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Sri Lanka - Mainstreaming trade policy

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1. Introduction

For decades after independence, Sri Lanka's image has been one of a "welfare state" characterized by programmes like generous food subsidy schemes and universal, free, publicly-managed education and healthcare systems. Rice subsidy was the most well known of these programmes. Attempts to introduce changes, even small, to this scheme at various times, for budgetary or political/ideological reasons, have met with political tensions and civil disruptions. The scheme was at the centre stage of politics and policy until its elimination in 1977. The 'rice politics' also symbolized the competition between traditional, low-productive rural sector and the modern, market-oriented, capitalist plantation and manufacturing sector. This clash between the two sectors was also aligned to a large degree with the political interests of the two main political forces in the country and was to manifest in different ways in the ensuing years (Athukorala and Kelegama 1998).

Understanding changes in economic policies requires examining the broader contextual political economy than merely describing policy episodes. This applies even after 1977 when a different economic course was chosen. As in a majority of countries around the world, political parties in Sri Lanka are also divided into two broad camps on economic policies – the right-of-centre and the left-of-centre. Development visions and policies reflect these positions. In the post-1977 period, liberal open-economic policies have been the basic framework, but governments have at times attempted to blend this with concerns like poverty and small farmers, at one time also with "free economy with a human face."

Sri Lanka was engaged on the PRS process since late 1990s. This paper examines the experiences gained in that process and lessons learnt in trying to formulate

consistent strategy and policies as regards overall development goals and aspirations on the one hand and sectoral trade and agricultural policies on the other. It will be seen that the PRS process provides a colourful testimony to the difficulty faced by development planners in arriving at harmonious policies. The paper also summarizes experiences with attempts on inclusive policy making process through stakeholder consultations.

The next section is the substantive part of the paper. It describes the PRS formulation process since 1998 and discusses various difficulties encountered and issues raised that need to be addressed. Section 3 presents some concluding remarks.

2. Experiences with PRSP formulation and issues on trade mainstreaming

This section has five sub-sections. The first three cover Sri Lanka's three PRSPs. The narratives cover both the PRS formulation process and the underlying issues. The last two sub-sections address two cross-cutting themes: the issue of trade mainstreaming in PRSPs; and inclusive policy making process through stakeholder consultations. Before the first PRSP is introduced in section 2.1, it is useful to note the evolution of the process and key policy documents formulated by various governments since 1977 (Box 1).

2.1 The First PRSP – Regaining Sri Lanka, 2002

The PRS process

The PRS process began in 1998 with work on the elaboration of a Poverty Reduction Framework (PRF). For this, a Steering Committee, a Consultative Committee and several working groups were formed. The first PRF draft was presented and discussed in May 2000 with 35 leading NGOs and community-based organizations. Subsequent stakeholder consultations took place in December 2000 (the first Development Forum) for which a draft PRS (GoSL 2000) was made available. This was met with limited success in mobilizing external resources. However, the consultative process continued with the aim of soliciting views and cooperation of all partners who have a stake in the development of the country. The PRS process was supported by several donors, notably the UNDP, World Bank, IMF, GTZ and ILO.

However, the PRS preparation process was gradually overshadowed by other events – the conflict in the country and also early election in December 2001. The new government attached less priority to the PRS process but the process continued in a limited form, with further stakeholder workshops and a second Development Forum in June 2002. Finally, in December 2002, the PRSP was submitted and

presented as an annex to the government's economic reform programme entitled "Regaining Sri Lanka: Vision and Strategy for Accelerated Development" (RSL in short) (GOSL 2002). Very little information about this document was divulged to the public, parliament, or even many members of the government. It was ultimately submitted to the IMF and World Bank in December 2002 as the PRSP. The RSL was transformed into a PRSP by grafting onto it the 2000 draft PRS document. The PRS formed Part II of the RSL and newly developed Part III contained Action Plans purportedly integrating Parts I, *Vision for Growth* and II, *Connecting to Growth: Sri Lanka's PRS*. Part III was prepared through a Working Group mechanism headed mostly by business and industry members hand-picked by the new government and assisted by a team of consultants. This enabled the government to claim that the RSL was prepared through an extensive consultation process, though no consultations took place on the vision of the document contained in Part I.

