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Private Sector Policy Support Unit Project, Sri Lanka

# **Developing the System of Business Service Organizations and Enhancing Policy Dialogue**

An Analysis of Selected Activities  
of the  
Private Sector Policy Support Unit, Sri Lanka

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## **ABBREVIATIONS AND ACRONYMS**

<b>BOI</b>	The Board of Investment (formerly the GCEC)
<b>BSO</b>	Business Service Organizations (Chambers of Commerce and Trade Associations)
<b>CCC</b>	The Ceylon Chamber of Commerce
<b>CISIR</b>	Ceylon Institute of Scientific and Industrial Research (now the Sri Lanka Institute of Science and Technology)
<b>CTTA</b>	Colombo Tea Traders Association
<b>EDB</b>	The Export Development Board
<b>Federation</b>	Used to refer to the Federation of Chambers of Commerce and Industry of Sri Lanka
<b>FVPPEASL</b>	Fruits and Vegetable Producers, Processors and Exporters Association of Sri Lanka
<b>GCEC</b>	Greater Colombo Economic Commission
<b>IASL</b>	Industrial Association of Sri Lanka, affiliated to the Ceylon Chamber of Commerce
<b>ISTI</b>	International Science and Technology Institute Inc.
<b>PSU</b>	Private Sector Policy Support Unit
<b>SLGTA</b>	Sri Lanka Gem Traders Association
<b>SLIST</b>	Sri Lanka Institute of Science and Technology
<b>SPA</b>	School of Public Affairs, University of Maryland, College Park
<b>USAID</b>	United States Agency for International Development (also AID)

## Executive Summary

The Private Sector Policy Support Unit was a USAID funded project in Sri Lanka. It was implemented during the period March 1990 to July 1993, by the School of Public Affairs, University of Maryland, assisted by International Science and Technology Institute Inc., the subcontractor responsible for technical assistance and local management services.

The purpose of the project was to improve the environment for private sector growth by enhancing the processes of policy dialogue. To achieve this purpose, financial grants were provided to business service organizations, chambers of commerce and business associations, to strengthen their institutions, improve their business services to members and to develop their analytical capacities. The funding also supported seminars and workshops, studies and research activities.

This study examines two important aspects of the work of the Policy Support Unit, (i) establishing new chambers of commerce in the provinces and (ii) promoting policy dialogue.

When the project began there were no chambers of commerce established and functioning outside the metropolitan region of Colombo (the commercial capital). Research conducted for the project identified many small business service organizations in the regional towns and cities. However, none of these organizations was linked to the established chambers and business associations in Colombo. Nor did any of them provide the services expected of business service organizations. These existing organizations functioned primarily as self help groups but some provided useful assistance to members, especially as savings and credit institutions. This base needed to be strengthened substantially in order to support the growth and development of the regional private sector.

Enhanced provincial or regional business service organizations would be able to make use of the new opportunities to discuss policies and programs with the regional administration and the recently established provincial councils. The services which small enterprises require, especially information to function efficiently, is provided in some measure by the public sector. However, this project found that the conditions were right for the private sector to organize and provide business services for itself. New chambers of commerce, if properly supported, would be able to provide a range of services which help business to be efficient and productive. As an important result, these chambers would be drawn into the regional economic policy arena.

The Private Sector Policy Support Unit was instrumental in establishing three new chambers of commerce. They were built on the base of existing associations and groups of business persons. It is quite likely that they will grow and strengthen organizationally as they have started with better defined objectives and are functionally linked to the main chambers and business organizations in the country. Several lessons were drawn from this experience. They indicate possible programs to further strengthen the system of business services and representational support for enterprises outside the metropolitan area.

The second activity that is examined in this study is the promotion of policy dialogue. The project sponsored a variety of activities which were designed to strengthen the process and content of policy dialogue. Sri Lanka is in the process of liberalizing its economy and providing more scope and space for the private sector to operate. Mechanisms for dialogue on the necessary policies were found to be not well developed. There were strong preconceptions in the minds of policy makers about the role that the



private sector ought to play. The private sector made important contributions to policy, especially on industry specific issues, through business service organizations. However, there were equally important issues which were relatively neglected. Some issues were contentious within the business community. Existing policies such as those on the exchange rate and special concessions benefitted some business groups and not others. A common position was not easy to develop. However, at the same time even within sectors or industry groups, systems for developing consensus on policies for medium term growth were absent. Short term concerns and protecting concessions dominated the positions taken by the private sector in its discussions with the public sector. The Policy Support Unit determined that medium term perspectives or strategies for a few selected sectors, prepared by the private sector would establish a platform for a new regime of policy dialogue.

For the first time, private sector groups with assistance from the project, prepared private sector perspectives and strategies for the development of specific sectors. Industry agendas were prepared for Tea, the leading export sector, Gem and Jewelry Sector, Fruits and Vegetable sector, and for manufacturing industry. The leading business associations in these respective sectors organized the studies with assistance from consultants. This showed how business service organizations can participate in the policy dialogue in an effective manner.

# Chapter 1

## Summary and Conclusions

### (a) Introduction

This study analyses two aspects of the work of the Private Sector Policy Support Unit (PSU), a USAID funded project in Sri Lanka. They are, (i) developing chambers of commerce in the provinces and (ii) promoting policy dialogue.

The project was implemented from March 1990 to the end of July 1993, by a cooperative agreement with the School of Public Affairs, University of Maryland (SPA/UMCP), assisted by International Science and technology Institute Inc. (ISTI) in the capacity of subcontractor responsible for technical assistance and local management services. The purpose of the project was to improve the environment for private sector growth by enhancing the processes of policy dialogue. This was to be achieved by providing grant finance to business service organizations (BSOs) - chambers of commerce and trade associations.

Research and analysis to plan the project and develop its activities identified interventions by BSOs that were most likely to achieve the project purpose. Activities to enhance policy dialogue had to be designed within the specific development context of the country, the prevailing government policy and the capacity of the BSOs to carry out various functions. The planned output included; (i) analytical activities that related to policies that the BSOs had researched and analyzed, (ii) seminars, workshops and other dissemination activities organized by the BSOs as part of the dialogue process and (iii) workshops and seminars provided by the PSU.

Previous studies commissioned by USAID to examine ways to develop the private sector had identified the main constraints and opportunities for intervention. The relative lack of discussion on common development goals between government and business groups was noted and the need for "strategic partnership" was stressed (Arthur D. Little Inc., 1983). Another study for USAID that was intended to formulate the PSU project, examined past policy research and analysis, and made an assessment of the capacities of a representative group of BSOs. That study found considerable scope for improvement (ISTI, 1988). The experience of the PSU confirms and adds to the previous base of information in this sphere.

The most important aspect of the project was the opportunity to examine and understand the role and contribution of BSOs to the development of private enterprise. Public officials and policy makers as well as the business community had many misconceptions about the role and effectiveness of BSOs. Often, representation and advocacy of business interests were viewed as narrow and detrimental to public welfare. When the BSOs are viewed primarily as advocacy groups and especially when they are considered to be only self serving, important opportunities to develop the private sector are missed. The BSOs form an important part of a "feed-back" system for policy making. They examine and review policies that affect business and convey the needs and views of business to the government and to policy makers.

BSOs "connect" enterprises to the business context and have a close understanding of the practical issues of business. This is vital knowledge for effective policy making and can be used by government. Services

to members, including useful commercial and market information, link businesses together through the BSOs. Good services strengthen the BSOs and increase their importance in the process of policy making. Such services are therefore critical to BSO development. The content of policy dialogue on private sector development can be built from the specific cases. BSOs have a good opportunity to pursue this endeavor. The Ministry of Industries, Science and Technology, convinced of the importance of BSOs and their role in national economic development on the basis of the experience in many developed and rapidly developing countries, is examining measures to extend the system. Discussions to mandate membership in BSOs, as in Germany, had been held. New and small BSOs supported the measure. They anticipated an expansion in membership and of their role in the system. The success of BSOs depends on their service capacity. Forcing membership on businesses without ensuring that BSOs provide adequate services is likely to weaken rather than strengthen the system.

The BSOs are established and maintained with considerable enterprise. Many BSOs, especially the smaller ones, view themselves primarily as lobbying groups. This role is important and requires ingenuity and skills in negotiation. However, similar efforts by BSOs are necessary to identify and provide other services to their members efficiently in order to improve business performance. BSOs themselves do not generally give adequate attention to their role as enterprises producing services efficiently. The services they offer have to be useful to business and must be improved and modified periodically to meet changing demand. Organizing basic services in commercial and trade information requires a different type of effort. A formal office is definitely needed. Besides, activities have to be planned and produced with adequate consideration for their effects on the revenue base of the BSO.

Business information for a particular sector is not easy to generate. The larger firms can bear the expense. But many others cannot devote resources for this purpose. Search costs are generally high. The cost to an individual business would be considerably lower when resources are pooled. The BSOs have an important role to play in developing the private sector by functioning as enterprising producers of business services. This includes linking with public sector agencies which produce data and information, interacting with them, and transmitting the needs of business back to them. Through the BSOs, a wide range of opportunities exist for the private sector to enter into strategic partnerships which increase the efficiency and lower the costs of public agencies and improve the performance of business.

Larger businesses had membership in more than one BSOs. Service capacity was concentrated among a few large BSOs. The structure of this "market" for business service was not fully competitive. Smaller BSOs were not quite clear about their role and function and tended to view themselves as "social service" organizations and considerable improvement in awareness was necessary. The BSO system needed improvement. Many existing BSOs did not function as efficiently as they could. The organizations needed strengthening and their activities had to be improved. When they functioned well, and there were a few good examples of it, the BSOs were also efficient producers of services to business other than representation and advocacy. However, many BSOs were volunteer organizations and lacked the characteristics of enterprise disciplined by the market.

The study is organized in the following way. Chapter 1 is the Summary and Conclusions. Chapter 2 is the introduction and approach of the study. It also contains a brief overview of the BSO system. Chapter 3, Developing Chambers of Commerce in the Provinces, examines the work of the PSU related to establishing new chambers of commerce in the provinces. This study does not deal with the large body of work undertaken by the PSU to strengthen existing BSOs. Chapter 4, Promoting Policy Dialogue, discusses selected cases of PSU assisted activities that resulted in BSOs preparing sectoral and industry agenda. Appendix A, Establishing New Chambers, is related to Chapter 3 and contains working papers

and notes which were prepared to assist the formation of new chambers. Appendix B, Preparing for Policy Dialogue, relates to Chapter 4 and contains notes and short papers presented to BSOs to initiate activities leading to policy dialogue, examples of analytical papers prepared by the PSU for BSOs and two discussion papers prepared by the PSU on issues related to policy dialogue and private sector development.

## **(b) Initial Findings of the Project**

### **(i) The Role of BSOs**

- BSOs in Sri Lanka have varying capacities, professional competence and membership bases.
- They provide a range of useful services which tend to reduce transactions costs for business by providing information about regulations and procedures, trade opportunities, and business links abroad. They also develop internal discipline among the members and assist in resolving commercial disputes through arbitration.
- A few BSOs are managed by a professional staff which also produce member services and provide the background work for representational activities. Elected councils perform executive functions and set the agenda for the BSOs. However, with a few notable exceptions, most BSOs are volunteer organizations with few member services. The activities depend on the initiative of the elected councils. As a result, there are fluctuations in the types and levels of activities. These BSOs are dominated by short term perspectives and concerns. The quality of the leadership plays the major role in determining the agenda for the activities of these BSOs and the positions they take on government policy.
- A fully capable and functioning system of BSOs does not exist. Although an apex organization, the Federation of Chambers of Commerce, exists, it is not yet capable of performing the apex role and winning the confidence of its constituent members.
- Most of the BSOs represent the interests of members to some level of government or public agency. The consultative process has not developed adequately to discuss economic policies to increase the scope for private economic activity and its efficiency.
- Representations on procedures or to maintain existing fiscal incentives to particular business groups, dominate over many important macro economic policy issues.

### **(ii) Representation and Weaknesses in the Processes.**

- The BSO structure is fragmented and dispersed with duplication of effort and seeming mis-allocation of resources. There is scope for specialization and for developing complementary in activities among BSOs.
- Although *a priori* reasoning indicates a wide range of issues on which business could take common positions, there are no automatic processes to create them.
- Business interests are represented through many channels. Individual businesses invoke direct

access to political machinery, policy makers and public sector agencies to protect or obtain special advantages. They also transmit their positions through BSOs. In many instances "by-pass" mechanisms, directly accessing politicians, have developed and weakened the process of policy dialogue. The demonstration effect of invoking political patronage spreads in the business community, weakening the willingness to carry out the research and analysis that is needed to support representations and policy dialogue.

- Invoking political channels for representation of individual gain has resulted in a large area of macro-economic policy and reforms being left relatively unexamined within the business community. The BSOs have not developed capacities to discuss and evaluate macro-economic management and related policies, those concerning public expenditure and investment especially on infrastructure, the government budget, welfare programs which affect the rural economy and the poor, or education and training.
- In many important ways, the private sector places itself in a position to be led by the government. It does not wish to draw too much attention to itself when it is successful and continues to be wary of government intentions.
- Policy makers are quick to point out the narrow self interest of the business community and its relatively short term perspectives in discussion of policy reform. There were many misconceptions and misinterpretations about the role and value of BSOs in the minds of the policy makers resulting in their potential contribution to policy making being discounted.

### **(c) Elements of the Strategy for PSU Activities**

In trying to improve the process of policy dialogue, the strategy of the PSU began with activities to strengthen the organizations and their professional capacity. The PSU concluded that:

- The BSOs are most likely to succeed in entering into partnerships with the public sector to promote enterprise development and growth if they are strong and viable organizations.
- They are most likely to be accepted into the policy making arena as important organizations if they provide useful and efficient services to members.
- They can undertake a wide range of activities related to commercial and business information. This includes information about the domestic business environment, procedures and regulations, and economic trends. It also includes information on costs of business, (e.g. wages in particular trades or occupations, infrastructure costs, credit and costs of funds). In addition, it includes information about competitor countries, foreign markets and trade opportunities.
- BSOs can be more effective if their representation is based on a strong and well serviced membership, knowledge of members' business problems and analysis to develop and expand business opportunities.

The project was implemented immediately after the most difficult and violent periods in the modern history of the country. The war in the north and east resumed soon after the project began and continued thereafter, making substantial demands on national resources, disrupting civil and commercial activities

in a large part of the country and imposing costs on the private sector. Uncertainty in the political arena constrained policy making and important liberalization measures proceeded slowly and cautiously.

Economic liberalization and related restructuring started in 1977 and created new opportunities for the private sector. One of the main objectives of successive governments since then has been to create more economic space for private enterprise. There is a strong emphasis on growth and on dismantling the controls that pervaded the system. However, past policies related to import substitution, subsidies and administered pricing had conditioned private enterprise as well as consumers and created dependencies that were not easily shed. The influence of the public sector had been pervasive and quick changes are difficult and costly.

Some features of this period which affected private enterprise adversely were:

- The private sector had survived and adapted to a system of controls and administered markets during the period 1970-77. Very high protection helped a relatively small manufacturing base. The export oriented commodity sector was heavily taxed.
- Regulations introduced during this time constrained entrepreneurial activity and the performance and growth of the private sector. The business acquisition act, the nationalization of foreign owned enterprises, and the creation of new public sector ventures in production and distribution had considerably restricted the role of the private sector.
- A ceiling on housing and property ownership had transferred a very large part of private assets to state hands. A limit on the extent of land ownership had been imposed and a land reform measure undertaken, with mixed results.

These and other policies conditioned the private sector to be cautious.

#### **(d) Extending the BSO Structure - Establishing New BSOs**

One component of the study analyses the work done by the PSU to form regional BSOs. Early in the project, the PSU determined that the institutional infrastructure for private enterprise in the rural sector was underdeveloped and that effective BSOs were needed. Small enterprises, located in towns and cities had no private sector service organizations to obtain the information needed by them to carry on and improve their businesses and to learn about the business environment. Public sector agencies, such as the Industrial Development Board, and offices of government ministries and public sector banks, provided some of the commercial services required by enterprises. Much more can be done to improve these services and their delivery. The BSOs could play an important role as intermediaries in this process.

Research commissioned by the PSU in a few towns uncovered a wide range of small BSOs. Most of them were volunteer organizations performing some representation functions and providing financial services to members. With resources and assistance, some of them seemed likely to graduate to a higher level of useful and effective service. After 1989, a large number of new local level BSOs had been formed with a substantial membership. This pattern was expected to prevail at other locations as well.

The PSU observed that:

- The formal BSOs were concentrated in Colombo, with very little if any outreach to the provinces.
- Business activities were growing in the provinces and new enterprises were emerging, but they depended primarily on service provided by the public sector.
- Some "support systems" had been built by the private sector, but there were very few "professional" BSOs - organizations which were service producers with hired staff at the executive level.
- Most BSOs were small. Most did not have formal offices and did not employ professional staff. Most of them functioned in towns. Almost every built up commercial area had a small association of traders or businessmen to protect their interests. They represented member interests to local governments and public sector agencies and were mutual self-help groups providing credit or operating revolving credit clubs. They had no links or only very weak ones with national level BSOs.
- Many BSOs collected money and performed social services during religious festivals. Most depended on the volunteer effort of members.
- The services available in the provinces were inadequate. They were insufficient to enable small and emerging enterprises to function and grow within a liberalizing economic environment. Commercial information was largely unavailable. A different type of organization providing basic services was necessary.
- The Industrial Promotion bill aimed to set up consultative mechanisms including Regional Industry Service Committees to advise the chief minister of the Provincial Councils on industrial development and to set up Regional Industrial Service Centers. The time was opportune for organizing business interests into chambers of commerce or associations to complement these public sector initiatives.
- Building on the existing base of local organizations offered the best opportunity for success. National BSOs had the capability to provide the regional BSOs with information and to train and improve the skills of the BSO officials.

Three new regional chambers of commerce were set up with PSU assistance. In addition, assistance was provided to strengthen an existing, large and well organized trade association in the southern province. The main observations and findings from this activity were:

- Strong support and assistance was available from senior public officials and elected officials in the respective provinces to establish the new chambers. These new organizations soon developed or strengthened their links with regional public sector organizations. A systematic process of consultation on regional private sector growth and resolution of procedural bottlenecks quickly emerged.
- Assistance was necessary to define the goals and to identify activities for the new organizations. Awareness of the responsibilities of the elected members and the fiscal implications of planned

activities was a critical need and had to be developed.

- When a private sector organization of this type was established where none existed, it became an important resource base. It attracted other services and resources. Furthermore, public sector agencies quickly sought to employ it as a vehicle for implementing their programs. This offered new opportunities for business groups to discuss local and regional issues and policies concerning business.
- Wide scope exists to promote awareness about the possible roles and functions of BSOs among the members and officials of the existing BSOs, especially those depending on volunteer effort. The regional BSOs that were established share many features with other national level BSOs. A heavy responsibility rests on the leadership. They need very quickly to develop capacities for internal democracy and consensual decision making.
- The decision to devote resources to establish a professional office is an important first step to produce member services, attract members and consolidate the BSO and put them on a path of rapid growth.
- The continuity of the BSOs would depend on how well they are able to identify member needs and provide useful services to business. These services include the production of directories of members and their capabilities. They also include provision of information about the local context for business, government regulations, procedures, programs and services to business, as well as market opportunities, all of which can be done at relatively low cost.
- As the regional BSOs grow they are well placed to take over some of the service delivery functions of public agencies. During the relatively short time they have existed, public agencies have used the new BSOs as a vehicle to reach the regional business community to provide information about government programs, as a forum to examine opportunities for regional development and as an instrument for assisting the business community with services.
- Training, building professional capacity, and establishing rules and codes of conduct are very important inputs to stabilize and enhance the regional BSO system. They have to be encouraged and must see self interest in networking with national BSOs as well as other regional BSOs. Consolidating the system can have a major impact on the level of service, costs of information and enterprise operation in the regions.

#### **(e) Enhancing Policy Dialogue**

At the start of the project the PSU determined that there were different channels to develop and enhance the process of policy dialogue. Some sectors of the economy which faced pressing issues as well as opportunities for rapid development, created favorable conditions for partnership between business and the public sector to develop economic strategies. The Gem and Jewelry sector had high export potential and abundant natural resources. It could have a strong positive impact on employment. The Tea sector which was the country's most important export earner, was declining in productivity and competitiveness. Structural changes were underway in the industry, but the private sector had to assess its role critically. Fruits and vegetables had high export potential and offered good prospects of improving the income of small holder producers in the rural sector. Manufacturing was growing fast, but was a relatively small



sector. A strategic vision developed by the private sector for each of these industries was very likely to become a platform for discussions on policy. These efforts would then demonstrate the possibilities for dialogue within the system. It was felt that developing a strategic perspective for each industry or group would provide a basic mechanism to bring the businesses in that industry or group together to focus on future possibilities and what they had to do to realize them. Meanwhile other specific opportunities were also expected to emerge and the PSU felt that the BSOs would then be able to develop activities leading to greater dialogue with the authorities.

The PSU made the following assumptions in carrying out its work:

- There is a strong likelihood of a beneficial demonstration effect from fruitful policy dialogue based on careful analysis and research.
- Strategic concerns identified by research and discussion with private sector leaders, BSOs and the business community, would lead to important policy measures.
- Strong competition would exist among business groups to determine the agenda for representation and discussions with the government or the public sector but this could be managed.
- Strategies to develop selected sectors would have an important impact on the BSOs which organized the work and their members. They would generate awareness of the prospects and possibilities for each sector, provide a perspective of the opportunities that could be seized, and indicate what action by the business community was required to realize that potential.
- Analytical activities create platforms for discussion to examine opportunities for partnership with public sector agencies and make it possible to move away from bargaining stances aimed at extracting privileges from the government.

Considerable effort was required to bring the groups of businesses together into BSOs. Assistance was needed for the purpose. The PSU provided such assistance to develop, organize and execute BSO activities. These activities demonstrated that:

- Long term views, generally considered to be absent among most businessmen, can be generated if cast in terms of a perspective of the future for business in a sector or area of activity, and if attention is focussed on their role in improving productivity and winning and sustaining new markets, especially export markets.

## **(f) Conclusions**

The activities of the PSU highlight the flexibility of the USAID project in responding to a range of needs which were identified during implementation. The project was designed to make possible quick responses and adjustments to the emerging needs of a wide range of organizations. The initiatives of the PSU demonstrate that direct participation in the activities of the BSOs is most likely to improve their performance and policy related activities. Whatever was suggested had to be put into operation. Besides, a demonstration product or service was necessary to begin discussions on carrying out specific activities.

The PSU established new chambers and in the process gathered useful knowledge about how the effort can be replicated. From the experience of the specific activities that were undertaken to establish new BSOs, it was seen that the following general steps need to be taken:

- Identify networks and organizations of business.
- Form an initiating group or core group of businessmen to pursue the formation of a BSO.
- Discuss the need for a formal organization and the implications of establishing and operating one.
- Establish a professional office quickly.
- Stress formalization, a constitution, registration, and rules and regulations of conduct.
- Develop services to members. Identify a few key services to attract and keep members and link each with its fiscal implications.
- Establish links and networks with public sector agencies and programs for private enterprise in the region in collaboration with national level BSOs and with the regional universities. This helps the new organization overcome initial resource constraints.
- Stress the need for inclusive membership to represent all the main economic activities of the region.
- Develop training programs for the new BSO management and professional staff with existing national BSOs.

The faster a new BSO is able to establish a professional office and network with other BSOs, the quicker it will be able to focus on member services to improve and enhance the private sector. This will also enable it to move away from social service activities and from an orientation towards being an all purpose development NGO.

Important organizations that work with the regional private sector such as banks, insurance companies, and management and accounting firms are vital resources during formation of the BSO. They help to identify the needs of the business community and quickly use the new BSO as a forum to discuss important business related issues. Similarly, the public sector is also quick to utilize the new BSO to discuss programs and projects in the region. Considerable publicity and good will is obtained rapidly in the process. However, this by itself tends to weaken the new BSO. It will benefit from the publicity only if it develops additional services to assist businesses.

Research and analytical capabilities had to be developed within the context of specific organizations. Although research units with competent staff are needed and will perform very useful functions, awareness of the need has to be built up within the BSOs. This will be a lengthy process. Even when grant funds were available, the BSOs were not able to obtain the necessary staff quickly.

New ideas and advice to improve their activities had to be "marketed" to the BSOs. This required working with the problems that the BSOs or member groups had identified. The PSU had limited capacity to assist BSOs with their research needs. A network of other agencies and individuals had to be built up.

This included the Institute of Policy Studies, a quasi public sector organization, the faculties of business and economics in the university system and private research institutes and consultants. The BSOs had mixed reactions towards the research and academic community. The links with them were not strong and there was hesitation on both sides about working together. The PSU developed networks by bringing in researchers and research agencies to work on specific activities. The PSU participated in discussions which brought both sides together.

The PSU worked closely with analysts and researchers who assisted BSOs with policy related activities funded by the PSU. Intermediation by the PSU was an important step in the learning process for the BSOs as well as the analysts. The industry agenda and strategies prepared by the BSOs and discussed in this paper were developed with the close collaboration and participation of the PSU.

The grant activities with policy content or policy implications that were undertaken included studies and analyses:

- Sector specific issues faced by the membership of a BSO.
- General economic issues related to credit, existing incentive programs and changes in them
- Macro economic issues which affect the environment for business.

The project demonstrates that BSOs can and will be involved in all three categories of activities. They have been slow to invest their resources in acquiring capacities for analytical work on the broader issues. The benefits from such action are perceived to be indirect and unclear. However, the private sector can and should, regularly review and comment on government macro economic policy and performance and examine the implications for business investment, productivity and competitiveness. This activity can be enhanced with mechanisms to link the BSOs with the research community. Quite often, the BSOs and the private sector have little interest in the macro economic issues that affect business. A regular calendar of activity related to regular events such as the national budget, the public investment plan and the review of economic performance can be developed. The Federation of Chambers and the Ceylon Chamber of Commerce are interested in pursuing programs which improve awareness and understanding of macro economic policies and the constraints under which government has to manage the economy.

## Chapter 2

### Introduction

#### (a) Scope

This study examines selected aspects of the work undertaken by the Private Sector Policy Support Unit (PSU) project in Sri Lanka. The project was designed to "strengthen the contribution of the private sector to the formulation, appraisal and implementation of market oriented economic policies" (Project Grant Agreement, Annex I, Private Sector Policy Support, Amplified Project Description, A.I.D. Project No. 383-0100 July 29, 1988.). It was one of three USAID projects to assist the government of Sri Lanka to "increase employment and incomes by the creation of a policy environment conducive to private sector growth". The other components aimed to provide assistance to (i) the Presidential Commission on Privatization, (ii) the Securities Council (now the Securities and Exchange Commission) and (iii) the Colombo Securities Exchange and a venture capital company.

