

Steady Slump in Growth Unfortunate

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Traumatic period

The past twelve months have surely been the most traumatic period which Sri Lanka has experienced in this country. The ethnic troubles of the past six years were compounded by political and social turmoil. Most serious of all, there was an alarming breakdown of law and order, and for the first time in our experience there were prolonged periods when the writ of the Government did not seem to apply even in the city of Colombo.

I need hardly elaborate on the near impossibility of satisfactory economic development in such conditions. The growth figures from 1987 sounded an unmistakable warning; the 1987 growth rate was 1.5 per cent, the lowest since 1971. The 1988 figure was 2.7 per cent. One shudders to even hazard a guess at the 1989 figure.

During the past eleven years there have been three plateaus of economic growth levels. In the period from 1978 to 1983 growth averaged a satisfactory 6 %; from 1984 to 1986, despite ethnic conflict, it was a creditable 4% to 5%; but from 1987 onwards it has averaged a poor 2%.

This steady slump in growth is unfortunate, because it is economic growth that creates more employment, more earnings, better nourishment, more savings for further investment, and, as a result of all these things, a happier, more contented society. While we fully appreciate that the alleviation of poverty is a national priority today, it is an inescapable fact that poverty can be alleviated only through a growing economy.

Economic development requires investment, the commitment of funds, the taking of risks. So far

Sri Lanka's efforts at encouraging investment have been concentrated on providing fiscal incentives. These are important, but not to the exclusion of more fundamental requisites.

In 1988 the International Chamber of Commerce (ICC) convened a Conference to consider the central economic issue of the need for more private investment in productive enterprise, nationally and internationally. Their findings were illuminating, particularly for Sri Lanka, which has neglected some of the fundamentals.

I shall quote from the ICC Annual Report for 1988. "The conditions which are most effective in attracting foreign private investment. The principal conditions are: a stable political system with a government which respects the role of business; an efficient and honest bureaucracy; rising standards of education, health care and social infrastructure; sound monetary and fiscal policies; moderate levels of personal and corporate taxation, flexibility of relative prices to reflect market signals; a legislative framework for business which is clear, stable and yet sufficiently flexible to adapt to modern commercial operations; the protection of private property rights, including rights in intellectual property; an impartial judicial system; and uninhibited access to the courts to redress wrongs and settle disputes."

Alarming deterioration in infrastructure

You will see that the ICC factors can be grouped under the broad headings of political, social and economic infrastructure, and include some items to which not much attention is paid by our authorities. To put it plainly, the

basics — not only of the economy but of society — must be right. It would be a salutary exercise, and a chastening one, to examine the ICC conditions and see how though Sri Lanka has put together an attractive package of tax incentives, their effect has been undermined by an alarming deterioration in the political, social and economic infrastructure.

I have chosen to stress infrastructure at the beginning of my speech, instead, as in the past, towards the end, because it has become of such over-riding importance. I now move on to other matters, and you will notice that many of the problems that exist have their roots in shortcomings in the infrastructure.

Garments continued to be our largest export in 1988. Unfortunately, the events of the past few weeks, when production has been seriously disrupted by regular work stoppages, may impose long-term damage on the industry because Sri Lanka's reliability as a supplier has now been called into question. It is sad that the biggest success story in the export field may falter due to self-inflicted wounds.

Tea prices have continued to be depressed. Due to the large wage increases granted in times of high prices, without provision for adjustment if prices fell, several plantations are operating at a loss. That is not all. In many speeches to you at the previous two Annual General Meetings I warned that continuing indiscipline in the tea plantations would have the most serious consequences if it went on unchecked. Not only has there been no improvement; there has been the added trial of external threats and sudden stoppages of work. To quote the Chairman of the Colombo Tea Traders' Association at their Annual General Meeting last month, "... one must sympathise with the producer who suffers threats to life and limb. We have some of the finest planters in the world, but many have lost their motivation and interest. The Superintendent has lost his author-

ity, many promotions have been politically motivated rather than earned and the trade is suffering for it." The long-term future of the tea industry must now be considered uncertain.

