

MACRO-ECONOMIC ASPECTS OF THE JANASAVIYA PROGRAMME

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The Janasaviya Programme draws attention to four basic aspects of macro-economic management — economic growth, employment, inflation and balance of payments. This paper will principally focus on these aspects. It will not deal with the incidence of poverty or its measurement. It will proceed on the basis that the levels of absolute poverty in Sri Lanka have reached the threshold of serious concern to policy makers regarding their social, political and economic impacts. Since the political and social dimensions are covered by other contributors, this paper will refer only to their economic consequences.

It is often asserted that economists do not pay sufficient attention to the problems of poverty. This is not entirely true. Those who have been dealing with the normative aspects of economics such as development policy and planning, have invariably come to grips with poverty issues. They have, however, differed in their approaches to resolving them.

For the sake of analytical convenience, it is possible to divide these approaches into those which advocate non-interventionist "trickle down effect" solutions and others which prescribe government intervention in some form or the other. In practice however, there is today a perceptible convergence towards the latter approach, the outstanding difference being in the degree of emphasis given to economic growth vis-a-vis poverty alleviation. This difference is also reflected in the methods of intervention advocated.

It is in this context that one must try to understand the attitude of international organisations such as the World Bank and the IMF. These organisations have been traditionally considered to be overly concerned with economic growth and monetary stability in less developed countries (LDCs) to the detriment of poverty alleviation. However, recent pronouncements made by the World Bank President and the Managing Director of the IMF seem to indicate that increasing attention is being paid by these

institutions to questions of poverty in LDCs. This change in emphasis reflects, on the one hand, recognition of a long standing concern of policy makers in third world countries about the social and political consequences of poverty. On the other hand, it reflects some new thinking among economists regarding the possible economic consequences of poverty, particularly its consequences for growth. Some prominent examples of this new thinking are reflected in Drownoski's "levels of living", the ILO's "basic needs", Chenery et al's "redistribution with growth" and, more recently, in Amartya Sen's "entitlements" and "opportunities"

It is not possible within the narrow confines of this paper to do justice to all these interesting theoretical developments which have made economists more sensitive to the questions of poverty. Essentially, what they suggest is the need to invest in human capital, not only as a means of overcoming poverty but also as a way of promoting development.

Macro-Economic Situation

Before we embark on an analysis of the macro-economic situation in Sri Lanka as a backdrop to the JSP, it is necessary to reflect briefly on the fundamental factors affecting poverty

Obviously, income distribution is an important factor. But two other factors of equal importance are the level of per capita income and, relatedly, the macro environment and corresponding policy framework within which redis-

Drownoski, J. *Studies in the Measurement of Levels of Living and Welfare* — Reprint No. 70-3, (1970) Geneva United Nations Research Institute for Social Development.

2. ILO, *Declaration of Principles and Programme of Action of the World Employment Conference*, Geneva (1976).
3. Chenery, H. Ahluwalia, M.S., Bell, G.L.G., Duloy, J.H., *Redistribution with Growth*, Oxford University Press (1974).
4. Sen, A. "Goods and People" paper presented at the Seventh World Congress of the International Economic Association, reprinted in Sen, A. *Resources, Values and Development* Oxford, Blackwell, 1984.

tribution and poverty alleviation measures are implemented. Thus, without a significant and sustained increase in per capita income levels, the net result of redistribution and poverty alleviation measures would be a redistribution of poverty and a general decline in living standards. Further, redistribution measures such as the raising of nominal wage levels will be of little welfare consequence if inflation were to constantly erode the purchasing power of money. Similarly, minimum wage legislation could be counter-productive in terms of employment creation if not accompanied by corresponding increases in productivity. In the absence of requisite productivity increases, employers will resort to a substitution of capital for labour.

Per capita income growth depends by definition on relative rates of growth of GDP and population. Sri Lanka's population growth, at a low of 1.4 percent per annum, partly helped by migration, compares well with many of the more advanced countries. There appears to be little room for any dramatic achievements on this front. Thus, the main thrust will have to be in accelerating overall economic growth.

Table I below provides interesting insights into Sri Lanka's position among a selected group of Asian Countries with regard to per capita income levels and rates. It may be observed that Sri Lanka's position has dropped from se-

cond place in the 1950s to 5th place in 1987. Simple arithmetic indicates that at the highest average rate of growth achieved so far of 6.2 percent per annum. It would take almost 32 years for Sri Lanka to reach Malaysia's present level of per capita income (See Table II). If Sri Lanka is even to reach present day Thai per capita levels, the period required would be approximately 19 years.

latter development is not surprising since foreign aid during the last decade has financed mostly large scale projects such as those in the Mahaweli Development Programme where capital intensity has been very high. Lower productivity, reflecting low levels of skills and management deficiencies, may have also played an important role.