"The objective of this cooperative agreement is to improve the contribution of the private sector institutions to market oriented economic policy formulation and implementation, through better capabilities in formulating and appraising economic policies". The Cooperative Agreement between USAID and SPA/UMCP.

The PSU functioned through a cooperative agreement with the School of Public Affairs, University of Maryland and was expected to provide assistance to chambers of commerce and trade associations in the form of financial grants and technical assistance to strengthen their institutional capacities. The strategy for the PSU activities was developed after initial research and enquiry. It was discussed at the project planning meeting held during July 31 - August 1, 1990. The findings were presented to a group including representatives from USAID, SPA/UMCP, ISTI, private sector leaders, professional staff of leading chambers and associations and policy makers. The PSU noted that Business Service Organizations (BSO's) were not ineffective and provided a range of useful services to members. However, there was considerable overlapping between their activities. As a result, the structure was fragmented and tended to make the organizations less effective (see section (c) below). This imposed significant constraints on the ability of BSOs to access the policy arena and engage in dialogue. Strong preconceptions about the limits on effective policy dialogue remained within political institutions as well as the public and private sectors. Adverse past experience in this connection has tended to dominate current processes. However, changes are taking place as the need for dialogue is perceived. As a result, new mechanisms for policy dialogue are emerging.

The approach of the project and the activities it undertook were based on the premise that **BSOs need to be efficient providers of services and to have strong functional links with their members before they can be effective in policy dialogue.** Policy makers and political managers tend to demand representational strength of those agents seeking policy changes. Therefore, BSOs, both individually and as a group, need to ensure improvement in this respect.

The work of the project involved many different elements. The grant process, which facilitated the project activities, had to be built up and the portfolio developed, the content of the grants had to be carefully framed, the needs of the recipients had to be anticipated and services provided to them to carry out their

activities. The PSU was the executive arm of the project and had a small office with two senior full time professionals, supported by part time technical assistance and by support staff.

### **(b) Approach**

"Ideas won by our intelligence, embodied in our outlook and forged in our conscience, are chains from which we cannot tear ourselves without breaking our hearts; they are demons we can overcome only by submitting to them". Karl Marx

"The ideas of economists and political philosophers, both when they are right and when they are wrong, are more powerful than is commonly understood. Indeed, the world is ruled by little else. Practical men who believe themselves to be quite exempt from any intellectual influences, are usually the slaves of some defunct economist. ... I am sure that the power of vested interests is vastly exaggerated compared with the encroachment of ideas".

John Maynard Keynes.

Chambers of commerce and business associations have not been the subject of close examination and analysis in the development literature. They have not been included among the organizations that are considered to be important and useful for economic activities. Some producer organizations have received attention in analytical work, especially farmers' organizations and those which utilize publicly held resources. These organizations have been treated as important instruments as well as subjects of public policy. Development programs have established and nurtured these organizations. However organizations like BSOs have been generally ignored. As a result, vital opportunities to develop enterprises have been missed. One important reason for this gap has been the way development policy has sought to identify points of intervention and improvement. It has treated business organizations as narrowly concerned with their own self interest and as being able to manage without outside assistance. However, the real position is different. What BSOs do is important to the performance of the private sector. What they can do requires more attention of analysts and policy makers who seek to promote private enterprise in developing countries. During recent years there has been a shift in donor attention towards NGOs but this has largely ignored organizations which service other enterprises. Important opportunities to assist small enterprises are missed because the role that these service organizations can play is not taken into consideration.

Policies for economic development are often based on theoretical foundations. However, technically correct policies are not readily accepted by governments nor easily implemented. One major reason is the difference between the assumptions that are made about the problem and its context by the proponents of policy and the reality within which the policy has to be implemented. Political factors and interest groups interact with the implementation process and modify the content and change the expected outcomes of policy.

Good analysis is essential to policy making. However, the agencies entrusted to carry them out have their own needs and demands. Increasing attention is paid by development agencies and analysts to the processes of policy formulation and mechanisms to build consensus (See for example, Meier Ed. 1991). Governments resist or are slow to adopt some policies which are technically sound because these policies

do not explicitly take into account the important features of the context, including political imperatives.

Policy dialogue is an important aspect of development assistance. Donors agencies promote policies which are expected to liberalize economies, expand trade and exports, and increase macro economic efficiency. For these policies to succeed, it is necessary to manage the interests of governments and of ruling political groups within them as well as the effects of these policies on vulnerable groups.

Understanding of the importance of political processes in policy making has grown with the effort to promote development, especially with the experience of donors and international lending agencies. Studies and reports prepared to support policy recommendations are criticized by host country governments because they offer advice that is unrealistic to implement. A World Bank report examining its relationship with Sri Lanka found many reasons for negative government reactions to policy advice. Studies sometimes offered ideal situation solutions without considering practical needs, indicating a lack of understanding of the processes that precede policy reforms. (World Bank 1987).

"The reaction of Sri Lankan officials to the Bank's economic and sector work has been striking: only three sector reports were singled out as having been very useful. The government sees general economic reports as serving a limited purpose since their recommendations, useful as they may be to donors at Aid Group meetings, are too general to be of much use to Sri Lankan officials. The lesson is that the Bank's most constructive contribution is to help with the practical problems of implementing policy changes, rather than providing theoretical textbook solutions".  
(The World Bank 1987)

This study considers a few elements of the rich literature on development issues related to the processes of policy making in developing countries. Themes from the economic literature are considered in terms of their impact on institutions and policy making. Institutions are viewed broadly as in the literature of the new institutional economics, to include rules and regulations that govern economic behavior and the organizations which develop, implement and monitor them. The study attempts to place BSOs within this context as organizations which provide the institutional infrastructure for private enterprise.

The recent writings in institutional economics provide very useful analytical tools which are important for this exercise. Specifically, the concepts of transactions and information costs and how they affect economic decisions are considered. The BSOs are viewed as organizations for collective action to improve the context for business by accessing decision making agencies and providing other business services. This includes the way in which they interact in the policy arena with governments and policy making bodies. BSOs can affect the context for business positively by imposing internal discipline, creating opportunities for collective action, and by providing services which reduce costs for business with timely commercial information. This aspect of BSOs is often neglected and overshadowed by what they do to represent the interests of businesses to policy makers and governments.

Important insights to the behavior of BSOs are obtained when the economic concepts of information are applied to them. Increasing attention is paid in theoretical economics to the costs of producing, obtaining and processing information for businesses and for other economic agents. These concepts modify the general framework of mainstream economics which had not focussed attention on these specific issues (see for example, Arrow, 1974; Marshall, 1974). The efficient performance of producers and markets is contingent on the system of information for appropriate decision making. Information has to be

produced like other services. Organizations which are able to assess the needs of businesses can efficiently produce the information that is needed. The BSOs have the potential to do this. The public sector has been a dominant producer of these services in many countries. However, additional inputs are often necessary to make the information flowing from the public sector truly useful to businesses.

Activities that were undertaken by the project are examined in terms of their impact on policy making processes. The development of BSOs, especially where such formal organizations did not exist, is examined as part of the process of developing private enterprise in the country, particularly in areas outside Colombo, the commercial capital of Sri Lanka.

The project viewed opportunities for future action and interventions to improve and widen the participation of the private sector in the process of policy dialogue from the perspective of how enterprises are able to organize for collective action through BSOs and what the BSOs can do to improve the climate for business. The project adopted an activist approach. It took special note of points of intervention which were likely to strengthen and smoothen the policy dialogue.

BSOs are not only organizations for collective action and advocacy but for production of highly useful business services. They have special advantages in producing these services. These advantages include access to policy making. Business services, including the provision of information for productive enterprises, must be generated efficiently. More attention needs to be paid to these aspects of BSOs.

### **(c) The Existing Structure of BSOs**

The system of organizations servicing private enterprise in Sri Lanka is fragmented and dispersed. However, there is a structure with federations at the apex, chambers as their members, and associations affiliated to the chambers. There is considerable scope for reorganizing, strengthening and developing this structure for more efficient and effective services. Many chambers and associations provide similar services to a relatively small clientele. The largest of the organizations, the Ceylon Chamber of Commerce, is the oldest and best organized. Many other organizations have been set up in competition or to provide for specific needs.

Many of the functions of an apex institution are performed by the Ceylon Chamber. Many product and sector specific associations are affiliated to it. Although it does not belong to the Federation of Chambers now, thus weakening the structure of representation, it is likely that it will do so in the near future. Many chambers retain the characteristics of associations and volunteer bodies, without adequate professional staff.

The interests of private enterprise located outside Colombo are still inadequately represented to the local, regional and national level public sector agencies. There have been many attempts to form institutions that support the needs of regional and local businesses. The All Ceylon Trade Chamber, which established branches in many towns around the country, did not provide regular services to members. The shell or design for activity and representation existed without the capacity needed to carry out the necessary functions.

In towns across the country, traders and businesses have formed associations. They are active in seeking benefits for their membership. They do not function as service organizations of and for business. They do, however, discuss issues that relate to the costs of business operations with the local government as

they arise. The primary function of these organizations is self help or mutual assistance; they operate revolving credit clubs, provide social services to the community during festivals, and assist members in distress with finance. Organizations with these functions are widespread and form a possible base that can be upgraded.

A functional hierarchy of representation of business interests is yet to be established. A structure where regional associations belong to national organizations, trade and sector associations belong to chambers, and chambers to federations of chambers is not properly established. Whatever exists is quite rudimentary and weak in structure. Large businesses irrespective of location are most likely to seek membership in the national level chambers located in Colombo.

The different levels of elected office and bodies of public administration have not yet been matched with private sector business organizations with the capacity to address issues that can be represented at those levels. This articulation needs considerable strengthening. The process of building a strong articulated or inter-connected system can begin simultaneously at many different points. There is wide scope for improving the services for private business at the regional and sub-national level. At the national level there is considerable scope for integration as well as specialization.

The present structure of BSOs has the following elements:

- A weak apex institution for the chambers, the federation.
- A relatively new set of institutions for the export sector - the exporter associations with a federation.
- A few well organized goal directed institutions with a clear member service orientation.
- Fragmentation of services and representation as a result of many chambers in the same field.
- Many BSOs that were established to provide greater opportunity for "leadership" or an "organization of our own" to a group of business persons and struggling to provide services to members.
- Organizations with a bias towards modern, urban based companies.
- Weak fiscal bases for many of the relatively recent BSOs.
- The representation of regional or rural business interests not well articulated within the present system.

The functional base of BSOs consists of the associations and organizations which belong to the Federation of Chambers of Commerce and Industry, the Ceylon Chamber, the Federation of Exporters and the National Exporters Association.

BSOs can be classified into those that are linked to a hierarchy and those which are not.

(1) Linked Organizations.

Federations consist of chambers and associations, e.g. The Federation of Chambers of Commerce



and Industry and the Federation of Exporters. The National Exporters Association has both individual businesses as well as a few associations in its membership.

The All Ceylon Trade Chamber "registered" trader's associations in towns across the country. The activity level of the local associations was highly varied. The central organization did not provide useful business services to its members. A majority of the member organizations were inactive.

The Federation of Chambers is at the Apex but has inadequate capacity at present to carry out the necessary functions. It does not contain the Ceylon Chamber which functions separately as an Apex organization. The Federation also has associations as members.

At the next level, there are chambers which have both individual members as well as associations. The Ceylon Chamber is the most important chamber of this type.

## (2) The Unlinked Organizations.

This group contains a large number of local level BSOs which are not members of chambers. They have varying degrees of formality and provide a variety of services to members. Usually, they have strong mutual assistance or self-help functions and collect funds for members and operate revolving credit funds. These organizations are not very "visible" and tend not to draw too much attention to themselves as BSOs. They tend to advertise their social service functions and provide community services, especially during times of religious festivals. They also sponsor community events. There are also other groups, mainly associations of professionals. These are not affiliated to central organizations but have clear business interests.

The BSO's can also be grouped into two major categories according to organization and function. The first consists of formal organizations with clear objectives and with professional secretariats. These are chambers of commerce or associations set up along the same lines as in other countries. The second consists of a large variety of organizations with varying degrees of formalization and depending primarily on the volunteer services of their members.

### (1) Formal BSOs with Professional Staff

Examples are the chambers, the federations and a few associations. There are also organizations that have a small professional staff but have not developed regular member services.

The services of these BSOs include:

- Organizing sectoral or other well defined interest groups into associations and providing them with regular secretarial services; organizing meetings, maintaining and circularizing minutes and dealing with correspondence.
- Providing business and trade information to members including market information, trade enquiries and investment opportunities,

- Liaising with foreign business through chambers, associations or direct contact.
- Preparing and assisting with representations to government agencies on behalf of member associations.
- Disseminating information through workshops and seminars.
- Supporting representations with research either conducted in-house or contracted out.
- Registering contracts, arranging for arbitration when business disputes arise, and maintaining a standard of business ethics and a code of conduct among members.

Many organizations in the first category are still in the process of organizing these services. Although some of them use the title of "federation" or "chamber", they do not perform the necessary functions. They have the formal structure, the mandate and the knowledge to seek assistance to develop into fully functional BSOs. Often they are constrained in this activity by the lack of a clear plan of action and by inability to access necessary human resources quickly or to win the commitment of members needed for successful implementation of programs.

#### (2) Volunteer BSOs.

These are organizations which depend primarily on volunteer effort to define their agenda of activities and to implement them. Many have developed capabilities to undertake projects as a means of generating funds. Some chambers and organizations undertake projects for (i) assisting small businessmen in credit programs; e.g. the Hambantota Chamber of Commerce, (ii) assisting women's small businesses to improve business administration and to acquire management training; e.g. the Women's Chamber of Commerce, (iii) organizing and facilitating workshops and seminars; e.g. the Federation of Chambers of Commerce. These organizations tend to carry out projects with outside funding, are designed and managed by an energetic core member group consisting often of the leadership. While the broad mandate as a BSO is usually maintained, the activities that are pursued tend to be dispersed over a wide range. The focus on member services is relatively weak. The lack of a core professional staff restricts the type of regular service that can be offered.

These BSOs are volunteer organization with self help and social service functions. They are established by a small group led by one or more dynamic or active persons. The core of activity is often quite hazy. The leadership tends to set the agenda and the organization is seen as an instrument of a small group of active persons. These organizations are not able to provide services to members and tend to have swings in membership.

#### (d) Professionally Staffed BSOs

Each BSO that is professionally staffed has the following characteristics. It has:

- A formal charter and is registered as an organization or established by an act of parliament.
- Rules for electing members, clearly specified duties and functions and terms and duration of office.
- A board of management or a council of elected members to act as the primary decision making

and advisory body.

- Membership dues that are subject to change according to the services of the organization.
- A secretariat consisting of professional staff with formal training.
- Links with chambers and BSOs in other countries and programs of collaborative work in investment and trade promotion and facilitation.
- A range of fee based services to members, e.g. certificates of origin, document certification, assistance with contracts, trade information, foreign trade links.
- Processes for functioning as the voice of the membership and representing their interests to government and public agencies.

The secretariat is the center of activity of such BSOs, organizing and expediting work. It services the affiliated member associations and groups some of which in time may develop their own secretariats for special projects. The elected members work closely with the secretariat, reflect the needs of members and determine policies for the functioning of the chamber.

Among organizations in this group there are many which do not have all of the above characteristics. What is lacking in most organizations even in the first category is the continuity of activities and member services and the development of professionally staffed secretariats. Developing programs of member services requires a continuity of support from the leadership of elected members. At this stage, emulation of other organizations is attempted. However, the practical aspects of assessing member needs and addressing them with activities requires an approach which is based on medium or long term planning. This is still absent.

In general, the BSO's, with the exception of a few, have been reactive in the field of services. The professional staff tend to maintain "low profiles" and wait for direction from the elected members or the affiliate bodies. In this sense, the role of elected members is exaggerated. They are most likely to address the immediate needs of one business group or the other. Common issues that are likely to be addressed are those relating to short term business costs or costs that are immediately apparent, taxes and loss of subsidies and assistance programs.

Development of new services does not seem to follow the pattern which a regular business will adopt. Medium term planning is conspicuous by its absence. Once again this seems to be linked to the way in which the organizations are structured. The BSO is a reflection of the membership. The elected leaders are responsible for the profile and in some ways the development of new programs. There is a strong perception that these organizations are the creatures of the sitting leadership; there is a feeling that "they have their turn". Internal examination and discussion in these organizations about what they should be doing for their members is not adequate. The periodic seminar or event providing media publicity tends to satisfy a part of the membership. This is a minimal "service" that leads to a basic satisfaction of the need for "belonging" to the right organization. Members, though business persons, seem to be still at the stage of not expecting very much from the BSO's. However, in the case of the Ceylon and National Chambers, perhaps because the member dues are sufficiently large and entry conditions stringent, member's expectations of a return through services are high.

A relatively low membership fee does not generate high expectations of services. Neither does it support the capacity to provide any. The BSOs through their internal policies condition the membership and determine the prospects for growth and expansion. The perceived success of the Ceylon Chamber and to a lesser extent that of the National Chamber has invited entry of other organizations seeking to provide services. Many have been floundering in the process. There is a lack of a clear perception about the role

and tasks of BSOs in the minds of the leadership and elected members of the more recent ones. In these cases, the organizations are those of the leaders or a small active group; it is their "club". The BSOs that have not matured and stabilized as providers of services share many features with clubs rather than professional organizations. It appears that a significant part of the membership in BSOs tend to identify with this image.

#### **(e) Finances and Funding**

The BSOs generate their income from member dues, contributions, fees for services, special levies and projects. The Ceylon Chamber and the National Chamber each has a franchise to issue certificates of origin and document certificates. The Ceylon Chamber receives substantial income from auctions for tea, rubber and spices, where a charge is levied on those offering produce for sale. None of the other BSOs had activities that generated this type of income. Special events, fee based workshops and seminars were organized by most BSOs. The Ceylon Chamber has its own facilities and a fully equipped auditorium with transcription capabilities. It has a regular schedule of seminars and workshops for members and the public on which it earns a net return.

A few of the chambers and associations have a strong fiscal base. They are able to maintain a secretariat, provide services on a sustained basis and plan and undertake new activities. Most of them, however, have a small or variable flow of revenue. Some like the Ceylon Chamber, the National Chamber, the Chamber of Small Industry and the Galle Traders and Industries Association, tend to put aside money each year and add to their savings. The programs of most other BSOs are constrained by their financial positions. BSOs other than the Ceylon Chamber have leased, rented or donated office space. Most organizations do not have on their staff professionals trained in chamber management. Exceptions are the Ceylon Chamber and the National Chamber.

Most BSO's have not clearly addressed the issue of funding in relation to the services they provide to members or the activities they can carry out on their behalf. The entry fee and the annual member dues are too low to support an equipped office with professional staff. This in turn prevents them from providing a level of service that would satisfy their members and enable the BSOs to play an effective role in the system. This vicious cycle hampers them in conducting surveys of member needs or preparing representations that would enable them to enter and remain active in the arena of policy discussion. Sustaining member interests and involvement is impaired. Continuous and effective provision of services to their members is, therefore, essential for the BSOs to maintain an effective participation in policy dialogue.

#### **(f) The Link between Services and Policy Dialogue**

In its work, the PSU addressed the central issue of the service orientation of the BSOs and of its role in providing business with useful inputs of knowledge. The policy reform process was approached as being a consequence of a strong member service base. Fruitful policy dialogue was seen to be more likely if the BSOs were seen as strong organizations of practical value. Private business expressed opinion and views through the BSOs. While it seemed that there was a need to consolidate services, develop specializations and improve the base of member services of most of the BSOs, getting to that point

depended on convincing the leadership of the need to invest in new ideas and capacity to execute them. The process of policy dialogue was a difficult issue to deal with and tended to divert the attention of the BSOs from their primary function. Many tended to think of the publicity value of getting particular concessions for "their members" as a primary task. The generally fragmented and divisive tendencies of the BSOs further complicated matters. There were strong feelings of getting to be the organization that was able to win a particular procedural change or policy reform. Cooperative efforts were generally few and tended to be linked to tax concessions. It was difficult to get consensus across BSOs as the reforms tended to have adverse effects on those who benefitted from the concessions under the present system.

There is a perceived sense of competition among the BSOs that has many positive and negative features. This tends to induce the organizations to satisfy member needs. On the other hand, it duplicates work and creates "noise" in the arena of representation. Businesses become uncertain where they can obtain the services they require. Furthermore, public agencies express their unhappiness about the multiplicity of chambers and organizations with each representing a small part of the business community. When public agencies wish to discuss impending policy changes or desire the views of business persons, they are unable to quickly assemble a "representative" group of business leaders without going to many different chambers and associations. The fragmentation in representation and service also offers many opportunities as the PSU found. There was the possibility of getting the different organizations to begin specializing in services according to their membership and addressing issues affecting particular sections of business and industry. At the formative stage of the institutional structure, forcing consolidation did not seem prudent. The driving force to form new business organizations is strong. Individuals seek to create new special interest groups on the basis of their experience with other chambers and associations where their "voice" may have been swamped by other more dominant interests. Dealing with this problem by building structures of representation was beyond the scope of the project.

### **(g) Conclusions**

BSOs, when they are well organized and professionally managed, provide a range of very useful business services. By servicing members, these BSOs acquire a good understanding of the economic issues facing specific sectors or groups of business. They represent interests of parts of the business community to government agencies. The possible role and function of BSOs is still largely misunderstood among policy makers in Sri Lanka. This is partly due to a lack of information and analysis of what BSOs do. Meanwhile, the literature on economic development has not examined the specific contribution that institutions such as BSOs can make to improve the process of policy dialogue. An improved system consisting of more proficient BSOs can play an important role in improving the performance of the entire private sector.

The system of BSOs in Sri Lanka is not well integrated. Although there are federations, chambers of commerce and associations of business and industry, they do not represent the businesses from the regional and local levels as well as they should. While some BSOs are developing their capacities and improving services, improvement of the system requires resources and interventions at various levels. One of the primary weaknesses in the prevailing system of BSOs is the relative lack of services for regional and rural businesses. Chambers of commerce and business associations are needed outside Colombo and they have to be organized and assisted during the initial stages. The new organizations which emerge have to be assisted to produce member services. The rudimentary BSOs which exist in the regions and small towns do perform useful services but they are capable of producing better services and being more effective.

Slow economic growth in the past, dominated by the public sector, resulted in a subordinate role for the private sector. The small BSOs outside the capital did not play a visible role in promoting private enterprise. Economic liberalization during the past one and a half decades requires a change in the role played by BSOs. They have to be more active in the policy arena in order to ensure that the scope for private enterprise is expanded. This demands that the BSOs become stronger and have capacities to analyze economic issues and transmit the information to the members. As importantly, by providing services to their members, the BSOs are able to maintain close contact with them and thus gain important insights into the issues facing particular sectors or areas of business. This knowledge is very important for formulating effective policies.

## Chapter 3

### Developing Chambers of Commerce in the Provinces

"The vast majority of non-governmental organizations (NGOs) are national or local in nature, and a successful transition to sustainable development will require substantial strengthening of their capacities. To an increasing extent, national NGOs draw strength from association with their counterparts in other countries and from participating in international programs and consultations. NGOs in developing countries are particularly in need of international support - professional and moral as well as financial - to carry out their roles effectively".

Our Common Future, The Brundtland Commission Report

#### (a) Introduction

There is a large body of experience and analysis of programs and policies to assist NGOs to improve their performance. NGOs are considered to be effective organizations to carry out development programs that reach local communities in developing countries. Governments have not always been successful in assessing needs at the local level and developing efficient programs. NGOs are an effective means of linking development programs to the intended beneficiaries. They have demonstrated capacities to efficiently deliver a wide range of services including primary health care, sanitation, water supply, credit, agricultural services, and information about resource management. They complement the services and activities of governments and improve access to basic services.

NGOS are also seen as efficient mechanisms to increase community participation in managing their social and economic environment. NGO assistance has covered a wide field of activity ranging from community development to management of local resources. However, services to improve production and productivity outside agriculture have received relatively little examination. Linking enterprises within countries, improving information flows to assist production and marketing, and improving products and commercial practices have not been primary activities of NGOs. Business and commerce have been relatively neglected. Although NGOs have been successful in community development programs, many other important opportunities to diversify and strengthen the rural economy of developing countries have been missed.

Most interventions and international support to NGOs initiate activities to improve small scale production. International networks function to improve the organizational capacities of local NGOs. However, similar programs to improve NGO capacities to assist rural enterprises with business services have not been developed. They are needed and can provide a vital link in assisting rural communities and enterprises to function more productively, and thus to generate larger income and employment. There are some donor assisted projects and programs which address the needs of the business community through BSOs. Agencies of the United Nation's including UNCTAD, ILO and UNIDO work with BSOs to improve their professional capacities and services. The objective is to improve their capacities in various ways - to increase the flow of trade information, to enlarge international trade in other ways, and to develop entrepreneurial skills. These agencies organize exchange programs for BSO professionals and

members to improve their professional capabilities. These programs focus attention on the larger national level BSOs. The local and regional BSOs have not received much attention. However, there is need to pay greater attention to, and provide resources for the development of the BSO system and especially that part which covers the rural and small enterprise sectors.

Field work by the PSU found that there is no organized, well developed capacity to service and represent the interests of private enterprise in the provinces. The infrastructure for discussions and dialogue between private business and the provincial administration is not developed. However, the new Industrial Promotion Act and the administrative reforms that have been undertaken to provide greater regional autonomy through Provincial Councils and Divisional Secretariats, require new capacities for services to private enterprises, and provide opportunities for representation and policy dialogue for provincial private enterprise.

The chambers and associations located in Colombo service the large scale national level businesses. The existing regional business associations are not linked to these chambers and do not receive these services. At present, the needs of the growing private sector in the provinces for business and commercial information are met only by BSOs located in Colombo.

Strengthening the system of chambers and associations in the provinces is an important component of a program to improve policy dialogue and representation. An initiative to develop institutional capacity for the provincial private sector must first enhance the performance of these institutions. To enter into informed discussion and dialogue with the provincial administration, these institutions must have the capacity to perform services for their members. Some national level chambers and associations have been able to increase their member base by providing information services to the provincial business organizations.

