



SIPG



Policy Brief on
**Current Sri Lankan Economic
Crisis and Lessons for other
South Asian Countries**



This policy brief is an outcome of a webinar on “Current Sri Lankan Economic Crisis: Lessons for other South Asian Countries”; organised by the South Asian Institute of Policy and Governance (SIPG) of North South University, Bangladesh on 24 April 2022.



“The root causes of the current economic crisis in Sri Lanka are mainly due to huge investments in unproductive development projects, poor governance, corruption, and mismanagement of funds.”

Mr. Channa De Silva

Chairman, Sarvodaya Development Finance, Sri Lanka

“Populist policies like banning chemical fertilisers resulted in declined food production and tax cuts have reduced the revenue collection causing this unprecedented crisis.”

Ms. Sulochana Ramiah Mohan

Deputy Editor, Ceylon Today, Sri Lanka





“It is necessary to accurately estimate the demand for development projects as well as the project's gestation period.”

Dr. Nazneen Ahmed

Country Economist, UNDP, Bangladesh

“A government should not experiment with foreign policy during volatile times such as pandemic, which may have contributed to Sri Lanka's current condition.”



Ambassador Shahidul Haque

Professorial Fellow, SIPG, NSU



“For Sri Lankans, the revenue drop was even before the pandemic, after the Easter Sunday bombings, that downturned their tourism sector. And later on, the pandemic hit the tourism sector severely.”

Dr. Gour Gobinda Goswami

Professor, Department of Economics, NSU

Background

Sri Lanka's quick descent from glory to a horrific financial catastrophe stunned the globe, especially the South Asian region. Many countries believe Sri Lanka is an "eye-opener" to understand how the policy decisions and the government's populist stance can trigger a crippling economic crisis. Sri Lanka was upgraded to an upper middle-income country in 2019. However, in the World Bank's newest nation classification by earnings, its status has been lowered from higher middle-income to lower-middle income.

Although the Government claims that the financial crisis stems from old debts that collapsed further during the Covid-19 pandemic, many consider Sri Lanka's present situation to be the result of long-running corruption, a lack of judgement and insight in governance, and the politicisation of local and foreign businesses at every turn. The current economic crisis has attracted considerable attention not only from the business communities, but also from academics and media outlets. Therefore, the international media outlets regularly publish news and features where academicians provide their opinions, suggestions, and ideas.

Such discussions and debates contributed to the decision to conduct a webinar on the present economic situation of Sri Lanka- 'Current Sri Lankan Economic Crisis: Lessons for other South Asian Countries', held on 24 April 2022, organised by the South Asian Institute of Policy and Governance (SIPG), North South University (NSU) of Bangladesh.

Expert Opinion on the Current Sri Lankan Crisis & Lessons Learned

A brief overview of Sri Lanka's current economic crisis

Dr. Gour Gobinda Goswami, Professor, Department of Economics, NSU gave the following "brief overview of Sri Lanka's economic position" that resulted in this crisis:

- Sri Lanka was formerly regarded as a role model for South Asia. But, even before the Covid-19 pandemic, the country was rocked by instability in GDP growth that started the present economic downturn. Sri Lanka currently has a GDP of only 2.5 percent.
- The country's national debt is currently at 83 percent of GDP, with a goal of cutting it to 71.2 percent by 2023, but it was not attained. Unfortunately, it's still under 10 percent of GDP and the country's sovereign bond came under CCC, which is a state of risk.
- The county has missed its payment of instalments and is seeking an IMF bailout, replacing its Finance Minister (who was the brother of the incumbent President). Sri Lanka has sought soft loans from India, China, Bangladesh, the ADB, and the World Bank to bail out the country from the present crisis.
- For Sri Lankans, the revenue drop occurred before the pandemic, after the Easter Sunday bombings, and it downturned the tourism sector. Later, the pandemic hit the tourism sector severely.
- The budget deficit was 7.97% in 2019 and rose to an alarming 9.8% presently. The current account deficit is at 3.18% to the GDP in 2018, but the country is facing serious difficulties due to the US\$15 billion denominated sovereign bond, whereas the total long-term debt is US\$45 billion.
- The market borrowing or the commercial loan stands at 47% of Sri Lanka's foreign debt, followed by 13% to ADB, and 10% each to China and Japan. The sources of growth in Sri Lanka and their debt financing are largely on infrastructure.

- The Government also took a step in the wrong direction when it introduced organic fertiliser. The food production and tea production, the main source of export revenue, has dropped drastically due to this policy.
- It is only India in the South Asian Region that has received an investment rating of BAA 3 and BBB- among South Asian countries, while Bangladesh, Pakistan and Maldives belong to speculative rates, while Nepal, Bhutan and Afghanistan have no ratings.

