

**A PROJECT REPORT ON**  
**“AN EMPIRICAL STUDY ON SRI-LANKA  
ECONOMIC CRISIS”**

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# **An Empirical Study of the Sri-Lanka Economic Crisis**

## **1. Introduction:**

The year of 2019 was a time which turned the world upside down from an unstoppable virus which created chaos. It is the biggest challenge that mankind is facing in the 21st century ( El-Erian, 2020). Sources said that the Corona virus was first identified in Wuhan China in December 2019 and later it was named COVID - 19 by the world health organization. China was the first country to lockdown their cities to stop the spread of the disease and later on it was detected in the European region as well. Italy, Spain and many more countries suffered from the virus causing those thousands of deaths. On the 11th of March 2020 world health organization (WHO) has announced that the virus is prevalent all over the world. The economic impact resulted by the pandemic is a crucial challenge to almost all the countries including small and emerging economies (IMF, 2020). COVID - 19 is so dangerous than any other virus in the world ([www.WHO.int](http://www.WHO.int)) .The WHO has identified this virus is more effective than other viruses because a single person who carries the virus can easily influence more than five other personals. Also this virus will cause more fatal results on elderly people and still the world is struggling to find a solid vaccination to fight COVID - 19. However COVID - 19 has infected the south East Asia as well and countries like India, Pakistan, and Bangladesh are facing the challenge of COVID -19 cases increasing significantly. First COVID - 19 case was detected in Sri Lanka was 27th of January 2020 and after that The Government has taken drastic and very effective action to prevent this virus and at the current situation in Sri Lanka was identified as one of the countries which controlled the virus successfully in the world ([www.WHO.int](http://www.WHO.int) ). However, social and economic impact caused by the pandemic is a serious challenge for Sri Lankan economy ahead. It was noted that responsive strategies are extensively encouraged by government to protect the industries.

### **I. IMPACTS OF THE COVID-2019 TO THE SRILANKA ECONOMY AND LOCAL CONSTRUCTION INDUSTRY:**

The Local economy mainly consists of exports, tourism, foreign employment and Industrial sector. Amongst them the industrial sector contributes a 27% from the GDP ([www.treasury.gov.lk](http://www.treasury.gov.lk): Mid-Year Fiscal Position Report- Ministry of Finance, 2019). The COVID - 19 viruses has struck the Sri Lankan economy more than what was expected in many ways. Exports, tourism, foreign employment and Industrial sectors are heavily affected by the pandemic. The unpredictable rapid pace of the virus has restricted all the human involvements in those

industries and crippled them in a short time of period. Many industries in Sri Lanka have been making responsive strategies to survive the businesses as it notices in international economy.

Most of the countries have closed their Airports and Harbors to prevent the arrival of the virus. Also they have locked down either the entire country or certain states and kept isolated to stop the spread of the virus (CRS, 2020). Basically, starting from the local street market business to worldwide exports and imports transactions were limited except for essential needs and even most of the share market locations were shut down. Many industries found Sri Lanka is also responding to the pandemic situation but some firms seemed getting panic with the given business scenario. The constructions related infrastructure like roads, irrigation, electricity, health were slowed and constructions related to leisure, manufacturing, and condominiums were stopped temporarily. Sri Lanka was totally shut down except for essentials on 23rd of March 2020 and the construction industry also went under full shutdown. The Sri Lanka government health authorities came up with an excellent method of controlling the situation and they have joined with the Sri Lankan three forces and Police for the execution. The three forces and the police are the most trusted party in Sri Lankan community and during the pandemic they have done a tremendous duty to overcome the problem.

## II. RESPONSIVE STRATEGY OF SRI LANKAN GOVERNMENT AND CONSTRUCTION INDUSTRY:

The political stability of a government is important to impose new regulations on crisis situations like this. The current government has taken proactive measures in controlling the spread of the virus in a very effective way like establishing quarantine centers which was introduced for the first time in the world. Isolating suspected patients and first contact personals in quarantine centers under the overall supervision and care was the main duty of the centers. The national intelligence network was occupied to track down the suspects based on inter graded plan and the special task force was formed for the entire operations. The government has imposed curfew in the beginning for the infected areas and gradually it has been imposed on the entire country. Also trespassing from district to district was strictly prohibited and those who were self quarantined at their houses were also monitored. Government has invested in many areas such as modifying hospitals into COVID - 19 related affairs and constructing new centers to monitor the suspected people as quarantine centers. Also the government has put up a fund to support the virus prevention actions and special COVID - 19 TASKFORCE CENTER was established to coordinate the all activities. The national intelligence was used by the government to track down the infected people and the people who got contacted with the infected people. To streamline the process, it developed an Android Application for quick access. The economic impact caused by the pandemic situation to Sri Lanka was alarmed with the significant drop of local currency against American dollar. In fact, many industries were seriously affected in Sri Lanka as it