The PSU conducted preliminary enquiries and small scale surveys to assess capacities of existing regional BSOs. This information identified the potential for better regional organizations to promote private enterprise in the provinces. Formal organizations with professional capacity to provide business services to members would reduce the information costs of businesses. At present, information about government regulations and incentives, trade opportunities and market information is not systematically available to many small and medium businesses in the provinces. These services have to be developed through organizations that have the capacity to provide such services.

Appendix A, Establishing New Chambers, contains notes and working papers prepared by the PSU to assist the formation and the initial work of new chambers. They include notes on organizing a chamber that were presented to groups of businessmen, material to help the new chamber conduct simple surveys of the needs of members, instructions on how to develop simple business services and notes from field visits.

#### **(b) Initiatives to Establish Provincial BSOs.**

The PSU helped to establish three new provincial chambers of commerce. Grants from the project enabled professional offices to be established and basic member services to be provided. Considerable ground work preceded the formation of these new organizations. Regular meetings were held with groups of businessmen to clarify the objectives and functions of the proposed BSO, formalize the organization, plan and budget for activities and services, and develop the membership. Networks were established with



national level BSOs to assist the new BSOs to develop professional capacity and member services. The PSU arranged training programs on management of BSOs and production of basic services with the Ceylon Chamber. The national BSOs considered the new BSOs as important links to the regional business community and arranged to provide information and other services. The Ceylon Chamber provided orientation to the members of the new chambers and organized new programs to provide them with services and business information. The national BSOs were an important resource for the development of the regional BSOs.

The three new chambers of commerce in the provinces were the Chamber of Commerce and Industry Central Province, The Wayamba (North Central Province) Chamber of Commerce, and the Hambantota Chamber of Commerce in the Hambantota district of the Southern Province. In addition the PSU funded the Galle Traders and Industries Association in the Galle District of the Hambantota Province. The first effort of the PSU was with a group of businessmen in Matara (in the Southern Province) to set up a BSO but this effort was not as successful as the others. A new BSO, the Matara Businessmen's Association, was actually formed but this did not ultimately receive PSU funding.

The experience gained in Matara contributed significantly to the work in other provinces. A few general principles were developed and helped expedite the formation of new BSOs. The following activities were undertaken in order to establish provincial BSOs.

- Field work to identify existing BSOs, business groups and organizations, which could form the nucleus of a new organization.

The PSU met key officials of large NGOs engaged in development projects, firms in accounting, banking and finance which had a clientele in the province, public officials, and officials of existing BSOs to assess both the need and prospect for setting up a chamber and the prospect of doing so successfully. This network identified key business leaders and potential nucleus groups and organizations.

- A core group consisting of business leaders and a few public officials was formed to pursue the idea of forming a professional BSO.

An agenda for the core group was developed. It included the following items:

Discussions to solicit interest among the business community to establish a BSO with a formal professional office and services to members. Efforts to identify potential members and to "sign" them on.

Preparation of a constitution with objectives and articles of association to be presented to a larger audience of businessmen in the province or area. Formal registration of the BSO under the Companies Act as a not-for-profit organization.

Examination of the fiscal implications of establishing and operating a BSO. Determination of start up costs, obtaining member contributions and establishment of a rate structure for membership.

- The PSU outlined its mandate and the possible support it could give the BSO when it was formed.

The core group was provided with introductory material and PSU staff made presentations about the advantages and resource needs of a professional formalized BSO. Specific opportunities to discuss policy issues relating to infrastructure, regulations and procedures with the provincial councils and local governments were examined. Public officials attended these meetings. They expressed strong support for dialogue and partnership on important issues to promote enterprise in the province and indicated the emerging opportunities for cooperation between government and the private sector.

- The PSU and the core group met with the Provincial Chief minister and executive staff to inform them of the proposed initiative and to seek their support.

### **(c) Lessons From the First Effort to Form a BSO in Matara.**

The experience in Matara was useful for the work which followed. It highlighted some of the critical issues in organizing a new BSO. The work in Matara was not successful and did not lead to the formation of a BSO within the expected time period. The core group held many meetings attended by a cross section of business which pledged support for the proposed venture. The PSU provided technical assistance and hired a consultant to work with the core group to:

- Prepare a work plan to establish the BSO.
- Prepare the Memorandum and Articles of Association, draft a constitution, identify office space and hire a professional executive for the BSO.
- Identify other BSOs in the province and solicit their interests in joining the venture.

The core group however was not able to proceed quickly. The difficulties included:

- It wished to form a Chamber of Commerce for Southern Province and was not able to bring other regional business groups together.
- It under estimated the effort required to win the support of businesses throughout the province if indeed, a provincial chamber was to be formed.
- The individuals in the core group were unable to take leadership and carry out the planned activities. They were hesitant to work closely with the provincial council and other public agencies and to draw on their resources. As a result, many of the initial activities to establish the BSO were delayed.
- Without a formal organization, the group was not able to access PSU funds.

During the course of this work, the PSU examined the needs and identified the prospects for establishing chambers in two other provinces. Discussions were held in the Central Province and the North Western Province. Meanwhile field visits to Matara identified a strong BSO with a large membership in Galle - the Galle Traders and Industries Association. Later, the Hambantota Entrepreneurs Agency, also in the Southern Province, contacted the PSU and started discussions about forming a chamber and obtaining funding for the venture.

A few issues related to the formation of new BSOs warrant close attention.

- **Formalization.**  
Establishing the new BSO as a registered entity under the companies act, with a constitution, formal rules and regulations was an important initial step. It distinguished the BSO form from other less formal ones. It also opened the door for interaction with the national level BSOs.
- **Setting up a professional office.**  
A professional office was essential for the BSO to produce member services quickly. This enabled the BSO to perform its mandated role.
- **The links with the public sector and the provincial council.**  
The new chambers had a unique opportunity to start their activities with very strong support and links with the public sector. This placed the new chamber at a great advantage over other organizations which had emerged before the provincial councils were formed. The success of the provincial system of administration was of high national concern. Dialogue between business and the provincial administration to develop the region had strong potential for a new public-private partnership. The new chambers also had to steer clear of direct affiliation to a specific political group. For this reason direct involvement of the provincial chief minister in promoting the chamber was likely to be counter productive. In all cases, the Chief Ministers of the respective provinces initiated action and provided support but made it clear to local business that the BSO was their organization and their responsibility. In the Central province, the Chief Minister arranged for the provincial ministry of industries to assist with the formation of the BSO. Initially, office space and logistical assistance were provided. The Chief Minister of the Wayamba Province provided a grant from the provincial administration to the new chamber and arranged to have an executive from an agency affiliated to the province to serve as the secretary general of the chamber for the initial period. In the south, when discussions with the Matara group were going on, the Chief Minister held several meetings to examine how the provincial council could assist the formation of a chamber.

The Chamber of Commerce and Industry of the Central Province was the first ever chamber of commerce to be formally registered outside Colombo. The core group of businessmen, assisted by the Provincial Ministry of Industries and the PSU, prepared the articles of association and the memorandum of association. A law firm was hired to register the chamber with the Registrar of Companies. The constitution of the chamber was presented in draft to a general meeting of businessmen in the central province and approved. The initial step of formalization placed the new organization on a footing very different from the other organizations of businessmen which functioned in the central province. It was registered under the companies act as a chamber of commerce with a constitution, objectives and articles of association that specified the organizational objectives, area of activity, conditions governing membership and election of office bearers. The officials were responsible for holding regular meetings and for keeping the membership informed about activities. Transparency and fiscal integrity of the organization was enhanced by these measures which required the accounts to be audited, presented and accepted by the membership.

Many NGOs in the country have been weakened by organizational features that resulted in inadequate transparency in fiscal operations. Donor funds of considerable magnitude flowed to the NGOs. Some had not developed protocols and systems to manage the funds efficiently. Often responsibility rested with a small minority within the organization and the membership did not participate adequately in decision

making, especially on financial matters. There was considerable discussion at the national level about the need to improve the financial discipline of NGOs. Most NGOs were not registered under the companies act but constituted under special provisions with the Ministry of Planning under the regional Development Division or with the Social Services Department. Some of the problems faced by the NGOs were the result of weak internal mechanisms of oversight and control. Although formalization by itself would not resolve these issues, it offered mechanisms for discussion and review and promoted wider member participation.

Many of the leading national BSOs had been established by law through acts of parliament. Only a few had taken the path of registering under the companies act. The PSU reviewed the different mechanisms for establishing BSOs legally, discussed them with the BSO formation committee in the Central province and decided to pursue formal registration under the companies act. This established a precedent. No chambers of Commerce had been registered with the Registrar of Companies outside of Colombo. The path was opened for others to become legal entities under the Companies Act.

Based on this experience, the other chambers which were formed were instructed and assisted to register themselves as formal entities. As a result, the Wayamba and Hambantota chambers were able to register themselves quickly. The businessmen in the core group set up to form a BSO understood the importance of this requirement. They had done so with their own businesses. The advantage of clear responsibilities and obligations of the management and the members was noted. Furthermore, it brought the features of enterprise necessary for the success of the BSO to the forefront. This view of the BSO as an enterprise of businessmen set up for the purpose of improving the environment and performance of business was important to steer it towards producing services. It facilitated discussions about programs and activities that the new chamber could undertake. Its role as a mediator between the regional administration, the public sector and members by providing services was examined.

#### **(d). Activities of the New BSO.**

The new chambers had to develop a set of activities and services quickly. The enthusiasm of the initial membership had to be sustained and new members attracted to the chamber. A few simple themes were used in the discussion to prepare the work plans for the new chambers. They included:

- Identifying and acquiring office space.
- Preparing a time table to hire and train a few professionals for the office.
- Establishing sub committees to deal with sectors and/or issues.
- Visiting the leading chambers in Colombo to find out how they are managed and what they do.
- Identifying opportunities to host workshops and seminars of interest to business.
- Developing basic services - preparing a member directory and a simple newsletter.
- Preparing an agenda and scheduling regular meetings with officials of the local government, provincial council, and line ministries to discuss issues of importance to business.

- Relating planned activities to the fiscal base of the organization - looking beyond the USAID grant.
- Networking with other BSOs, universities and public sector agencies.

This required considerable planning and effort. Staff had to be recruited and trained while the members of the chamber themselves were finding out what a chamber was expected to do. The PSU prepared a few introductory guidelines for starting member services.

The new BSOs were well equipped relative to others to start services to business. They had the capacity to assemble information about local business quickly and to become centers containing local business capacity and capabilities.

Each of the activities required assistance from the PSU. Two related themes were used in the discussions with the management of the new BSOs and they were successful in getting the businessmen to focus on the issues.

- The BSO was an enterprise and required a business perspective.
- The BSO had to generate cost effective services to the members (present as well as prospective).

This enabled the PSU to get the management to focus on activities which could be sustained and improved. The PSU assisted the BSOs with prototype products - member directories, news letters and commercial information. It helped them to "install" these activities within the organization. Once the BSOs were formed they were quickly used by the public sector. The BOI held a regional workshop jointly with the new chamber to discuss its new incentive schemes and its plan to promote foreign investment in the central province. The new Regional Industry Service Committees set up under the Industrial Promotion Act, invited members from the chamber. This gave the chamber direct access to the regional industrial policy making system.

One of the most important areas of service for the new BSOs - information that could reduce costs and improve efficiency for business - had been overlooked as an important and useful activity by most existing provincial BSOs. After specific service possibilities were identified with assistance from the PSU, and samples provided, the BSOs were willing and able to pursue their production. Information about the economic environment, regional business opportunities, and costs of business was not widely available. The PSU demonstrated that the chamber could produce these information services by contracting the work out, e.g. to the university. The large market for business services was found to be relatively unexplored. The provincial chambers had a major role to play in developing this sector and an opportunity to develop a sound fiscal base doing it.

#### **(e) Important Lessons**

1. The new chambers were most likely to succeed when they were built on existing broad based business organizations. Developing consensus from outside, to form a representative organization was time consuming and difficult. The experience of the PSU in Matara bears this out. The core group was diffident to include wide participation from the start. As a result it did not build a critical mass of support to create a BSO.

2. Formalization has both advantages as well as disadvantages. However, it weans out groups that are not able to do the background work themselves. Pushing groups with strong volunteer motivation to set up formal organizations imposes serious demands which may not be willingly accepted nor maintained. The responsibilities of a new BSO demand considerable volunteer effort. There is no direct personal gain to the founder members besides prestige and standing which in most cases they already have. Strong leadership, while very important at the initial stages, poses problems for successors. Formal organizations help to reduce some of these problems with shared responsibilities and codes of conduct. Registration as a entity under the companies act results in wide publicity and is quite beneficial to the new organization. The organization is known, it cannot be exclusive and is not able to operate as a "club" for an elite. A formal organization also enhances the financial controls and responsibilities essential to manage grant funds.
3. A professional office is an important step to begin functions and services. Although businessmen are aware of the quality and skill of staff needed for an office, many of the existing BSOs had not advanced to this point and therefore had a relatively weak member service base. The new regional chambers were assisted and encouraged to set up offices and to focus on member services. This imposed considerable fiscal burdens and demanded that managers focused on developing medium term plans. The elected leaders had to increase their awareness of the role of a chamber and what it had to do as a chamber.
4. Developing work plans with specific activities and services is critical to the expansion of the new chamber. It is not obvious nor simple to determine where they should begin. The leading chambers in Colombo are a very valuable resource to build awareness of the basic functions and activities of chambers. Member directories, seemingly simple to develop, form the base of a chamber's information system. Knowing the members; what they do, the lines of business they are in and their capacities, is a basic element of information sought through chambers. The high ground of dialogue with public agencies cannot be maintained without the support of knowing the membership. A member directory enables the regional chamber to network with national chambers and to exchange information. Visiting businessmen are also most likely to enquire about the membership and its characteristics.
5. The good will of regional public agencies has to be quickly utilized. The new chamber has to reflect the interests and opportunities that emerge through discussions with the regional public agencies to the membership, and use this to expand membership and to develop services. This requires the formation of subcomm.ttees dealing with issues related to the main business activities of the region. The management has to reflect on the membership size that is desired to stabilize the financial base of the new organization much like a new business. Considerable opportunity exists to participate in public sector programs related to industry and business. The planned activity of the Hambantota chamber, to provide information to members about the benefits of opening tax files, is one example of long term business thinking. Small business is well known to operate outside the tax net. However, by doing so businesses are unable to access formal credit, are not aware of the full costs and are unable to plan for expansion. By directly seeking assistance to become business tax payers, the businessmen open the door for discussions on the reciprocal rights to better infrastructure and a better environment for business. Many similar opportunities exist for regional business and can be pursued through the BSOs.

6. Some of the smaller BSOs located in towns and cities were not likely to graduate to chambers due to their characteristics. Some were organized on ethnic lines and did not provide regular business services. The traders organizations provided useful services to members and protected member interests. They discussed lease and rental rates on commercial property owned by the local authorities. However these organizations also acted at times to restrain entry of others into commercial areas and market places. They reflected the intense competition for resources - market sites. Many of these organizations can benefit from programs which assist them to focus more attention on additional member services.

## Chapter 4

### Promoting Policy Dialogue Analysis of Selected PSU Supported Activities

"People of the same trade seldom meet together, even for merriment and diversion, but the conversation ends in a conspiracy against the public, or in some contrivance to raise prices."

...."The interest of dealers, however, in any particular branch of trade or manufactures is always in some respect different from, and even opposite to, that of the public. To widen the market and narrow the competition is always the interest of the dealers." .....

....."The proposal of any new law or regulation of commerce which comes from this order, ought to be listened to with great precaution, and ought never to be adopted till after having been long and carefully examined, not only with the most scrupulous, but with the most suspicious attention."

Adam Smith

"Chambers of Commerce in Sri Lanka are petition writing organizations."

A senior public official.

#### (a) Introduction

A large part of economic analysis rests on the notion that self interested behavior of individuals, under specific conditions, will lead to the general welfare of the public. However, associations of business persons have been considered with ambivalence and suspicion. It is felt that they will tend to put forward suggestions that benefit them, often without consideration of the "public good". This perception persists and policy makers in Sri Lanka are quick to point out many instances where business has proposed measures that are narrowly self serving and make little or no contribution to any discernible public benefit. However, there have been many instances of self serving proposals by business persons that have received favor of the government.

Since 1977, private sector leaders, spokespersons and successful managers have been drawn into many national activities. Private sector managers have been appointed to important Presidential Commissions to reform systems of Taxation, Tariffs, Finance and Banking. These appointments have been based on the achievements and knowledge of the individual rather than on their representation of broad private sector interests. Members of the private sector have been appointed to important public sector agencies including the Monetary Board of the Central Bank, boards of the public sector banks, the Export Development Board and the Industrial Development Board. The Industrial Development Strategy of the Ministry of Industry, Science and Technology was prepared with considerable inputs from the private sector. Various committees which prepared the strategy were headed by individuals from the private



sector. The Industrial Promotion Bill of 1990 which followed the strategy, established an Industrialization Commission, an Advisory Council and Regional Industry Service Committees. They are designed to have a significant private sector input. Managers from the private sector have also been selected to manage important public enterprises. The Ministry of Plantations, which managed the nationalized plantations until recently, had many former private managers in key positions.

However, the individual roles played by competent private sector persons have to be separated from their representation of broad interests. The need for competent and enterprising managers was acute and the public sector needed to draw on the scarce human resources of the private sector. The large diversified private companies had well trained managers at the top level who were aware of the specific opportunities and constraints for business, especially for exports. They understood the demands of the modern market place. The public sector required the managerial and entrepreneurial skills of the private sector for new public sector agencies that promoted or managed enterprise.

Policy makers in the government and the public sector were nevertheless not willing to draw on private sector views in formulating policies. They had a strong perception that the private sector is not able to develop common positions on economic policies because of the multiplicity of their interests. Policy makers and public officials were conditioned to develop policies without attempting to create a broad consensus among all sections of opinion. They believed that private sector groups did not have the capacity to analyze macro economic policies and to contribute to the process of policy formulation. There were strong tendencies both in the public sector and among private sector groups, including the BSOs, to accept this position. Macro economic policies were considered to be outside the area of concern for private enterprise. The ideological debates about the structural adjustment programs supported by the World Bank and the International Monetary Fund generated strong political debate but the private sector as such did not take positions on these programs. Information on macro economic policies was not widely available and informed discussions were in any case rare. Even in the political arena, elected representatives were often critical of policies and attempted to mobilize opposition without a full grasp of the facts. The administration perceived the political costs of popular dissent, generated by political mobilization, to be high. The short term response was to keep policy making within the public sector and to reduce the spread of information. This had two effects on the process of policy making. The prospects for the economy in the short and medium term, the review of recent performance or emerging issues related to economic management were not discussed by the private sector, though private sector entities are often the subjects of policy and the agents expected to generate economic growth that these policies aim to stimulate. Political sensitivities dominated the flow of information on the course that the government was setting for the economy. Critical appraisal of economic performance, especially when contained in documents prepared by the international donor agencies, were highly restricted and not subjected to review by a broad group of participants. They were considered to be dangerous instruments in the hands of political opponents of the government. Policy makers did not consider it necessary to discuss with the private sector the course the government was attempting to set for the economy other than through official documents which were made available long after policies had been decided. The parliament was one forum where this discussion took place. But there was a wide disparity in the access to information between two groups of elected representatives and officials - government and non government.

Appendix B, Preparing for Policy Dialogue, contains discussion notes and analytical papers that were produced by the PSU. They include short papers on broad macro economic issues as well as specific sectoral issues. The appendix also contains the notes prepared by the PSU to initiate work by BSOs on industry and sector agenda.

## **(b) Macroeconomic Policy**

One reason why senior public officials have not favored consultative mechanisms enabling private sector business views to access the macro policy making arena is that business groups tend to represent a small minority of economic interests which have narrow positions to defend or win. The public sector has assumed the mediating role for the public and the consumer. Admittedly, businesses are not all competitive or efficient and they often do not have views favoring shifts in the economic context towards greater competition. While public sector perceptions cannot be overlooked, the fact is that private business is increasingly becoming an important actor in the economy. The modern sector is winning and extending export markets, drawing foreign investments and generating growth in income and employment. While policy makers certainly do not have to entertain the narrow interests of business when formulating macroeconomic policies, a well-informed modern business sector - or better, all parts of business - should certainly be able to make a useful contribution to sound policy making. Awareness of this is not developed by autonomous processes. Mechanisms for consultation have to be deliberately created and nurtured. While private business groups wish to participate in national economic decision making, they have to make an investment in learning and awareness to enable them to participate effectively in this arena.

There are two related aspects to the issue of business participation in the process of policy making. One relates to the need for business to be aware of macro economic issues and the other to the need for policy makers to develop awareness of the role that business can play in policy making. The PSU considered that better awareness of macro economic problems and policies among the BSOs and their members was necessary for effective policy dialogue. A broad framework was prepared to guide possible PSU action. However, the private sector groups had been conditioned to accept this arena as the exclusive domain of the public sector. Furthermore, some considered that investment of resources to gain better understanding of the broad issues related to the economy were not likely to yield direct benefits. As a result, very important issues that had a direct impact on the private sector were left unexamined by business e.g. public expenditure and investment, the government budget deficit, macro economic policies and their impact on interest rates and exchange rates. There were no regular activities within the BSOs to develop awareness of the economic issues facing the country and to throw light on how the private sector was affected by and could respond to them. Two qualifications need to be made to this statement. One, the specific concerns of business groups afforded some opportunity to examine issues in the larger context. Two, although the links between the research community, the university faculty and the BSOs were quite weak, workshops, seminars and discussions were periodically organized by BSOs and other private sector organizations. These helped to improve awareness of economic problems. In addition, associations of professionals, private research institutes and analysts reviewed economic policies, the annual budget, prospects for the economy and other specific economic issues.

## **(c) Broad Business Policies**

BSOs and business groups generally react or respond to policy changes that affect the conditions for business or an industry. Nevertheless, a continuing concern about the need to improve the climate for business and industry through appropriate incentives, has been expressed by business leaders and groups. However, these concerns are not usually formulated as programs of action and dialogue that can be undertaken by BSOs. Both business and policy makers have to modify their perspectives if conditions for the business sector to grow rapidly are to be created. To effect this change, business has to accept and actively promote conditions for competition and market expansion. Regulatory infrastructure has to be

strengthened for this purpose. The public sector has to create the environment for viable enterprises which are also capable of entering the international market place. Existing businesses are unlikely to support measures that increase competition even if they improve their own medium term economic prospects.

The present infrastructure in transport and communication is not adequate to support the rapid expansion of enterprise. Therefore it is surprising that BSOs and business groups have not vigorously pursued a dialogue with the government to make rapid improvements in infrastructure. The various incentives for exports and selected industries offset costs of transactions and infrastructure and reduce the price disadvantages they face compared with competitors in other countries. There are many opportunities for the private sector to actively engage in dialogue regarding infrastructure development and financing. The various fiscal incentive schemes, especially those to promote export production, have increased distortions between domestic producers and exporters.

#### **(d) Sectoral and Industrial Policies and Programs**

The specific concerns of business offer opportunities to develop and expand on the existing processes of dialogue. Sectors which have high growth potential, or constitute an important part of exports, or with good possibilities for links to the small scale production sector and with positive distribution effects, are particularly likely to be interested in developing mechanisms for policy dialogue. The discussions on procedures and those concerned with maintaining present advantages were very important elements in ongoing discussions. But overall perspectives of the private sector were still set by the public sector.

The PSU strategy to assist the BSOs consisted of a few interrelated elements. Expediting the activities the BSOs proposed to undertake required additional assistance, to plan, program and execute them. The PSU found that it was much easier to get the work done if a few simple principles were followed. Without limiting the PSU assistance to advice, the PSU developed a range of "products" and services which the BSOs themselves could undertake to produce. This required the PSU to have its own capacity to produce useful "demonstration" services. Research staff was hired to produce a range of demonstration products and services and to work with the BSOs. These prototypes included short policy papers, newsletters and material to develop computerized member directories. The prototypes were then presented to BSOs together with information about the resources needed to produce them. The PSU thus came to be seen as a generator of ideas beneficial to the BSOs. Requests to assist BSOs with their representations and other services followed. This process was built over a period of year. In most instances, the work was considered very useful and further joint activities to improve the BSO services were requested and undertaken (See "Installation Initiatives of the Private Sector Policy Support Unit, Gunatilleke, N. 1992).

#### **(e) Facilitating BSO Work in Industry-Wide and Sectoral Programs**

There are at present no private sector institutions which provide regular analytical services to the private sector. Awareness of the need for research and analysis to support representation and to facilitate policy dialogue, is also inadequate. However, there are strong signs that many BSOs would seek to improve their capabilities in this area. Building "in-house" capabilities for research and analysis is hampered by many factors. One of the important factors among them, is the time consuming effort to identify suitable personnel and to retain them within the BSOs. BSOs are unable to afford going rates for skilled analyst-researchers. Even when junior personnel are hired and trained on the job, they are lost to private business after a few years.

Analytical and research skills are scarce and a few groups and individuals service a varied clientele including international donors, the government and the private sector. A preliminary step to build the research capacity of the BSOs would be to develop networks with existing analytical and research institutions and agencies. These links enable BSOs to access skills as required. However, the private sector through the BSOs should have regular programs which draw on these resources. This process will familiarize the BSOs with the prevailing market for analytical skills. The BSOs could also do well to develop programs which are undertaken jointly with universities and research institutions. Researchers and analysts have to become aware of the links to business and industry that BSOs can provide. Interaction with the business community can enhance the quality and content of learning and training in the university system.

The activities undertaken by the PSU in relation to some issues are briefly outlined in the sections below. Three of these are broader in nature while three relate to specific sectors, though broader issues - such as the relationship between research and industry - are raised in these as well.

#### **(f) An Agenda for Industry**

The Industrial Association of Sri Lanka (IASL) is a new organization affiliated to the Ceylon Chamber of Commerce. The IASL was preparing its agenda for activities and sought the assistance of the PSU through the Ceylon Chamber of Commerce. The PSU assisted by helping the CCC with organization of a workshop on issues in financing for manufacturing. Analysts were identified to prepare short papers. The PSU used this opportunity to initiate discussions with the council of the IASL which indicated interest in developing a broad agenda for the manufacturing sector.