In the preamble to the PRSP, the government declared that its "single minded priority is to overcome the debt crisis", a major issue then. This provided the rationale for the strict austerity measures followed in the subsequent months. As for poverty reduction, the government position was that this is possible only through accelerated economic growth at 8-10 percent rates, and not the usual 4-5 percent.

Following the submission of the PRS to the World Bank and IMF, negotiations began for PRS-related loans and facilities (PRGF, EFF of the IMF, PRSC, and so on). The response was positive and Sri Lanka started to receive funds for the PRS implementation (see Venugopal 2006 for details on the process). Consistent with the objectives and priorities of Sri Lanka's PRS, it was decided that the PRSCs would support reforms in two major areas: i) accelerating economic growth and supporting private sector development; and ii) strengthening governance in the public sector and improving the welfare system. Furthermore, the PRSC proposed to help the government in the following areas (World Bank 2003):

1. Move forward with the structural reforms, create conditions for accelerating economic growth, and send a strong signal to the private sector.
2. Continue fiscal consolidation and also have some fiscal space for the priority PRS programmes; and
3. Improve public sector governance, and strengthen institutional framework and capacity in the management of public resources.

Commentary – poverty, agriculture and trade issues in the PRSP

A critical assessment of the World Bank/IDA document on the first PRSC clearly shows that the objective of the credit facility was supporting an ambitious reform agenda, similar to a typical SAP, and not necessarily meant for any strengthened poverty focus. The inclusion of the PRS document in the approval documentation is misleading on this point. Indeed, the CSOs then alleged that the use of PRSP in

Box 1:

Key national development and sectoral policy papers

May 1977 to Aug. 1994 - Government of the United National Party (UNP)

- *National Agriculture, Food and Nutrition Strategy: A Change in Perspective*. Ministry of Plan Implementation, June 1984
- *National Agriculture, Food and Nutrition Strategy*, 1984 – 1988. Under the leadership of the National Planning Department of the Ministry of Finance and Planning.

Aug. 1994 to Sept. 1999 - Government of the People's Alliance (PA)

- *Policy Statement of the Government* - 1995, Ministry of Finance and Planning.
- *National Policy Framework for Agriculture, Lands and Forestry*, 1995-1998, Ministry of Agriculture, Lands and Forestry.

Oct. 1999 to Nov. 2001 - Government of the People's Alliance (PA)

- *Poverty Reduction Strategy (Draft)*, 2000 – prepared under the leadership of the External Resources Department of the Ministry of Finance and Planning.
- *Vision 2010*, Prepared by the National Planning Department of the Ministry of Finance and Planning in May 2000 and completed in 2001.

Dec. 2001 to Apr. 2004 - Government of the United National Front (UNF)

- *Regaining Sri Lanka* (with the PRS 2000 as an addendum), Dec 2002, the national development policy framework of the Ministry of Finance.
- *Agriculture Policy*, 2003-2013, in 2003, Ministry of Agriculture, Livestock and Samurdhi.

May 2004 to Nov. 2005 - Government of the United Peoples' Freedom Alliance (UPFA)

- *Sri Lanka New Development Strategy: Framework for Economic Growth and Poverty Reduction*, 2004, NCED, Ministry of Finance and Planning.

Nov. 2005 onwards - Government of the UPFA

- *Mahinda Chintana: Ten-Year Horizon Development Framework*, 2006–2016, Department of National Planning, Ministry of Finance and Planning, 2006.
- *National Agriculture Policy*, Sept. 2007, Ministry of Agriculture Development and Agrarian Services.

the RSL was only to satisfy the requirement for receiving PRSC, and there is hardly any mention of the poverty impacts of the proposed reforms. Some argued that although the RSL goes in the name of Sri Lanka's PRS, it is obviously a package of economic reforms designed to carry forward the SAPs that the WB and IMF have been imposing on Sri Lanka over the last two and a half decades, under different names (MONLAR 2003).

All subsequent loans and facilities did mostly focus on a programme of accelerated reforms in areas like labour market regulation, property rights in land markets, privatizing the power and banking sectors, and rationalizing the civil service. The GoSL also undertook a speedy process of implementing the economic reform programmes - in all, 36 new laws were introduced as part of the 2003–06 programme.

