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Tracing the Link Between Social Harmony and Sri Lanka's Economic Development

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August 2019

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There had been a time when [Sri Lanka was only second to Japan in Asia](#) on just about any socio-economic indicator in Asia—this fact has been reiterated by Dr. Indrajit Coomaraswamy, Governor, Central Bank of Sri Lanka, frequently in his speeches.¹ This was at the time that Sri Lanka gained its independence.

While other nations have continued to climb up the ladder of economic development, several factors, in particular, internal conflict contributed to Sri Lanka drastic drop in position. This *Policy Brief* attempts to highlight a few elements—pertaining to the adverse economic impacts of internal social conflicts—which require heightened attention in order to make Sri Lanka a prosperous nation.

I. Missed Investment Opportunities

Sri Lanka has missed several investment opportunities due to internal conflicts. In July 1983, a group of over [30 representatives from Japanese companies](#), including Sony, Sanyo, Marubeni and the Bank of Tokyo, which were considering investing in Sri Lanka arrived in the country.² However, Colombo had been set ablaze by rioters during this period. The investors returned to Japan the following day, leading to the loss of substantial foreign direct investment (FDI) from Japan.

Investments from [Motorolla Company and Harris Corporation](#) was another lost opportunity for Sri Lanka.³ Unfortunately, those investments were attracted by ASEAN countries. [Japan was the number one foreign investor in ASEAN countries](#) with a cumulative investment, as of March 1989, of about USD 14.5 billion.⁴ Japanese investment was a crucial determinant of the accelerated pace of development, particularly in Malaysia, Thailand and Indonesia, in the 1980s.

According to Skaperdas (2008), an important impact of violent conflicts on the economy seems to be through [portfolio substitution effects](#), namely, shrinkage of investment or capital flight, because firms would refrain from investing in violence-prone areas or tend to relocate assets to peaceful regions.⁵

In the aftermath of violent activities, the political authorities should instill confidence in local and foreign investors, by ensuring political stability in the country. It should be widely underlined that the adverse impact of the diversion of foreign investment will have to be borne by all the communities irrespective of color, creed or religion.

Lachman (1996) describes [riots as a breakdown of the rule of law regime](#) of a country.⁶ Terrorist activities have become a global phenomenon which is not an unusual experience for investors. However, riots as a result of the breakdown in law and order, make the decision-making process of investors extra cautious as such activities reflect a severe downturn in the conduciveness of the business environment of a country.

II. A Nation Left Behind

Sri Lanka as a nation, has however continuously lost golden opportunities to become a prosperous country. In 1998, Professor Donald Snodgrass stated that the [first 50 years of Sri Lanka's independence](#) can be considered as one of such lost opportunities.⁷ Even after 70 years of independence we keep losing the opportunities.

There is no doubt that the Easter attack was a severe blow to the economy. However, the riots that took place around the island, during the [second week of May 2019](#),⁸ also affected the sentiments and confidence in an extremely negative manner. It was reported that various meetings scheduled with foreign investors by the [Government and public institutions were cancelled](#).⁹ Although it is too early to give evidence of incidents similar to diversion of Japanese investments in 1983, there may have been cancellations and postponements of the foreign investment decisions due to recent conflicts.

The economic growth of the country was severely derailed due to the internal conflict that prevailed over 30 years. Ten years after the war, we are still unable to achieve comprehensive reconciliation between the Sinhala and Tamil communities. The recent incidents have added to tensions between the Sinhala, Tamil and Muslim communities, thus posing a new socio-economic challenge.

III. Boycotts Cripple the Economy

Small businesses affected by the riots will have to manage their businesses on two fronts. They must not only focus on their primary business which involves trade on a daily basis, but also manage physical repairs, replace stocks and claim insurance or compensation for any damages to their business. They will have to appeal to customers to resume their transactions. This challenge becomes exacerbated when one community boycotts another community's businesses.

The recent boycotts were aimed at crippling businesses of the Muslim community. When businesses collapse the immediate victims are the employees. It is unknown whether the proponents of these racially motivated boycotts have considered the fate of the livelihoods of the non-Muslim employees employed by Muslim businesses.

When the businesses of a country are crippled it creates ripple effects across the entire economy. When a business entity is destroyed, all layers of its supply chain are also affected. Such adverse economic impacts trickle down irrespective of the ethnicity or religion of the victim. Small businesses, in particular, contribute a great deal to move the wheels of an economy by providing employment opportunities and innovation. Providing moral support along with financial assistance to affected parties is important to minimise the impact of such incidents.

IV. Deteriorating Efficiency of Labor

[Dr. Indrajit Coomaraswamy](#) notes that Sri Lanka is on the cusp of being an ageing population at a much earlier stage of our development process,¹⁰ that is we are growing old before we become rich. Therefore, we cannot drive growth through labor augmentation and measures need to be taken to increase labor productivity. Kato and Sato (2016) states that [ethnic and religious violent conflicts](#) exert negative effects on the gross value added per worker and capital/labor ratio.¹¹ When there is mistrust among workers, the efficiency of an organisation goes down. The psychological impact of violent activities cannot be healed quickly. It affects the productivity of labor adversely.

