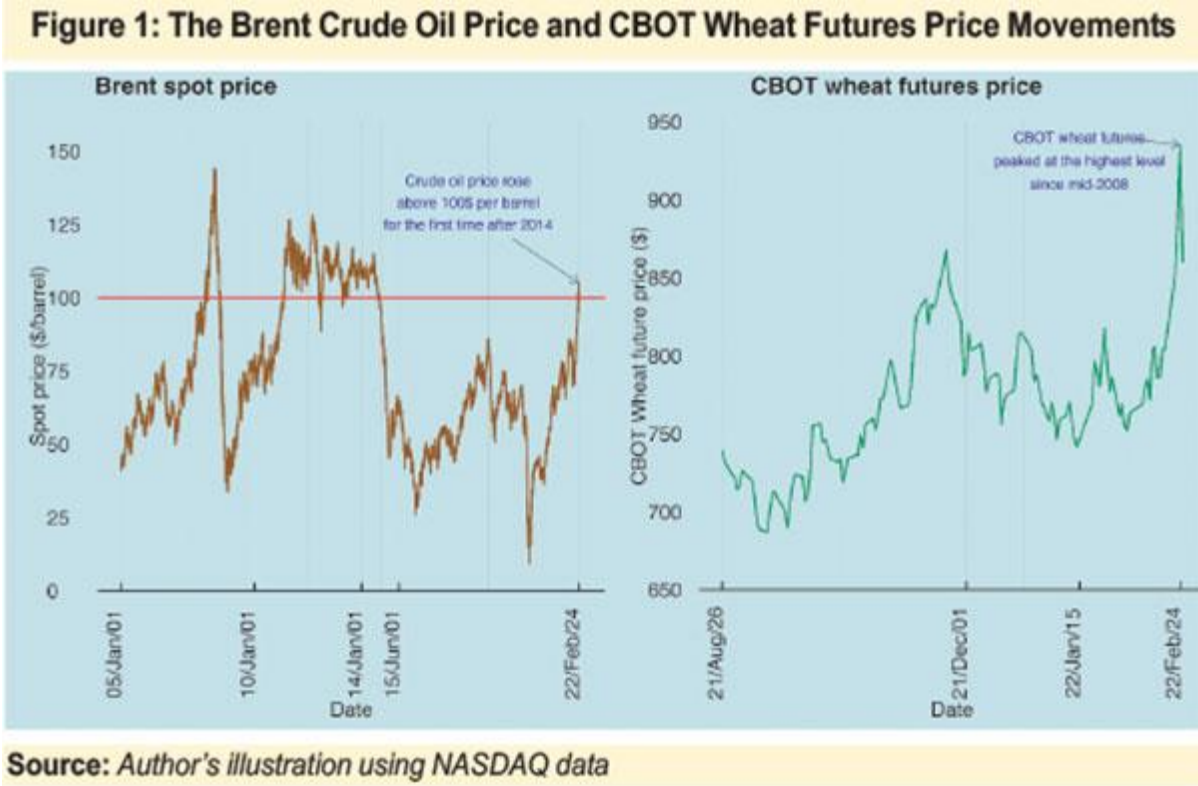




BUSINESS

Russia-Ukraine conflict: Economic implications for Sri Lanka

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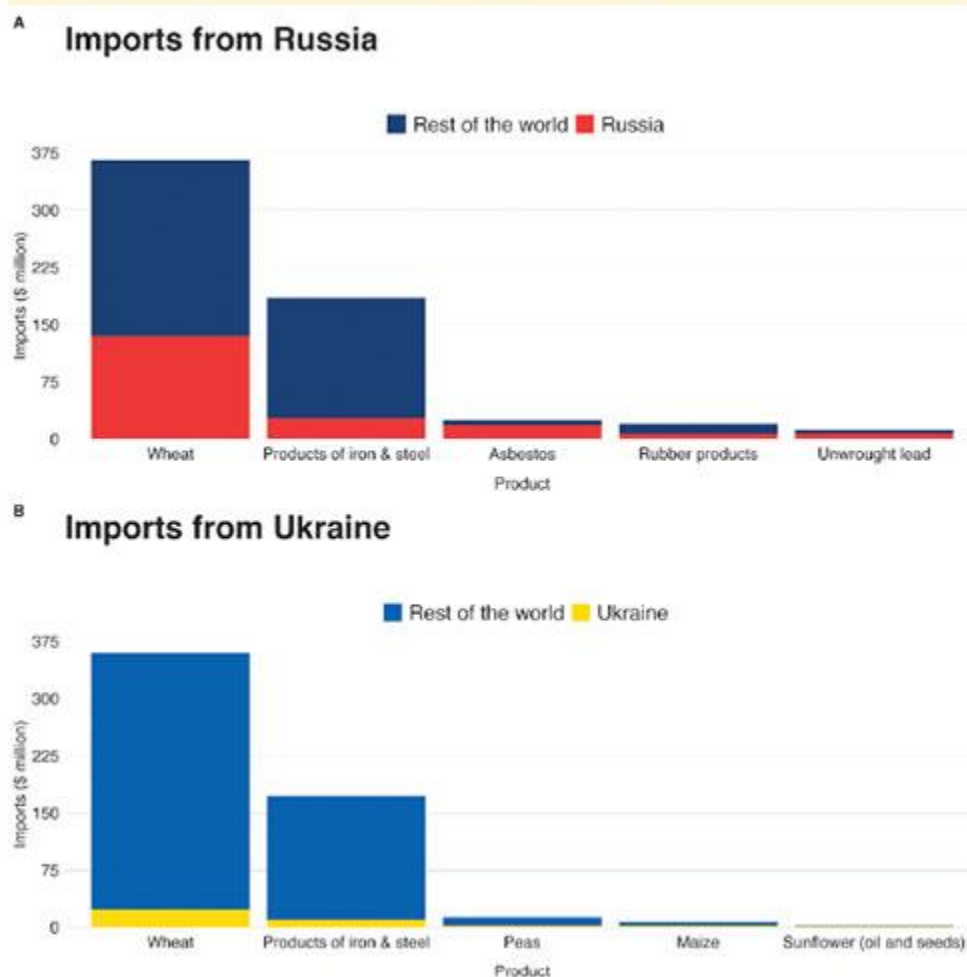


f By Asanka Wijesinghe



The Russian invasion of Ukraine deepens the existing global supply chain bottlenecks and associated rising inflation, clouding the prospects of a smooth global economic recovery after the pandemic. The West, led by the US and the EU, swiftly imposed strict economic sanctions, targeting Russian billionaires, oligarchs, political leaders, and state-owned and private companies, generating additional uncertainty over the global economic outlook. The initial disunity in the West on cutting off Russia from SWIFT—a global financial telecommunication system that enables the smooth and rapid cross-border transaction of money—was resolved over the weekend. Such a move will inevitably make payments for Russian exports and imports hard. The ongoing military conflict in Europe could not have come at a worse time for Sri Lanka given its own prevailing high inflation, rising energy costs, and scarcity of foreign exchange. Against this backdrop, this article discusses the economic impact of the European conflict on Sri Lanka, the sectors that will be hit hard, and ways to mitigate the negative impact.

Global Economic Impact

Figure 2: Sri Lanka's Imports from Russia and Ukraine

Source: Author's illustration using Trademap data

Immediately after the Russian invasion on 24 February, commodity markets rallied and the Brent spot price of a crude oil barrel reached USD 105 for the first time after 2014. Similarly, the cost of wheat futures for March 2022 in the Chicago Board of Trade (CBOT) exchange peaked, at its highest since mid-2008 (Figure 1). The Russian Federation and Ukraine as Europe's breadbasket- are major cereal, fertiliser, critical minerals, and iron and steel exporters. Meanwhile, the Western powers were busy over the weekend in negotiating tighter sanctions on Russia.