The process of formulation of the 2000 PRSP is important because this was the only time when a broad, nation-wide consultation process was set in motion for the preparation of any national development plan. The consultation itself is considered to be of a limited nature, mainly soliciting feedbacks on completed drafts from technical experts and line ministry officials. The process was criticized for not being a genuine desire to seek inputs but merely to satisfy a donor demand. Indeed, the preparation process was led by the External Resources Department of the Ministry of Finance and Planning, and not by the Department of National Planning that traditionally has the mandate for such a work. The final draft of this PRSP was ready by 2000 but was not formally presented to donors. One message of this PRSP was that the government's role is to create an environment which stimulates the participation of all groups of society in the realization of economic growth, and reflected a view that the government should not try to directly stimulate the process of poverty reduction. What was formally presented to the donors was the RSL strategy of December 2002, which was formulated without any comparable consultation with the public, or even within the members of the government party.

There was some acknowledgement that the PRSP did not address much poverty issues. For example, in their Joint Staff Assessment (JSA) of the PRS, the World Bank and the IMF noted that "the overly broad discussion is not always grounded in data, which makes it hard to quantify the major impediments to poverty reduction. This in turn makes it hard to link diagnostics and analysis to the setting of policy priorities" (JSA 2003). It also noted that there appeared to be some disconnect between the agricultural sector issues and approach for improving the sector's productivity described in the main text and the Action Plan matrix. For instance, while the main text advocates private sector driven productivity improvements, the action plan appears to advocate continued state interventions.

In presenting poverty diagnostics, the PRSC noted the following points. Low labour productivity in agriculture is the major factor behind persistent rural poverty.

A dominant constraint to raising productivity is said to be excessive government intervention in agricultural commodity and factor markets (notably restrictive land policies, with state ownership of near 80 percent of all land, which limited efficient land use and allocation, regulations that limited technology imports, commodity price interventions, continuing emphasis on input and credit subsidies at the expense of more productive public investments, and unpredictable trade policies).

In the discussion of agricultural productivity and growth as a component of the rural sector development, the PRSC also outlined the agreed framework for actions in the area of "Trade Policy" as follows. In order to induce more private investments in agriculture, agro-industry and storage, reduce within-year price fluctuations, and improve food security, the government will need to resist the pressure to continue seasonal altering of tariff rates. Over the short-to-medium term, the government needs to commit to *reducing tariff protection gradually for various agricultural commodities*. This reform will reduce the bias in favour of particular crops (e.g. rice, potatoes, chillies, onions) and thus allow improved domestic resource allocation and reduce the taxation of consumers who are made to pay above-world market prices.

It was further said that with the removal of price distortions, cropping patterns would adjust to changing economic incentives, including shifting from low-value and low-productivity activities (such as rice production) towards commercial production of alternative higher-value crops. To minimize the adjustment cost associated with tariff reforms, other critical policy changes will have to match the phased tariff reductions with measures to lift the constraints on domestic, commodity and factor (land, seeds, technology and water) markets and to improve rural infrastructures. These complementary actions will help ensure that farmers have the freedom and the capacity to alter their resource-use decisions to meet the changing needs of the market.¹

Despite the close link between poverty and agriculture, the extent and depth of analysis of agricultural trade in the PRSP was limited. Having identified export-led growth as the main strategy, the PRSP relied heavily on trade liberalization. Not only it did not consider domestic agriculture as a source of growth but also failed to consider the impact of trade liberalization on different groups of poor and vulnerable people, particularly farmers producing importables, mainly food. This imbalance in emphasis between export-oriented policies and the domestic food sector was a major defect of the PRSP that led to its widespread criticism.

The whole process was dismissed by many stakeholders in the country as "donor-driven", and that the PRSP was formulated merely to receive funding from the

¹ Annex III. Rural Sector: Enhancing Agricultural Productivity Growth, The World Bank, 2003.

donors. The failure to make decisions on agricultural trade policy reflecting the views of stakeholders was considered to be a significant weakness.

