." Among approaches in other countries are the following. In Brazil there is a program headed by a new Ministry of De-Bureaucratisation. In Peru, following studies by Hernando De Soto and others, there is an informal producers development program. It is suggested that the very severe unemployment problem in China is being solved by the enterprise program there. Following the close of this study, an

evaluation of the Philippine program was received and this is discussed in the addendum as it is a highly recommendable one.

A second strand of data also motivated this study. Investment in Sri Lanka as depicted by the gross capital formation by private sector and corporations was Rs. 33 billion in 1984 and Rs.35 billion in 1987 in current terms. As the value of the Rupee has been clearly eroding due to inflation, investment in real terms has been falling. The type of investment that Sri Lanka, especially through foreign funded schemes, has been promoting has consisted of imported goods. The import of machinery and equipment has been falling from 209 million SDR in 1983 to 174 million SDR in 1987. The value of an SDR has been close to the US Dollar and rising slowly. But the Yen and DM rose dramatically within this period. The yen doubled in value, nearly, after 1985. As those of our imports which are from Japan and Germany are quite high, the investment opportunity represented by our spending probably diminished dramatically. The World Bank Handbook states that Sri Lanka's average annual real growth rate of investment in 1980-1985 has been a negative 4.4.

These figures and the interpretation of them may be disputed. However it is clear, and has been for a while, that Sri Lanka has been suffering a declining in-

1. The White Paper on the Alleviation of Poverty may be referred to in this connection. Discussions on the numbers and structure of demographic features are available in several excellent articles by Raja Korale, Dept. of Census and Statistics.
2. The World Bank publication of 1987, *The Alleviation of Poverty under Structural Adjustment*, by Lionel Demery and Tony Addison, provides a discussion. However the use of a phrase is not to illuminate it, so, I would recommend Hernando De Soto *The Other Shining Path (El Otro Sendero)*, 1986, 1987, 1988, eds. The Source for figures that follow is the *Central Bank of Sri Lanka Annual Review*, except where otherwise stated.



vestment rate for the past five years or more.

This has occurred after a spurt in investment and during a period of increasing imports and spending. One might note, as a snippet, that imports of passenger cars increased. New registrations have increased from the 5-6 thousand a year range in 1980-1984 to eleven thousand a year in 1986-1987.

It may be noticed that the decline in investment accompanied a decline in real wages. The real wages index published by the Central Bank for workers in Commerce and Industry declined from 105 in 1980 to 94 in 1987. In the developing countries that had negative rates of growth of investment in 1980-1985 it may be observed that many had declining or low rates of growth of real wages for workers. This suggests that the decline of domestic investment may be associated with a declining consumer market at the mass wage-earner level.

The decline of investment, probably due to low wages, would have reduced employment opportunity. The low wages were upheld as a policy, as may be seen in any investment promotion brochure published by the GCEC or FIAC in this period, to attract investment. However at 31st March, 1984, employment in the GCEC was below 30,000 in active employment and indeed in all the Stock Exchange listed companies (167 active companies) was 47,000.

Experts who have studied some or all of the aspects considered in the above characterisation may find detailed objection to this. However the general thrust of the above two strands of data have withstood several presentations and appears both correct in thrust and extremely serious in implication. It seems clear that the Sri Lankan econo-

my is being engulfed by a tidal wave of idle persons while investment policy is dealing with a handful of persons, though no doubt in a sophisticated manner.

This paper reports the results of several policy research studies I conducted to develop a viable method of handling this situation. It is restricted to the development of a financing method.

### COST OF A JOB

In all employment generation schemes, an initial consideration is the start-up and continuing financing of the work. In so far as foreign funds for financing imports or other expenditure is concerned there is at present in Sri Lanka a need to repay by foreign earning. Owing to the policies being followed, it is also required of schemes that they be self-financing. This is, apparently, a needed budgetary policy. This presentation and analysis has to be constrained to this framework, as set by the Ministry of Finance, as we were informed.

