during the turbulent nineties. I must emphasize that it is hazardous to pass judgement on things that happened in the recent past. Moreover, I shall be making my observations as a person who has been very closely involved with the policy evolution and events during the last two and half decades, and it will not be easy to be dispassionate and objective. It is good to be back among friends at the ICRIER who know Sri Lanka very well. I think you should use your extensive knowledge to sift through what I say and make an independent judgement.

PART I
Background

Like other countries of South Asia, and many others outside, Sri Lanka went through an eventful and tumultuous period in the nineties. Its experience, however, was unique in many respects. For the most part of its long history, Sri Lanka has had a free and open trade and economic regime that was the obvious choice for a small country with a limited domestic market or hinterland. Its dependence on international trade was overwhelming. For about two decades after the mid 1950s, Sri Lanka experimented with a dirigistic and inward-looking regime, when it imitated parallel Indian policies, oblivious to the fact that policies relevant for a large economy with a huge domestic market such as India's had little relevance. It was also influenced by the then fashionable policies of protectionism, import substitution and national self-reliance. When these isolationist policies brought the economy to a virtual halt, in 1977, Sri Lanka overwhelmingly voted for liberalisation and opening of the economy to winds of free trade. In this action, Sri Lanka was years ahead of other emerging nations. As a result, economic growth doubled, average incomes rose to the highest levels in South Asia, and unemployment was reduced dramatically. Meanwhile, it continued its longstanding commitments to investing in human resources and promoting gender equality. The quality of life as measured by indices of literacy, poverty and longevity placed it among the ranks of more affluent nations. Also, it managed to preserve its vibrant democratic traditions and institutions, although a preoccupation with a multiplicity of elections and an unique electoral system appears to have led to economic policy slippages.

There were two aspects, which have continued to haunt Sri Lanka during the last half century after regaining independence. The first was a commitment to welfarism, where the State assumed increasing responsibility for the welfare of the poor, which inevitably led to huge budget deficits in all years but one. As the former Premier Lee Kwan Yew of Singapore

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[1] I am greatly indebted to extensive research assistance and helpful comments by Dr Ranee Jayamaha, Assistant to the Governor at the Central Bank. The views expressed are my own and they do not reflect the official point of view.

Many countries followed Sri Lanka with the open economic policies in the wake of global liberalisation of the mid eighties. Faced with problems after the early start, Sri Lanka commenced a policy of rationalizing its welfare commitments with a view to living within its means, but the task has proved to be difficult. At about the same time, a conflagration of the conflict has imposed severe burdens on society. Fortunately, the resilience of the liberalised private sector led economy has kept Sri Lanka afloat.

It is convenient to demarcate Sri Lanka's post 1977 economic reforms into three periods. The first was an initial phase from 1977 to 1987 when after an initial spurt in liberalizing trade by eliminating controls and progressively reducing import tariffs (including abolition of export taxation), the economy was opened for foreign investment through a concessionary tax regime. A substantial investment in infrastructure was launched with concessional foreign finance. The second phase, which commenced in 1988, witnessed an intensification of the planned privatization programmes, and a rapid dismantling of industrial controls along with a further reduction in import tariffs. Nearly 43 privatizations took place while competition was introduced to government monopolies such as insurance. The next phase commencing in 1994 strongly accelerated the privatization programme, with the large enterprises in the infrastructure field being thrown open for private participation. Chief among them were the telecommunications, electricity, ports and airline industries. Also, privatized were the management of the nationalized plantation sector. The further rationalization of import tariffs and income taxation and introduction of value added taxation led to strong shifts from direct to indirect taxation. The protected financial and insurance sectors were opened for foreign investment and the public transport system was rationalized. This period showed a qualitative expansion of economic reforms.

In that sense, the nineties can be deemed to be the testing period for the expanding free market economy of Sri Lanka. The fact that it managed to insulate itself reasonably well from the Asian economic crisis after 1997 was a reflection of the resilience of the private sector led economy. The recent slowdown of the economy from the middle of 2000 reflected a serious global recession as well as a drought of unprecedented proportions, compounded by intensified terrorist activity culminating in a devastating attack on the international airport.

PART II
REAL SECTOR

Investment and Growth

The new wave of liberalisation in the 1990s laid the foundation to attract new foreign investments, reform the financial markets and the privatization of public enterprises facilitated primarily through capital inflows to the fledging share market. Investment as a ratio of GDP rose from 22% in 1990 to 28% by 2000. Sri Lanka's investment/GDP ratio compared well with India (26% in 1990/91 and 23% in 1999/2000) but not so well with South Korea (37% in 1995) and Malaysia (41% in 1995).

On average, the Sri Lankan economy recorded a growth of 5% during the latter part of the 1990s, which was commendable given the world recession that affected most developing countries and the Asian currency crisis, which led to loss of investor confidence in the region as a whole. The most significant factor that kept the growth momentum during the 1990s was the commitment to a liberal trade and investment regime. The growth achieved in the 1990s was largely investment-related, where foreign investment accounted for a larger share.

Following the high growth rates during the nineties, the GNP per capita in 2000 was at US$841, one of the highest in the South Asia region. As shown in **Table 1** much of this increase was achieved in the latter part of the nineties – where the GNP per capita rose from US$ 469 in 1990 to US$ 710 in 1995 and to US$ 841 in 2000.

Meanwhile, Sri Lanka's Human Development Index (HDI) in the 1965 was only lower in the Asian region to that of Japan and Singapore. With faster economic growth, Malaysia, South Korea and Thailand exceeded Sri Lanka's HDI by 1994, although Sri Lanka was able to maintain its position ahead of China, Indonesia and the Philippines.

Table 1: Comparison of GDP Growth and per Capita GNP (US$)

Year	Sri Lanka		India		Pakistan		Bangladesh		Nepal		Bhutan	
	GDP	per capita GNP	GDP	per capita GNP	GDP	per capita GNP	GDP	per capita GNP	GDP	per capita GNP	GDP	per ca GNP
1990	6.2	469	5.4	361	4.6	366	6.6	294	4.5	198	6.6	
1995	5.5	710	4.2	364	5.1	456	4.9	260	3.5	210	7.4	
1996	3.8	747	8.1	407	5.0	474	4.6	336	5.3	214	6.0	
1997	6.4	804	4.8	435	1.2	464	5.4	342	5.0	230	7.3	
1998	4.7	826	6.6	433	1.2	449	5.2	348	3.0	213	5.5	
1999	4.3	813	6.4	455	3.7	441	4.9	361	4.4	231	5.9	
2000	6.0	841	5.2	n.a	4.4	432	5.9	362	5.8	244	6.1	

Sources: Key Indicators of Developing Asian and Pacific Countries-2001,
ADB Economic & Social Statistics of Sri Lanka, Central Bank of Sri Lanka – various issues

management. The agricultural sector's share in GDP which stood at 38% of GDP in 1950, declined steadily to 26% in 1990, to 23% in 1995 and further to 19.4% by 2000. In terms of its contribution too, the agricultural sector recorded erratic fluctuations during this period. In 1995, industry (manufacturing and construction) overtook the agricultural sector, indicating a significant structural change in the economy.

The uneven performance of the agriculture sector is attributed to persistence of government direction and regulation, which stultified farmer incentives, while the rest of the economy, was being liberalised.