remains common to the world. This paper highlights how industries were affected and reactive strategies were taken to respond it. Accordingly, construction industry was mainly opted for the review. Most of the construction workers get their wages on a daily basis or twice a month. According to sources, there are 188,877 workers who are engaged in the construction field in Sri Lanka and 680,000 people were directly and indirectly depend in the sector. The construction industry contributes 9% to the national GDP. There is no confirmation on their wages where they have been paid or not. The industry of construction is a field which is not based on an upfront payment system. By looking at the crisis, the central bank of Sri Lanka has granted a series of facilities to small and medium scale companies such as working capital loan scheme and investment purpose loan scheme. In the construction industry, most of the payments are done after a certain time of credit period. The total value of the construction Industry in Sri Lanka is worth of Rs. 397.77. Billion and from this more than 50% of the work has been completed without getting paid by the Client to the Contractor and most of the payments are still not settled by the contractor to the Supplier ([www.srilankabusiness.com](http://www.srilankabusiness.com)). But in overall, construction sector companies and product manufacturers should come up with a holistic plan to make it as a successful.

### III. ECONOMIC SHOCK RESULTED BY COVID-19 AND STRATEGIC RESPONSE OF SRI LANKAN CONSTRUCTION INDUSTRY:

Within the financial year of 2020, Sri Lankan government has given a considerable percentage of tax concession to the taxpayers and consumers as a motivation to boost the investment on the local SSRG International Journal of Economics and Management Studies (SSRG-IJEMS) – Volume 7 Issue 6 – June 2020 ISSN: 2393 - 9125 [www.internationaljournalsrg.org](http://www.internationaljournalsrg.org) Page 75 economy. On the other hand government has expected a Rs. 500 Billion in revenue for the year 2020. But, as per the pandemic situation, there is a question mark to the government whether it will experience the expectation in time (ICRA Lanka simulations, 2020). According to Asian Development Bank, Sri Lankan Economy is forecast a 2.2% growth during the year 2020 and with the effect of the COVID - 19 impact, it is expected to slow down the growth of the economy in the mid-year. However, it is also predicted that the growth will be regained at the later part of the year. Meanwhile, it has also predicted that a 9% depreciation of the local currency against the USD (Asian Development Outlook, 2020). Additionally, 25% exports for the USA and 36% for Europe had been temporarily held up due to the crisis and very low percentage of exports were executed during the pandemic period. This paper makes a special attention to Sri Lankan construction industry as it contributes to the local economy in a significant way including indirect impacts like job opportunities. The seriousness of the Covid-19 and aftermath for construction industry is connected to different matters. Most of the related sectors of construction industry like cements, paints, building materials, cables,

electronic items and chemicals depend on the raw materials imported from China and India. Thus, depreciation of local currency against foreign currency is a negative impact as costs extra for the industry (Asian Development Outlook 2020). Most of industrial product manufacturers in Sri Lanka should revise their pricing strategies due to the extra risk of currency fluctuation, for instance cement industry is one of the critical sector faces this type of a risk when importing raw materials like gypsum ([www.srilankaimporter.com](http://www.srilankaimporter.com)). In addition, most of the construction projects were going on an upwards trend after the presidential election and the sectors like road infrastructure, industrial factories, leisure sector, housing apartment sector were booming in massive scale. But due to the COVID - 19 issue all the projects were shut down and most of the workers were stuck inside the Colombo city. Most of the construction companies found difficulty in maintaining their carder due to the restricted crossing over district. Paying wedges, fulfilling basic needs was a huge issue that the contractors faced. When it comes to the hospitality and condominium sector, those sectors are always interconnected and contribute a lot to the construction sector. World class condominium companies started their projects in Sri Lanka Such as PORT CITY, The One by Ritz Carlton, Shangri-La Hotel by Shangri-La group, ITC by Indian Tobacco Company, and some local projects like Water front, Marine Drive Hotel Project, 606 tower, Vinil City hotel are also some highlights. All these projects are held up due to the situation and contractors and suppliers are facing issues when recovering their investments on time. Thus, it looks like there will be very slow growth of the industry for the next three months.



Source : <http://in.pinterest.com>

The 2019–2022 Sri Lankan economic crisis is an ongoing economic crisis in the island

nation of [Sri Lanka](#) largely attributed to the economic mismanagement of the incumbent government, leading to unprecedented levels of inflation, near-depletion [foreign exchange reserves](#), shortages of medicinal supplies and rising prices of basic commodities. The crisis has said to be caused by multiple compounding factors such as [tax cuts](#), [money creation](#), a nationwide policy to shift to organic or biological farming as well as events such as the [Easter bombings](#) in 2019 and the [impact of the COVID-19 pandemic](#). The subsequent economic hardships resulted in the public openly voicing their dissent, leading to one of the largest demonstrations in the island's history: [The 2022 Sri Lankan protests](#).

