



Election Campaign Myth Buster #2

Subsidies & Controls are a Panacea for Farmers' woes

The long-term prospect of our agricultural sector is severely constrained by extreme inefficiencies in both markets and public policies. This casts a very heavy burden on all Sri Lankans, particularly the poor and vulnerable. Many of the latter include members of our rural population who are trapped in an unsatisfactory status quo of low-productivity, low-income agricultural activity. This latest Pathfinder Foundation Election Myth Buster seeks to demonstrate how this unwarranted reliance on subsidies and administered prices imposes a heavy burden on the entire population and serves as a drag on the development prospects of our economy and nation.

Inefficient Government Policies - 80% of our land is owned by the State

Generally, Sri Lanka's public policy has focused on laws, subsidies and administered prices which yield highly perverse outcomes in the agricultural sector. The state owns 80% of the land in the country, much of which is grossly underutilized. On the other hand, other more productive enterprises face great difficulty in acquiring land for economic activity. The disposal and/or leasing of land would unleash economic value by bringing unused and underutilized land into use. It would also mobilize much needed revenue for the government resulting in expanded economic opportunities overall. However since Independence, ideological strait-jacketing and populist politics have prevented Sri Lankan political leaders from taking such a bold decision.

In addition, laws related to land use and ownership distort the efficient functioning of the land market. This constrains investment and discourages the emergence of commercial agriculture. These laws also cause distortions in the market which lead to sub-optimal patterns of land use in terms of crop-mix and the perpetuation of the fragmentation of land holdings. Tragically, the best commercial returns are not secured from land.

Input Subsidies and Price Controls

Subsidies and administered prices compound the inefficiency of public interventions in the agricultural sector. Free water, highly subsidized fertiliser and guaranteed producer prices trap many people in low productivity/low income farming activity. This is reflected in the

fact that although agriculture accounts for 30% of our country's work force, it constitutes merely 10% of GDP. While the very costly and inefficient support for agriculture does serve to keep people above the poverty line, it keeps many mired in a situation with little hope for improvement of incomes or living standards. Due to these misguided policies, while the poverty headcount amounts to 6.7% of the population (with a poverty line of \$1.50 per day), actually 25% of the population lives below \$2.50 per day. The future prospects of this segment of the population can be improved by releasing them from their entrapment by switching from a policy of subsidies and administered prices to a well-targeted social safety-net based on cash transfers. This should be supported by training and skills development that empowers people to move to higher value employment in more productive sectors of the economy.

The current counter-productive policies in the agricultural sector go a long way towards explaining why a large proportion of the rural population continue to be plagued with economic insecurity and low living standards. (Concurrently, in the urban sector rigid labour-market policies encourage arrangements of casual and informal employment of labour and job insecurity).

Low-income Trap & Higher Cost of Living

Not only do these highly misguided agricultural policies trap farmers into low-income lifestyles, they also impose burdens on the population as a whole through higher taxes and prices. The ill-effects stemming from the poor use of land, and of human and financial resources are worsened by the high costs associated with the inefficient and ineffective agricultural extension system. Technology absorption and productivity in Sri Lanka are well below those in a comparator country, Thailand.

However in spite of their dismal economic track record, this framework of inefficient, highly wasteful and politically expedient policies are kept in place. Some politicians and intellectuals thrive on unrealistically perpetuating romantic notions of an idyllic agricultural lifestyle, claiming that these harmful policies can reinstate a return to a traditional rural past. Though this may secure votes for politicians, in practice, they trap a large number of people into a life of hardship/insecurity/social backwardness and compound this by imposing additional burdens in the form of higher taxes and prices and lost economic opportunity.

Inefficient Markets

The distorted signals transmitted by these public policies have created inefficiencies in factor and product markets which have had a negative impact on output (growth), employment and incomes. The land policies have resulted in land-use patterns which yield low returns. Similarly, the crop mix is also sub-optimal with current policies discouraging switching to production of higher value commodities, particularly exports. The overall policy-mix also perpetuates low productivity agriculture (particularly paddy) on fragmented land holdings,

thereby curtailing the emergence of commercial agriculture which yields higher returns. The removal of subsidies/administered prices and restrictive laws would incentivise land consolidation and greater investment in agricultural activity. This would promote the emergence of a more efficient sector which would replace the current situation which constitutes a major drag on the prospects of the people and the economy. At present, farmers are kept afloat by policies that trap them just above the poverty line. In addition, scarce financial and human resources are diverted away from economic activities with greater potential.

Self-sufficiency at any cost?

Here again, there is need for ‘myth busting’. There has been an almost theological commitment to self-sufficiency in rice production for several decades. There is no justification for continuing to prop-up, at great cost, low productivity paddy cultivation on fragmented land-holdings in the wet zone. This is particularly so as most of the country’s rice requirement can be met through increasing yields in the dry zone where there is greater potential for improvement. There is also the option of importing rice to make-up for any shortfall as world market prices tend to be competitive in a context where the local cost of production is high. The land released from paddy production in the wet zone can be utilized for commercial production of higher value crops.

The current mix of policies which deters commercialisation of agriculture has also meant that there has been gross under-investment in storage, refrigeration and transport facilities. This has meant that post-harvest losses can be as high as 40%. This is another cause of the abysmally low productivity levels in Sri Lankan agriculture. The government lacks fiscal space to undertake this investment. A new mix of policies is necessary to create the businesses which can sustain this much needed investment.

Liberalizing Policies and Liberating the People

Changing land laws and phasing out subsidies and guaranteed producer prices will improve resource allocation. This will increase the growth potential of the economy, raise the capacity to generate better quality employment, and improve the prospects for productivity led increases in incomes which are more sustainable. Above all, it would dismantle the misguided and politically expedient policy framework which is currently depressing the living standards of many people by trapping them in low productivity, low income agricultural activity.

Your comments are welcome at

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