While the fate of Ukraine hangs in the balance, the consensus among analysts is that Ukrainians were mounting a fierce and unexpected resistance, effectively increasing the pressure on Russia. The US, EU and their allies are contributing to the military conflict by providing financial and military assistance to Ukraine while imposing sanctions on Russia to make transactions difficult. Thus, the severity of the global economic impact will be determined by the scope and duration of the conflict and the effectiveness of Western sanctions.

Western countries will be keen to minimise the spillover effects of sanctions on their economies. Like Germany, the major European economies heavily depend on Russia making it necessary to exempt the energy sector from sanctions. Indeed, the sanction package unveiled by the Biden administration did not target the energy sector. As long as payments for energy-related transactions go through non-sanctioned and non-US financial institutions, an unconstrained flow of money is guaranteed. Thus, oil prices dropped in futures closing below USD 93 a barrel in New York. However, that optimism was largely in early trade on 28 February. The Brent price rallied over 100 dollars again while wheat, soybean, and corn futures were up. Cutting off Russia from SWIFT and imposing sanctions on the Russian Central Bank can deal a severe blow to the Russian economy in the long run. A collapsing ruble can be a harbinger of Russia's economic collapse. A possible economic recession will reduce Russian demand for foreign products, and if Russia cuts off natural gas to the European market, a likely outcome will be a recession.

