Rethinking Sri Lanka's economic crisis

Interview with Ahilan Kadirgamar on Sri Lanka's political economy in a time of great crisis.

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Over the past several months, stories about Sri Lanka's deepening economic crisis were prominent in regional and global media. Yet much of the coverage converges on the symptoms of the crisis, from the country's large foriegn-debt burden, depletion of foreign exchange reserves to challenges in meeting its energy needs. However, questions about long-term features of the country's political economy, and its connection to present difficulties, have largely been ignored. Have policy decisions of the past decades made the Sri Lankan economy more or less vulnerable to shocks, like those seen after the pandemic? How are experts and opinion-makers debating the economy in the public sphere? And what are the realistic choices for the present government?

These were some of the questions we discussed in our interview with Ahilan Kadirgamar, a political economist, Honorary Chairman of the Northern Co-operative Development Bank, and Senior Lecturer at the University of Jaffna. Kadirgamar provides a long view of the ongoing crises, describing not just the trajectory of the Sri Lankan economy and its structural features, but also the problems with current framings of the debate.

Himal Southasian: How would you characterise the economic challenges being faced by Sri Lanka today, and are there longer term trends in the country's political economy that might help us make sense of the present?

Ahilan Kadirgamar: This is by far the most devastating crisis Sri Lanka has faced since Independence in 1948. The current conjuncture is similar to the 1930s when Sri Lanka was not only pummelled by the Great Depression but also a malaria crisis leading to tremendous suffering. While the COVID-19 pandemic has led to both a medical emergency and considerable economic disruption, the ongoing economic crisis in Sri Lanka is much broader, and longer in the making than the pandemic.

The Sri Lankan economy has been crisis-prone since liberalisation in the late 1970s. It was the first country in Southasia to undergo structural adjustment and be set on a neoliberal trajectory. Those economic changes brought about by the J R Jayawardena government, locally called the 'open economy reforms', were pushed through with authoritarian power used not just for repression of minorities, but attacks on trade unions and the Left more broadly. While we remember how the Jayawardena government enacted the Prevention of Terrorism Act (PTA) in 1979 and was complicit in pogroms against the Tamil minority, we tend to forget how the trade unions were crushed by the regime in July 1980. Tens of thousands of workers were thrown out of work, free trade zones with little room for labour organising were established and the workers' movement is yet to recover to this day.

The economic bubble that began with the opening of the economy in the late 1970s, propelled by the inflow of Western capital, started to peter out by 1982. The horrifying July 1983 pogrom was an attempt by the Jayawardena regime to deflect attention from the economic downturn. Then with the onset of the civil war, neoliberal policies could not continue full steam as the state's priorities shifted to managing a war-time economy. In this context, during the dark years of the protracted 26-year-long war, global capital lost interest in Sri Lanka. It was in late 2009, with the cataclysmic end to the war and authoritarian stability imposed by the Rajapaksa regime that saw the considerable inflow of global capital albeit towards speculative ends. That dynamic was reinforced by the tremendous flow of capital to the emerging markets after the Great Financial Crisis of 2008. Sri Lanka was considered both an emerging market and a post-conflict economy, and the value of the stock market in Colombo quadrupled in the 18 months after the war.

A decade ago, I characterised these political-economic changes after the war with an authoritarian regime and their pro-market policies as the second wave of neoliberalism in Sri Lanka. It is that second wave of mounting financialisation that has thrown Sri Lanka deep into the current crisis albeit pushed over the cliff by the disruptions of the pandemic.

HSA: Public conversations on the economic crisis seem to include a wide range of issues, from agricultural policies and trade regulations, to monetary policy and foreign credit. Is it possible to separate some of the symptoms of the economic downturn from their causes?

AK: Well, the economic policy packages over the last few decades have impacted almost every sector, and the varied problems affecting different aspects of the economy have evolved over time. For example, if we take agricultural policies after liberalisation, there has been a secular decline of state investment in agriculture. Furthermore, these policies reduced the rate of growth of agricultural production, and liberalised trade in agriculture, increasing the imports of agricultural produce. Sri Lanka's macroeconomic policies have sought to take forward infrastructure development, real estate investment for tourism supported by foreign capital, but to the detriment of small-scale agriculture and self-sufficiency in food. So, we need to look at each sector such as agriculture separately, but also understand that the changes in those sectors are a consequence of the neoliberal economic policy packages.

HSA: There seems to be a general consensus that Sri Lanka's already somewhat tenuous economic position was significantly weakened by the COVID-19 pandemic. What kinds of macroeconomic and policy positions did the current government take in response to the pandemic? And what is your assessment of those responses?