There were many protests to the PRSP from the CSOs. A group of over 125 CSOs known as the *Alliance for the Protection of Natural Resources and Human Rights in Sri Lanka* rejected the proposed PRSP and in a letter to the IMF and World Bank called for more meaningful and substantive negotiations. They asserted that there have not been adequate consultations with the civil society and affected groups during the PRS development process and many reforms are being pushed through without due consideration to putting in place adequate social safety nets. The Alliance alleged that contrary to the Fund and Bank's stated commitment to principles of country ownership and participation that are supposed to guide the PRS process, this document was written to mirror the Fund and Bank's policy recommendations for Sri Lanka. The Alliance demanded that the approval and implementation of the PRSP is halted until it can be redrafted based upon full civil society and social movement participation.

In a paper that explores the roles of the domestic actors and donor community in the evolution of Sri Lanka's post-conflict economic package of 2001-2004, it was even argued that the inappropriateness of this economic package was a critical element that contributed to the overall failure of the peace process (Venugopal 2009). In addition, the government's simultaneous pursuit of fiscal austerity to secure desperately needed concessionary financing from the IMF meant that not only was there very little in the way of a peace dividend to distribute, there were instead cutbacks on subsidies and employment.

The end result was that the government, architect of the RSL, was dissolved prematurely after being in power for only two years and replaced with a new government after elections in May 2004. This government had been supported by a broad coalition of forces, including the left-oriented parties that opposed blatantly outward-oriented, open-market economic policy of the government that was in power since 1977 and became allies in defeating it in 1994. Yet, the economic policies of this new government continued to embrace the same open-economic policies. An attempt to undertake sweeping tariff reform in agriculture by drastically cutting back protection for food products, in 1995 when the Uruguay Round Agreement began, was withdrawn. Nevertheless, the left-oriented coalition parties withdrew support and the government collapsed in 2001. The lack of poverty focus in the reform agenda was a major reason for these political problems, and which influenced the development policy framework of the next government.

2.2 The second PRSP - National Poverty Reduction and Growth Strategy, 2004

The RSL had thus a short lease of life. The new government in 2004 announced a new policy framework titled *Sri Lanka: New Development Strategy*, with a

separate poverty reduction and growth strategy imbedded in it. The new strategy was compiled from several background documents prepared then by the new government, notably the *Economic Policy Framework 2004 - Creating our Future and Building our Nation*, and the vision further articulated in the 2005 budget speech. One significant re-focus in the vision and main objective was the recognition of “special consideration given to pro-poor growth strategies” along with the acceleration of economic growth. The new strategy is premised on “pro-poor, pro-growth” income improvement and redistribution policies with complementary participation of a socially responsible private sector and a strong public sector. It was claimed that higher economic growth alone is not sufficient to reduce poverty and a focus is needed on pro-poor growth strategies.

A new PRSP evolved from the above New Development Strategy during 2004 and 2005, called *National Poverty Reduction and Growth Strategy* (NPRGS). However, this policy strategy too had a very short lease of life itself since the term of the President Kumaratunga ended in November 2005. But many elements of this strategy and approaches taken in translating them into actionable projects were used in the preparation of the economic development strategy of the next government headed by President Mahinda Rajapaksa, discussed next. By now, the balance of the political position had shifted away from the previous one-sided attention to liberal policies and export-led growth towards a strategy that also spoke of non-export agriculture, poverty and the role of state.

2.3 The current PRSP - Ten-year Horizon Development Framework 2006-2016

The SLFP leadership that formed the government in November 2005 under President Mahinda Rajapaksa had the support of a broad coalition of parties, including left parties and splinter groups espousing ultra-nationalism. The most important document that influenced subsequent policies was the Election Manifesto of the President, known as *Mahinda Chintana*. It contained many elements aimed at strengthening the role of the government in the management of the economy and scaling up welfare-oriented policies and subsidies, thus deviating markedly from the policies of the past, and indeed even further from the previous UPFA governments (1994-2005).

