

Sri Lankan Crisis

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Abstract:

Background: Many have argued that the current Sri Lankan crisis was caused by the economic impact of the COVID-19 pandemic and the Ukraine war, and the country's overdependence on predatory Chinese lending. Sri Lanka's problems are more deep-rooted and have their origins in economic policy that focused on providing fiscal SOPs and a family-run political establishment that enabled the government to ignore sound advice.

Critics say the roots of the crisis, the worst in several decades, lie in economic mismanagement by successive governments that created and sustained a twin deficit – a budget shortfall alongside a current account deficit.

“Sri Lanka is a classic twin deficits economy,” said a 2019 Asian Development Bank working paper. “Twin deficits signal that a country's national expenditure exceeds its national income, and that its production of tradable goods and services is inadequate.”

The collapse of tourism caused by travel restrictions, the consequent draining out of foreign reserves, and rising food and energy costs caused by the Ukraine conflict seem to have led to an economic collapse

The situation in Sri Lanka is much more than just an economic crisis. Clearly, this is a humanitarian crisis. The question is, how did it occur, and how did the government of Lanka lose all its money? The purpose of this research paper is to answer these questions.

This study identified many causes for this social, economic and political catastrophe in Sri Lanka; Biased international relations, Chemical fertilizer ban, Civil unrest, Collapse of Small and Medium Enterprises, Collapse of tourism industry, COVID-19, Crisis management problems, Delayed vaccination programme, Energy shortage, Environment disasters, Family Politics, Forex shortage, Government borrowing for consumption, High Inflation, Lock-downs, Medical emergency due to drug shortage, Misuse of legislature, Money printing to settle government's recurrent expenses, Crude oil supply shortage, Political influence in civil matters, Problems handling Diplomatic relationships, Repeated School closure, Russia-Ukraine war effect, Threat to the minorities, Unrealistic financial planning, Unresolved War crimes and post-war crimes, Violation of human rights, and Violation of international trade law.

Materials and Methods: Secondary research, also known as desk research, is a research method that involves compiling existing data sourced from a variety of channels like Newspapers, Websites.

Results: To study and analyze the various reasons contributing to the crisis – failed agriculture and energy policy, Dependence on Tourism Sector and Agriculture, not much contribution in the manufacturing sector, How Family run Politics have ruined the Economy and What can India and Global Economies can learn from Sri Lankan Crisis.

Conclusion: The severity of Sri Lanka's economic crisis is evidenced by the fact that the country is being widely pointed to as a textbook case of how an economy should not be managed.

Sustainable policy, this was something in which Sri Lanka failed miserably. Any extreme step without planning will lead to the downfall and collapse of that policy first and then the economy. Keeping high aims for one's nation is good, but if that comes with a cost of playing with people's life and that's where the tragedy begins

Key Word: Economic Crisis, Failed Sustainable Policy.

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I. Introduction

Sri Lanka's future was looking prosperous at the end of its 26-year civil war in 2009. Its post-war GDP growth was reasonably high at 8-9% per annum till 2012. Sri Lanka's budget deficits were high during the war and the global financial crisis of 2008 drained its forex reserves. Its strategic location in the middle of some of the world's most important shipping lanes and within close proximity to India has given the country a competitive advantage when it comes to attracting FDI. The island nation has been transitioning from a predominantly rural-based economy to one that is more urbanized and focused on services and tourism. However, terrorist attacks in the country in 2019 and 2020 and the Covid-19 pandemic brought this progress to a halt. “Covid-19 caused a major blow to the tourism sector and caused many Sri Lankans working abroad to

come back home, as they lost their jobs. Compounding this misery is the fact that Sri Lanka imports more than it exports, which also has an effect on foreign currency reserves. Sri Lanka's Debt to GDP Ratio is 111%. It owes more than it produces. "With limited investments into manufacturing and value addition (with apparel being the one exception), Sri Lanka has been reliant on tourism, migrant labour and commodity exports to generate dollars for the economy". The spike in oil prices on an economy totally dependent on imported oil has been more than the proverbial last straw. The governance at the top was very unusual, to say the least. Four brothers became the President, the Prime Minister, and Ministers for Finance and Agriculture, and a fifth -- the Minister for Sports -- was a nephew. How can one expect sound democratic governance in an atmosphere of nepotism like this? Many policies of the administration of former President Gotabaya Rajapaksa led to the aggravation of the economic crisis. The tax cuts given in 2019, when Sri Lanka was already seeing low tax revenues, led to larger fiscal deficits, resulting in international ratings agencies downgrading Sri Lanka, effectively shutting the country out of international capital markets. The chemical fertilizer ban was another mistake which led to agricultural output decreasing significantly.

II. Various Causes Contributing to Sri Lankan Crisis & Lessons India can Learn.

❖ *Sri Lanka's Agricultural Policy / Food Security*

"It's clear that agriculture, done right, is the best means the world has today to simultaneously tackle food security, poverty and environmental degradation." -Irene Rosenfeld - Was CEO Kraft foods.

The agriculture sector in Sri Lanka always acts as a major economic strength to the national economy as it ensures the food security, employment and poverty alleviation of rural communities. The sector is mainly driven by variety of distinct sub sectors which include crop cultivations such as paddy, tea, rubber, coconut, vegetables, fruits, export crops and sugar while in addition livestock and fisheries sectors also provide a substantial contribution simultaneously. The Agriculture Sector is the cornerstone in Sri Lanka's Economy with more than 70% of the population living in rural areas depending on agriculture for their livelihoods.

Currently this sector contributes to about 18% of the GDP and 30% of the employment.

Sri Lanka's President Gotabaya Rajapaksa promised in his 2019 election campaign to transition the country's farmers to organic agriculture over a period of 10 years.

In June 2021 Rajapaksa's government made good on that promise, imposing a nationwide ban on the importation and use of Synthetic fertilizers and pesticides and ordering the country's 2 million farmers to go organic.

The result was brutal and swift. Against claims that organic methods can produce comparable yields to conventional farming, domestic rice production fell 20 percent in just the first six months. Sri Lanka, long self-sufficient in rice production, has been forced to import \$450 million worth of rice even as domestic prices for this staple of the national diet surged by around 50 percent.

No meal is complete without Rice in Sri Lanka. Lunch, Dinner, Dessert – You name your time and place, chances are rice will be on the table. The Average Sri Lankan eats 107 Kilogram of rice every year. Across Sri Lanka the rice crops are stunted. In Northern Sri Lanka the average output used to be 4.5 tons per hectare that was before the economic crisis, now just 2.3 metric tons the gap is massive. Almost 2 million people in the country are rice farmers, that's nearly 25 % of all people engaged in farming. Harvest has fallen below expectation, with no foreign exchange Sri Lanka could not import fertilizers or fuel for tractors or farming equipment. Earlier you could farm 75 acres of land with 75000 Sri Lankan Rupees that is nearly \$197, your output would be 40 bags of rice from each acre, now that's changed the average cost is almost 200000 Sri Lankan Rupees even then your output is only 18 –20 bags of rice. Everything is more expensive. Urea once sold 1500 Sri Lankan Rupees now almost 40000 Sri Lankan Rupees. The ban also devastated the nation's tea crop, its primary export and source of foreign exchange. According to one estimate, the president's agrochemical ban was poised to save Sri Lanka the \$400 million it was spending yearly on synthetic fertilizer, money it could use toward increasing imports of other goods.

