

Economic Policy Statement
made by the Hon. Prime Minister – 20.10.2017

Hon. Speaker,

I take this opportunity to clarify the current status of the economy and the way forward for our government and people.

I emphasized the need for rebuilding the Sri Lankan Economy when I delivered the Economic Policy Statements in 2015 and 2016.

The challenge faced by us today is to sustain what we have built, and strengthening the economy. This task has two prongs. The first is to stabilise the economy creating a country free of debt for our future generations. The second is to expand the economy giving all Sri Lankans the chance for prosperity.

Strengthening and Expanding the Economy

We inherited a plagued economy. Since 2015, our Government took a number of major steps to stabilise the economy. As I mentioned in the Economic Policy Statement last year, there is no use of holding the past responsible. We should try our best to go forward getting the past faults rectified.

Despite the reasons which are beyond our control and challenging domestic and global conditions, we were able to sustain a steady GDP growth rate of 4.4%. We were able to maintain the unemployment rate at 4.2% and to reduce the budget deficit to 5.4%.

Perhaps the most important thing is the change of our focus than the statistics. We focussed on a development based on tradable goods rather than developing on non-tradable goods. For years, the growth of the Economy of Sri Lanka was heavily reliant on huge public investments in infrastructure. Only the industries such as construction industry were strengthened by such investments. Concurrently, the exports share of the GDP of Sri Lanka was decreased gradually.

Managing the National Debt

We inherited the challenge of high debt with deficits in our current account balance and the government budget. Years of low government revenue paired with rigid expenditure flows led to financing the budget deficit from domestic and foreign borrowings.

In 2015, 90.6% of the Government total revenue was spent for debt servicing. This amounted to 80% in 2016.

It is an urgent need to draw our attention on spending more than the revenue. We have initiated a process of fiscal consolidation based on revenue generation by passing the Inland Revenue Act, which is already yielding returns.

Public finances have been strengthened and revenue has increased as a percentage of GDP during the past two years. The ratio of revenue to GDP in 2016 increased to 14.2% from 11.4% in 2014. For the first six months of 2017, revenue to GDP now stands at 6.7% of GDP from 6% in the corresponding period in 2016. It is expected to reduce the current debt which is 79.3% of the GDP to 70% of GDP by 2020. We expect to maintain the budget deficit below 3.5% by then. We will strengthen the Fiscal Management Responsibility Act affirming our commitment towards fiscal consolidation.

In the midst of all these, we have many other challenges in 2018 and 2019 in terms of public debt management and fiscal consolidation.

The domestic debt portfolio mainly consists of Treasury Bonds. Around 30% of the Treasury Bonds will mature by 2019. Similarly, Sri Lanka Development Bonds, which is a USD denominated domestic debt instrument, worth of over USD 2.3 billion will mature by 2018. In addition, the composition of the foreign debt portfolio was also changed considerably. This change was occurred mainly due to the increase of mobilizing commercial loans such as the issuance of International Sovereign Bonds. We have to pay USD 1.5 billion in 2019 for maturities of International Sovereign Bonds. Further we have to pay annually thereafter.

When considering the public debt service payments based on the outstanding debt as at end of August 2017, we have to pay Rs. 1,974 billion in 2018. We will have to pay Rs. 1,515 billion in 2019. It means we have to pay more than 3,489 billion in 2018 and 2019 for debt servicing.

In order to overcome these unprecedented challenges, the government has initiated a prudent debt management strategy. Our traditional approaches to debt management will have to change to cope with new risks and structural and regulatory changes.

Our policies will be targeted on forward-looking liability management strategies. Accordingly, the funds required by the government will be raised with transparency and predictability. Under the medium – term debt management strategy, the detailed strategies of government borrowings will be known in advance to the domestic and foreign debt portfolios. In addition, we will introduce a comprehensive secondary market trading platform and a liability management fund. These reforms and future reforms will come into

effect under the new Fiscal Liability Management Act that provides legal framework for a prudent debt management strategy.

The changes we have made by introducing the new Inland Revenue Act have been commended by the international community as well as domestic economic actors.