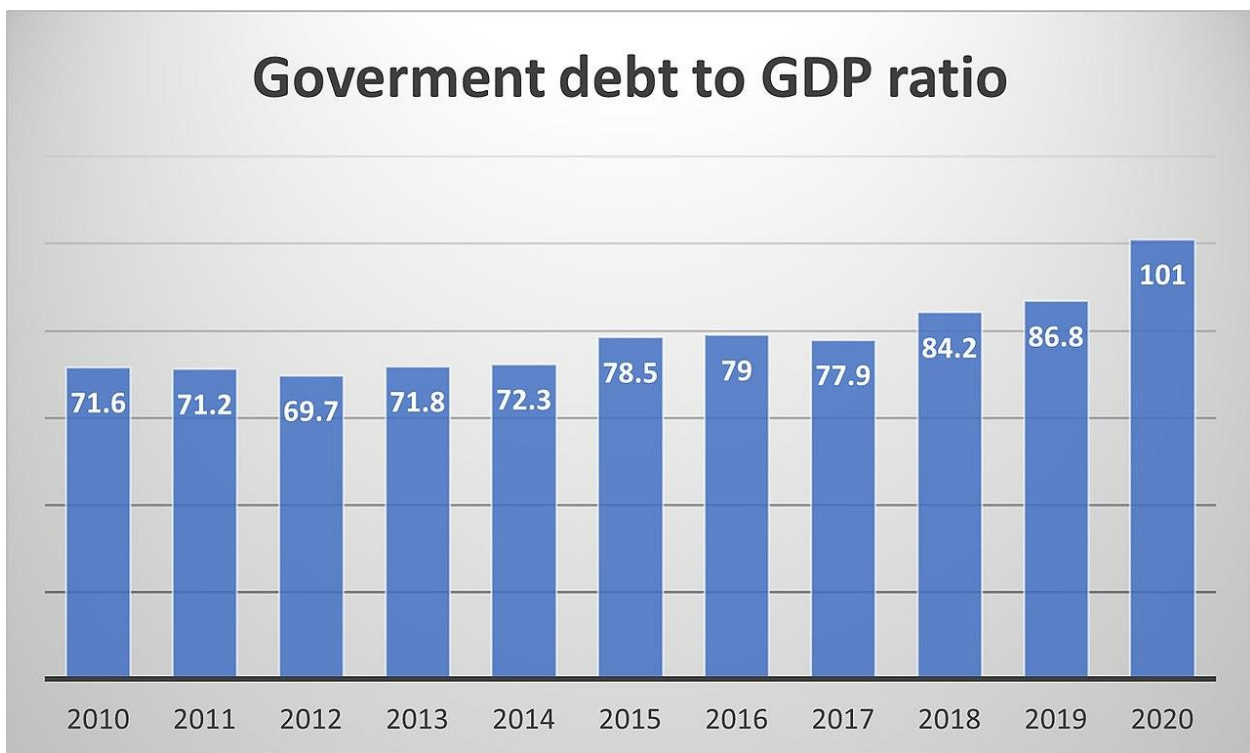
Sri Lanka had been earmarked for [sovereign default](#), as the remaining foreign reserves of US\$1.9 billion as of March 2022 would not be sufficient to pay the country's foreign debt obligations for 2022, with US\$4 billion to be repaid. An International Sovereign Bond repayment of US\$1 billion is also due to be paid by the government in July 2022. According to [Bloomberg](#), Sri Lanka has a total of US\$8.6 billion in repayments due in 2022, including both local debt and foreign debt. In April 2022 Sri Lanka announced that it is defaulting making it the first sovereign default in Sri Lankan history since gaining independence in 1948.

According to W. A. Wijewardena, a former Deputy Governor of the [Central Bank of Sri Lanka](#), the country was a long way into an economic crisis in 2015. The government which came into power in 2015 knew this and had been warned by the [Institute of Policy Studies of Sri Lanka](#) of a number of risks. While then Prime Minister Ranil Wickremesinghe in 2015 had presented a strong economic policy to address the situation, the coalition government could not get the policy pushed through Parliament which would eventually result in further policy confusion in the coming months. The government did not adequately address the economic warnings and emerging dangers, consuming itself in other government related activities such as "constitutional reforms". Certain practices, including those by the Ministry of Finance led by [Ravi Karunanayake](#), were globally frowned upon. Election related economic decisions were pushed such as excessive distribution of freebies. The [Institute of Policy Studies of Sri Lanka's](#) 2014 State of the Economy Report highlighted [hot money](#), worrying borrowing practices, temporary and superficial quick-fixes and monopoly of FDI flow into one sector, viz. hospitality. Further political turmoil in 2018 worsened the economic outlook. By that time, the government had carried out several reforms under an IMF supported program towards fiscal monetary consolidation and had successfully controlled inflation. These reforms included an automatic fuel pricing formula which significantly reduced fiscal risks posed by state-owned enterprises (SOEs), raised the [Value Added Tax](#) (VAT) rate from 11 percent to 15 percent and broadened the VAT base by removing exemptions. Many of the reforms were reversed by the new government after the 2019 elections.