By November 2021, with tea production falling, the government partially lifted its fertilizer ban on key export crops, including tea, rubber, and coconut. Faced with angry protests, soaring inflation, and the collapse of Sri Lanka's currency, the government finally suspended the policy for several key crops—including tea, rubber, and coconut—last month, although it continues for some others.

The government is also offering \$200 million to farmers direct compensation and an additional \$149 million in price subsidies to rice farmers who incurred losses. That hardly made up for the damage and suffering the ban produced. Farmers have widely criticized the payments for being massively insufficient and excluding many farmers, most notably tea producers, who offer one of the main sources of employment in rural Sri Lanka. The drop in tea production alone is estimated to result in economic losses of \$425 million.

Human costs have been even greater. Prior to the pandemic's outbreak, the country had proudly achieved upper-middle-income status. Today, half a million people have sunk back into poverty. Soaring inflation and a rapidly depreciating currency have forced Sri Lankans to cut down on food and fuel purchases as prices surge. The

country's economists have called on the government to default on its debt repayments to buy essential supplies for its people. When Rajapaksa announced the shift to organic, less than three per cent of Sri Lanka's farmland was farmed without chemicals. The country needed time to change and adjust to the organic way of farming. They also needed support and good organic substitutes to smooth the transition. Bhutan, for example, announced in 2008 that it will become fully organic by 2020. Bhutan is yet to achieve that target.

Lesson for India

Finance Minister K.N. Balagopal openly admitted that the State (Kerala) can draw lessons from the economic crisis in the neighboring country. Ill-advised policy of switching to organic farming, shunning chemical fertilizers, has led to a steep fall in agricultural production and export earnings from tea in Sri Lanka. Kerala is also on the same page to some extent as it is bringing around 82,000 hectares of farmland under organic cultivation. According to the data with the agriculture department, out of the target of 82,000 hectares only 57,000 hectares were switched to organic mode by March 2022.

P. Indira Devi, agriculture economist and former director of research, Kerala Agricultural University, said "I will not say that the State should completely switch to organic farming all of a sudden without taking note of the technological advances in modern farming. But the State has the scope to experiment with organic farming, imbibing lessons from scientific methods. Whenever we adopt a new mode of cultivation, the long-term socio and ecological impact has to be considered."

Case Study: Sikkim's Successful Organic Farming

Organic agriculture uses naturally occurring substances while prohibiting or strictly limiting synthetic substances. This enhances agro-ecosystem health, including Biodiversity, Biological cycles and soil-biological activity. From 2003, the state began reducing the subsidy on chemical pesticides and fertilizers by 10 per cent every year and banned them completely in 2014. Their sale and use were made punishable by law with an imprisonment of up to three months or a fine of up to Rs 1 lakh or both. "Initially, there was apprehension among farmers and, in some villages, they refused to take up organic farming. But with continuous training and education, there was a shift in their mindset," says M K Pradhan, additional director of the Sikkim Organic Mission (SOM), the nodal agency established to fast-track Sikkim's transition in 2010.



Household food security and the nutrition situation in Sri Lanka is set to deteriorate. Today, Sri Lanka is experiencing food insecurity due to the economic crisis in two ways: First, the escalating human unrest, protests, and long queues for food; second, the extreme dependency on foreign countries, for credit and aid. Skyrocketing food costs are making it harder for the population to meet their food needs. 70 % of households have had to reduce food consumption as food prices have reportedly increased by 73 % in the last two years.

A survey conducted by UNICEF in April concluded that at least 62% of households have experienced a fall in income, which has significantly impacted their diet and their ability to afford nutritious food. The monthly cost of a nutritious diet has gone up by 156%. According to the Sri Lanka situation report released by the WFP World Food Programme's on June 14, an estimated 5.7 million people are in need of humanitarian assistance in 25 districts across the country after months of economic meltdown



Lesson for India

A big lesson to learn for India from this situation is to be self-sufficient in food production.

As per the data released by the Ministry of Consumer Affairs, around 1550 Tonnes of food grain have been wasted during the Covid-19 pandemic in the Food Corporation of India’s Godowns, due to a lack of a proper mechanism to store the food grains, and this should be avoided at all costs, especially at a time when food resources have become scarce all over the world.

❖ Downfall of Tourism

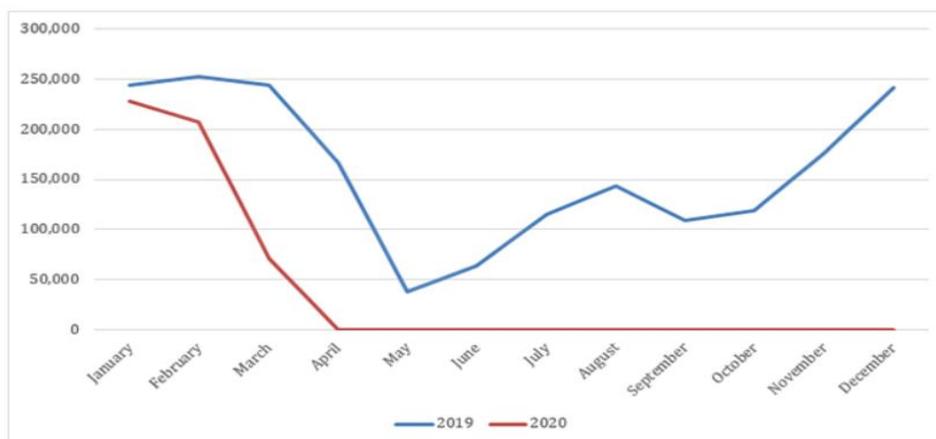
Tourism is defined as “a social, cultural and economic phenomenon which entails the movement of people to countries or places outside their usual environment for personal or business/professional purposes” by the United Nations World Tourism Organization (UNWTO).

Sri Lanka’s strategic location, attractive natural endowments, cultural diversity, and rich history, together with the peaceful, clean, safe and foreigner-friendly environment, provide the basis for this industry to flourish.

The country’s tourism sector has grown over time to emerge as one of the most valuable players in the Sri Lankan economy, by heavily contributing towards employment generation, FOREX earnings as well as ensuring a steady supply of revenue for the successive governments in direct and indirect ways. Tourism in Sri Lanka accounts for almost 12 percent of the country’s GDP and is the third-largest source of foreign exchange reserves—behind worker remittances and the apparel industry.

The 2019 Easter Sunday Bombings marked the beginning of the collapse of this industry. This was followed by the double-whammy of the COVID-19 pandemic and the Ukraine–Russia conflict amidst the current economic crisis in Sri Lanka—undoubtedly making the revival of this sector extremely challenging.