If Sri Lanka is to accelerate the growth

TABLE II

SRI LANKA - GDP GROWTH AND INVESTMENT

	1971-77	1978-82	1983-87
GDP growth rate ¹	2.9	6.2	4.1
Investment ²	15.7	27.6	25.1
Foreign Savings ²	3.2	12.8	8.5
National Savings ²	12.5	14.8	16.5
ICOR ³	5.4	4.4	6.1

1 - in constant prices

2 - as percentage of GDP

3 - ICOR - Incremental Capital Output Ratio

Table II above depicts succinctly the economic growth outturn in Sri Lanka during the last twenty five years. It may be observed that two factors have fundamentally affected economic growth - the investment ratio and the capital-output ratio. An improvement in either or both of these factors is required to accelerate growth. Foreign aid appears to have played a major role in promoting growth during the last ten years, while the capital-output ratio has increased, reflecting a higher capital intensity. The

process and provide more employment opportunities it must increase the ratio of investment to GDP and reduce the capital output ratio. The ratio of investment to GDP, as Table II indicates, will have to be increased by raising either domestic savings or foreign savings, or both. Domestic savings can only be increased by reducing consumption, usually of basic items, which affects the middle classes and the poor. To mitigate the burden on these classes, it would seem that greater reliance will have to be plac-

TABLE I A COMPARISON OF SRI LANKA'S GROWTH PERFORMANCE WITH THAT OF THE OTHER COUNTRIES

Country	1950 GDP		1960 GDP		1970 GDP		1980 GDP		1987 GDP	
	Per Capita	Rank	Per Capita	Rank	Per Capita	Rank	Per Capita	Rank	Per Capita	Rank
	a/		a/		a/		a/		a/	
Sri Lanka	113.8	2	142.1	4	183.2	3	250.7	7	390.9	5
Burma	42.2	5	66.2	7	80.4	8	169.9	8	210.7b/	8
India	55.9	3	73.4	6	98.6	6	253.7	6	291.2b/	7
Korea	-	-	151.4	3	266.8	2	1507.2	2	2993.1	1
Pakistan	-	-	50.6	8	87.1	7	286.9	5	337.5	6
Philippines	170.6	1	253.4	2	179.0	4	720.7	3	596.4	4
Thailand	53.5	4	96.8	5	178.8	5	714.0	4	914.4	3
Malaysia	-	-	275.5	1	380.1	1	1743.2	1	1710.6	2
Memo Items:										
United States	1882.8		2833		4917.3		11787.1	18,300	18300.8	
United Kingdom	722.4		1379.1		2224.4		9829.9		13440	

a/ In US\$.

b/ 1986

ed on foreign savings, essentially foreign aid.

But foreign aid, from whichever quarter, whether from international financial institutions such as the World Bank, the IMF, or bilateral donors, will not be forthcoming unless a country shows itself capable of absorbing the aid and utilising it efficiently. Bilateral donors have shown a tendency in recent years to follow the prescriptions of the World Bank and the IMF. These prescriptions are seen as comprising a series of structural adjustment measures. In Sri Lanka's case, these essentially entail measures directed towards lowering the ICOR or, in other words raising the efficiency of capital (See Table II). The high ICOR is undoubtedly partly attributable to the capital intensity of donor funded, large-scale projects such as the Mahaweli. However, even allowing for this, the ICOR remains high. Therefore measures must be taken to improve the quality of investment and raise its productivity.

Structural Adjustment

Measures aimed at improving the allocative efficiency of capital are those which seek fundamentally to make market prices reflect opportunity costs and give the right signals to producers and consumers alike. These measures try to remove distortions brought into the price system by arbitrary (albeit well-intentioned) interventions of government. Price distortions have resulted in heavy direct as well as indirect subsidies to inefficient industries.

Correction of price distortion entails a narrowing or even elimination of deviations of market prices from the real costs of factors of production and, therefore, goods and services to society. This in effect means that wage rates, interest rates and exchange rates all have to be corrected. The series of adjustments which will bring these required corrections about are collectively referred to as structural adjustment - a term that has come into vogue with the policy prescription of the IMF and the World Bank. It has been observed in recent years that the success of these changes is very closely linked to corresponding institutional changes aimed at improving management, technical skills, and marketing, and that the latter are therefore necessary concomitants of successful adjustment packages.