The previous administration also drafted the 2019 Central Bank Bill to make the Central Bank independent from political influence by banning the Treasury Secretary and any member of

the Government from becoming members of the Monetary Board. Money printing was also to be banned as the bill states “The Central Bank shall not purchase securities issued by the government, by any government-owned entity, or any other public entity in the primary market, Then Central Bank Governor, Dr. [Indrajit Coomaraswamy](#) noted Balance of Payments issues, increased inflation and asset bubbles as reasons for the ban. The Sri Lanka Podujana Party led by the Rajapaksas opposed an independent Central Bank and discarded the bill as soon as they came to power.

Many experts compared [Lebanon's economic situation](#) with that of Sri Lanka and had warned that Sri Lanka too was on the way to defaulting on its sovereign bonds. Both nations had similar issues, including deep economic crises occurring after their successive governments piled up unsustainable debts following the end of civil wars.



Source: [https://en.wikipedia.org/wiki/File:Government\\_debt\\_to\\_GDP\\_ratio.jpg](https://en.wikipedia.org/wiki/File:Government_debt_to_GDP_ratio.jpg)

A. What is the economic crisis?

Economic crisis is usually seen as a situation in which the economy of a country experiences a sudden downturn in its aggregate output or real gross domestic product (GDP). The result of the economic crisis is a decline in real income per capita and an increase in unemployment and poverty.

B. What is the Sri Lanka economic crisis?

Sri Lanka is currently in the throes of an unprecedented economic turmoil since its



independence from Britain in 1948. The crisis is caused in part by a lack of foreign currency, which has meant that the country cannot afford to pay for imports of staple foods and fuel, leading to acute shortages and very high prices.

C. Why is Sri Lanka economic crisis?

The 2019–2022 Sri Lankan economic crisis is an ongoing economic crisis in the island nation of Sri Lanka largely attributed to the economic mismanagement of the incumbent government, leading to unprecedented levels of inflation, near-depletion foreign exchange reserves, shortages of medicinal supplies and rising prices.

D. How is the Sri Lanka economic crisis?

The free-market economy of Sri Lanka was worth \$84 billion by nominal gross domestic product (GDP) in 2019 and \$296.959 billion by purchasing power parity (PPP).

## **2. Review of literature:**

**Rasika S. Jayasekara (2022)** It is widely recognized that better health is a prerequisite for the overall economic and social development of a nation. Sri Lanka, like many other countries experiencing the epidemiological transition, will have to make effective decisions on health-care service management and the development of education and training programs for health-care professionals. This paper provides a comprehensive review of current health service administration, health status, trends and issues, and health financing and resource allocation in Sri Lanka. The review revealed that Sri Lanka has achieved a relatively high health status given a low level of spending on its health-care services; however, Sri Lanka still experiences vital health problems in all stages of the life cycle, mainly related to lifestyle and the epidemiological transition associated with widespread societal and economic crises.

**S Danoshana, T Ravivathani 2021** Now corporate governance issues have received wide attention of researchers for more than three decades due to the increasing economic crisis around the world. This research study consider the impact of corporate governance on the performance of listed financial institutions in Sri Lanka as main objective and recommend a suitable corporate governance practices for improving performance of listed financial institutions. To achieve these objectives, the researcher use Return on equity, Return on assets, as the key variables that defined the performance of the firm. On the other hand, Board size, Meeting frequency and audit committee of the company are used as variables to measure the corporate governance. Twenty five listed financial institutions were selected as sample size for the sample period of 2008–2012.

