# Spotlight: Econ Op-eds in Summary

Week ended 19th May '21

## In Summary

*The underneath contains summaries of the articles given above, including key extracts from these articles.*

**1. Port City Economic Commission Bill is far from objective of developing as regional financial centre**
**By: Lasantha Somaratne**

- The Port City Economic Commission bill will ensure that the area acts as a 'free zone', having differing laws from the rest of the county. The first free zone in the country was established in Katunayake, in 1978, and was successful in bolstering apparel exports. One of the most successful free zones in the world is the Dubai International Financial Centre (DIFC).

- The development of such zones are able to attract skilled workers, financial capital and trade flows. Leadership is a key component for the success of Port City, with the bill having diluted this, as it is not chaired by the President nor Prime Minster. Efficiency within the zone is also affected, as regulators may not be well equipped to deal with a global financial centre.

- Given that there is no difference in the legal system applicable between the country and the zone, the Bill may not provide sufficient incentives to bring in major competitive advantages for the country. Regardless, the Bill will be a major step in bringing Sri Lanka closer to being a regional player, and it should focus on being the financial centre for South Asia.

The Port City Economic Commission Bill by its name is the governing law of the land. It has sub-sovereign status or a certain level of autonomy with regard to commercial operations within the zone, which is not a new concept. The concept of 'free zone, free economic zones and free financial zone' is dated and well-established around the world.

The history of free zones dates back to 1959; it was first established in Shannon, Ireland known today as Shannon Free Zone, spread across 600 acres adjacent to Shannon Airport.

Asia quickly learnt and adopted the concept. Countries like Singapore and Malaysia, taking the first mover advantages established very successful free zones. Those free zones played a vital role in economic development of those countries.

The establishment of a free economic zone in Sri Lanka dates back to 1978, the first in South Asia with the enactment of the Greater Colombo Economic Commission and the establishment of Katunayake Export Processing Zone (KEPZ). Since then, many steps were taken to improve and widen the framework. The establishment of KEPZ signifies the birth of a successful apparel manufacturing sector in Sri Lanka, the single largest export income earner today.

However, the world of free zone evolved and expanded at a much faster than the rate at which we adopted. The most successful financial centres in the region such as Singapore and Dubai adopted the concept of free zone beyond the manufacturing and processing and established a novel concept 'free financial zone'. The establishment of such free financial zones enabled them to overcome one of the major challenges, the lack of trust in the local legal and regulatory system in establishment of a global financial centre.

One of the fastest growing and successful ‘free financial zones’ in the world is Dubai International Financial Centre, widely known as ‘DIFC’, established in 2004. The emirates with a legal system based on the Islamic law principles, lacked the necessary global recognition for an international financial centre. Birth of the DIFC with a fully-fledged legal system including its own judiciary, chaired by a chief justice was a game changer. Since then, DIFC has accented to 16th place in The Global Financial Centres Index (GFCI) in 2021 rankings.

The DIFC is an integrated financial centre completely insulated from commercial and civil laws of the emirates for conduct of financial transactions, with a comprehensive state-of-the-art regulatory system which eventually received global recognition. The success of any financial centre depends on its legal system and the regulator. The key component of a financial system is the regulatory process.

To maintain the highest level of credibility, The Dubai Financial Services Authority (DFSA), the regulator of DIFC, has always employed highly credible foreign regulators, vastly experienced at key financial centre regulatory bodies. Similarly, DIFC courts comprise of foreign judges with international reputation and a chief justice of high credibility. The mechanism and the credible team together have created the trust among the global financial market participants to do business at the DIFC.

Quite similar to the benefits of an economic or an industrial free zone which includes attracting FDIs, boosting exports, diversification of the economy and creation of employment opportunities for local labour force allowing them to compete in the international scale, financial free zones attract financial capital, talent and trade flows.

**Key components of a financial centre**

Leadership

With the above introduction to the DIFC, we should evaluate the proposed Port City Economic Commission Bill objectively. To give high level powers to the DIFC, the role of its chairman has been entrusted to the deputy ruler of the Dubai. In contrast, the president or the minister in charge will appoint the chairman of Port City Economic Commission. This arrangement has diluted the power of the commission to an ordinary body. If the commission is to be chaired by the President himself, the Prime Minister or at least the minister in charge of the subject economy or finance, the commission would have been made more powerful.