This election manifesto was transformed into a new national development strategy under the title *Mahinda Chintana: Ten-Year Horizon Development Framework 2006-2016* (THDF) (GOSL 2006), and is currently the main reference document for all national planning, also substituting for the national PRSP. The THDF embodies a strategy of restraining the open-economic framework set in motion after 1977, and zealously followed during the RSL years, by refocusing attention on, *inter alia*, the agriculture sector and import substitution, stronger government intervention in the production system, reinstatement of subsidies, and active perusal of trade

policies. The THDF showed a high-level of consideration towards the plight of the farmers and rural producers. While acclaiming widely recognized free-market policy prescriptions as necessary to move the economy forward, it makes space for most of the pledges present in the manifesto such as extensive protection to agriculture producers, reclaiming state ownership of large economic assets and expanding government.

On trade policy in general and agricultural trade policy in particular, Box 2 summarizes the vision and sectoral policy of the THDF. What follows presents some commentaries on these statements.

As regards the statements on the 60 percent tariff and the safeguard, note that this desire to apply 60 percent tariff to protect strategic agricultural commodities is not consistent with the country's WTO obligation, as Sri Lanka's WTO bound tariffs for all agricultural products are only 50 percent. Raising the bound rate is possible but only through negotiations with trading partners, which is often difficult and protracted. No initiative has been taken so far on this. Second, the statement speaks of a liberal trade regime supported by adequate safeguards. This presumably is for the rest of the agricultural products (i.e. other than strategic) but again so far there is no indication of Sri Lanka taking an active role in the WTO negotiations on special safeguard mechanism (SSM) to ensure that what will come out of these negotiations is what Sri Lanka has in mind as an effective instrument.

An issue may also be raised on the position of "adopting stable trade policies". As discussed in the previous chapter, one of the defining features of Sri Lanka's tariff policy for the recent 3-4 years has been frequent variation of tariffs on key

Box 2

Vision and policy of the THDF on agricultural trade

Vision - An agriculture sector contributing to regionally equitable economic growth, rural livelihood improvement, and food security through efficient production of commodities for consumption, for agro-based industries and for exporting competitively to the world market (page 3.)

Sectoral Policy - Adopting stable trade policies: Liberal trade regime supported by adequate safeguards (page 7.)

By way of further articulating this vision, the THDF states the following on agricultural trade: *"Direct involvement in the commodity market will be gradually reduced and by 2009, agriculture trade policy will become more stable and transparent for the main food commodities. The high rates of specific duties used to protect strategic agricultural commodities will be replaced by a duty of about 60 percent..."*

food products. Indeed, tariffs during 2006-2010 have been most volatile for any period in the recent history. While this gives an impression that the government is actively using trade policy to attain some goals, this practice is not consistent with the declared goal of providing a stable and transparent trade policy. Traders in particular have complained that the government has introduced several new import duty measures labelled as cesses and levies in an effort to circumvent too frequent adjustments in the announced tariff level. Moreover, one other recent practice is also not consistent with the above declared policy – the conversion of many tariff lines into specific rates from *ad valorem* tariffs before. All these point to the government facing continued difficulty in providing a stable trade policy environment. As discussed in the previous chapter, the difficulty emanates from the tendency of the government to use tariff to balance the interests of producers and consumers in the short-term without making efforts to understand the source of the problem and exploring alternative non-trade instruments to address them. And as a last point, applied tariffs on many sensitive products have been found to exceed 60 percent, the maximum promised in the THDF.

2.4 Towards mainstreaming trade in the PRSP

There is some indistinctness about the meaning of the term mainstreaming. A commonly understood meaning of this term is that trade policies should be supportive of the core national development goals such as growth and poverty reduction. It involves the systematic promotion of mutually reinforcing policy actions across government departments and agencies, creating synergies in support of agreed development goals. While a reading of the key national policy documents is very useful, more can be learnt from observing actual implementation also *vis-à-vis* policy statements in these documents. There are also other ways to conceptualize the relationship and through that to understand the mechanics of mainstreaming. For example:

- Integration of trade policy into national macro-economic policies and poverty reduction strategies,
- Integration of trade strategies into sectoral policies, and
- How trade specialists, poverty experts and sector analysts work together to develop a common understanding of trade policy impacts.