The data will be collected by using the secondary sources. According to the analysis, variables of corporate governance significantly, impact on firm's performance and board size and audit committee size have positive impact on, firm's performance. However, meeting frequency has negatively impact on firm's performance

**(Larry Elliot, 2020)** The entire tourism industry was shattered by the pandemic and tourist destinations like Europe, China, Eastern Asia, USA were totally unvisited Political instability was shown in most of the countries and most governments were put into great difficulty by showing the inability to control the spread of the virus

**Ozili, & Arunx 2020** a former Deputy Governor of the Central Bank of Sri Lanka, the country was a long way into an economic crisis in 2015. The government which came into power in 2015 knew this and had been warned by the Institute of Policy Studies of Sri Lanka of a number of risks. While then Prime Minister Ranil Wickremesinghe in 2015 had presented a strong economic policy to address the situation, the coalition government could not get the policy pushed through Parliament which would eventually result in further policy confusion in the coming months. The government did not adequately address the economic warnings and emerging dangers, consuming itself in other government related activities such as "constitutional reforms". Certain practices, including those by the Ministry of Finance led by Ravi Karunanayake, were globally frowned upon. Election related economic decisions were pushed such as excessive distribution of freebies. The Institute of Policy Studies of Sri Lanka's 2014 State of the Economy Report highlighted hot money, worrying borrowing practices, temporary and superficial quick-fixes and monopoly of FDI flow into one sector, viz. hospitality. Further political turmoil in 2018 worsened the economic outlook. By that time, the government had carried out several reforms under an IMF supported program towards fiscal monetary consolidation and had successfully controlled inflation. These reforms included an automatic fuel pricing formula which significantly reduced fiscal risks posed by state-owned enterprises (SOEs), raised the for Value Added Tax (VAT) rate from 11 percent to 15 percent and broadened the VAT base by removing exemptions. Many of the reforms were reversed by the new government after the 2019 elections.

**Kanchana N Ruwanpura, Neil Wrigley 2011** Complementing the rise of ethical trading initiatives there has been a parallel growth in the number of academic studies tracking their origins and evolution, and assessing the implementation and success of social auditing practices. Despite this, the consequences and responses to the implementation of codes of conduct relating to labour standards at sites of production remains an understudied topic. This article focuses on those issues in the context of the global apparel industry using evidence from interviews with managers in the Sri Lankan garment manufacturing sector. In particular, it focuses on the contradictions and tensions inherent in compliance, and the anxieties management face during a period of global economic crisis, in a country which is generally considered to be in the vanguard

of promoting and protecting ethical labour standards.

Anne Thushara Matthias, Saroj Jayasinghe

**The Lancet Global Health, 2022** Threats to health from an economic crisis are multifold. 1 Stress and lack of health care can increase cardiovascular morbidities. Malnutrition can affect generations of children. Communicable diseases can increase due to rising costs of amenities and the weakening of preventive and control measures. The accompanying political uncertainties, widespread protests, and social disruptions adversely affect mental health and worsen quality of life. These multiple crises have the potential to cripple health systems. At the time of writing, Sri Lanka announced it would be defaulting on its debts. 2 There is already a severe shortage of foreign exchange, leading to drug and device scarcities that have affected routine surgeries and clinical services. Lending organisations, such as the World Bank and International Monetary Fund, are negotiating relief packages and these could include costcutting measures and restricting the services provided by the tax-based health system. These strategies could adversely impact a health system that has an exceptional record of achievements, despite relatively low investments in health, providing all levels of care with no user charge. What can we do? At a macro level, health care professionals have already advocated for political changes, justice, and more transparent decision making that would help us overcome the economic crisis. A charter of the Professionals of Sri Lanka has been circulated, and many health-care professionals are participating in protests calling for change. First, and at a more specific level, actions including tapping into social networks and professional organisations overseas to obtain financial donations and drugs, consumables, and equipment must be taken.

Second, cost-effectiveness of interventions will have to be a priority concern. A series of steps are proposed, as follows: more reliance on clinical judgment during clinical practice rather than laboratory investigations, development of appropriate costeffective protocols for management, and prescribing of generic medicine.

### **3. Objective:**

1. To study of srilanka economic crisis.

## 2. Lessons learned from srilanka economic crisis to Indian economy

### Research gap:

The srilanka economic crisis data received from a number of studies available on srilanka economy. Later, than the widespread survey of the existing literature it is observed that whereas, some researchers examined the causes and impact of financial crisis and its arranging time in arrange of happening of events, whereas other group of researcher try to study the sector bases implications of the financial crisis and they have tried to offer remedies for mitigating aftermaths of the crisis. It is observed that though the large numbers of studies are carried on covering the different aspects of the crisis, but there are insufficient studies that deal with the intra and inter comparisons of economic 16 indicator in India to observe how the financial crisis has impacted the Indian economy. So, the present study deals with pre crisis and post crisis comparisons of the economic indicator of India separately which is not yet agreeably enclosed by the existing studies.

### **Scope of the study**

This study limited to srilankan economy perspective how an economy is impacted with excessive debt and unbstable policies if government will impact the nations growth.

### Methodology:

The present study is a descriptive and empirical research. This research attempts to study srilanka economic crisis by applying various economic indicator .

### Secondary Data:

The secondary data constitute reports and other records of the concerned bank reports, handbook of statics on the Srilanka economy, government publications, articles, book, journals and websites.