Dilution of role of the regulator

The registration of companies under the Port City Commission will not be different from companies incorporated elsewhere in Sri Lanka; the registration will be under the registrar of companies. Contrastingly, the DIFC has its own company registrar with its own company law.

Port City regulation is entrusted with existing regulatory bodies such as the Central Bank and SEC. It should be evaluated whether existing regulators have the capacity to compete with global financial centre regulators like DFSA. The fact is the existing regulators lack international experience in financial centre regulation in the global context. Moreover, expecting a credible regulatory system under such inexperienced regulators is far from reality. As a result, the objective of modern global financial centre housing under the port city will be a tough ask.

Judiciary system

Except an Arbitration Centre under the international arbitration code, the legal system applicable under the Port City will be the local legal system. Major difference in the DIFC as a financial centre is, it has a separate legal system, a commercial and civil law enacted by the DIFC and a separate court system. Port City will have to refer commercial and civil disputes to the local judicial system. There is no proposal to establish even a special commercial court under the Port City, dedicated for resolving civil and commercial disputes within the Port City. To make port city a reliable financial centre for the region, the port city should have enacted its own legal system and commercial courts system. In that sense, the proposed Port City Economic Commission Bill will not bring major attractiveness and competitive advantages to the port city for the development as an international financial centre.

**Conclusion**

Sri Lanka adopted the concept of free zone much earlier than its peer group, setting up the first industrial free zone in 1978. Since then, the concept of free zone has expanded into many sectors, latest being the financial free zone. Despite the early start, Sri Lanka lacked the progression in embracing the changes while countries like Dubai, Malaysia and India established financial free zones.

The key pillars of a financial free zone are the constitution of its formation, the regulator and the judicial system. In comparison to the most competitive regional financial centres such as the DIFC in Dubai, the Port City Economic Commission Bill doesn't have provisions to establish a credible mechanism to attract global financial market participants.

Nevertheless, the proposed Port City Economic Commission Bill is one major step towards a long journey. The major advantages of Sri Lanka are its comparative cost, the strategic maritime location and being at the edge of South Asia; a home of one quarter of the global population with a robust growth outlook. The Port City at the initial stage should target for facilitation of South Asian trade among the hostile neighbours quite like Dubai facilitated the trades within troubled Middle East. Eventually, the scope of the port economic commission should be enhanced to house a state-of-the-art regional financial centre, initially targeting to be the financial centre for the South Asia.

For the full article – Refer Daily FT

**2. COVID-19 resurgence a severe threat for economic revival**
**By Nimal Sanderatne**

- Expected economic revival in 2021 might be quite challenging in Sri Lanka due to the resurgence of Covid cases in many regions. Further disruptions in agricultural production, manufacturing and services may further lead to reduced employment, increased poverty and food insecurity. Exacerbating the impacts are the policy challenges relating to the agricultural and manufacturing sectors which could lead to higher imports and lower exports.

- Even though the considerable level of mobility during the New Year season is often identified as the cardinal error leading to the increase in Covid cases, more factors such as relaxation of restrictions for some tourists could have contributed to the introduction of new mutations. Whatever the actual reason is, it is clear that it is related to the impatience to get the economy moving by relaxing restrictions.

- According to the annual report of Central Bank, Sri Lanka expects to rebound strongly in 2021 and sustain high growth. This was however under the assumption of a recovery in the global economy and its direct effect on increasing exports. At present this is quite unrealistic due to the fact that cases are building up in Sri Lanka as well as the severe situation in India. Thus, for a sustainable economic recovery, successful Covid containment is a mandatory requirement.

The resurgence of COVID-19 and its rapid spread in most regions of the country is a serious threat to the economy. The much anticipated economic revival in 2021 may face serious difficulties owing to production activities being hampered by the spreading of COVID-19 in many parts of the island.

**Fall in production**

Most economic activities are likely to be hampered by the resurgence of COVID-19. Agricultural production, manufactures and services are likely to face severe setbacks in the coming months owing to lockdowns, travel restrictions and non-availability of fertiliser and raw materials. Reduced employment would depress incomes and increase poverty. Widespread food insecurity is most likely.

