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Issue Brief

The IMF-World Bank Plan for Sri Lanka:

Will It Help or Hinder South Asian Success?

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EXECUTIVE SUMMARY

Sri Lanka is at a critical moment in its history. After nearly two decades its civil war is drawing to an end. In this context, the International Monetary Fund (IMF) and World Bank are expanding their role in post-conflict Sri Lanka. As a required first step in obtaining a broad package of loans from these international financial institutions (IFIs), in June of 2002, the Sri Lankan government submitted a Poverty Reduction Strategy Paper (PRSP) that the IMF and World Bank will be approving this April. However, the policies outlined in this PRSP could lead to a reversal of Sri Lanka's impressive record on economic growth and social development over the last few decades. The process through which the PRSP was drafted and approved also raises serious questions about the opportunities for public input into decisions that will have an enormous effect on the lives of the people of Sri Lanka.

Sri Lanka is unusual in having achieved very high levels of social progress, such as life expectancy (73.1 years) and literacy (91.6 percent), for a country of its relatively low income level. It has also maintained an impressive rate of 2.9 percent per capita GDP growth over the last two decades. Its overall human development index, as measured by the United Nations Development Program, was 0.741 for 2000, which was almost equal to Turkey's (0.742), a country that has nearly twice the per capita income as Sri Lanka.

There is concern however that the PRSP now under consideration will hinder the progress that Sri Lanka has made. The policies contained in the Poverty Reduction Strategy Paper do not adequately consider Sri Lanka's experience with social and economic development since independence. This is especially true for a number of specific policies included in the PRSP that could have a profound impact on social and economic development: privatization, land law reform, and labor market reform. These policies resemble the standard policy prescriptions of the "Washington consensus" that have been advocated by the IMF and World Bank throughout the developing world over the last two decades. The implementation of these policies in Sri Lanka, with seemingly little regard for the specific features of Sri Lanka's economy and society, may undermine the factors that have allowed the country to make relatively good progress by most measures of economic and social development.

By promoting a greater role for the private sector in nearly every state-run enterprise or social service as part of its loan conditionality, the IMF and World Bank are overlooking the gains that have been made in Sri Lanka through social investment by the government. According to government spending estimates listed in the PRSP, this increased role for the private sector will mean spending cutbacks in general public services as well as social welfare and community services. Furthermore, given the track record of the policies advocated by the IMF and World Bank elsewhere in the developing world there is little reason to believe that greater private sector involvement, either in public enterprises or essential social services, will necessarily lead to increased poverty reduction or higher economic growth in the case of Sri Lanka. In fact, there are many examples to be found where the involvement of the private sector does not bring about improved efficiency, while raising the cost of services provided to the poor.

Land law reform is of concern because of its potential to cause mass rural to urban migration. The Sri Lankan PRSP anticipates that by the year 2010, 50 percent of the population will be living in urban areas. Currently a little more than 23 percent of the population is urban. The PRSP does not explain how the country will be able to cope with such a massive rural to urban migration, either in terms of ensuring adequate housing and infrastructure for the migrants, nor by generating enough employment to ensure that they will have jobs in the cities.

The labor market reform detailed in the PRSP is intended to create a flexible labor market in Sri Lanka, similar to what the IMF and World Bank have advocated elsewhere. Since the late 1990s the IMF has been singling out certain laws that it argues hinder labor market flexibility. These include the Termination of Employment of Workmen Act (TEWA), the Industrial Disputes Act (IDA), and changes to workers' funds, the Employees' Provident Fund (EPF) and Employees' Trust Fund (ETF). While labor law reforms may be necessary, the government and IFI reforms may undermine important worker protections exactly at the time when other reforms are creating major disruptions in the labor market. Specifically, the TEWA and IDA reforms are likely to lead to job loss due to increases in the number of workers being fired. In addition, the speeding up of the dispute resolution process between employers and workers would favor employers because they have better access to the mail and transport system in Sri Lanka. The EPF and ETF reforms, as with the proposed pension reform also contained in the PRSP, would create problems with provision and coverage.

Poverty reduction and economic growth in Sri Lanka are important and necessary goals. However, the proposed PRSP does not seem likely to reduce poverty or increase growth. The policies laid out in the PRSP seem not to have focused on what aspects of Sri Lankan development policies over the last few decades may have worked and why. Rather, the recommended policies appear to be designed to bring the country more into conformity with the IMF and World Bank's traditional recipes, without offering evidence that this formula will produce better results than the current and past policies of the country. There is a real basis for concern that such policies will undermine Sri Lanka's progress in development and put it on a path more similar to those less successful countries that have followed the tutelage of the IFIs in Sub-Saharan Africa, Latin America, and elsewhere.

INTRODUCTION

Sri Lanka is at a critical moment in its history. After nearly two decades its civil war is drawing to an end. In this context, the International Monetary Fund (IMF) and World Bank are expanding their role in post-conflict Sri Lanka. As a required first step in obtaining a broad package of loans from these international financial institutions (IFIs), in June of 2002, the Sri Lankan government submitted a Poverty Reduction Strategy Paper (PRSP)[2] that the IMF and World Bank will be approving this April. However, the policies outlined in this PRSP could lead to a reversal of Sri Lanka's impressive record on economic growth and social development over the last few decades. The process through which the PRSP was drafted and approved also raises serious questions about the opportunities for public input into decisions that will have an enormous effect on the lives of the people of Sri Lanka.