Since being transformed to be an export-oriented economy in the late 1980s, trade policy measures have been an integral part of the national development strategies of Sri Lanka over the last couple of decades. In that sense, Sri Lanka's PRSP was not significantly different from other development strategies announced prior to that. For example, the PRSP observed that "Sri Lanka's economy is highly open, with total trade equivalent to more than 70 percent of the GDP. The economy is bound to become even more exposed to international markets as regional and multilateral trade accords broaden Sri Lanka's market access. The Government is

committed to reducing trade protection and establishing a two-band tariff system. Efforts are being made to establish a range of bilateral and multilateral trade accords to expand international market access, with the Free Trade Agreement with India being the first of several efforts to expand market access" (PRSP Ch. 3, Page 4, GoSL 2002).

The PRSP argued for widespread trade reform based on efficiency criteria: "Raising agricultural productivity and promoting commercialization will require a stable and predictable agricultural trade policy regime. High rates of protection for food crops penalize the poor because the vast majority of the rural poor are net food buyers. High and variable rates of trade protection for agricultural products discourage agribusiness investment and confine domestic producers to thin and volatile domestic markets. Government will forge an agricultural trade regime built on predictable levels of tariffs to support efficient agricultural commercialization" (PRSP Ch. 3, Page 33, GoSL 2002).

Thus, it could be argued that Sri Lanka's PRSP, at least in its design, exhibited good practices in mainstreaming trade issues. It has been suggested that trade enters PRSPs in two basic ways (UNCTAD 2004).

1. Projections of export and import growth become a part of the macroeconomic framework.
2. Inclusion of a wide range of trade objectives and trade policies related to those objectives.

Within this approach the focus is identifying a country's trade interests within the context of its development objectives, translating those trade interests into a set of trade objectives and identifying trade policies and complementary non-trade policies that are also essential for meeting those objectives. The essence of this approach is that it requires a two-way mainstreaming of both trade and development into poverty reduction strategies.

Thus, the right question to ask is how did various trade policy options relate to the overall development strategy and what were the poverty impacts of them? The former would have been answered by exploring questions such as in what products and sectors does the country has a comparative advantage, and what are the demand growth prospects of different products and sectors in markets? The latter is related to issues such as the magnitude of local value-addition and externalities associated with these products and sectors and the employment intensity of specific trade activities and their linkages with the rest of the economy.

As observed by the World Bank and IMF while endorsing the first PRSP (the 2002 RSL), the disconnect between the issues and approach for improving productivity of the agriculture sector in the main text, on the one hand, and the recommended

actions cited in the Action Plan Matrix, on the other, indicated incomplete attention to following through the chain of reasoning. Despite being soundly supported by arguments in favour of greater liberalization, the PRSP failed to address poverty implications of trade policies, nor adopted measures to minimize the impacts on the affected population groups. However, this does not fully explain the subsequent opposition to and rejection of the RSL by the people. There was also a complex dynamics involving the weak progress in the peace process and pressures from the government's simultaneous pursuit of fiscal austerity in order to secure desperately needed concessionary financing from the IMF and World Bank. The resulting cutbacks in subsidies and employment opportunities severely eroded little support the RSL commanded in the absence of the broad consultation recommended for the PRS process (Venugopal 2009).

The development plan of the present government based on the THDF is claimed to have greater ownership by being completely home grown and having a high degree of country ownership. It attempts to overcome the weak ownership of major reforms undertaken under earlier governments by adopting a more gradual approach to reform. The core of the THDF is to achieve high growth rates through investment in large scale infrastructures and the knowledge economy, and to focus on rural development to help lagging regions.

There is also no evidence that the THDF, including its policies, was based on a sound poverty analysis as called for by the PRS process, and so it cannot also claim to be an improvement over the former PRSPs on this ground. Its proposed strategy to deal with necessary reforms in the agriculture sector is weak, and its recommended solutions risk delaying the inevitable pressure for deep reforms of the sector. While it uses a simpler language that advocates trade liberalization, it did not attempt to discuss options and determine appropriate trade policy in a participatory way drawing upon the perspectives and aspirations of stakeholders. Supply-side issues which facilitate trade and complement trade policy (e.g. infrastructure, marketing etc.) appear to be well covered thereby justifying urgent donor attention and resources. And as a last point, the THDF is also subject to the same criticism as the previous PRSPs in not taking initiative to demonstrate through *ex ante* impact analysis that the proposed trade measures were indeed designed to support poverty reduction.

