ITC Executive Forum

BUSINESS FOR DEVELOPMENT:
IMPLICATIONS FOR EXPORT STRATEGY-MAKERS

SRI LANKA

PRO – POOR EXPORTS STRATEGY –
THE ESSENTIAL INGREDIENTS

Cancún, Mexico – September 2003

1. Introduction

Sri Lanka's human development index is by far the highest in South Asia and exceeds that of some wealthier countries. This level of human development has been achieved through the provision of universal access to health and education and continued investment in the social sectors. Economic Development, however, has lagged consistently behind social development. More over it appears to have largely by-passed the rural areas, where about 80 percent of the population lives.

While it is recognized that the nature and causes of poverty are multi dimensional, the most widely used macro indicator of resource deprivation is that of income or consumption poverty. There are two types of standards for the measurement of poverty, namely the relevant and the absolute. The former involves calculating a poverty line and defining those falling below that line as poor. In the latter case, the lowest segment of the income or expenditure distribution is defined as the poverty group. Both measures provide valuable information.

Use of a higher poverty line implies a significantly higher level of poverty than does use of a lower poverty line. It is reasonable to assume that the majority of those living below the lower poverty line are victims of chronic (or long term poverty) while those living in the income band between the lower and higher poverty lines are vulnerable to transitory (or short term) poverty. If a dollar a day is used as the poverty line (adjusted for purchasing power parity) only around 7 percent of the Sri Lankan population is poor. But when the poverty line is increased to dollar two a day, the poverty level increase to over 45 percent.

The bulk of the rural population is engaged in such activities as small scale agriculture and coastal fishing, which are greatly influenced by seasonal factors. Despite this vulnerability, in countries which experience a steady growth of rural per capita incomes which are widely shared, the trend is for the absolute poverty level to decrease over time. But in the case of Sri Lanka, even though per capita GDP growth averaged nearly 4 percent per annum during the 1990s, the expected decline in the poverty level did not occur. This suggests that growth strategies pursued during the past decades have not been sufficiently broad-based and that the bulk of the poor have failed to enter the main stream of economic development.

2. Analysis of Some Causes of Poverty

2.1 Poverty by Sector

Poverty in Sri Lanka is a distinctly rural phenomenon. According to the last survey carried out by the Department of Census and Statistics, 88 percent of the total poor (those falling below the poverty line) reside in the rural areas, compared with 8 percent in the urban areas and 4 percent in the estate areas.

If a higher poverty line is used, poverty incidence is highest in the estate or plantation sector areas. A shift from the lower to the higher poverty line is accompanied by a substantial rise in the poverty level, the most pronounced being in the estate sector (25 – 45 percent). This would suggest that "border Line" poverty is a significant problem in all three sectors, (viz. rural, estate and urban) with the estate sector showing the highest level of vulnerability. However, the estate community does have reasonably stable employment, free housing (although of poor quality) and access to basic health facilities. A recent World Bank study has concluded that even though estate households account for only 4 percent of all poor households, they are among the poorest in Sri Lanka.

About 43 percent of principal income earners in poor households are employed in agriculture. Sluggish agricultural growth in the 1990s (at less than 2 percent per annum) certainly contributed to keeping poverty in the rural and estate areas at relatively high levels.

Available evidence shows that the bulk of the poor comprise among others the following groups.

(a) Farmers cultivating low value crops especially on very small holdings;
(b) Plantation workers;
(c) Workers in the fisheries and livestock sectors;
(d) Workers in cottage or small industry that cater to low income markets and have low wage rates.

The breakdown of poverty by occupational category reveals that farmers have the highest instance of poverty (52 percent). The level of poverty among production workers is also quite high (38 percent). The majority of production workers have low skills and are engaged in providing low value goods and services to small, low income, informal markets.

2.2 Inadequate Growth and Unequal Opportunity

In the 1990s GDP growth in Sri Lanka averaged 5.1 percent while per capita GDP growth averaged 3.9 percent. However, neither the GDP growth rate nor its distributive effect were sufficient to bring about a marked reduction in the poverty level. In other words economic growth has not automatically trickled down to the poor.

Sri Lanka's current economic growth strategy is unlikely to achieve a sustained and broad-based reduction in poverty unless corrective measures are taken. For example, the textiles and garments industry which is the largest export earner (accounting for 52 percent of exports) and which provides employment for over 300,000 women from less privileged backgrounds, faces looming Multi Fibre Agreement (MFA) problems.