**Global revival**

Meanwhile, global economic revival too may be delayed owing to a continued spread of COVID-19 in some countries. The expected 'V' shaped global recovery is unlikely though some countries like the United States appear to be containing the pandemic. International travel restrictions could also hamper the expected revival of tourism later this year.

**Economic downturn**

Unlike in 2020 when our economic growth was mainly affected by the global economic downturn, this year's economic performance will be hampered mostly by the dislocation of both agricultural and industrial production in the country due to the resurgence of COVID. This resurgence was due to the haste to normalise the country and adoption of inappropriate policies.

All blame for the economic disruption cannot be on COVID-19. Apart from the impact of COVID-19, inappropriate economic policies could bring about severe difficulties to increasing production of both agriculture and manufactures.

**Tourism**

Tourism and related services could be severely restricted by COVID in originating countries, restrictions in international travel and the COVID situation in the country. On the other hand, the relaxation in restrictions to enhance tourism has been a reason for the spread of COVID in the country.

**Policies**

Appropriate economic policies are crucial to mitigate the emerging problems. Conversely, ill-advised and inappropriate policies could aggravate the economic downturn and hardships of people. The ban on chemical fertiliser is a glaring example of this.

Output of rice and other food crops as well as tea and rubber output is likely to fall drastically later this year and in 2022. This implies higher food imports and lower agricultural exports. It will result in drastic reduction in farmer incomes, higher food prices and widespread food insecurity among the poor.

**Decision making**

Has the Government heeded either technical advice of agronomists, agricultural economists or farmers before this drastic decision was taken? There is a spate of scientifically based articles on the inadvisability of banning chemical fertiliser immediately in the media and among scientists.

**Relaxing restrictions**

There is a broad consensus that the cardinal error was the relaxation of preventive measures during the Sinhala and Tamil New Year that resulted in the spread of the dangerous virus. Relaxation of restrictions for some tourists could have contributed to the spread of the virus and the introduction of new mutations of it.

There was also considerable social irresponsibility in the manner in which people acted that contributed much to its spread. There was no exemplary behaviour with the higher echelons of society and political leadership.

**Precondition for economic revival**

The country's economic performance would be determined largely by the measure of success in containing COVID-19. The eradication of COVID-19 is a pre-condition for economic revival.

The World Health Organisation (WHO) had warned all countries that haste to get economies to function may endanger the containment of COVID-19. They had repeatedly advised that containment of COVID-19 should precede the reopening of economic activities as the spread of COVID-19 would paralyse economic activity.

Sri Lanka's medical services had also warned about the possibility of a third wave if restrictions were lifted during the festive Sinhala and Tamil New Year. These predictions have materialised and the third wave of COVID is extensive and beyond the capacity of the medical facilities to cope with it.

**Vulnerability**

The country's economic vulnerability could be compounded by inappropriate policy responses that would aggravate the global and local economic shocks. For instance, the current shortages in fertilisers that farmers are experiencing could reduce rice, vegetable and food production.

The ban on chemical fertilisers could result in a severe drop in food availability requiring large food imports at high prices. Similarly, loss of tea and rubber production would affect export earnings.

**Manufacturing**

There are indications from time to time of manufacturing industries having difficulties in obtaining raw materials. This, together with travel difficulties and lockdowns could hamper industrial production as well.

In such a grave context inappropriate economic policies could heighten difficulties and hamper production.

**Unrealistic expectation**

In this backdrop, it is unrealistic to expect the realization of the Central Bank's optimistic economic scenario expressed in the Annual Report of the Central Bank for 2020 that the "Sri Lankan economy is expected to rebound strongly in 2021 and sustain the high growth momentum over the medium term, buoyed by growth oriented policy support."

This expectation of economic rebound at the beginning of this year was based on the prospect of a global economic recovery would enhance the country's exports and revive global travel and tourism. This is not likely this year with the increasing spread of the virus in several regions of the world and in Sri Lanka. In fact the situation in the country and in neighboring India could be more potent than the global situation and retard the economy.

**Conclusion**

The containment of COVID in the country is a precondition for economic production and income generation. While foremost efforts must be given to this, the economic difficulties should not be compounded by inappropriate policies.

For the full article – Refer The Sunday Times