The manufacturing sector was growing more rapidly than other sectors of the economy during the past decade. New capacities were being created and export markets were being developed in a range of new activities. Policy makers sought to improve the flow of foreign direct investment to assist the growth of industry. Incentive schemes of the Board of Investment (formerly the Greater Colombo Economic Commission) created a dual system for enterprise. Export manufacturing within the free trade zones had lower taxes, faced lower costs for infrastructure, and had easier access to imported raw material and inputs. Those located outside faced different costs and conditions. By the end of 1992, the BOI extended incentive schemes outside the free trade zones and introduced schemes for small and medium scale export manufacturing activities as well as service enterprises. During the course of 1992, policies were adopted to reduce the difference between the incentive regimes for domestic producers and exporting firms under the BOI.

In Sri Lanka, government strategies for manufacturing were developed by different public sector agencies. The BOI dealt with foreign direct investment. The Ministry of Industries Science and Technology addressed policies for domestic and non BOI enterprises. Meanwhile, the EDB prepared plans, developed policies and assisted the export sector. However, the private sector had not examined for itself, what it considered to be the prospects and possibilities for manufacturing and exports. It was felt that discussion within the private sector was likely to be of significant practical value. Business needed to be aware of the changing environment for manufactures, and the possible responses to meet the challenges of new markets.

The strategy for industry was expected to present a private sector view of the potential for industry and exports and to identify strategic possibilities. There were a few businesses which had performed very well

in manufactures during the past decade. They had entered new markets, improved productivity and expanded their scale of operations. Some had developed successful sub-contracting links locally while others were able to establish joint ventures with foreign companies. Weaknesses in infrastructure, problems posed by the trade regime and the high cost structure were serious constraints to expansion. Individual firms had learnt important lessons and gained considerable experience in expanding manufacturing and exports. However, these lessons had not been put into a perspective of possibilities for the entire sector.

The various BSOs representing the interests of industry were beginning to develop new links with the social science research community. However, both sides were not aware of the mutual benefits of working together. Researchers considered the needs of business to be too narrow and limited to analytical support for special advantages or to retain subsidies and other benefits. Business considered analysts to be impractical or theoretical. Meanwhile the university system did not work closely with the business community in order to further knowledge and analysis of the conditions specific to industry in Sri Lanka. An activity which enabled the research community to contribute to the private sector's understanding of issues, if properly designed, was likely to be a lasting mutual benefit. An activity where industry examined possible future scenarios based on sound analysis was considered to be timely by leaders of the IASL.

The activity was organized under the direction of the IASL and supported by the CCC under the grant it received from the PSU. The IASL obtained assistance from the Marga Institute, a Sri Lankan development research organization, to coordinate the preparation of the agenda and to organize a workshop to present the agenda to industry representatives. Industry leaders agreed to prepare issues papers as inputs to the effort.

The most important contribution of the agenda was to improve awareness among private industry of the emerging opportunities and likely scenarios for industrial growth and development. The agenda attempted to change the dialogue for growth by focussing on the future and examining the roles that business and industry had to play. When industry was able to present strategies based on its experience and plans, instead of merely contending with government for fiscal incentives, a new basis for dialogue was created. The public sector often complained that private industry did not have long term plans and strategies to achieve them. This was largely correct. The public sector is unable to project development prospects from its vantage point without a substantial input from the private sector. Strategies and plans for action for private industry prepared by the private sector form a vital contribution to this process. The Agenda for Industry supported by the PSU helped the private sector to make this contribution.

#### **(g) The Quality Awareness Program**

Sri Lanka is vigorously pursuing the development of exports. The 1990's have been declared the Decade of Exports and a range of new activities to increase awareness of the need for improvements in production, market access and productivity have been proposed. Government agencies promoting foreign investment and export development are being streamlined to meet the challenge of increasing competitiveness and product quality and new export incentive schemes have been established. The BOI which has the mandate to promote foreign investment and develop free trade zones, extended activities outside the Colombo metro area and included agriculture and small scale manufacturing in its promotional activities. The Export Development Board has the mandate to promote and expand exports. It had identified and developed new sectors and provides a range of services including product development and

marketing. The EDB prepared an export development plan with substantial private sector inputs. The EDB organized export product associations and the Federation of Exporters.

Quality improvement offered a new opportunity for a dialogue between private enterprise and the public sector on a range of issues affecting the international competitiveness of Sri Lankan exports. Mechanisms to establish improved product and process standards were already in place. The Sri Lanka Standards Institute (SLSI) had the mandate to promote quality development and had programs to inform industry of the International Standards Organization (ISO) 9000 Series standards. However, progress was slow and serious resource constraints hampered expanding programs.

Moreover, the awareness among exporters and industrialists of issues related to quality management and standards was relatively weak. There was no discussion among industrialists about "good manufacturing practices", international standards and quality systems, whereas these issues were at the forefront of the concerns of newly industrializing countries such as Thailand, Malaysia and Singapore. These countries were forging ahead in assimilating the new standards into their production processes.

Business in Sri Lanka was not paying attention to the international discussion of total quality management. This was a serious weakness in the export sector. The integrating European Market was establishing standards for imports and the Sri Lankan exporters had to become quickly aware of them. Tea exports to the EEC were already under the new standards. The CTTA had provided the tea export sector with the necessary information. However, the growing non-traditional, small scale producers of tea were still far from developing the basic elements of quality management systems. In general, other sectors were completely unaware of the issue. A program to increase awareness of the need for quality systems was soon accepted by the leading ESOs to be a critical activity.

A Quality Awareness Program was undertaken by the Federation of Chambers of Commerce with the grant funds it received from the PSU. This project was expected to work closely with the SLSI and its ongoing programs for quality improvement. Planned activities included workshops and seminars to introduce the concepts of quality systems and to prepare basic quality improvement manuals for a few important export oriented activities. A small unit with professional staff was to be set up to organize and expedite the tasks. It was soon apparent that exporters were very interested in developing systems for quality improvement and management. However, at the initial stage only the basic information could be provided. Preparing quality manuals for specific sectors required more careful study and preparation than was possible during this period.

The program operated at two levels. The need for quality improvement had to be perceived and accepted by top management. Seminars were organized for CEOs, and the concepts of quality management and how improved quality led to gains in productivity and competitiveness were presented. Programs for middle management were jointly organized with the larger BSOs. The second component of the awareness programs consisted of preparing quality manuals. This activity was considered to have significant commercial potential. After the initial work of awareness creation, there was a strong possibility of building a sustainable enterprise sponsored by the Federation to provide services on quality improvement to industry. During the course of this work, individual businesses requested assistance on a fee paying basis to develop quality systems. One notable example was an export lapidary that was cutting and polishing emeralds and re-cutting heat treated sapphires from Thailand. The entrepreneur considered a quality management system to be an important improvement to his business. This sector was attracting foreign investors seeking joint venture partners to establish high quality cutting and finishing of imported stones. A few lapidaries had established a good reputation for high quality work. Meanwhile, the new

export sector in cutting and finishing diamonds was drawing attention to the skills available in Sri Lanka. The smaller lapidaries needed quality management systems and there was a high potential for services in this area. The beneficial spread effects of one satisfied customer were likely to be high.

The program was hampered by two issues from the start. Although the BSOs and business leaders were convinced of the need for a quality awareness program they were not clear how it should proceed - whether it should be general and broad based or focussed on specific sectors. Both aspects were seen to be important. The need for quality systems had to be spread throughout the business community. Competitors were improving product and service quality and increasing productivity, standards were being set for products entering specific markets. Therefore, all business needed to be aware of the changing requirements of entry and product performance. Some of this information was being provided through workshops and seminars, e.g. the EEC conducted a workshop assisted by the Federation, on new market entry conditions in Europe. The BSOs were not clear how the Federation sponsored activity to set up an enterprise for services in quality management would proceed - which BSO should take the lead, how oversight was to be provided, and what the links would be between the BSO quality awareness program and the SLSI.

Discussions were held with the SLSI before the quality awareness program was launched. The SLSI was already engaged in training industry and promoting standards and quality improvement. They also had the mandate for activities related to ISO 9000 standards. The quality awareness program of the Federation expected to strengthen links between the SLSI and industry. The awareness program was to be a joint effort between the Federation and the SLSI. Many professionals from the SLSI were resource persons to the workshops and seminars of this program. The BSO network was quickly able to extend the awareness program to a wide audience. Workshops were held for export oriented craftsmen producing brass and wooden handicrafts, for fruit and vegetable producers and for the gem and jewelry sector. However, the organizational arrangements between the SLSI and the Federation were not formalized and coordination was weak. Some opportunities were lost as a result.

The next stage of the program, preparing quality system manuals for enterprises was more demanding than the basic workshops. No work in this area had been done previously. Businessmen were unaware of the costs of developing systems specific to their firm and were hesitant to make the necessary investment. To sustain the activity, it had to be marketed and promoted like any other enterprise. This need was not clearly addressed when the program was launched. Meanwhile, other jurisdictional issues also emerged. The SLSI had the mandate to deal with programs and activities to promote quality and to establish standards. Some of the SLSI professionals were not completely convinced that a private sector program was necessary to deal with quality awareness. The SLSI also operated with serious fiscal constraints and was unable to develop an extensive outreach program to educate business about the need to improve quality to retain and extend markets, especially international markets. The full potential of the program was not realized as a result of these tensions.

The grant resources could have been utilized to improve the existing information flows and to strengthen organizational links between the SLSI and the BSOs. The program did achieve part of this objective. However, it surfaced other issues related to program assistance - the SLSI had difficulty in obtaining basic office equipment and publications to support out-reach activities, which the awareness program was able to obtain quickly with grant funds. There was a concern that effort would be duplicated, that the private sector would draw attention to itself and down play what the public sector agencies were already doing. In spite of these undercurrents of concern, the program had considerable outreach.

#### **(h) Industry and Research Linkage. The Gem Traders Association**

Very high potential for economic activities was identified in this sector. The EDB had many programs to develop designs, technology, marketing and production. New capacities were created for export oriented production in jewelry and gems. Other programs such as the work of the USAID Technology Initiative for the Private Sector, had also been developed to directly assist individual businesses in the sector to acquire and develop technology and marketing. The main features of the sector included:

- The major part of the sector consists of traditional businesses engaged in mining, production and exports. A large part of the transactions is carried out in parallel markets outside official and legal channels.
- New commercial enterprises had been established with foreign investment. They included high value cutting and polishing of stones, including diamonds, and contract jewelry making.
- Sri Lanka is an important source of investment quality and high value colored gem stones. But the base for value addition is quite small and commercial capacities need substantial improvement.
- A very large volume of raw material was exported to Thailand without any value addition. Almost all of it was Geuda which is obtained as a by-product in mining in Sri Lanka. This is a corundum which is heat treatable for color enhancement and yields sapphires. Within a decade, the heat treatment of Geuda has created a new, large scale gem and jewelry industry in Thailand, which has become a leading international center for heat treatment and a major market for the supply of jewelry and finished gem stones.
- Meanwhile, in Sri Lanka, capacity for heat treatment is dispersed and small scale. The volume of production is very low compared with raw material availability and exports.
- Heat treatment technology is not diffused. Research is being conducted at a few public sector agencies without the benefit of shared results and cross fertilization of ideas.
- A presidential commission has examined mechanisms to develop the sector. It recommended streamlining the regulatory functions and the creation of new institutions to assist with development. It also suggested the formation of a Gem and Jewelry Authority to replace the public sector agency the State Gem Corporation. It proposed the setting up of a Gem and Jewelry Exchange to facilitate trading. Some industry groups were promoting the concepts of a new state sponsored financial institution, the Gem Bank. The latter had support among some policy makers while the Presidential Commission on Finance and Banking felt that it would be expensive and inefficient.

The PSU assisted one of the leading BSOs in this sector, the Sri Lanka Gem Traders Association, with the intention of generating sector wide policy initiatives. An agenda for the sector was to be prepared and presented at a symposium held during the international gem and Jewelry exhibition, Facets 1991. The work was not completed in time as it required considerable organization and coordination of effort. One part of the agenda focussed on regulatory impediments and identified possible areas for remedial action. The agenda itself was prepared with inputs from public sector officials. This was considered to be a



useful means of obtaining the support of the public sector policy making agencies. The Association provided inputs to the work, but the final product fell short of meeting the objective of a document which would indicate new avenues for partnership, collaboration and policy dialogue to increase growth.

Meanwhile the association was engaged in important discussions to promote the Gem Bank and other regulatory reforms. A policy permitting imports was enacted in 1992. This increased imports of uncut or rough stones for value added activities and it provided new opportunities for the sector. However, the interests of different groups in the sector were not the same. The traditional gem trade had problems of liquidity and working capital. The geuda trade had provided a new source of funds for mining through the Thai traders who came in large number to purchase geuda. At the initial stages, the local traders were content to dispose of the material for which they found little commercial value or use. Little was also known about the use the Thais had for the material. In time a bi-lateral agreement was made between Sri Lanka and Thailand for the export of geuda. As knowledge of the use the Thai's were making of the raw material slowly grew, there was a strong backlash from producers, who wished to make use of the raw material themselves. Representations were made by groups to curtail exports of the geudas. Meanwhile, miners who enjoyed profits from the trade and high liquidity from the extraction of the traditional raw material wanted the prevailing arrangements to continue.

One major obstacle to the development of the gem and jewelry sector has been the limited supply of raw material. Sri Lanka has traditionally mined high value colored stones. Very little work has been done to develop a market for commercial sized colored gem stones. Meanwhile, the processing industry depended on the volume of the available raw material. The industry was of the view that nearly nine tenths of an average mining run produced material that was useful for commercial activity, the production of cut and polished small, calibrated sizes for mass market jewelry. However, a substantial proportion of the mined material was not directly usable for this purpose. The availability of more raw material is important for promoting rapid expansion of ancillary activities in cutting and polishing. The available skills were already drawing international investment to Sri Lanka. Small quantities of the Thai heat treated sapphires, from Sri Lankan raw material taken there, was sent back to Sri Lanka to be re-cut and polished. Traditional Sri Lankan practice of maintaining weight of stones, the caratage, was not conducive for a commercial market in gems. Closer links to the international market, especially for commercial gems was expected to have a strong positive impact on a range of ancillary activities including lapidaries. Traditional practices and craft skills had to change to meet international demand and the prevailing responses were slow. Heat treatment on a larger scale had the potential to trigger a wide range of connected commercial activity. A larger supply or availability of stones was needed to expand the market and to bring buyers to the country. The jewelry industry, still small in scale, would benefit from the increased supply of gem stones. Other constraints, such as the availability of precious metals, were being addressed by policy makers. Regulations and restrictions for importing gold had been relaxed but needed further change. Meanwhile, the traditional methods of disposing gems, especially the large underground market and resultant tax evasion, were strong obstacles to winning the favor of policy makers. Policies and action on many fronts were necessary to develop the market for gems and jewelry.

Heat treatment was seen as an important way of increasing the supply of usable stones. The EDB promoted heat treatment through subsidized credit for equipment and by developing training programs for heat treatment. Small operations for heat treatment emerged. Sri Lanka also started producing heat treatment equipment and adapting imported machinery.

An important issue in heat treatment was the identification of appropriate raw material. The type of treatment depended on the raw material. This knowledge was not well developed. The same raw material

was given different names by different users. Information on scientifically determined optimal treatment was not readily available to industry. Research at a few universities progressed without strong links to the industry. A small volume of contract work for individual businesses was carried out. The public sector institutions had a serious constraint in conducting experiments due to lack of funds for raw material. Thus the scientific community and industry worked largely in isolation.

A common research agenda seemed possible and necessary to hasten the development of heat treatment activity. The PSU presented the idea of a research agenda to a group of scientists already involved in heat treatment experiments, private sector participants in the gem sector and public officials dealing with the sector. It was met with strong support and acceptance. The objectives of the research agenda were to:

- Develop and standardize the information about heat treatment, including a common terminology for the raw material consistent with scientific knowledge.
- Conduct controlled experiments to determine most efficient and economically optimal color enhancing heat treatment methods.
- Share research information and present the findings at a national symposium.

The participants in a controlled experiment to evaluate different heat treatment methods were researchers from the University at Moratuwa, The Institute of Fundamental Studies, The Sri Lanka Institute for Science and Technology (formerly the CISIR) and a private exporting enterprise. The objective of the experiment was to identify efficient techniques, equipment and develop a uniform classification of color enhancable raw material. The standardized nomenclature for the different types of raw material that could be heat treated was a vital step in developing the gem sector. This was the first controlled experiment to compare techniques and the results of research carried out in Sri Lanka.

The heat treated material was valued independently by a panel from the State Gem Authority. The research was important in another respect. In the past, research agencies had not been able to acquire adequate raw material for experiments. However, the president of the Gem Traders Association, loaned a large quantity of raw material for the experiment. Furthermore, assurances were given that additional raw material would be made available based on the results of the experiments.

The work was conducted with a high degree of success and generated broad based satisfaction among the participant researchers and the members of the Gem and Jewelry industry. The most important impact of this work is the link between industry and research. Each group has increased its knowledge and awareness of possible collaboration. Earlier, there had been strong notions in the industry that technical problems in heat treatment e.g. choice of heat treatment equipment and identification of appropriate raw material, had been overcome. However, the pooling of information proved that some issues remained and had to be resolved through research and analysis. Similarly private enterprises in heat treatment had conducted their own experiments and learnt techniques at a high cost. They were not aware of the ongoing research at the universities and research facilities and the potential contribution these could make to industry. As a result many heat treaters in industry continued to make the same mistakes. Distributing capacity for heat treatment widely i.e. spreading it as a cottage industry without a strong information base could well have created an economic disaster. Many varieties of corundum exist and most of them undergo color changes when treated by controlled heat. The ranges of heat, the conversion ratios, the color changes to be expected, the proportions of success, all constitute necessary information for success in commercial ventures. However, all this is largely private information in Sri Lanka at present. Thai

business had the advantage of massive scale experimentation. It sets the market conditions. If it shifts supply away from blue to another color for sapphires, a marginal producer like Sri Lanka may find it difficult to dispose of its product. The flexibility of adapting to changing color fashions in the market for gems depends on scientific skill and knowledge. This coordinated and integrated research work makes a significant contribution to lowering production costs, improving quality and increasing market adaptability in this sector. Therefore, it has the potential of expanding the size of the market.

The work sponsored by the PSU provides a body of scientifically tested and codified information on raw materials suitable for heat treatment and color enhancement, the methods which are more successful in color conversion, the process of heat treatment, the equipment needed and the calibration of instruments. Many existing training programs for heat treatment, promoted the activity without providing information on the costs and the techno-economic factors involved.

### **(i) A Strategy For the Development of the Tea Sector**

Tea generates the largest net export revenue for Sri Lanka. However, the sector was losing its international competitiveness. Productivity was well below potential. Production costs were high. Strong political forces prevented the adoption of the necessary structural reforms. Most of the plantations were in the hands of the government. They were administered by two large corporations. Discussions and plans for restructuring management were under way when the project started. The private sector was consulted and participated in various committees examining options and policies relating to the restructuring of the plantations. The sector had been a major source of revenue for the government through export taxes. However, the two corporations incurred substantial losses which were underwritten by public sector banks.

Two important issues confronted the sector:

- Restructuring management, which would alter existing commercial relationships and benefits. Resident labor, represented by a minister in the government, was not mobile and there was strong political opposition to untying its links to the plantations.
- New investments were needed to improve the declining productivity of the sector. Technological improvements from planting to processing, were necessary. It was unlikely that the necessary capital could be mobilized within the country.

The Colombo Tea Traders Association (CTTA) is the primary representative of interests in the tea trade. It brings traders, producers, and brokers, and recently small holder producers and factory owners, together within one organization. It is one of the oldest trade associations in the country. Its origins date back to the colonial period. Some members of the CTTA are large foreign companies with a long history in the trade. The CTTA organizes the tea auction which is held at the premises of the Ceylon Chamber of Commerce. The CTTA works with public agencies to maintain rules and regulations governing the trade in and export of tea. The CTTA is affiliated to the Ceylon Chamber and generates substantial revenue for it through the tea auction.

Nationalization of foreign owned plantations in 1973 changed the management of tea production and trading. Bi-lateral trading agreements were made with a few countries. These opened new market opportunities for low grown tea, which had previously been low valued. The auction system continued

but bi-lateral arrangements with socialist countries and special sales were also conducted.

Some analysts contended that the interests of the CTTA did not coincide with those of primary producers and value added manufacturers. Meanwhile newspaper reports alleged collusion and unfair practices in trading but these allegations have not been substantiated. Clearly there were a few large traders at the auction with liquidity for transactions much greater than the others. But no review of the trading system, its strengths and weaknesses and the opportunities for improvement in it had been done. Discussions with the trade indicated that there was considerable scope for improvement and that internal discussion about various systems was needed.

In early 1991, the CTTA requested the PSU to help it to prepare a representation to the EDB to continue an export refinance scheme. This provided the opportunity to start a discussion with the CTTA and the Ceylon Chamber about broader issues affecting the sector. The industry was aware that the tea sector was faced with serious problems and required major structural reform. However, the private sector had not conducted its own review and prepared its responses to the crisis. Public officials and policy makers considered the existing consultative mechanisms to be adequate to discuss and resolve the issues facing the sector. This view, however, was not shared by most industry leaders. A true partnership had not been forged between the private and public sectors to energize and transform the sector. Besides, there were no mechanisms to reconcile the conflicting interests of producers, plantation labor, traders and value added exporters. Discussions with the industry indicated strong interest in examining the future prospects of the sector and the possible role that business could play in realizing the industry's potential. The leadership of the CTTA was convinced that the different groups in the sector needed a better understanding of the issues facing the sector. A strategic perspective was considered essential if the tea industry was to develop and improve its competitive position in the international market.

Plantation restructuring began with the award of management contracts. This was the first step in a process of divestiture. International firms had responded to the call for bids. There was political opposition to the award of contracts to firms from countries which competed with Sri Lanka. A case was made by some industry groups to protect the strategic national interest by restricting the entry of foreign investments to the sector. National management and entrepreneurial capacity were considered to be adequate to energize the sector. There were other fears. There was political opposition related to the potential impact of restructuring on the resident work force of Indian origin, especially the possible effects of displacement of labor on the rural economy. Political mobilization against restructuring was a constant threat. The sector evoked strong public emotions. Traders were viewed by some analysts as a rent earning class which did not contribute to the development of the sector. Reports on excessive earnings from trading, and on collusive practices were highlighted in the press.

A small holder sector had grown after nationalization of the plantations. It had a strong base in the southern part of the country. New markets based on these low grown teas had emerged and high export prices were being obtained. Producers expressed resentment towards traders during price slumps when they were hard pressed to maintain operations. Popular conceptions of trading as a purely rent seeking activity with little economic merit were voiced. Producers of tea, especially small holders, did not see their interests to be coincident with those of the traders.

The new management contracts for the plantations provided opportunities for direct sales by-passing the Colombo auction. Droughts and the civil disturbances during 1986-89 in the southern part of the country had disrupted production and maintenance. The small producers and factory owners were hard pressed to carry on activities. Meanwhile, a range of subsidies and state assistance programs for replanting,

fertilizer, credit and investment were gradually withdrawn.

The PSU presented a note on possible activity to the CTTA, to examine future prospects and possibilities for the sector and to mobilize other groups around it (See Appendix B). It was discussed with officials of the CTTA, and the Ceylon Chamber which acts as the secretariat for the CTTA. A subcommittee was appointed and work started. Short papers were commissioned to examine a range of issues including the auction system, prospects for value added activities in tea, and an overview of emerging political issues related to labor and small holder producers.

Meanwhile the CTTA took steps to improve the efficiency of the trading system. This activity was preceded by important actions by the CTTA. Rules of association were changed to broad base membership and to enable other important groups in the tea sector, such as the small holders associations and small factory owners to join. Criticisms expressed about the auction system were met with statements and reports about the merits of an auction system. How the specific system functioned and what improvements were possible had to be addressed. The CTTA decided that the rules of the auction had to be reviewed and measures to promote greater efficiency of transactions identified and implemented. The CTTA had the experience and capability to adapt itself to changing circumstances.

The strategy was intended to get the sector and its constituent parts to reflect on the pressing issues of the sector and how to resolve them. The discipline that the CTTA exerted on the membership through its rules of association, by-laws and committees is easy to overlook. There is a constant effort to maintain business ethics, and sustain contractual obligations among members. While perceptions of collusive practice are hard to dispel, the impact of a market place without the rules of trading is likely to be disastrous. During price booms, many new players were attracted to the trade. Informal contracts and price cutting existed. Imposing discipline in the market place was a major service performed by this BSO.

This activity provided an important opportunity for the different parts of the sector to review their roles and prospects for sectoral development. It created self awareness, and improved the base for informed discussion. It was a significant step for the private sector to develop a perspective of what was possible and the role they could play in improving the performance of the sector. Workshops were held to prepare the strategy study and brought industry groups together to discuss major issues facing the sector. This initiative increased the awareness of the industry about the context within which they operated, the interdependence between production, trading, value added manufacture and marketing. For the first time, the different private sector interest groups collectively reviewed the sector and examined strategic options for the future.

#### **(j) The Strategy for the Fruit and Vegetable Sector**

The Sri Lanka Vegetable Producers, Processors and Exporters Association was established with the assistance of the EDB. The close dialogue between the members and the EDB, enabled effective policies to be formulated and implemented. However, the rapidly expanding sector was encountering many serious constraints. Research and analysis was required to determine the future course of the sector. The Export Development Plan 1991-1995, prepared by the EDB, projected growth for the sector at rates based largely on the performance of the recent past. In spite of its name, the membership of the SLFVPEA consisted primarily of exporters who purchased a large part of their goods in the open market. Some supply links were formed but exports were not linked strongly to production. Market information relating to domestic supply as well as export market needs was not widely available. Individual exporters

established links with buyers and supplied to order. A few were quite successful and had pioneered new market niches. Many supply problems remained. Quality varied widely. A large part of the production of fresh fruits and vegetables perished before it reached the domestic market.

This sector linked the small scale producers to a potentially large export market, which yielded high returns. Discussions and research indicated that much of the potential was not utilized. After discussion with the SLFVPPEA, the PSU proposed that the association should develop a strategy for the sector. This should identify the prospects for growth and the major constraints on growth. It should also make proposals to overcome these constraints and set up an infrastructure for coordination of research and information flows and policy making. A grant was provided to the SLFVPPEA to commission a strategy for the sector.

