

Charting the Way Forward: Prosperity for All

Pathfinder Foundation

Colombo

May 2015

Table of Contents

Introduction.....	3
1. Maintaining Sound Macroeconomic Fundamentals.....	9
2. Improving the Business Climate.....	11
3. Factor Markets.....	13
3.1.1 Factor Markets - Land.....	13
3.1.2 Factor Markets - Labour.....	14
3.1.3 Factor Markets – Financial & Capital Markets..	15
4. Exports & FDIs.....	17
5. SMEs.....	20
6. Increasing Agricultural Productivity.....	21
7. Education, Training and Skills Development.....	23
8. Empowering the Plantation Community.....	25
9. Reforms of State Owned Enterprises (SOEs).....	27
10. Towards Efficient Public Service Delivery.....	29
11. Social Protection.....	31
12. Capitalizing on Emerging Mega Trends.....	33
Conclusion.....	36

Sri Lanka needs to follow good practice which is being pursued by an increasing number of countries around the world. All handouts, subsidies and other welfare measures, included in the manifestos, should be costed and specific measures should be identified for financing the incremental costs involved. This will enable the voters to assess the financial viability of the promises included in the manifestos of political parties. It should also assist in making a clean break from the 'auction of non-existent resources' which have characterized party manifestos in the past.

Introduction

The Pathfinder Foundation (PF) has been a long-standing proponent of prudent economic policy-making in Sri Lanka. It has been a constant advocate of reforms to accelerate economic growth and development.

With Parliamentary elections looming on the horizon, Sri Lanka is on the verge of entering a new political cycle which offers a window of opportunity to implement important changes.

It is timely, therefore, to seek to inform the manifesto preparation processes of the political parties and to stimulate public discussion. In this connection, the PF commissioned a series of studies on key policy areas which will be important determinants of a successful transition of the Sri Lankan economy to a sustained high growth path. This was supported by several public seminars, comments from leading experts and enriched by drawing on the experiences of other countries.

In this document, the PF has avoided getting into specific prescriptions or models based on any particular dogma and have focused instead on putting forward practical, pragmatic and implementable reforms for consideration by political parties. These are being put forward in the spirit of constructive engagement to promote the improvement of the lives of all Sri Lankans.

The Sri Lankan economy needs further reforms to achieve the objective of sustained high and inclusive growth – an avowed objective of all political parties. Sri Lanka has become an ‘aspirational society’ which seeks to achieve upper-middle income country status and beyond expeditiously. It is incumbent, therefore, on all political parties to be able to respond to the evolving aspirations for prosperity among all segments of Sri Lankan society. Failure to do so is likely to result in very damaging political and social repercussions however democratic the new dispensation.

This Blueprint is intended to inform the policy formulation processes of political parties to assist them to meet the aspirations of all Sri Lankans through promoting accelerated growth which is inclusive and regionally balanced. In advocating this Blueprint for change, cognizance has been taken of the need to transform the economy from one which is characterized by low productivity agriculture/low technology manufacturing/and traditional services (retail/wholesale trade, transport and communication and public administration) into a modern economy based on higher productivity agriculture/higher technology manufacturing and modern services, such as shipping, aviation, ICT/BPO/KPO, financial services and education/health).

This transformation of the economy cannot be achieved without the implementation of very urgent measures to stabilize the economy and to increase its productivity/competitiveness through a package of much needed structural reforms.

The last six months have given much credence to Lee Kuan Yew's statement that elections in Sri Lanka are 'an auction of non-existent resources'. The populist measures introduced in the Budget Speech (November 2014) and greatly compounded in the Interim Budget (January 2015) have seriously undermined fiscal stability. The budget deficit, in 2014, was 6% of GDP compared with a target of 5.2%. There is likely to be further deterioration in the fiscal position without urgent remedial action on both the revenue and expenditure fronts (see Section 2 for action points). It is crucial, therefore, that the manifestos of political parties exercise far greater fiscal responsibility in the preparations for the Parliamentary Elections. The people of this country should not be misled by 'giveaways' which will eventually have to be either eroded through higher inflation or reversed through taxes/administered price increases.