The principal concessional financing scheme in Sri Lanka is the Small and Medium Industrial loan scheme financed by the international agencies. In the review by the World Bank at the end of 1987, prior to further funding of this scheme, it was found that loans had been given to agriculture and service business as well as industry. Considering data not too far away from the date of review so as to minimise the effect of the eroding Rupee, it was found that the loan cost per job created averaged over Rs.200,000. This figure was in conformity with results of evaluations of similar loan programs in Brazil and in Thailand, converted at prevailing exchange rates.

This could be considered a starting point. The Central Bank Industries division (research) suggested a range from Rs.80,000 to over Rs.300,000 for the cost of a job in recognised industries. Their survey does not permit direct calculation of this figure as their's is an annual flow survey. This figure includes equity as well as loan. The Arthur D. Little Inc. study presented to the Government in 1983 encouraged investment in specified sectors with details of private sector development. However it did not specify a job cost of

investment. They did present a cost flow calculation for recommended domestic production sectors. The raw material and power costs per employee ranged from Rs. 1 million to over Rs. 200,000 annually.



The capital cost, loan and equity, per employee as projected, and realised where projects are in operation, in FIAC projects was also considered. Nearly three hundred very diverse projects were surveyed. The cost of one job had an upper level of around Rs. one and a half million. For service bureaus and offices, costs were down to Rs.18,000. However the median was around Rs.225,000.

Businessmen have not disputed these figures, and, in the quoted company sector, have pointed out that many overheads have been left out that should belong in an economic analysis in the capital costing.

### PROBLEM

The total cost of creating sufficient jobs under the present open system in what are considered ex-ante to be viable projects entails a financing requirement of impossible proportions. 800,000 jobs at Rs.200,000 a job would cost Rs.160 billion in capital spending alone. Moreover, 200,000 persons roughly enter the labour force every year.

To solve this problem a different tack has to be taken. The following methodology suggests itself.

The feasible range of investment capital per job was taken as Rs.13,000 to Rs.5,000 in 1988 — Rs. A median of Rs.10,000 was aimed at. The projects undertaken under this scheme must be voluntary and therefore also subject to banking feasibility and viability.

In the Research reported at the SLAAS (vide footnote), the results of this survey were reported. A preliminary survey was made of persons who had been successful with their development loans, mainly small and medium industry loans, as to their current experience. These businessmen were incidentally by no means small businessmen. They stated areas in which they had success and where they had orders in hand. They wished to be funded generally to very large amounts to be able to meet these orders. They had good track records.

It was discussed with these persons whether they would simply agree to a process where funds would be provided not to them but to informal sector workers who would provide product to meet the orders. This was agreed to by the businessmen. It was envisaged that there would be no investment in managerial control nor infrastructure. This would enable the financing limits suggested above to be met.

### SCHEME

The following scheme suggested itself. The businessmen act as buyers of the final product, subject to their quality control, and which they use to fulfil the export orders. They provide the requisite technology. The bank involved would finance the capital, including working capital, which may be under centralised storekeeping arrangements. The capital is simply given to informal sector workers in some form of self-organisation. It has appeared to me that working groups that have had experience of doing a project as the NHDA housing communities would be an appropriate association of producers. However, for the purposes of this paper, the form of this does not concern us at the moment. The bank has to be repaid. This would be by an export levy imposed at point of export.

It should be clear that this scheme is envisaged for export only, basically, items that should not have been produced in any similar scale prior to or outside the scheme.

Several bankers were surveyed and it was rapidly realised that there was great

enthusiasm for the scheme and that in fact it would be possible to negotiate down the rate of return provided to the banks. For it covered their requirements.

The Central Bank has been regularly mopping up excess funds in the depressing economy. By release of such funds, and other sources, sufficient funds would be available. The issues of management and legal dimensions have been studied but only the financing plan, being novel, is presented here. The types of projects varied greatly. The range included ornamental fish, electronic assembly, fishing, agro-processing, sericulture, special handwork products as kimonos, embroidery, hand-made or assembled ornaments and simple ensembles, specialised agricultural (intensive market type) products, etc. At his point there is considerable trained expertise in a variety of these areas in Sri Lanka. As a crash program, some garment quota items could be released to this scheme from the GCEC, to fulfil geographical employment creation requirements.