With the reforms such as the new Inland Revenue Act, Foreign Exchange Act, Fiscal Liability Management Act, Corporate Intents of the State Owned Enterprises and close monetary-fiscal coordination, we will steer this country towards robust and judicious management of our financial resources and fiscal framework.

Maintaining Low Inflation

Our government is taking a two-pronged approach to address the price stability.

We expect to provide the opportunity of buying the food items at a lower price throughout the year in order to control the short-term price fluctuations resulting in hardships to the people. We will improve the domestic supply chains and distribution networks to do so. In the meantime, we will allow importing of food products and other essential commodities at reasonable costs within the competitive market framework. We have reduced taxes on food commodities substantially over the past three months. We urge domestic wholesalers and retailers to pass the benefit of these reductions to the consumers.

However, the government will provide the space to the Central Bank to carry out its monetary policy independently to maintain price stability on a sustainable basis. The Central Bank is moving towards a new monetary policy framework targeting a flexible inflation. The aim of this framework is to maintain a low inflation continuously while supporting the economic activities. With this change of policy, our people will get the opportunity to live comfortably with the security of stable prices.

Development under Vision 2025

As we emphasised in the Vision 2025 document launched in September, we want to transform Sri Lanka into the hub of the Indian Ocean, safeguarded by a knowledge-based, highly competitive, social market economy. Our ambition is to make Sri Lanka a prosperous country by 2025.

For this vision to become a reality, our activities should join hands with the external world. Sri Lanka is a small island right in the middle of a large world. For thousands of years we have benefitted from being located strategically. Unfortunately, we seem to have forgotten this competitive advantage of the location. Our vision is to reclaim that mantle of

international connectivity. In here, we have to leave behind the decades of inward-looking policies that shrouded our capacity to grow.

For this vision to become a reality, we must encourage the entrepreneurs to diversify our exports. From that, our export basket will be improved with diversity. For decades, we have relied on the same exports products such as garments, rubber, and tea. These have been the giants of our exports economy. But now, we should diversify our exports by adding value added goods and services.

And also, we should integrate into the producer – driven value chains. If we enable our domestic businesses especially small and medium enterprises to create linkages with the international value chains, we will be able to see immense leaps in productivity and profits.

Further, we must provide the opportunity for the private sector to drive growth and investments. We have relied on the public sector for too long ignoring the private sector. We have scared away private investments with unclear policies and complicated procedures for too long. The effort of our government is to create an economy firmly based on foreign and domestic private investment, driven by a dynamic and forward - looking private sector.

A 3-Year Economic Delivery Programme

To kick-start this transformation, we will implement a comprehensive economic strategy over the next three years.

We intend to raise per capita income to USD 5000 per year.

We hope to create one million new jobs.

Our target is to increase foreign direct investment to USD 5 billion per year.

We plan to double the exports to USD 20 billion per year.

Enriched and Empowered People

The goal of these development strategies is improving the lives of the average Sri Lankans. Thus we will strive for two basic economic outcomes:

Increasing and improving jobs.

Raising incomes and expanding the middle class.

For this, our crucial need is to enhance education and skill development to enable all citizens to contribute to a knowledge-based economy.

Unemployment rate among the youth, those who have passed GCE A/L, and females, estimated at 18.5%, 39.9% and 6.5%, respectively. This illustrates the current structural deficiencies in the domestic labour market and the issue of skills mismatch.

Recognizing these shortcomings, the government will be initiating a number of basic educational reforms. We will guarantee 13 – years of education for everyone. After the GCE Ordinary Level examination, students will be directed to higher education, vocational education, jobs and training.

Furthermore, Information and Communication Technology, which is a need of the hour will be included in the school curriculum and the intake to universities in such disciplines will be increased. This also aligns with government's broader objectives and effort towards a digitally empowered economy. This approach will provide the opportunity for the youth to engage in better jobs while getting their skills developed.