Sri Lanka is unusual in having achieved very high levels of social progress, such as life expectancy (73.1 years) and literacy (91.6 percent), for a country of its relatively low income level. It has also maintained an impressive rate of 2.9 percent per capita GDP growth over the last two decades. This progress was achieved even as the country struggled through a bloody civil war.

The PRSP now under consideration contains many of the standard policy prescriptions of the "Washington consensus" that have been advocated by the IMF and World Bank throughout the developing world over the last two decades. There are few, if any, examples of countries where these policies have produced the sort of progress achieved by Sri Lanka. The implementation of these policies in Sri Lanka, with seemingly little regard for the specific features of Sri Lanka's economy and society, may undermine the factors that allowed the country to have made impressive gains in most measures of economic and social development.[3]

[2] The Poverty Reduction Strategy Paper (PRSP) is a document required to be prepared by all low-income countries that qualify for assistance from the World Bank's International Development Association. The document outlines a government's poverty reduction strategy and overall economic development plan for a three-year term. The PRSP marks a change from the IMF and World Bank's earlier structural adjustment programs, and is intended to be a country-owned document, written with civil society participation, and providing adequate poverty and social impact analysis to show how the government's policies will reduce poverty and promote growth. See www.worldbank.org/poverty/strategies/. There is evidence that the Sri Lankan PRSP did not adequately adhere to any of these guidelines.

[3] Civil society groups in Sri Lanka have also raised concerns that the set of neoliberal reforms the government has already undertaken since 1977 of opening up the economy by reducing tariffs, allowing for increased foreign direct investment, and creating export processing zones, has had a negative impact on malnutrition, rural poverty, and inequality. They are therefore wary of further IMF-World Bank led reforms that may not necessarily contribute to economic growth or facilitate poverty reduction. See statement by Alliance for Protection of National Resources and Human Rights, an umbrella civil society group representing more than 125 trade unions, nongovernmental organizations, and religious clergy, http://www.geocities.com/monlarslk/Statements3.htm.

BACKGROUND

In June 2002, the Sri Lankan government submitted a Poverty Reduction Strategy Paper to the IMF and World Bank at a donors' Development Forum in Colombo. The PRSP process was undertaken by the government in the context of obtaining further loans from the IMF and World Bank. The document outlines economic development policies that the government plans to undertake over the next three years, although its repercussions will be felt for years to come. The Fund and Bank are to approve the PRSP in April, at which time they will also conclude negotiations on a possible $375 million IMF Poverty Reduction and Growth Facility (PRGF) loan,[4] allowing for the World Bank to approve further individual project loans to support the implementation of the reforms detailed in the PRSP. These steps are viewed as prerequisites for the much-anticipated meeting with donors in Tokyo in June, which will include both the government and the rebel forces from the country's North.[5]

In July, in an effort to "maintain the necessary pace of structural reform in preparation for the PRGF" (IMF Country Report No. 02/199, September 2002, p 22), the Sri Lankan government introduced 36 bills into its Parliament, directly corresponding to the reforms detailed in the PRSP. These included fiscal reform, land law reform, and labor market reform. The government attempted to force these bills through Parliament without following normal procedures of providing adequate opportunity for parliamentary review and comment, so that the Fund and Bank would approve the PRSP and subsequent PRGF loan disbursement by the end of 2002. Due in part to opposition from civil society, the timeline has since been pushed back and the executive boards of the Fund and Bank will now be meeting in April to approve the PRSP.

The PRGF was adopted as a replacement for the prior ESAF (Enhanced Structural Adjustment Facility) of the IMF. The purpose of the change, which was made in response to criticism from NGOs and governments, was to include the participation of broad sectors of society in the design and implementation of an economic program, and to make sure that the conditions agreed to by the borrowing country would contain explicit goals and methods for reducing poverty.

But the PRSP for Sri Lanka has failed to include civil society in its preparation and appears oriented towards overhauling those institutions and practices (e.g. health care, public education, rural development) that have most likely contributed to the country's relative success in social development.

[4] It is worth noting these new loans will add to Sri Lanka's existing external debt load of $8.6 billion. Source: "Sri Lanka: Selected Issues and Statistical Appendix," September 2002, p 93.

[5] See World Bank's Sri Lanka news page: http://lnweb18.worldbank.org/sar/sa.nsf/8b211d2239d56913852567d7005d8e54/cc155509068a68966525685c003ccd75?OpenDocument; "IMF Says Sri Lanka Headed for 3-Year Concessionary Loan," Anusha Attygalle, Dow Jones News Wire, January 31, 2003; and "UN, World Bank, ADB assess Sri Lanka's reconstruction needs," Shimali Senanayake, AP, March 31, 2003.

SRI LANKA'S PROGRESS IN SOCIAL DEVELOPMENT

Sri Lanka has made significant progress in the realm of social development over the course of the last few decades, while also achieving impressive economic growth. Sri Lanka's human development index[6] reflects this progress, improving over the years from 0.616 in 1975, 0.697 in 1990 to 0.741 in 2000. Its HDI level is higher than other countries in its income bracket, such as China, Indonesia, and India, and almost equal to Turkey's (0.742), a country that has nearly twice the per capita income as Sri Lanka. Given that per capita income is actually one of the components of the HDI, this means Sri Lanka's life expectancy and literacy rate are more advanced than Turkey's: 73.1 years for life expectancy compared to 69.7 years, and 91.6 percent literacy rate compared to 85.1 percent, for the year 2000. The PRSP attributes Sri Lanka's success in social development to heavy investment by the government over the years in the social sector.

