Spotlight: Econ Op-eds in Summary

Week ended 20th November '19

In Summary

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

1. Formidable economic challenges for new President
By: Nimal Sanderatne

- The newly elected president will face formidable economic challenges caused from the fundamental macroeconomic weaknesses of the economy. Political stability and peaceful conditions are vital pre-requisites to be ensured for economic development. Sound economic policies should be carried out irrespective of the election promises made.

- Large scale foreign borrowing and further burrowing to service those borrowings has increased our external financial vulnerability. Improving the BOP is essential in overcoming this. While a BOP surplus is expected for 2019, much higher export growth is vital in sustaining this in the longer term. Policies that encourage manufactured, agricultural, ICT exports, alongside new export sectors, are important.

- Reduction of the high public debt levels through reducing fiscal deficits also remains key. Political compulsions have derailed fiscal consolidation processes in the past. Means of curtailing government expenditure while enhancing government revenue should be explored. Certainty of such economic policies is vital to generate business confidence and attract FDI that would drive economic growth.

The President elected today will have to face daunting economic challenges. The fundamental macroeconomic weaknesses of the economy must be addressed by sound economic policies effectively executed to achieve economic stability and get the economy into a higher trajectory of growth than the current economic growth of less than 3%.

Economic challenges

The foremost economic challenges facing the new President are the servicing of the foreign debt, reducing the fiscal deficit, improving the balance of payments by reducing the trade deficit by expanding exports, and stabilising the macroeconomic fundamentals by pursuing pragmatic and appropriate economic policies and restoring foreign and investor confidence to get the economy moving.

These are formidable challenges owing to their magnitude and the political environment. Their resolution would be even more difficult if the election promises are granted immediately and the macroeconomic fundamentals are weakened further. This is so as the plethora of premises will increase public expenditure while reducing revenue.

Immediate concern

The political developments immediately after the presidential election would have an important bearing on the economy. Peaceful conditions and political stability are vital after the presidential election. The newly elected President has to work together with the Prime

Minister and government and prevent a constitutional crisis similar to the one in October 2018.

A post-election chaotic state of affairs would cripple the economy once again and make the resolution of economic problems exceedingly difficult. Ethnic and religious harmony that is a perquisite for the country's economic development, has to be ensured from the commencement of the new regime.

Economic policies

It is imperative that the new President commences his term with sound economic policies irrespective of the election promises. He must establish the preconditions for economic growth without delay. Although this may not be politically feasible owing to the commitments given during the election campaign, the President should be advised that although good economics is bad politics in the short term, sound economic policies are good politics in the long run. The economic problems of the country can only be solved by a long-term perspective of economic development.

External financial vulnerability

The external financial vulnerability of the country has arisen due to large scale borrowing to finance massive infrastructure projects that have not increased foreign earnings. Consequently, due to low balance of payments surpluses the servicing of the debt required further borrowing that has increased the nation's external financial vulnerability.

The foreign debt has ballooned to US$ 54 bn at the end of 2018 and its servicing costs are in the range of US$ 3-4 bn.

The servicing of the foreign debt and containing it is of foremost importance to reduce the country's external vulnerability. This in turn requires an improvement in the balance of payments by reducing the trade deficit by expanding exports. The challenge is to reduce the trade deficit substantially by a much higher export growth than achieved recently.

Favourable factors

The good news is that this year's trade deficit is likely to be around US$ 8 bn or less. In the first 7 months of this year the trade deficit fell to US$ 2.7 bn compared to US$ 4.4 bn in the same period last year.

If tourism picks up and workers' remittances do not fall much, there is a prospect of a higher balance of payments surplus that would ease the burden of foreign debt servicing. However, in the longer term a much higher balance of payments surplus needs to be achieved by higher export growth.

Higher exports

This year's reduction in the trade deficit has been brought about by an increase in exports by 2.4% and reduction in imports by 24.6%. It is vital that policies are put in place that would enable a spurt in manufactured exports, enhances agricultural export surpluses, expands new export possibilities and enhances information technology services (ICT).

The export strategy prepared by the government should be executed vigorously to achieve the country's export potential. Sri Lanka that has been and will continue to be an import-export economy will face severe hardships without a new thrust on exports. This is a priority for the new regime.

Public debt

The containment of the public debt by a reduction of the fiscal deficit is vital to stabilise the economy. The public debt has grown to massive proportions. In 2018 the public debt had risen to Rs.12 tn or 83% of GDP. Debt servicing costs alone absorbed nearly the entirety of government revenue. Consequently, the government has to borrow for its other expenditure. Furthermore, this state of public finances distorts priorities in government spending.

Fiscal consolidation

Bringing down the fiscal deficit is vital for economic stabilisation and economic growth. Reducing the fiscal deficit is one of the most challenging tasks as government expenditure has exceeded the original estimates. This year's fiscal deficit is likely to exceed 5% of GDP.

The process of fiscal consolidation that began in 2016 and was progressing reasonably well has been derailed by excessive public spending this year owing to political compulsions. If the promises made during the election are fulfilled there would be a surge in public expenditure and a fall in revenue. This means that fiscal consolidation that is fundamental to achieving economic stability and growth would be adversely affected. The government would need to find ways and means of curtailing government expenditure and enhancing government revenue.

Economic growth

Stimulating economic growth would require stabilising the macroeconomic fundamentals, especially achieving a manageable fiscal deficit of about 4.5% of GDP. Of utmost importance is a framework of economic policies that is certain, realistic and pragmatic. The certainty of economic policies is vital to generate business confidence and attract foreign direct investment (FDI) in export manufactures.

For the full article – Refer The Sunday Times