2.3 Isolation and a Lack of Economic Integration

People living in remote areas are subject to economic isolation due to lack of access to markets, information and basic infrastructure facilities among which are telecommunications and information technology. The poor can therefore benefit from improved transportation and information systems as well as higher output prices and stimulated employment.

2.4 Slow Growth in Agriculture

Agriculture accounts for roughly 40 percent of the work force and 18 percent of GDP. Low labour productivity in agriculture is a major contributor to persistent rural poverty. Crop yields have either stagnated or declined during the 1990s. The poverty situation in rural areas would have been therefore aggravated if not for income transfers to the rural areas, including income transfers from rural young females employed in the garment factories mainly in the Western Province which includes the capital city of Colombo.

The single most important impediment to agricultural prosperity is an overly restrictive policy regime due to state ownership of some 80 percent of the lands, restrictions on technology imports and land usage. Other important factors are limited post harvest processing and value addition, lack of access to investment finance and the disruption of agricultural markets due to the armed conflict that prevailed in the North and East.

One of the factors inhibiting rural development and which encourages rural to urban migration is the lack of secured property rights to land. Most poor farmers cultivate land parcels for which they do not have clear title. As a result land cannot be used as collateral for loans, reducing the credit worthiness of agricultural operations.

Social Exclusion and Powerlessness

At its peak, the Sri Lankan government expended nearly 2 percent of GDP in social support programmes such as Samurdhi. Despite good intentions these projects and programmes have failed to empower the poor to alleviate poverty due to dependency effects and patronage.

Barriers to Urbanization

Sri Lanka has an over regulated labour market, which reduces flexibility, discourages formal sector employment and provides incentives for enterprises to operate in the "unregulated" informal sector. Difficult procedures and extended delays in involuntary separation, the need for official approval for worker retirement, labour market protection against involuntary separation which extended even to senior company management, complex and non-timely dispute settlement procedures, limited safety net coverage for displaced labourers and an administrative approach to managing labour market affairs inhibited employment creation and effective funding of the labour market.

3. The essential ingredients of the Pro Poor Export Strategy

In terms of the Regaining Sri Lanka strategy, achieving a 10 percent economic growth rate depends critically on increasing exports and expanding access to overseas markets.

3.1 Value Addition to Rural Products

Here the Strategy adopted is to organize individual small producers in the industry sector and farmers in the agriculture sector into viable legal entities called Export Production Village (EPV) Peoples companies under an EPV Programme and linking them to export houses for supply of selected products for which there is a demand in international markets. The strategy aims to utilize rural raw materials and skills for the export production effort in a meaningful manner, in order to ensure the benefits of exports trickles down to rural producers.

In Sri Lanka as in many other developing countries rural producers are exploited by middle men particularly in the agricultural products sector. The strategy effectively eliminates the middle men by the national Trade Promotion Organization (TPO) replacing the middle men and acting as the link between the producers and export houses in order to ensure fair trading practices.

The strategy aims to go a step further to add value to rural produce by establishing export processing companies (EPCs) in the rural production areas. The majority investment of 51 percent in EPCs is by the link exporter/s, while 28 percent is in the hands of the EPV companies owned by the rural producers, and the balance investment of 21 percent is held initially by State Institutions such as the national TPO to be transferred to the rural EPV Companies when the rural producers are able to buy over the investment made by the TPO on their behalf.

In Sri Lanka post harvest losses in the agriculture sector is estimated to be as high as 30 percent due partly to inadequate use of post harvest technologies and mainly to losses incurred during transportation of fresh produce from rural producing areas to urban centres. Therefore, the strategy of value addition through EPC companies ensures increased incomes to the rural producers.

It is also significant to note that most rural producers who are engaged in production activities under the EPV/EPC exports strategy are those who are beneficiaries under the State social support programme known as "Samurdhi", as their incomes are below the poverty line. The objective of the strategy is therefore to enhance their living standards by providing them opportunities to increase their incomes through gainful employment and to make them self-reliant.

3.2 Enhancing Productivity and Competitiveness

Under this strategy the national TPO has embarked on several programmes related to specific product sectors which also encompasses and benefits the poor. Some of these are briefly outlined below :

3.2.1 The national TPO has embarked on a programme to encourage regional plantation companies in the plantation sector to diversify production from the main plantation crops of tea, rubber and coconut to other agricultural crops. The strategy will not only enhance profitability of the plantation sector companies but will also directly benefit the poor estate communities by providing them employment and increasing their incomes. The strategy also ensures increase in overall export earnings. Discussions have already been held with the regional plantation companies to diversify production by cultivation of spices for which there is a ready export market, particularly in view of the fact that the range of spices produced in Sri Lanka are of high quality. Assistance and incentives in the form of low cost financing will be arranged to the regional plantation companies by the national TPO to encourage intercropping or mono-cropping of unutilised spice lands. It is estimated that approximately 6000 hectares of land suitable for the cultivation of spices and related crops are available both in the private and public sector plantations.