> …Sri Lanka's health and demographic indicators are comparable with those of far wealthier Asian nations due to a wide range of pro-poor policies and programs, including subsidized health, subsidized education, targeted food subsidies, subsidized transport, and broad-based family planning services, which have been in existence for several decades.
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> -- "Connecting to Growth: Sri Lanka's Poverty Reduction Strategy," Government of Sri Lanka, June 2002, p 89.

Table 1 (see below) compares per capita income growth and social indicators for Sri Lanka with the World Bank's top ten debtor countries. These numbers provide evidence of Sri Lanka's achievement in social development over the last few decades. The comparison countries were chosen to demonstrate Sri Lanka's standing in relation to other countries that receive a large amount of IMF and World Bank assistance. The problematic policies contained in the PRSP call into question the validity of imposing such policies on a country that has actually been making significant progress in both economic and social development, even as it has dealt with the effects of a civil war.

In 1960 Sri Lanka's life expectancy at birth was 60.1 years, in 1980 it was 67.6 years, and in 2000 it had increased to 73.1 years. Infant mortality dropped from 69.4 deaths per 1,000 live births in 1960 to 34.4 deaths in 1980 to 14.9 deaths in 2000. Literacy increased from 80.5 percent of the population ages 15 and above in 1970 to 85.3 percent in 1980 then up to 91.6 percent in 2000. Comparing this scenario to other countries shows Sri Lanka has done about as well as Turkey, the Philippines, and Mexico, in improving its social indicators over the last few decades.

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[6] The Human Development Index, used by the United Nations Development Program, is a composite measure of the following components: life expectancy at birth, the adult literacy rate and the combined gross primary, secondary, and tertiary school enrollment ratio, and GDP per capita in PPP US$. See http://hdr.undp.org/statistics/faq.cfm.

Sri Lanka's annual per capita income growth from 1975 to 1980 averaged 3.02 percent, and from 1980 to 2000 it was 2.9 percent. By comparison, Mexico's average annual per capita income growth rate had been 4.09 percent from 1975 to 1980, then decreasing to less than one percent, 0.31 percent, from 1980 to 2000. The divergence in these two countries' growth rates over the last twenty years represents the difference between adding almost eighty percent to national income over a twenty-year period in Sri Lanka versus increasing it by less than ten percent in Mexico.[7] This is of particular interest given that Mexico is seen as a success story for having followed the "Washington consensus" path since the 1980s of opening up its markets, liberalizing trade and capital account, and encouraging foreign direct investment through NAFTA. There is concern that the policies contained in the PRSP will negatively impact Sri Lanka's social development and economic growth, as Mexico -- and Latin America generally -- has suffered a dramatic slowdown in economic growth co-incident with the extensive implementation of these policies over the last two decades.

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[7] Sri Lanka's real per capita GDP was $746 PPP in 1980; it increased by 77.2 percent to $1322 PPP in 2000. By contrast, Mexico's real per capita income was $3176 PPP in 1980 and increased by only 6.4 percent to $3379 PPP in 2000. See Table 1. Source: World Development Indicators 2002 and author's calculations.
Note also that Sri Lanka's growth over the last two decades -- fueled in part by the garment industry which is set to contract due to the WTO's Multi Fiber Agreement phase out in 2005 (see p 11) -- has been achieved despite a loss of an estimated 2-3 percentage points of GDP a year due to the civil war which began in 1983. The government has spent between 5-6 percent of its GDP in recent years on military expenditures. See "Sri Lanka Poverty Assessment," Report No. 22535-CE, World Bank, June 2002, pp viii, 23, 56, 61.

"WASHINGTON CONSENSUS" FOR SRI LANKA?

The policies contained in the Poverty Reduction Strategy Paper do not adequately consider Sri Lanka's experience with social and economic development since independence. This is especially true for a number of specific policies from the PRSP that could have a profound impact on social and economic development: privatization, land law reform, and labor market reform.

Privatization

> The role of the government in economic development has been clearly defined, concentrating its economic activities only in areas where market mechanisms fail to function effectively, such as education, health, the environment, rural and small sector activities, safety needs for the poor, and social and cultural development.
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> -- Faiz Mohideen, Sri Lanka's Alternative IMF/World Bank Governor, Statement at 2000 IMF/World Bank Annual Meetings.

By promoting a greater role for the private sector in nearly every state-run enterprise or social service as part of its loan conditionality,[8] the IMF and World Bank are overlooking the gains that have been made in Sri Lanka through social investment by the government. As detailed in the previous section, Sri Lanka's social development is at a higher level than other countries in its income group. The Sri Lankan government acknowledges in the PRSP that the country's progress towards fulfilling the Millennium Development Goals was due to previous state investment in social development.

However, according to government spending estimates listed in the PRSP, an increased role for the private sector will mean spending cutbacks in general public services as well as social welfare and community services.[9] Furthermore, there is not sufficient evidence provided by the IMF and World Bank in the case of Sri Lanka or elsewhere in the developing world that greater private sector involvement, either in public enterprises or essential social services, will lead to increased poverty reduction or higher economic growth.