Sri Lankas Tourist Numbers 2019 - 2020





Source: Central Bank of Sri Lanka

Lesson for India

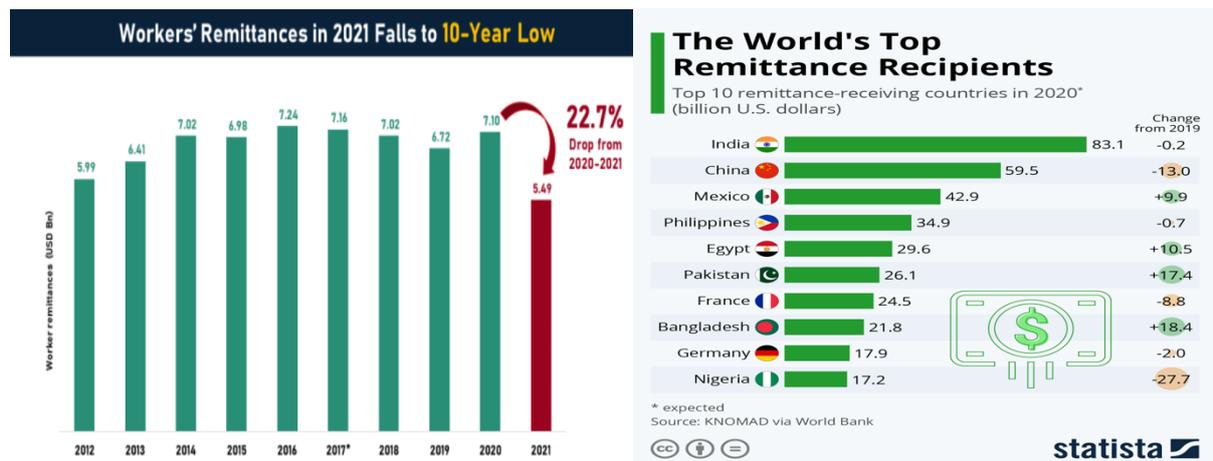
The Indian Travel and Tourism Sector contributed to nearly \$194 billion, around 6.8 % of Indias GDP, during the calendar year 2019. The tourism and hospitality industry hardly finds sufficient support from the Government, even when it is needed the most. During Corona crisis period, the industry requested repeatedly for intervention in helping the sector to survive. When financial pancakes were announced, tourism sector did not find any preference, except some scanty offers

❖ **Remittances to SriLanka**

When migrants send home part of their earnings in the form of cash to support their families, these transfers are known as workers’ or migrant remittances. Workers’ remittances have been a key pillar of Sri Lanka’s foreign currency earnings.

How can remittance positively impact an economy?

- ✓ At the micro-level, remittances boost a family’s income, which leads to improved nutritional outcomes, higher spending on education, increased purchasing power, more disposable incomes, and a better standard of living.
- ✓ Remittances also enable recipients to boost their investments and savings.
- ✓ Remittances also keep the foreign reserves of India stable, thereby helping the Indian rupee hold up against the US dollar and other major currencies

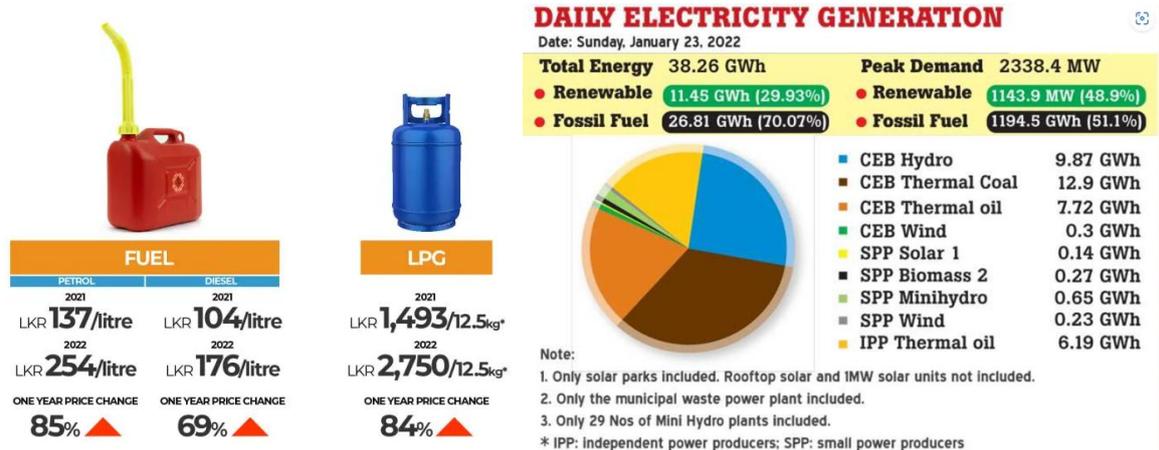


❖ **Energy Crisis**

Due to shortage of fuel, many power plants have to be kept shut, which is resulting in a power crisis in the country. Some power plants are resorting to hydro energy using the waters basically used for irrigation purposes. Due to insufficient rain and increased use of reservoirs for the power plants, water shortage is anticipated which, as per experts, will badly affect agricultural production and may lead to food crisis.

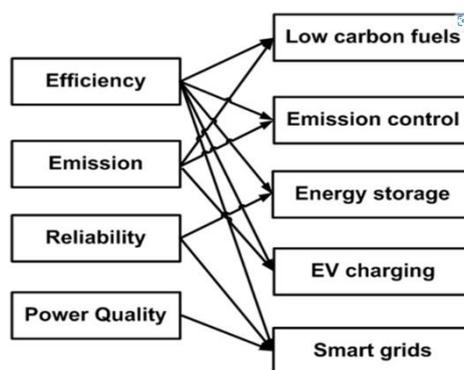
Sri Lanka roughly spends \$500 million a month to source diesel and gasoline. Diesel is the most commonly used fuel for public transport, and motorists outside the capital have reported long queues at understocked pumps. Sri Lanka has no significant fossil fuel reserves. It does, according to the World Bank, have good potential for solar and wind power. Yet it has failed to develop either technology. It gets around a third of its electricity from imported oil, a third from imported coal and a third from domestic hydropower. The

Ceylon Electricity Board (CEB), Ceylon Petroleum Corporation (CPC) and the Ministries of Power and Energy seem to be at loggerheads; further aggravating the crisis at hand