Riots and other violent activities not only have a short-term impact on labor productivity but also create a long-term impact on the labor force. Children who experience violence will be the future labor force of the country. Those traumatic experiences can impact their future behavior. According to Sharkey et al. (2014), [personally experienced violence](#) has long lasting, beyond-monetary impacts on the individual such as on the educational performance of students.¹² Therefore, the non-financial costs citizens experience living through times of heightened social tension is a matter which requires serious attention.

V. Dwindling Sense of “Us”

Professor Ricardo Hausman (2018) states countries that have more [‘personbytes’](#) are more diversified and able to make “less ubiquitous” products.¹³ He notes that when countries bring different skills together, they can produce more things. Although the said theory is emphasised in relation to immigration policies, it can be used to promote the feeling of “togetherness” of a society as well. The theme of “sense of us” can be applied to enhance the competitiveness of Sri Lanka’s tourism. Being a multi-ethnic, multi-religious society, Sri Lanka can leverage its cultural variety and diversity as an attraction for tourists. However, ethnic/religious riots will be a significant stumbling block for such a development strategy. Ethnic tourism is a product, and can be promoted easily while enabling the ethnic groups to showcase their rich cultures and heritages and to revive their traditions, languages and cultural pride.

It is observed that a key element of ethnic tourism is the [“quest for cultural otherness.”](#)¹⁴ Sri Lanka should be able to expand this tourism product to capture the cultures of all social groups in our society and showcase the country’s rich diversity. However, prior to positioning our diversity as a tourism commodity, internal peace and harmony needs to be restored. Tourism Malaysia is an example that does this successfully by promoting the delightful multi-cultural fabric of Malaysia to the world. The Sri Lankan tourism industry was affected by Easter Sunday bombings. As Sri Lanka prepares to help the industry bounce back, it is vital to reiterate the adverse impact of ethnic/religious riots. Members of all communities would be privileged through cultural tourism. Cultural tourism must be prioritised to expand Sri Lanka’s tourism portfolio. However, the authorities alone will not be able to do this. All the communities have

a role to play in removing suspicion and mistrust, to integrate into above-mentioned economic programs.

Sri Lanka has been struggling to become an export-led economy since independence. However, the country has not been able to diversify its export basket and increase its complexity sufficiently even [after 70 years of independence](#).¹⁵ In order to grow our economy by adding new products and services to the production portfolio, we need new knowledge and [know-how](#). Professor Ricardo Hausman states that the key to such diversification is access to know-how, but know-how often has to come from people.¹⁶ [India, Singapore, Vietnam and other dynamic economies](#) have accessed to know-how through FDI, flexible immigration policies and diaspora networks.¹⁷

When the country's security situation is under threat, having flexible immigration policies, however, would be difficult. Sri Lanka was about to launch an [on-arrival visa scheme](#) prior to the Easter attack.¹⁸ When communities act responsibly, with a genuine patriotism, it would be difficult to abuse open immigration policies which have been identified as a key measure to promote economic growth via export diversification.

However, ethnic/religious riots lead to a reversal of the desired results. The 'Black July' riot of 1983 is an example. These conflicts between communities compel fellow Sri Lankans to migrate exacerbating the problem of brain drain. People who left their motherland with bitter sorrowful memories and pain will also find it difficult to return and contribute to the country's development. Obtaining the support from the diaspora will also be difficult in such a context. Citizens, not just those from affected communities, will leave the country when they see that the country's development agenda is going nowhere. This potential rise in migration will hinder Sri Lanka's goal of achieving a Knowledge Economy.

VI. Undermining the Country's Competitiveness

The Governor of the Central Bank of Sri Lanka, Dr. Coomaraswamy, also notes that Sri Lanka has now, in some sense, [handed its economic sovereignty away](#) due to its external debt burden and the resulting reliance on international Credit Rating Agencies (CRA), international creditors, and agencies like the IMF.¹⁹ The country has to operate within a pretty tight policy framework. Sri Lanka, as a lower-middle-income country, is no longer entitled to receive concessional funding, and therefore, must play by the rules of capital markets.

The [rating assigned by CRAs](#) play a significant role in determining a country's borrowing cost. The main CRAs namely Fitch, Moody's and Standard & Poor use various qualitative and quantitative variables as determinants of the rating provided by them. Analysis of the methodologies of CRA reveal that qualitative factors are as important as quantitative macro-economic variables. The qualitative political and social indicators, represented by the rule of law, political stability, corruption control, regulatory quality and government's effectiveness, significantly affect the rating.²⁰ The key macro-economic fundamentals of Sri Lanka were not

in a bad shape in October 2018, as reflected in the Staff level agreement reached with the IMF on the [Extended Fund Facility \(EFF\) arrangement review](#) on 26 October 2018.²¹ The country was, however, downgraded a few weeks later due to [political upheaval](#).²² Riots influence the CRAs when assessing the robustness of the rule of law and the efficiency of the government of a country.

