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Points to ponder before privatizing public agricultural institutions

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I wish to share a few lines of thoughts on privatizing institutions serving the agricultural sector, expecting that it may help us to proactively ponder prior to privatizing and thereby address the probable adverse implications. I wish to emphatically state that I am by no means opposing public sector reforms. I am only proposing for effective and meaningful economic reforms. The points that I am raising are based on a book, that I recently read, titled "Smallholder Cash Crop Production Under Market Libaralisation: A New Institutional Economics Perspective" edited by Andrew Doward, Jonathan Kydd and C. Poulton of the Imperial College at Wye, England, published in 1998.

Since the 1950s the strategies adopted to achieve economic development in Sri Lanka, as well as most developing countries, has oscillated between the two extremes of depending on the state and depending on the private sector. There are political proponents to support both extremes; some guided by strategic pragmatism and some infatuated by idealism. Needles say, that as the oscillation achieves equilibrium, the best strategy for economic development ought to be the middle path, of using a mix of state and private sector. Though there are theoretically strong reasoning in favor of privatization, unfortunately we Sri Lankans have to undertake privatization not on such reasoning, but frankly because we do not have a choice. We are so much in debt that we are compelled to "sell-off" public assets to meet loan repayments and public expenditures and to obtain further loans we need to accept conditions of privatization imposed by international lending agencies. Yet if we are convinced of the need to follow a middle path in economic development and could make our point clearly and fact-fully we should be able to convince the international lending agencies.

After all those in these agencies are as ignorant or sensible as we are.

The book mentioned above summarizes the response of the small holder cash crop farming sector of some African and Asian countries to the adoption of structural adjustment policies in the past two decades advocated by international lending agencies.

We all know that privatization is referred to in different terms when applied to different levels of the economy and depending on who is being addressed by whom etc. Structural adjustment simply refers to adopting policies and government finances at the macro scale of economy, to favor private sector lead economic development and at an institutional scale privatization may be referred to as organizational reform and so on. We, in Sri Lanka too have adopted structural adjustment policies since the early 1980s but the adoption of these policies in the agricultural sector was rather late and slow.

In the agricultural sector we have initiated reforms in the land markets, trade, internal marketing, input provision such as in extension, supply of water etc. It is definitely to early to judge success or failure of these reforms. But before we get in to mess we could perhaps learn from experiences of other countries. To quote from the above mentioned book:

"Although African governments were slow to respond to external advice to liberalize the agricultural sector, most have traveled a fair distance in this path but have, at best realized modest success. In particular, input and credit supply systems for Smallholder agriculture are in a parlous state and, in general, are failing to make progress towards the World Bank's objective of rapid sustainable intensification."

The authors point out that many were successful in identifying the failures of public institutions (government failure) but not probable failures of private institutions (market failure). As in the countries reported in the book, in Sri Lanka too we observe that arguments for privatizing are centered largely on the inefficiencies of state provision of services arising due many factors such as corruption, over-employment, lack of motivation for productivity improvement and so on. We should acknowledge that some of reasons for public sector inefficiency were closely linked to the politicization of the management of these public institutions. We should not fail to understand why public institutions were created in the first place. The public institutions were created, as there wasn't a private sector to undertake such economic services in the agricultural sector at that time. Virtually all services to the irrigated colonization schemes where paddy production was dominant were provided by the public sector since the 1950s. Despite what ever is said of public institutions we have achieved near self-sufficiency in rice production.

At this point in wanting to privatize the public sector (going by the 'waves' on development thinking and the lack of choice) we should first give due credit to the public sector for what we have achieved thus far in terms of agricultural production whilst accommodating politicization. Next prior to privatizing we should ponder whether yet we have a private sector that is capable of undertaking what the public sector did thus far (even as alleged inefficient). Let me quote from the above-mentioned book on experiences of some African countries that undertook privatization in the agricultural sector.

"An alternative explanation for the apparently disappointing response to market liberalization was that ... an unduly optimistic view (was held) of the potential of the African private sector to provide the services previously provided by the state organs. ... Private traders, often discriminated against and harassed for decades, did not possess the managerial skills, business experience or capital to move straight in to large-scale activity. In many places, indigenous entrepreneurs have never fulfilled these roles, even prior to independence. Rather ethnic minorities, such as South Asians and Lebanese (this is in African countries) have carried them out. One of the aims of nationalist, post-independence governments had been to prevent such groups from achieving economic dominance, given the weak ness of indigenous entrepreneurs. Beside this ethnic angle, there were reasons why private enterprise alone might be reluctant to take on some of the former activities of parastatal organizations. In rural areas, for example, small holders are often geographically dispersed, roads and communications poor and the volumes of business insufficient to encourage private sector service provision.