Under this programme there is also potential for the regional plantation companies to shift reliance from cyclical commodities to agri business which includes high value fruits, vegetables and floriculture products. In most areas climatic conditions and the geographical locations offer potential to supply fruits, vegetables and floriculture products to major consumption markets. Producers who will be engaged in these programmes mostly belong to the estate poor.

3.2.2 The apparel Industry which accounts for over 50 percent of export earnings employs over 300,000 females, from poor rural families, in urban garment factories. Most factories especially of the Medium to Small category face the threat of closure, with the abolition of the MFA in 2004, unless strategies are adopted to make them more competitive or to find alternative business opportunities.

Strategies that are adopted to ensure competitiveness of the apparel industry include Promotion of the image of the industry, Increasing market access, Market intelligence, Aggressive marketing in existing markets and Exploring new markets.

Programmes are also undertaken to improve technology, for design and product development, for backward integration, to reduce manufacturing costs and to reduce lead times of supply.

Another strategy is to increase the productivity of a minimum of 50 percent of the apparel industry by approximately 30 percent by 2007, to reduce manufacturing costs.

It is also proposed to provide a supportive framework to small and medium industrialists to make a smooth transition to alternative business or aid easy exit from the apparel industry. In order to provide alternative employment opportunities to production workers from poor backgrounds, the leather products and footwear industry is considered to be a good bet as it requires similar skills.

3.2.3 In the case of the Gem and Jewellery industry an upmarket strategy of value addition and 'Branding' is adopted. For this purpose the intrinsic and unique qualities of the well known 'Ceylon Blue Sapphire' is to be used to add value to the jewellery products exported from Sri Lanka targeting the upper end niche markets. It is estimated that by converting just 25 percent of gems exported from Sri Lanka to Jewellery products, additional value addition and export earnings will be in the region of Rs. 4 billion (US$ 400 million).

As Sri Lanka has the technology to convert the abundantly available raw material resource of 'Geudas" to blue Sapphires, the trickle down effects of the strategy related to increased export earnings is expected to pervade the entire value chain of the industry. In this regard, it is significant to note that the beneficiaries at the lower end of the value chain will be the gem miners who belong to the poorer segment of the community.

3.2.4 Most of the production workers engaged in the handicraft industry are from village areas and are low wage earners. In this sector the strategy is to impart training in production skills, product and design development, productivity improvements and exposure to modern market requirements, in order to enhance the incomes of low wage earners. Most of them belong to the 'artisan' category at present and are reluctant to move away from their traditional production methods, to which they have become accustomed.

3.3 Improving Infrastructure Facilities and Access to Markets

Here the overall strategy aims to improve infrastructure facilities and the means of production, to connect poor regions to dynamic markets. It consists of three components.

(a) Grant full ownership of land to one million farmer families who occupy and carry out farming activities in state lands at present, to enable them to offer such lands as collateral to financial institutions and obtain credit facilities to carry out production activities in a meaningful manner.

(b) Build a modern express way network to lower the transport and marketing costs faced by the poor;

(c) Repair, maintain and rehabilitate strategic roads to lower farm to market costs;

In this context the national TPO has embarked on the implementation of a programme to take information technology and e-commerce to the rural areas. The strategic approach is to establish e-commerce centres in the provinces and linked to a Central e-commerce facility and Cyber Trader at the TPO Headqaurters which in turn is linked to several international data bases through the Internet. The e-commerce centres access latest market and buyer information related to the products that are produced in the rural areas and provide them to rural producers on a timely basis. They are also provided facilities to directly access the internet and are also provided e-mail facilities to enable them to correspond with buyers, trade support institutions and business counterparts. Web advertising services to promote the products that are produced at a rural level and services for the production of modern promotional material such as CD ROMs are also provided.

The national TPO is also in the process of establishing an On-line Trading Platform to enable marketing transactions, including payments, to be carried out electronically in order to ensure all rural production systems are geared to make use of the benefits of modern information technology.

Conclusion

The overall objective of the pro poor export strategy is to create an awareness among rural producers of modern export marketing techniques, to enable them to effectively integrate into the international trading system and reap the full benefits of their production efforts. In order to achieve this objective, state agencies have already embarked upon several supportive programmes, the more important ones of which have been outlined in this paper.