The Government will encourage the private sector to develop the skills of the market by investing on skills development and joining hands with the public – private sector initiatives. Recent estimates show that 23% of the population will be elderly by 2042. With the rapid increase of the aged population, skill development programs will also target older workers. And also, action will be taken to tackle the drop in productivity due to outdated skills.

The government is planning to formulate policies to have a balance between the needs of foreign employment and domestic labour market. As the first step, labour shortages in the market will be filled. Foreign employment will be promoted only when the earnings are high and, only when the earning opportunities are available for skilled workers.

With better working conditions such as improved public transport and flexible working conditions, there is a chance that Sri Lankans living abroad will actively contribute to the country's growth process. We can expect their engagement for the development of our country and overall improvement in working conditions.

Currently, 60% of the employed population is engaged in informal and illegal economic activities. 40% of the employed population is engaged in vulnerable categories of jobs. We will take steps to uplift the standards of all jobs and to secure the social recognition and safety by providing internationally accepted certifications and licenses. This will result in minimizing the informal nature of the jobs. A contributory pension scheme will be introduced for those who are employed in the informal sector. This will result in minimizing the likelihood of poverty after retirement.

Trade and Tariff Reforms for the Growth of Export Targets

We were a trading nation since the era of ancient kings. Sri Lanka was the hub for transferring goods and knowledge from East to West, and West to East. We should learn from the history on exports and private sector growth which are key elements for becoming a higher middle-income economy.

People living in developed and developing East Asian and South East Asian countries such as China and Thailand have better jobs and higher living standards than the average Sri Lankans. I remember travelling to villages in these countries in 1979. They did not have many comforts or western foods enjoyed by Sri Lankans by then.

But today, the situation is different. How Sri Lanka lost its pace of development while other countries were progressing? This is a question that we should ask from ourselves. They embraced open economic policies focused on exports. Meanwhile, we looked inwards and adopted closed policies. Therefore we missed 30 years of valuable opportunities.

As I said before, Sri Lanka's exports are still based on traditional plantation crops together with apparels and tourism. We still compete for apparel with lower income economies resulting in pressure to keep our wages low. Still our biggest foreign exchange earner is foreign employment sector. Yet all these foreign exchange earnings are insufficient to meet our import bills. This lack of export growth contributes to the pressure on the balance of payments. This results in the depreciation of rupee and affects the prices of goods.

On the other hand, other middle-income countries such as Thailand and Vietnam are exporting a more diversified range of high-value products such as automobile parts, machinery and electronics. They are leaving us behind. We will have to catch up to our competitors. We have to change all these things if we are to strengthen the economy and to create more jobs.

We have obtained good results from the steps we have taken to stabilise the economy. Therefore, we should now focus on adopting an export-led economical growth strategies and policies by providing high-value and diversified products and services.

A key part of this policy will be entering into Free Trade Agreements with partner countries around the world. We are making great progress towards mutually beneficial Free Trade Agreements with Singapore, China, and India. These deals will give our economy a massive boost by opening huge new markets to our entrepreneurs.

We must ensure that both local manufacturers and export manufacturers are competitive through this export-led strategy. Businesses may have to restructure focusing on which

aspects make them competitive. Only then Sri Lanka will become a highly competitive economy.

To ensure a smooth transition for these companies, the government will be formulating a trade adjustment package. We have already taken steps in that regard, enacting the Inland Revenue Act and the Foreign Exchange Act, and moving forward with the Anti-Dumping Bill. We are also formulating a new National Export Strategy and a new National Trade Policy. The government is also establishing a National Single Window for Trade facilitation, and creating a new development bank for development financing with an export-import window.

Strengthening our Capacity for Growth

For our export-led economic strategy to be a success, we must target and obtain much more Foreign Direct Investment and Local Private Direct Investment in high-value products. Foreign Direct Investments have been the engine of growth for East Asia and South East Asia, and Sri Lanka can certainly attract similar or higher levels of investments.

For this, it is essential that we improve the investment climate. We should push Sri Lanka to top positions in relevant global indicators.

We will simplify the hurdles that investors currently face in dealing with the large number of government agencies. The reform agenda and an organizational setup focusing on implementation and continuous review of progress are already in place.