Question mark over largest exports

It is a tragedy of the first magnitude that large question marks hang over our two largest exports, garments and tea, which between them accounted for 55 percent of the country's export earnings in 1988. The consequences of their collapse would be too horrendous to even contemplate.

However, there is a ray of hope for the tea industry. The new Minister for Plantation Industries, the Honourable Gamini Dissanayake, has shown an uncommon grasp of the needs of the industry, and has enlisted the help of the private sector in the form of a newly established Tea Council, on which most sectors of the industry are represented, which is to serve as an advisory body to the Sri Lanka Tea Board.

The Minister of Plantation Industries has also agreed to set up a Rubber Council/Board to serve as an apex body for the rubber industry. These new bodies will equip the tea and rubber industries with the best institutional framework they have ever had, and I hope that the expected results will accrue.

The gem industry's exports have been increasing over the years, but it is still not operating anywhere near its potential. According to the trade the purchase of geudas by Thai gem merchants and their conversion to sapphires in Thailand has helped greatly to build up Bangkok as one of the world's great gem centres. The agreement between the Sri Lanka and Thai governments about the purchase of geudas has channeled some of the trade into legitimate exports, but the long-term answer is to develop the technology to process geudas ourselves, and the internal market-

ing system to pay the miner a fair price. The work done so far is reported to be promising. However, neither the trade nor the Government has come up with the incentive which will produce the kind of quantum leaps in exports which occurred in the 1970's with the introduction of the CRA schemes. The Sri Lanka Gem Trader's Association, which is affiliated to the Chamber, will soon be releasing a report which will contain proposals for the development of the gem industry.

Manufacturing industry as a whole also remains an under-developed sector, despite the progress made in some fields. I shall briefly mention a few problems that handicap local industry. Although some locally manufactured products are subject to price control, similar imports are not. Again, while some locally manufactured goods are required to comply with Sri Lanka Standards, the corresponding imported articles are not. Local industry also has to contend, in some cases, with overseas suppliers who dump inferior quality products in Sri Lanka at very low prices.

Search for an industrial policy continues

The search for an industrial policy continues. The document produced by a committee and released in March 1987 was a start, but it depended too much on one key proposal - the introduction of Transferable Tax Credits (TTC's). In November 1987 the Chamber addressed a memorandum to the Minister of Finance and Planning drawing attention to aspects of the TTC scheme which were not clear and which required careful study. The Chamber was also concerned that the TTC scheme, which would be complex and dependent on a number of variables, had not succeeded anywhere in the world, and would be in the nature of an experiment with our industrialists as the guinea pigs. I think we have enough problems without venturing to indulge in the luxury of a theoretically elegant scheme which might prove unworkable and harmful in

practice.

The industry which has suffered most due to the problems of the past few years is tourism. Until the return of normalcy, the impressive tourism plant built up in the good years should be given every support. The authorities are to be commended on all the relief measures they have already agreed to.

In the field of taxation I would like to spotlight the thoroughly unjustified taxation of provident funds, which are taxed not just once, which would be bad enough, but twice. Firstly, provident fund balances to the credit of private sector employees are taxed at up to 15% of the employer's contribution on retirement, although inflation has already taken a heavy toll of the real value of the balances. Secondly, there is the iniquitous taxation of provident fund incomes introduced in the Budget Speech of November 1987. Although the tax was reduced from 20% to 10% by the Budget Speech of March 1989, the relief to employees was more than outweighed by the simultaneous removal of the exemption of interest on Government securities in computing provident fund income. I strongly urge, on grounds of equity and humanitarianism, that the state should cease to regard provident funds as a source of revenue.

For eighteen years the Chamber and other private sector bodies have urged the repeal of the Business Undertakings (Acquisition) Act of 1971. We were therefore relieved that the Act was repealed by Parliament on 25th November, 1988. But even before the repealing Act had been certified, a senior Chamber member was taken over under Emergency Regulations in much the same manner that enterprises had been acquired under the Business Undertakings (Acquisition) Act. The Chamber protested strongly to His Excellency the President against the take-over and pointed out the damage caused to the business climate.