

## Spotlight: Econ Op-eds in Summary

Week ended 18<sup>th</sup> September '19

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### In Summary

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

#### **1. Declining agricultural exports since 2018 serious economic concern** **By: Nimal Sanderatne**

- Agricultural exports are more significant than indicated by their export values since the import content is much lower than for manufactured exports. Despite recent export growth, agricultural exports (with the exception of sea food exports) have been consistently declining despite the international demand. This can have negative impacts on BoP and economic growth.
- Tea exports, which have a high domestic value addition, have decreased due to a decline in the exportable surplus and lower prices. While natural rubber exports are low, rubber manufactures have earned significantly. Hence, rubber has the potential for a higher contribution to export earnings. Thus, increasing production of these crops are vital.
- Declining trend of coconut exports is likely to continue. However, unless production is increased to match rising domestic consumption, trade balance can be impacted through imports of edible oils. While increasing spices production is vital, Sri Lanka's reputation for quality spices is threatened by mixing of low-quality imports which can have long run implications.

The recent decline in agricultural exports is a serious economic concern as it has an adverse impact on the country's BoP and on economic growth. The decrease in agricultural exports has dragged down last year's and this year's noteworthy export growth.

Total exports increased by 10.2% in 2017, by a further 4.7% in 2018 and increased by nearly 5 % in the first six months of this year. Despite this recent export growth, agricultural exports fell by 6.8 % last year and by a further 6 % in the first half of this year, compared to the same period last year.

#### **Significance of agricultural exports**

Tea, rubber and coconut accounted for 94% of exports in 1950. Even in 1977 these three crops constituted 79% of total exports. That pattern has changed after the liberalisation of the economy in 1977, when there was a significant diversification of the economy and of exports.

By 2000 agricultural exports declined to 20 % of total exports and tea rubber and coconut exports amounted to only 17% of total exports. In 2018 total agricultural exports accounted for less than 17% of total exports. This diversification of the economy and exports is a favourable development. However, agricultural exports declined due to lower exportable surpluses owing to lower production, and, especially in the case of coconut, higher domestic consumption too. Tea production on estates and rubber production on estates and small holdings have been unsatisfactory.

This recent unsatisfactory performance of agricultural exports is worrying as all agricultural exports, with the exception of sea food exports, decreased in 2018 and in the first half of the year. There is an international demand for most agricultural exports that cannot be met owing to inadequate production and quality issues.

## Tea

Tea has been the country's main export from pre-independence times. Even today tea is the main agricultural export. Tea exports declined by as much as 6.6% in 2018 and by 6% in the first half of this year compared to the same period last year. This is owing to both a decrease in the exportable surplus of tea and lower prices. Despite the declining importance of tea in total exports, its value addition is higher than those of manufactured exports that have a high import content. Therefore, it is important to increase productivity and production, especially on the tea plantations that have low yields owing to the senility of large extents of estate tea land, inadequate replanting and under planting and labour scarcity.

## Rubber

Rubber exports declined owing to both a decrease in production and the use of most natural rubber produced in the country being used for manufactures. While rubber exports accounted for only US\$ 31.6 mn, in 2018, rubber manufactures earned US\$ 875 mn. This use of natural rubber for manufactures is a favourable development. Had rubber production increased, it would have made a more significant contribution to the country's export earnings. The effective implementation of the Rubber Master Plan to increase natural rubber production by expanding the area cultivated with rubber would contribute much to improving the trade balance.

## Coconut

Export earnings from Coconut have diminished over the years. It amounted to only US\$ 316 mn in 2018: a dip of 11.3% from the export earnings of 2017. This declining trend is likely to continue as domestic consumption is increasing, while there is no commensurate increase in coconut production. While increasing the export surplus of coconut is unrealistic, coconut production should be increased to meet increasing domestic consumption needs. Otherwise there would be an adverse impact on the trade balance owing to an increase in edible oils.

## Spices

Spice exports declined by 11.3% in 2018. There appears to be an alarming development in the export of spices. Sri Lanka's reputation for high quality spices is being undermined by the mixing of low-quality imports and exporting these as Sri Lankan products. This could harm the country's reputation for high quality spices and ruin spice exports in the long run. The potential for increasing spice exports must not be frittered away as the revival of spice exports is of importance for the country's export earnings.

## Final word

The significance of agricultural exports is more than indicated by their export values as their import content is much lower than for manufactured exports. Increasing the country's agricultural exports is vital to improve the trade balance and BoP. This is particularly so with respect to tea, spices and minor crop exports that have fallen.

[For the full article – Refer The Sunday Times](#)

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## 2. A new chapter in lending in Sri Lanka – pros and cons

By: Prasad Edirisinghe

- The General Manager of the CRIB had announced that the Bureau plans to release credit scores of banked citizens from August 2019 onwards. Although this is yet to be done, this could make the country's lending circle much stronger, healthier and could upgrade Sri Lanka's ranking on the World Bank's Ease of Doing Business index.
- The new credit score would make the process of obtaining loans faster for those who have inadequate documentation or collaterals. The Bureau's plan to incorporate utility bill payments to the score also facilitates borrowings for new borrowers. It could also help revive the deteriorating asset quality of the country.
- However, this score comes with a few issues. First of which is the involvement of third parties in borrowing transactions, due to the inability of parties to complete the requirements to obtain a loan and due to tedious tax and legal processes to transfer loans. Another is the exclusion of the informal borrowings from the score due to non-availability of data, resulting in the score not painting a totally accurate picture of one's creditworthiness.