It is important that the 'hole in the government budget', which has been created by the Budget Speech (November 2014) and the Interim Budget (January 2015) is not worsened by self-seeking (anti-people) promises made in the political party manifestos for the Parliamentary Elections. In this connection, Sri Lanka needs to follow good practice which is being pursued by an increasing number of countries around the world. All handouts, subsidies and other welfare measures, included in the manifestos, should be costed and specific measures should be identified for financing the incremental costs involved. This will enable the voters to assess the financial viability of the promises included in the manifestos of political parties. It should also assist in making

a clean break from the ‘auction of non-existent resources’ which have characterized party manifestos in the past.

It is also important to recognize that not only have the macroeconomic fundamentals been undermined, but the growth momentum has also been weakened largely due to political uncertainty, the disruptions caused by the change in government in a highly politicized system; and the deteriorating macroeconomic outlook.

The new political cycle presents an opportunity to break out of the repeating cycle of stop-go policies which have characterized the last four decades. A key lesson to be learnt from the 2012 – 2014 period is that stabilization measures alone are not enough to achieve sustained growth which touches the lives of the people. They need to be complemented with structural reforms which strengthen the growth framework through boosting productivity/competitiveness. This is the only way one can achieve sustained increases in people’s incomes. Handouts and subsidies which are not linked to productivity are simply not sustainable. This document seeks to set out ways and means of achieving sustained and inclusive growth and development.

A key message is that Sri Lanka needs a new growth model. It has to be based on private investment. The country’s fiscal deficit and public debt dynamics preclude any possibility of a ‘statist’ growth and development process. It is domestic private investment, as well as Foreign Direct Investment (FDI), which will have to act as the locomotive for driving the

economy forward. The space for releasing the creative energy of private enterprises, ranging from small farmers and microenterprises to large corporates, should be promoted by achieving macroeconomic stability and improving the business climate.

This document addresses actions related to maintaining macroeconomic stability; improving the business climate; strengthening factor markets; promoting exports and foreign direct investment; SME development; increasing agricultural productivity; upgrading education, skills and training; reforming SOEs; improving public service delivery; empowering the plantation community; social protection; and capitalizing on some emerging mega trends.

While all these areas require attention, a number of them are medium to long-term challenges. The government, which emerges after the Parliamentary Elections, will have to prioritize and fast-track some measures to stabilize the economy and to boost the flagging growth rate. Such measures should include, inter alia, reform of public enterprises and improvement of the business climate.

The inefficient (often loss-making) operations of SOEs continue to be a drag on the development prospects of the country. There are a number of policy options for addressing this issue: privatization, strategic investments/PPPs, listing minority stakes on the stock market and securing private management. All but the last option have the added advantage of mobilizing much needed revenue for the budget (see also Section 8).

Private investment, both domestic and foreign, has been the most disappointing aspect of the post-conflict narrative. The highest priority, therefore, needs to be attached to stable and predictable policies as well as decisive action to improve the Ease of Doing Business (see also Section 2).

The PF has been motivated to produce this Blueprint, as the time is now ripe to unleash the considerable potential for Sri Lanka's rapid development. The restoration of peace, the strategic location, a literate and trainable labour force, improved infrastructures and the commencement of a new political cycle all combine to make the timing right for a major policy effort as well as focused and well-coordinated action to chart the way forward.

1. Maintaining Sound Macroeconomic Fundamentals

Since the liberalization of the economy, Sri Lanka has been characterized by repeating cycles of stop-go policies as a result of unstable macroeconomic fundamentals. Unsustainable budget deficits have been the main cause of this instability. It is, therefore, important, that a sustainable medium-term budgetary framework is maintained. This would serve to contain inflation and stabilize the balance of payments. This would, in turn, create the enabling conditions for low interest rates as well as a stable and competitive currency. It also provides a conducive framework for maintaining sustainable debt dynamics. Strong macroeconomic fundamentals are an essential precondition for developing a robust growth framework. It is also important to recognize that Sri Lanka is now operating within a new paradigm, following its graduation to lower-middle-income-country status. It is becoming increasingly exposed to the discipline imposed by rating agencies and international capital markets. This will continue to be an important factor in macroeconomic policy-making. In this connection, the erosion of fiscal discipline reflected in the populist Budget Speech (November 2014) and the Interim Budget (January 2015) is a source of concern. The highest priority needs to be attached to arrest and reverse the slippage in fiscal consolidation. As mentioned in the Introduction, all handouts, subsidies and other welfare measures should be costed and the means identified to finance them. These exercises should be placed in the public domain and all

stakeholders should have the opportunity to assess them critically.