If Sri Lanka is to avoid a Greece type crash, improving the countries competitiveness is a must to attract FDI and improve exports. Peace and stability is an important determinant of the competitiveness of an economy. We climbed up the [Global Peace Index \(GPI\)](#) in 2018²³ as a result of Sri Lanka being one of the safest countries in the world. One thematic domain of GPI is the extent of ongoing domestic and international conflict. The UK established the '[Riots, Communities and Victims Panel](#)' after the 2011 riots, to explore the cause of riots and how communities can be more socially and economically resilient, in order to prevent future disorder.²⁴ Sri Lanka can look to the UK for lessons to minimise the fallout of similar riots in the country. Failure to bring perpetrators of internal conflicts to justice will undermine trust in the rule of law. Impunity is a key obstacle for promoting the rule of law. Dr. W. A. Wijewardena notes that [violating property rights](#) causes a long-term output loss via non-investment or inadequate investment in physical property and human capital.²⁵ It also feeds into macro-economic stress which leads to the downgrading of a country's prospects in the long term.

VII. Discouraging Digital Economy

In the aftermath of the [Easter Sunday bombing](#) and when subsequent riots were staged, social media was blocked in Sri Lanka.²⁶ A similar block was put in place following the violence in [Digana in 2018](#).²⁷ Social media platforms, such as Facebook, are catalysts for economic activity in an ecosystem composed of marketers, app developers, and providers of connectivity. High mobile penetration and access to the internet have created a conducive environment for [digital economic opportunities](#) to thrive in Sri Lanka.²⁸ Social commerce, that is, marketing via social media has also become popular in Sri Lanka. Digital start-ups are also heavily impacted when social media is suspended. Such decisions adversely affect the country's competitiveness as well. Sri Lanka must prioritise digitisation in its economic agenda. At a time when Sri Lanka is being promoted as an IT business process outsourcing (BPO) destination, banning social media and other digital platforms will impede such booming business activities.

However, there should be strategic measures to curb disinformation. Malaysia, France and Germany have adopted [legislation to fight fake news and hate speech](#).²⁹ Australia has proposed a similar bill to regulate social media after the [live streamed New Zealand massacre](#).³⁰ Singapore has also proposed the '[Protection from Online Falsehood and Manipulation Bill](#)' to prevent the communication of false statements of fact.³¹

However, legislative measures for Sri Lanka must be considered in a cautious manner, striking a balance between freedom of expression and curbing fake news and hate speech.

Telecommunication regulators can, however, negotiate with social media companies to take necessary action to discourage fake news which have an adverse impact on social harmony. The action plan against disinformation, introduced by the EU, is an example of an effective strategy.³² This [Action Plan](#) enabled the EU to build up capabilities to proactively address disinformation.³³ People have a responsibility to understand that disinformation damages democracy. Each and every one of us in our society needs to do a fact check of information prior to clicking the ‘share’ button.

VIII. Slowing Down the Growth Process

According to social science scholars, there is a [lower incidence of riots](#) in a growing economy.³⁴ They argue that in a [booming economy](#) the pie is growing and people have much to gain by living in harmony as everyone potentially gets a bigger slice of the growing pie that could be threatened by communal violence.³⁵ On the other hand, when the businesses are destroyed by ethnic/religious riots, the government is compelled to grant relief packages to affected parties. In a country like Sri Lanka where the government’s revenue is extremely constrained and severe pressure is emanating for fiscal consolidation, allocating money for such relief packages is a challenging task. The government will be pushed to switch expenditures and reprioritise development programs to find the fiscal space. This will derail the country’s development agenda and the consequences will have to be borne by all communities.

If financial institutions are required to give a moratorium and other concessionary loans to affected businesses and industries, it will impact the resilience of the financial system as well. Hampering financial intermediation also contributes to slowing growth. All communities will be victims of this vicious cycle.

IX. Increasing Communal Disharmony

We have not been able to create a genuine ‘Sri Lankan identity’ yet. According to Ericson (1994), identity is not only individual, but also collective and social.³⁶ Identity is the difference, character and sense of belonging found in interpersonal interactions and interactions between groups.³⁷ People are considered the greatest asset of a nation. Our inability to have ‘unity in diversity’ has made it difficult for Sri Lanka to make its people a winning force for the country. Singapore has introduced the [Maintenance of Religious Harmony Act](#)³⁸ to take action against those sowing religious discord and ensure that religion is not exploited for political or subversive purposes. [Canada](#) too has introduced similar legislation.³⁹ If the true spirit of all religions is followed, these kinds of statutes would not be required. In the absence of a unique identity as a nation, branding the country’s image in a competitive world is also an arduous task.

X. Conclusion

Social disharmony costs the economy in various ways. Fostering good interfaith relations is, therefore, the responsibility of not just religious leaders and politicians but all stakeholders of our society. Diffusing tensions among communities should be a long-term genuine plan which needs to commence at schools. Citizens living in a diverse society, like Sri Lanka, need to work towards a common goal. Irrespective of race or faith, the common goal of protecting and developing the country must transcend religious, racial and cultural boundaries.

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