[8] "Directors commended the authorities for the successful divestiture of the government's holdings in a number of major enterprises, and supported the privatization program for 1998. Directors encouraged the authorities to establish a timetable for the next wave of privatization, and to continue their efforts to promote the commercialization and increase the transparency of all enterprises remaining in the public sector." From IMF Press Information Notice No. 98/58, August 12, 1998. This quote is representative of the IMF's policy on public enterprise reform in Sri Lanka. See also "Sri Lanka: Recent Economic Developments," IMF Staff Country Report No. 98/95, September 1998, Annex II and III, pp 60-76.

[9] Government spending on general public services is set to contract by 1.5 percent of GDP between 2002 and 2006 from 5.6 to 4.1 percent, while spending on social welfare and community services is set to decrease by 0.9 percent of GDP from 3.7 to 2.8 percent. See "Connecting to Growth: Sri Lanka's Poverty Reduction Strategy," Part II of "Regaining Sri Lanka," Government of Sri Lanka, June 2002, p 108.

The PRSP outlines a policy framework that advocates an increased role for the private sector if not outright privatization of numerous state-owned enterprises as well as private sector involvement in government-run essential services. The IMF has recommended public enterprise reform through privatization of most state-owned enterprises in each of its country reports in recent years.[10] The Fund asserts that the country's history of "nationalization" and "protectionist measures" has led to the majority of sectors in the economy being government-run,[11] and recommends that the majority of government entities be privatized or restructured with the private sector's involvement, including most recently the Ceylon Electricity Board (CEB) and the Ceylon Petroleum Corporation (CPC).[12] The World Bank's private financing arm, the International Finance Corporation (IFC), is already arranging financing for the privatization of the Commercial Bank of Ceylon and Sri Lankan Life Insurance Corporation; yet the IFC points out that both enterprises are currently profitable and running efficiently.[13] Neither the Sri Lankan government in the PRSP, nor the IMF in its reports, provide adequate evidence explaining why every state-owned enterprise would necessarily be better run by a private company. Past experiences in Sri Lanka and elsewhere have demonstrated that privatizations can often be mired in corruption and do not necessarily lead to improved efficiency.[14] In addition, if there are not adequate safeguards, privatizations may lead to large-scale job losses in some industries, especially in a context of labor market reform that may not provide an adequate social safety net or resources for job retraining services.

The partial privatization of essential social services is also being advocated. The World Bank argued both in a 1998 report on Sri Lankan social services and a June 2002 poverty assessment that improved targeting of services to the poor, partial privatization of social services, and decreased government spending on the social sector would improve efficiency and foster poverty reduction.[15] The PRSP therefore calls for an increasing role for the private sector in education, healthcare, and social welfare programs, with an eye towards focusing on delivery of these services to the poor, while simultaneously planning decreases in government spending in these

[10] See footnote 8.
[11] See again "Sri Lanka: Recent Economic Developments," 1998, p 68.
[12] The IMF highlights in its September 2002 Country Report that "[t]he privatization program is on track and state enterprise restructuring has begun" (p 9). As part of this, the Fund set out the private sector restructuring of the CEB and CPC as requirements for the final disbursement of $64M under Sri Lanka's April 2001 Stand By Agreement (SBA) with the Fund, and for continuing progress on negotiations for the PRGF. See "Sri Lanka: 2002 Article IV Consultation and Final Review Under the Stand-By Arrangement--Staff Report; Staff Statement; and Public Information Notice and the News Brief on the Executive Board Discussion," IMF Country Report No. 02/199, September 2002, pp 1, 9, 14, 19-22.
[13] "Sri Lanka: Proposed Investment in Commercial Bank of Ceylon," Acting Corporate Secretary, International Finance Corporation, December 30, 2002.
[14] There are examples worldwide of corrupt privatization deals. There were reports of corruption in the sale of Air Lanka to Emirates airline in Dubai; see "Sri Lanka to renegotiate controversial deal with Emirates airlines," Agence France Presse, January 21, 2002. As another example, in Brazil in 1999, wiretapped conversations of President Cardoso's revealed that he had pressured a state bank pension fund to financially support one particular company he had ties to during the privatization auction of the state telecommunications company, Telebras, in 1998. See "New Scandal Threatens Cardoso Government," EFE News Service, May 26, 1999.
[15] See "Sri Lanka Social Services: A Review of Recent Trends and Issues," World Bank Report No. 17748-CE, April 1998, pp 5-9, and "Sri Lanka Poverty Assessment," World Bank, 2002, pp 2, 28-41, 57-60.

areas. In addition, social insurance programs are to be encouraged to be provided on a "commercial and competitive basis."[16]

Experience with public sector reforms advocated by the World Bank in other countries indicates that caution is warranted. In Uganda, for example, the IMF and World Bank have advocated the need for cost recovery in education and health care through the implementation of user fees. In their 2002 Joint Staff Assessment of Uganda's PRSP they noted that "[c]ost effectiveness and quality of outcomes in the social sectors are still outstanding issues to be addressed," arguing that the elimination of user fees in education and health had an adverse effect on the quality of those services.[17] Yet the elimination of user fees for primary education through the Ugandan government's 1997 Universal Primary Education program brought about a large increase in school enrollment. By 1998, total primary school enrollment had increased by almost 3 million children, doubling the number of children receiving a primary education.[18] In spite of such evidence, the IMF and World Bank continue to argue against the elimination of user fees while promoting a greater role for the private sector in social services. However, it is difficult to see how charging often unaffordable fees to the poor, to improve the delivery of these services, will facilitate poverty reduction.