Causes of the Sri Lankan economic crisis

Channa de Silva, Chairman, Sarvodaya Development Finance, stated some of “the root causes for the current economic crisis in Sri Lanka”. These are:

- Huge investments in unproductive development projects, governance issues, corruption, mismanagements of funds;
- A 90% drop in tourism income due to the terrorist attack and the pandemic;
- A drop-in remittance;
- Inflation and currency depreciation due to money printing rather than seeking help from the International Monetary Fund (IMF);
- Losing 3 billion in Chinese investment;
- The populist policies, like banning chemical fertilisers, resulted in declined food production;
- A huge tax cut in 2019, which resulted in a loss of US\$3 billion and reduced the revenue collection;
- The borrowing was for unproductive projects. The Government has built flyovers, ports, airports, and cricket stadiums in remote places like Hambantota, where there is a scarcity of water and essentials, spending a sum of almost US\$4 billion. These large projects, without any return on investment, increased foreign debts.

Lessons for Bangladesh and South Asia

Dr. Nazneen Ahmed, Country Economist, UNDP Bangladesh, spoke on “the lessons for Bangladesh and South Asia from this crisis.” She underlined the need to accurately estimate the demand for development projects as well as the projects’ gestation period. Other recommendations from her speech were as follows:

- Bangladesh must also consider the possibility of a future increase in the borrowing rate as the country’s Per Capita Income (PCI) rises to maintain economic growth.
- Emphasis should be given to policies, debts, and inflation, as well as policymaking, revenue collection, and spending quality on the development budget, to determine how we might save and avoid projects that would result in a large debt burden.
- Bangladesh depends on readymade garments and Sri Lanka mainly on tourism for foreign exchange. So, no South Asian countries should depend on only a few industries.
- Populist policies like tax cuts can hamper revenue earning for Bangladesh, because the tax to GDP ratio is very low in Bangladesh, and she provides energy subsidies.
- Investment in large projects in Sri Lanka has hampered the revenue, too. So, countries need to think of the gestation period and when they can reap the benefits from those projects.
- In Bangladesh, some of the development projects get delayed, increasing not only the cost, but also increasing the debt burden. So, the demand for these projects should be studied and then investment decisions for large projects made.

Geopolitics and foreign policy lessons

Ambassador Shahidul Haque, Professorial Fellow, SIPG, NSU spoke on 'Geopolitics and foreign policy lessons from the Sri Lankan Crisis'. He stated the following points:

- Sri Lanka has traditionally been a “theatre of geopolitics in the region,” maybe because it sits in the middle of the Indian Ocean and because of their various policies.
- And, very lately, when things are extremely upsetting, whether in Afghanistan or next-door neighbor Myanmar, or in Eastern Europe with conflict between Ukraine and Russia, we see that Sri Lanka is sort of in the midst of all these, like Bangladesh and other South Asian countries.
- So, a government should not experiment with foreign policy during volatile times such as pandemics, which may have contributed to Sri Lanka’s present crisis. Geopolitics and economics go hand in hand.
- Moreover, when the country needed to go to the IMF and seek redress, it did not do so. And, that has really put Sri Lanka in a situation where they are facing difficulties in having a discussion with the IMF right now.
- On foreign policy, Sri Lanka has been a promoter and very strong supporter of the non-aligned movement. But we also see the current government of Sri Lanka has tried to fine tune, rebalance, or shift from those policies, as they have tried to move out from the Non-Aligned Movement and go towards a full neutrality kind of a posture in foreign policy. That’s something new, as there’s a difference between neutrality and the Non-Aligned Movement.
- In 2019-20, when the Rajapaksa family was taking over, people saw a tilt in their policies or projects. Giving projects to China was neither a manifestation of a policy of neutrality, nor a Non-Aligned Movement. That created a little geopolitical tension in the region between India, China, the United States, and others.

Conclusion

In this whole process, it is the people who have suffered. The situation in Sri Lanka is very difficult to comprehend. When Bangladesh looked at Sri Lanka, we always found Sri Lanka was way ahead of us. So, it's a lesson for Bangladesh as well. The Rajapaksa family's actions had an impact, and the President tried to rebalance that. In the process of rebalancing, the Government ended up being too far away from both parties, China, and India. It created a situation where they needed most of the support, but none of them was there except India, which came in very strongly, and now we are talking about a US\$2 billion support package.

Bangladesh was very generous in terms of coming forward to help Sri Lanka in this crisis and that's what we should be doing in South Asia. We should stand beside each other when there's a hit. This present economic situation has had a ripple effect all over South Asia and beyond, whether it is in Delhi, Dhaka, Islamabad, or Kathmandu. Everybody is looking at their ledger to see how much money is still there and the likelihood of not flying out of that. Some governments are taking steps proactively to avoid the crisis Sri Lanka is going through, which is a good factor in many ways for those countries.

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This policy brief has been prepared by editing the following news article written by one of the panellists of this webinar; Ms. Sulochana Ramiah Mohan, Deputy Editor, Ceylon Today, Sri Lanka;

Mohan, S. R. (2022, April 30). Lessons for other S. Asian Countries. *Ceylon Today*.