Table 2: Growth Trends and Sectoral Contribution during 1990-2000

GDP Percentage Change (1990-2001)

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000
1. Agriculture	**8.5**	**1.9**	**(1.6)**	**4.9**	**3.3**	**3.3**	**(4.6)**	**3.0**	**2.5**	**4.5**	
2. Mining and Quarrying	**9.1**	**(10.0)**	**(6.0)**	**11.9**	**6.0**	**3.4**	**8.9**	**3.8**	**(5.4)**	**4.1**	
3. Industry	**7.5**	**5.8**	**8.6**	**9.4**	**8.3**	**8.1**	**5.8**	**8.0**	**6.6**	**4.5**	
Manufacturing	9.5	6.8	8.8	10.5	9.1	9.2	6.6	9.1	6.3	4.4	
Construction	2.9	3.1	8.1	6.5	6.0	4.9	3.4	5.4	7.1	4.8	
4. Infrastructure	**4.4**	**7.7**	**6.7**	**4.9**	**3.8**	**6.0**	**6.4**	**8.7**	**8.0**	**8.3**	
Electricity, Water and Gas	10.2	7.1	5.4	12.0	9.9	10.2	(2.0)	8.2	10.1	9.5	
Transport, Storage and Communication	3.8	7.8	6.9	4.1	3.1	5.5	7.5	8.8	7.7	8.1	
5. Services	**4.3**	**5.7**	**4.9**	**6.8**	**5.7**	**4.7**	**5.6**	**6.6**	**4.4**	**2.9**	
6. GDP	**6.2**	**4.6**	**4.3**	**6.9**	**5.6**	**5.5**	**3.8**	**6.3**	**4.7**	**4.3**	

(a) Provisional

Sectoral Share of GDP (1990 - 2001)

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000
1. Agriculture	**26.3**	**26.8**	**25.9**	**24.6**	**23.8**	**23.0**	**22.5**	**21.9**	**21.2**	**20.7**	**1**
2. Mining and Quarrying	**2.5**	**2.1**	**1.7**	**1.9**	**2.0**	**1.9**	**2.0**	**2.0**	**1.9**	**1.8**	
3. Industry	**22.3**	**22.0**	**22.7**	**22.4**	**22.7**	**23.1**	**23.1**	**23.4**	**24.1**	**24.0**	**2**
Manufacturing	14.9	14.7	15.3	15.2	15.4	15.7	16.2	16.4	16.5	16.4	1
Construction	7.4	7.3	7.4	7.2	7.3	7.4	6.9	7.0	7.6	7.6	
4. Infrastructure	**11.1**	**11.2**	**11.2**	**11.4**	**11.5**	**11.4**	**11.9**	**12.2**	**12.6**	**12.9**	**1**
Electricity, Water and Gas	1.3	1.4	1.2	1.3	1.5	1.5	1.3	1.4	1.5	1.5	
Transport, Storage and Communication	9.9	9.8	10.0	10.1	10.1	9.9	10.6	10.7	11.1	11.4	1
5. Services	**37.8**	**37.9**	**38.5**	**39.7**	**40.0**	**40.6**	**40.5**	**40.5**	**40.2**	**40.6**	**4**
6. GDP	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**10**

(a) Provisional

Sectoral Contribution to GDP Growth (1990 - 2001)

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000
1. Agriculture	**31.2**	**9.4**	**(8.3)**	**15.0**	**12.3**	**12.3**	**(24.6)**	**10.6**	**11.5**	**22.1**	
2. Mining and Quarrying	**4.3**	**(6.6)**	**(3.6)**	**4.0**	**2.6**	**1.5**	**5.7**	**1.2**	**(2.2)**	**1.7**	
3. Industry	**29.1**	**30.1**	**49.1**	**34.5**	**38.1**	**39.3**	**41.8**	**29.2**	**32.5**	**25.1**	**3**
Manufacturing	25.8	25.5	36.5	28.1	30.8	33.1	35.6	23.3	22.2	17.3	2
Construction	3.3	4.6	12.7	6.5	7.4	6.2	6.2	6.0	10.3	7.8	
4. Infrastructure	**9.1**	**20.9**	**20.2**	**9.3**	**8.8**	**14.0**	**21.6**	**16.5**	**20.5**	**24.0**	**1**
Electricity, Water and Gas	2.1	2.0	1.7	2.3	2.5	2.7	(0.8)	1.7	2.9	3.1	
Transport, Storage and Communication	7.0	18.9	18.5	7.0	6.3	11.3	22.4	14.8	17.6	20.9	1
5. Services	**26.3**	**46.2**	**42.6**	**37.2**	**38.2**	**32.9**	**55.5**	**42.5**	**37.7**	**27.1**	**4**
6. GDP	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**10**

(a) Provisional

fruit and fish products entering international markets. The growing contribution of the manufacturing sector in 1990s was largely due to the textile, wearing apparel and leather products, which together accounted for 72% of industrial output. Essentially, this was the result of the country exploiting apparel quotas of buying countries in the US and Europe.

The diversification of exports from primary agricultural products, (tea, rubber and coconut) that were subject to considerable price volatility to relatively broad based industrial exports was a notable development. Manufactured exports, which accounted for only 0.5% of total exports in 1948 and 1.2% in 1971, accounted for 73% and 78% of total exports in 1996 and 2000 respectively, of which textiles and garments accounted for 63% and 70% of industrial exports respectively (Table 3). Taking all factors together, it could be said that the industrial sector was at its best during the nineties. However, the world recession that set in during the latter part of the nineties has reduced demand for garments and textiles from the US and Europe and combined with the worldwide excess capacity, has resulted in lower prices for these products.

Table 3: Industry and Manufacturing Exports Growth And Share of Manufacturing Exports

Year	Manufacturing Growth	Manufacturing Exports	Mfg. Exports as a % of Total Exports
1990	14.0	31.1	52
1991	9.5	18.3	62
1992	12.3	43.8	72
1993	13.4	19.2	73
1994	8.6	14.1	75
1995	9.9	19.6	75
1996	7.3	4.7	73
1997	10.2	14.3	74
1998	7.5	5.0	75
1999	4.5	-1.6	77
2000	11.0	20.6	78

Source: Central Bank of Sri Lanka

Services Sector

The Port of Colombo improved significantly throughout the 1980s and indicated a record growth during the 1990s and emerged as a hub port in the region. The inauguration of the new oil terminal and the new container yard in 1999 increased the volume of business of the port and facilitated port services during the nineties**.** The completion of new container terminals in 1995, enabled the Port to handle 1.4 million containers (a 12-fold increase by 1996 compared with 1982).

The nineties also witnessed major changes in the telecommunication sector. In 1991, the Dept. of Telecommunications handed over the operational functions to Sri Lanka Telecom – a public corporation - which was reconstituted in 1996 as a government-owned limited liability company. In 1993, Sri Lanka introduced the first digital earth station in Colombo together with packet-switched data services. In 1994, Sri Lanka linked to SEA-ME-WE-II Analogue Optical Fibre Submarine cable. In 1997, 35% of the share capital of Sri Lanka Telecom was sold to the Japanese communication giant, NTT, for US$225 million, marking a landmark in the telecommunication services in Sri Lanka. At the same time, four private service operations in wireless, telephone and mobile telephones were permitted to operate. The television transmission services continued to progress with active competition between two state channels and five private operators.