Experience shows that adjustment

policies have had their heaviest toll on the poor, the destitute, women and children. This is brought out forthrightly in a UNICEF study entitled "Adjustment with a Human Face". The rich and the upper middle classes have the capacity to adjust their income generating sources to changing market situations. The poor, as well as the lower middle classes, do not possess such power and they experience further exacerbations of their meagre and impoverished living conditions as a result of structural adjustment. Such conditions become immediately reflected in levels of food intake, nutritional and health standards.

Janasaviya and Structural Adjustment

Whether dictated to by the World Bank and the IMF or not, Sri Lanka has to undertake certain structural adjustment measures if she is to improve efficiency and accelerate economic growth. Such measures, however, will take a long time to bear fruit in terms of increased incomes and employment opportunities. Meanwhile, the poor and vulnerable sections of the population must be protected against any further exacerbation of their living standards. In spite of the controversy over the actual numbers involved, there is a growing consensus that large numbers of people in the country belong to the category of the vulnerable. The Janasaviya Programme, therefore, could be a vehicle of assisting such people in the context of structural adjustment.

The Janasaviya Programme will not only provide basic needs such as food and clothing to a section of the population whose productivity levels have been severely eroded due to malnutrition, poor health, and social backwardness; it will also provide them with opportunities to find productive self employment, until such time as the organised sector expands sufficiently to provide more stable employment and incomes.

The JSP aims to alleviate poverty within two years through an entitlements grant, split into a consumption component (valued at Rs.1458 p.m. and given in the form of entitlement certificates) and an investment component (Rs.1042 p.m.). The consumption component will be disbursed immediately for the purchase of essential commodities, while the investment component will be allowed to accumulate in a bank deposit and released at the end of two years, subject to the presentation and approval of a sound investment scheme. Beneficiaries may, if they so wish, save a part of the consumption component

and then withdraw it in the form of cash, inclusive of interest, at the end of one year. The JSP beneficiaries will also have the opportunity of drawing on the investment component in advance, as a bank credit, using the JSP deposit as collateral. Again, the proviso is that a sound investment scheme needs to be presented by the prospective recipients of this credit.

The Economic Consequences

The success of the programme in terms of its objectives as well as its economic consequences vis-a-vis economic growth, employment, inflation and balance of payments, will depend on several factors, including:

- the magnitude of the programme and mode of implementation;
- methods of financing; and
- supplementary measures.

The JSP is intended as initially a consumption augmentation programme which will raise the level of demand for essential commodities such as foodstuffs, clothing, medicine etc. The magnitudes in terms of beneficiaries and entitlements are yet unknown. These will only become known through a number of planned surveys, the application of selection criteria with respect to beneficiaries, and an enumeration of the entitlement methods; until then, it is not possible to make any quantitative assessment of the demand impact of JSP. Obviously, the higher the demand generated by the JSP for essential commodities the greater will be its initial inflationary impact. Domestic production will take time to respond to the expansion of demand. Meanwhile, the gaps in supplies will have to be met from imports (which will have balance of payments consequences) if inflation is not to entirely dissipate the redistributive gains.

The inflationary and balance of payments consequences will also depend on the ingredients of the basket of entitlements. If the entitlements are basically for food items and other commodities which could be produced domestically and within a short period, the consequences would be less severe than otherwise. Such a principle would also have a salutary effect on domestic production and self employment opportunities.

The selection criteria has to be such that the poorest of the poor are the first beneficiaries. To be effective in terms of cushioning the most vulnerable sections of the population it is necessary to select beneficiaries on the basis of those

who will most need income assistance to withstand the economic shocks of adjustment.

Related to this is also the principle of disbursements, which has consequences not only for the levels of consumption but also for social justice. If the beneficiaries, irrespective of their current income levels receive the same entitlements, obviously those with higher incomes will benefit more. Further, the gap between those at the margin of non-eligibility and those who are eligible will also widen. To avoid this, it would be necessary to apply a "topping up" principle in disbursing entitlements.

Financing of JSP

There are five basic methods of financing the JSP each having macro-economic implications —

- i. Reduction of other budgetary expenditure;
- ii. New revenue measures;
- iii. Non-Bank borrowing;
- iv. Bank borrowing;
- v. Foreign aid.