Retrieved from <https://ceylontoday.lk/2022/04/30/lessons-for-other-s-asian-countries/> last accessed on 20 June, 2022

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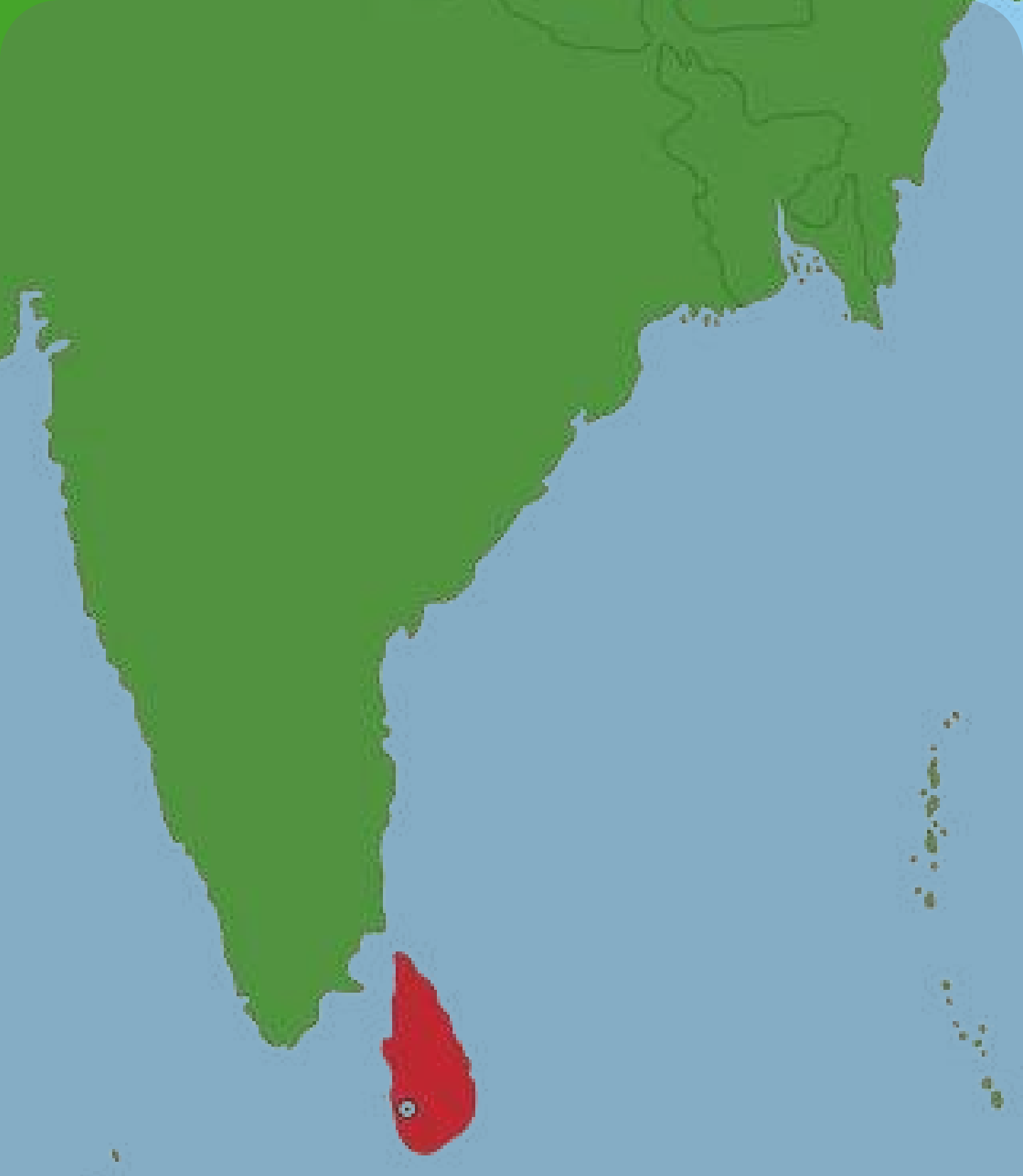


SIPG



South Asian Institute of Policy and Governance (SIPG) was formally inaugurated in 2008 as a tailor-made education and research program under the then Department of General and Continuing Education. The International Master's Degree Program in Public Policy and Governance had been a landmark in the history of North South University in Bangladesh. The program has been able to garner a formal recognition as an attractive center for the higher education of the incumbent young civil servants of the Government of Bangladesh and other South Asian Countries (Sri Lanka, Bhutan and Nepal). In 2018, after a decade, the Public Policy and Governance Program (PPG) was upgraded to a full-fledged Institute as SIPG. Till 2022, the Master in Public Policy and Governance (MPPG) program has produced more than 170 graduates from Bangladesh, Bhutan, Nepal, and Sri Lanka. Recently, in 2021 SIPG has also commenced the Executive Masters in Policy and Governance (EMPG) for the professionals from Bangladesh.

Moreover, in 2019, SIPG launched a specialized research center called the 'Center for Peace Studies (CPS)'. CPS aims to facilitate the academic study of peacebuilding and the promotion of a resilient society through evidence-based and empirical research. CPS also conducted several certificate courses on, Geopolitics of Peace, Pandemic & Development jointly with the O.P Jindal Global University, India; The Rohingya Crisis in collaboration with the University of Arizona, USA; and Humanitarianism, Policy, and Diplomacy in partnership with the Bangladesh Institute of Peace Support and Operation Training (BIPSOT).



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