Increasing growth to 5-6% will depend on investment flows to the country

By Jayampathy Jayasinghe

Sri Lanka sees a reshaped recovery on the cards assuming a focused growth to pre-pandemic output level. But the critical challenge is to lift the growth rate to 5-6 percent and to maintain it in the medium term depending on how investments will perform. "But Sri Lanka had little fiscal space to rely on when compared to other countries that rolled out large fiscal and monetary stimulus packages. Sri Lanka had to depend on monetary policies of the Central Bank to ensure that the borrowing cost was kept low," said Dr. Dushni Weerakoon, Executive Director of the Institute of Policy Studies (IPS) on the topic, "Sri Lanka: State of the Economy 2021" at the launch of the IPS 2021 annual report at a webinar held in Colombo.

"We have very low reserves in hand and 72 percent of revenue collection went for interest payment of debt. Foreign debt amounts are of sizable amount in the medium term and we have low reserves in hand. But this kind of flexibility is not available in the IMF programmes and that may be the reason why Sri Lanka is not keen to engage with the IMF facility. The Government too will not resort to harsh austerity measures that may have unintended consequences that will have social unrest in the country," she said.

Replying to a question from the panel, she said that tightening of monetary policy in the US will have direct consequences to Sri Lanka's exchange rate. However inflation has not taken root in the US but is a transitory phenomenon.

Dr. Asanka Wijesinghe, Research Economist of the IPS, referring to the ongoing trade war between the US and China due to different ideologies, said the issue has not been resolved as yet and the tariffs adopted by former President Donald Trump have not been reversed by President Joe Biden as yet as they fear a backlash in some constituencies.

Although there is no de-globalisation there is a slowdown in globalisation, according to economists. Although the WTO's initial predictions were gloomy regarding trade that predicted a collapse, it is now looking better.

The US is now looking at the possibility of looking at realigning itself with supply chains of critical goods such as raw materials like lithium and cobalt and semi-conductors. Their strategy is to take products away from China and to align with countries in the European Union (EU) and Japan, India and Australia. On the contrary China's strategy is to align itself with strategic economic partnership with countries in the region. Sri Lanka has a chance of benefiting from China's huge global trade. It is also important for Sri Lanka to align with EU markets for local exports. The GSP + withdrawal can affect Sri Lanka by US$627 billion including textiles and seafood markets. Sri Lanka can gain a lot by exporting semi - conductors and electronic goods to the global market.

Dr. Missanka Warusawitharana, Financial Economist, Johns Hopkins University, said looking at Sri Lanka's evolution of the economy from a longer perspective, the growth trajectory is a bit slower at the end of the war in the early part of 2010.

The growth has lagged behind Sri Lanka's neighbours. The slow growth has been attributed to the productivity growth that has not been able to reach its potential. The manufacturing sector in Sri Lanka has not done well to reach a higher growth trajectory due to trade restrictions, he said.

The removal of hinderances to the private sector will enable businesses to reach a higher growth rate. However the fiscal situation of the country, driven by structural imbalances in budgets over the decades under multiple administrations has contributed to the weakening of the economy. The higher debt growth has interacted with the low productivity growth of the country, faced with difficult fiscal choices to be made.