

The Sri Lankan ECONOMY

PART ONE

Perception / Claim

Stock market has plunged due to business confidence 'plummeting'

Reality

The stock market has been quite buoyant

A stable financial system that creates a favourable environment for depositors and investors and the effective functioning of markets promoting investment is vital for economic growth.

The Central Bank is deeply committed to contribute to the prosperity of Sri Lanka ameliorating the quality of life of people through sustainable wealth creation including all segments of the society.

The beginning of a year may be a good time for

Reflection

Assessment

Planning future action

At the same time let's try to understand the country's economy thrust, direction and targets.

Many negative claims and perceptions leading to gloom and doom have been built up systematically, through:

▼ Deliberate misinformation and negative publicity campaigns conducted by interested parties, including terrorist groups and sympathizers - Eg: 'failed state', 'banana republic' campaign

▼ Promotion of various economic and political agendas to undermine the economy and thereby, the country - Eg: threat of non-payment of sovereign debt

▼ Let's therefore take a look at Sri Lanka's performance and judge for ourselves.

▼ To do so, let's examine some of the claims/perceptions and assess such claims against the reality and/or the actual ground situation...

Perception / Claim
Sri Lanka's growth is erratic and unsustainable

Reality

Sri Lanka has been experiencing strong and sustainable growth

Sri Lankan economy recorded a growth of well above 6 per cent for the third consecutive year for the first time since Independence, demonstrating that Sri Lanka has now moved on to a higher growth path of above six per cent per annum from the historical average of around four to five per cent. The economy grew by 6.8 per cent, the annual average rate of unemployment reached its lowest ever recorded level of 6.0 per cent, while the per capita income rose further to US dollars 1,617 in 2007. This performance is commendable, as it was achieved in a challenging environment of heightened security concerns arising from intensified terrorist activities and rising petroleum and commodity prices in international markets which threatened the achievement of price stability. Sri Lankan growth has outperformed peers in the region, as well as single B and BB peers.

See Chart C & D



Perceptions / Claims vs. Reality

Perception / Claim

Growth has been only in services

Reality

All economic sectors have posted strong growth

SERVICE SECTOR

The services sector continued to be the major sector of economic expansion during the year contributing 62 per cent to overall economic growth, with the share of total GDP remaining at the same level as in 2006.

It also provided employment to approximately 41.2 per cent of the labour force. The service sector growth was driven by export trading services and port related services, reflecting the healthy external demand, while the domestic oriented services, such as banking and telecommunication services also contributed significantly towards the better performance.

INDUSTRY SECTOR

Industry sector contributed 28.4 per cent share of GDP in 2006.

The textile, wearing apparel and leather products category, which is the major export oriented industrial sub-sector of the country, recorded a higher output with the increased utilisation of Generalised System of Preference (GSP+) duty concessions. Garment industry contributed more than 40 per cent of total export earnings grew by 4.0 per cent in 2006 and expanded by 8.4 per cent during the first nine months of 2007 with the benefit of GSP+.

AGRICULTURAL SECTOR

The sector contributed 12.1 per cent share of GDP in 2006. In the year 2007, most of the sub-sectors in the agriculture sector achieved relatively high growth rates except for tea and paddy. Continuous efforts to enhance the quality of Sri Lankan tea, higher global demand and increased value added led tea prices to rise well above the global average price, offsetting the decline in production in 2007. Rubber production benefited from attractive prices, combined with the adoption of new technologies. In order to develop the rubber sector, steps were taken to increase the cultivation area, providing more incentives to growers and improved extension services. Coconut production rose by 3.0 per cent during the year benefiting from favourable weather but the prices of coconut and coconut based products increased sharply reflecting the world trend of increasing demand for organic oils to produce bio-fuel as a supplement to expensive fossil fuel.