Actions

- Maintaining a sustainable medium-term budgetary framework.
- Strengthening revenue performance by widening the tax base and improving tax administration.
(In this respect, consideration should be given to implementing the recommendations of the Tax Reform Commission which have not already been applied.)
- Increasing the share of direct taxes in revenue collection to achieve a less regressive tax system.
- Conducting a rigorous public expenditure review based on clearly established priorities to rationalize recurrent expenditure and prioritize public investment on the basis of a coherent development strategy and through adherence to evaluation based on rates of return.

While robust macroeconomic fundamentals are absolutely essential, sustained 8% plus growth cannot be achieved without an expansion in the productive capacity of the economy. The subsequent sections seek to elaborate upon ways and means of doing so.

2. Improving the Business Climate

Recording a growth rate of 8% or more over a sustained period of 10 – 20 years, as achieved by the successful countries of East and South East Asia, is eminently feasible. For this to be possible, high priority should be attached to strengthening the business climate. The strength and dynamism of the private sector will be the crucial determinant of Sri Lanka's development prospects as mentioned in the Introduction, a country with Sri Lanka's budget deficit and debt profile does not have the headroom to sustain a dynamic state-driven development process (unlike a country like China which has robust deficit and debt outcomes). The key challenge is to boost the confidence of both domestic and foreign investors. A combination of transparent pro-business policies and a reduction of transaction costs through a rigorous deregulation process would be important in this respect.

Actions

- Predictable and consistent policies based on consultation with stakeholders.
- Streamlining regulations and processes to reduce transaction costs (establishing effective one-stop shops where ever feasible).
- Improving Sri Lanka's ranking in the World Bank's Doing Business Index.
- A robust legal framework which reinforces the sanctity of contracts and enables speedy arbitration.

- Reducing rent-seeking opportunities through rigorous application of streamlined rules and regulations and minimizing discretion.
- Providing clarity regarding the respective roles of the public and private sectors. Where the state sector is involved in commercial activity in competition with the private sector, it should be on the basis of a level playing field.
- Identifying opportunities for PPPs in major infrastructure and other projects.
- Introducing transparency and competition in contracts and procurement processes.
- Maintaining the rule of law and avoiding impunity in order to create a propitious environment to boost investor confidence and enable the attaining of a range of economic and social objectives.
- Building a harmonious society to minimize the risk premium attached to the economy due to ethno-religious tensions.
- Strengthening Sri Lanka's diplomatic relations with both traditional and emerging economic partners and leveraging these to meet Sri Lanka's socio-economic goals particularly through attracting FDI.

3. Factor Markets

3.1 Land

Priority should be attached to making the land market work better for all Sri Lankans. At present, difficult access to land is a major obstacle for businesses. Nearly 80% of land is owned by the State. Hence it is important to have clear and transparent policies related to the ownership, lease and utilization of land. At present 30% of the workforce is employed in agriculture accounting for only 10% of GDP. It is important, therefore, to address patterns of land-use and product mix to increase productivity as a means of increasing rural incomes. In urban areas, government agencies such as the Railways and the Postal Department own valuable land around the country which are currently underutilized. It is important to release the value of such land through its more productive commercial use. In the process, much needed revenue can also be mobilized for the government. Priority should be attached to a comprehensive approach to optimize land utilization in a pragmatic non-ideological manner, which generates benefits for the people of the country through increased employment and income in a manner which balances the national interest and commercial realities.

Actions

- Reviewing land-use and product-mix in the light of self-sufficiency (excess production) in paddy and declining profitability of some tea, rubber and coconut lands.
- Releasing value of under-utilized state land in urban areas, including those owned by Government Agencies like the Railways and Postal Department.
- Reviewing land legislation which currently obstructs more productive use of land.
- Clear and transparent policies in relation to ownership and/or leasing of land for industrial purposes. There should be clarity regarding the purpose and scope of Industrial Parks.
- Development of a land bank, involving pre-cleared properties which is accessible online.

3.2 Labour Markets

The current rigidities in the labour market act as disincentives to the creation of more higher-value employment. It is important to adopt an approach which brings about a better balance between workers' rights, rates of return to investors and employment creation. The current labour laws are leading to a casualization of employment in the formal sector with an increase in temporary and casual jobs. In addition, enterprises in the informal sector are discouraged from upgrading their operations and entering the formal sector due to the high costs involved, especially in relation to

labour. The upshot is that overall labour standards in the country are probably lower than one would expect in a context of more flexible labour laws. In addition, higher productivity/income employment is being curtailed.