### Period of study:

The present study examines the selected economic indicators for a period of years of srilanka economic crisis (2019-2022)

### Tools for data analysis:

#### 1. Impact of Covid-19 on Poverty:

The COVID - 19 pandemic has had countless effects on every aspect of life. However, it has particularly affected the economy and poverty levels. The impact of COVID - 19 on poverty in Sri Lanka has halted significant poverty reduction progress due to how the pandemic has affected work stability and household income. The update includes a special focus Section, which discusses the impact of COVID-19 on poverty. With jobs lost and earnings reduced. especially in

urban areas and among private sector employees and informal workers, the \$ 3.20 poverty rate is projected to have increase from 9.2 percent in 2019 to 11.7 percent in 2021. With jobs lost and earning reduced poverty increased significantly in 2020. Over 500,000 people are expected to have fallen into poverty as a result of the crisis. Source: Sri Lanka Development Update 2021 - Economic and Poverty Impact of COVID - 19 (The World Bank) Above graph presents which led to an increase in the \$3.20 poverty rate from 9.2 percent in 2019 to 11.7 percent in 2020. This more than reverses the progress made since 2016, when the poverty rate was 11.0 percent. Estimates using the national poverty line suggest a similar trajectory. Extreme poverty (as measured by the \$1.90 a day poverty line) is projected to have double from 2019 levels. Moreover, the poverty gap, which measures the distance to the poverty line, is estimated to have increased from 17.9 percent in 2019 to 20.0 percent in 2020. This implies that not only are there more poor people, but also that the poor have fallen deeper into poverty.

## 2. Impact of Covid-19 on Household Income:

The impact of COVID - 19 on poverty in Sri Lanka and the ensuing instability in the labor market has had significant effects on households and forced many to adjust their lives. In just the first few months of the pandemic in 2020, nearly 40% of households had lost all of their income and 93% faced some consequences from the pandemic. Sri Lankan's are still feeling the effects of the initial economic shock. Because of reduced income, families have to find alternative ways to meet their basic needs. For many, food insecurity is now a prominent issue. As a result, many people have cutback on food consumption. To save on costs, households may consume less nutritious food, which could adversely impact the health of people, especially children.

## 3. Impact of COVID-19 on GDP of Sri Lanka:

If the government did not intervene, GDP would be lower than the level under the baseline (No COVID-19) for more than 20 years; With the actual additional cash transfers to the households decided by the Government (only for 2020), GDP is not going to reach the GDP level without COVID-19 even 20 years later; With a lifecycle approach only for 2020, the GDP would recover much before compared to the other scenarios. Impact of COVID-19 on GDP of Sri Lanka If the government did not intervene, GDP would be lower than the level under the baseline (No COVID-19) for more than 20 years; With the actual additional cash transfers to the households decided by the Government (only for 2020), GDP is not going to reach the GDP level without COVID-19 even 20 years later; With a lifecycle approach only for 2020, the GDP would recover much before compared to the other scenarios.

The reports provide an update on Sri Lanka's economy and outlook, highlighting the devastating impact of the pandemic. Sri Lanka's economy contracted by 3.6 percent in 2020, the worst growth performance on record, as is the case in many countries fighting the pandemic. At the same time increased expenditures and lower revenues amid the pandemic contributed to a

deterioration of the fiscal situation. Public and Publicly guaranteed debt is estimated to have increased to 109.7 percent of GDP. Reserve declined to an 11 year low in February 2021, and the exchange rate depreciated by 6.5 percent from January through March 17, 2021. Striking a balance between supporting the economy amid COVID - 19 and ensuring fiscal sustainability remains a key challenge. The government took proactive measures to mitigate the impact of the pandemic. Despite limited fiscal space, resources were allocated (approximately 0.7 percent of GDP) for health measures, cash transfers and postponed tax payments. While public

Expenditures increased declined, resulting in a widening of the fiscal deficit in 2020. Due to the economic contraction and the elevated fiscal deficit amid COVID - 19, public and publicly guaranteed debt is estimated to have increased to 109.7 percent of GDP. In line with the government strategy to reduce external debt over the medium-term, debt financing relied increasingly on domestic sources.