We launched the eight-fold action plan on Investment Climate Reforms in July 2017. It was developed following in-depth key stakeholder consultations to understand the obstacles faced by business owners and investors. This engaging and transparent approach is the key to success of the reforms. We will contribute to raising Sri Lanka's Ease of Doing Business ranking from 110 in 2017 to 70 by 2020.

Additionally, the steps are being taken to establish a Single Window for new business registration that brings more than 20 Government agencies together.

Comprehensive Industrial Strategies

Moreover, we will implement a comprehensive industrialization strategy that connects manufacturing with other sectors. Since economic liberalization in 1978, our progress in human development aspects have been on par with advanced economies. Yet our industries have declined.

The contribution of industrial activities and the manufacturing sector to economic growth has remained stagnant during the last two decades. Industrial activities contributed 27.6% of GDP in 2000 and only 29.7% in 2016. Inability to remain competitive, lack of value addition and lack of sophisticated technology are the main reasons for this situation.

We will revitalise the manufacturing sector by introducing a clearly defined industrialisation strategy.

Promotion of Tourism

In 2016, we have attracted more than 2 million international visitors generating an estimated revenue of USD 3.5 billion. The industry provided 320,000 local jobs in 2015. In the coming years, we will strengthen the tourism sector so that we can work towards our goal of attracting five million tourists to Sri Lanka every year.

Massive resort hotels dominated our tourism sector in the past. But current research shows that 90% of Sri Lanka's hotels have less than 10 rooms. This is an Airbnb economy. This is an economy where every individual with a spare room has the capacity to earn cash. We will streamline the informal sector and ensure the quality and standards.

Tourists are not just coming to Sri Lanka for the standard hotel holiday. Therefore, the government will take steps to develop tourist attractions. Sri Lanka will be made a destination where tourists should come for unique experiences. Travellers have focussed on a number of sectors such as our culture, cuisine, traditions, wildlife, Ayurveda and meditation.

The contribution of all stakeholders in the public and private sectors is required to boost the tourist attraction. 4-year tourism development strategy which we prepared consulting all relevant stakeholders will provide the base to achieve the tourism vision 2025.

China and India are our biggest and most rapidly expanding markets. We must shift our tourism strategies accordingly. We have to expand our connections with the countries from which the well-spending tourists are coming. We have to liberalise access to sea and air services. Therefore action will be taken to develop air access domestically and internationally, while facilitating cruise services and the establishment of yacht marinas.

Improving Opportunities for Housing

With all our focus on growth, we have certainly not forgotten the fundamental needs of our people. Our goal is to provide shelter for all in 2025.

The government is drafting a new national housing policy built on three key features. First, the policy is a people centric policy. People will engage in decision-making, actions, and responsibilities. Secondly, we are going to pursue integrated and inclusive urban housing development. Thirdly, we will ensure that housing development is sustainable.

We have allocated Rs. 75 billion to the National Savings Bank to provide housing loans at concessionary rates, and we have allocated Rs. 75 billion for the urban regeneration programme and other housing programmes.

The Government will not act as the sole owner. The Government will act as a delegated authority. The government will play the central role in setting the framework for housing development, but a lesser role in providing investment. We will enable the people and private sector to take control of investing on housing.

Market-driven Public-Private Partnerships (PPP)

We recognise the need for sustainable investments in socio-economic infrastructure such as education, health, electricity, roads and highways. It will contribute to Sri Lanka's rapid transition into a middle-income country. Our aim is to utilize PPP to gap these investment opportunities.

Accordingly, the government will formulate a clear PPP policy with a well-defined legal, regulatory and institutional framework to attract private players with the requisite capacities. Potential areas for expanding PPP include healthcare, leisure, tourism, education, ports and aviation, transportation, highways, information and communication technology, and energy. We will prioritize expanding opportunities for alternate financing to support PPP programmes.

