XI

SRI LANKA'S ECONOMIC DEVELOPMENT DURING TWENTY-FIVE YEARS OF INDEPENDENCE

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Introduction

The first quarter-century of Ceylonese independence began with high hopes for economic achievement, based on what then appeared to be enormous assets: a literate, well-fed population; a competent public administration; prosperous export industries which had amassed large Sterling balances supplying tea, rubber, and coconut products to the wartime Allies; well-developed economic and social infrastructure. It seems a fair judgment that achievement has fallen short of these hopes. Production has grown slowly and foreign exchange has been in critically short supply during most of the period. Ever-worsening overpopulation has constituted a treadmile against which all development efforts must struggle. It is true that the period has seen some notable achievements—in spreading social services to the entire population, lessening interpersonal income inequality, and increasing food production. Yet the increasing emphasis on averting a food crisis by growing more food domestically, rather than buying it abroad with the earnings of viable export industries represents a lowering of the sights of economic policy which reveals how difficult the past 25 years have been for the Ceylonese economy.

Ceylonese economic development in 1948-73 can usefully be divided into two subperiods of roughly equal length. In 1948-60 Ceylon failed to realign its export economy so as to cope with a new and less favorable set of factor growth rates and satisfy the social demands of a politically articulate populace. The critical event of the era was the failure to correct the worsening foreign exchange position after 1955. This omission forced severe restrictions on imports and other foreign payments, beginning in 1961. In the 1960-73 era, the nation struggled to escape from a now-perennial foreign exchange crisis. The economy, everywhere constrained by import shortages, grew much less rapidly—but the position of the lowest income groups did improve substantially.

Development in 1948-60

The 1948-60 experience and its historical background have been analyzed elsewhere.[1] This was a period of significant, if unsustainable, economic growth. Real

1. Donald R. Snodgrass, *Ceylon: An Export Economy in Transition* (Homewood, Illinois: Richard D. Irwin, Inc., 1966).

Gross National Product rose by about 90% (equivalent to 5.5% per annum); with a small improvement in the barter terms of trade between the end years of the period, real Gross National Income practically doubled.[2] Despite the addition of more than two and a half million souls to the population, living standards did rise significantly. Private consumption per head (valued in 1959 prices) can be reckoned at Rs. 376 in 1948 and Rs. 516 in 1960. Private consumption was supported by government transfer payments which consistently exceeded tax and other payments by households to the government.[3] Public consumption outlays more than doubled in real terms, as competing regimes broadened the coverage of education, health, and other social services. The average Ceylonese of 1960 was thus distinctly better off than his counterpart of 1948. But adequate provision had not been made for maintaining this improvement after 1960.

In the long run, what did not happen in 1948-60 may be more important than what did. To sustain moderate growth after 1960 would have required that export earnings be plowed back into investment in other sectors of the economy. Instead consumption claimed most of these flows while investment generally remained below 10% of GNP until 1955, even then advancing only to 13% by 1960.[4] Major increases were achieved in paddy production (which doubled between 1947-49 and 1959-61) but progress in refurbishing existing export industries or diversifying into new areas in either agriculture or industry was far more modest. So the structure of production changed little as population grew and, after 1955, the foreign exchange problem worsened rapidly.

In 1956-60 moderate downturn of export prices (from an historically high level) was juxtaposed on rapid increases in import volume financed by expansionary fiscal policy.[5] External assets dropped from Rs. 1,275 million at the end of 1956 to Rs. 541 million four years later. No government of that turbulent period dared to risk its political life by taking the unpalatable measures which could have stemmed the tide, so by the time the problem was finally tackled, in early 1961, supply of foreign exchange had fallen to a crisis level.

The main immediate effect of population growth in 1948-60 was to push up private and public consumption needs, diminishing the investible surplus. The employment

2. See the Appendix for the numbers upon which all estimates of economic growth in 1948-73 are based.

3. Snodgrass, pp. 272-73.

4. According to my national accounts estimates (Snodgrass, p. 269) the only year in the 1950-55 period when gross fixed capital formation exceeded 10% of GNP was 1953, when it briefly touched 11%. Estimates of the Department of Census and Statistics (cf. Snodgrass, pp. 240-43) give higher ratios because they underestimate GNP.

5. Export prices fell only 12% from 1955 peak to 1958 trough, after which they recovered slightly. But import volume rose 35% between 1955 and 1960. See Central Bank of Ceylon, *Annual Report of the Monetary Board to the Minister of Finance for the Year* 1973, Colombo, 1974, Tables 50 and 51.

problem began to command attention only after a 1959 sample survey indicated a worsening situation.[6]

Income distribution changed little during this period—at least between 1953 and 1963, the years for which survey data are available.[7] The share of the highest decile of income recipients did decline, but those of the deciles just below the top rose, leaving overall pretax inequality unchanged. Considerable levelling of welfare disparities probably did occur as a result of broadened government social programs.