Implications for Sri Lanka

Overall, Russia and Ukraine account for 2% of Sri Lanka's imports and 2.2% of export destinations. However, both countries are vital import sources for wheat and export destinations for Sri Lanka's black tea (Figure 2 and 3). Russia and Ukraine purchase about 18% of fermented black tea (>3kg) exported by Sri Lanka. Similarly, 45% of Sri Lanka's wheat imports are sourced from Russia and Ukraine. In addition, more than half of Sri Lanka's imported soybeans, sunflower oil and seeds, and peas are from Ukraine. Moreover, Russia and Ukraine are significant sources for asbestos, semi-finished products of iron and steel, copper (cathodes), and potassium chloride for fertiliser.

Unless the Ukraine crisis is not solved immediately, the fuel and commodity prices can rise further. The inflationary pressure in the Western markets, especially in Europe due to rising energy prices and supply chain bottlenecks, may reduce consumers purchasing power, lowering the demand for goods exported by Sri Lanka. Europe is a significant export destination for readymade garments, tea and spices, and seafood.

There is also a growing tendency for increased military expenditure in the long run, which might reduce the "peace dividends" for European households. For example, the German Chancellor committed 2% of GDP for defence expenditure, addressing an extraordinary session of Bundestag. Replacing consumerism with militarism will adversely affect countries like Sri Lanka that depend on the European export market. In addition, a prolonged conflict will impede Sri Lanka's ability to purchase necessary raw materials like fertiliser. Imports

Lanka's exposure to the situation is mainly through linkages to the commodity and E export markets rather than direct exposure to the two countries involved in the confl

Mitigation

Sri Lanka should focus on safeguarding access to vital raw materials and food commc Globally, responding to the crisis, countries are stockpiling grain and exploring alteri ways to do business with Russia in purchasing raw materials. Sri Lanka has limited o mitigate the impact on already deteriorating food security conditions and access to r materials. As wheat and rice are substitutes, high wheat prices may increase the dem rice.

Thus, it is necessary to remove input shortages like fertiliser to ensure domestic proc adequate. Due to the current foreign exchange crisis, Sri Lanka's ability to effectively shocks is constrained. Thus, the urgent priority is to resolve the current foreign exch crisis to regain the ability to trade swiftly. Achieving debt sustainability and securing inflows from multilateral institutes might be the options at Sri Lanka's disposal. The:

entering forward contracts for raw materials and fuel and negotiations with friendly countries for food on predetermined prices are possibilities.

Link to Talking Economics blog:

Russia-Ukraine Conflict: Economic Implications for Sri Lanka

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BUSINESS

SEC directs CSE to temporarily close the stock market

Published 11 hours ago on 2022/04/18

The Board of Directors of the Colombo Stock Exchange (CSE) by way of a communication dated 15th April 2022 has called upon the Securities and Exchange Commission of Sri Lanka (SEC) to temporarily close the stock market citing the present situation in the country.

Many other stakeholders of the securities market including the Colombo Stock Brokers Association have also sought the temporary closure of the market on the same grounds.

The SEC has carefully considered the grounds that have been adduced by them and has evaluated the impact the present situation in the country could have on the stock market, particularly the ability to conduct an orderly and fair market for trading in securities.

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HNB renews long established partnership with Expo Property Developers

Published 11 hours ago on 2022/04/18

HNB PLC has renewed its partnership with Expo Property Developers (Pvt) Ltd to present customers with special feature/value additions on properties offered by the real estate giant.

The partnership will be an opportunity for HNB customers to gain access to one of Expo Property Developers exclusive luxury condominiums spread out across the city of Colombo from March. A special ceremony was held at HNB towers to mark the occasion with the presence of HNB Deputy General Manager- Retail and SME Banking, Sanjay Wijemanne and Expo Property Developers Expo Property Developers (Pvt) Ltd Director, Gratien Fernando.

“This is an ideal time for prospective homeowners to invest in the home of their dreams. (

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BUSINESS

SL delegation heads to U.S. to seek USD 4 bailout from IMF

Published 11 hours ago on 2022/04/18

Minister of Finance, Ali Sabry and a delegation left the island yesterday for discussions with the International Monetary Fund in order to receive its financial assistance and thereby rebuild confidence about Sri Lanka among the global investor community.

The delegation which left for Washington, D.C. included Governor of the Central Bank Dr. Nandalal Weerasinghe, Secretary to the Ministry of Finance K.M.M. Siriwardena and a senior delegation from the Ministry of Finance and the Central Bank.

Finance Minister Sabry recently stated to foreign media that talks with the International Monetary Fund (IMF) would begin on Monday (18) seeking a bailout of USD \$ 4 billion.

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