Spotlight: Econ Op-eds in Summary

Week ended 28th August '19

In Summary

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

1. Political compulsions are destabilising the economy
By: Nimal Sanderatne

- Politically driven economic policies targeting the upcoming elections can lead to a fiscal slippage. This could result in higher public debt that would create adverse impacts on Sri Lanka's macro-economic fundamentals. The resulting debt-servicing costs could eat up government revenue, limiting funds that would be available for other essential expenditures.

- Increases in foreign debt have already exceeded expected thresholds. Therefore, this can lead to a debt trap, particularly if those burrowed funds aren't utilized to increase export earnings. Further, the dominance of political narratives would distort economic issues in the run up to the elections.

- Regardless of the outcome of the election, the next government would have to deal with the above adverse impacts. The economy is likely to get worse, as the adoption of sound economic policies will be put aside until a new parliament is elected. Hence restoring the economy will be a massive challenge.

Political compulsions

The political compulsions of the elections are driving the government to adopt policies that would enhance the government's votes. These policies are moving the economy into the brink of an economic crisis.

This is especially so with respect to heavy public expenditure that would expand the fiscal deficit. Resolving the resultant deterioration in macroeconomic fundamentals would be a herculean task for whoever forms the next government.

Economic consequences

The expansion in the fiscal deficit will erode price stability, increase public debt, exert pressures on the exchange rate, affect external trade adversely and people's livelihoods would be affected on top of the adversity caused by the tourist crash.

Public debt

The debt-to-GDP ratio at the end of 2018 was as much as about 80%. This is an unacceptable level. Its further increase this year and its servicing costs are a severe burden.

Implications

In most years the debt servicing costs exceeded or absorbed nearly all government revenue. The means that funds are not available for other essential expenditures. This has been an important reason for low growth.

In such situations all current and capital expenditure have to be met by further borrowing from domestic and foreign sources. This results in a distortion in priorities in public spending. The means inadequate funds for education, health and development projects.

Increasing debt

The acknowledged threshold for the fiscal deficit is about 3 to 4% of GDP and the debt-to-GDP ratio is expected to be kept at no higher than 60% of GDP. The current position exceeds both these thresholds. It is also not merely the amount of the public debt per se but its use, impact and the capacity to repay that matters.

Debt is not necessarily bad for an economy. Foreign debt provides the means by which the savings-investment gap could be reduced. However, when a country's foreign borrowing exceeds an amount where its servicing costs through export earnings are too high, then it is on the road to a debt trap. This is particularly so if the borrowed funds are utilised in a manner that does not increase the country's export earnings.

Politics and economics

Vast majority of the electorate consider the presidential election as of foremost importance. This is perhaps due to the view that whoever wins the presidential election would swing the electorate to the winning candidate's party or alliance.

The focus is gradually shifting from who would be the Presidential candidates to who will be the President of the Republic. Although economic issues would figure in the coming two elections, most references to the economy will be distorted and not based on actual economic facts and on sound economic thinking. Political issues would no doubt dominate the election campaign.

Formidable challenges

Whatever be the political outcomes, the next government would have to face the serious economic issues of a high foreign debt of over US$ 50 Bn and difficulties of meeting the high foreign debt repayment obligations. The vulnerability of the country's external finances would be a mammoth problem.

Conclusion

The adoption of sound economic policies would have to await the outcome of the presidential election and then another period of uncertainty till the parliament is elected. Meanwhile, the state of the economy is likely to get worse and the remedial measure more difficult to adopt.

Restoring economic stability and enhancing economic growth are massive challenges for the next government.

For the full article – Refer The Sunday Times

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2. Time that Govt. sees reality – CCI drops to 36
By: Rohantha N.A. Athukorala

- The economic vision for Sri Lanka set in 2015 has yet to fully materialize, with key initiatives to drive tourism being dead in their tracks. This results in an expectation that the country's second quarter growth could be negative, resulting in year end growth of only 2.9% - one of the lowest in the region.

- The low growth is mainly driven by a fall in consumer and business confidence. This sentiment was emulated in both the consumer and business confidence indices released by Nielsen, with the Consumer confidence index hitting an all-time low of 36 and the Business confidence index hitting a low of 81.

- Prior to the Easter Sunday attacks, overall volume of household consumption had dropped through 2017 and in 2018 up to the third quarter. This trend was reversed through tax breaks rather than an increase in household income. However, in the last three to four months things have once again become very challenging for the Sri Lankan household with even consumption of milk powder contracting.

The 2015 promise

As we look back, we find that the promise set for the country economically in 2015 has not materialized. Unfortunately, we are reeling after four years with a disastrous performance of 3% before the disaster in April and behind India, Pakistan and Bangladesh. It is estimated that 2Q2019 might be at minus growth and the year will end at 2.6% growth as per the latest ADB forecasts.

George Soros at the Harvard Economic Forum, said: "Your sweet spot in the economy is tourism." When the diagnostic was done on Sri Lanka's tourism industry, the key issue highlighted was the need to build a strong positioning in the global traveler.

The research revealed that the awareness of the product was at a low 4% globally. However, even after five years the 'global communication campaign' has not taken off ground which is unfortunate given that almost Rs. 6 bn remains idling in the bank accounts of Sri Lanka Tourism.

This is only just one of the key economic strategies that has not been implemented, which has caused severe ramifications to the industry. The last straw was when the private sector of the tourism sector took a decision not to support the Government agenda to drive a 'push strategy' of staging road shows in Europe. In simple words the industry emphasized the need of the hour was a 'pull strategy' initiative like a global media campaign similar to Maldives, Malaysia and Thailand.

Consumer Confidence Index crashes

Data reveals that the proposed relief measures adopted post the Easter attacks have also not worked though many commitments were communicated immediately after 21April.

Some speculate that the manner in which the crisis was managed further aggravated the situation rather than neutralising it. This has resulted in the latest Consumer Confidence Index released by Nielsen hitting an all-time low of 36(the lowest in the last 36 months) whilst the Business Confidence Index has also hit a low index of 81 as at end June.

If we do a reality check of a Sri Lankan consumer purchasing (prior to the Easter attack) as per Nielsen data, things were very rough at the household end. The overall household volume consumption had dropped the whole year of 2017 and in 2018 upto Q3 (for almost two years in a row).

To be specific,

1Q 2017	-3.3%
2Q 2017	-3.1%
3Q 2017	-3.7%
4Q 2017	-8.2%
1Q 2018	-11.7%
2Q 2018	-14.5%
3Q 2018	-8.3%

but then things began to improve with many tax breaks given by the Government rather than household income increasing. However, in the last three to four months things have once again become very challenging to the Sri Lankan household with even consumption of milk powder contracting.

Summary

In marketing, we call this marketing myopia; we see how the consumer requirement has changed but an organization continues to hold on to the product. By this time the consumer has started to move to a competitor product.

For the full article - Refer Daily FT