AK: The government wasted valuable time even after the pressures of the COVID-19 pandemic on the economy became obvious. They kept repeating their 2019 election manifesto, 'Vistas of Prosperity and Splendour', as if nothing had changed with the pandemic and the onset of the economic crisis. This was perhaps their biggest blunder as they only seemed keen on consolidating power and pushing through what they considered an easy fix through financialisation, as with the 20th Amendment which centralised authoritarian power under the executive presidency, and the Port City Bill which aims to create a financial city on reclaimed land. By the time they tried to push through the Kotelawala National Defence University (KNDU) Bill to militarise and privatise higher education, resistance from different sections of society began mounting. It was only in late 2021 when they announced the budget for the following year that they even conceded the country was in crisis.

The people, however, recognising the crisis, started looking for other avenues to stabilise their economic situation, including through a turn towards agriculture. But that was undermined by a sudden ban on importing chemical fertilisers in early 2021. With the pandemic and the lockdowns, working people, particularly day-wage-earning households, have been devastated by dwindling income streams, and relief for people in Sri Lanka has been abysmally low even compared to other

Southasian countries.

HSA: How have economists, policy-makers and opinion-makers in the public sphere discussed and debated this crisis? Do we see polarisation along certain lines of thought that perhaps also map onto the political or ideological divisions within the country? And do you think some views get more exposure than others?

AK: There is very little substantive debate on the economy. While the government is publicly claiming it will not go for an International Monetary Fund (IMF) agreement, they are in fact exploring avenues to approach the IMF. The Opposition, particularly the Samagi Jana Balawegaya (SJB), believe the IMF is the magic bullet. Most of the political actors and even the analysts as usual are predictably invoking corruption and believe that somehow the IMF and support from China and India can solve Sri Lanka's deep crisis. However, given the scale of this crisis – and I would compare it to the time of the Great Depression of the 1930s – there needs to be a radical departure from our past policies. But that is not happening. Sri Lankan economists have become lazy, regurgitating the policy prescriptions put forward by the IMF, World Bank and other international agencies, and have lost their capacity to rise up to the challenge to address this historic crisis. The IMF may only provide a facility on the order of USD 2 billion or at most USD 3 billion, but the trade deficit in 2021 was USD 8.1 billion. Those pushing for an IMF agreement believe that will allow Sri Lanka to borrow again from the international capital markets to bridge the trade deficit until such time that tourism takes off. In reality, the cost of borrowing is going to be out of the reach of Sri Lanka, particularly as global conditions have changed, with the Federal Reserve in the United States set to raise interest rates. Furthermore, borrowing in the capital markets and rolling over debt will only prolong the debt crisis that has trapped Sri Lanka.

HSA: Recently there has been some debate on whether the use of the word 'neoliberal' accurately describes the current government's economic policies given its imposition of price controls and trade protectionism on certain fronts. How would you describe the government's economic policies – do you think it is as black and white as has been suggested?

AK: In Sri Lanka over the last few decades, there is a dearth of political economy scholarship and Marxist analysis, and thus few have engaged with theorisation of neoliberalism. In fact, some of us back in 2012 organised a three-month-long weekly seminar with younger academics and activists, to understand developments in Sri Lanka, drawing on critiques of the neoliberal project. That helped create a debate on neoliberalism in Sri Lanka. One can appreciate the value of using the framework of neoliberalism for analysing our economic context only if we see local developments in the global context. Then it becomes evident how it is all part of a massive class project of finance capital with an ideology that reifies free markets and individual agents, aggressively pushes austerity and tacitly backs an authoritarian state as long as it serves the interest of capital.

It is unfortunate that our academics and intellectuals are yet to engage rigorously with the vast literature on neoliberalism, but I also see that as a consequence of their class character, and how they are beholden to Western interests, be it donor-funded research projects or neoclassical economic analysis perpetuated in the Western academy. While this is true to an extent in many other countries in the Global South, there is some resistance to these ideas, especially during crisis times, that leads to debate on alternatives. In India for example, I follow research published on MacroScan run by the Economic Research Foundation in New Delhi that provides an alternative to conservative and mainstream positions in economics. In Sri Lanka, that is largely absent.

I would say, since the late 1970s, successive governments in Sri Lanka have been following neoliberal policy packages, and that this trend accelerated after the end of the war in 2009.

Furthermore, while there are some differences in how successive governments – or, for that matter, new finance ministers and Central Bank governors – may approach these policy packages, the thrust remains the same shaped by the neoliberal vision. The Rajapaksa regime, for instance, conceals its otherwise very market-friendly policies in rhetoric of welfarism and rural upliftment. However, when we look at their privileging of the financial sector and low investment in key public sectors, their neoliberal bias is hard to miss.