Despite strong economic growth in countries which are major sources of tourists to Sri Lanka, frequent and more flights to Colombo and promotion campaigns carried out by the Government and the private sector**,** tourism suffered many setbacks due to escalation of the conflict. The tourism receipts rose from US$ 120 million in 1990 to US$ 228 million in 1994, but the sector suffered major setbacks due to incidents of terrorism in the latter part of the nineties. Reflecting the impact of lower tourist arrivals, gross earnings from tourism declined from US$ 267 million in 1999 to US$ 238 million in 2000 **(Appendix Table 2).**

Sri Lanka's financial services continued to grow throughout the nineties through improved banking services and broad basing of financial assets and investments. Towards the end of the decade, 26 banks operated in Colombo (two State-owned banks, eight domestic private banks and sixteen foreign banks). Many of the banking and financial institutions introduced credit card services, electronic fund transfers and telephone banking services to their customers. To facilitate low value, but high volume transactions among banks, the Sri Lanka Inter Bank Payment System (SLIPS) was introduced in 1993. The system is now being expanded allowing the public to pay utility bills, insurance premia, etc., through the system. Sri Lanka implemented the Society for World Wide Inter Bank Financial

1990	401
1991	443
1992	548
1993	627
1994	690
1995	727
1996	832
1997	921
1998	999
1999	1,056
2000	1,160

Source: Central Bank of Sri Lanka

All in all, Sri Lanka's growth performances in the nineties clearly reflected the benefits of early liberalization and the slow but steady policy reforms introduced throughout the period. Initially, an incredulous public brought up on state regulations and welfare funded to doubt the wisdom of the reforms, but once the benefits of economic freedom began to materialize, they became ardent supporters of change.

Social Welfare

Primarily attributed to the spread of free and universal education since the 1940s, a clear demographic transition by way of low population growth was seen during 1990-2000. In the first half of the 1990s, population growth averaged only 1.5% per year while in the second half, the growth declined to 1.3% per year. Improvements in health resulting from free medical care since the 1940s has raised the prospect of an ageing population, posing new challenges to social security. Considering the growing number of pensioners of the public services, and the related high costs projected for the next decade, the expenditure on non-contributory pension schemes requires new thinking in order to protect the future stream of income of pensioners and address attendant fiscal problems.

Another notable feature of the post-liberalisation era was the sharp growth of Sri Lankans seeking overseas employment, driven by the growth in demand for labour in oil producing countries and poverty at home. Their savings remitted home became a major source of support for the balance of payments. Very soon, their remittances exceeded the annual earnings from traditional sources of earnings such as tea, rubber and coconut. As shown in **Table 4** gross foreign remittances by expatriate workers nearly trebled between 1990 and 2000.

the "decade of exports" with a target of doubling the per capita income of the Nation. I must say that successive governments that came into power since 1977 placed lot of trust and confidence on the Central Bank which enabled the Bank not only to maintain monetary and price stability with greater freedom, but also to be in the driving seat in coordinating other policy reforms. Although this was a tall order for the Central Bank, it was able to steer many of the generic reforms and those specific to the financial sector. Its economic policy advice to the Government has played an important role in shaping the overall economic policy of the country.

The liberalization of exchange controls was indeed another important factor. With the removal of the remaining current account restrictions, Sri Lanka accepted obligations under Article 8 of the Articles of Agreements of the IMF in March 1994. This was a major stride in the liberalization process, which enabled Sri Lanka to remove controls in the capital account selectively. To attract foreign investments to the capital market, waivers were provided to foreign investments in the capital market and also for repatriation of profits. Tariff structures were further rationalized by reducing maximum tariff, the number of tariff rate bands to two and reducing ad hoc exemptions. The new industrial policy that was introduced at the beginning of the nineties helped to boost the industrial sector's growth. The nineties also saw a coordinated policy package compared to the previous decades although in many years the fiscal magnitudes couldn't be maintained at desirable levels.

Let me now proceed with some of the key policy reforms.

decade. The exchange rate adjustment in 1989, corrective adjustments made to the prices of wheat flour and bread, increases in the fertilizer prices, the consequent upward revision of the guaranteed procurement price of paddy and the increases in fuel prices due to the Gulf crisis contributed towards the upsurge in inflation during that year. This called for a considerable tightening of monetary policy, which continued throughout the decade. The rate of increase in prices eased somewhat although inflation continued to remain at double-digit levels in some years. Strong capital inflows during the early years led to attempts at sterilization, which caused interest rates to rise to unprecedented levels. The capital flows moderated with the onset of an election with administered prices of wheat flour, bread and kerosene declining during 1994-1995, inflation dropped to a single digit level (8.4% in 1994 and 7.7% in 1995) as measured by all available indices. The double-digit inflation re-emerged in 1996 (the CCPI rose to 15.9% and the GCPI rose to 14.6%) due to drought conditions, which affected domestic food production, higher international commodity prices and reduction in the subsidy of wheat flour and higher energy costs. In 1997, the annual average inflation declined to 9.6% and further to 6.2% in 2000.

Table 5: Sri Lanka's Inflation during 1990-2000

(annual average in %)

Year	CCPI(1952=100)	GCCP	WPI (1974=100)	GDP	CDCPI
		(Ja-Ju 1989=100)		Deflator	
1990	21.5	24.6	22.2	20.0	
1991	12.2	11.5	9.2	11.0	
1992	11.4	9.4	8.8	10.0	
1993	11.7	8.4	7.6	9.5	
1994	8.4	4.7	5.0	9.3	
1995	7.7	3.9	8.8	8.4	
1996	15.9	14.6	20.5	12.1	
1997	9.6	7.1	6.9	8.6	7.4
1998	9.4	6.9	6.1	8.4	7.3
1999	4.7	3.8	-0.3	4.4	3.6
2000	6.2	3.2	1.7	6.7	3.6

Source: Central Bank of Sri Lanka

Taking the decade as a whole, it could be said that Sri Lanka has experienced a double-digit (12%) inflation with annual averages varying between 5-21%. To a large extent, this high inflation has been caused by domestic factors, primarily the persistent fiscal deficits. In several instances during the 1990s, monetary policy has been made ineffective due to monetisation of the budget deficit. This in turn has led to depreciation of the Rupee.

bank market developments and the reserve money target, and determine the desirable amount and range of intervention for rupee liquidity. Repo and reverse repo rates have been used as the main policy interest rates during this period.

Appendix Table 3 indicates the trends in money and credit aggregates during 1990-2000. Following the encouragement given to the private sector-driven growth process, credit to private sector increased throughout the 1990-2000 period thus increasing the broad money supply growth to 19.2% by 1995. By tightening the monetary stance, the money growth was brought down to 13% by the end of 2000.

As in other areas, the monetary policy management also faced a number of challenges during the latter part of the 1990s. Partly due to fiscal imbalances**,** a prolonged liquidity shortage emerged during 1999 and 2000. The Central Bank continued to provide temporary liquidity through its reverse repo window, although this was a standing facility used at the discretion of commercial banks. **Table 6** indicates the main changes in the interest rates during this decade.

Table 6: Interest Rate (Percentage)

End Period(a)	Bank Rate	Repo Rate (overnight)	Reverse Repo Rate (overnight)	Call-Money Rate
1990	15.00			14.00-19.00
1991	17.00			12.00-18.00
1992	17.00			18.00-32.00
1993	17.00	16.50		16.50-18.50
1994	17.00	20.00		20.00--23.00
1995	17.00	16.50		20.00-58.00
1996	17.00	12.75		17.50-28.00
1997	17.00	11.00		12.00-20.00
1998	17.00	11.25	15.00	13.00-14.00
1999	16.00	9.25	13.48	10.00-13.25
2000	25.00	17.00	20.00	22.50-32.00
2001	18.00	12.00	14.00	12.50-13.00

(a) End year figures

Source: Central Bank of Sri Lanka

Since 2000, the reverse repo rate has become the most important tool in providing liquidity and stabilizing the upper end of inter bank call market rates. Although statutory hedged inflation-targeting framework, which is expected to be adopted soon. More importantly, reserve money targeting has changed the focus of monetary policy away from the external balance (under a fixed exchange rate regime) to the internal balance. These targeting regimes presuppose domestic price stability as the prime objective of monetary policy. A Monetary Policy Committee (MPC) has been appointed to monitor closely the movements of the reserve money target and make monetary policy recommendations, which will be made public in a transparent manner.

