EF 3460 AISIA PACIFIC ECONOMIES

COUNTRY RISK ANALYSIS

SRI LANKA 1989-1999

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Sri Lanka—Country Risk Analysis

Introduction

Sri Lanka gained independence from British colonial rule in 1948. Economic reforms from 1977 onwards, Sri Lanka had continued implementing liberal market-friendly trade policies. Sri Lanka had been able to achieve moderate rates of economic growth. Agriculture had been the leading sector in the economy up to the 1970s, when the main policy emphasis had been on import substitution. In the past, Sri Lanka inherited a dualistic agriculture economy. This dualistic agricultural economy consists of ‘plantation agricultural sector’ and a ‘non-plantation agricultural sector’. The plantation agricultural sector is concerned with the production of tea, rubber and coconut, etc. the produce of this sector is mainly directed towards the export market. The non-plantation agricultural sector is concerned with the production of food crops and livestock products. But Agriculture livelihood depended on uncertain weather condition and world market prices. It may cause market unstable. From 1977 onwards, policies had shifted towards the promotion of export-oriented manufacturing activities. Major exports currently included clothing, tea rubber products, gems and jewellery, and coconut products. The reform measures undertaken by Sri Lanka had immense socio-economic implications. Previously, Sri Lanka had sought to create a welfare State, through a high level of State intervention. It had change policies and now relied on market forces to generate and maintain the growth momentum needed to ensure the economic and social well-being of the people. Economics reform in the 1990s. Tariff reduction programme and the elimination of import licensing for most non-agricultural product, with the goal of improving the country’s export
competitiveness. Besides, the government set a goal that Sri Lanka should become a newly industrialized country (NIC) within next decade. And Government made effort to provide adequate infrastructure facilities throughout the country, including telecommunications, transport and port facilities. The Government had simplified investment procedures.

Generally say, economics in Sri Lanka is growing after 2 economics reforms. As, the GDP from 1988 to 1999 have kept on a positive improvement (Table 1). But there are still have some potential economics risk that should improve within the country.

![Table 1: GDP Growth](image)

<table>
<thead>
<tr>
<th>Year</th>
<th>Rupee</th>
</tr>
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<tbody>
<tr>
<td>1988</td>
<td>0.00</td>
</tr>
<tr>
<td>1989</td>
<td>200,000.00</td>
</tr>
<tr>
<td>1990</td>
<td>400,000.00</td>
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<td>1991</td>
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<td>1993</td>
<td>1,000,000.00</td>
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<tr>
<td>1994</td>
<td>1,200,000.00</td>
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</tbody>
</table>

**Risk Analysis**

**National Account**

Too rely on the imports of good and services, the imports of goods and services is in average 40% of GDP but export of goods and services is in average 35% of GDP. (Table 2) If the foreign exchange rate is changed dramatically, then their net export may suffer.
Negative net primary income from abroad, it means that the income to abroad is larger than the income from abroad; it may because of the large amount import payment, etc. It may enlarge the total expenditure since this item have a high annual % increase from 10% in 1991 to 54% in 1999. Although it may not have significant change or no significant proportion of GDP (1% of GDP), we should aware of this change.

**Fiscal Situation**

Long term Fiscal Deficit, which may affect the foreign investor incentive to invest. Sri Lanka’s fiscal situation has deteriorated significantly in recent years. The overall fiscal deficit (excluding grants and revenue) is estimated to have been about 14 percent of GDP in 1997 and the 1999 is about 15% of GDP (Table 3).
The adverse consequences of high fiscal deficits are becoming increasingly and continuously which because:

- First, the task of regaining macroeconomic stability is made more difficult, with an excessive burden placed on monetary policy.
- Second, national saving are depressed, limiting the scope for domestic investment and public debt is very high.
- Third, the ability to attract sustainable foreign savings in the form of foreign direct investment is diminished.
- Forth, the process of structural reform is jeopardized, particularly financial sector reform as the government continues to rely on financial repression.
- Fifth, the crowding out of spending in the health and education sectors and the slowdown in capital expenditures endanger future economic growth.

Heavy debt burden, total debt is extremely large proportion per GDP from 1988 to 1999 which change from 76% to 209% of GDP (Table 4). Foreign grants and borrowing financed the Government’s budget deficit, largely because of the exceptional increase in foreign loans connected with imports of military hardware. Although Sri Lanka continued to benefit from High Debt in a country may cause a
higher interest paid in every year and it may form an unhealthy economic atmosphere in a country at finally.
**Recommendation**

After the Civil War, more and more investment capital was poured into nonproductive weapons purchases and military budgets. Until now, the conflict occupied a much greater place in political than in economic developments, but the corrosive effects of war eroded even further an already untenable economic structure based largely on government control of the economy. Although there are some improvement after the economics reform, it still have some risk which we should pay attention.

For the National Account, the government should have some suitable measurement to reduce import of goods and services, since the country may be sensitively affected by the foreign exchange rate. And it may affect the overall GDP. Conversely, it is good that the country keep in limited inventory (only 0.009% of GDP in 1999), as inventory is easier outdated and worthless. But we should aware that there may have shortage if anything suddenly happened, such dearth or chaos.

For fiscal deficit, a balance and sustainable fiscal correction will require adjustments which are also consistent with improving both the efficiency of operations and the incentives for private investment. Hence, the quality and composition of fiscal adjustment are no less important than the magnitude and speed of deficit reduction. Specifically, the demands for productive spending in areas such as education, health care, and infrastructure will need to be met. To provide room for such expenditure, other current spending, including on subsidies and on the wage and pension bill, will need to be restrained.
Finally, as a member of the WTO, Sri Lanka should place emphasis on the infrastructure such as consummate transportation, telecommunication facilities, etc and fair trade policy such as low government intervenient, simple procedure, low tariff or taxes. All this can attract more foreign investment, even local investment. And it may benefit to our GDP and their citizens at eventually.