HSA: In the past several months, there has been quite a bit of coverage of the Sri Lankan economy in the international press. How reliable have you found these stories? And are there other interesting observations to be made of such coverage, particularly in light of the growing geopolitical tensions in the Indian Ocean region?

AK: My perspective all along is that international coverage has given too much importance to geopolitics with a focus on India and China, as opposed to the ground realities in Sri Lanka. It is shallow analysis on the part of the international press and think tanks, and even more so when Sri Lankan intellectuals reduce it to such a geopolitical framing. Some years ago, I highlighted that it was not so much the Chinese debt trap that we have to worry about but the sovereign debt owed to capital markets, as our external debt amounted to 10 percent and 40 percent of debt respectively to each of these sources. I argued that it was the neoliberalisation of Sri Lanka's economy with greater integration with global finance capital that would push Sri Lanka into a deeper crisis. Few paid attention at that time, but now amidst this crisis, suddenly everyone is talking about sovereign bonds.

Going back to five centuries of colonialism, Sri Lanka's economy has been shaped by geopolitical manœuvres and remained a dependent economy trodden by international trade. Therefore, changes in the global political economy have always had a tremendous impact on the island. While it is important that we see our situation amidst broader global trends, the problem is how we contextualise the analysis of the Sri Lankan economy at each point in history without just reducing it to a global story. I have seen this as a problem with sections of the Left as well, where some leftists believe taking a position on China and the United States is tantamount to solving the class problem in Sri Lanka.

HSA: Recently, ratings agencies Fitch and Standard & Poor's downgraded Sri Lanka's long-term sovereign ratings which purportedly reflects Sri Lanka's inability to maintain sufficient foreign exchange. How accurate are such assessments and how seriously should we take them? In general, what is your opinion on the politics of rating agencies, and their impact on economic policies and decisions?

AK: The rating agencies, the international financial institutions and global financiers reinforce each other, particularly during the last four decades when global finance capital is hegemonic. Rating agencies are, therefore, not neutral and wield considerable impact in terms of directing the flow of global capital. Their assertions lead to self-fulfilling prophecies. So, if the ratings go down claiming Sri Lanka cannot access sufficient foreign exchange, the bond markets will require a higher premium on Sri Lankan bonds, making it harder to access foreign loans.

HSA: Finally, what are Sri Lanka's best options to address the current economic situation? Are there ways for the government to improve the country's fiscal position while protecting those who might face poverty as a result of policies that might lean towards austerity?

AK: Sri Lanka's trade balance, with imports being 80 percent higher than exports, means that it is going to be a long time before exports catch up with imports, regardless of development policies, if the external market is left to its own devices. There is no option for the government but to restrict imports, and prioritise essential goods such as food, medicines and intermediate goods, including the fuel necessary for production, domestic consumption and exports. In order to prioritise such imports, the state needs to install a public-distribution system, where the state takes charge of imports. Otherwise, private traders who import will not prioritise, and they will continue to import luxury items if that is where there is a higher margin, as has been the case over the last two years.

President Rajapaksa's move to cut taxes soon after the elections in 2019 meant that government revenues fell to historical lows of 9 percent of the GDP. As a result, the government has not been able to provide relief to the people during this devastating crisis. Given that it is difficult to burden the public with indirect taxes, and for that matter even direct income taxes, in a time when the economy is shrinking, incomes streams are reducing and cost of living is rising, the government should implement a wealth tax and redistribute wealth for both relief to the people and for state investment to dig the economy out of the crisis, including to create demand to stimulate local production.

These are formidable times, and, if we are to borrow from global history, a situation similar to the crises of the 1920s and 1930s. Among the options before the world then were communist revolution and fascism. Amidst that crisis, John Maynard Keynes provided a very different economic approach along with a policy regime that culminated in the social welfare states, which in fact saved capitalism. The times are similar, and the question is if Sri Lankans are willing to think outside the box rather than regurgitating old platitudes about the economy? Whether we like it or not, there are going to be tremendous changes, including the emergence of radically different institutions, as with the food subsidies, free education and universal healthcare systems after the crisis of the 1930s – or for that matter, the neoliberal reconfiguration of state and society after the crisis of the 1970s.

We are already witnessing the unravelling with various quarters on the ground asserting different demands; the mounting trade unions struggles and farmers protests are telling. The future trajectory is going to depend on how working people put forward challenges and how the elite and ruling classes try to manœuvre the crisis. Over the last four decades in Sri Lanka, the excesses of the elite, including their iniquitous accumulation and conspicuous consumption have come at the cost and suffering of the working people toiling in the garment factories, in tea plantations and as migrant domestic and informal workers. But that path has reached its tipping point, and it is a class struggle hidden under the disruptions of the pandemic and simmering with the economic crisis that will determine our future.

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