Action

- A constructive tripartite (government/employer/Trade union) review of legislation to introduce greater flexibility to the labour market while maintaining a balance between worker protection, rates of return to investors and generation of higher value employment.

3.3 Financial and Capital Markets

Developing the financial sector and capital markets, the lifeblood of the economy, is important for increasing the efficiency of financial intermediation and the allocation of capital for productive purposes. Operational costs in the banking sector are high when benchmarked internationally. This is largely due to high overheads generated by too many banks/branches. This contributes to the uncompetitive spreads (differential between deposit and lending rates) which increase the cost of funds in the economy. In addition, there is a long-tail of small non-bank institutions which amplify risks related to the financial sector significantly. While there can be

trade-offs between the interests of individual institutions and systemic stability, the latter should be given priority as contagion effects can undermine the whole financial services sector. There is therefore, a case for financial sector consolidation.

In addition, capital market development should be deepened to foster the stability of institutions and the development of new products to meet the needs of a modernizing economy. The special needs of an ageing population would also have to be addressed.

Actions

- Ensuring financial sector consolidation leads to greater stability while increasing the access to financing of the different segments of the economy, including SMEs, start-ups and business expansions.
- Further developing the long -term debt market.
- Encouraging angel investors and venture capitalists.
- Developing the mortgage industry to increase the affordability of home ownership for an aspirational society.
- Boosting the pension industry to address the needs of an ageing population in a sustainable manner.

4. Exports and Foreign Direct Investment

As growth is constrained by the size of the market, small countries like Sri Lanka need to attach the highest priority to export growth. With a domestic market of only 21 million people, it is not possible to attain sustained 8% plus growth without rapid export expansion. Currently, goods and services exports amount to about 20% of GDP. The corresponding figures for Malaysia, Thailand and Vietnam are 70% - 75% of GDP. In addition, experience from the successful countries of East and South East Asia reinforces the very strong nexus between an increase of FDI, export expansion (the trade – investment nexus) and accelerated growth on a sustained basis. A key challenge, therefore, is to double FDI from the current 2% of GDP to at least 4%.

Sri Lanka can benefit from the enormous potential stemming from the preferential access to a market of 2.5 billion people through the FTAs with China (to be completed this year) and India. The combined effects of these bilateral FTAs, infrastructure development in both Sri Lanka and India as well as the Commercial Hub Legislation, which provides off-shore status for FDI, can have a transformative impact on the development prospects of the country. The overall landscape for both FDI and exports will also be improved by Prime Minister Modi's 'Make in India' policy and China's "Maritime Silk Road (MSR) Initiative". The 'Make in India' policy is likely to introduce dynamism into India's hitherto sluggish

manufacturing sector opening up opportunities for developing regional supply chains. The MSR provides the opportunity to capitalize on Sri Lanka's strategic location, particularly for services such as shipping, activities related to a commercial hub and light engineering.

One may conclude that proximity to India and closeness to China can be key drivers of transformation to a sustainable growth – model based on FDI – led export expansion.

It is also necessary to recognize that over 50% of Sri Lanka's exports continue to be directed to Europe and the USA. It is important, therefore, that these markets are consolidated and built upon. In addition, US investment funds account for a major share of the inflows into the Sri Lankan bond and stock markets.

Actions

- A competitive exchange rate and trade policies (particularly para-tariffs and levies) which do not create a bias against exports.
- The Export Development Board should complete its preparation of an export strategy expeditiously. It should prioritize product and market diversification.
- Expanding market access through regional and bilateral trade agreements while consolidating and building upon the traditional commercial relationships including completing a well negotiated CEPA with India and an FTA with China..

- Prioritizing trade facilitation, particularly to take advantage of the FTAs with China and India (e.g. automated customs clearance, harmonization of standards through Mutual Recognition Agreements and integrated check points to expedite clearance).
- Investment promotion, which is aligned with the country's development strategy (growth sectors) and increasing the effectiveness of the Board of Investment.
- Continuing infrastructure development to improve both domestic and external connectivity.
- Improving the capacity for economic diplomacy by strengthening the Commercial Sections of Sri Lankan missions abroad.
- Providing incentives to companies and business associations to establish investment and trade promotion offices in the major commercial centers in China and India.
- Requesting China and India to establish trade and investment facilitation centers in Colombo as other countries have done.

