



**ECONOMIC CONSEQUENCES OF THE POLICY SHIFT FROM IMPORT
RESTRICTIONS TO LIBERALISED IMPORTS**

THE CASE OF SRI LANKA

(1960 - 1984)

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I certify that the substance of this thesis has not already been submitted for any degree and is not being currently submitted for any other degree. I also certify that any help received in preparing this thesis and all sources used have been acknowledged.

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Abbreviations used in this Thesis

A E R	American Economic Review
E I	Economic International
E J	Economic Journal
I E R	International Economic Review
I S I C	International Standard of Industrial Classifications
J D E	Journal of Development Economics
J D S	Journal of Development Studies
J I E	Journal of International Economics
J P E	Journal of Political Economy
J R S S	Journal of Royal Statistical Society
O E P	Oxford Economic Papers
P D R	Pakistan Development Review
Q J E	Quarterly Journal of Economics
S I T C	Standard International Trade Classifications

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Abstract

In 1960, twelve years after independence, Sri Lanka made the first major shift in the economic strategy; import substitution industrialisation (IS), in order to transform the colonial "dualistic export-import economy".

The achievements during the IS regime were not impressive. All major indicators showed that the IS regime was incapable of solving any of the major economic problems of Sri Lanka.

Having realised the futility of pursuing further with this strategy the Government in 1977, shifted her economic strategy towards liberalisation. The immediate consequences were spectacular, unprecedentedly higher rates of growth in GDP, imports and employment were achieved. However, the progress started waning in the subsequent years.

The impact of the policy change in 1960 to IS industrialisation and the subsequent shift of policy in 1977 were analysed by using some selected indices such as contribution of IS and XP to total demand growth, Effective Tariff Rate (ETR), Domestic Resource Cost (DRC), Real Effective Exchange Rate (REER) and Bias Against Exports. A regression analysis was also made to examine the relationship between the incentive package and the growth in the manufactured exports.

Data were obtained from the Central Bank, Custom Reports and Ministry of Industries and Scientific Affairs.

During the IS regime more than half of the manufacturing sectors showed negative value added at world prices. Tariff rates and growth in manufacturing sectors did not show any correlation, but viewed through DRC fair level of "efficiency" was found among the manufacturing sectors.

Sri Lanka liberalised only domes-

tic market and imports in 1977 and the non traditional exports were placed slightly above free trade level. However, they were discriminated against as fairly high import tariffs were present, while the traditional exports were severely discriminated against by both import and export duties. The negative protective rates were not to be found after the policy reforms and "efficiency" improved marginally.

The growth impulses after the policy reforms in 1977 came from non tradables, agriculture, manufacturing and exports, recorded a relatively slower rates of growth. The pre-policy reform period (1970-77), showed an overall bias in favour of manufactured exports, but the overall bias of the system after the policy reforms in 1977 was against the manufactured exports. The Government expenditure was quite heavy creating a heavy budget deficit. The public sector was dominating in the industrial sector even after the policy reforms in 1977. These two factors undermined the policy reforms. The Real Effective Exchange Rate (REER) and manufacturing export growth showed a positive correlation.

Sri Lanka took the correct step by liberalising the imports and domestic market initially leaving the manufactured exports sector for a later period, as most of her industries were inefficient. However, inability to prevent proliferation of non tradables, the dominance of the public sector industries and the huge budget deficit undermined the whole liberalisation process.

Inordinate delay in liberalising the manufactured exports which could have carried forward the achievements of import liberalisation exacerbated the already decelerating economic growth.