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Liberalisation of the Economy —

An essay in Political Economy

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Most of the development models prescribed for the less developed countries—of which there are literally, hundreds—accept either a strong regimentation of the economy or a massive intervention on the part of the State in almost all aspects of economic activity. Except for a few economists, most of those who have written on developmental economics have implicity advocated a plethora of controls and rationing, amounting to a strong ordering of society. Perhaps the popularity of such models may have stemmed from the experience of the U.S.S.R., and the People's Republic of China in elevating themselves into World Powers of the front rank. However, the costs of such development in terms of human misery and sacrifice, in terms of the continuing deprivation of human rights and in terms of the everlooming threat of agricultural crises have apparently been ignored. Even the vast and still barely tapped natural resources of such countries have not been taken into account. Perhaps there was also a psychological factor involved in making a fetish of such developmental models in that in such models, the Economist becomes implicitly a virtual dictator.

What has been said above is meaningful in the light of the experience of Sri Lanka in its efforts at development. In the early seventies the myth was woven that Sri Lanka was a model which most less developed countries of the world should try to emulate. In fact the myth was powerful enough as to bemuse the Governor of the World Bank, for he hailed Sri Lanka's efforts at achieving economic growth whilst also ensuring increasing equality in income distribution. In fact a number of studies highlighted Sri Lanka as a model of increasing redistribution of income coupled with growth.[1]

Though there was a swelling chorus of praise for Sri Lanka in striking what was termed a fine balance between growth and income redistribution, there were economists who questioned this myth. Of course their voices were muted, perhaps even hushed. Faulty methodology used in basic research, circular thinking all led to this grand myth.

Like yesterday's fashions, these alluring ideas capture the minds of economists and then fade away into oblivion. Perhaps as Professor E. J. Mishan once pointed out, like yesterday's lovers economists write first and repent later.[2]

On top of all this we were strongly wedded to the idea of centralised planning. We had a plethora of plans our own: six year plans, ten year plans and five year plans. All of these plans plotted beautifully the path along which the economy would traverse during the planning period: targets were set both sectorally and globally and were put before the public with a maximum of fanfare and solemn oaths of dedication. These plans bring to mind what Professor Dudley Seers said once regarding what he termed Pseudo Planning:

"The basic reason why pseudo plans are produced are not always the same. Sometimes the plan is little more than an appeal for aid showing a large foreign exchange or savings "gap"....

".....a plan is a political asset— where there are elections an electoral asset.....

"Sometimes the fanfare with which a plan's targets are announced is so loud that one suspects the publication of targets has been confused with achieving them."[3]

However the very statistics which our Economists used to prove that Sri Lanka had achieved a fine balance between Income Redistribution and Economic growth also revealed evidence which proved the opposite. Thus for example the Consumer Finance Survey carried out by the Central Bank in 1963 and 1973 revealed that between 1963 and 1973, per capita consumption of rationed rice actually fell especially in the case of the lower income groups:

CHANGE IN THE PER CAPITA CONSUMPTION OF RATIONED RICE

(Measures of rice per 2 months per spending unit)

Income class (Rupees per 2 months)	1963	1973
0 — 50	13.87	5.94
51 — 100	19.30	8.48
101 — 200	14.75	10.23
201 — 400	14.55	12.28
401 — 800	12.86	12.26
801 — 1600	11.67	12.01

(*Source:* Central Bank of Ceylon, Survey of Consumer Finance 1963 & 1973)

In addition to all this, unemployment was becoming a problem of gigantic proportions topping the one million mark. And this unemployment was chronic, seemed never to end—for those who were unemployed.

It is in this context that one must look at the latest concept which has been offered as a solution for the country's ills: Liberalisation of the economy. The question which arised now is whether the term liberalisation of the economy is a cry of despair brought about by the failure of past policies or whether it is a mere positive meaningful concept.

It is a meaningful concept if one were to look at the functioning of an economy from a systems-analytic point of view. If we look at economy as a system capable of self-sustenance (within limits, of course,) then we have to look closely at the negative feedback mechanisms which are built into the economy in order that it may sustain itself. For example, shortages give rise to a rise in prices which in turn should activate the negative feedback mechanism of impelling producers to produce more of the goods concerned which in turn will alleviate the shortage and reduce prices.