The PRSP also advocates an increased role for the private sector in the provision of clean water to the poor.[19] There are numerous cases worldwide where the private sector's provision of water has increased inefficiency, failed to provide the poor with clean water, and the water provided has been priced out of the reach of the poor.[20] Multinational corporations such as Suez, who had participated in a number of water privatization efforts in developing countries, have even begun recently to opt out of privatization because it appears that privatizing such services in poor areas will not allow the supplier to recoup its costs.[21]

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[16] See "Connecting to Growth: Sri Lanka's Poverty Reduction Strategy," 2002, pp 73-83.

[17] "Poverty Reduction Strategy Paper Annual Progress Report: Joint Staff Assessment," IMF and World Bank's International Development Association, August 26, 2002, p 7.

[18] See World Development Indicators 2002 and IMF Press Information Notice No. 98/37, June 11, 1998.

[19] "The draft National Policy on Rural Water Supply and Sanitation Sector recognizes that water is a basic human need, but also has an economic value. Users should contribute to investments and bear the recurrent costs of drinking water and utilizing sewage and sanitation services....Government estimates that the investment requirements in the water sector will be as much as Rs.50 billion over the 2001-2010 period.…This underscores the importance of attracting private sector investment into the provision of clean water. A pre-requisite to this is the introduction of a water pricing policy that is based on the cost of delivering water and other economic criteria." "Connecting to Growth: Sri Lanka's Poverty Reduction Strategy," 2002, p 78.

[20] In Manila, Philippines, the privatization of the water system led to increased inefficiencies, rising prices, and decreased access for the poor. In 2002, five years after privatization, the French company Suez's subsidiary, Ondeo, along with the Philippine company involved, Benpres, pulled out of the deal because of financial losses, due in part to their inability to convince the government to raise rates high enough. See "Philippine-French joint venture pulls out of Philippine water concession," Agence France Presse, December 9, 2002, and "Bid to end Philippine water agreement," Roel Landingin, *Financial Times*, p 36, December 10, 2002. A similar scenario was repeated in Atlanta, Georgia, in the United States, where 94 percent of the country's water systems are publicly-controlled. Atlanta's water privatization also caused increased inefficiencies, rising prices, and decreased access for the poor. In this case it was the city government asking the private company involved, United Water -- also a subsidiary of Suez -- to leave, less than four years after the deal between the city and the company was made. See "As Cities Move to Privatize Water, Atlanta Steps Back," Douglas Jehl, *The New York Times*, Section A, p 14, February 10, 2003.

[21] See "Suez introduces its 2003-2004 action plan: refocus, reduce debt, increase profitability," Suez Press Release, January 9, 2003.

Pension reform in the form of partial privatization is also outlined in the PRSP, similar to the social security reform advocated by the IMF and World Bank in many other countries. The transition from government-provided defined benefit payments for the elderly to privately-administered defined contribution accounts in other countries has not brought about the expected increase in coverage and has increased fiscal deficits during the transition. In addition, the promise of high rates of returns to the private accounts has not materialized in most cases, as administrative fees paid to the financial industry have drained away much of the value of these accounts.[22] It is of questionable merit to advocate this reform in Sri Lanka without adequate poverty and social analysis, particularly given its negative outcomes elsewhere. In recent policy documents, the World Bank has also begun to question its advocacy of this type of pension reform.[23]

Land law reform

The Sri Lankan PRSP anticipates that by the year 2010, 50 percent of the population will be living in urban areas.[24] Currently a little more than 23 percent of the population is urban. This enormous rural to urban migration of a quarter of the population is to be facilitated by land law reform, as well as state investment in rural education and vocational training.[25] The state presently owns about eighty percent of the land in Sri Lanka. The majority of the rural poor cultivate land to which they do not hold official title. The land law reform proposes that these farmers be given freehold titles to their land, which are official land titles that would give them the option to sell that land. The World Bank has argued the case for this kind of land reform in recent country documents, stating the need to create a "flexible" market for land in Sri Lanka.[26] The Bank specifically points to Thailand and Indonesia as examples of other Asian countries that have successfully undertaken land reform in previous decades.[27] The IMF and World Bank, however, do not make the case that Sri Lanka's peasants would be better off with this type of land law reform than under the current arrangement.

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[22] See Dean Baker and Debayani Kar, "Defined Contributions from Workers, Defined Benefits for Bankers: The World Bank's Approach to Social Security Reform," July 2002, Center for Economic and Policy Research (CEPR); and Dean Baker and Mark Weisbrot, "The Role of Social Security Privatization in Argentina's Economic Crisis," April 2002, CEPR.

[23] See Peter Orszag and Joseph Stiglitz, "Rethinking Pension Reform: Ten Myths about Social Security Systems," in *New Ideas About Old Age Security*, Robert Holzmann and Joseph Stiglitz, eds., February 2001, World Bank.

[24] "Connecting to Growth: Sri Lanka's Poverty Reduction Strategy," 2002, p 83. It is worth noting that the UNDP's estimate of Sri Lanka's 2015 urban population in its 2002 Human Development Report is a more modest 29.9 percent.