5. Small and Medium Enterprises (SMEs)

The SMEs are the main source of employment generation in a modernizing economy. The overall business environment should assist SMEs to improve their competitiveness and market access. The major internal challenges related to SMEs include their sub-standard technology, low productivity, inferior product quality, weak access to new markets, lack of financing and financial management and scarcity of skilled labour. Their expansion is also constrained by institutional bottlenecks, lengthy and onerous bureaucratic procedures, fragmented support schemes, and a heavy regulatory burden.

Actions

- Streamlining the current highly fragmented institutional structure to improve coordination for effective delivery of support services.
- Coherent and well-coordinated interventions on training, inputs (including technology), financing and marketing in order to create an eco-system which encourages start-ups, innovation and business expansion.
- Increased market access by creating/strengthening links to domestic and/or international supply chains. This also generates other benefits such as access to technology, knowledge and financing through links to larger enterprises.
- Strengthening the capacity and empowering Regional Chambers.

6. Increasing Agricultural Productivity

The basic issue in the agricultural sector is that too many people produce too little. As a result, even with extensive support in the form of subsidies, free water, guaranteed prices and tax exemption, productivity and incomes remain low. Despite this, a large proportion of the population remains in agriculture due to the security provided by the support measures. The upshot is that there is a misallocation of financial and human resources to a low productivity sector, thereby diverting scarce resources from the newer more dynamic sectors in the economy. Furthermore, the population, as a whole, is compelled to bear the burden of this expensive support through higher taxes and food prices.

Actions

- Introducing legal reforms and policies which address land fragmentation while incentivizing land consolidation.
- Encouraging commercially viable agriculture while very gradually phasing out inefficient support measures, thereby releasing both financial and human resources needed for higher productivity economic activities as a means of addressing rural poverty.
- Introducing health and environmental standards for agricultural production to address problems such as chronic kidney disease.

- Reducing post-harvest losses by encouraging improved transport and storage.
- Strengthening extension services and research capacity to improve seed varieties and agricultural practices. This assumes even greater importance in the context of the adaptation requirements associated with more frequent extreme weather events (floods and droughts) as a result of climate change.

7. Education, Training and Skills Development

Sri Lanka can no longer depend on a growth strategy which leverages low wages and an increasing labour supply. The next phase of development will have to be driven by more skilled labour and technological upgrading in the context of an ageing population (i.e. declining population of working age).. The lack of human resources could well become the binding constraint which restrains the country's development prospects.

The current education system has been successful in terms of attaining very high participation rates, including for girls. However, learning outcomes have not been aligned with the needs of a rapidly modernizing economy. Education, training and skills development should be better aligned with the country's development strategy i.e. the needs of those sectors which drive the growth model.

Actions

- Shifting the focus of the entire education system from exam-based learning by rote to one where there is emphasis on fostering creativity, creative thinking and innovation.
- Strengthening Maths, Science and English education.

- Aligning training and skills development to the priority sectors of the country's development strategy.
- Increasing investment in tertiary education on the basis of a pragmatic and non-ideological approach to public, private and mixed provision.
- Strengthening regulation and quality assurance in private provision of tertiary education.
- Restructuring and upgrading the multitude of learning and skills development institutions and schemes (lessons can be learnt from East Asia and Germany).
- Reforming the state-owned Universities in order to make them internationally competitive.

8. Empowering the Plantation Community

The plantation community, comprising predominantly people of Indian Tamil origin, is marginalized and oppressed. They have been living in economic, social and political isolation for many years. They deserve special attention. This community lags behind other communities in terms of several social and economic indicators such as standard of living; nutrition; housing; ownership of assets and land; health standards; educational attainment, particularly at the tertiary level; participation in the public service; and women's empowerment. Public services have not reached them fully, particularly at the Divisional Secretary level. Intra-plantation variations in terms of geography, size and management are other serious concerns. Mainstreaming parity with other communities has been the expectation of this community. In order to narrow the gaps which exist in the selected development indicators, affirmative action is essential on a priority basis.