A consultant to the association prepared the document. Drafts were circulated and discussed with the Department of national planning( which was preparing the national strategy for food and agriculture), the EDB and the department of agriculture. The proposals quickly gained the attention of policy makers dealing with the sector. The document gained acceptance by a broad coalition of policy makers and businesses in the sector as a plan of action. There were specific proposals for consultative processes. These were quickly organized. The strategy had prepared a phased plan for action based on a diagnosis of the major problems faced by exporters. It was noted that, in Sri Lanka, the link between production and exports was quite weak. Exporters shipped what was available. It was felt that the system of market signals, as well as the arrangements for disseminating them, should be strengthened. It was recognized that the system of production should be more market oriented. The document highlighted the need to assess the efforts in other countries of the region that had been successful in fruit and vegetable exports. Links between production, grading, packing, transport and export marketing were examined and recommendations made for action for improvement in a phased program. Using funds from the PSU, the association established their own office. It also began to develop a computerized information base of suppliers and members.

The strategy also stressed the need for the association to expand membership to include producers and producer associations. It recognized that the association could play an important part in expanding opportunities in the sector for other business participants. The BOI extended its incentives to the agriculture sector and promoted new export oriented ventures in agriculture. Export expansion required better market information. organization of production and supply for which strategic perspectives were essential. The strategy prepared with the PSU grant was the first step in this process. It examined the strategic opportunities for exports and made an assessment of the prospects for this export sector. Furthermore, it presented a framework for a partnership between private enterprise and the public sector to set priorities and goals to achieve the potential of this important export oriented sector.

### **(k) Conclusions**

The activities undertaken by the BSOs that were examined above illustrate possible mechanisms for policy dialogue on important economic issues. In spite of commonly held views that private sector organizations would not pursue common positions, they are interested and with assistance are capable of doing so. Timely assistance and advice plays an important role in facilitating this endeavor.

The PSU assisted the grant recipients with the policy activities they proposed to undertake. The PSU participated in developing the proposal and provided technical assistance to carry them out. Some BSOs

requested research assistance from the PSU for their representations. It provided the PSU with opportunities to discuss additional analytical activities the BSOs could undertake. The PSU prepared discussion papers for the BSOs to begin the process of activities which led to the formulation of sector strategies. The analytical resources needed to prepare them were not available within the BSOs and had to be obtained elsewhere. The PSU assisted many BSOs to identify analysts and researchers from other organizations. The networks connecting business and education are weak at present and can be considerably strengthened. The BSOs can play an important role in this process. The Industry Agenda and analytical activities related to them are preliminary steps in a process of creating awareness about the prospects for business and the major issues confronting it. The grant funding process provides an important mechanism for making these activities possible. However, finance was not the most critical constraint which prevented these activities from being undertaken. The opportunities had to be identified and presented to the BSOs. They responded very favorably to suggestions and opportunities which enabled them to examine sectoral prospects.

There is a strong likelihood that BSOs will continue to work with research organizations and analysts to prepare private sector strategies for particular sectors as a basis for policy dialogue. Programs of intervention which promote links between the BSOs, universities and the research community will considerably strengthen this activity. The public sector institutions will find such activities to be a very useful basis for a more effective formulation of policies.

These activities point to possibilities for further work to enhance the process of policy dialogue. Direct assistance to BSOs to access analytical skills and research will be an important task. Creating research departments or units may take considerable effort with little success in the short term. However, the process should be started to enable business to have organizational capacity to develop industry points of view, analysis and research on development issues affecting the private sector. Attention has to be given to increasing awareness among business persons at all levels about the advantages of being informed about the economic context for business.

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## Appendix A

### Establishing New Chambers

#### (a) Introduction

This appendix contains material developed by the PSU to help establish new chambers in its original form with minimal editing. The material is intended to provide the reader with a "road map" of the PSU's activities and contains notes and ideas that were presented to BSOs to improve their work. Establishing new chambers was only one part of the activities of the PSU. The major part of the activities of the PSU consisted of strengthening existing BSOs. This latter activity provided the PSU a framework to carry out its work to establish new chambers. Discussion papers that were presented to BSOs to develop their services and improve specific activities had utility for the new chambers as well. The focus on member services was found to be weak among some of the established BSOs. Assisting the new chambers to identify potential services, to assess member needs, to focus on the financial aspects of the organization were all considered to be very important if they were to succeed. Notes and discussion papers which were prepared in connection with the formation of new chambers are presented in this appendix.

The need for and the possibility of establishing new chambers was evident from the information that was gathered from the field. A small survey commissioned by the PSU and conducted by Survey Research Lanka, perhaps the first of its kind, indicated that a wide range of BSOs existed in small towns and cities across the country. A significant proportion of them could become more proficient organizations to provide services to the growing community of small business. The survey results are presented in I. The request for proposals related to the survey is included as II. Discussion papers given to the groups which got together to form the new provincial chambers. This document is item III of the appendix and examines issues related to the formation of a new chamber. A document on how to conduct a survey of member needs, given to new and existing BSOs is IV, notes from field meetings to set up new chambers is item V, a note on the fund raising effort for new BSOs is VI and the final item is a document on developing new chamber services prepared by the PSU and given to BSOs.

## An Assessment of the Service Capability of Business Associations in the Western Province

In 1991 the PSU commissioned a rapid appraisal of smaller BSOs in the Western Province. It was carried out by a market research firm, Survey Research Lanka Ltd.(SRL). The scope of work and the survey method was developed by the PSU and modified after preliminary field work by SRL. The primary objective of the survey was to obtain the main characteristics of the small BSOs which functioned in towns and cities throughout the country. The survey found that a large number of organizations of businessmen, offering a variety of services to business existed. Most collected money had significantly large memberships and were not visible to casual observers. They did not advertise their presence nor attract attention other than as providers of community service during times of religious festivals. Some of these organizations can quickly graduate to become efficient providers of business services. The following information is from the final report presented by SRL. The information below is indicative of activities and prospects for BSOs in the provinces and regional towns.

### 1. Population of Business Associations in the Western Province

On the basis of data received subsequent to the submission of the Final Report, the total number of business associations identified by the survey as currently operating in the Western Province is revised from 100 to 114.

These associations are distributed as follows:

Description	Colombo	Gampaha	Kalutara	Total
Traders (all types & sizes)	37	11	16	64
Three Wheeler Owners	11	5	2	18
Private Bus Operators	3	2	1	6
Taxi Drivers	4	5	3	12
Lorry Transporters	1	2	-	3
Ornamental Fish Breeders	1	-	-	1
Flower Pot Manufacturers	-	1	-	1
Bakery Owners	1	-	-	1
Milk Producers Co-op Societies	2	-	1	3
Poultry Farmers Co-op Societies	2	1	2	5
T O T A L	62	27	25	114

Bearing in mind the technique adopted for purposes of 'netting' the business associations in the survey location, the possibility of the field interviewers having missed a few is real.

It is estimated subjectively that the actual number of business associations of the type identified by the survey in the Western Province would be in the interval 125 j: 10.

## 2.8 Objectives of the Associations

Given below are the proportions of Associations which claim to have as their objectives the following:

To engage in social service activities	81%
To assist members financially	58%
To assist members non-financially	54%
To improve the business skills of members	65%
To make representations on behalf of members	31%

## 2.9 Representations

Although only 31% of the sample Associations indicated that "To make representations on behalf of members" is one of their objectives, the survey revealed that in actual fact 60% had done so.

Of this 60%, 40% had made representations to Local Authorities while the balance (60%) had discussions with higher authorities (e.g. Ministries)

## 2.10 Source of Funds

All the associations charge regular fees from their members 82% monthly and 18% annually. A little less than 80% of the associations also charge an 'entrance fee'.

Only 26% of the associations have sources of funds other than fees from members.

Bank Accounts are owned by a little less than two-thirds of the associations.

The 'entrance fees' charged by associations are distributed as follows:

Less than Rs 50	- 67%
Between Rs 51 & 100	- 20%
Between Rs 101 & 250	- 13%

The annual membership fees of the association are distributed as follows:

Less than Rs 100	- 26%
Between Rs 101 & 300	58%
More than Rs 300	- 16%

Given below is the distribution of associations based on their estimated annual receipts by way of membership fees.

Less than Rs 10,000	29%
Between Rs 10,000 & 50,000	29%
Between Rs 50,000 & 100,000	24%
More than Rs 100,000	16%

According to the findings of the survey, the average annual receipts per Association from membership fees is Rs 86,000.

Hence, if the total number of Associations in the Western Province is fixed at 125# the total amount collected annually from all members of such associations would exceed Rs 10.75 million.

2.11 Links

Only 25% of the Associations have any links with similar or related associations.

2.12 Services to Members

Given below are the proportions of associations which described their current and future range of services to members as follows:

Current Services

Financial assistance to members to meet funeral expenses	35%
Financial assistance to members for other purposes	25%
Other types of assistance to members	45%
Issue of identity cards to members	5%
Assistance to members to improve their business	20%

Future Services

* Self Employment Training Program	5%
* Pension Scheme for members	5%
* Skill Enhancement training Program	5%
* Compensation Scheme for Disabled members	5%
* Loan Scheme for members	15%
* To obtain credit facilities for members	5%

## II

### **Developing a Regular Market Survey to Assess Service Capacity of Business Associations**

#### **Request for Proposals**

The Private Sector Policy Support Unit, wishes competent and qualified enterprises to submit a proposal for the activity described below. The proposal should be available by the 12<sup>th</sup> August 1991. It should contain a time frame for the various activities, a budget and a delivery date. The preferred time schedule for the task is for all activities to be completed within three calendar months. The results would be presented incrementally as the survey consists of four stand alone efforts.

#### Background

There is very little assembled information about the spread and the activities of private sector associations. However, small scale investigations indicate that there is a wide institutional variety supporting and representing private business enterprise. These institutions do not seem to be operating on the basis of services to members. Membership dues of a small quantity are usually charged but there does not appear to be a clear indication and an acceptance, by the management of these institutions, of responsibility to provide services to members. Private enterprise requires information and services to perform efficiently. Some of the services have to be generated by the private sector itself. A dynamic private sector requires an efficient institutional support system which is dedicated and equipped to provide appropriate services. A "market survey" of associations and the services they provide is needed to assist in this task.

Voluntary associations of varying capacity and ability serve the private sector business community. They are part of an old tradition and form wide networks of associations and institutions. Most of these associations are not linked to each other functionally. There is no clear hierarchy of association with progressively higher levels of representation and wider spread of activity. However, the general operating characteristics of these organizations have common features. Many of the smaller associations are involved primarily in producing social service products. Support to enterprises are not widely supplied and representation functions are mostly ad hoc. Most associations depend on a few strong individuals to give it direction. They are most likely to produce social goods and services. These are not services and goods which are related directly to the improvement of the enterprises. They tend to be for the consumption and direct benefit of the larger public and tend to obtain publicity for the particular business group. This type of association is not yet self confident to begin providing services to the membership. Civic services tend to dominate the activities of these associations. There are some which operate revolving credit funds, represent members to formal financial institutions and get involve in civic activities.

The public sector provides many services to the business community. These services are of special significance in the rural sector. Information and extension services are organized and

delivered by public agencies and institutions. The business community tends to organize itself to articulate needs and wants, to represent needs to the government. However, institutional links with reciprocity is not wide spread. The public sector tends to assist in the formation of some associations. However, they tend to quickly become clients for public sector services without adequate independent capability. Besides the chambers and associations that are located in Colombo, traders and businessmen form associations in small towns and urban centers.

The private sector is expected to bear an increasing proportion of the responsibility to promote growth and diversification of the economy. This requires the expansion of services available to enterprise. The state sector, meanwhile, is seeking means to reduce expenditure and to pass on costs of services to customers. Within this changed context, the private sector business associations would have to provide a range of new services to the business clients. The scope to produce and supply business services, to a range of enterprises both large and small, is very large. However, it is necessary to identify existing capabilities of the various associations and institutions servicing the private sector.

### **The Market Survey**

It is unlikely that a one time enquiry would be sufficient to gain an understanding of the market for business services and provide information on how supply can be organized and delivered by the private sector. The market would have to be assessed regularly. It may be possible to institutionalize this activity within the established chamber network. Considerable gains in the use of resources may be possible. At present, the chambers and associations in Colombo are not strongly linked to those based outside Colombo. However, many large businesses located outside Colombo are represented by one or more Colombo based business association. But more may be possible in terms of links and networked activities with the associations in other towns.

There is very little information about the membership and activities of the associations in the small towns and the rural sector. A "market survey" is one way of assessing what exists and what may be possible in the near to medium term.

The proposed market survey of business associations and chambers of commerce would have two parts. The first would examine the "products" made and used by the Colombo based associations and chambers. It would examine the membership base, the line of "products" and services that are prepared by these institutions, the "inputs" used and the packaging that is undertaken. The separation of the Colombo based chambers from others is for convenience. Many share common features with those in the provinces.

The chambers of commerce offer a wider range of services than do most associations. They provide both member specific as well as general customer services. This part of the market survey would list out activities, their scale and their scope. The two large chambers, Ceylon and the National provide many specialized services. The CCC holds the Auctions for Export Tree Crops. It certifies documents as does the National Chamber. The NCC has had a strong business in Measurement Certification. This activity is on the decline following the rapid move towards

the use of containers. In additions to these activities, the chambers are an important source for trade information and trade enquiries.

The chambers and Business Associations perform an important task in "assembling" parts of the business enterprise. Although they do not provide a "full service", with modest inputs and organization it is possible to significantly increase the service base.

The proposed survey would examine service products at the design stage. The chambers are in the process of expanding activities and developing a new product range.

The second component of the survey will develop typologies of business association in the provinces. It would also identify the operating characteristics of the associations that service the small and medium sized enterprises. We would be interested in looking at the present scale of operation, scope of activity, the commercial orientation; fees and charges if any, for services. An overview of the services provided by public agencies would also be provided. This would include the activities of the IDB, the Commerce Department, the Industries Ministry etc.

This market survey component would not be able to span the entire population or the entire "universe". To develop the principles and methodology, we will begin with Kandy, Galle, Matara and the outer perimeter of the Western Province. We presume that a very large proportion of organized commercial activity would be spanned by these areas.

The PSU is examining means to conduct regular surveys that enable the chambers and associations to assess the market for their products. At one level the chambers would be supplying an established clientele. On the other, they become aware of a growing market, especially among a new client group, the small associations in the provincial and small town settings. We will be interested in knowing who is "producing" what, how and for whom. The survey would also identify potentials for market development.

The time frame for the proposed activity is three months. The market survey design would be submitted in draft for discussion within the first week. During the second week the survey methods and instruments would be checked and calibrated. The expected output would be in the form of a report which would categorize and list all chambers and associations in the selected area. It would identify the products of the institution, the size of the market that is supplied, the potential client base. An overview of the association finance and income will be included. Wherever the association produces for sale, the inputs used, staff, equipment, site and other material would be identified along with a clear valuation.

(prepared by Nimal Gunatilleke 1990)



### III

#### NOTE: Issues Related to the Formation of a Chamber.

(This note was adapted for specific provinces)

At the initial stage a core group consisting of members from leading commercial establishments have voluntarily associated to assist in the formation of the chamber. They have contributed to the work that has gone in to organize the chamber. They are now at the stage of deciding on the membership and the mechanisms which will gather a critical mass of businessmen together in the chamber. Who should be informed, how many should be invited to join at the initial stage, what considerations should apply? This note outlines a few issues that may assist in the task of membership gathering.

#### **1. Who should be in the Chamber?**

The chamber in the broadest sense would seek to harbor, service and represent the business community in the Province. The chamber is formed to provide a service and to assist enterprise of the private sector. Can the entirety of the private sector be collected, represented and serviced through one institution which is yet to be formed? It is unlikely that all interests and needs could be serviced through one institution. Where can the task begin? The purpose is to be "aggregative", to be "inclusive" to assist those who would have a significant collective impact and to do it efficiently and productively within realistic bounds of resource costs.

All businesses cannot be quickly and efficiently organized into a chamber in a short time. The diversity of interests could weaken the new organization and dilute the impact of the services it undertakes. On the other hand if the new organization is narrow and restrictive in its membership it may be hampered in performing the tasks of a chamber. If you begin with a diversity of interests based on sectors, size of enterprise and other operating characteristics, the initial agenda will not be easily defined and members will tend to fall off in their enthusiasm and support.

One possible step would be to begin with:

- Enterprises and businessmen who will collectively account for a large proportion of the commercial strength in and the vicinity. Proven business leaders, accepted by the community of businessmen to be successful, resourceful, dynamic, interested in promoting business concerns for the sector, the region;
- Pay attention to special concerns of diversity, leaving out prominent or important businessmen may not be prudent;
- Young and relatively new entrepreneurs;
- Manufacturing businesses;
- Businesses producing for exports, contemplating or capable of producing for exports;
- Those who have investible surpluses and may be looking at opportunities to expand, develop or initiate new enterprises;

- Businessmen who reflect the regional specializations, in agriculture processing (e.g. Tea, Fisheries related, Coconut related, Paddy, vegetables), industries, services and trading.

These characteristics offer a guide to inviting the initial membership.

It will then be possible to form a Board, inviting a few (15 or so) of the prominent, leading, important members who have agreed to join. The board will provide the leadership and the overall management guidance to the chamber.

## 2. How many persons should be invited initially?

Clearly, the number should be a manageable one. If the initial membership is too small and not adequate to form the nucleus of a effective chamber, then getting more members would be harder. If it is very large and contains many who expect services that take a while to assemble and deliver, there will be a rapid depletion of the member base. While the large number will initially give the impression of institutional strength, it will hide the demand "overhang" - a large potential burden to service clients without installed capacity.

The initial number should be adequate to :-

1. Begin operations;
2. Represent a significant share of important parts of private enterprise;
3. A critical mass which will quickly attract other business groups.

The number should be decided on the contribution to the rapid growth of the institution, the chamber. A few discussions among members of the core group would be useful in this matter. Business strength should be an important concern.

## 3. How can small and medium enterprises be represented?

Once the core group begins organizational work, and the chamber is formed, it will be useful to consider the agenda for the first year. An outreach program to bring in some of the small and medium scale enterprises should be considered. In this regard, an intermediate level of representation through associations should be considered. Even at the initial stage it will be useful to have under the umbrella of the chamber, those who are vocal, visible and can be mobilized quickly. Here is one example, the traders' association(s) in the town are likely to have many needs and demands that they now try to meet through different channels - local government, access to political authority etc. The chamber can become a forum to represent, resolve a host of issues related to public access, waste disposal, etc. For example the Municipal council would have a number of outstanding issues that they wish to resolve together with the police and the traders - these include the use of the main street frontage and the area in the vicinity of the main bus stand. The chamber can take the issue of making the town an efficient, clean well functioning unit catering to different forms and size of businesses. The business community can find expression through the chamber on practical matters and represent their cases to the appropriate decision making level which can at the same time be held accountable because of the larger representation of the chamber - a larger pressure group, the effort is a chamber activity. At the initial stage activities of this type can help to develop the chamber's image, with a theme such as Representation of Business for Constructive Action.

Bringing in associations is important to make the chamber a true representative of business in the province. It will be important to avoid the image of a small, exclusive "club" where "only the big and the powerful meet to organize more advantages for themselves".

It is perhaps counterproductive to directly bring the small enterprises into the chamber. It may be better to encourage group formation and institution building by paving the way for associations to come into the chamber. A parallel effort to link up with organizations which represent small and medium enterprise can be undertaken. Already an organization has been formed to assist this sector. It can bring in associations to the chamber for screening and possible membership. It will be useful to have a few such associations at the start. It will help the managers to assess the types of needs and demands which the chamber may consider servicing.

However, it may be wise to think strategically and within the "big" picture. After all this effort is historic!

#### **4. On Member Contributions and Fees.**

It is useful to consider a few options when deciding on the chamber entry fee. First, the fee or the price will be associated with a service which will be given sooner than later. The "prestige value" of joining will be a very short lived factor unless the chamber can gain access to decision making institutions and obtain redress in visible and important ways. Furthermore if the chamber has an initial membership which is considered a "good, strong group" capable of organization and obtaining results based on the success in the field of business, it will inspire confidence and encourage others to seek entry. The price should inspire confidence that something can and will be done through the chamber, that it is worth the investment and that prominent members of the business community have made contributions and joined. (The news will spread informally however quiet the chamber is about it!)

There is a great advantage for this chamber that should be exploited fully. It is the first to be formed outside Colombo, the effort is therefore a historic and endeavor. The membership drive should stress this.

#### **5. Legal Status of the Chamber : Some Options.**

In creating a suitable legal status for the proposed chamber, a couple of options exist : incorporating the chamber or functioning without incorporation. If the membership decides to incorporate the chamber it is possible to do so through the Registrar of Companies or by an Act of Parliament. In the event that it is decided to function without incorporation, there is sufficient precedent to indicate that several business associations including the National Exporters Association, the Chamber of Small Industries amongst others, continue to function very successfully in this manner. However, in lieu of several advantages to be secured, incorporation under the Companies Act No. 17 of 1982 as a non-profit business organization remains an appropriate measure. Some of these advantages are the possibility to conduct business on a more certain and legal footing, particularly with foreign clients, and the possibility to serve as the "umbrella" organization for the numerous smaller business associations that exist. The latter advantage is particularly relevant in presenting the views of the business community in a manageable, coherent and effective manner.

(prepared by Nimal Gunatilleke, PSU 1990)

**NEEDS SURVEY  
OF  
POTENTIAL CHAMBER MEMBERS**

1. DO YOU HAVE REGULAR MEETINGS WITH OTHER BUSINESSMEN? (PLEASE TICK APPROPRIATE ANSWER) YES.... NO ....
2. HAVE YOU MADE REPRESENTATIONS TO THE GOVERNMENT ON YOUR OWN ? YES ..... NO ....
3. WHICH SECTORS AND GROUPS OF BUSINESSMEN DO YOU THINK OUGHT TO BE IN THE CHAMBER? (PLEASE NOTE DOWN)  
.....  
.....
4. WHICH SECTORS AND GROUPS OF BUSINESSMEN, IF ANY, DO YOU THINK SHOULD NOT BE DIRECTLY BROUGHT IN TO THE CHAMBER?  
.....  
.....
5. WHY WOULD YOU LIKE TO SEE A CHAMBER FORMED?  
  
GIVE STRONGER IDENTITY TO THE BUSINESS COMMUNITY YES ... NO...  
ENABLE EFFECTIVE COMMUNICATION WITH GOVERNMENT YES ... NO ...  
STRENGTHEN POSITION OF PRIVATE ENTERPRISE YES ... NO ...  
  
OTHER .....
6. DO YOU OBTAIN BUSINESS RELATED PUBLICATIONS REGULARLY?  
YES ..... NO .....
7. DO YOU SUBSCRIBE TO A BUSINESS INFORMATION SERVICE?  
YES .... NO ....
8. DO YOU FIND THE INFORMATION YOU RECEIVE USEFUL?  
YES ..... NO .....
9. DO YOU SEEK INFORMATION ABOUT MARKET OPPORTUNITIES?  
YES .... NO .....

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10. WILL YOU SEEK INFORMATION FROM THE CHAMBER? YES ... NO ...

In order to design the activities of a chamber, the following types of information along with your views given above will be very valuable. As you well know, the chamber will have to provide services to a membership. What the members want and may want depends on how well the chamber staff know the needs of the members. Member profiles are a useful way to do this. Initially some basic items of information can be gathered, and developed later by sub-sector.

**MEMBER PROFILE**

1. ORGANIZATION TYPE :

- A. ASSOCIATION OF BUSINESSMEN
- B. PUBLIC QUOTED COMPANY
- C. PARTNERSHIP WITH LOCAL COLLABORATION
- D. PARTNERSHIP WITH FOREIGN COLLABORATION
- E. FAMILY OWNED
- F. SINGLE OWNER PROPRIETORSHIP
- G. OTHER

2. TYPE OF BUSINESS :

- A. AGRICULTURE PRODUCTION
- B. AGRICULTURE PROCESSING
- C. MANUFACTURING
- D. HANDICRAFT
- E. WHOLESALE
- F. RETAIL
- G. TRANSPORT
- H. OTHER.....

3. PRINCIPAL ACTIVITY WITH AVERAGE ANNUAL PRODUCTION/TURNOVER :

	PRODUCTION/TURNOVER	EXPORTS
A. AGRICULTURE .....	.....	.....
B. INDUSTRY .....	.....	.....
C. TRADE .....	.....	.....
D. TRANSPORT .....	.....	.....
E. FINANCE .....	.....	.....
F. EXPORT .....	.....	.....
G. OTHER .....	.....	.....

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4. SECONDARY ACTIVITY WITH AVERAGE ANNUAL PRODUCTION/TURNOVER:

.....

5. ESTIMATED VALUE OF CAPITAL AND ASSETS .....

6. TOTAL NUMBER OF EMPLOYEES :

A. MANAGEMENT ....

B. UNSKILLED ....

7. IF PRODUCTION IS EXPORT RELATED :

A. PRINCIPAL EXPORTABLE PRODUCTS

B. ANNUAL PRODUCTION AND EXPORT CAPACITY

C. EXPORTS IN PAST THREE YEARS WITH COUNTRY OF DESTINATION AND VALUE

YEAR	COUNTRY 1	COUNTRY 2	COUNTRY 3
.....	.....	.....	.....
.....	.....	.....	.....
.....	.....	.....	.....

8. CONSTRAINTS AND PROBLEMS RELATED TO EXPORT/MANUFACTURE OF PRODUCTS ?

ACCESS TO MARKETS?

ACCESS TO RAW MATERIAL?

ACCESS TO WORKING CAPITAL?

ACCESS TO INVESTMENT CAPITAL?

TELEPHONE?

TRANSPORT?

WATER ?

ELECTRICITY?

9. ARE YOU PLANNING TO MAKE NEW INVESTMENTS? IN THE SAME LINE OF OPERATION.... NEW VENTURE .....

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10. TYPE OF INVESTMENT

BUILDING..... MACHINERY .....  
OTHER..... TRANSPORT EQUIPMENT.....

NOTE: THE QUESTIONS RELATE TO BROAD CATEGORIES AND SOLICIT ANSWERS ONLY IN RELATION TO DEGREE, EXCEPT IN THE CATEGORIES RELATING TO VALUES. THIS INFORMATION CAN BE VERY USEFUL FOR DESIGNING CHAMBER SERVICES. FOR EXAMPLE ONCE IT IS KNOWN THAT A GOOD PROPORTION OF THE MEMBERS IN MANUFACTURING ARE CONTEMPLATING INVESTMENTS IN BUILDINGS, THEN INFORMATION ON DESIGN, COSTS OF INPUTS, BUSINESSES THAT CAN SUPPLY SERVICES, ALL FORM AN INFORMATION BASE THAT IS NECESSARY TO THESE BUSINESSMEN. SIMILARLY, THE SECTORS, e.g. MINOR EXPORT CROP TRADING WILL BE INTERESTED IN PRICES, EXPORT OPPORTUNITIES. IN THIS MANNER A "INFORMATION SENSITIVITY" CAN BE DEVELOPED IN THE CHAMBER AND A SET OF INFORMATION TO SERVICE THE CLIENTS IS DEVELOPED. CLEARLY WHAT IS DONE WILL DEPEND ON PRIORITIES AND ADVANTAGES THAT ARE IDENTIFIED LOCALLY.