[25] "To reverse the relentless fragmentation of agricultural lands into ever smaller plots, one option is to equip the rural population with the skills and ability to migrate to urban areas, where higher productivity employment opportunities are more abundant. Government will promote rural-to-urban migration that does indeed reduce poverty by enhancing the quality of rural education and vocational training and by improving the quality of labor market information services." "Connecting to Growth: Sri Lanka's Poverty Reduction Strategy," 2002, p 62.

[26] See "Sri Lanka: Non Plantation Sector Policy Alternatives," Robert Hunt and Douglas Lister, World Bank, March 1996; and "Sri Lanka Poverty Assessment," World Bank, 2002, pp 56-57.

[27] It is worth noting that Indonesia's land reform under Suharto was marred by widespread violence. See *Rich People, Poor Forests*, Nancy Lee Peluso, University of California Press, June 1992.

There are further reasons why this land law reform is of concern. The agricultural policies implemented by the government over the last ten to fifteen years, supported by the IMF and World Bank, have had the effect of diminishing state assistance to the agricultural sector. Price supports, subsidies, and the availability of credit have all been scaled back or eliminated. Price setting mechanisms such as the Paddy Marketing Board have been shut down. According to farm and labor groups, these actions taken together have had the impact of lowering the market prices for farmers to a level below production costs. [28] The Fund and Bank's policies of privatizing the state banks is likely to further reduce the availability of agricultural credit for small farmers. Land law reform in this context may compel farmers to sell their land in hopes of better opportunities in the cities.

However, encouraging small-scale farmers to migrate to urban areas in large numbers will not necessarily improve their economic situation. There is evidence from other countries' experiences that rapid migrations result in large numbers of urban poor.[29] The full phase out of the Multi Fiber Agreement under the WTO in 2005 will lead garment sector jobs to move largely to China, which will have a major negative impact on Sri Lanka's labor market.[30] There will also be urban labor market consequences from demobilization of military forces as well as job losses to overseas workers resulting from instability in the Middle East.[31]

The ownership of small land parcels by the rural poor has arguably provided them with a last means of survival and prevented farmers from becoming fully destitute. Encouraging these small-scale landholders to sell their land and seek off-farm employment in villages and urban areas in large numbers creates a potentially dangerous situation, since they will not be guaranteed employment when they reach the cities. Furthermore, combining this land law reform with the other policies of privatization and labor market reform contained in the PRSP could lead to increased economic instability, rather than the desired outcomes of poverty reduction and growth.

Labor market reforms

In the area of labor market reform, the PRSP details reforms that will create a flexible labor market in Sri Lanka, similar to what the IMF and World Bank have advocated elsewhere. The IMF has singled out certain laws that it argues prevent the development of a more flexible labor

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[28] See "Sri Lanka's Poverty Reduction Strategy: A Trade Union and Worker Response," Prepared with Sri Lankan trade unions by the ILO, December 2002, pp 23-24.

[29] See A. S. Oberai, "Population Growth, Employment and Poverty in Third World Mega-Cities," in Proceedings of the International Population Conference Montreal, 1993, Vol. 2, pp. 105-119; and Ajit Singh, "Urbanization, Poverty and Employment: the Large Metropolis in the Third World," *Contributions to Political Economy*, Vol. 11, 1992, pp. 15-40.

[30] The MFA phase out will lead to factory closures and rising unemployment as China and India attract away business; see "Greater China's Accession to the WTO: Implications for International Trade/Production and for Hong Kong," Prepared for Fifth Annual Conference on Global Analysis, Joseph Francois and Dean Spinanger, June 2002; and "Productivity, Competitiveness and Job Quality in Garment Industry in Sri Lanka," Prepared for the ILO, by Saman Kelegama and Roshen Epaarachchi, Institute of Policy Studies, Colombo, Sri Lanka, November 2001.

[31] Remittances from overseas workers are the second largest source of foreign exchange in Sri Lanka after garment exports. About 90,000 Sri Lankan jobs were lost during the 1990-91 Gulf crisis and war; the current war could well have a similar impact. See "90,000 Sri Lankans to Receive Gulf War Compensation," Xinhua News Service, June 16, 1994.

market since the late 1990s.[32] These include the Termination of Employment of Workmen Act (TEWA), the Industrial Disputes Act (IDA), and changes to workers' funds, the Employees' Provident Fund (EPF) and Employees' Trust Fund (ETF). The IMF insisted that the Sri Lankan government undertake these reforms before the PRGF could be approved.[33] The World Bank echoed the IMF in this, pointing to the easing of labor restrictions in Sri Lanka's export processing zones as a good model for labor market flexibility.[34]

The Sri Lankan government introduced the labor law reform legislation in July 2002, along with the other 30-plus pieces of legislation. Revisions to the TEWA were intended to make it easier to fire workers without ensuring adequate compensation; the changes to the IDA were supposed to allow for faster resolution of labor disputes; and the reform of the EPF and ETF was to provide a greater private sector role in administering these accounts. Opposition by the trade unions was able to weaken the legislation, and the Labor Minister committed to not implementing the reforms until such time as an adequate social protection scheme was in place to deal with the resulting increase in unemployment.