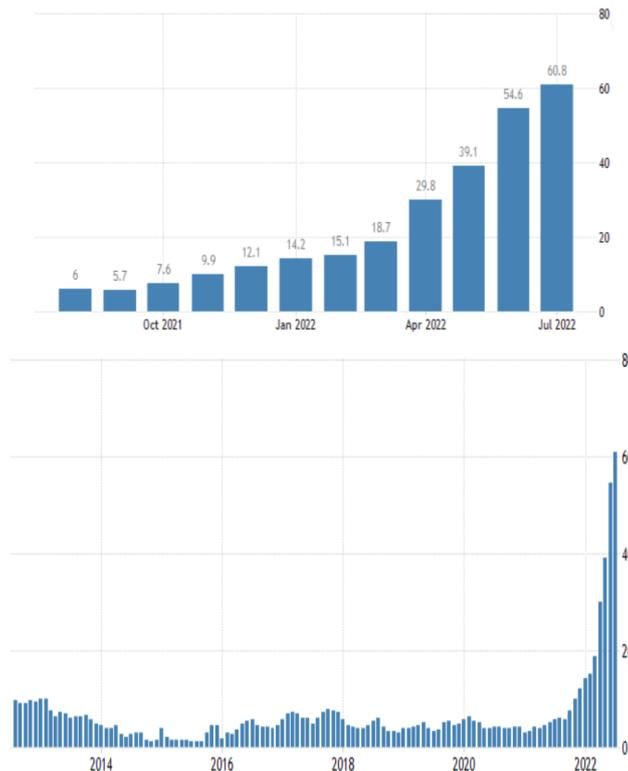
Lesson for India

- ❖ In respect of energy security, much attention has been given to enhancing oil security through the diversification of sources and supply routes and creating emergency stocks.
- ❖ India has a reserve oil storage of 74 days, but this needs to be increased keeping in mind the ongoing fuel crisis around the world created due to the Russia-Ukraine war.
- ❖ Secondly, India seems to be on the brink of a power crisis with the ongoing coal shortage at a time when the country is dependent on fossil fuels for more than 60 per cent of electricity generation.
- ❖ Investment in research and development (R&D) to switch to renewable energy sources. Transitioning from fossil fuel-based energy to clean energy with extensive battery storage. Need for Wind and Solar Hybrid Policy, Flex Engine – Ethanol Blending, Green Hydrogen – Green Ammonia.
- ❖ Electrification of Transport (Public Busses, Rail & Implementation of Bharat 6 emission standards
- ❖ India is needs to head towards clean power including renewables like wind, hydro, solar, geothermal, bio & tidal power to supplement fossil fuel-based electricity generation.
- ❖ Almost 84% of solar equipment requirement in the country is met through imports from China. India is heavily dependent on China for solar photovoltaic cells. Silicon wafers and solar lanterns in 2019–20 was from China. Dumping of Chinese solar panels led to a loss of nearly 2 lakh jobs as nearly half of the domestic industry capacity remained idle (Criticism)
- ❖ GST increased from 5% to 12% on renewable products (Criticism)



❖ Inflation

The annual inflation rate in Sri Lanka jumped to a record high of 60.8% in July of 2022

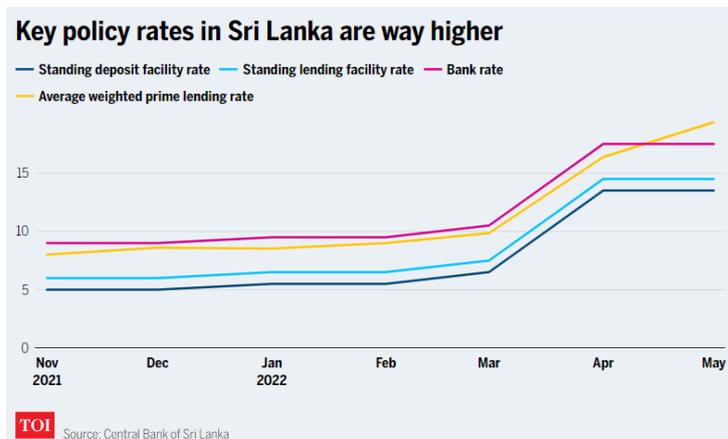


Sri Lanka's central bank raised key interest rates to the highest in two decades on July 7 to bring down record inflation.

The bank increased the standing lending facility rate by 100 basis points to 15.50% while the standing deposit facility rate was similarly raised to 14.50%, the highest since August 2001. "The Board was of the view that a further monetary policy tightening would be necessary to contain any build-up of adverse inflation expectations," the central bank said in a statement.

Bank rate jumped from 9% in November to as high as 17.5% in May. Average weighted prime lending rate is at 19.36 % in May as compared to 8% in Nov 2021.

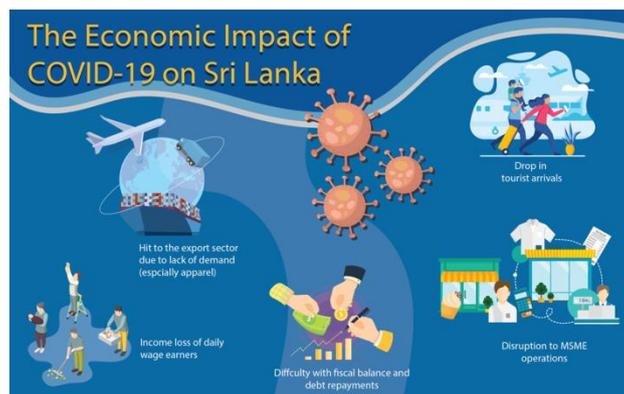
Standing lending facility is a lending facility in which healthy banks are allowed to borrow all they want from a central bank.



❖ **Health Care**

Health-care systems are nearing collapse, with patients at risk from power shortages, a lack of medicines, and equipment shortages. The country imports around 85% of its medical supplies. But with foreign currency reserves running low, essential drugs are now difficult to obtain.

Electricity shortages mean healthcare professionals are forced to diagnose and treat their patients' using flashlights.



❖ *Lesson for India*

As much as 75% of the APIs (Active Pharmaceutical Ingredients) used in the formulations of essential drugs in the National List of Essential Medicines (NLEM) are sourced from China.

In medicines, India has relied exclusively on China for imports of APIs for paracetamol and streptomycin and has very high levels of dependence on other antibiotics like ciprofloxacin and amoxicillin. China has also been supplying the APIs for rifampicin, used for treating several bacterial infections including tuberculosis. Besides these medicines, more than 95% of imports of penicillin in various forms have been from China. Imports of other major APIs for which largely come from China include semisynthetic penicillin (6- amino penicillanic acid) and ibuprofen, a common medicine used for treating pain, fever and inflammation of various kinds, including arthritis.

According to a response to a query in Rajya Sabha, India has the world's third-largest pharmaceutical industry for which 2/3rds of its key ingredients come from China.

Excessive Money Printing:

Money printing in a country means printing the currency of a government by an authority approved by the respective government. The CBSL has the sole right and authority to issue currency in Sri Lanka which includes both currency notes and coins as stipulated in the Monetary Law Act No. 58 of 1949.

To cover government spending, the Central Bank began printing money in record amounts ignoring advice from the International Monetary Fund (IMF) to stop printing money and instead hike interest rates and raise taxes while cutting spending. The IMF warned that continuing to print money would lead to an economic implosion.