(b) Exchange Rate Policy

(i) Liberalisation of Exchange Controls

The nineties witnessed a strong relaxation of exchange controls and the adoption of a market-oriented exchange rate policy, both of which have contributed significantly to attract foreign investment and maintain an average growth of 5% during the nineties. Permission was granted in 1990 to approved country funds, regional funds and non-resident individuals to invest in shares in listed companies up to 40% of the issued share capital and this was increased up to 100% in 1992. The 100% transfer tax on share purchases by foreigners was abolished at the same time. A Share Investment External Rupee Account (SIERA) was introduced to facilitate and monitor such investments. In 1991 Sri Lankan residents were permitted to open Resident Foreign Currency accounts (RFC) in commercial banks. The repatriation and surrender requirements in respect of export proceeds were abolished in 1993. Export proceeds were permitted to be retained in foreign currency accounts either in Sri Lanka or abroad.

The remaining restrictions in respect of travel, overseas educational expenses and miscellaneous remittances were removed and Sri Lanka accepted obligations under Article VIII of the IMF in March, 1994. This was a landmark in the history of Sri Lanka's exchange controls and it set the pace for progressive capital account liberalization. In 1995, commercial banks were permitted to obtain foreign loans up to 5% of their capital and reserves. This was relaxed to 15% in 1997 with the introduction of foreign currency loans to non-BOI exporters. Permission was also granted to private firms on a case-by-case basis to undertake investments abroad since 1996. Taking the liberalization measures further, commercial banks were permitted to provide foreign currency loans to non-BOI exporters from either their domestic units or from their Foreign Currency Banking Units (FCBUs) subject to some safeguards.

selling rates of the US$ at the beginning of each day. The margin between the buying and selling rates was gradually increased from 1% in 1992, to 2% in 1995. This allowed Sri Lanka's exchange rate to be determined by market forces to a large extent with some intervention to avoid sharp fluctuations.

The continuous depreciation of the Sri Lanka rupee as dictated by market forces, probably prevented the Sri Lankan economy being hurt by the East Asian crisis during 1997-1999. The small but continuous adjustments that took place in the exchange rate throughout the 1990s made it possible to insulate the economy from the widespread contagion that engulfed other countries which maintained a fixed relationship to the US dollar, such as Thailand and Indonesia. However, the world recession and its impact on trade-dependent economies, coupled with severe terrorist attacks and internal political instability resulted in the Sri Lankan economy coming closer to a foreign exchange crisis in late 1999 when its reserves dropped very low. The increased balance of payments deficit largely due to high oil prices and security related additional imports resulted in a gradual reduction in the official reserves. Sri Lanka's trading partners, who suffered the impact of the Asian crisis had depreciated their currencies and had gained a competitive advantage. This made the maintenance of the crawling band exchange rate regime difficult and the Rupee came under pressure in the last quarter of 1999 and during 2000. Domestic interest rates were raised and interventions were made in the foreign exchange market to defend the Rupee by allowing it to depreciate within a narrow band. This band was widened from 2 to 5% and again to 6.8% in 2000 and to 10% in January 2001. Although initially helping to stabilize the rate, the continuously widening band appeared to give a signal to the market for a continuous depreciation of the Rupee. Hence it was decided to give up the nominal policy anchor of the exchange rate management.

Thus, a fundamental change in exchange rate policy was announced on January 23, 2001 by moving out of the managed float of the exchange rate to an independently floating arrangement. Certain precautionary measures such as limiting bank's exposure to foreign currencies (open positions), penalties on delayed receipt of foreign earnings were taken to prevent an overshooting. The Central Bank stopped announcing rates at which it will buy or sell foreign currency. The anticipated overshooting in the market was short-lived because the rate was not seriously out of alignment. Immediately, it went up to Rs. 98 to the US dollar, but soon stabilized at around Rs 88.90 per dollar within a week. The Central Bank now participates actively in the foreign exchange market through buying and selling at 'near' market rates. At present, the intervention by the Bank is limited to instances where it is each day, sets a Reference Exchange Rate Range (RERR) and the mid point of the RERR, which is based on calculations for the real effective exchange rate, adjusted for current market developments. The Committee looks into the changes in the REER vis-à-vis the five major currencies (US$, Stg. Pd., the Yen, the D-Mark and the Ind. Re.) and 24 currencies of which many of them are Sri Lanka's trading partners. **Table 7** indicates the movements in the REER during the nineties. While being effective in stabilizing the foreign exchange market, some of the prudential measures announced together with the floatation had limited the growth of the foreign exchange market. Many of these prudential measures (limits on banks' daily net foreign exchange exposures, settlement of export credit by exporters promptly within 90 days, the limitation on banks' forward transactions with their customers, a 50% rupee deposit requirement to back banks' forward sale of foreign exchange, the prohibition of pre-payment of import bills) have been removed or reduced during 2001 with a view to enabling the market to grow in line with fundamentals.

Table 7: Nominal Effective Exchange Rate (NEER) and Reference Effective Exchange Rate (REER)

1995 = 100

	NEER	REER
1990 Dec	120.8	98.3
1991 Dec	119.0	100.2
1992 Dec	116.3	107.2
1993 Dec	107.9	105.4
1994 Dec	105.0	102.0
1995 Dec	96.2	101.0
1996 Dec	94.0	111.3
1997 Dec	99.0	126.1
1998 Dec	87.4	111.6
1999 Dec	84.0	110.4
2000 Dec	78.4	111.8
2001 Dec	71.5	111.5

Source: Central Bank of Sri Lanka

Table 8: Defence Expenditure

As a % of GDP

	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995
Total Defence Expenditure	1.4	1.2	1.1	1.4	2.1	3.6	3.4	4.6	3.6	3.1	4.1	4.0	4.2	4.2	4.6	6.5
Defence	0.7	0.6	0.5	0.8	1.3	2.8	2.4	3.1	2.1	1.6	2.1	2.8	3.0	3.1	3.4	5.4
Public Order and Safety	0.7	0.6	0.6	0.6	0.8	0.8	1.0	1.5	1.4	1.5	2.1	1.2	1.2	1.1	1.2	1.1

As a % of Deficit 1/

	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995
Total Defence Expenditure	5.9	7.5	6.4	10.6	23.9	30.8	28.0	41.3	22.8	27.7	41.9	33.8	53.1	48.0	43.5	64.2
Defence	3.0	3.6	3.1	6.0	14.6	24.3	19.8	27.6	13.6	14.5	21.1	23.3	37.8	35.6	32.0	53.4
Public Order and Safety	2.9	3.8	3.3	4.6	9.2	6.5	8.2	13.7	9.2	13.3	20.7	10.5	15.3	12.4	11.6	10.8

Memo;

	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995
Budget defici as % of GDP	23.1	15.6	17.4	13.4	9.0	11.7	12.2	11.1	15.7	11.2	9.9	11.9	8.0	8.7	10.5	10.2

1/ Deficit before grants and privatisation

Towards the end of the decade, defence expenditure pre-empted about 47% of government deficit compared to only 3% prior to 1980. High defence expenditure of around 5-6% of GDP, which constitutes 25% of recurrent expenditure, was clearly not sustainable. The budgetary outturn in 1995 reflected some progress towards fiscal consolidation. This could not be sustained in 1996 and 2000.