There is a limit to which budgetary expenditure could be reduced without having deleterious effects on economic growth and employment, unless of course these reductions are brought about by forced savings through a better management of resources. The government's capital expenditure is financed to a significant proportion by foreign aid. Reductions in local consolidated fund allocations would lead to a reduction of foreign aid and absorption, since almost every project is co-financed. Reduction of aid absorption is not desirable because it could make donors more cautious with regards to future pledges.

New revenue measures to be effective must be significant and capable of being collected. The easiest to collect and the most effective in this regard are the trade or sales-based measures. But they invariably have an impact on domestic price levels.

Non bank borrowings from captive sources such as the National Savings Bank and the EPF are already utilized to the maximum extent possible. What remains therefore for further exploration is expanded open market operations in Treasury Bills and long-term government securities.

There is no similar physical constraint on financing through Bank borrowings (printing money). The limitation here is that, if it is resorted to on a significant scale, it will result in a dangerous expansion of liquidity in the system.

Foreign aid financing of a significant

proportion of the additional commodities required to sustain the JSP consumption package could mitigate not only inflationary but also balance of payments pressures. There are indeed incentives for donors to assist the JSP in this manner. Firstly it provides the donors with the possibility of participating in a unique poverty alleviation programme. Secondly, it will assist aid absorption by allowing counterpart funds generated from local sales of aid goods to be utilised to meet rupee expenditure of projects supported by them.

Supplementary Measures

Supplementary policy measures required to mitigate the inflationary and balance of payments pressures of the JSP include credit controls and the maintenance of a stable real exchange rate. Most important, however, are measures directed towards stimulating agricultural and industrial production.

The extra purchasing power generated by the JSP in the hands of the poor is bound to increase demand primarily for food items. An accelerated agricultural development drive is therefore crucial in order to arrest a potentially steep rise in both domestic food prices and food imports. Agriculture also offers wide opportunities, particularly in the case of minor crops for export development. Such a development strategy is also important to channel the JSP investment component into productive use.

A similar effort is required to accelerate the development of the industrial sector in order to meet the expected expansion in domestic demand and to increase export earnings. The basic strategy with regard to industrial development is contained in the Industrial Policy Statement adopted by the government. A crucial role in this strategy will have to be played by private sector industries, particularly by small manufacturers in the context of the JSP.

JSP Investment

The JSP will help resolve to some extent a principal problem with regard to small enterprise development, that of capital. The investment component of Rs.25,000 appears at a first glance to be quite small. However, where a project in the perception of a bank appears to be viable, there is the possibility of obtaining supplementary loan financing upto almost three times this amount. Further, where necessary several Janasaviya beneficiaries could get together and pool their capital, in order to set up a large enterprise.

Capital, however, is only one factor of production. The poorest of the poor, to whom the Janasaviya Programme is targeted, are also socially backward, they do not know how markets operate, what goods are in demand, what quality is acceptable to buyers, and the costs of production that will yield a reasonable return on capital for their sustenance and future expansion of business. There must be an effective mechanism, supported by government, to help JSP investors obtain this information. On this information hinges the type of technology, to be adopted, the skills to be employed and other facilities that must be provided, including infrastructure and marketing assistance.

One of the most effective methods of delivering the required knowledge of products, know-how, and marketing facilities, is to forge links between small enterprises and organised manufacturing enterprises. This is the method that has proved successful in Japan, Korea and recently, Thailand. In Sri Lanka, we already have some examples of successful experiments by Bata, Ceylon Tobacco and a few others. What is required now is to forge a wider network of such linkages.

Conclusion

In the foregoing discussion, the Janasaviya Programme was presented as an essential element of an adjustment programme that is required to generate economic growth and ensure future incomes and employment. Its success, however, as pointed out, will depend on the methods of financing and implementation.

Contingent on these methods, the country is bound to experience inflationary and balance of payments pressures, some of which can be mitigated in their economic impact by the types of supplementary measures that have been alluded to above. It would, however, not be possible to avoid either inflationary or balance of payment consequences altogether.

While every effort must be made to keep this inflation as low as possible, it must also be recognised, however, that inflation is a necessary safety valve in the event of the real resources required by the JSP not being forthcoming. Herein lies the importance of donor support over the short term. In the absence of real resource transfers of this kind, inflation must inevitably and necessarily dissipate the effects of the redistributive measures in order to avoid shortages and distorted relative price signals.