From December 2019 to August 2021, Sri Lanka's money supply increased by 2.8 trillion rupees -- a massive 42%.

❖ *Sri Lanka's Debt Trap*

After a devastating civil war ending in 2009, the government resorted to expensive borrowing from international bond markets for the reconstruction process. Successive Sri Lankan governments have been increasingly borrowing from private international capital markets through the issuance of sovereign bonds. The top holders of the Sri Lankan government's debt, in the form of international sovereign bonds (ISBs), are the following firms:

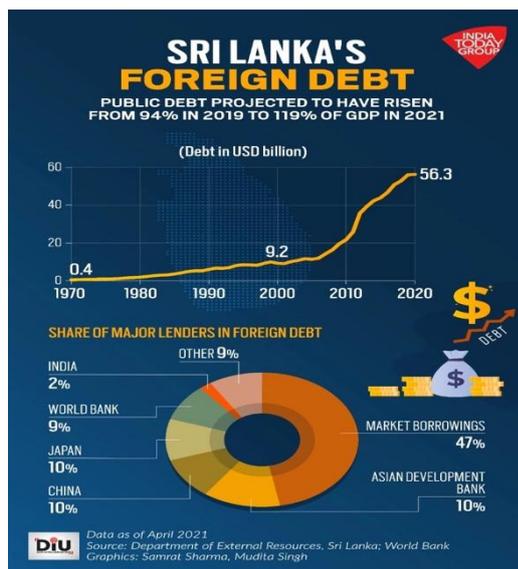
- ✓ **BlackRock (U.S.)**
- ✓ **Ashmore Group (Britain)**
- ✓ **Allianz (Germany)**
- ✓ **UBS (Switzerland)**
- ✓ **HSBC (Britain)**
- ✓ **JPMorgan Chase (U.S.)**
- ✓ **Prudential (U.S.)**

It was the scramble to repay some of this debt, that matured in 2017, that pushed the Sri Lankan government to offer the Hambantota Port for lease. China accepted the offer in return for \$790 million that was used to repay the debt to the international markets, not to China.

As much as the West blames Chinese predatory lending, only 10 to 20 percent of Sri Lanka's foreign debt is owed to China. The majority is owed to U.S. and European financial institutions or Western allies like Japan.

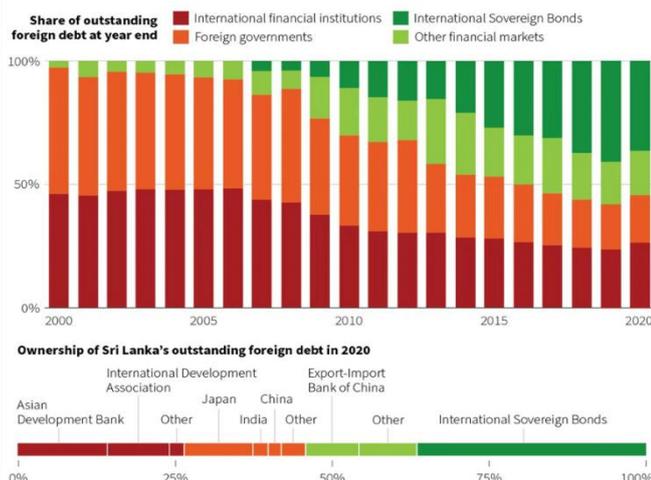
Large foreign loans, contracted at high interest rates, have pushed the country into a debt trap. This has already forced Colombo to hand over the Hambantota Port to China Merchant Port Holdings at the end of 2017 with a 99-year lease.

Around 60 percent of low-income nations and 30 percent of middle-income ones are in debt distress or at high risk of it. Pakistan, Bangladesh, Tunisia, Ghana, South Africa, Brazil, Argentina, Sudan — the list of those in trouble is growing rapidly.



Sri Lanka's foreign debt

Repeated cycles of borrowing from capital markets, including the International Sovereign Bonds, have made them the largest source of foreign funding for Sri Lanka.



❖ Tax cuts

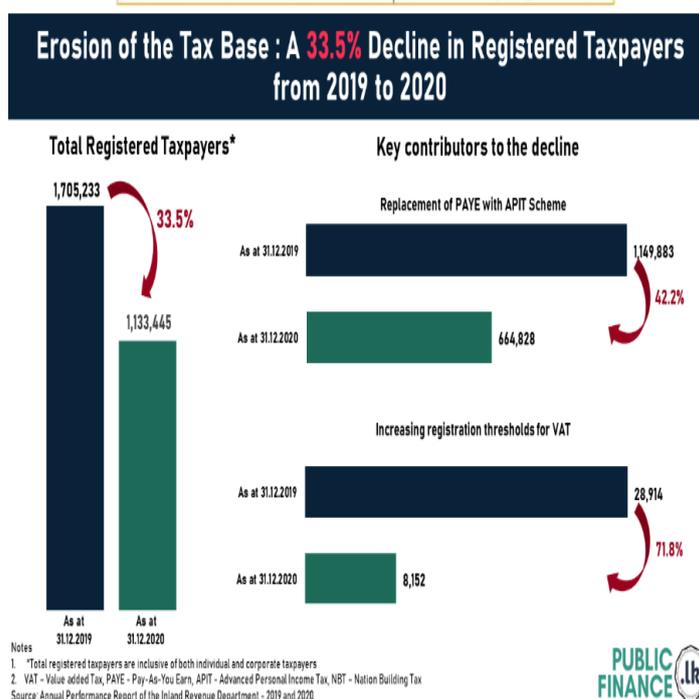
Sri Lanka government announced tax cuts at a time when the state funds were already buckling under the weight of a failing economy—traced back to the 2008 Financial Crisis and the 2009 Civil War. To meet 2019 election promises, the government proceeded to initiate deep tax cuts mere months before the pandemic made landfall. There has been a decline in Sri Lanka's tax base between 2019 and 2020 with 33.5% decline in the number of registered taxpayers (corporate and individual) in the country.

The most prominent change to the taxation system was the Value Added Tax (VAT) being brought down from 15 percent to 8 percent. While the Nation Building Tax (NBT) of 2 percent was abolished and combined with the Ports and Airport Development Levy, the tax on Telecommunication Tariffs was reduced by 2.5 percent. A few other taxes that were eliminated include the Economic Service Charge, Debit Tax on Banking and Financial Institutions, VAT on Sovereign Property, Capital Gains Tax on the Share Market, Pay as You Earn (PAYE) Tax, Credit Service Tax and the Withholding Tax on Interest Income.

“Gotabaya’s tax relief package derailed our financial situation, leading to debt repayment at a huge social cost,” said Patali Champika Ranawaka, member of parliament and leader of the new political movement, 43 Brigade.