While all segments of society, including the trade unions, acknowledge that some reforms to labor laws are necessary, the government and IFI reforms may undermine important worker protections exactly at the time when other reforms are creating major disruptions in the labor market. Specifically, the TEWA and IDA reforms are likely to lead to job loss due to increases in the number of workers being fired. In addition, the speeding up of the dispute resolution process between employers and workers would favor employers because they have better access to the mail and transport system in Sri Lanka. The EPF and ETF reforms were similar to the proposed pension reform mentioned above, and would create the same coverage and provision problems as pension reform would. The other major trade union concern was the undemocratic nature of the process of the implementation of the labor market reform. Unlike the Ceylon Chamber of Commerce, the trade unions were not involved in the process of drafting the PRSP, nor were they involved in formulating the labor market reform.[35] Such tripartite consultations between the government, employers, and workers are required by the guidelines of the IFIs' PRSP process as well as by Sri Lanka's ratification of the ILO's Convention 144 that calls for tripartite consultations. The lack of such a consultation process has the impact of creating conflict and possible instability in the industrial sector.

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[32] See "Sri Lanka: Recent Economic Developments," 1998, pp 54-59.

[33] See "Sri Lanka: 2002 Article IV Consultation and Final Review Under the Stand-By Arrangement--Staff Report; Staff Statement; and Public Information Notice and the News Brief on the Executive Board Discussion," 2002, p 22.

[34] See "Sri Lanka Poverty Assessment," World Bank, 2002, pp 57-58. It is worth noting that the lack of labor protection in Sri Lanka's export processing zones (EPZs) are in violation of the ILO's Core Labor Standards. See "Petition to Remove Sri Lanka from the List of Beneficiary Developing Countries under the Generalized System of Preferences," AFL-CIO, December 2, 2002. It is therefore curious that the IMF and World Bank are promoting policies that would make the entire economy resemble the EPZs.

[35] See "CCC Strategy to Reduce Poverty," *Sunday Observer* (Colombo), Business Section, March 10, 2002, http://origin.sundayobserver.lk/2002/03/10/bus02.html; "Support Should be Given to Those with Skills: Poverty Reduction Strategy," *The Island* (Colombo), Business Section, May 4, 2002, http://origin.island.lk/2002/05/04/busine08.html; "Dangers Behind the 36 Bills," People's Alliance Against the Sale of Public Assets to Foreign Corporations, *Daily Mirror* (Colombo), Opinion Section , August 2, 2002, http://www.dailymirror.lk/2002/08/02/opinion/2.html; and "Lanka under IMF, World Bank spell," Feizal Samath, *Sunday Times* (Colombo), February 23, 2003.

The argument put forth by the government and IFIs for their labor market reform is that current labor laws in Sri Lanka contribute to unemployment and impede productivity growth. However, they do not present any research indicating that these labor market protections generate higher unemployment or impede productivity.[36] In addition, a recent study by consultants to the government of Sri Lanka found that between 1990 and 2001 while average real minimum wage rates decreased in every sector (agriculture, industry, and services), the overall rate of productivity grew by approximately 3 percent a year during the last ten years.[37] Neither the government nor the IFIs provide adequate evidence supporting their claim that the removal of labor market protections would necessarily be conducive to poverty reduction or economic growth. Furthermore, the labor law reforms outlined in the PRSP and then passed this January would, if implemented, lead to increased job insecurity in an environment without proper unemployment insurance. If greater mobility of workers is to be promoted, adequate social protections to account for the increased job loss must be taken into account. In addition, as noted above, the impending repeal of the Multi Fiber Agreement has already led multinationals to move factories to China, where labor is cheaper and there are fewer labor rights. Sri Lanka is therefore not poised to compete with China on the bases of cheap and unprotected labor, nor is it in its economic or social interests to do so.

It is worth noting the gender implications involved in the combined impact of each of the above reforms. Women comprise the majority of Sri Lankan workers employed in both of the key foreign exchange earning sectors of the economy, the garment industry and overseas remittances. Women account for somewhere between 70 and 90 percent of garment industry workers and account for almost 70 percent of Sri Lankan overseas workers.[38] In this context, the policies contained in the PRSP, given their potential impact on the Sri Lankan economy, will have a particularly large impact on female workers.

[36] A recent study of OECD countries indicates a lack of evidence for the widely accepted notion that institutions designed to protect labor are related to unemployment. See Baker et al, “Labor Market Institutions and Unemployment: A Critical Assessment of the Cross-Country Evidence,” November 2002, Center for Economic Policy Analysis, New School University.
[37] See National Productivity Policy, Ministry of Employment and Labour of Sri Lanka, 2002, www.slproductivity.org.
[38] Sources: Department of Census and Statistics, Ministry of Finance and Planning, Government of Sri Lanka; and Sri Lanka Bureau of Foreign Employment.

CONCLUSION

Poverty reduction and economic growth in Sri Lanka are important and necessary goals. However, the proposed PRSP does not seem likely to reduce poverty or increase growth. While the drafters of the document note Sri Lanka's relative success in these areas over the last five decades since independence, they do not appear to have taken the particulars of this experience into account in their policy recommendations. The IMF and World Bank along with the Sri Lankan government seem not to have focused on which aspects of Sri Lankan development policies over the last few decades may have worked and why. Rather, the recommended policies appear to be designed to bring the country more into conformity with the IMF and World Bank's traditional recipes, without offering evidence that this formula will produce better results than the current and past policies of the country. There is a real basis for concern that such policies will undermine Sri Lanka's progress in development and put it on a path more similar to those less successful countries that have closely followed the policy advice of the IFIs.