Moreover, services such as research and extension have clear public goods properties, which will tend to discourage private sector involvement. There are in other words high probabilities of market failure in key liberalized markets. Other services, such as wholesale grain trade and some agricultural processing operations, exhibit the significant economies of scale, such that even where services are provided by private operators, the market may not be competitive and prices offered to farmers may be depressed"

The experiences we in Sri Lanka have by now realized, in privatizing the marketing of paddy by privatizing the Paddy Marketing Board, is closely similar to above quoted experiences of African countries. Since privatization or elimination of the Paddy Marketing Board during the past few years we have not observed much success of private sector involvement.

The paddy purchase prices offered by the private sector was much below the cost of production of paddy. The private traders did not have the required finances, storage space etc to fill the vacuum created by the withdrawal of the state sector. Again the state has to provide subsidies to the private traders as well as farmers to store paddy. We do not know whether these subsidies cost more than maintaining the Paddy Marketing Board. Whether the price competition provided by the Paddy Marketing Board would prevail given the present non-competitive monopolistic nature of the paddy marketing sector is yet to be seen but the present signals are that competition among private traders seem to be not providing better prices to farmers. The private traders tend to collude rather than compete on prices. This reminds me of how, about 15 years ago, a manger of a rural cooperative in Ridimaliyadde (close to my birth-village) in Mahiyangana taught me of the minimum role of state institutions in rural agricultural marketing. Whilst doing a study on 'irrigation practices in non-paddy crop cultivation' in Nagadeepa irrigation scheme in Ridimaliyadde, I stepped into the government cooperative. As one would expect, it had mostly empty shelves, with few bakki's with few kilos of karawela and parrippu. I asked the manager, whether there was any purpose served by keeping the cooperative open, only to sell karawela and parippu. He pointed to the price board, and said that, at least the prices on the board assures a minimum prices for the farm products and that service itself warrants to have the cooperative. Did we have this wisdom prior to deciding to eliminate the Paddy Marketing Board? What is the mechanism that we put in place to assure fair prices through private sector competition in paddy marketing? This is not to say that the Paddy Marketing Board was efficient and did not require reform.

It did require reform but not elimination of its functions. Even if it was to be eliminated we should have thought of how the state could sustain some functions that the private sector may not provide and how the private sector could be guided such that efficiency and equity are both achieved.

This article is not expected to be empirical and an academic critique of the privatizing process but as said earlier to be briefly suggestive of what we should ponder prior to privatization. Hence let me briefly focus on an agricultural institution that is impending privatization- the public banks. The public banks, particularly the Peoples' Bank and the Bank of Ceylon were established to provide development financing, in which financing the agricultural sector was primary. I read recently several articles in the newspapers arguing for and against the privatization of these banks.

Some were very fact-fully critical of the weaknesses of the marketing strategies of these banks. Being a customer of one of these banks for nearly two decades I would agree that these banks are not efficient, as we would like those to be. Yet we should not ungratefully forget that these banks were initiated primarily for a purpose that the private sector did not efficiently undertake, that is financing the rural agricultural sector, which these public banks did thus far.

Among the more than 25 or so private banks in Sri Lanka we are yet to see success in rural agricultural financing.

The book that I have mentioned above clearly documents the experiences of some African and Asian experiences with respect to the importance of agricultural credit to support commercialization of agriculture.

It proposes the need to strengthen alternative institutions to support the supply of credit prior to withdrawal of state institutions and dependence on the private sector. The formal private sector may fail to fill the vacuum that would be created in rural agricultural financing with privatization of the public banks.

The reforming of the banks may be inevitable for reasons mentioned above. Yet, learning from other countries and from our recent experiences in privatizing paddy marketing, let us seriously "think before we leap" on how we could sustain or replace some of the functions that the private sector may not be capable in providing. In banking one such could be the financing of rural agriculture due to its inherent nature of high transaction costs, high risk (not only induced by nature and markets but also by the political system) and thereby low profit. Yet we have to sustain rural agricultural finances; for sake of food security, for sake of sustaining the livelihood, unfortunately of those who feed us, the farmers.