The high fiscal deficits were also a result of low level of government revenue of around 17% of GDP and a high recurrent expenditure of around 20% resulting in continuous current account deficits. The lower level of revenue is attributable to lower profit taxes from public enterprises, a slow growth in excise taxes and a decline in customs duties. The recurrent expenditure continues to remain high, mainly due to the escalation of security related expenditure, the high cost of interest payments on public debt and the high cost of the public service. Public investment remained at a low 6.5% of GDP. Reflecting the high budget deficit, public debt has increased to 97% of GDP by 2000. This situation was further aggravated by escalating losses in certain public enterprises such as the Ceylon Petroleum Corporation and the Ceylon Electricity Board, which resorted to large extrabudgetary financing from the banks, which was largely due to delayed price adjustments and internal inefficiencies. **Table 9** indicates the overall and primary deficits of Government during the 1990s.

Table 9: Fiscal Deficit, Primary Deficit and Revenue Deficit of Government 1990-2000
(As a percentage of GDP)

	Overall	Primary	Current A/C
1990	-9.9	-3.5	-1.2
1991	-11.9	-5.9	-2.0
1992	-8.0	-1.9	-0.9
1993	-8.7	-2.6	-0.8
1994	-10.5	-3.9	-2.9
1995	-10.1	-4.3	-2.7
1996	-9.4	-3.1	-3.8
1997	-7.9	-1.7	-2.2
1998	-9.2	-3.8	-2.4
1999	-7.5	-1.9	-1.0
2000	-9.9	-4.2	-3.4
2001	-10.5	-3.8	-4.0

Source: Central Bank of Sri Lanka

The National Budget also provides a considerable volume of funds to over two hundred public institutions and statutory agencies, many of which have outlived their usefulness. Seriously overstaffed and oblivious to norms of prudent management, most of these enterprises could have been wound up without an adverse effect on the economy. But they had become important sources of political patronage, thus deriving protection from governments. In the nineties, several of redundant public enterprises were in a protracted process of liquidation and several potentially viable ones were privatized. The slow progress in this area partly reflected the complications of process of divestment and partly reflected the lack of focus on essential public sector reforms.

Finally, the high and rising expenditure on interest payments on public debt has been a major concern in fiscal policy management. The debt service payments pre-empted a fourth of government revenue during this period. The problems of high public debt are consequences of persistently high fiscal deficits, declining government revenue and rising cost of borrowings. The present level of debt servicing also raised several fundamental problems. To mention a few, government debt is a charge on the National Budget and needs to be serviced through Government revenue or additional borrowings and external debt servicing has been a claim on the balance of payments. Fortunately, the foreign debt service is low at about 14% of foreign earnings, owing to resorting to highly concessional and longer-term borrowing. Whilst interest payments on public debt have risen from 3% of GDP in 1980 to 6% at the end of 2000, the revenue/GDP ratio has declined from 20% to 17%, reducing the ability of the Government to service such debt without curtailing much needed public investment. **Appendix Table 4** indicates the rising public debt levels and the debt servicing issues.

The lack of fiscal discipline impacted not only on the implementation of the monetary policy but also on all other policy areas. Large domestic borrowings by the Government crowded out resources from the private sector, led to high interest rates and discouraged investment, with adverse impact on the economy through inadequate infrastructure facilities, inadequate development of skills and human resources and poor delivery services. What is needed is a strong economic growth of about 7-8% combined with a rising level of government revenue and foreign exchange earnings. It would not only reduce the present level of debt burden but also provide leeway for future borrowings.

in the 1949 Monetary Law Act which set up the Central Bank.

The functions of the Central Bank, which have evolved over the last five decades, have varied depending on the priorities identified in different periods. At the beginning of nineties, while pursuing price and exchange rate stability, the Bank devoted considerable resources in promoting lending to sectors with high social priority and to promote economic growth. But by the end of the decade, the Bank has realized the futility of following multiple objectives and has decided to concentrate on the core central banking functions of achieving price stability and financial system stability. During the nineties, where monetary policy tools were made increasingly market-oriented, a sound financial system was necessary for the propagation of policy and improving the monetary transmission mechanism. That would not mean that the Bank would completely disengage itself from the ultimate goal of promoting all-round development. Hence, it will continue to play a promotional role in regional development through its regional offices and the Regional Development Banks where it owns a significant share. Having identified the weakness of agricultural markets as an obstacle to agricultural development, it is also engaged in promoting forward and futures markets through private sector partnerships.

To achieve the two main objectives, the Central Bank has effected several changes during year 2001. I consider it worth mentioning some of the important ones to illustrate the point that the Central Bank is actively pursuing the proposed policy reform agenda. While achieving its main objectives, the Central Bank also wishes to become the main policy "think tank" of the country resourced by highly skilled staff. This required reducing the size of the Bank and recruiting new staff with specific skills. The Bank offered a voluntary retirement scheme to its officers while retaining the skilled and trained officers with the Bank. This reduced the number of officers from 1901 to 1200. To keep up with the modern day requirements, the Banking Department is now reconstituted as four new departments, namely, the International Operations Dept., the Domestic Operations Dept. the Payments & Settlements Dept. and the Finance Dept. The Bank has embarked on a payments reform program within which a real time gross settlement system and a scripless securities settlement system are expected to replace the current deferred net settlement system and the scrip trading system respectively, by mid next year. To raise the financial reporting framework to international standards, the Central Bank prepared its year 2001 accounts on International Accounting Standards with greater disclosures and mark to market valuation methods.

government debt held in the Central Bank portfolio during the 1980s, conscious attempts were made to establish a primary dealer system, which was expected to promote markets for government debt securities. The primary dealer system, which was set up in 1992, (only with commercial banks) was reformed in 1994 by expanding the dealership to non-bank institutions with dedicated capital. In addition, the Central Bank started issuing Treasury bonds of 2-6 year maturity in 1997 and this was further expanded in 1998 to provide a medium term benchmark interest rate and a risk-free yield curve beyond one year. Similarly, the Bank made Treasury bonds eligible for transactions at the secondary window of the Central Bank as in the case of Treasury bills, and permitted the use of Treasury bonds (repos) and outright buying and outright selling at its secondary window from 1998 onwards. Although the benchmark yield curve has been on a gradual increase during 1997 to 1998, due to increased fiscal deficits and borrowing requirements of the Government, Sri Lanka has not yet achieved a benchmark yield curve as a reference to other market yields. It is also making arrangements to hand back the public debt management function, which it had undertaken thus far as an agent of the treasury. This would enable the monetary policy functions to be more independent and also to enable the Government to build up portfolio management capabilities. Similarly, the Bank plans to return the financial management of the national social security system – the Employees Provident Fund – to the government.

(ii) Other Institutional Reforms

Throughout the nineties the Bank took the lead in financial sector reforms. It has provided assistance and guidance in development and sophistication of financial services. They include the payments through credit and debit cards, telephone banking, Internet banking and private banking for some customers. Even under difficult conditions in the nineties, the reform program continued although the progress was slow. It has been a pioneer in establishing the Credit Information Bureau and the only Credit Rating Agency in the country. The Bank has assisted human resource development in the financial institutions by organizing training and has taken a lead role in the analysis and dissemination of economic information. From its inception, the Bank has been the main provider of essential economic data and information in the country. Beginning 1999, the Central Bank has commenced compiling a financial survey on an experimental basis. The survey covers not only licensed commercial banks but also licensed specialized banks and finance companies. **Table 10** below shows selected indicators of financial depth in Sri Lanka since independence.