With the recent announcement of releasing credit scores of banked citizens commences a new chapter of the country's lending industry. The General Manager of the Credit Information Bureau (CRIB) Nandi Anthony stated that the Bureau plans to release credit scores of banked citizens from August 2019 onwards (Daily Mirror, 25 July 2019). This is long overdue. The new application certainly uplifts the country to the next level as far as credit evaluation myths are concerned. According to Anthony, the facility will be further extended to all citizens by late 2020.

Under the circumstances, all lending institutes will have to redefine their credit disbursing calculations and approaches. It makes the duties of credit managers and officers easier but also challenging in a different way. The published article further said that the credit scores are calculated using a process which ranges from 250 to 900. When the probability of default is high, the score is low and when it is low the score is high. In layman's terms, if you pay your dues on time you get a high credit score and if you don't pay your dues on time you get a low credit score. When the score is high you are on a better footing to attract decent rates of interest from lending institutions. The CRIB also expects the credit scores to influence the decisions of financial institutes in offering attractive rates for creditworthy customers. They could demand lower interest rates for credit based on their positive credit scores.

### Disadvantages

There are approximately 33 banks and 48 finance companies in Sri Lanka with a workforce of around 88,000. As mentioned earlier, all managers and officers who deal in credit in these financial institutions have a challenging task ahead. They would certainly be asked to consider a reasonable weightage to the solvency of their customers during the credit evaluation process based on the Individual Credit Score allocated by CRIB. The challenge starts there. Accordingly, the system has two main disadvantages;

#### 1. Third party involvement

there are situations in the market where some loans are being paid by third parties. Where the loan is paid by a third party who operates behind the scenes or taken on behalf of another person who doesn't have adequate documents to obtain a financial facility. In

most cases, it is done on-fee basis by the dummy applicants. In some instances, the original party makes payments for a couple of months and then transfers the asset off the record. The custody of the asset is taken over by a third party.

Another common reason in the market to service loans on third party basis is due to tax and legal complications of the new party. Hence, they mutually agree to service the loan on the original owner's name. Given these conditions, the Individual Credit Score makes no impact on the credit officer's credit opinion of an individual. Hence, credit officers and managers should detect such situations, inform their superiors and convince them to make better credit decisions.

## **2. Informal borrowings**

Similarly, CRIB doesn't have the information pertaining to informal borrowings and their monthly rental commitment of customers. However, we shouldn't forget the fact that there exists a vast but undisclosed money lending market in the country. It is evident in most cases that go bad that the genuine information which would have been useful in evading doubtful lending had not been surfaced during the evaluation process – particularly information concerning customers who have borrowed informally from local money lenders and institutes. Such monthly commitments create a colossal deficit in the cash flows of customers.

There is a trend building in the country of settling formal borrowings with informal borrowings to clear irregular CRIB records and then reverting back to formal borrowings. The cash flow issues of such customers remain unchanged though the CRIB records are clear. The credit managers and officers should bear in mind that the intended Individual Credit Score is generated based purely on the repayments of formal borrowings available to CRIB. Hence, credit managers and officers should do their homework during the evaluation process to find out the actuality without depending on the Individual Credit Score alone.

## **Advantages**

### **1. Inadequate documents**

However, there are many positive aspects of the Individual Credit Score. We have seen many customers who are capable of servicing rentals comfortably but don't possess adequate documents to prove their creditworthiness. Under such circumstances, the credit score plays an important role. When they have a history to influence their credit rating, obtaining a fresh or enhanced facility is stress-free. It certainly encourages young and genuine entrepreneurs to obtain financial facilities without a tussle.

Anthony further mentioned that CRIB's next step is to map utility bill payments to the process (how well and promptly you pay your electricity bill, water bill, and telephone bill). This mechanism creates a great impact on new borrowings of freshers who have not borrowed before from the financial industry. As per the data disclosed, the CRIB currently covers 46.5% of the country's adult population, which includes 6.3 mn adults and over 212,000 firms. This figure is expected to significantly increase with the augmentation of data from non-financial intuitions in the future.

### **2. Poor asset quality**

In a scenario where the quality of assets is deteriorating, the Individual Credit Score plays a major role where the quality of credit and its volume are concerned. Fraudulent documents and deeds are everywhere in the industry. Hence, the immovable asset quality is questionable at times. Similarly, the movable (vehicle) market is highly volatile. Thus, collateral dependency is not advisable all the time as a fallback option. Similarly, a lengthy

litigation process which drags cases over four to five years is not prudent most of the time. It should be the last line of defense and treated as the last recourse. Recovery of the loan through agreed monthly rental is the best option available to settle a financial obligation. Such being the case, repayments are mainly determined by the character of the borrower and not by the face value of the collateral offered or the strength of the documents.

## Conclusion

The CRIB also plans to enhance the accessibility of the CRIB reports and scores by enabling citizens to obtain the CRIB reports and scores online. It would be similar to obtaining a medical report from your medical laboratory in the future. Once in a while, you can check your credit score online. On your own, you can assess whether you are running a healthy credit score or not. You can take necessary precautions to rectify your situation as you do with your health. Nevertheless, have in mind that bankers and financiers are trained to look suspiciously on those rectified situations even though you have a healthy record afterwards, and be mindful to maintain an unblemished credit record right throughout. It is also understood that retail outlets too will have access to their customers' credit information to draw their credit limits. These moves make the lending circle of the country much stronger and healthier. The credit score upgrades Sri Lanka's ranking on the World Bank's Ease of Doing Business index. Non-Performing Advances (NPA) which are rising at an alarming level at present can be curtailed to a large extent by applying credit score to the credit evaluation process.

[For the full article - Refer Daily FT](#)

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