Thus any meaningful planning must try not to destroy the built - in defence mechanisms in the economic system but to strengthen them and make them work more efficiently.

What has been said above is very simple economic theory but none the less often forgotten.

In fact what had happened in Sri Lanka in the past was that the built in defence mechanisms were deliberately atrophied by ill-conceived and massive intervention on the part of the State.

In fact State intervention down the decades since Independence was restrictive in the extreme, preventing the economy from functioning properly, in fact emasculating the economy. Let us take a few examples of how the economy got emasculated as a result of massive State intervention.

We have had a consumer subsidy and rationing scheme which to say the least has been counter-productive. When the consumer is given rice either free or at a grossly subsidised price, the price mechanism is so affected that the producer has to be given an incentive to produce, in the form of a guaranteed price for rice. This forces the Government to buy some minumum quantity of rice from abroad in order to meet its commitments to the consumer for which increasing amounts of foreign exchange have to be made available. This also has further effects on the economy, seriously affecting Government expenditure on the current account, causing budgetary deficits and affecting adversely the cost of living. Thus in fact despite the subsidies the consumer is not benefited for the government's desperate attempts at raising sufficient revenue causes the price levels to rise continuously, thus destroying the original aims of the subsidy schemes and or causing the government to extend the subsidies and rationing schemes in a desperate bid to curb the rising costs of living. This, in turn, gives rise to further budgetary deficits and spiralling cost of living. Here is a classic example of the opposite of the negative feed-back mechanism:- the positive feed-back mechanism where subsidies and rationing give rise to greater budgetary deficits which give rise to rising cost of living which in turn impels the government to extend the rationing and subsidy schemes which again give rise to further subsidies and so on.

In fact, even the guaranteed price scheme for rice has failed to make the country, relatively speaking, self sufficient in the production of its staple food item—rice. For despite forty years and more of the Guaranteed Price Scheme and the regular expansion of the area under cultivation and other supporting services for agriculturists, we are still sadly far away from the goal of self sufficiency in the production of rice. The reason for the Guaranteed Price Scheme, being a failure was that among other things the price under the Guaranteed Scheme was often below the actual market price or even the cost of production. For the continually widening Budget deficits and hosts of restrictions on the economy have given rise to spiralling prices. In fact, the farmer, denied the most important inputs such as a regular supply of water and cheap fertiliser does not find that the price under the Guaranteed Price Scheme gives him any incentive to increase his production.

Literally hundreds of such examples of severe restrictions of the economy could be enunciated but I think the point has been made now.

Thus all the massive interventions on the part of the State in the workings of the economy gave rise to the emasculation of the negative feed-back mechanisms of the economy and led to the operation of what has been called positive feed-back mechanisms which dragged the economy deeper and deeper into the mire.

If we look at the economy in this fashion then the term liberalisation of the economy becomes meaningful. It does not mean non-intervention on the part of the State, it does not mean Laissez Faire Capitalism; it means that the government will intervene in the economic affairs of the country in order to activate, strengthen and fortify the negative feed-back mechanisms of the economy: it means to steer the economy when necessary and not to guide it forwards by pulling at the nose rings! Thus liberalisation of the economy is not to open the doors wide for a regression to the late nineteenth century, when capitalism stood exposed red in tooth and claw, condemned by all with a social conscience.

However the transition from a restricted and cramped economy to a more liberal and buoyant economy could be painful and a phased out program would be necessary to achieve the transition to a liberalised economy peacefully. This is not mere economics but political economy for subsidies and rationing schemes did shelter and cushion the consumer from sudden shocks and left him dependent upon the subsidies and rationing schemes. The consumer could resent—no he might feel it painful—this sudden transition. This is why this article was titled "An essay in Political Economy". For from the point of view of political economy, a well thought out package deal has to be offered to the people during the transition period. This will alleviate the pains of transition whilst keeping political stability which is all important if the economy has to be set upon the road of rapid and self sustaining growth.

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