Development in 1960-73

The years since 1960 have seen much slower economic growth than those before. The growth rate of real GNP dipped below 4%. The permanent foreign exchange crisis necessitated frequent international borrowing to finance an import bill from which all luxuries, and then increasing quantities of more essential goods had been purged.[8] Gross foreign assets nevertheless continued to slip away until 1972. Generally lower export prices contributed to Ceylon's woes through 1968, at which prices strengthened, even exceeding the 1955 boom level during the 1973 upset of world commodity prices. The Dudley Senanayake regime of 1965-70 was able to obtain net official loan receipts averaging Rs. 200 million in 1966-70 (perhaps because of payments lags, aid receipts reached even higher levels in 1971-72).[9]

Offsetting these increased means of import finance, however, were dramatic increases in import prices, resulting from rising world prices and successive rupee devaluations. Whereas import prices had risen by only 46% in 1948-60 (and not at all in 1951-60), the rise in 1960-73 was a startling 152%. Much of this increase occurred in 1973, as a result of world grain shortages and the withholding of supplies by petroleum exporters. Imports had to be restricted almost as severely in the early 1970's as they had been in the early 1960's; the import volume index for 1973 stood at its lowest level since 1949.[10] Thus it is not surprising that per capita levels of income, private consumption, and even public consumption increased only marginally in 1960-73.

With the capacity to import so severely constrained, the necessity to develop means of earning or saving more foreign exchange was even more urgent in 1960-73 than it had been in 1948-60. Yet progress along either line continued to be slow—in part because export industries and import-substituting industries themselves continued to be heavily dependent on imported intermediate and capital goods. Rubber output

6. See "A Survey of Employment, Unemployment, and Underemployment in Ceylon", *International Labour Review*, March 1963, pp. 247-57. The Survey showed 10.5% of the labor force to be unemployed, with 45.4% of those employed in rural areas and 29.0% in urban areas unable to find 40 hours of work per week on a year-round basis.

7. Central Bank of Ceylon, *Survey of Ceylon's Consumer Finances*, Colombo, 1954; *Survey of Ceylon's Consumer Finances* 1963, Colombo, 1964.

8. Official foreign debt soared from Rs. 294 million at end-1960 to Rs. 2,795 million at end-1973. Central Bank, *Annual Report* 1973, Table 38.

9. *Ibid.*, Table 47.

10. *Ibid.*, Table 51.

did go up on the strength of the replanting campaign but tea production levelled off in the face of stagnating, price-inelastic world demand and increasing competition from other producers. Coconut output continued to fluctuate from year to year with no apparent trend. Real value added in manufacturing grew by fits and starts, averaging only 5.3% a year.[11] Tourism added a tiny element of dynamism, but in general economic restructuring proceeded so slowly that Ceylon was forced to think more and more about growing her own food. Fortunately it did prove possible to raise paddy output by another 50%, after the doubling of 1948-60. Production of subsidiary foodstuffs also increased, so food supplies generally remained adequate for the growing population. Indeed, nutrition seems to have improved somewhat as compared to two decades before: average daily calorie intake rose from about 2,000 to 2,200, while consumption of fruit, vegetables, eggs, and milk all increased.[12]

In 1960-73 the full force of population growth hit the labour market. The population between 15 and 65 years of age—roughly, the working age range—soared from about five and a quarter million to seven and a half million. Despite gaps in the available statistics and difficulties of interpretation, it is evident that the growth of labour supply during this period far outran the demand for labour being generated by the slowly growing economy. By any measure, labour surplus increased by leaps and bounds. Estimated open unemployment climbed from 370,000 in 1959, to 550,000 in 1969/70, to a staggering figure of 793,000 in 1973.[13] Underemployment, by any definition, undoubtedly increased. And labour force participation rates, particularly for women, declined as "discouraged workers" abandoned the unrewarding search for employment.[14] As a result of its long-standing commitment to extensive free education through the university level, Ceylon also became an outstanding example of the growing global phenomenon of educated unemployment.