Actions

- Reduce malnutrition to be on par with other communities, with a focus **particularly** on feeding programs for pregnant mothers and children.
- Integrate the estate health system into the national system to provide higher quality service.
- Develop a programme to ensure the provision of decent housing with legal ownership, in collaboration with Plantation Companies as well as foreign and domestic donors.

- Increase the number of students qualifying for G.C.E A/L in the Science and Maths streams, thus paving the way for increasing the university admissions in those streams.
- Develop schemes to increase the numbers joining the public services, particularly at the higher level.
- Increase female representation in the elected bodies to empower them.
- Improve public service delivery at the community level.
- Develop programmes to address the special problems of people living in the Southern and Sabragamuwa Provinces.
- Develop a medium term strategy for multi-donor (governments, Corporates, multi-laterals and NGOs) support, focusing particularly on education, malnutrition, health and shelter to reduce the gap in the socio economic indicators between the estate and other sectors of the economy.

9. Reform of State Owned Enterprises (SOEs)

Sri Lanka has over 300 SOEs operating under different legal structures. While there has been improvement in the overall performance of SOEs, they continue to be a drag on the economic prospects of the country. The rates of return are low and some SOEs incur losses/arrears which have a negative impact on the state banks' balance sheets and contribute to the build-up of contingent liabilities of the government which undermines its financial stability. SOEs also constrain the development prospects of the country by providing a low return on the considerable financial and human resources absorbed by them. SOE reform can contribute significantly towards strengthening the growth framework of the economy by increasing productivity/competitiveness.

Actions

- Increasing the autonomy and accountability of decision-making processes while strengthening the Boards and Management of SOEs.
- Introducing flexibility into ownership structures of commercial SOEs through adoption of a pragmatic attitude to privatization (including employee shareholding) and PPPs.

- Where majority private ownership is considered unfeasible, a stock market listing of minority stakes of commercial SOEs brings about increased disclosure which strengthens corporate governance and increases operational efficiency.
- Increasing operational independence to respond to market signals thereby reducing the need for: (I) government assistance from a constrained budget; and (II) protective barriers which limit competition thereby increasing prices and lowering quality for the consumer.
- Benchmarking performance of state-owned monopolies against international standards.
- Expedious implementing of the findings contained in COPE reports.

10. Towards Efficient Public Service Delivery

The efficiency of the public service, in terms of policy development and service delivery, is a crucial determinant of the competitiveness of an economy. Modern economies attach a high premium to sophisticated regulation to balance competing interests in liberalized markets. In addition, efficient service delivery is crucial not only to achieve a competitive economy but also to meet the needs of poor and vulnerable sections of the society. The Sri Lankan public service is one of the largest in the world on a per capita basis. It has increased from 600,000 in 2005 to 1.4 million today. It absorbs considerable human and financial resources and yields a very low return. High priority needs to be attached to downsizing as well as improving productivity, morale and accountability. As a lower-middle-income country, with no access to concessional financing, Sri Lanka can no longer use the public service as an employment agency. This places an even higher premium on increasing the competitiveness of the economy and empowering young people through better education, training and skills development to promote a modern economy with high value employment.

Actions

- Using natural attrition and Voluntary Redundancy Schemes to reduce the size of the public service, learning from the experiences of other countries. Attention should be paid to careful sequencing with policies designed to create the conditions for generating alternative employment.
- Increasing autonomy and accountability of public servants.
- Introducing an independent and demand-driven recruitment system.
- Introducing an independent institutional arrangement for appointments, promotions, etc.
- Strengthening induction and subsequent in-service training programs.
- Improving the performance appraisal system and exploring greater recourse to performance – based pay.
- Using electronic databases and ICT solutions to improve service delivery.

11. Social Protection

A well designed, targeted and efficiently delivered social safety net becomes even more important when accelerating progress to a more competitive economy. It becomes necessary to provide social protection to meet the inevitable transitional costs, as the structure of the Sri Lankan economy evolves. The underlying principle should be protecting workers not unproductive jobs. A second objective for social protection is to support the poor and vulnerable in society. The social safety nets for both these purposes should be based on well-designed income transfer programs and not on subsidies and guaranteed prices which lead to an inefficient use of resources. They also have the perverse consequences of increasing the burden on the people through higher taxes and prices.

Sri Lanka has a long tradition of poorly designed and targeted social protection programs. The currently operational programs are no exception.