Table 1: Taxes Abolished in Sri Lanka in 2019-2020

Tax Category	Amendment
Value Added Tax (VAT)	Reduced from 15 to 8 percent.
Nation Building Tax (NBT)	The earlier 2 percent of NBT was abolished. NBT was combined with the Ports and Airport Development Levy with a relevant ratio of 10 percent.
Economic Service Charge	Eliminated
Debit Tax on Banking and Financial Institutions	Eliminated
Capital Gains Tax on the Share Market	Eliminated
VAT on Sovereign Property	Eliminated
Pay As You Earn (PAYE) Tax	Eliminated
Withholding Tax on Interest Income, other types	Eliminated
Credit Service Tax	Eliminated
Tax on Telecommunication Tariffs	Reduced by 25 percent.

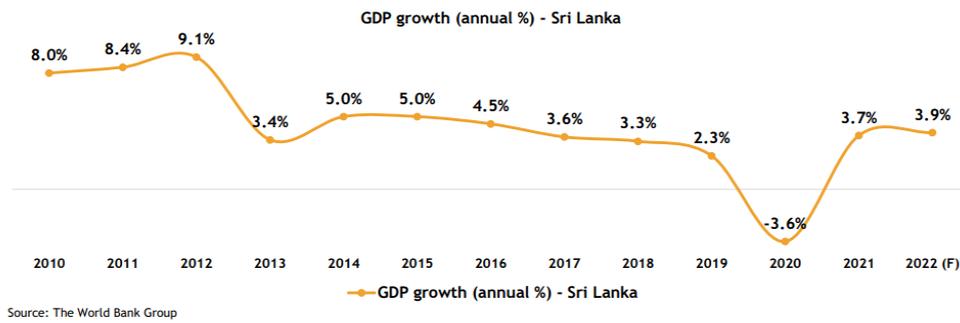


Economic growth and prosperity require investment. And investment can either be funded through savings or borrowings. Investment may come from household savings in banks or taxes that are not used for recurrent state expenditure. If households do not save enough and the Government does not tax enough, then external borrowings must fund investment to increase production and employment. To avoid a foreign debt trap, the Government should impose adequate levels of taxation or, alternatively, ensure it is in a position to borrow from domestic private savings to finance national plans and related investment.

India has a federal structure where states are equally responsible for economic growth. However, there is a growing tendency where local leaders are behaving irresponsibly with the announcement of freebies.

❖ GDP

The country's GDP growth rate had plummeted from 8.01 percent in 2010 to (–) 3.56 percent in 2020 when the pandemic hit.

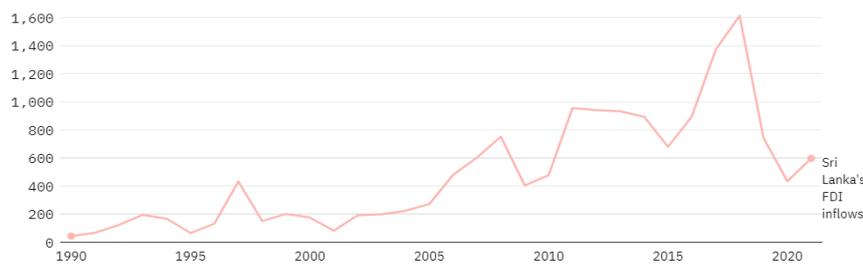


❖ **Foreign Direct Investment**

A default is bad news for foreign investors, as they value political stability and economic certainty when looking to launch operations in a new country. Sri Lanka has enjoyed an increase in FDI flows over the past decades, reaching a peak in 2018 before recording a significant drop in 2019 and 2020. If the FDI in a country goes down, so does the foreign currency in its reserves.

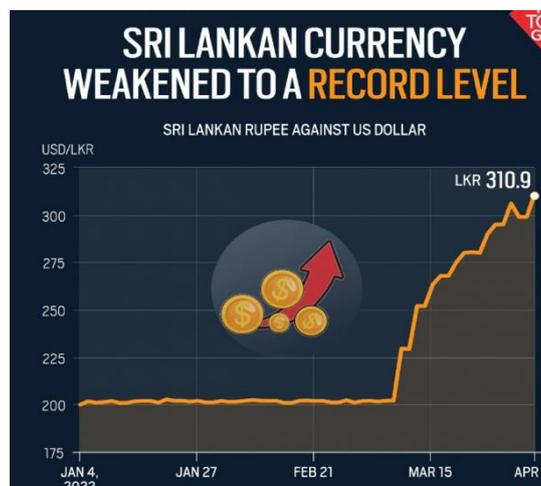
Sri Lanka 's FDI inflows reached record high in 2018

FDI inflows in \$m, 1990–2021



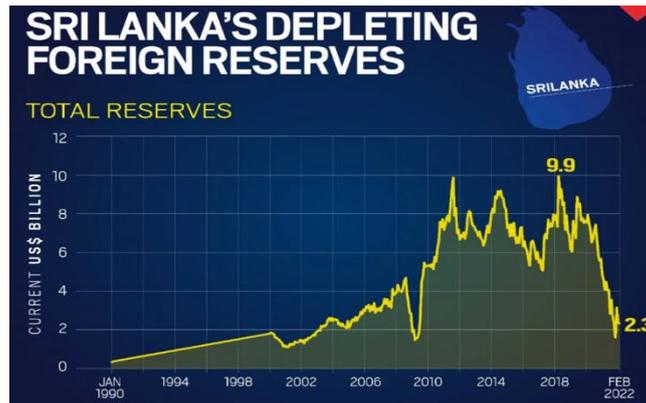
❖ **Weak Currency**

The Sri Lankan Rupee depreciated by more than 50 per cent against the US dollar this year alone. This means that Sri Lanka now has to shell out nearly Rs. 310 to buy a dollar now, compared to Rs. 200 in January 2022. The Sri Lankan Rupee has depreciated against the Indian Rupee by 31.6 per cent, the Euro by 31.5 per cent, the pound sterling by 31.1 per cent, and the Japanese Yen by 28.7 per cent between January 1 and March 31, according to the Central Bank of Sri Lanka.



❖ **Forex Reserves**

The foreign reserves in Sri Lanka in 2018 were near USD ten billion. This nosedived to under USD two billion in 2021.



❖ *Trade deficit in Sri Lanka*

In the globalized world, there is no country self-sufficient in the sense of producing all the goods and services it needs. Sri Lanka is a trade deficit economy as its imports are more than its exports.

In Jan and Feb 2022, Sri Lanka shipped goods worth US\$1 billion and imported products worth US\$3 billion. That means Sri Lanka is heavily dependent on countries to import goods.

Here is a list of Sri Lanka's top imports and exports reported in 2021.

Top Imports

Product
Machinery, Mechanical Appliances, etc.
Electrical Machinery and Equipment
Knitted or Crocheted Fabrics
Plastics and Articles
Pharmaceutical Products
Cotton
Rubber and Articles
Iron and Steel
Paper and Paperboard
Man-made Staple Fibers

Top Exports

Product
Knitted or Crocheted Apparel & Clothing
Not Knitted or Crocheted Apparel & Clothing
Coffee, Tea, Mate and Spices
Rubber and Articles
Fish and Crustaceans
Natural or Cultural Pearls & Precious Stones
Electrical Machinery and Equipment
Mineral Fuels and Oils
Machinery, Mechanical Appliances, etc.
Preparations of Vegetables, Fruits, Nuts & Other Plants

It imports petroleum, sugar, lentils, and transportation equipment, among other essential items.