In the post-1977 phase of liberal economic regime, key sectoral ministries assumed greater control over the process of formulating strategy and policies for their respective sectors. While desirable in many ways, this also runs the risk of undermining consistency between national and sectoral plans on the one hand and among sectoral policies on the other. Likewise, the fact that the two main political parties of the country have somewhat different political ideologies has also influenced the consistency of sectoral policies. Indeed, there have been instances when national and sectoral policy frameworks have undergone changes even when

a Cabinet is reshuffled. Policy consistency can also be affected when the Executive President and the Prime Minister come from different political parties, but this has not been a big issue for Sri Lanka because except for two short periods (1994 and 2001-2004) both have been elected from the same party.

It is a common practice in Sri Lanka for a newly-elected government to announce a policy framework based on its election manifesto. This is also evident from the listing in Box 1. There are some downsides of this practice. For example, for reasons of prior policy commitments made in the manifesto as well as time constraints, stakeholder consultations, feedbacks and consensus building gets undermined.

2.5 Inclusive policy formulation process through stakeholder consultation

In the course of the background work for this paper, many consultations were held with experts, stakeholders, officers and industry representatives – in groups and one-on-one discussions – to understand views and positions on appropriate trade policies and trade mainstreaming and the policy making process. With further liberalization of agricultural markets as the primary policy challenge, a series of questions were posed to them to sharpen the focus.

First, stakeholders expressed broad agreement to the definition of trade mainstreaming understood as a mechanism of avoiding policy and programme contradictions and a means of maximizing sector synergies. There was a widespread agreement that many past policies have not been ‘mainstreamed’ in this sense. This was particularly so when it came to national policies on poverty and rural employment on the one hand and trade policy on the other. A majority of stakeholders supported further liberalization of agricultural markets over the medium to long term, although there was a lack of clarity in their views on the length of this period.

Second, as regards tariff policies, a concern was expressed that the pass through of the change in the border measures to lower levels remains incomplete due to non-competitive markets along the chain. A parastatal body (STE) could in theory contribute to creating competitive markets but this too has not worked.

Third, trade and market liberalization over the years have not been as effective as expected, or promised, in improving poverty levels among small farmers and rural poor. For example, the across the board sharp reductions of import tariffs in 1995 with the Uruguay Round Agreement caused a marked decline in national production of several products (notably of onions, chillies and potatoes) but no alternative products or non-farm rural activities were thought of or provisioned for offsetting the negative impacts. An expansion of fruit and vegetable crops, aimed at export markets, to replace the deprotected crops could have been done, for example. In view of this, and similar other experiences, stakeholders felt strongly that trade policy changes should

not come in isolation but accompany with a package of measures, e.g. an aggressive diversification programme and non-farm activities supported by credit and other incentives. This lesson was said to be totally forgotten while launching programmes like the RSL and PRSP during 2002-2004. It was felt that while trade reforms were made, the government proceeded to implement a strategy that withdrew support to agriculture, on the ground that the type of agriculture hitherto practiced offered limited prospects for further growth and income.

Thus, on the whole, one dominant point that came from the stakeholder consultations was that there was a failure to mainstream trade policy into national development policy (the PRSP) which assigned high importance to goals such as poverty alleviation in rural areas in particular. In addition, the following points also came out clearly from the discussions.

Policy coordination - This has become very difficult due to the existence of a large number of ministries and agencies with overlapping responsibilities. The consequence of this has been felt on the failure to analyze the full range of the impacts of tariff adjustments. Trade policies typically tried to simultaneously manage the interests of producers (e.g. rice) and consumers (e.g. rice and wheat flour imports). But this does not work when there is an absence of a legally-empowered apex body with capacity to analyse impacts and to moderate adjustments.

Choice of appropriate policy instruments – Another reason for frequent policy reversals, creating uncertainty for traders and others, is inadequate homework on the choice of appropriate instruments. In a value chain context, there is a large set of potential instruments that can be used for attaining certain results, including both trade and non-trade instruments. Some problems are best addressed through non-trade instruments, while others require trade instruments, with some combination essential in other cases.