Reasons for the Sri-Lanka crisis:

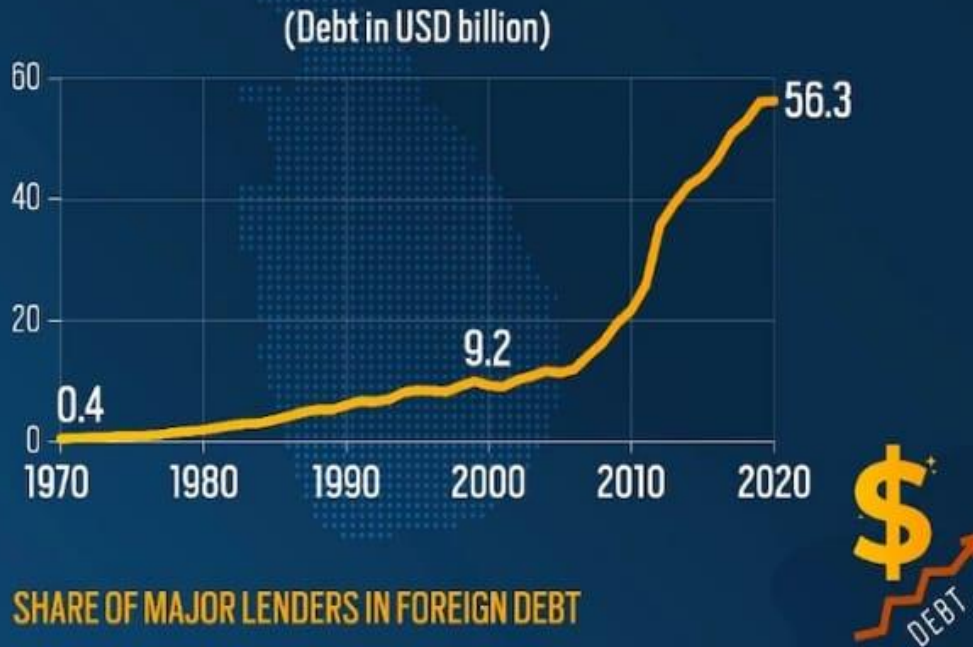
- Default on foreign debt: Economic mismanagement has depleted most of Sri Lanka's foreign reserves. Sri Lanka defaulted on its foreign debt worth \$51 billion as it faces the worst economic crisis, for the first time since it independence in 1948.

Sri Lanka's high dependency on imports for essential items like sugar, pulses, and cereals may result further in the economic meltdown as Sri Lanka lacks foreign reserves to pay for its import bills.

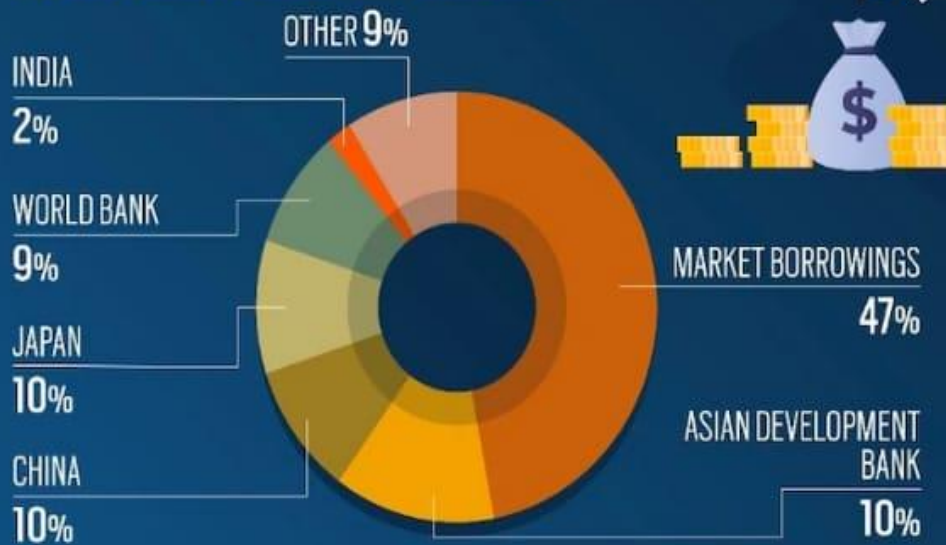
The situation was further aggravated due to additional tax cuts which ended up hurting Government Revenue.

# SRI LANKA'S FOREIGN DEBT

PUBLIC DEBT PROJECTED TO HAVE RISEN FROM 94% IN 2019 TO 119% OF GDP IN 2021



## SHARE OF MAJOR LENDERS IN FOREIGN DEBT



Data as of April 2021

Source: Department of External Resources, Sri Lanka; World Bank

Graphics: Samrat Sharma, Mudita Singh

Source <http://www.Indiatoday.in>

- Debt Trap Diplomacy: It is claimed that Sri Lanka was caught in a vicious web of money lending by China for Infrastructure projects (Hambantota Port) and was unable to pay them back.
- Fall in tourism: The rise of the Covid-19 pandemic and Easter bomb blast 2019 led to a fall in

tourism revenues, as loss of visitors from three key countries- India, Russia and UK.

Tourism earnings fell from \$4.4 billion in 2018 to \$506.9 million in 2021.

Tourism is Sri Lanka's third largest foreign exchange earner.