Actions

- Designing an income transfer program for those living below a carefully calibrated poverty line.
- Providing time-bound income support for those who lose their jobs as a result of

economic progress. This should be supported by re-training programs.

- Using technological advances to strengthen the delivery systems for social protection programs.

12. Capitalizing on Emerging Mega Trends

There are some mega trends which would need to be addressed as part of a forward looking development agenda for the country. It is expected that **urbanization** would take place at the rate of 3% of the population per year. Priority would need to be attached to keeping pace by creating cities with a high quality of life to meet the expectations of an increasingly aspirational and growing urban population. This will require investment in infrastructure, housing, commercial, and leisure space. In this connection, it is important to build upon the ongoing Metro-Region and 'Second Tier Cities' development programmes that are designed to bring about regionally-balanced development by fostering growth poles in different parts of the country.

Climate Change is likely to have an increasing impact on development outcomes in all countries, and in turn needs to be factored into policy-making. More frequent extreme weather events will require a higher premium being attached to adaptation measures and disaster management. In addition, the recent pledges made by China and the US on reducing CO₂ emissions has made it more likely that there will be a long overdue agreement on a post-Kyoto Protocol UN International Climate Convention.

The implications of such an agreement would need to be factored into future policy-making.

One such implication could be an international commitment to move towards greater use of **renewable energy**. In this respect, priority should be attached to explore the potential of solar and wind energy in the context of Sri Lanka. The shift to **clean energy** also requires expeditious action to develop Sri Lanka's natural gas discoveries which can also have a positive impact on the historically large oil import bill. The government's recently announced 'Energy Strategy' should be the subject of consultation among all stakeholders prior to expeditious implementation.

Mega technological trends, such as big data, cloud technology, smart connected devices, and advanced robotics (including automation of knowledge work) is likely both to create opportunities and cause disruptions, globally. Sri Lanka would need to respond to these trends in a way which addresses both the opportunities and challenges from a local perspective.

There is also a case for signing the WTO's Information Technology Agreement (ITA) which would entail elimination of all tariffs on products listed in the document. At present, 77.5% of IT products are not subject to tariffs and the average tariff stands at only 4%. Hence there would not be

major changes in the tariff structure not a loss of much revenue. Most imports are capital goods which would serve to lower cost of production in this sector that has considerable potential for growth. In addition, signing the ITA would keep tariffs at a constant level thereby facilitating long-term planning. This would enhance the attractiveness of Sri Lanka as a location for investment in the IT sector for both domestic and foreign investors.

Conclusion

Sri Lanka has the most propitious set of circumstances for over 50 years. Over the last five decades there have been major drags on the economic prospects of the country, such as severe terms of trade decline, rapid population increase and a high dependency ratio; inappropriate inward-looking policies and most damagingly the civil conflict. Today, there are no such major drags on the economic prospects of the country. In addition, economic geography is particularly favourable. Sri Lanka is located in Asia, the most dynamic region in the world. It also enjoys the advantages of close relations with China and proximity to India, the two emerging giants in the global economy. However, the benefits of such a positive historical conjuncture can only be realized through a concerted program to increase productivity/competitiveness of the economy which also strengthens the growth framework. This Blueprint seeks to contribute towards charting the way forward. It presents a menu of options. The government of the day would need to calibrate the speed and sequencing of the changes. The overall thrust is to shift from a culture of entitlements to one which unleashes the capabilities of Sri Lankans, especially the young, through their empowerment based on increased opportunities for human resource development on the one hand and productive high value employment on the other.

The government, which assumes office after the Parliamentary Elections will be confronted with the twin challenges of deteriorating macroeconomic fundamentals (largely because of fiscal indiscipline) and a loss of growth momentum. Swift and decisive action will be necessary to stabilize the economy and strengthen the growth framework through a package of fast-track structural reforms. The Sri Lankan people are now aspirational and impatient. Governments will be judged by their capacity to deliver improving living standards. The old stop-go policies of deceiving the people with handouts and then imposing burdens on them are unlikely to be politically and socially tenable in the future. The country needs a new paradigm of economic policy-making which seeks to break away from the short-term politically expedience of the past. This document seeks to inform the political parties regarding the ways and means of ***charting the way forward*** on the basis of good economics being good politics in the medium-term.

**Please share your comments with us via
pm@pathfinderfoundation.org**