While Ceylon found it difficult to increase income per head in 1960-73, it did substantially equalize income distribution. Since 1963 inequality among earners and spending units has been cut sharply; the shares of the top two deciles have fallen while those of the bottom eight have risen.[15] Further progress was also made in welfare-redistributing tax and benefit programs.[16] Thus, despite the slow growth of mean

11. Central Bank *Annual Reports* for 1968 (p. 39) and 1973 (Table 5).
12. Based on food balance sheets for 1952-53 (Snodgrass, p. 321) and 1971 (*Statistical Pocket Book of the Republic of Sri Lanka* 1973, Colombo: Department of Government Printing, 1973, p. 57).
13. "A Survey of Employment..."; International Labour Office, *Matching Employment Opportunities and Expectations. A Programme of Action for Ceylon*, Geneva, 1971; and Central Bank, *Annual Report for* 1973, pp. 11-12.
14. Declining participation rates through 1968 were found for some groups by P. J. Richards in his *Employment and Unemployment in Ceylon*, Paris: Organization for Co-operation and Development, 1971, pp. 49-53. Data from a 10% sample of 1971 census returns (*Statistical Pocket Book* 1973, pp. 10-11, 25) suggest subsequent further declines. A crude indicator is the falling ratio of persons whose usual economic status is employment to total population ages 15-64 which is shown in successive population censuses: 58.2% in 1953, 55.6% in 1963, 50.7% in 1971.
15. See Central Bank, *Annual Report for* 1973 pp. 10-11; also Richards, pp. 149-70, and Economic Commission for Asia and the Far East, "Distribution of Income and Wealth in Ceylon", Bangkok, mimeographed, 1972. H. N. S. Karunatilake "Changes in Income Distribution in Sri Lanka". Central Bank of Ceylon, *Staff Studies*, vol. 4, No. 1, (April 1974) pp. 1-23.
16. See Lal Jayawardene, "Sri Lanka", in Hollis Chenery and associates, *Redistribution with Growth*, London: Oxford University Press, 1974, pp. 273-79.

income, low-income families did see improvements in their material well-being. This is an achievement which many faster-growing economies cannot claim.

Conclusion

Until the recent shift of focus from economic growth measured by GNP per head to income distribution and the redressal of poverty, Sri Lanka was widely regarded as a laggard in development. Now, however, a "revisionist" school of development economists is recasting her as a success because of her social development achievements.[17] The issue is only partly one of values; there is also the question of what patterns of development are sustainable through time.

We have noted that economic growth slowed after 1960. The same can be said of most social advances. The major improvements in education and health were made before 1960, when government outlays for social programs rose to 8% of GNP.[18] Thereafter, social development's share of GNP slowly declined as it became increasingly difficult even to maintain the newly-won standards of service. The only social development criteria by which performance in 1960-73 exceeded that of 1948-60 are reduction of income inequality and rises in the absolute incomes of the poor. We need to ask how these improvements came about and whether they are sustainable in the future.

It appears[19] that higher payments to paddy planters and other small scale producers were the major factor raising the earned incomes of the poor in 1963-73; these in turn originated in efforts to grow more food in view of the foreign exchange shortage. This reallocation of resources and slanting of incentives toward subsistence could certainly be expected to reduce inequality. Over the 1963-73 decade it also increased the absolute incomes of the poor substantially.[20] Whether it can continue to do so in the longer run, however, is questionable.

Over time, raising the incomes of any substantial part of society requires growth in national income. Raising national income requires a relative shift of resources *away* from paddy production and other relatively low productivity uses.[21] And this in turn requires export earnings and capital inflows to finance investments which will restructure the economy. It is this that was not achieved in 1948-73, and with saving and investment rates still low and the foreign exchange and overpopulation problems worse than ever, prospects for achieving it in the near future appear dim. Until some way is found to make the economy grow fast enough to finance sustained social progress, Sri Lanka will serve as a better illustration of the limitations of a direct approach to problems of social equity than of its benefits.[22]

17. The Chenery and associates volume cited in the preceding note consistently takes the "revisionist" view.

18. Snodgrass, pp. 269, 388-89; Central Bank, *Annual Report for* 1973, Tables 8 and 36.

19. See Jayawardene *op cit.*

20. Jayawardene estimates (p. 278) that real income and social benefits received by the lowest four deciles of households rose by 58% in 1963-73, compared to an average of 35% for all households. I cannot reconcile these figures with my own estimates (based on official data) that real GNI per head rose by only 10% in 1963-73, real private consumption by 20%, and real public consumption by 10%.

21. When population growth is allowed for, GNI growth becomes a necessary condition even for maintaining existing income per head. See Gavin W. Jones and S. Selvaratnam, *Population and Economic Development in Ceylon.* (Hansa Publishers, Ltd., Colombo, 1972) for an analysis of the economic costs of population growth.

22. For a similar view, see Arun Shourie, "Growth, Poverty and Inequalities", *Foreign Affairs*, January 1973, pp. 340-52.