(Prepared by Nimal Gunatilleke PSU, 1991)



## Notes From Meetings with the Initiating Groups Provincial Chambers.

### 1. The Southern Province

#### Dates Visited.

Nov. 30/90, Dec. 4-7/90, Jan 23/91, Feb. 7/91, Feb 21/91, Feb 27- 03/91.

The PSU has been working with a group of businessmen from Matara who are working towards a chamber for the southern province. The coordination at Matara is by Mr. S. Ranaweera of the firm of Chartered Accountants, Ranaweera & Nagasinghe.

After an initial meeting with Mr. Ranaweera in Matara and his partner Mr. Nagasinghe in Colombo, the PSU organized a meeting of businessmen in Matara. Thirty five leading businessmen from Matara attended and indicated serious interest in establishing an institution to serve the private sector business community.

At this meeting the PSU explained its purpose and mandate. The PSU stated that it would seriously consider assisting the program of an new institution, if it were to be formed in the southern province. The businessmen outlined a range of the business service needed and explored the prospects of an institution to provide them. A small working committee was formed and would begin the work to formalize the institution.

At the subsequent meetings in Matara, the PSU discussed the registration and incorporation of the institution. The working committee expressed the desire to form a chamber and to call it the South Lanka Chamber of Commerce. The PSU impressed upon the committee, that it would have to draw leading businessmen from other areas of the south if it were to maintain the coverage. Furthermore, the PSU indicated the need to consider the member base of the proposed chamber in order to have institutional as well as financial viability. The numbers had to be large enough to be a strong representation of business interests of the province. The PSU provided a document outlining principal issues to consider in the formation of a chamber. ( See Document. Note: Issues Related to the formation of a Chamber ..) The PSU reiterated the importance of developing services to the membership. This would mean profiling the members, finding out their needs and developing appropriate services to them.

The PSU visited and established contact with the Ruhuna University. Discussions were held with the head of the Department of history and Economics, the Dean of the Faculty of Humanities and Social Sciences. The university indicated serious interest in the issues related to the private sector. They would be interested and capable of providing a range of research and information services to the new institution as well as to business enterprises in the province. The PSU discussed the southern province development strategy and the possible role for the university. The university can be a vital institution to discuss and disseminate considered views about private sector development and investment in the province.

During 27 February to 3 March, the PSU met with the committee to assist them in developing the work plan, to demonstrate office set up, chamber service provision. The entire staff of the PSU was present.

The working committee representatives met the PSU on Friday the 15 March to discuss the work proposal. They have planned to meet with businessmen in Galle and Hambantota.

## 2. The Central Province Chamber of Commerce and Industry.

The provincial government has taken the initiative to form a chamber. It has used the resources of the provincial ministries, to supply services to assist in the formation. The endeavor began with the chief minister and some of his senior staff organizing a meeting of leading businessmen from the province on the January 12, 1991, to discuss the formation of a chamber.

The invitations were sent out by the public sector commercial banks. They selected from their clients and their knowledge of enterprises. A total of approximately 100 invitations were sent out and 82 persons from all three districts attended.

The chief minister addressing the businessmen, impressed upon them the value of a chamber and how it can assist in gathering and delivering services of the public sector. A chamber will enable businessmen to gather and discuss common needs, present views to government and to organize demand for a range of business services. This opportunity, according to the chief minister, had to be utilized to develop capabilities and institutional strength of the private sector with significant assistance from the provincial government. The public sector will play a facilitating role, the chamber initiative will have to be primarily from the private sector. The chamber will be a useful institution only if it can provide services which will help members in business.

The chief secretary of the provincial council Mr. S.D. Rajapakse initiated the meeting. He informed the businessmen that there were 10-15 business associations in town. They interacted with the local government and addressed specific interests of businessmen, primarily traders operating in the town and its vicinity. For larger scale activity higher level of organization and institutional strength was needed. A chamber would be an important institution to which foreign enterprise as well as local enterprise will visit to directly find out about businessmen's views. A range of training needs for improved enterprise performance can be identified and services organized through a well functioning chamber.

Dr. Cochrane COP of the PSU, introduced the PSU and its mandate. He outlined the types of assistance the PSU provided to chambers and business associations to strengthen their institutions, technical assistance to prepare policy representations and improve research capacity and to develop business services. There were no chambers outside Colombo which functioned to promote and facilitate private enterprise. There were important market opportunities for a chamber in the provinces. There was a wide range of services that can be provided. They included information about investment opportunities, government regulations and policies, that had to be supplied quickly to the business community. A chamber had to demonstrate its usefulness to a membership through demand driven services. It must perform services which businessmen cannot perform for themselves. Neither can the public sector provide these services efficiently because it is not able to understand the needs of private business as a chamber or business organization would. The government is enthusiastic about chambers. The chamber can become an important institution to channel representations to government, it would discuss with the

members about the issues in exports, imports, taxes and tariffs. A convincing representation will require information and data that resides with the business community.

It was explained that the Industrial Promotion Act would provide new opportunities for private sector institutions such as chambers and associations to represent business. The regional bodies for industrial promotion will be another opportunity for the provincial chambers. The PSU intended to assist the private sector support group for the council. The businessmen's interests are necessary for the country, and it was being recognized. Overseas investors need a realistic assessment and turn to the local business community.

Finally the PSU mandate was reiterated, a three year life span and grant assistance based on assessment of capability of the association. The PSU would consider assistance with setting up the office, the member support and volunteer effort was shown to be vital for setting up the chamber.

The PSU indicated that it would be useful to form a small action committee, to take up the issues of the chamber formation. This group met the same afternoon and decided to formulate the articles of association and Memorandum of Association. The PSU sent copies of sample articles to the Chief Secretary.

#### Meeting # 2.

15 businessmen in the committee, the Chief Secretary, and the secretary Min. of Local Government, Education, Industry and Animal Husbandry.

PSU participation. Dr. Cochrane, Mr. Nugawela and Dr. Gunatilleke.

On the 17<sup>th</sup> of March the committee met to discuss the draft constitution. each clause and item was taken up for discussion. Changes were made to the draft with respect to the powers; formation of district or special area branches, including associations in the membership, operating a bank account,

Changes were noted with respect to the composition of the committee, it would have representatives from the three districts, 4 for Kandy, two each for the other two, the president and the two vice presidents from the three districts.

The operating language of the proposed chamber will reflect the needs of the members.

The discussion included the minimum size of the forming member group and the financial considerations. A small group may not be able to generate the business strength as well as the financial capability to undertake the member services. Therefore it is necessary to get a number large enough to give the activity momentum and to prevent another group forming an institution in competition.

Comments: This meeting was the result of joint work between a small group of businessmen and Mr. Weerasekera. The business group is willing to take a back seat and let the organizational work be done by the government officials. What they may find difficult to do is to change the agenda of work unless they define it and take a leadership role. The chamber can very easily become a small and ineffective

organization. The public sector officials have good ideas for the chamber. However all of them are related to training, seminars and workshops for the general business community - somewhat like public goods and not demand driven member services.

### 3. The North Western Province.

13<sup>th</sup> February.

The PSU (Dr. G. Cochrane, Mr. D. Nugawela and Dr. Nimal Gunatilleke) visited the chief minister Mr. Gamini Jayawickrema Perera. He introduced the president and secretary of the Chamber organizing committee, along with the Director of the Industrial Services Bureau. This chamber has started with strong assistance and direction from the chief minister. The effort has got wide publicity in other provinces, public sector circles and in the chamber community in Colombo. The office bearers have been suggested by him. They are young and somewhat diffident about their role.

At the meeting Dr. Cochrane explained the PSU project and the activities it supports and undertakes. It was stated that the PSU would seriously consider assisting provincial chambers, to develop the institution, to improve services to members and to obtain specialized technical assistance. The Chief Minister explained the need for a strong private sector, and an institution to service it. The ISB is seen as an important institution which would provide some of the required services. There are strong expectations that the it can perform an important role in the activities of the chamber.

The PSU visited the ISB and the demonstration and training center associated with it.

The PSU discussed the need to expedite the formation of the chamber with the organizing committee. The PSU offered to send copies of articles of association of the Ceylon and National Chambers.

Meeting # 2 20<sup>th</sup> February.

Present. Organizing committee and 15 businessmen. PSU, Konrad Adenauer Stiftung, the SMED/FNS rep. The Federation, the National Chamber of Industries, the Chamber of Small Industries and the director of the ISB.

The Colombo based chambers introduced themselves and explained the work they do, representation was a major area of their activity and was based on the access they had to decision making. They operated on the basis of task oriented committees.

During the course of the discussion, one of the major issues was how diverse interests could be accommodated within a chamber. The PSU stressed the principle of collecting a large share of business and enterprise strength was pointed out to be an important consideration in determining the initial membership. A diverse membership may have different needs and requirements. But getting a good cross section of the business enterprise in the province was necessary and as the chambers in Colombo had done, they could be serviced through committees.

Organizing Committee. Chairman . Mr. Asita Gunasekera. Secretary Mr. Manjula Narayana.

## VI

### The Fund Raising Effort for New Chambers and BSOs

The Chamber will need funds to operate. Providing services to the members, the primary purpose of the chamber, will require people, ideas, and finances. The quantity of funding depends on the work that is planned. An office has to be set up, operational staff hired, and activities undertaken on a regular basis. The core group will have to assess the financial needs at the start.

The operating funds for the chamber will be obtained from different sources. Member contributions from subscriptions, fees and payments for specialized services will form one component. How much can and needs to be raised will depend on the size and economic strength of the membership. All operating funds might not be obtained from member contributions. Special activities for a larger clientele, regular seminars and workshops can be other sources of funding. These activities will require planning, ideas and execution.

**The chamber is a new enterprise** and therefore will not have a proven record of achievement. Getting members to join will be an important activity in itself. It will be useful to consider the financial implications of size and spread of membership for the purpose of planning the operations of the chamber.

Outlined below is a simple illustration of internal generation of funds.

<u>Member Strength</u>	<u>Fee</u>	<u>Annual Fund</u>
1. 30	Annual Rs. 500 Annual Rs. 2,000	Rs. 15,000 Rs. 60,000
2. 50	Annual Rs. 500 Annual Rs. 2,000	Rs. 25,000 Rs. 100,000
3. 75	Annual Rs. 500 Annual Rs. 2,000	Rs. 37,500 Rs. 150,000
4. 100	Annual Rs. 500 Annual Rs. 2,000	Rs. 50,000 Rs. 200,000

The chamber will require an initial fund. It will have to be raised from the membership at inception along with the regular subscription. This fund will be needed for setting up the chamber office, recruiting personnel and obtaining equipment along with other operating costs.

For the chamber to be viable and efficient will require a paid staff along with advisory assistance from the membership. The paid staff will man the operational posts and service the members on a regular basis. Even on modest assumptions a staff of five persons will require a budget of approximately Rs. 300 - 350,000. This is without the necessary costs of setting up an office - renting space, obtaining office equipment and supplies.

If the chamber services the Southern province, it will have to cover the territory of the three districts, Galle, Matara and Hambantota. There will be special and different needs of the businessmen in these areas. For wide representation, the chamber will require a capacity to address the needs of different types of businesses. The capabilities and the staff of the chamber will have to be designed appropriately.

The financial implications of the proposed venture will emerge from an assessment of the anticipated coverage, the initial membership and the short-medium term goals and the associated work plan.

Prepared by Nimal G. Gunatilleke. 03.02.1991

## VII

### **Introduction to Developing Chamber Services (Prepared for the Central Province Chamber)**

The Central Province Chamber will have a number of tasks to perform. Among these would be the task of offering a variety of services to its membership. While the details of the services that could be offered will depend on the membership profile, and needs articulated by the membership, two broad areas of activity that the chamber will need to be engaged in can be identified at this stage. These areas are, (a) Representational activities, and (b) Information gathering, processing and dissemination.

(a) **The Representational functions** of the chamber will involve promoting private sector interest in the Central Province. It will be important for the chamber to establish and maintain cordial relations with the provincial government. It is likely that at the provincial level the private sector will have to work very closely with the public sector. As such, good relations must be maintained at all times, so that constructive and fruitful dialogue can be engaged in. The role of the chamber in facilitating this will be critical.

(b) **Information Gathering** - The chamber should gather, store and disseminate a variety of information that is important to its membership. Some initial categories of information that the chamber might collect are as follows :

- (1) Commodity and agricultural products in the Central Province;
- (2) Market reports on specific products and items in the Central Province;
- (3) Statistical data on the province's products and the economy at large;
- (4) Trade and commercial news including information on activities in the province, Sri Lanka and the international setting;
- (5) Industrial and technological information;
- (6) Product reports;
- (7) Trade directories;
- (8) Shipping information;
- (9) Activities of the Central Province Chamber and other chambers.

#### **(1) COMMODITIES/AGRICULTURE**

A variety of information relating to agriculture and other commodities should be collected by the chamber. It is very likely that quite a large percentage of the chamber members will be involved with these two sectors, and would like to draw on this information. The information can in most cases be obtained quite easily. It is important to focus on commodities and agricultural products that are of relevance to the Central Province.

Information can be collected in the following categories.

- Price information - wholesale and retail
- Domestic and overseas market information
- Information regarding Colombo Auctions if applicable
- Specific information regarding the major agricultural products of the province. This

would involve contributing to journals in this field. Members could come and read the journals in the Chamber library or have it photocopied and mailed to them for a fee.

- Technological information - e.g advancements in agro processing, new equipment and where it can be obtained,etc.
- Financing information for ventures in these areas.
- Information about associations specializing in these particular fields, based in Colombo or elsewhere. The Central Province Chamber should be able to at least provide a contact whom members could communicate with regarding very specific information that the chamber is unable to provide.

Much of the information regarding prices and financing can be obtained very easily. e.g. ARTI publishes a weekly Food Commodities Bulletin, CDA publishes a bulletin giving coconut and coconut product prices. Similar bulletins are published for tea. Some of the other information regarding associations of producers of specific products, could probably be obtained from existing chambers.

## **(2) COUNTRY/MARKET REPORTS**

- With the government's emphasis on export development as a growth strategy the chamber will have to play an important role in assisting local businesses/entrepreneurs in identifying foreign markets for their products.
- Initially the chamber could contact the trade/commercial representative of foreign missions to Sri Lanka. It is possible that they might be able to provide some information. In addition they could also provide information about chambers in their countries with which the Central Province Chamber could then establish direct contact. A list of foreign missions to Sri Lanka, with addresses and telephone numbers is attached.
- Later on the chamber should develop the capacity to collate information regarding specific countries or markets for specific products, and present it to members in report form. Initially however the chamber should at least be able to identify foreign buyers, and link them with producers from the central province.
- The chamber should also develop a capacity to conduct surveys - collate the information and present it to relevant groups within the membership. The assistance of the Economics and Commerce Departments at the University of Peradeniya could be sought in this respect.

## **(3) STATISTICAL DATA**

One of the services the Chamber should offer its members is easy access to statistical data and information. Some statistics that will be of importance to the members will be prices, interest rates, wages, export/import data, etc. The chamber can subscribe to various publications of statistical data published by the respective statistical research institutes. Listed below are some places where the chamber can receive data on a regular basis:

- Agricultural and Research Training Institute (ARTI)
- Census and Statistic Bureau
- Central Bank
- Export Development Board (EDB)



- GCEC
- Tea Board

The Chamber can also formulate a section in the monthly newsletter (description follows) with statistical data and information, relating to the particular needs of the businessmen of the Southern province with information collected from the above (and other) sources. It might be useful for the Central Province Chamber to establish links with the Ceylon Chamber of Commerce, either through correspondence (initially) or a database.

#### **(4) TRADE & COMMERCE**

There is a need to promote the business intelligence services in the central province and establish linkages with the traders and their business interests. The following may be of interest to the members of the Central Province Chamber:

- Trade regulations and restrictions
- A list of brokers and marketing agents
- A listing of trade contacts - information can be collected relating to the product and its exporter/importer. Details consisting of the name, address, telex and telephone number should be collected. Other services offered by members of service organizations can also be listed.
- Information on trade inquiries collected from overseas and outstation firms to establish relations with firms in the Southern province.

#### **(5) INDUSTRIAL & TECHNOLOGICAL INFORMATION**

The key to efficient production is the availability of information on the latest methods and technology. The Central Province Chamber should update its members with the latest industrial and technological innovations. Industrial/Technological Information can be collect under the following sub headings:

- Agricultural technology
- Building materials
- Energy facilities
- Transport
- Pesticides, etc.
- Textiles
- Plant and Machinery Sources
- Packaging

The information can be received from various sources. Four useful international Industrial/Technology guides are :

1. Asian Agribusiness
2. Asia-Pacific Tech Monitor (APCTT)
3. Trade Promotion
4. Technology Transfer International, U.K.

Local technological information can be gathered from several importing and manufacturing companies. For example, news on the latest agricultural chemicals and equipment can be received from the following companies:

- Anglo-Asian Fertilizers Ltd.
- Baur & Co. Ltd.
- Chemanex
- Hayleys
- Chemical Industries (Colombo) Ltd. (CIC)
- Mackwoods Ltd.
- Finlay Chemicals & Dyes (Pvt.) Ltd.

The above local companies are located in Colombo and the names were taken from the Yellow Pages. These firms must be having a number of regional outlets and the first step for the Central Province Chamber is to make contact with them. The Chamber should make contact with the head office and get on their mailing list.

#### **(6) PRODUCT REPORTS**

This section could contain reports on product reports manufactured or grown in the Central Province. The resources of the Peradeniya University could be deployed here to secure information of relevance to the business community in the province. The reports could be generated on a user fee basis though initially broad categories maybe dealt with.

#### **(7) TRADE DIRECTORIES**

Another very useful item that could be highlighted in the newsletter is a listing of available foreign trade directories. These trade directories, published by chambers of commerce and various agencies in foreign countries, contain valuable trade and business information in the country concerned. Business persons in the Central Province could utilize the information available in these directories to establish trading links with potential clients overseas. Once again, the newsletter could be deployed to inform the membership about the availability of specific directories and members could call over at the Chamber office to obtain greater details. They would then have access to contact addresses and other information about possible trade ventures with foreign clients.

#### **(8) SHIPPING**

Information in this regard could take the following forms.

- A schedule of cargo ships arriving and departing from the Colombo and Galle ports. A listing of the different shipping agents, the shipping lines they represent, the routes travelled by these vessels, a general idea of the agent's fees and other information could also be provided on a quarterly basis.
- Details on freight transactions, costs and changes in procedures that might have been recently introduced.
- An index of the bulletins and supplements of the foreign shippers' councils that maintain trade links with business persons in the Central Province. Once again, the membership could obtain detailed information from the copies available at the Chamber.

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## **(9) CHAMBERS OF COMMERCE**

- The Central Province Chamber should have information regarding other chambers (both local and foreign) and the services they offer. Especially at the outset, the South Lanka Chamber will not be able to offer a range of services that will meet all the needs of its entire membership. The Chamber should therefore, be in a position to direct members to other associations/chambers that can provide the services that it is unable to provide. Alternatively, in the case of information that the chamber itself does not have, it could offer a service whereby it obtains the information from other sources and sells it to the individual/business seeking the information. This would not be an especially difficult task since the Central Province Chamber would have already established links with other, older, chambers which would probably have the information at hand. This sort of arrangement would generate revenue, and enable the chamber to strengthen its relations with other chambers, with relatively little effort.
- Brochures and handbooks of other chambers, their publications, etc., will be useful information to collect.
- The following are the major chambers/business associations in Colombo.
  - 1) The Ceylon Chamber of Commerce  
50 Navam Mawatha  
Colombo 2  
Tel: 449353
  - 2) The National Chamber of Commerce of Sri Lanka  
2nd Floor, YMBA Bldg  
Main Street  
Colombo 1  
Tel: 545409
  - 3) The Federation of Chamber of Industries and Commerce  
29, Gregory's Road  
Colombo 7  
Tel: 699530
  - 4) The Sri Lanka National Council - ICC  
51 Sir Marcus Fernando Mawatha  
Colombo 7  
Tel: 691290
  - 5) Women's Chamber of Commerce and Industry  
10 1/1 Sir Marcus Fernando Mawatha  
Colombo 7  
Tel: 685913

- 6) The Ceylon National Chamber of Industries  
Flat 20, 1st Floor, Galle Face Court 2  
Colombo 3
- 7) The Sri Lanka Chamber of Small Industry  
250, BO1 Liberty Plaza  
Colombo 3  
Tel: 421954
- 8) National Exporters Association  
50/21 Old Kesbewa Road  
Boralesgamuwa  
Tel: 583162
- 9) The Mercantile Chamber of Commerce of Ceylon  
94 Prince Street  
Colombo 11  
Tel: 25451
- 10) The Sri Lanka Gem Trader's Association  
c/o The Ceylon Chamber of Commerce  
50 Navam Mawatha  
Colombo 2  
Tel: 26096
- 11) Sri Lanka Jewellery Manufacturing Exporter's Association  
c/o EDB Service Division  
Ramada Renaissance Hotel  
Sir Chittampalam A. Gardiner Mawatha  
Colombo 2  
Tel: 438513-5
- 12) The Ceylon Hardware Merchant's Association  
70 K.Cyril Perera Mawatha  
Colombo 13  
Tel: 422779
- 13) The Tourists Hotel Association of Sri Lanka  
c/o Ceylon Chamber of Commerce  
50 Nawam Mawatha  
Colombo 2  
Tel: 433148

- 14) All Ceylon Trade Chamber  
212/45, 1/3 Bodiraja Mawatha  
Colombo 11  
Tel: 432428

## 10. STARTING A NEWSLETTER

Having gathered information relevant to the business community in the Central Province, the Chamber needs to identify a vehicle for passing this information on to its members. The publication of a **NEWSLETTER** detailing information of relevance to the business community in the Central Province would be an important activity that could be undertaken in this respect. Access to accurate and comprehensive business and economic information remains an important tool in advancing the economic potential of the province. Needless to say, the acute dearth of business and economic information at the provincial level has impacted negatively on business persons. Hence, the role of the Chamber in bridging this "information" gap for the Central Province will be a vital undertaking.

The proposed newsletter could provide information on a range of business and economic related activities in the province, in Sri Lanka and on the international setting. The newsletter could also serve as a forum for informing business persons in the province about foreign investment opportunities, potential joint venture operations and other foreign trade related activities. A profile of relevant statistical data, recent changes in rules and regulations affecting the agricultural, industrial, manufacturing and trading potential of the province remains another area for exploration in the newsletter. The newsletter could also effectively be a conduit for information and greater interaction with numerous other chambers in the rest of the country and those located overseas.

An important feature of the proposed newsletter would be its concise, pithy and lucid format. It should be structured in a style that the business persons in the province would be comfortable with. Publishing the newsletter in Sinhala and English languages should also be strongly considered.

The newsletter should not necessarily contain all the information available on a particular topic. Instead, the newsletter would index the reports, surveys, studies and other information recently received; the members could then obtain the specifics involved by visiting the Chamber office. In this connection, the involvement of the Peradeniya University, Department of Economics and Commerce staff in conducting surveys, reports and feasibility studies remains salient. The newsletter could indicate some of the more extensively researched topics covered by the University staff and make them available to the general membership and others on a fee based system as well.

The format in which the newsletter might identify some of the information it has gathered is as follows:

A typical listing in the newsletter, of the trade directories held in the chamber:

Germany

Kompass Deutschland, Volumes 1-3.

Germany: Kompass Deutschland, 1991.

Korea

Inchon Business Directory, 1990/1991.

Korea : Inchon Chamber of Commerce and Industry 1990/91.

A typical listing of trade contacts:

**PRODUCTS**

FRESH COCONUT with water (in bags)  
DESICCATED COCONUT (in 5 ply kraft  
paper bags with polytene inner liner)

**EXPORTER'S DETAILS**

Natasha Exports  
P.O. Box 32  
Wattala, Sri Lanka  
Contact: Mr. Perera  
Tel: 55321  
Tlx:            Fax:  
Bankers: Habib Bank

A typical listing of a trade inquiry:

**CINNAMON**

San Diego Products, 1330 La Miranda Drive, San Marcos, California 92096, U.S.A., Tlx:  
(619) 744-9558

It will be very useful to obtain the trade information bulletins from the Ceylon Chamber, visit and meet with the staff who prepare it, in order to get ideas to prepare your own.

(Prepared by the PSU Samantha De Silva, Avanthi Moonesinghe, Nimal Gunatilleke)

## **Appendix B**

### **Preparing for Policy Dialogue**

#### **(a) Introduction**

This appendix contains discussion papers, examples of analytical papers prepared by the PSU and the notes prepared by the PSU to initiate activities by the BSOs which were to result in enhanced policy dialogue. The purpose of including these papers is two fold. First to under score the deliberate effort that was needed to initiate activities which the BSOs and the private sector subsequently found to be quite useful. Second, the papers illustrate the type of analytical support activities which are needed to assist the BSOs and the private sector to improve policy dialogue. A great deal of work remains to be done in order to help the private sector to become more aware of the role it can play in the policy arena. There are many economic issues about which the private sector must be better informed. However, the processes of improving the awareness of the private sector about these issues are still at a rudimentary stage. More effort is needed to link universities and research institutions with the BSOs. The work of the PSU illustrates what is possible in terms of networking, linkage and inter-action between the private sector (through BSOs) and the university and research communities.

The first item in this appendix is a short discussion paper about the need and prospects for a strategic partnership between the private and public sector. This paper was an input to the process which resulted in the PSU assisting selected BSOs to prepare industry agenda. The second paper is an example of what may be useful for policy discussions between the public sector and private business. Item III, is the draft of the terms of reference for the strategy for tea sector which was undertaken Colombo Tea Traders Association. Items IV and V are two papers prepared by the PSU to assist the CTTA with their representations. Item VI is a note prepared by the PSU to initiate the preparation of a strategy for the gem and jewelry sector undertaken by the Sri Lanka Gem Traders Association. The final item is a PSU outline for a strategy for the fruits and vegetable sector. This note formed the basis of a proposal by the Sri Lanka Fruits and Vegetable Producers and Processors and Exporters Association and led to the preparation of a strategy for the sector which opened new avenues of policy dialogue for the sector.