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Table 1: Growth and Social Indicators - Sri Lanka + Top WB Debtors*

	1970	1975	1980	1985	1990	1995	2000
Human Development Index							
Korea		0.691	0.732	0.774	0.815	0.852	0.882
Argentina		0.785	0.799	0.805	0.808	0.83	0.844
Mexico		0.689	0.734	0.752	0.761	0.774	0.796
Russia			0.809	0.827	0.824	0.779	0.781
Brazil		0.644	0.679	0.692	0.713	0.737	0.757
Philippines		0.652	0.684	0.688	0.716	0.733	0.754
Turkey		0.593	0.617	0.654	0.686	0.717	0.742
Sri Lanka		**0.616**	**0.65**	**0.676**	**0.697**	**0.719**	**0.741**
China		0.523	0.554	0.591	0.625	0.681	0.726
Indonesia		0.469	0.53	0.582	0.623	0.664	0.684
India		0.407	0.434	0.473	0.511	0.545	0.577
Per Capita Income (PPP 1975 Intl$)**							
Korea		1693	2131	2665	4109	5637	6509
Argentina		4553	4870	3767	3573	4482	4635
Mexico		2600	3176	2894	2954	2959	3379
Russia					4664	2953	3137
Brazil		2304	2835	2489	2574	2763	2856
Turkey		1726	1769	1808	2237	2428	2612
China		273	326	457	645	1098	1489
Philippines		1502	1732	1337	1542	1488	1487
Sri Lanka		**643**	**746**	**799**	**942**	**1141**	**1322**
Indonesia		467	611	679	903	1195	1140
India		461	469	498	648	762	883
Average Annual Per Capita Income Growth, Preceding Five-Year Period**							
China			3.59	7.03	7.12	11.24	6.27
Sri Lanka			**3.02**	**1.37**	**3.36**	**3.90**	**2.99**
India			0.34	1.22	5.40	3.31	2.99
Korea			4.71	4.57	9.04	6.53	2.92
Mexico			4.09	-1.84	0.41	0.04	2.69
Turkey			0.49	0.44	4.35	1.65	1.47
Russia						-8.73	1.22
Argentina			1.36	-5.01	-1.05	4.64	0.67
Brazil			4.23	-2.57	0.67	1.43	0.66
Philippines			2.89	-5.04	2.88	-0.71	-0.01
Indonesia			5.51	2.15	5.87	5.75	-0.94
Life Expectancy							
Argentina	66.8	68.2	69.6	70.7	71.6	72.7	73.9
Korea	59.9	63.9	66.8	68.7	70.3	71.8	73.2
Sri Lanka	**64.6**	**66.2**	**67.6**	**69.0**	**70.2**	**71.4**	**73.1**
Mexico	61.7	64.2	66.8	69.0	70.8	72.0	73.0
China	61.7	64.7	66.8	68.3	68.9	69.4	70.3
Turkey	56.7	59.3	61.4	63.4	66.1	68.3	69.7
Philippines	57.4	59.3	61.3	63.4	65.6	67.7	69.3
Brazil	58.9	60.8	62.6	64.1	65.6	66.9	68.1
Indonesia	47.9	51.3	54.8	58.6	61.7	64.1	66.0
Russia			67.1	68.8	68.9	64.8	65.3
India	49.4	51.8	54.2	56.6	59.1	61.4	62.8

Table 1 Continued

	1970	1975	1980	1985	1990	1995	2000
Literacy							
Russia	98.2	98.5	98.8	99.0	99.2	99.4	99.6
Korea	86.8	90.2	92.9	94.5	95.9	96.9	97.8
Argentina	93.0	93.7	94.4	95.1	95.7	96.3	96.8
Philippines	83.6	86.4	88.9	90.9	92.4	94.0	95.3
Sri Lanka	**80.5**	**83.0**	**85.3**	**87.1**	**88.7**	**90.2**	**91.6**
Mexico	74.9	78.7	82.3	85.3	87.9	89.8	91.4
Indonesia	56.2	62.9	69.1	74.7	79.6	83.6	86.9
Brazil	68.1	71.8	75.5	78.4	80.9	83.2	85.2
Turkey	56.6	63.2	68.5	74.0	77.9	81.9	85.1
China	51.3	58.2	65.5	71.9	76.9	80.8	84.1
India	33.1	36.9	41.0	45.2	49.3	53.3	57.2
Infant Mortality							
Korea	46.0	33.2	25.8	17.6	12.2	9.8	8.2
Sri Lanka	**53.2**	**43.8**	**34.4**	**24.8**	**18.5**	**16.5**	**14.9**
Russia			22.1	20.7	17.4	18.1	16.2
Argentina	51.6	42.6	34.8	29.0	25.2	22.2	17.4
Mexico	73.0	61.8	51.0	42.8	36.4	32.2	29.2
Philippines	83.2	74.0	64.6	46.0	37.0	35.0	30.7
Brazil	94.6	83.8	70.6	59.0	47.8	37.7	31.7
China	69.0	48.0	42.0	37.0	38.0	36.2	32.0
Turkey	144.0	127.2	109.2	89.4	58.0	44.4	34.5
Indonesia	118.0	108.6	90.0	75.2	60.0	46.0	40.9
India	137.2	130.2	114.8	97.0	80.0	74.0	69.2

*Countries ranked by 2000 value for each indicator.

**Per capita income in PPP constant $ derived using US GDP deflator (Economic Report of the President).

Sources: Human Development Report 2002 and World Development Indicators 2002.