Strengthening Public – Private Partnerships in the Agriculture sector

We hope to harness the power and energy of PPPs to improve efficiency and productivity of agriculture. The agriculture sector is saddled with major issues such as low productivity, lack of diversification, inefficiency in water management, and poor management of weather disruptions. Weaknesses in the sector contribute to food insecurity and regional poverty.

We will revitalise this sector through investments in agricultural research, extension services, water resources, and infrastructure facilities. We will facilitate the shift from traditional low value to modern high value agriculture. We will encourage scientific farming, promote agro-based industries and initiate commercial agriculture with the participation of farmer organisations and the private sector.

We will encourage the small and medium scale agri-businesses to invest in commercial agriculture and value chains through the agriculture modernization project. Further, we hope to see the modernization in the plantation sector.

The government will also promote information and technology enabled agricultural extension services to farmers by encouraging mobile phone-based services. This will turn the farmers who are depending on the on subsidies into agri-businessmen.

Supporting SMEs through Swashakthi

Another key feature of our support for the small businessman is the Swashakthi loan scheme. The government launched Swashakthi with the intention of supporting small and medium scale entrepreneurs to start self-employment projects and industries to strengthen the village economy. We have seen high demand for this scheme. That means we have deep wells of entrepreneurial capacity just waiting to be tapped. We will extend this scheme further to support the entrepreneurial skills and ideas of the youth.

We are in the process of launching several new schemes to support technology based SMEs. In order to improve the efficiency of government loan schemes and refinance schemes, we will also continue efforts to consolidate such schemes. We urge financial institutions to keep intermediation costs low, so that the whole country can benefit from reasonable interest rates on loans.

Empowering Women

We aim to create an environment where all citizens have the opportunity to achieve higher incomes and better standards of living. Therefore one of our main priorities is creating safe working conditions for women.

Women participation in the labour market remains low in Sri Lanka compared with majority of advanced and emerging market economies and the region. The present Women Labour Force Participation Rate is less than half of that of males, lingering around 30%-35% since 1990s. This participation is not enough to sustain the high growth momentum of the economy.

We should improve the public transport systems enabling women to travel comfortably to their workplaces. We are introducing the Light Rail Transit (LRT) with this purpose. This will greatly ease the current passenger congestion and provide a convenient and a safe mode of transport.

Furthermore, the National Child Day Care Centre Guidelines as already approved by the Cabinet will assist in creating more affordable and transparent childcare centres across the island. People will have the opportunity of obtaining their services at a reasonable rate.

Archaic labour laws which restrict females from effectively participating in the labour force, contribute to lower participation and lower productivity levels. Therefore, the government is committed to introduce new legislation. The present situation in the private sector on maternity benefits and access to tertiary and vocational education facilities will be improved.

We will encourage and strengthen the Small and Medium Enterprises. Women can play a major role in these enterprises.

Building a Stronger Economy

A number of projects which accelerate our journey towards a stronger economy are being implemented. We are building a well-planned expressway system from Hambanthota to Kandy. We have obtained funds for that. We started a joint venture in Hambanthota Port this year. Discussions are being held to start a joint venture in Mattala Airport as well. We have started working on Hambanthota economic zone. Millaniya Trade Zone has been planned already. Wayamba Industrial Zone has also been planned. The constructions of those zones will commence next year.

The construction of the first stage of the port city which will be developed as a Financial City is nearing completion. We will develop the Kandy City by joining hands with the Japanese government. India and Japan are extending their assistance to construct LNG plants. Tourism Zones in the Southern have been planned. Acquisition of lands is taking place now. We will start working on tourism zones in Iranavila and the Eastern Province soon.

The Budget 2018 which will accelerate these programmes will be presented in Parliament next month. The Budget will provide the opportunity to extend the development which was limited to the Western Province, to all over including Southern, North-Western and Central Provinces.

Those who can develop with skills and effort will be encouraged by the Budget. Others will also be supported.

This is a very challenging journey towards prosperity. This is a plan to enrich the country by 2025. This is an effort to make Sri Lanka again, the economy and trade hub of the Indian Ocean. I urge all of you to join hands with me in this challenging journey towards prospering our motherland.