- Agriculture crisis: In 2020, due to ban on chemical fertilizers and switching overnight to make agriculture 100% organic had a negative impact on the economy, especially in rice and sugar production.

In just one year, the state of agriculture productivity totally devoid of any fertilizer and pesticide fell into ruins as farmers were unprepared for the sudden shift to organic farming.

The government revoked the fertilizer ban in November 2021, but by then the damage had already been done as food security of the nation had totally broken down due to a Sri Lanka's agricultural land remaining unused due to a lack of timely availability of fertilizers leading to fall in productivity.

According to estimates, Sri Lanka's paddy, tea and rubber production are dependent on chemical inputs in a range of 90-94%.

Organic farming can do more harm than good if implemented in a hurry without preparing the infrastructure and the farmer mindset and most importantly ensuring that food security is not adversely compromised due to its adoption owing to low yield than conventional farming.

- War-induced inflation: The ongoing Russia-Ukraine war resulted in steep price inflation of crude oil, sunflower oil and wheat.

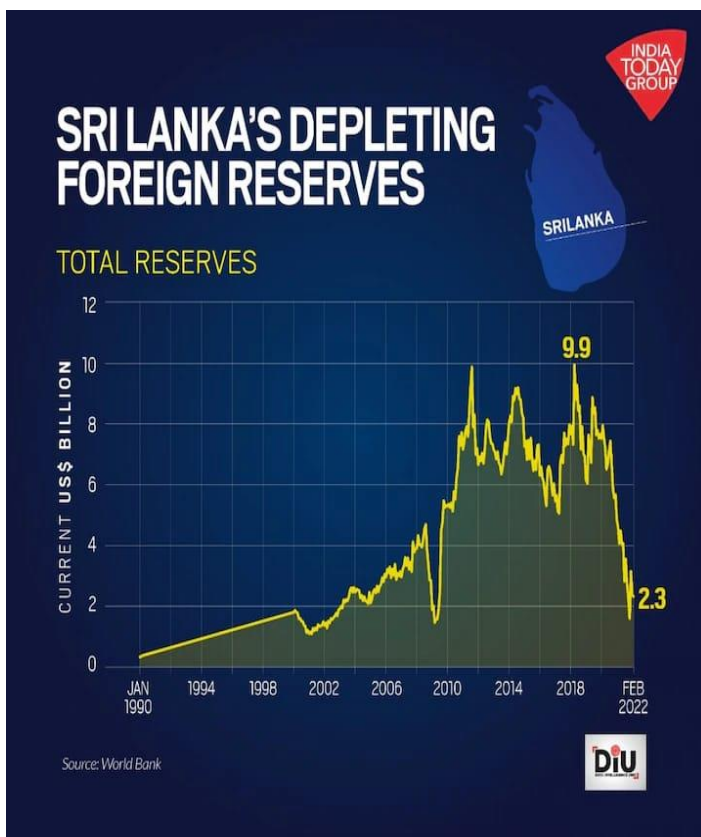
Crude oil prices hit a record high in 14 years with prices soaring over \$125/barrel.

As per the Central Bank of Sri Lanka, headline inflation rose to 18.7% and food inflation stood at 30.2% in March 2022.

- Fall in FDI: Foreign direct investment (FDI) has drastically decreased to \$548 million in 2020 as compared to \$793 million and \$1.6 billion in 2019 and 2018, respectively. In 2022, Sri Lankan Rupee depreciated by more than 50 percent against the US dollar, 31.6 percent against Indian Rupee.

### Weak Currency:

On the other side, 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.

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.

source: <http://www.Indiatoday.in>

Measures taken by Sri Lanka to control the crisis

- Banned import of luxury vehicles, chemical fertilizers and food items like turmeric to prevent foreign currency outflows.
- Enhancing remittance inflow by establishing a contributory pension scheme for migrant employees, etc.
- Government has made provisions for Special Deposit Accounts to boost investors' confidence.
- Assistance from bilateral partners like Bangladesh, India and China.

So far, India has provided financial assistance of US\$ 2.4 billion.

## Conclusion

As study suggested that country debt and equity should be trade off. If it exceeds the normal level against GDP of state, government should act proactive manner, if government is not acting according to welfare of nation and acting according to short-term motives like introducing schemes, pensions, subsidies which will impact the sustainability of nation and integrity as well.

As there are several reasons for this crisis like complete adoption of organic farming, Covid floods, Easter bombings in 2019 and several other natural disasters created some damage to GDP of state economy but the major damage happened because of unstable socialistic policies of Podujana Peramuna party government leads to high inflation and economic crisis

This is also one of the great learnings for developing nations how far they can go for debt in their GDP and dependence of foreign trade and foreign exchange, self-sufficiency of economy also matters in the present competitive era.



Source: <http://in.pinterest.com>

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