Sri Lanka: No quick fixes for household debt crisis!

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Thanks to elections, rural debt problem has resurfaced as a prominent issue in the public domain. While some candidates have vowed to cancel the rural debt, others have pledged to find solutions to the problem and the agrarian crisis. Such accentuated attention from the people who seek power to assume the highest political office is a positive development though should be read with care. Recognising the problem is the first step to address it. While the bulk of the problem remains to be solved, solutions could learn from measures already taken. This article makes an attempt to understand the problem of indebtedness both at the rural and urban setting. I argue that over-indebtedness is a direct outcome of the unchecked government policy of rapid financialization over 15 years. The impact of debt waiver introduced in 2018, in easing the debt burden from households is problematic. Debt cancellation is useless in an environment where people lack the means to fulfil basic needs. Precarious lives of rural and urban poor should not be tools to be manipulated for political gain. Policymakers should face real socio-economic questions on reviving productive capacities of the economy to generate decent jobs and provide living wages, land, housing and public things.

Financialisation and poverty

For a country of 21 million people, Sri Lanka has a deep mosaic of formal and informal finance network. It could be the largest finance network per capita in South Asia. Between 2005 and 2015, the number of registered finance companies increased from 28 to 44. This is also supplemented by a significant portion of unregistered microfinance institutions, and other actors of the informal money market. One may assume that such a rapid expansion of the finance sector, which designates increased access to financial services, would trigger development and enhanced living status.

Data narrates a different story. The recent elevation of Sri Lanka to the status of an upper-middle-income country whitewashes deepening inequality. Household Gini coefficient, which measures inequality have increased to 0.45 in 2016 compared to 0.35 in 1973.

When the wealthiest 20% bags a monthly income of 158,072, the poorest 20% only gets an income of 14,843. Such a disparity is also visible in an urban, rural and estate sector comparison. Instead of jobs that can guarantee living wages, 68% of the available jobs in Sri Lanka came from the informal sector by 2017. Unstable and hazardous living conditions grounded on deepening inequality, informalisation of the labour market and intensifying financialisation became very clear with the microfinance crisis. A lot has been said on this. However, government action and response of policymakers do not show a clear understanding of how this problem is connected to broader economic questions related to government policies.

Debt relief, a bail-out package to finance companies

In the aftermath of protests by the indebted women in the North, the government announced a debt waiver to 12 drought-affected districts. A total of 45, 139 loans were waived off under this policy. However, it's a minimal measure to address a profound and widespread problem.

As I mentioned above, it was only implemented in 12 drought-affected districts. Only those who had defaulted three times could enjoy the benefit of Rs. 100, 000/= of their debt being waived off. Other women who defaulted more than three times or managed to meet weekly payments with enormous difficulties were not entitled. Also, indebted women of the other 13 districts were excluded from it. According to the Household Income and Expenditure Survey 2016 districts such as Kalutara, Matara, Galle, Hambanthota, Nuwara-Eliya, Matale and Kandy also record a very high prevalence of debt related to finance companies. In addition, these places also indicate a significant dependence on the informal sector by borrowing from money lenders and retail outlets.

And even in the 12 districts could it really lift debt burden off the shoulders of indebted women? The way this relief measure had been executed through finance companies makes it look like a bailout package to the finance institutions. According to the 2018 Annual Report of the Ministry of Finance 37 registered microfinance institutions and finance companies benefitted from the debt relief package.

The other element of the government action was an interest rate cap to regulate interest rates of microfinance lending. The Central Bank, the empowered entity to regulate the financial sector is a reluctant actor. Instead they advocate self-regulation. After mobilising by researchers and activists, an initial proposal was made to impose an interest rate cap of 30%. When it was implemented in December 2018, this rate was pushed up to 35%. The government is working towards introducing a new credit regulatory authority Act to regulate the money lending institutions, including the microfinance sector.

The poverty capital

Can a debt relief programme, an interest rate cap and regulation address the problem of indebtedness? Are these adequate measures to address the predatory practices of microfinance?