Year	Narrow Money (M_1) as a % of GDP	Broad Money (M_2) as a % of GDP	Financial Sector Contribution to GDP(%)	Total Financial Sector Assets as a % of GDP
1950	20.6	22.1	0.9	39.1
1960	15.7	20.5	0.7	37.0
1970	14.0	22.1	1.1	61.6
1980	13.4	28.2	3.0	96.2
1990	12.3	28.1	4.6	111.2
2000[a]	9.4	32.0	7.6	129.0

[a]Provisional
Source: Central Bank of Sri Lanka

The Central Bank was instrumental in amending several statutes of the financial sector institutions with a view to improving their efficiency and soundness. Important amendments were introduced to the Banking Act of 1988 providing more powers to the Central Bank to regulate and supervise financial institutions more effectively. Laws were made to improve the government debt securities markets and to scripless trading of government securities, to create more market-oriented treasury bonds and to increase the efficiency of the secondary market in government securities. During the nineties, a system of dedicated primary dealers was established to promote the debt securities market. It pioneered the establishment of the National Savings Bank and the National Development Bank. Well ahead of many other Asian countries, in 1994, Sri Lanka enacted laws to encourage financial institutions to adopt appropriate accounting and auditing standards, which are in line with international standards.

To reinforce the stability of commercial banks, the regulatory system has been improved with quarterly off-site monitoring and regular monthly meetings with all banks together. The risk weighted capital adequacy ratio, which has been set at 8% (Basle Guidelines 1) since 1989 was raised to 9% and is expected to increase to 10% by 2003. Approval has been granted to domestic banks to issue debentures and augment the capital base of domestic banks.

In sum, the Central Bank keeps abreast of global developments and innovations and has endeavoured to adopt them in the country, with a view to creating a prudent and efficient financial centre in Sri Lanka.

tariffs was reduced and the 3 bands that prevailed at that time were reduced to 2 bands (10 & 25%) in 2000. The tariff reforms during the nineties clearly reflected three main policy considerations; i.e., to: (i) prevent the inflow of cheap imports to the country; (ii) provide appropriate safeguards for the protection of the domestic industries; and (iii) provide incentives to local producers and exporters through the reduction of export tariffs, in particular the non-traditional exports. Effective 1999, zero tariff bands were applied on imports of transport, communication, medical equipment and computers, which led to the enhanced use of computers and other communication systems towards the end of the decade.

(e) Privatisation Policy

Foreign participation in the share market

The Government began to divest its ownership in state enterprises reconciling its role to that of a facilitator. The privatization programme, which began with the privatization of United Motors – a government-owned business undertaking – brought in US$2.5 million at the start. A newly designed incentive package consisting of simplified and unified procedures for investment approval, tax holidays, concessionary duty rates and exemption from existing exchange control regulations were extended to foreign investors, in particular to those who transacted in the share market in 1991. By end 1992, majority shares in 18 state enterprises had been divested and the privatization proceeds amounted to US$30 million and this increased to US$40 million from the privatization of 12 more State enterprises in 1993. A list of privatized institutions/entities is given in **Appendix Table 5.** In order to proceed with the privatization in a more systematic manner, the Public Enterprise Reform Commission was set up in 1995.

The newly elected Government in 1994 made a clear commitment to pursue the process of economic liberalization and to strengthen the market-friendly economic environment and promote the privatization programme. In 1992, a programme of restructuring the plantation sector was introduced under which the management of state plantations was given to 23 regional plantation companies (RPC) to be managed by private companies on a profit-sharing basis for a 5-year contract period. However, the managing companies did not have an incentive to invest and make improvements in view of the short 5-year contract, the management contracts were extended to 50 years and privatized during 1995-1997. Resources were mobilized from the Asian Development Bank and the Overseas Economic Cooperation Fund of Japan to improve their productivity.

Government successfully launched a floating rate note in the international capital market to raise US$50 million, which in fact was an acid test of the perception of the country's economic viability. These resources were used to retire public debt.

The conflict also led to macroeconomic instability in that the budget deficit during the 1990s continued to remain around 9-10% of GDP. The defence expenditure, which was 1.1% of GDP in 1982, escalated to 5.0% by 1996 with a marginal slow down to 4.5% by 2000. This undoubtedly manifested in two digit level inflation, and high interest rates which continued throughout the 1990s. The Government continued to borrow not only from the banking sector but also from the non-banking sector recording negative savings throughout the nineties. As shown in **Table 11** below, the war and the resulting political instability were reflected in low domestic savings. Despite the generation of low domestic savings, the marginal propensity to consume by Sri Lankans remained at high levels. The growth momentum picked up by the early 1990s recorded an investment/GDP ratio of 27% in 1994, but this was moderated during 1995 to 1997 by the war-related defence expenditure. Clearly, the conflict has been serious drag on the economy.

Table 11: Savings and Investment as a percentage of GDP

Year	Domestic Savings as a % of GDP	National Savings as a % of GDP	Government Savings as a % of GDP	Foreign Savings as a % of GDP	Investment as a % of GDP
1990	14.3	16.8	-1.2	7.9	22.2
1991	12.8	15.2	-2.0	10.1	22.9
1992	15.0	17.9	-0.9	9.3	24.3
1993	16.0	20.2	-0.8	9.6	25.6
1994	15.2	19.1	-2.9	11.8	27.0
1995	15.3	19.5	-2.7	10.4	25.7
1996	15.3	19.0	-3.8	8.9	24.2
1997	17.3	21.5	-2.2	7.1	24.4
1998	19.1	23.4	-2.4	6.0	25.1
1999	19.5	23.5	-1.0	7.8	27.3
2000	17.3	21.4	-3.4	10.7	28.0
2001	15.5	19.9	-3.8	6.8	22.3

Source: Central Bank of Sri Lanka

(a) Non- Diversification of energy sources

complacency that has set in the electricity monopoly has contributed to the continuing power deficit.

In the decade of the 1980s when big investments like the Mahaweli Project was progressing, core infrastructure investment amounted to 4.1% of GDP, but this declined to 3.4% in the 1990s. In contrast Malaysia, Thailand, Philippines and Indonesia maintained 6-8% of GDP on infrastructure investment in the 1990s. From about 1993, major infrastructure projects were considered under BOO/BOT arrangements for private sector investments because of fiscal constraints, but the progress has been slow due to a weak regulatory framework, lack of efficient procurement procedures and the uncertain investment climate.

(b) The absence of appropriate regulatory structure for utilities

In addition to the inability to cater to the growing demand for infrastructure facilities such as electricity, telephones, gas, water, etc., Sri Lanka has also failed to put in place appropriate structures to regulate the pricing and investment policies of infrastructure development and utility services. A misconception that only the Government is capable of providing these services has created negative attitudes to private sector involvement. Without rules of operation laid down by regulators, investment is discouraged. Sri Lanka has regulators for the telecommunications and the insurance industries. Others for gas, water, electricity, and transport are absent.

(c) Legislative and regulatory environment

Sri Lanka has also failed to keep up with changing legislative and regulatory enforcement. The Companies Law and the Bankruptcy Law have not been updated and smooth exit strategies by businesses are not possible in a reasonable period of time. Although Sri Lanka passed special debt recovery laws in mid 1980s, the actual debt recovery under these laws has not been very significant. Although there has been a tendency for prompt repayment when noticed of impending prosecution and seizure, banks continue to be stuck in courts in prolonged debt recovery processes.

(d) Good Governance and best practices

practices are adopted. Thus, there is now a greater awareness and commitment to adopt internationally accepted best practices for good governance and accountability.

(e) Competitiveness

As a highly trade-dependent small economy, strengthening Sri Lanka's competitiveness is crucial to achieving high and sustainable economic growth in an increasingly globalised economic environment. Although Sri Lanka has made considerable progress in opening the economy to external trade, liberalizing foreign exchange payments and simplifying trade procedures to encourage foreign investment, further measures to enhance the overall efficiency are needed. By concentrating on the comparative advantage of cheap labour and natural resources, most Sri Lankan industries have become price takers in today's competitive world. Sri Lanka was ranked 44 out of 60 countries in the Global Competitiveness Report (trial survey) conducted by the World Economic Forum (WEF) in 2000. In the same survey conducted in 2001, Sri Lanka ranked 57 out of 75 countries. The key to building a competitive industrial base is innovation and sustainable increases in productivity through continuous upgrade in technology. This can only be achieved, especially in developing countries like ours, through bringing together the critical mass in the private sector to muster the required resources and support. Although Sri Lanka was an early starter in computerization, it has been very slow in rising to meet the Internet challenge. As in the case of India, Bangladesh, Bhutan and Nepal, a comprehensive IT and E-commerce policy is yet to be announced in Sri Lanka. To explore the full potential of e-commerce, we need to establish backward linkages with financial, legal and telecommunication infrastructure.