## Institutional Development and the Private Sector The Elements of a Strategic Partnership<sup>1</sup>

### 1. Introduction

The search for alternative models of development are reemphasizing the potential of the private sector and the need for mechanisms to improve its performance. Two related themes emerge, the first deals with allocative inefficiencies generated by public control and the search for mechanisms to transfer decision making from public to private hands in some activities. The second relates to the need for facilitatory activities to sponsor and to enhance the capacity of small enterprise scale sectors? This has been a public sector activity.

### 2. Themes

Large and persistent fiscal deficits, slow growth of exports and disappointing performance of the manufacturing sector demands a search for new means to energize the economy. The private sector is considered a part in which large unused potentials reside. Mechanisms to release the potentials are not apparent. Neither the public nor the private sector is a monolith. The need for institutional forms to "mediate", "represent" and articulate needs of the various components of the private and public sectors, have to be either created or revived.

The climate for discussion between the private and public sectors, is opportune. There is strong will within parts of the two sectors, to jointly develop the elements of a strategic partnership. However the form of this partnership can take has not been clearly articulated, by the public or private sector groups.

The mechanisms and institutions, which could facilitate a strategic partnership are not self evident. Some elements of the private sector would view such activity with suspicion, considering it to be a step towards more regulation or constraints. Meanwhile there are a range of economic issues on which the private sector can engage in dialogue with the public sector. However, the private sector could do well to increase its knowledge and awareness about these issues before taking up positions.

#### 2.1 Macro Issues.

##### (i) Resource allocation, capital formation.

What is the role of the private sector in setting priorities for investment?

Sri Lanka has been examining the need and prospects for reducing the public sector deficit and making the large pools of savings in the insurance, provident and pension funds available to the private sector,

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<sup>1</sup> This is an edited version of a PSU note, subsequently adapted for a discussion group which met in 1990 to examine the research agenda for Sri Lanka, for the International Development Research Council, Regional Office, Delhi. The ideas were discussed with a few development analysts and senior policy makers.



for more than a decade. However, the public sector continues to mobilize and use national resources for new schemes, while infrastructure and skills remain inadequate to support rapid growth.

Can a private sector "strategic investment perspective" to examine the potential to convert the savings more efficiently be facilitated?

The private sector investment performance is not unrelated to the public sector efforts. Public investment and the size of fiscal deficit affects the business climate. The signals used to convey information about the investment climate, and how they are perceived by the investing agents can be changed with a significant impact on investment and output.

(ii). Industry and manufacturing.

Can the performance of the manufacturing sector be improved by strategic plans for the selected sectors?

The manufacturing sector is expected to provide a substantial proportion of the new employment in the next decade. It is expected to lead growth, improve in labor productivity and international competitiveness. Some components of manufacturing would have better potential for growth than others and the participants would have to be aware of the opportunities and have strategies to seize them.

In the short term, the extent of the possible "coordination" between the private and public sector, is illustrated in part by examining the more successful components of the economy. They include, in agriculture, some forms of contract farming, and small holder horticulture, light engineering and the apparel sector. They indicate the possibilities for an effective partnership. Institutional capacities have to be built within sectors to examine their potential and to develop the basis for dialogue and discussion with the public sector.

## 2.2 Sectoral and Micro Issues.

What are the investments from the public sector that complement private sector investments?

Private sector investments will be enhanced by some types of public investments in social and economic infrastructure. This is well known. However, the choice of public investments, "signal" the prospects for private sector in specific activities. The private sector could develop "strategic plans" based on intended public sector investments. It could also "flag" public sector investments that could enhance the performance of existing and potential private sector agents. The discussion of national investment from a private sector perspective is thin. This is based partly on perceptions that discussion should be limited to the policy regimes governing investment and not on the composition or aspects of the investment mix. Where the public goods promote expansion and entry of new capital, generating new impetus in a sector, the private sector may readily enter into fruitful relationships with the public sector. The private sector may initiate such discussions.

The Institutional mechanism have to be created to facilitate exchange of views and to enable participation in developing the investment climate, identifying strategic national investment opportunities. Discussion does take place but can be developed further.

The experience of the public agencies set up to promote foreign investment, GCEC, FIAC and the development of the garment industry is one model that warrants close examination. The GCEC, a semi autonomous institution was formed by the public sector, with strong links with the private sector. A new ministry of-Textile Industries was set up at the apex of the public sector to coordinate policy. However, investment decisions in the allied garment industry were channeled through the institutions, GCEC, FIAC and LIAC, and coordinated by the Ministry of Industry and Scientific Affairs. The interaction between the local textile manufacturers, garment manufacturers set up in the EPZ and the public sector agencies engaged in export development may not have taken the strategic development prospects of the sector into account. The transformation of the sector in the medium to long term could have been "Planned" jointly by the private sector participants, potential investors and the public sector agencies. Needs on the "demand" side of production; identification and access to markets, and on the supply side; skill development, process and technology upgrading; require communication between the "compartments", private and public sector.

## II

### WHAT DO WE HAVE TO DO FOR A LARGE INCREASE IN THE FLOW OF FOREIGN INVESTMENTS?

#### **I. The case for policies to increase the flow of Foreign Direct Investment.**

A large increase of Foreign Direct Investment has to be sustained for a decade or more to achieve our social goals of rapid employment creation and a significant improvement in the standard of living of the average Sri Lankan. Consensus is almost reached, by political managers and decision makers in the country, that we need to reach and maintain average economic growth rates of over 7% for at least the next decade. The necessary rates of national capital formation will require a significant volume of foreign resources. Today, a growing proportion of international surpluses are channelled in the form of FDI. Multi-lateral and bi-lateral finance and assistance stops short of directly enhancing production and developing export capability. Equity finance with access to markets and prospects of imparting technical and managerial capability is urgently needed to fuel growth and advancement. Meanwhile the efficiency of total national investment must improve and levels of domestic savings should increase. However, a national capacity to access and sustain high levels of FDI is vital.

A program is needed to create the pre conditions for sustained high levels of FDI, the national system has to develop capability to select types of FDI most suited for our development needs and the capacity of the local enterprise community has to be enhanced to enable activity such as joint ventures and joint market development.

#### **II. The Pre-Conditions for Increased FDI.**

The level of FDI in the Asian region grew rapidly during 1971-81 and declined thereafter. The share of FDI in total financial flows has also declined. Sri Lanka captured about one quarter of the FDI flow to South Asia during 1977-85. The cumulative FDI we obtained was about 40% that India mobilized during the same period. However our performance does not match that of our South East Asian neighbors who have grown faster, created more employment and improved their standards of living rapidly. Studies of foreign investment in the Asia Pacific region indicate that level and type of FDI to the region is changing. These changes are driven by the needs of the surplus nations including the Asian giant, Japan.

FDI flows appear to be driven by low risk investment environments. Steady high economic growth rates are a significant attraction. Low inflation driven by national fiscal prudence is important for continuity of flows. Realistic exchange rates and interest rates, forward looking trade and industry policy is essential. A social and political environment committed to seeking national benefits from FDI forms the base of generating investor confidence.

#### **III. There is an Urgent Need to Develop A Legal Framework for Enterprise Development and Support Large Scale Investment**

Attracting FDI depends on a healthy market environment. The World Bank in its recent annual survey of developing nations emphasized the importance of competitive markets. The report added "markets can't operate in a vacuum - they require a legal and regulatory framework that only

governments can provide". Correspondingly, investments have to be supported by an adequate legal framework. It was generally assumed that our common law based on English and Roman Dutch Law principles would be familiar to foreign investors and their legal advisors. However, these laws relating to contracts, companies and maritime presupposed a limited form of trading and business activity. Prior to 1978, for almost two decades there was a substantial growth of state activity in the commercial and the financial sphere, accompanied by laws to facilitate such state participation. This legislation also contributed to the creation of a legal and bureaucratic culture antithetic to private entrepreneurial efforts and to the flow of FDI.

The dramatic reversal in economic strategy in 1977 saw some legislative changes. A new investment regime, revised intellectual property laws and updated company laws formed part of the new legislative agenda. These legislative responses were however somewhat *ad hoc* in character and were not integrated into a broad legal framework intended to facilitate economic liberalization and rapid transformation. Several vital areas such as the need for a comprehensive investment code (to cover both domestic as well as Free Trade Zones), the regulation of private capital markets, banking and finance remain unchanged. The resolution of commercial and investment disputes, including the process of debt recovery (notwithstanding the recent reforms) continue to be problematic areas calling for urgent reform.

The need for review and reform of the commercial, financial and investment laws and codes is urgent. It is needed to meet the new investment and growth objectives of the government.

#### **IV. We Have to Develop a FDI Strategy.**

A set of short and medium term measures are needed to attract and sustain a large flow of FDI. However these measures would be successful in the long term only if cast in a long term strategic perspective. Strong policy reversals, nationalization of foreign assets in the past, a weak legal framework and inadequate experience dealing with modern international business enterprise will not attract a large scale flow of FDI in the short to medium term. Clear and transparent measures are needed in many areas of the economy.

Local economic capacity and surpluses may not be efficiently employed in enterprise based on the elaborate and costly infrastructure in the Mahaweli unless issues of tenure and land ownership are clearly addressed. The local financial system should become more responsive to enterprise needs. The self assurance that private enterprise can be managed with simple safeguards must emerge soon. Political managers and decision makers have a vital role to play in creating the environment for this necessary self assurance.

The flow of FDI depends on features of the operating economic environment. As a country with a relatively low per capita income and small economic base, we lack a range of infrastructure pre requisites. For too long we have been complacent about our transport system, communication and enterprise supports. What we have now, only provides for the economic level we have achieved. A significant increase in the standard of living requires a substantial improvement in the infrastructure. This is needed not exclusively for FDI but for enhancing the productivity of the national enterprise base. Selective improvement of enterprise zones is one important approach since the total system cannot be improved simultaneously. However, a clear perspective of the needs of different classes of local enterprise is needed.

## V. Large Scale Special Incentives are a Give Away About Poor Infrastructure Supports

Special fiscal concessions for FDI is an important signal of desire and intent to use foreign resources. However, the level of concessions is clearly perceived by the investor as a discount for weak or inadequate enterprise support systems. If time schedules for approvals are not clear and not maintained in practice, if the project appraisals are not as professional as the investor is accustomed to, if regulations are extensive and not easily decipherable, and if legal and financial supports are inadequate, the concessions tend to be a gross approximation of the discounted unanticipated costs of setting up and operation.

We know we cannot continue to attract FDI with fiscal concessions. It will only lead to a debilitating duality within the system. We need to pick targets for improvement in the enterprise infrastructure system that will enhance productivity from both FDI as well as local enterprise. We need to consider substantial programs for infrastructure development and to sustain the effort.

## VI. How can the GCEC Improve Performance in FDI?

The professional staff strength and skill mix available to the GCEC is inadequate to sustain a major effort to promote FDI. It is unlikely that the GCEC would attract and maintain the necessary personnel. For important activities such as appraisals, it is useful to consider the development of a system with participation of banks which have experience and capacity to undertake such work. It is important to develop a national capability to facilitate enterprise in general and FDI in particular. The role of the GCEC as a FDI facilitator would be enhanced by measures to access and share existing capacities and resources. It is useful to consider **a rapid appraisal of the capacity to facilitate FDI in the system**. A program to assess the capacity and ability of the financial institutions to support a range of activities to facilitate and expedite FDI should be examined very soon.

Note prepared by Nimal Gunatilleke for the GCEC (now the BOI) reflecting the views of private sector leaders gathered through the BSOs. PSU 1991.

### III

#### Towards a Strategy for the Sri Lanka Tea Industry. The Prospects for Sri Lanka Tea in the International Market.

#### DRAFT TERMS OF REFERENCE

##### Introduction.

The Tea sector in Sri Lanka is at an important stage of its development. It has enjoyed a pre-eminent position as a producer of high value high quality tea for 125 years. However, a range of decisions regarding the organization of production of tea in the country - nationalization in the early 1970's, changes in the external market conditions - the entry of new producers, changes in technology and the emergence of new markets have changed the context for Sri Lankan tea. Over the years, we have lost ground in the market place. Productivity has fallen below those of other producers, costs have risen, production organization has not been able to respond to the market needs. The recent initiatives to privatize plantation management offers new opportunities for the sector to meet this challenge.

The Colombo Tea Traders Association together with assistance from the Ceylon Chamber of Commerce seeks to prepare a study that examines feasible strategies and options for the Tea Industry in Sri Lanka. The study does not aim to be comprehensive in coverage. The primary objective of the study is to highlight the prospects for the industry by the necessary and feasible initiatives. It will make use of the extensive studies that have been conducted as part of the plantation management restructuring, and other available studies and documents.

The Specific areas to be covered by the study are:

1. The changing position of Sri Lanka in the international market. An overview of share in world production, trends and prospects for the future. This will indicate what changes the local industry may have to prepare itself for in face of increasing supply by other lower cost producers.
2. The present status of the Tea industry. This will outline, production organization, the product mix, infrastructure support and changes over time. It will be a diagnosis of the strengths and weaknesses of the industry and possibilities for the near and medium term.
3. The implications of the privatization of management, issues and prospects. Productivity, cost, technology and market positioning. The section will broadly examine the necessary environment for the continuation of the privatization process with emphasis on the issue of stability of supply.
4. The marketing process. The study will examine the functioning of the auction system, its strengths and weaknesses and make suggestions for possible improvement. There will be specific attention to the bye-laws and conditions of sale and the regulatory framework governing the sale of tea.
5. The regulatory environment for the development of the tea industry, this section will cover the prevailing regulations and procedures related to plant material, inputs, industrial activity and market development.

6. The incentive framework for the industry, prevailing schemes for the sector, continuity and stability of signals, biases if any that repress value added production or continue to provide relative benefits to bulk and processed exports. Special emphasis on the conditions of export sector finance.

7. Responding to emerging opportunities. The study will explore the development of markets and factors promoting/inhibiting it. It will also include the prospects for intra regional activities -SAARC region, for sharing technology, information and production capacity where feasible and possible. This will also examine prospects for market integration.

8. Based on the overview, the study will identify the elements of a strategy. It will review the EDB's five year plan as one benchmark. It will point out possibilities for institutional reform, investments that are required, and the initiatives that are necessary to generate the possible rates of growth and transformation of the sector.

(Prepared for the CTTA by Nimal Gunatilleke, PSU 1992)

## IV

### Financing the Tea Trade: The Need for Credit at Competitive Rates

#### Introduction.

The Tea sector dominates Sri Lankan exports. It contributes the largest net export earnings and employs over a million persons in production, trade and other value added activities. However, while world production and exports grew steadily, Sri Lanka's contribution declined from 19% in 1970 to approximately 9% in 1988. Though tea has been produced in the country for nearly 125 years, the trading of tea within Sri Lanka is relatively recent. Formerly, most tea estates were in the hands of British and private companies. Today, a majority of the tea exported from the country, passes through the Colombo Tea auction. Traders secure orders, package and export the tea. Ensuring a strong demand for the tea and keeping the supply moving is a vital function of the traders and brokers.

Over the last decade, the composition of suppliers to the world market has changed and Sri Lanka has reduced its contribution significantly. Meanwhile the product mix in tea has also changed. In bulk tea, most world suppliers offer CTC while Sri Lanka continues with orthodox teas. However, there has been a slow change in the composition of Sri Lankan exports with value added products including packeted teas, increasing from about 30% of exports in 1980 to 40% by 1990. The Tea sector needs to transform and do so at a faster pace. Finance plays a vital role in this endeavor. It has to be available on time, at rates which enable local producers to compete effectively in the international market and in adequate volume to ensure appropriate scale.

#### Export Incentives for Tea: The Packaging Refinance Scheme

Trading requires finance as working capital. In simple terms, the teas offered at the auction have to be cleared for the next batch of produce. If the traders are consistently unable to finance purchases at the auction, unsold supplies build up. The average auction price will tend to fall as a result of the build up of supplies unless demand is strengthened due to other factors.

The packaging refinance facility provides working capital for preparation of tea for exports. It was expected to promote value addition prior to exports. The refinance facility enabled participating commercial banks to on-lend funds at concessionary rates, to purchase tea and prepare it for export.

A very large volume of finance is required to purchase tea at the auction. Usually there is a waiting period of two-three months from the time of purchase till funds are realized after the tea is received by the over seas buyer. The terms and conditions under which various traders operate vary according to the size of operation, links with the purchaser and established credit worthiness. Credit from commercial sources are available for annual rates ranging from 22-28% The refinance facility provides credit at 16% for bulk teas and 11.8% for value added tea. A rebate of 4% is given if the funds are returned within the stipulated three months. Most traders are able to operate within this time period.

Most countries competing with Sri Lanka provide concessionary finance to the Tea Sector. During the past year the rates on short term credits in India range from 6-8%, in Indonesia it was about the same. Both countries offer teas which compete quite effectively with our own. These countries are also





lower cost producers of traditional teas and are better placed to enter the value added activities related to tea. The advantages that Sri Lankan teas had as an early entrant to the market has been out competed by new entrants. The Export Development Board and the Sri Lanka Tea Board have developed a comprehensive strategy to enhance Sri Lanka's international competitiveness into the 21st century. An important component of this strategy deals with extending incentives to increase productivity, encourage diversification and promote value added activities.

The incentive schemes have to distinguish between stabilization of the traditional components of the sector and promoting the relatively new ones. At present the proportion of earnings is higher from the bulk exports than from

the various forms of value addition. Though the packaging refinance scheme offers higher concessions for value added teas, the proportion of exports continues to be dominated by bulk and orthodox teas.

#### Securing a Competitive Edge in the International Tea Market: Options and Implications

Removing the concessions offered to the tea sector through the packaging refinance is unlikely to result in improved performance. A set of coherent, transparent incentives where borrowing leads to value added activities would be welcome to the various participants of the sector.

At the moment, on-lending through the refinance facility is offered by all major banks. However, it seems that established traders have better access. The mix in the lending in volume terms favors traditional activities in spite of the higher concessions for value added activities.

Promotion of value added activities, bagging tea, flavoring and packaging for presentation require high initial investments. Machines have to be imported, markets studied and accessed and products designed to suit new demands. These investments also require development assistance. The banks are not as responsive nor willing to risk funds on new entrepreneurial ventures related to tea. Funds continue to move to the traditional activities while the need is for transformation of the sector.

Enhancing productivity, reducing cost and improving products are vital to maintain the competitive edge. The incentive schemes for the tea sector, for production, trading and product enhancement have to consider what the competition is getting.

### **REFINANCE SCHEME FOR TEA**

#### CATEGORY I - BULK AND PACKETED TEAS

Central Bank Interest Rate to Commercial Banks	13%
On lending by Commercial Banks	16%
Rebate for payment within 90 days	4%
Effective Rate of Interest	12%

#### CATEGORY II - TEA BAGS, GREEN TEA, INSTANT TEA

Central Bank Interest Rate to Commercial Banks	8%
On lending by Commercial Banks	11.8%
Rebate for payment within 90 days	4%
Effective Rate of Interest	7.8%

Removing the concessionary finance will lead to higher trading costs. Large and established firms will obtain better terms. However, in order to transform the balance of exports more finance would have to flow to the value added components. This would require a different risk taking approach by the banks towards risk taking ventures and entrepreneurial activities in the tea sector.

Removal of the refinance scheme without compensating systems would reduce the competitive position of the orthodox teas which continue to form the major share of the exports. Furthermore it would retard the development of value added teas. Without the availability of the refinance scheme, credit for purchase at the auction will cost more. The cost of funds will be in the range of 18-24% depending on the customer. New entrants and small traders may pay rates that are even higher. The returns in the bulk tea trade tend to be in the 2-5% range. The returns are higher in value added products, and the quality teas. However, it seems that players in the tea market even for value added products tend to operate in the bulk market as well. Although individual entrepreneurs have changed their export product mix dramatically towards value added teas, a critical mass of such enterprise has yet to develop.

The higher cost of funds will increase the operating costs of traders who purchase tea at the Colombo Auction and ship in bulk or after adding value. Without the refinance the trading costs will increase and the trader margins will fall for those who are unable to pass on the cost to the clients abroad. The larger bulk buyers may pass on the costs while the smaller ones absorb it. The higher costs of funds are not directly related to the FOB prices which are determined in the international market. Sri Lanka is an important supplier but not the dominant one. Close substitutes are emerging for Sri Lankan teas and market opportunities in allied value added areas may be affected if the demand shifts away from Sri Lanka to competitors such as India (Assam and Darjeeling) and the newer Indonesian teas.

The refinance scheme is but one instrument for promoting the shift in the export market supply of tea. It is necessary to keep close sight of the relationship between incentives for the various components of the sector and the targets for productivity improvements, and the transition and transformation. Improving the performance of the plantations, developing new HYV, perfecting tissue culture or allied means of propagation, enhancing productivity and reducing costs have to be addressed. At the factory level, plant and machinery have to be upgraded, improved and developed. Once the product reaches the auction, prospects for value addition have to be examined and promoted. A package of linked incentives are therefore necessary with an overview of the sector and prospects for its development in clear focus.

The proportion of export earnings from bulk teas was nearly four fifths (79%) in 1980 and had declined to 60% of the total in 1989. The Tea Development Plan for 1991-95 aims to address the main issues of the sector from production to marketing inclusive of value addition. At the end of the period the proportion of value added products in total tea exports is expected to rise from about 40% to about 55%. Some incentive schemes are to be phased out including the packaging refinance while others will be retained. Those retained include subsidies for replanting and in-filling as well as a range of value added activities. (investment + Actual and Estimated Targets)

However, the value addition is best developed in a context where the bulk markets and trading operations are stable. The financial incentives for trading could be operated on a "sliding scale" and linked to market conditions and value added activities. Value addition requires the tea in the first place. Distinction could be made between tea for bulk exports and for value added processing. Incentives can be higher for the latter. However even here the refinance alone will be inadequate to promote large scale value addition within a medium term perspective.

(PSU, 1991. Glynn Cochrane, Nimal Gunatilleke, Shenuka Chanmugam and Sujit CanagaRetna).

## **The Tea Trade**

### **Increasing Sri Lanka's International Competitiveness**

#### Introduction

This paper was intended to explore the impact on the tea trade in Sri Lanka of the existing packaging refinance scheme. Research indicated that the issues involved were not simply limited to financing the trade but more intimately linked to increasing Sri Lanka's international competitiveness.

#### I. The Packaging Refinance Scheme

Sri Lanka has lost considerable ground in the world tea market. The situation is not self-correcting, indeed with Sri Lanka's cost structure the situation will worsen.

New entrants are using processes which are more cost effective and have significantly better demand prospects as in the case of CTC teas. Many of the exporters also have a larger proportion of value added products in total exports. Removing the concessions offered to the tea sector through the packaging refinance facility is unlikely to result in improved performance. A set of coherent, transparent incentives where borrowing leads to value added activities would be welcome to the various participants of the sector.

The packaging refinance scheme was a good idea to promote value added activities in tea. However, in retrospect, it seems that the expected gains were not realized due to a host of reasons including the targeting of recipients, the administration of the funds and the links to related value added activities.

This facility provides working capital for preparation of tea for exports. It was expected to promote value addition prior to exports. The refinance facility enabled participating commercial banks to on-lend funds at concessionary rates, to purchase tea and prepare it for export.

The refinance facility provides credit at 16% for bulk teas and 11.8% for value added tea. A rebate of 4% is given if the funds are returned within the stipulated three months. Most traders are able to operate within this time period. Credit from commercial sources is available at annual rates ranging from 22-28%. This facility has been used by tea traders to purchase at the auction and prepare the product for export. According to the available data, the total facility for the tea sector was approximately Rs. 500-600 million, in 1990 the facility was extended to Rs. 700 million. The credit tends to turn around 6 - 8 times a year. The proportion of exports financed by the facility has been in the range of one quarter to one third and is declining as a result of the higher Rupee value of the exports. The terms and conditions under which various traders operate vary according to the size of operation, links with the purchaser and established credit worthiness.

The incentive schemes have not distinguished adequately between stabilization of the traditional components of the sector and promoting the relatively new ones, while the first objective is important the second is crucial. At present the proportion of earnings is higher from the bulk exports than from the various forms of value addition. Though the packaging refinance scheme offers higher concessions for value added teas, the proportion of exports continues to be dominated by bulk and orthodox teas.

If there was no refinancing, the higher cost of funds will increase the operating costs of traders who purchase tea at the Colombo Auction and ship in bulk or after adding value. Without the refinance facility trading costs will increase and the trader margins will fall for those who are unable to pass on the cost to the clients abroad. The larger bulk buyers may pass on the costs while the smaller ones absorb it. The higher costs of funds are not directly related to the FOB prices which are determined in the international market. Sri Lanka is an important supplier but not the dominant one. Close substitutes are emerging for Sri Lankan teas and market opportunities in allied value added areas may be affected if the demand shifts away from Sri Lanka to competitors such as India (Assam and Darjeeling), and the newer Indonesian teas.

The results of the financing scheme are not yet good enough. It is now evident that a modified scheme is needed to promote value added activities in the tea sector. It should link production, trading, packaging, manufacturing, marketing, promotion and exports. These incentives have to consider the roles of specific public sector agencies as well as specific private enterprises.

## II. Securing a Competitive Edge in the International Tea Market: Options and Implications

The Tea sector should dominate Sri Lankan exports. Its future and enhanced productivity is critical to national economic recovery. It contributes the largest net export earnings and employs over a million persons in production, trade and other value added activities. However, while world production and exports grew steadily, Sri Lanka's contribution declined from 19% in 1970 to approximately 9% in 1988. Though tea has been produced in the country for nearly 125 years, the trading of tea within Sri Lanka is relatively recent. Formerly, most tea estates were in the hands of British and private companies. Today, a majority of the tea exported from the country, passes through the Colombo Tea auction. Traders

### REFINANCE SCHEME FOR TEA

#### CATEGORY I - Bulk and Packeted Teas

Central Bank Interest Rate to Commercial Banks	13%
On-lending by Commercial Banks	16%
Rebate for payment within 90 days	4%
Effective Rate of Interest	12%

#### CATEGORY II - Tea Bags, Green Tea, Instant Tea

Central Bank Interest Rate to Commercial Banks	8%
On-lending by Commercial Banks	11.8%
Rebate for payment within 90 days	4%
Effective Rate of Interest	7.8%

secure orders, package and export the tea. Ensuring a strong demand for the tea and keeping the supply moving is a vital function of the traders and brokers.