### CONCLUSIONS

This was a practicality oriented policy study. The practicality of a of a new financing technique was all that was to be established. There were businessmen with successful track records in borrowing term development loans. They wished to participate and had orders in hand. Bankers with term loan experience and decision making seniority were willing to fund. So the scheme would be a practical one.

Curiously, resistance and very stiff resistance at that, was encountered, not at this practical level of person surveyed but with thinking Administrators. Among general public persons too I have come across the same argument. This is an adverse reaction to the "giving" of money. My use of that term with respect the provision of capital to the poor or informal sector (informal means not in a formal organisation as a corporation or company) was construed as a 'free money' scheme.

As there is a specific levy as well as price negotiations and interest rate negotiations involved, this scheme is not economically a 'free money scheme' but rather a non-subsidised scheme. In fact

our feasibility calculation was on the basis of ensuring a basic income to the informal or poor workers or worker associations. This was set at only Rs.2100 per month inclusive of profit sharing but exclusive of building up equity in the enterprise, which will mature effectively as the loan is paid off over time, i.e. the levy tapers off and more of the export price accrues to the workers.

However, I would prefer to point out that as a matter of policy it should be realised that "Capitalism arises out of Giving". This may appear strange to persons outside the field of Finance. For many persons usually come across capital in the form of inheritance from their parents or their spouse's parents. This often means acrimonious sibling squabbles or "Grabbing." However, in the creation of capital by entrepreneurs there is often an act of "giving" that occurred in the past which enabled the creation of the enterprise. It may have been a Bank Manager who stuck his neck out. It may have been an investor, even a close relative, who believed. But generally that Act of Giving is necessary. Successful banking does not proceed by taking or the Spirit of Taking. That would break down the client base. Every successful banker is psychologically attuned to Give or provide 'free money' so as to bring in business over time. That is the formula of success that an unsheltered practice would teach him or her.

### THEORY

Some persons have inquired why the situation described could have come

3. From George Gilder, *Wealth and Poverty*.
4. This is actually a very unrealistic constraint. In the creation of mass employment only exceptional mismanagement could have enabled such a situation. For Sri Lanka it would be more reasonable to base the strategy on the domestic market and to export to countries of similar or lower overall socio-economy as within SAARC.

about, as normal equilibrium economics does not envisage the opening pointed out by the scheme presented.

The reason is the malfunctioning of the Banking system. The Mercantile Establishment is allowed prime and easy facility by the Banks. However that is a very small and unenterprising group with respect to productive development.

There exist many good entrepreneurs. They are new to the banking system. They are able to borrow within the limits of their mortgageable assets and associate guarantors. The possibility of 800,000 jobs is well beyond their collective scope in this system. Moreover there is no share market nor venture capital market nor even appropriate markets for assets that reflect correct international prices. So they may have the orders and executing ability but have no method of financing. This scheme enables this financing while letting the banks and the brokers in the 'virtual' share market off the hook. For this reason the scheme is a specific financing remedy and not a general nor permanent policy recommendation.

### ADDENDUM

A word should be said of Corazon Aquino's Community Employment and Development Program. Its core is to not allow engineers to specify contracts but only allow them to prevent clearly unsound acts. Otherwise village organisations specify contracts for regular and special programs. The villagers in groups especially the unemployed, bid. The lowest tenderer gets the job. Moving earth by bamboos and gunnys instead of tractors is allowed. This also enables the villagers to participate. Fully, unlike in the Marcos years. Over 600,000 jobs at a cost below R.10,000 per job have been created in two years. A job is defined as giving two months pay by way of successful contract under the scheme. These persons can carry on thereafter. Over 60% of the beneficiaries have been hitherto never employed male youths. Unlike our scheme this scheme has not had to be constrained to be self-financing and self export financing.