Recognizing the importance of improving competitiveness of key industries, the Government, has encouraged the formation of a National Competitiveness Council. The Council will work closely with the private sector, analyzing competitiveness constraints, assessing needed reforms, making recommendations to senior policy makers and facilitate the monitoring of policy implementation.

Cooperative Wholesale Establishment - the institutions which experience problems in sorting out their outstanding debt to the banking sector. These big state-owned entities continue to be dependent on the two state banks for meeting their large import bills. Very large bills of these enterprises create volatility in the exchange market. The foreign currency exposures of banks to these enterprises can cause volatility in the small forex market. Hence, the Central bank is now engaged in improving the capabilities of large public enterprises and the state banks in managing their foreign currency risks more efficiently.

It is also important to strengthen and activate the functioning of the inter bank market as well. The market capabilities of a core set of dealers would need to be developed to improve inter bank liquidity and resiliency. Repo transactions among banks need to be developed to facilitate short-term liquidity requests of banks. This would be essential in the light of payments reforms envisaged by the Bank in the near future.

Concluding Remarks

In summary, the growth path that shaped Sri Lanka's economic performance during the nineties has been very rough indeed. The ripple effects of the war were reflected directly in the fiscal numbers with widespread effects on all other activities. The overall fiscal policy was characterized by high deficits and excessive borrowing, contributing towards ballooning government debt. On average, in the 90s, the budget deficits were in the order of 10% of GDP. In other words, the Government had been spending for its day-to-day operations beyond its revenue capacity.

As I explained earlier, having committed to the continuation of market-friendly policies and taking strong policy actions to correct several structural weaknesses and fiscal imbalances, it is also necessary to emphasize the development of infrastructure, public enterprise reform and revive the encouragement of the private sector. The completion of the reform agenda is the main policy thrust of the new Government. The new development plans aim at transforming Sri Lanka into a modern equitable, globally integrated and internationally competitive economy with 7-8% annual growth. Sri Lanka should also look at the revitalization of the rural economy not through subsidies but through technological transformation in agriculture, development of rural infrastructure and generation of income earning opportunities for the poor by creating efficient markets, while targetting affordable income transfers to the really needy.

AppendixTable:1

KEY ECONOMIC INDICATORS

OUTPUT										
GDP at current market prices (Rs. billion)	322	667.8	768	890	1018	1106	1256	758	509	1008
GNP at current market prices (Rs. billion)	319	659.1	757	880	1002					993
Per capita GDP at market prices (US$)	473	713	759	814	839					
Per capita GNP at market prices (US$)	469	709	748	804	823					
REAL OUTPUT (percentage change)										
GNP	6.2	5.9	3.2	6.8	4.6					
GDP	6.4	5.5	3.8	6.3	4.7					
Agriculture, forestry and fishing	8.8	-3.3	-4.6	3.0	2.5					
Mining and quarrying	9.1	3.4	8.9	3.8	-5.4					
Manufacturing	9.4	9.2	6.5	9.1	6.3					
Construction	2	4.9	3.4	5.4	7.1					
Services	4.3	5.1	5.8	7.1	5.2					
AGGREGATE DEMAND AND SAVINGS (per cent of GDP)										
Consumption	85.3	84.7	84.6	82.7	81.1					
Investment	22.2	25.7	24.2	24.4	25.1					
Net import of goods & non factor services	-10	-10.4	-8.9	-7.1	-6.5					
Domestic savings	14.3	15.3	15.3	17.3	19.1					
PRICES AND WAGES (percentage change)										
Colombo Consumers' Price Index (1952 = 100)	21.5	7.7	15.9	9.6	9.4					
Greater Colombo Consumers' Price Index (Jan.-Jun. 1989 = 100)	24.6	3.9	14.7	7.1	6.9					
Wholesale Price Index (1974 = 100)	22.2	8.8	20.5	6.9	6.1					
GNP deflator	20	8.4	12.3	8.7	8.4					
GOVERNMENT FINANCE (per cent of GDP)										
Revenue	21.1	20.4	19	18.5	17.2					
Expenditure and net lending	31	30.5	28.5	26.4	26.3					
Current	22.3	23.1	22.8	20.8	19.6					
Public investment	8.3	7.9	6	5.8	6.7					
Current account deficit/surplus	-1.2	-2.7	-3.8	-2.2	-2.4					
Overall deficit	-9.9	-10.1	-9.4	-7.9	-9.2					
Deficit financing	9.9	10.1	9.4	7.9	9.2					
Foreign	5.7	4.5	2.3	1.9	1.7					
Domestic	4.2	5.1	6.5	3.4	7					
Privatisation proceeds		0.4	0.6	2.5	0.4					
Government debt	96.5	95.2	93.3	85.8	90.8					
Foreign	54.9	51.9	46.8	42.3	45.3					
Domestic	41.6	43.3	46.4	43.5	45.5					

(a) Average of four Quarters
(b) Average of 1st,2nd, and 3rd Quarters1st quarter.