Imports are so essential that the government had to cancel examinations for millions of school students because it ran out of printing paper.

Lessons for India

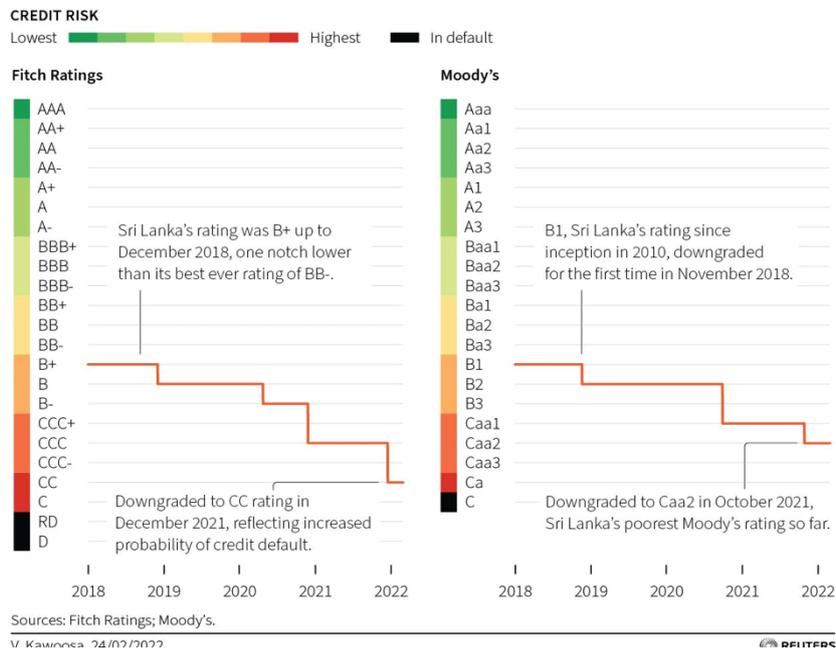
Kautilya's economics as prescribed in 'Arthashastra' also emphasizes the importance of developing industries that can make the nation self-sufficient. India is on the right path by initiating programmes like Atmanirbhar India that encourages localized production as well as introducing production-linked incentive schemes (PLIs) for various sectors of the economy.

"In order to promote growth of global trade with emphasis on exports from India and to support the increasing interest of global trading community in INR, it has been decided to put in place an additional arrangement for invoicing, payment, and settlement of exports / imports in INR,"

❖ Credit Rating

Sri Lanka's falling credit score

The debt-laden island nation is struggling to fill its shrinking foreign currency reserves and raise funds from the international capital markets after a series of credit rating downgrades. Credit ratings are an independent assessment of a country's creditworthiness and an indication of the risk associated with lending money to it.



Sri Lanka missed interest payments on its \$1.25 billion international sovereign bonds maturing in 2023 and 2028. Global rating agency Standard and Poor today lowered long-term foreign currency sovereign credit rating on Sri Lanka to "SD" (selective default) from "CC" as the crisis-hit Island nation missed an interest payment on bonds.

Sri Lankas Failed Infrastructure Projects

NelumKuluna: Financed with almost \$100 million in loans from China, the NelumKuluna tower was to be the tallest building in all South Asia, housing luxury hotel rooms, conference halls, shopping malls, and the infrastructure needed to power digital television networks. From its inception, the Lotus Tower has been a point of debate, with critics of the tower arguing that it is essentially an expensive political vanity project, which should not have been a priority given the ever-growing debt burden that the country has to bear.

During president Mahinda Rajapaksa's rule, the small sea town of **Hambantota** got internationally recognized when the president came up with ambitious plans to build an international airport, a **seaport** and an **international cricket stadium**, which has a greater number of seats than the total population of the town. While many lenders like India denied providing Sri Lanka with the loan because of the lesser opportunity in that area, China went ahead and provided the country with loans and assistance. The port drew only 34 ships in 2012, and there is just one international flight per week at the airport.

❖ Political Dynasty

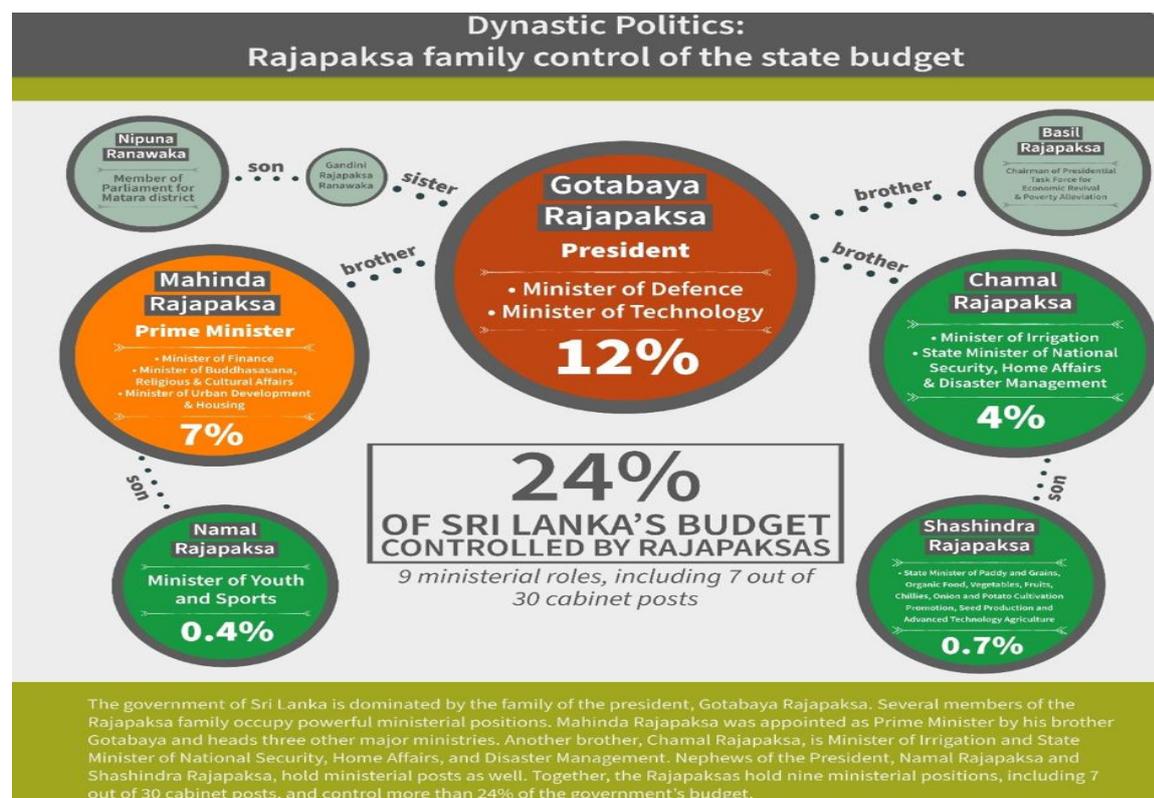
In Sri Lanka, for decades, only a few families have controlled wealth and political power. This tradition has created a vicious cycle in which political parties and all other functioning institutions serve primarily the interest of these families and not the state. Elections have become a process of handing power from one family to another, with succession tightly controlled.