Communication failure – While changing a policy, it is not enough just to state one specific goal, often vaguely, like raising production. What is needed is also to explain the full range of the impacts expected, based on analyses and facts. If the immediate goal is higher producer price (say 20 percent higher), the communication should also say something about its impact (negative) on consumers and industry, and explain the rationale involved, as well as the timeline of the implementation (to prevent reversals). This process must also include stakeholder consultation.

3. Conclusions

The discussion on Sri Lanka's PRSP experience and the relevant policy environment points to several conditions to be satisfied if robust trade-related measures are to be mainstreamed in future exercises of national development or poverty strategies.

A new poverty alleviation strategy for Sri Lanka must be well grounded on economic realities of the particular development situation faced by it but equally importantly must receive support of the majority of population. The initial PRSP/RSL itself was donor-driven and lacked country ownership as it was not developed through a process that reached consensus and supported by a strong communication strategy. The Medium Term Development Framework that succeeded the original PRSP is based on populist ideas that show a high level of concern to the political interests, but is not well grounded on economic realities in a manner that accelerates growth in agriculture.

A process that ensures full public participation and develops widespread consensus may never be achieved as its implementation results in gainers and losers. A well informed debate on economic policy making for a number of reasons will be beyond the ability of the poor to participate, especially on trade policy that seems so remote from the villages. However, if the poor are empowered by making them clearly understand the role expected of them in the adjustment process and the safeguards put in place to cushion any negative impact that will achieve the objective of reaching consensus and understanding without expecting them to fully involve in the debate. For example, a more practical approach to garner the support of the rural poor would be to explain well to them that the limited role agriculture can serve in increasing their incomes and the implementation of the new policy involves difficult choices such as training and relocating them to new industries and sub-sectors.

But poverty impacts of trade policy must be assessed at different sub-national spheres including regional and sectoral groupings as due to its very nature affected groups are going to be aggregated in different rural regions and an impact such as a rise in unemployment will be experienced over particular regions. Prioritization of poverty pockets such as regions or sectors need to be quickly revealed from such analysis thereby facilitating introduction of rapid remedial measures.

The evidence that high economic growth is the most resolute factor leading to poverty reduction is too strong to ignore. Yet past strategies such as growth first and distribution later carry high risks for sustaining such a strategy long enough to increase the size of the growth dividend. Appropriate safety nets for the affected groups should be integrated in policy from the inception.

Safety nets decoupled from sectoral interventions must be an integral part of the reform process. Reform measures are often sidetracked by such linkages. Given the fact that poverty in Sri Lanka has remained a rural phenomenon, channelling assistance to agriculture has been treated synonymous with targeting poverty. Policy makers tend to resort to such paths for reasons of easy targeting instead of devising safety nets that are too complex to design and implement. However, it is necessary that assistance to agricultural producers affected by changing economic prospects be decoupled from programmes developed for agricultural development.

Trade policies must be informed by long term sector development strategies and kept in place for a period sufficiently long for the response to materialize. Agriculture is known for lagged supply response due to various structural impediments. Therefore, policies once introduced and assessed to be relevant should be maintained long enough for results to be visible. Sri Lanka has been observed to make too frequent changes in policies giving a very short-term character to policies to the detriment of long-term, sector-wide adjustments. There is an inconsistency between what the PRSP says and what is done in practice. For example, the THDF says that “the government will forge an agricultural trade regime built on predictable levels of tariffs to support efficient agricultural commercialization” and yet the recent years have seen one of the most frequent changes in tariffs.

As evident from the first PRSP experience and subsequent national policy making attempts, to ensure agriculture transformation and poverty alleviation, economic growth outside the agriculture sector should be sufficiently strong to create a demand-pull on labour currently engaged in agriculture. Other sector-specific policies such as those aimed at creating a conducive environment for relocation of labour outside of the agriculture will be useful but of limited effectiveness in the absence of such a pull factor. Any development strategy that aims to transform the other sectors of the economy should simultaneously address concerns of those rural masses that rely on agriculture. As observed with the first PRSP, the political influence exercised by the rural population is significantly high relative to its importance in the overall economy, thus jeopardizing any attempt that fails to address their apprehensions. This would be possible if development opportunities are extended to the rural non-farm sector and linkages between rural economies and dynamic markets elsewhere strengthened through an activist strategy.

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