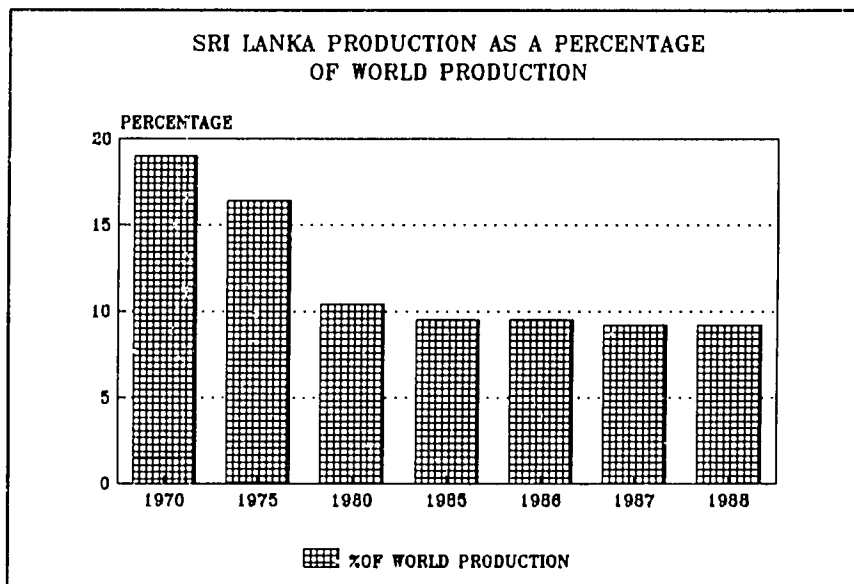
Over the last decade, the composition of suppliers to the world market has changed and Sri Lanka has reduced its contribution significantly. Meanwhile the product mix in tea has also changed. In bulk tea, most world suppliers offer CTC while Sri Lanka continues with orthodox teas. However, there has been a slow change in the composition of Sri Lankan exports with value added products including packeted teas, increasing from about 30% of exports in 1980 to 40% by 1990. The Tea sector needs to transform and do so at a faster pace. Finance plays a vital role in this endeavor. It has to be available on time, at rates which enable local producers to compete effectively in the international market and in adequate volume to ensure appropriate scale.

Most countries competing with Sri Lanka provide concessionary finance to the Tea Sector. During the past year the rates on short term credits in India and Bangladesh range from 6-8%, in Indonesia it was about the same. Both countries offer teas which compete quite effectively with our own. These countries are also lower cost producers of traditional teas and are better placed to enter the value added activities related to tea. The advantages that Sri Lankan teas had as an early entrant to the market has been out competed by new entrants. The Export Development Board and the Sri Lanka Tea Board have developed a comprehensive strategy to enhance Sri Lanka's international competitiveness into the 21st century. An important component of this strategy deals with extending incentives to increase productivity, encourage diversification and promote value added activities. The Tea Development Plan for 1991-95 aims to address the main issues of the sector from production to marketing inclusive of value addition. At the end of the period the proportion of value added products in total tea exports is expected to rise from about 40% to about 55%. But how is this to be done? Some incentive schemes are to be phased out including the packaging refinance while others will be retained. Those retained include subsidies for replanting and in-filling as well as a range of value added activities. The proportion of export earnings from bulk teas was nearly four fifths (79%) in 1980 and had declined to 60% of the total in 1989.

At the moment, on-lending through the refinance facility is offered by all major banks. However, it seems that established traders have better access. The mix in the lending in terms of volume favors traditional activities in spite of the higher concessions for value added activities.

Terminating the refinance scheme without compensating systems would reduce the competitive position of the orthodox teas

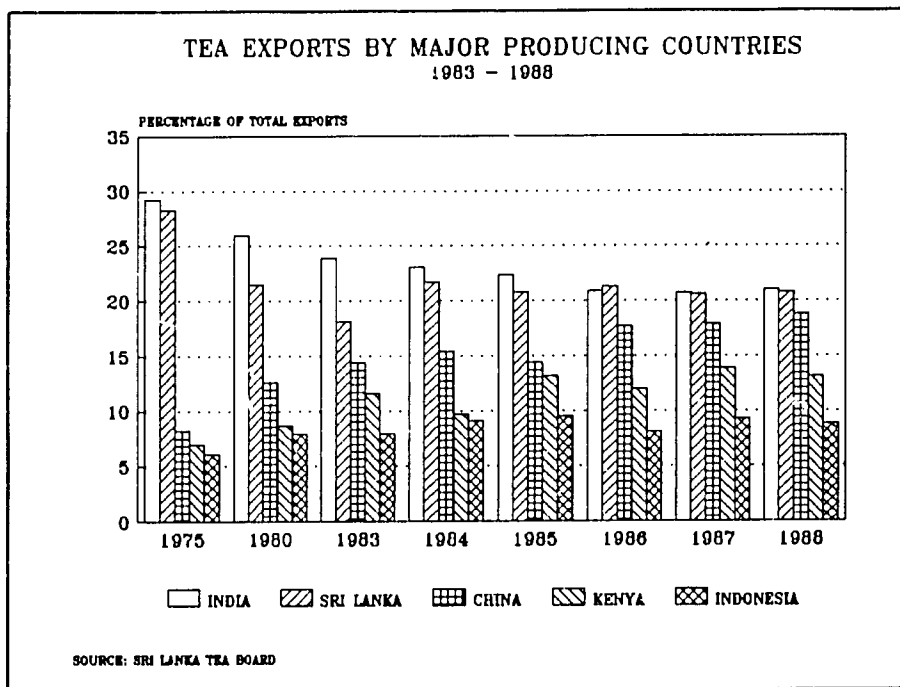
which continue to form the major share of the exports. Furthermore it would retard the development of value added teas. Without the availability of the refinance scheme, credit for purchase at the auction will



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cost more. The cost of funds will be in the range of 18-24% depending on the customer. New entrants and small traders may pay rates that are even higher. The returns in the bulk tea trade tend to be in the 2-5% range. The returns are higher in value added products, and the quality teas. However, it seems that players in the tea market even for value added products tend to operate in the bulk market as well. Although individual entrepreneurs have changed their export product mix dramatically towards value added teas, a critical mass of such enterprise has yet to develop.

Withdrawing the concessionary finance will lead to higher trading costs. Large and established firms will obtain better terms. However, in order to transform the balance of exports more finance would have to flow to the value added components. This would require a different approach by the banks towards risk taking ventures and entrepreneurial activities in the tea sector.



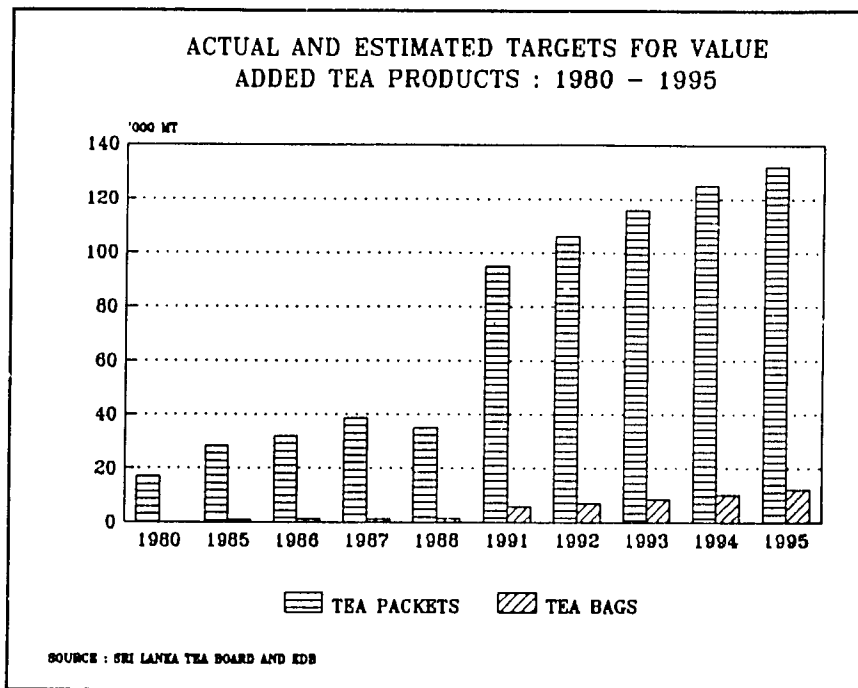
#### Increasing Value Added Production:

The refinance scheme is but one instrument for promoting the shift in the export market supply of tea. It is necessary to keep close sight of the relationship between incentives for the various components of the sector and the targets for productivity improvements, as well as the process of transition and transformation. Improving the performance of the plantations, developing new HYV, perfecting tissue culture or allied means of propagation, enhancing productivity and reducing costs have to be addressed. At the factory level, plant and machinery have to be upgraded, improved and developed. Once the product reaches the auction, prospects for value addition have to be examined and promoted. A package of linked incentives are therefore necessary with an overview of the sector and prospects for its development in clear focus.

Enhancing productivity, reducing costs and improving products are vital to maintain the competitive edge. The incentive schemes for the tea sector, for production, trading and product enhance-

ment have to consider the incentives that the competing countries are getting. The export duty favors value added exports on a sliding scale, with bulk tea going out at Rs. 1.50 a kilo and bags at Rs. 0.50 a kilo.

Promotion of value added activities, bagging tea, flavoring and packaging for presentation require high initial investments. Machines have to be imported, markets studied and accessed and products designed to suit new demands. These investments also require development assistance. The banks are not as responsive nor willing to risk funds on new entrepreneurial ventures related to tea. Funds continue to move to the traditional activities while the need is for transformation of the sector.



The growth targets for export earnings in the tea sector have been projected as a relatively slow annual rate of 1.5% for the period 1990-1994. The export earnings from bulk teas are expected to decline by an annual average of 3%. Earnings from packeted teas would grow at 4%, tea bags, a very small proportion of the total earnings, by an impressive 25%, and other value added by 6.3%. The composition of exports would change as a result of new investments totalling Rs. 853 million during this period. However, the change in the composition of earnings is too slow to effect the necessary transformation of the sector and to meet the growing challenge from competitors. The proportion of earnings from bulk teas stood at 60% in 1990 and is expected to fall to 46% by 1994. Tea bags would contribute approximately one tenth of the earnings, up from a projection of 4.6% in 1990. The rates of transformation have to be considerably higher to place the tea sector on a satisfactory competitive setting.

It appears that value addition is best developed in a context where the bulk markets and trading operations are stable. The financial incentives for trading could be operated on a "sliding scale" and linked to market conditions and value added activities. Value addition requires the tea in the first place. Distinction could be made between tea for bulk exports and for value added processing. Incentives can be higher for the latter. However even here the refinance alone will be inadequate to promote large scale value addition within a medium term perspective.

However, the dimensions of the task to transform the sector are illustrated by the volume of investment required to obtain a relatively modest increase in export earnings; a total planned investment of Rs. 853 million generating an increase of Rs.1,010 million (in constant 1988 prices). The investment targets and the export earnings are likely to have changed but they are indicative of the tasks ahead. Clearly, the incentive schemes and the investments have to be

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coordinated, new targets of opportunity identified and mechanisms placed for a more rapid transformation.

**INVESTMENT TARGETS  
FOR THE TEA INDUSTRY 1990 - 1994**

**III. Proposed Further Research and Analysis**

The need to transform the tea sector has been recognized and accepted by analysts and decision makers for a long time. The sector has to transform from a low value added, high production cost sector to a high value added, efficient sector. This transformation will have to take place at a pace much faster than in the recent past if Sri Lanka is to maintain its present market position let alone improve it. Though the components for development and transformation have been identified, a strategy and tactics are needed.

TYPE OF INVESTMENT	RS. MIL.
Establishment of Information Assistance Center	10.0
Promotion of National Logo for Marketing Value-Added Tea products	280.8
Scheme for Restructuring Tea Market	100.0
Assistance for Development of Packaging and Printing	60.0
Blending and Packaging	0.5
Assistance for Investment in Tea Bagging Machines	50.0
Assistance for CTC Products	300.0
Development of Iced Tea Mixing and Joint Ventures for Marketing	52.0
<b>TOTAL</b>	<b>853.3</b>

**IV. Issues For Decisions**

Source: Export Development Board, National Development Plan, 1990-1994 Vol 2

- (i) Should the packaging refinance scheme be continued in its present form?  
If not, should it be modified and combined together with other schemes?
- (ii) Are the growth rates for the value added components of the tea sector, at the optimal levels?  
If not, which components have to be favored and what are the feasible growth rates?
- (iii) Are complementary changes in the organization of plantation and production needed to energize the tea sector?  
  
If not, will the set of incentives now in place and proposed for the immediate future be adequate to meet the competitive challenge?



## Annex

### **Possible areas for further work include:**

#### 1. Plantations and Production.

An assessment of the various schemes to upgrade the plantations,

The impact of the replanting incentives for the private sector in terms of productivity, quality improvement, income and exports.

A review of the capacity to develop and propagate planting material, a review of installed capacity and needs for an aggressive transformation.

A review of the capacity for basic plant research.

The special needs of the small holder low grown tea sector. This component of tea caters to a relatively new West Asian market, and indications are that even here value added activities will tend to be located outside Sri Lanka. Once again , the market tendencies are keeping the exports to these markets in a relatively simple state.

Examination of the prospects for improving the processing capacity and factory development.

#### 2. Value Addition, Market Access and Exports.

Identifying the package of value added activities which will have the fastest growth and earning potential.

Identifying the concessions and areas for joint ventures with private and foreign enterprise.

Assessing the impact of the various incentive schemes, from replanting subsidies to export credits in terms of effect on market access, transformation and competitiveness

(prepared by Glynn Cochrane, Nimal Gunatilleke, Shiranthi Gnanaselvam, Shenuka Chanmugam and Sugit CanagaRetna PSU 1991)

**NOTES: A Strategy for the Development of the Gem and Jewelry Industry.**

The gem and Jewelry industry has great potential and can become a dynamic and significant component of exports. New activities have been added to this industry, Gem and diamond cutting and polishing. There is considerable potential for value added in the industry and will require complementary investments in human resources, process and technique development and design capacity along with investment funds. A strategy is needed to take the industry from the present state to the potential position within a time horizon of one decade.

The strategy for the Gem and Jewelry Industry will begin with:

Short term stabilization by examining capacity and potentials within each of the components of the industry,

Resource enhancement and development,

Improving and rationalizing the regulatory and facilitatory framework,

Selecting sub components of the industry for rapid development, heat treatment, Technology, and process development, design improvement.

The human resource development component and the financing of the strategy with the sources of contribution - public agencies and private enterprise, will be developed. The market development activities have to be undertaken. Sharing of risk in the expanded and new venture areas will be required. Costs of funds and potential yields have to take into account the competing investment opportunities and the pay offs in terms of foreign earnings, market access, employment and income.

Some of the elements of a strategy have been outlined in the paper prepared by the PSU. The issues are discussed below.

**(i) The Natural Resource Base, Access and Pricing.**

The natural resource base for gems is not well identified to facilitate a rapid expansion of the production and output of the Gem and Jewelry sector. In broad terms the geological mapping of the country identifies gem bearing soils and locations. However, these are not sufficiently detailed to enable large scale commercial investments that would support the proposed new dynamic industry. It requires more intensive scientific enquiry and work is underway in research institutions.

The issue of resource identification and utilization requires a policy framework which is sensitive to the opportunities and needs of a sector that is expected to generate substantial new employment and export earnings. There is a need to underwrite exploration and identification of gem yielding lands, a system of allocating the lands to prospectors, maintaining standards of mining to prevent some types of environmental degradation or imposing costs on other users of land and water resources. Resource costs

have to be assessed to prevent over use or waste. These issues have to be built into a program and have to become an essential part of the strategy.

(ii) Co-ordination of Policies.

The co-ordination between resource identification, use and finance had to be developed. The supply system required attention. The effect on "public goods" had to be taken into careful consideration at the outset. The sector had to be fitted into the environmental policy of the country and the determination of how certain lands were used, how costs of environmental damage were shared between sector, and economic agents have to be clear and transparent. Issues such as conversion of lands related to agriculture, to water resources such as catchments, have to be addressed.

The financing for resource identification and supply development at the primary stage of obtaining the raw material for the gem sector had to be developed. The principles had to be identified. Would the access to finance for resource development be relatively liberal, will there be considerations of technique, process and scale? How will participation of different agents, small scale, corporate sector and the foreign or foreign financed firms be determined? These are issues that require attention in the strategy.

(iii) Heat Treatment.

One resource that has drawn considerable attention is the mineral resource input for heat treatment, the Geuda. The value added potential of this resource is considered to be large and Sri Lanka is considered to have a very large raw material base. However, the use of this raw material to develop a sector in Gems and Jewelry requires many complementary developments. For approximately a decade, the raw material for heat treatment was exported to Thailand which has developed a significant capacity to treat and market the resultant blue sapphires. Together with the large scale dynamic jewelry sector this has led to the development of a market for gem stones that is very large compared to Sri Lanka.

Large scale increase in demand for the raw material will be generated by increased domestic capacity for heat treatment. The treated stones would then be either sold directly or fed into a local, enhanced jewelry industry. At each stage, resources, finance, design, technique and process, issues emerge and the strategy has to deal with them in a coherent, co-ordinated manner. Greatly expanded supply has to be matched with expanded demand and sale. Entering the export market creates another set of issues that have to be addressed. Expanded supply of a range of products from the sector is by itself only one part of the strategy.

Heat treatment raises important issues about techniques and processes. Different quality equipment is available in the market and there has been considerable progress in developing local machinery. There are differing views among scientists and leading businessmen about the vital technological requirements to improve the geuda sector. There is no consensus about the most important requirements for the development of the sector. Finance, human resources, equipment, market access are all necessary. In the heat treatment enterprise, there are strong indications that skill in selecting the inputs is not abundant and that it has to be developed along with skills in the application of the treatment techniques.

At present, a few enterprises carry out heat treatment on a commercial scale. If this activity is to increase by a very large factor, a range of skills will be needed. Neither the dimension of human

resources needed nor the capacity to produce the skills have been assessed. The government is discussing the needs of the industry and how this component of the gem sector can become a significant contributor to export growth. A time frame, capital requirements, process and technique requirements have to be worked out in broad outline.

While product development takes place identification, access and entry into markets requires attention. At present, Bangkok, Hong Kong and Taipei are major market centers for the Gem and Jewelry Industry in the Asian region. It is unlikely that Sri Lanka would emerge as a major market place for gems without a very large increase in the quantity of stones offered for sale. There would have to be large increases in the production of treated stones (and calibrated stones) and market development is critical to sustain the effort.

Market access and product development have to be simultaneous. Assessing market needs and capacity to adapt to them are vital. The sector would have to acquire the dynamic capability of meeting shifting tastes and be able to supply within a context of both shifting products and markets.

In the Geuda component, there are issues which have to be placed within the context of sector development. Processing technology and raw material identification have some degree of substitutability. Good output from heat treatment is dependent on the selection of input. The rate of success and the value enhancement is based on both the skill of selecting the input and the knowledge of how best to treat it for optimal value enhancement. In some ways it is similar to the processing of rough stone from the mine. How it is cut, the size and the shape seriously affects its sale price. The cutting and polishing is dependent on skill and experience. The proportion of stones damaged in the process of cutting and the subsequent loss in value is not readily known. Therefore, the costs of operation, the margin of earnings are not completely identified.

#### (IV) Complementary Efforts.

The development of the sector will require a range of initiatives. The administrative framework would have to become more accommodative and responsive, pro-active and facilitatory. Mindful of public finance and revenue considerations, the changes would have to be in the direction of promoting expansion of resource flows, access to markets and a better trading environment. The actual and perceived obstacles in obtaining raw material, machinery and equipment, and how the various public sector agencies can assist in improving conditions are being documented at the exporters fora, the regular meetings between businessmen and the public sector.

However, the mechanisms for the necessary initiatives, the institutional framework for implementation and the organization of the resources remain a major task to be accomplished. Some areas will require the promotion of enterprise and building capacity from a very small base. For example, the equipment sector supporting the Gem and Jewelry Industry will expand to support a larger output. At present, in the polishing, and heat treatment, local equipment has been fabricated based on designs of imported machines. For cutting and polishing, especially calibrated stones, adaptations on a small scale are available. One manufacturer has secured orders for export of machinery to the United States. The needs and requirements of this fledgling component of the Gem and Jewelry industry have not drawn the attention of policy makers. There is relatively free entry of different types and brands of machinery into the country. There seems to be a capability in the light engineering sector to adapt and modify designs to suit the local requirements and to produce equipment that is able to provide the needed service at a significantly lower cost.

(V) The jewelry sector.

The jewelry sector has a large traditional craft based foundation. Considerable development is possible and needed in design capability. Meanwhile the access to raw material is tightly controlled. Gold is not naturally available in the country and was imported under strong restrictions until recently when liberalization measures were introduced. The Jewelry sector participants indicate that improved availability of raw material is critical to the expansion of the sector. Initially there is serious concern about smuggling to neighboring India. But the Gem and jewelry sector cannot expand unless, the volume of gems in the system increases significantly, the volume and design of the jewelry sector increases.

In the view of some spokes persons from the trade, the two sub sectors, gems and jewelry are interrelated and require co-ordinated policies for development. Availability of resources, access and pricing, craft practices, the improvement of skills and processes, financing and market development are common concerns and require serious attention.

(VI) The Diamond Cutting and Polishing Industry.

This is a relatively recent addition to the Gem and Jewelry Sector. The total capacity that has been installed is not very large in comparison with other countries. The unit size and the number of participants have grown quickly. The value added potential in the industry is very large. The capital investments, knowledge and access to information and markets, demanding. However, the potential for this component of the Gem Industry can be enhanced and developed along with the skill development and service capabilities in the Gem sector. Furthermore, this sector has the potential of attracting a significant volume of new investments based on the availability of trainable skilled manpower.

(Prepared By Nimal Gunatilleke, PSU 1990).

## VII

### NOTE: OUTLINE FOR A STRATEGY FOR THE DEVELOPMENT OF THE EXPORT ORIENTED FRUIT AND VEGETABLE SECTOR

The fruit and vegetable production sector has dynamic components which are relatively new, export oriented and reaching out to new markets for Sri Lankan products. It is important to consider the commercial prospects and possibilities for the sector in the medium term in light of the urgent need to generate foreign exchange, employment and income.

What are the possibilities for expansion and development for this sector? What actions have to be taken in the policy arena, supply of knowledge and information, development of complementary resources to facilitate the potential growth? What is the case for promoting the sector and how can it be done?

At present new and important areas for investment have emerged in the fruit and vegetable sector. Some are in the mould of the FTZ operations, others are linked to foreign markets and a considerable degree of Sri Lankan enterprise has gone into the effort. The new agriculture infrastructure set up in the Mahaweli systems requires a set of investments in agriculture - horticulture outside the traditional crops. The generation of foreign earnings is a vital concern especially since the systems were developed with foreign borrowing.

While the strategies for development and expansion of the traditional components of agriculture continue, (plantation tree crops, traditional agriculture in food crops) to be developed, there is an urgent need to assess and examine the potential for the value added and high income generating cash crop fruits and vegetable production. A wide range of vegetables are grown in small holdings at present. The upcountry production system is based largely on imported seed, and a range of other inputs produced locally as well as imported. The product is moved out of the growing areas to a central market in Colombo. There is no extension system of the traditional kind to support the sector. The low country vegetable sector is organized along similar lines but depends on a more disaggregated marketing system, including the markets and fairs of the towns in the outskirts of Colombo.

The fruit production system also has a large small holding-home garden component. Orchard based production is a small but important component, with the small land holding dominating the production base. The Mahaweli scheme specifically earmarks some of the systems for fruit-horticulture production. Considerable work has already gone in to identify suitable crops for the systems and how they can be introduced. The potential returns to investments, the complementary inputs in research services, market development will require more attention.

A strategy for the fruit and vegetable sector will examine the feasible options and the course of action within the specific context of Sri Lanka. The small holding sector engaged in production of fruits and vegetables requires attention - specialization according to regional "comparative advantages" the Agriculture Productivity Village experiment, the access to markets and quality control the Export Production Villages are two examples. How can the supply base be changed to respond to export demand? Based on possible market entry can supply be organized on a small holder based agriculture, what are the desired or needed institutional supports to address the risk taking activity related to

transformation or specialization within a village or small holder group?

There are issues to be addressed in the supply side, scale, selection of crops and varieties, research and information on crops and inputs, value added and income generation. On the demand side, the identification of products and markets - market development requires careful attention. Furthermore there are issues in the legislative, administrative framework that requires attention, the supply of plant material and seeds for production, pricing of inputs, land, water, fertilizer and agro-chemicals to obtain and maintain productivity as well as price of output at internationally competitive levels. Developing support services in transport, cooling and refrigeration, brokering, research and development etc. is an important consideration. The institutional infrastructure developed to support a largely domestic fruit and vegetable sector will require change to meet needs of the international market.

The strategy should address the primary issue, can a significantly larger export oriented fruit and vegetable sector be developed in Sri Lanka in the medium term? Is it possible and desirable? The outline will identify the potential areas for intervention to support development and expansion of the sector, policy initiatives and the package which will best address the development needs of the sector. It will identify priorities for action in supply, demand and the regulatory system. It will examine issues in market development and the institutional needs to support the sector. The strategy will outline possible time frames for the various actions, the agents undertaking the action and the costs. The strategy will also address the issue of potential benefits for the participants, producers, service enterprises, and the expected foreign exchange costs and earnings. The development of value added processing based on the production will be considered. It is not the actual products but the possibilities, the potentials and how they can be readily identified - market opportunities not only for primary product but for a range of value added processed products. Once the issues in the sector are perceived in this manner the "inputs" for the activity become clear, supply considerations, scale and organization, support and extension services, institutions to share risk not only with the venture but with the growers as they move from one product to another in the face of demand. What safety nets and support systems are needed to cushion the producers the base of the system. How can some security be installed to support enterprise and initiative in the grower?

The strategy will pay special attention to the role of the private sector, on the basis of present and potential resources available to them. A related and important issue that will be addressed is if and how the sector can be made into one that draws investible surpluses of local enterprise, attracts overseas investments in the form of joint ventures.

The information needs and how they will be institutionally supported will be examined with specific examples. How can a system of information be developed within the national system with capacity for early warning and monitoring demand shifts.

The desired sector strategy can be limited to major parts of the fruits and vegetables. The time frame for delivery would be three calendar months for the final report from date of acceptance, with an outline within one month and a draft within two months.

(Prepared by Nimal Gunatilleke, PSU 1990)