APPENDIX

Extimates of Economic Growth, 1948-73

				Growth rate (%)		
	1948	1960	1973	1948-60	1960-73	1948-73
Population (000)	7,244	9,896	13,251	2.6	2.3	2.4
GNP at factor cost (Rs. millions)						
In current prices	3,000	6,287	15,155	6.4	7.0	6.7
Deflator (1959=100)	90.7	100.0	146.0			
In 1959 prices	3,307	6,289	10,383	5.5	3.9	4.7
Real GNP per capita (Rs.)	457	636	784	2.8	1.6	2.2
GNI at factor cost (Rs. millions)						
In current prices	3,000	6,287	15,155	6.4	7.0	6.7
Deflator (1959=100)	93.3	98.6	164.5			
In 1959 prices	3,214	6,278	9,212	5.7	3.0	4.3
Real GNI per capita (Rs.)	444	634	695	3.0	0.7	1.8
Private consumption (Rs. millions)						
In current prices	2,400	5,020	12,203	6.3	7.1	6.7
Deflator (1959=100)	88	98.3	157.2			
In 1959 prices	2,727	5,107	7,763	5.4	3.3	4.3
Real private consumption per capita (Rs.)	376	516	586	2.7	1.0	1.8
Public consumption (Rs. millions)						
In current prices	300	911	2,043	9.7	6.4	8.0
Deflator (1959-100)	96	100	142			
In 1959 prices	313	911	1,439	9.3	3.6	6.3
Public consumption per capita (Rs.)	43	92	109	6.5	1.3	3.8

Source Notes:

Population: See Snodgrass, p. 307; *Statistical Pocket Book* ...., p. 9; Central Bank *Annual Report for* 1973, p. 12.

Current price estimates: 1960 and 1973 figures from Central Bank *Annual Reports* for 1968 (pp. 37, 42) and 1973 (Tables 4, 8), respectively; 1948 estimates from an earlier series (see Snodgrass, p. 240), raised slightly to improve comparability with later Central Bank data.

Deflators: 1960 and 1973 deflators for GNP and GNI implied in Central Bank data: 1948 GNP and GNI deflators based on Snodgrass, p. 398, and other data on 1948-50 price trends; private consumption deflated by Colombo consumer price index (see Snodgrass, p. 397, and Central Bank *Annual Report for* 1973, Table 54); public consumption for 1960 and 1973 deflated by central government employees wage rate index (see Central Bank *Annual Report for* 1973, Table 60), and for 1948 deflated by 1950-59 price relative implied in Snodgrass, pp. 269, 271.

Real estimates: GNP and GNI in 1960 and 1973 from Central *Bank Annual Reports* for 1968 (pp. 39-40) and 1973 (Tables 5 and 6); all others deflated as described in preceding note.

Indicators of Social Development, 1948-73

Literacy of population age 10 and over (% of total)

	1953	1963	1971
Male	80.7	85.6	85.2
Female ..	55.5	67.3	78.1
Both sexes ..	69.0	76.9	70.7

Source: *Statistical Pocket Book* 1973, p. 9.

Life expectancy at birth

	1946	1953	1962	1967
Male	43.9	58.8	61.9	64.8
Female ..	41.6	57.5	61.4	66.9

Source: *Ibid.*, p. 17.

Vital statistics

	per 1,000 *of population*			*per*, 1,000 *live births*	
	Births	*Deaths*	*Natural Increase*	*Maternal deaths*	*Infant deaths*
1945	35.9	21.5	14.4	16.5	139.7
1950	39.7	12.4	27.3	5.6	81.6
1955	37.3	10.8	26.5	4.1	71.5
1960	36.6	8.6	28.0	3.0	56.8
1963	34.1	8.5	25.6	2.4	55.8
1968	32.0	7.9	24.1	1.8	50.2
1972	29.5	8.0	21.5	1.2*	45.1

*1971

Source: *Ibid.*, p. 19.

Health facilities (per 100,000 of population)

	Hospital beds	*Doctors*	*Nurses*
1948	260	9.5	13.1
1960	294	12.3	34.2
1972	288	15.7	38.1

Sources: *Economic and Social Development of Ceylon (A Survey)* 1926-1954, Colombo, 1955, p. 99; *Statistical Abstract of Ceylon* 1961, Colombo, 1961, p. 75; *Statistical Pocket Book* 1973, p. 32. All data refer to government institutions only.

Distribution of income among income recipients

% of total income accruing to:	1953	1963	1973
Top 10% ..	42.49	39.24	29.98
Next 10% ..	14.16	16.01	15.91
Next 20% ..	18.33	20.44	23.21
Next 20% ..	12.02	12.37	15.85
Bottom 40% ..	13.00	11.94	15.05
Gini concentration ratio ..	.490	.491	.402

Source: Central Bank, *Annual Report for* 1973, p. 10. Gini concentration ratios calculated from decile shares.