Booted out in the crisis, the most recent family to hold power were the Rajapaksas. The Rajapaksa family regime spanned nearly fifteen years from 2005 to 2022, briefly interrupted from 2015 to 2019.

The family first came to power in 2005 when Mahinda Rajapaksa was elected president of Sri Lanka. Under his leadership, the military managed to put a stop to the South Asian nation's almost three-decades-long civil war, which finally ended in 2009. The conflict was a clash between the Sinhalese-dominated Sri Lankan government and the Liberation Tigers of Tamil Eelam insurgent group, which had hoped to establish a separate state for the

nation's ethnic Tamil minority, who make up about 15% of the population of 22 million. By leading the military into a triumphant victory over the Tamil rebels and appealing to the nationalist sentiment of the Buddhist-Sinhalese majority, a popular and charismatic Mahinda tightened his grip on power. The Rajapaksa brothers were seen as war heroes by the Sinhalese majority.

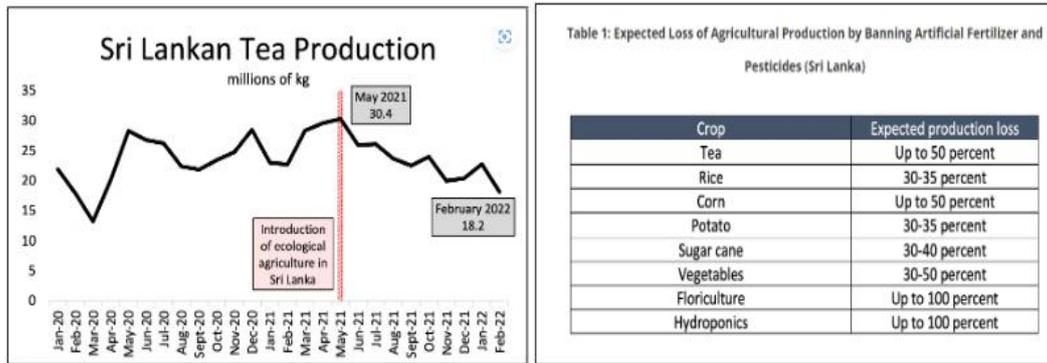
The President appointed several members of his family to major ministerial positions. Mahinda Rajapaksa, older brother to Gotabaya and former President, heads three large ministries in addition to his role as Prime Minister: Minister of Finance, Minister of Buddhasasana, Religious, and Cultural Affairs, and Minister of Urban Development and Housing. Another brother, Chamal Rajapaksa, is Minister of Irrigation and State Minister of National Security, Home Affairs, and Disaster Management. Nephews of the President, Namal Rajapaksa and Shashindra Rajapaksa, also hold ministerial positions – Namal is the current Minister of Youth and Sports while Shashindra heads a State Ministry focusing on agriculture. Yoshista Rajapaksa was Ex chief of Staff to PM. The Ministry of Defence, which has the largest budget allocation, and a newly established Ministry of Technology, are overseen by President Gotabaya Rajapaksa himself.



❖ *Over Military Spending*

Sri Lanka's recent military expenditure on the war against Tamils has been reported to be as follows; The Eelam War III between 1995 and 2002 had a cost of 1.3 million dollars. During Peacetime between 2002 and 2005, about 1 and half million dollars was spent, and soon after, the Eelam War IV from 2006 to 2009, an additional 1.5 million dollars was spent. Even after ending the war in 2009, Sri Lanka has continued to expand its army through the elite Special Task Force, Police and is today allocating 11% of its annual expenditure on defence. Sri Lanka had allocated 3.3% of its GDP to military expenditure during the war. After the cessation of war, military expenditure has not been considerably reduced. Though the proportion has been shown at 2.1%, the real military expenditure is reported to be 1.7 million dollars more than during the war period. With the spending of 170 million dollars on pension payments alone for the retired military personnel. The Government of Sri Lanka has raised the salary of the defence personnel by 45%, even after the war and has deployed the bulk of its army in the Homeland of Tamils.

(Below Figure is Impact of banning Artificial Fertilizer and Pesticides and sudden move towards Organic Farming)



❖ **Conclusion**

The severity of Sri Lanka’s economic crisis is evidenced by the fact that the country is being widely pointed to as a textbook case of how an economy should not be managed. Sustainable policy, this was something in which Sri Lanka failed miserably. Any extreme step without planning will definitely lead to downfall and collapse of that policy first and then economy. Keeping high aims for one’s nation is good, but if that comes with a cost of playing with people’s life and that’s where the tragedy begins.

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Sri Lanka's Economic Crisis Explained

On top of a reliance on imports, and inability to buy them due to rapidly depleting foreign currency reserves, Sri Lanka is currently over **\$51 billion** in debt to foreign entities. Here's a look at how it happened.

2009
The country's civil war ended and the government turned its focus towards to economic development, stressing local production and sales over exports.

2019
Significant tax cuts were introduced draining government revenues.

2020
The COVID-19 pandemic hit severely hurting Sri Lanka's tourism industry.

2021
A ban on imported fertilizers was implemented to counter the depletion of the country's foreign currency reserves. But a reliance on local, organic fertilizers led to a crop failure and further reliance on food imports.

Apr 2022
Protests began in Colombo demanding President Gotabaya Rajapaksa's resignation.

May 2022
Pro-government supporters attacked protesters resulting in Prime Minister Mahinda Rajapaksa stepping down. Food inflation increased over 57%.

June 2022
The IMF arrived in Sri Lanka to discuss a potential bailout.

3 Key Causes of the Crisis:

- A significant reliance on imports
- Foreign currency reserves near empty (down 90% from 2019 level)
- Defaults on massive debt payments

The Crisis at a Glance

- \$51B** Current debt
- 39%** Current consumer inflation
- \$50M** Foreign currency reserve levels

Sri Lanka: Foreign Debt Summary as of end April 21

The country's recent defaults on its debt payments will discourage lenders to provide funds and with little foreign currency to buy even food and fuel imports, it will be a long time before the debts can be paid.

What it Means:

- Protests in Colombo are becoming increasingly violent
- People are queuing for entire days to get fuel and food

In a bid to counter the effects of the crisis, the government is currently in talks with the IMF to discuss a bailout. Additionally, China has engaged the country in debt restructuring talks and ministers have gone to Russia to discuss discounted oil prices.

Source: Department of External Reserves, Sri Lanka

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