See Chart A & B

Perception / Claim

FDI has dried up because of terrorist violence

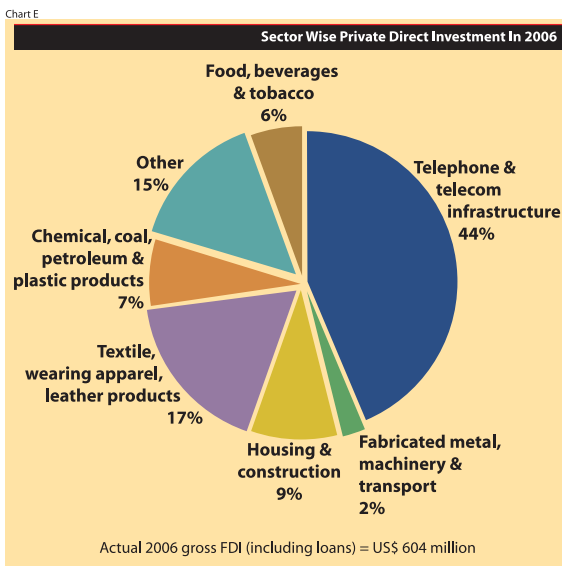
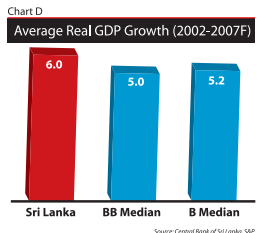
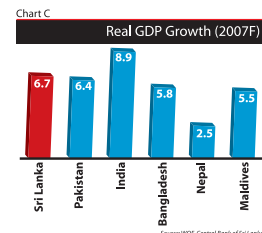
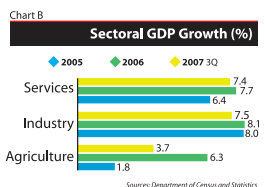
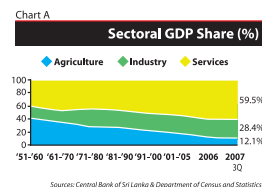
Reality

There has been a strong FDI pipeline

Foreign Direct Investment (FDI) inflows increased by 21.6 per cent to US dollars 734.4 million in 2007.



Growth in all sectors anticipated



accounted for more than 50 per cent of total FDI inflows to the country.

The BOI, the apex government institution entrusted to attract and promote foreign and local investment to the country continued to play a major role in enhancing FDI in 2007. More than 70 per cent of FDI were invested in the area of infrastructure development including telecommunication, power generation and housing property and office complex development.

BOI approved 605 new projects in 2007 under Sections 17 and 16 of the BOI Act with an investment commitment of Rs.489.4 billion compared to 364 projects approved in 2006 with service sector absorbing 154 projects with an investment commitment of Rs.160.6 billion of the contracted investment in 2007 under the Section 17 of the BOI Act while the Rs.20.6 billion was absorbed by the factory industry. The major recipients of investments included housing and property development, telecommunication, power generation and infrastructure development projects.

Within the factory industry sector, textile, wearing apparel and leather products; chemical, petroleum, coal, rubber and plastic products; food, beverages and tobacco products; non-metallic mineral products and fabricated metal products, machinery, and transport equipment categories were the major recipients of contracted investment in 2007. During 2007, 48 contracted projects were expanded with the investment commitment of Rs.70.4 billion. Key features of attracting FDI in Sri Lanka were geographic position, strategic access to Indian markets, high quality workforce, open market economy.

See Chart E

Perception / Claim
Domestic investment has declined because of low business confidence

Reality

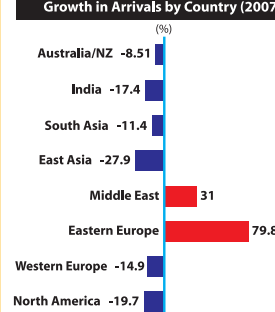
Gross Domestic Investment has steadily increased

Investment to GDP increased 32 per cent in the past five years. Private sector investment accounted for 86 per cent of total investment expenditure, and increased by 30 per cent during 2006.

Highly targeted public sector investment accounted for 14% of the total in 2006.

Predominant sectors: construction, manufacturing, telecommunication, services, transportation, leisure.

Chart F



Actual 2006 gross FDI (including loans) = US\$ 604 million

Sources: Central Bank of Sri Lanka & Board of Investments

Sources: Sri Lanka Tourist Board