Microfinance is an industry that sprouted in Sri Lanka within a short period. According to research, numbers of microfinance institutes multiplied after disasters; natural and man-made. One such occasion was the tsunami in 2004. Another was the end of the Civil War in 2009. As a result of increased donor funding, the number of MFI outlets increased from 83 in 2002 to 14, 000 by 2015. Since the provision of affordable credit to rural poor started to change hands from the government to private market actors in early 90s, donor funding has played a significant role in determining the character of microfinance and its role in addressing poverty. Despite the expansion of the formal banking sector in Sri Lanka, the poor people, as well as people who are almost poor, are more likely to access the informal sector for their financial needs. Regardless of the national statistics, this category encompasses about 40% of the country's population and has been ideal fodder for the microfinance industry to feed on. The formal banks have not made an effort to lend to this 'financially risky' group. However, the growing microfinance industry has created them a profitable business venture to expand corporate lending. The microfinance industry is seeking innovative ways to penetrate into the "unbanked and financially underserved" group of poor people by tapping into highly available credit from international investors and local banks. The task of the microfinance industry is to cater to their "appetite for different financial services". Mobile finance is an example of such innovative digital financial practices. A finance company, in partnership with a telecommunications service provider, started the first of such services in Sri Lanka in 2018. Poverty has become a profitable business for them.

The finance industry has been profiting from the refusal of the politicians as well as policymakers to accept serious dispossession embedded into the present economic development strategy. National indicators of poverty in Sri Lanka indicate that conditions of poverty have improved progressively. Poverty Head Count Index accounted by the Department of Census and Statistics demonstrate a gradual decline in the status of poverty across Sri Lanka from 1996. Poverty headcount index accounts for the number of people excluded or falls behind from participating in market activities as consumers. How could one explain such a steady decline of poverty and a heightened situation of insolvency and indebtedness in the rural and urban sectors? If overall poverty has reduced, why do women and men kill themselves unable to pay their weekly debt instalments? Deteriorating living conditions in the face of increasing costs for education, health care, transport, housing and food have forced people to borrow for consumption. Debt driven consumption has led to an artificial improvement in poverty statistics. Refusal to recognise this complex nature of poverty where the poor are trapped within a web of debt will undoubtedly lead to more loss of lives of poor women and men. 'Enterprise Sri Lanka' is the highest manifestation of such a denial. For poor borrowers, loans usually mean loss of land, houses, gold, migration and even loss of lives. Unlike for the poor, loans have been extremely profitable for the lenders.

What to do?

The solutions proposed to this debt menace have been to cancel the debt and pump more money to the poor. Viyathmaga, the intellectual and professional lobby that creates policies for a future government led by Gotabaya Rajapaksa, has proposed to release 25% of all Samurdhi balances to the account holders to enhance their purchasing power. Also, they are proposing to introduce a moratorium on capital repayment. Pumping money to the economy would temporarily ease the problem by facilitating consumption and get the economy going. However, it's only a temporary remedy. None of the exchanges on cancelling debt address the close nexus between increasing indebtedness and the state policy of financialisation. The proposal unless carefully monitored may finally end up benefitting the elitist layer of the society.

The financial sector may be a golden goose with benefits limited to the financiers and the rich. For the rest, the financial system has been at the heart of disinvesting funds from the productive services that can generate decent jobs, deliver living wages and fund public services and public infrastructure. A perfect example is the boom in Real Estate in Sri Lanka. When high-end housing complexes proliferate Colombo opening up investment opportunities for the wealthy, renting houses/ apartments has become an almost impossible task even to the middle class. The irony of such financialised development is when the same finance sector starts to loan to the homeless poor who cannot find money to pay for housing advances when they rent.

Therefore, addressing indebtedness among rural and urban poor needs a comprehensive approach which accounts for its basic underlying causes. Re-orienting the state-owned banks to their public role and renationalizing development banks and restructuring the formal banking sector to embrace the poor and formulating policies on land and housing which restrict financial expropriation are a must. These policies should be in tangent with state action to reverse structural reforms which have weakened public enterprises, and public services. A debt write-off should also accompany creation of mechanisms to obtain easy and affordable credit for the poor. Examples from North of Sri Lanka show that the co-operatives are capable of serving this function. As much as the poor should not be a profitable market for a few, the poverty and the poor should not be the subject of quick-fixes and political mileage.

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