	1990	1995	1996	1997	1998	1999	2000	91-2000	91-1995	1996-2000
EXTERNAL TRADE (percentage change) (c)										
Terms of trade	-12.5	-1	-0.5	6.8	14.2	-5	-6.1	4.3		.9
Export unit value index (1997 = 100)	9.1	14.8	11.6	9.3	11.6	-8.5	1.5	5.7		.5
Import unit value index (1997 = 100)	24.7	15.6	12	2.4	-2.2	-3.5	8.1	6	6.9	3.4
Export volume	29.7	7.1	4.1	10.6	0.1	5	18.3	7.3	6.9	7.6
Import volume	7.6	2.7	-0.4	12.3	12.4	0.2	12.9	9.9	12.2	.6
EXTERNAL FINANCE (US$ million)										
Trade balance	-703	-1,505	-1344	-1,225	-1,092	-1,369	-1,798			
Exports	1984	3807	4095	4639	4798	4610.1	5522			
Imports	2686	5311	5439	5864	5889	5979.3	7320			
Services and income account (net)	-98	-18	-92.3	-1	-35	-107	-266			
Current private transfers (net)	362	675	710	788	848	887	974			
Current official transfers (net)	62	61	59.1	54.8	52	26	25			
Current account balance	-377	-786	-676.9	-393	-226	-563	-1.065			
Overall balance	119	52	-67.8	163	37	-263	-522			
Current account balance (per cent of GDP)	-4.7	-6	-4.9	-2.6	-1.4	-3.6	-6.4			
External assets (months of same year imports)	3.7	3.6	[illegible]	[illegible]	[illegible]	5.2	3.5			
Overall debt service ratio (per cent of X G & S)	17.8	13.8	15.3	13.3	[illegible]	15.2	14.7			
Total external debt and liabilities (per cent of GDP)	72.7(d)	75	68.6	62.3	61.6	63.5	59.8			
EXCHANGE RATES										
Annual average										
Rs/US$	40.06	51.25	55.27	58.99	64.59	70.39	75.78			
Rs/SDR	54.42	77.74	80.23	81.17	87.66	96.25	99.899			
End - year										
Rs/US$	42.58	54.05	[illegible]	61.29	67.78	72.12	[illegible]			
Rs/SDR	57.25	80.39	81.39	82.69	95.44	98.87	104.31			
MONETARY AGGREGATES(at market prices-percentage of GDP)(e)										
Narrow money (M1)	12.3	11.3	[illegible]	9.6	9.5	9.8	9.4			
Broad money (M2b)	28.1	34.2	33	32.4	31.1	32.4	32.2			
Net external assets of the banking system	1.1	10	8.1	10	9.2	7.6	4.7			
Net domestic assets	25.1	24.3	24.9	22.3	21.9	24.8	27.5			
Domestic credit from the banking system to										
Government (net)	11	5.3	[illegible]	[illegible]	[illegible]	7.8	10.7			
Public corporations	4.9	[illegible]	[illegible]	[illegible]	[illegible]	1.1	2.1			
Private sector	20.2	26.9	[illegible]	24.3	24	24.9	24.5			
Reserve money	9.8	11.8	11.1	9.4	9.1	9.1	8.4			
INTEREST RATES (per cent per annum at end year)										
Treasury bill rate										
3 month	17.41	19.26	17.45	9.97	12.01	11.79	17.77			
12 Month	18.36	18.97	17.38	10.21	12.59	12.77	18.22			
Repurchase rate (overnight)		17.8	[illegible]	[illegible]	11.25	9.25	17			
Rediscount rate (overnight) / Reverse repo rate		20	[illegible]	[illegible]	[illegible]	13.48	20			
Deposit rates										
Commercial banks' weighted average deposit	12.9	12.4	12.3	[illegible]	9.2	9.1	9.89			
Commercial banks' 12 month fixed deposit (max.)	21	15.5	17.8	15.25	13	12.5	15			
NSB savings	16.2	12	12	10.8	10.5	9.2	8.4			
NSB 12 month fixed deposit	18.5	16	15	11	11.5	11.5	15			
Lending rates										
Com. Banks' weighted average prime lending	18.5	20.1	20.2	15.2	14.9	15.9	21.46			
Bills purchased & discounted	14.5 - 30.	1.0 - 30.0	11.0-30.0	1.0 - 30.0	1.0 - 30.0	1.0 - 30.0	1.0 - 25.0	11.6-29.5	12.2-30.0	11.0-29.0
CAPITAL MARKET										
All Share Price Index (1985 = 100)	384	663.7	603	702.2	597	573	447.6	699.53	814.5	584.56
Sensitive Price Index (1985 = 100)	680	990.5	897.7	1068	923	938(f)	698.5	1042.21	1179.38	905.04
Value of shares traded (Rs. million)	1563	11249	7403	18315	18130	14294	10624	14238.3	14723.4	13753.2
Net purchase by non nationals (Rs.million)	391	-89.7	351.6	716	-1,517	-902	-3364	758.42	1303.32	213.52
Market capitalisation (Rs.billion)	[illegible]	[illegible]	[illegible]	[illegible]	117	[illegible]	[illegible]	[illegible]	[illegible]	110.48

(c) A new trade indices series has been introduced from 1998. description on change of the methodology. Data for 1990 have been obtained by splicing the previous annual trade indices series.
(d) Excluding commercial bank external liabilities.
(e) Monetary data for 1990 are based only on data of the domestic banking units, while data from 1996 - 2000 are based on the aggregated data pertaining to both domestic banking units and foreign currency banking units.
(f) The Milanka Price Index (MPI) was introduced in January 1999, (1998 December = 1000) to replace the Sensitive Price Index.

Tourist Arrivals, Employment and Accommodation Capacity in the Touris

Item	1990	1991	1992	1993	1994	1995	1996	199
1. Tourist Arrivals (No.)	**297,888**	**317,703**	**393,669**	**392,250**	**407,511**	**403,401**	**302,265**	**366,1**
1.1 Arrivals by Region								
Europe	176,856	194,413	256,485	257,883	261,045	254,730	171,888	2
North America	8,084	11,519	12,954	13,743	15,612	14,565	12,462	1
Asia	100,004	92,543	107,103	105,093	116,352	118,323	102,558	1
Australasia	8,914	12,247	12,759	11,610	12,033	10,254	8,763	1
Other Regions	4,030	2,981	4,368	3,921	2,469	5,529	6,594	
1.2 Arrivals by Purpose of Visit	297,888	317,703	393,669	392,250	407,511	403,101	302,265	3
Pleasure	277,722	295,781	373,198	387,151	377,537	383,570	286,924	3
Business	15,250	12,073	15,353	3,923	21,340	10,772	8,781	1
Other	4,916	9,849	5,118	1,177	8,634	8,759	6,560	
2.Excursionist Arrivals (No.)	3,954	2,665	5,651	6,093	8,413	10,556	12,863	1
3. Accommodation								
3.1 Number of Establishments	770	925	879	845	1,030	1,118	1,308	1,33
Hotels and Restaurants	274	328	363	356	467	525	639	641
Travel and Transport Agencies (c)	154	208	203	213	239	265	317	341
Recreational Agencies	9	10	10	12	14	14	13	13
Tourist Shops	333	379	303	241	266	269	300	302
Other		-	-	23	44	45	39	39
3.2 Capacity in Graded Establishments								
No. of Units	120	122	127	129	134	138	143	158
No. of Rooms	9,556	9,679	10,214	10,365	10,742	11,255	11,600	12,3
No. of Beds	18,669	18,947	19,907	20,242	20,929	21,197	22,040	22,9
Annual Occupancy Rate (%)	47.2	48.4	55.3	57.0	56.6	52.6	40.3	49.
3.3 Capacity in Supplementary Establishments								
No. of Units	96	109	128	140	169	169	223	227
No. of Rooms	1,080	1,191	1,305	1,562	2,045	2,045	2,509	263
No. of Beds	2,152	2,400	2,620	3,182	3,783	3,783	4,574	458
4. Employment (No.)								
4.1 Direct Employment	25,000	26,878	28,790	30,710	35,064	36,260	31,963	34,0
4.2 Estimated Indirect Employment	35,000	37,629	40,306	42,994	49,090	51,100	44,748	47,6
5. Gross Tourist Receipts (US$.Mn)	120.0	152.3	191.9	202.5	227.6	214.0	162.1	200.

Source : Ceylon Tourist Board

a) Revised;
b) Provisional;
c)Includes Airlines and the Ceylon Tourist Board.

Trends in Money and Credit 1990-2000

	1990	1991	1992	1993	1994	1995	1996	1997	1998
Broad Money Supply(a)	18.5	22.1	17.4	23.4	19.7	19.2	10.8	13.8	9.7
Net ForeignAssets	-27.7	258.5	70.8	129.8	34.0	3.2	-7.0	44.3	5.0
Net Domestic Assets	21.5	12.8	10.7	2.9	13.6	27.4	18.1	4.0	11.8
Domestic Credit	13.3	10.2	12.7	4.6	15.3	28.8	12.7	8.1	14.3
Claims on Government (net)	-2.1	0.1	-6.6	-18.4	6.1	23.8	36.9	-4.5	26.4
Claims on Public Corp.	12.8	-10.0	4.8	-47.3	-33.6	65.2	16.5	3.4	-15.5
Claims on Private Sector	24.1	20.5	22.9	20.5	20.8	28.4	7.8	11.5	13.1

(a) Point to point growth rates are given

Source: C

1994	70.8	13.7	
1995	66.7	16.5	5.5
1996	61.1	15.3	5.2
1997	54.3	13.3	5.1
1998	55.5	13.3	5
1999	57.8	15.2	4.8
2000	53.5	14.7	5.8

(a) As a percentage of earnings from merchandise exports and services
(b) Short-term debt as a percentage of total debt