Sri Lankan government to implement new economic austerity measures

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The United National Front (UNF) won the parliamentary elections in Sri Lanka last December by exploiting widespread resentment to the previous Peoples Alliance (PA) government over the country's protracted civil war and declining living standards. Having come to power, however, the UNF has made further inroads into jobs, conditions and public spending, while blaming the PA for the country's deepening economic problems.

Rural Economic Affairs Minister and Deputy Finance Minister Bandula Gunawardane regularly appears on television citing the indices of the grave economic crisis. According to him, the government's expenditure was double its income by the end of the PA's term of office. Just to service the annual debt, Sri Lanka needs $US3.27 billion, but its total annual income is just $US2.78 billion. Total government debt stands at $US14.51 billion. When asked what he proposed, Gunawardane declared that he was making "the public aware on the crisis"—a sure indication that the government is prepared to call on working people to make more sacrifices.

The recently released annual report of the Central Bank of Sri Lanka for the year 2002 provides a detailed picture of the country's economy which was hit by a 3.7 percent decline in the growth rate last year. Per capita GDP fell by 6.89 percent, from $US899 in 2000 to $US837 in 2001, indicating a drastic decline in living conditions for the majority of the population.

The report blamed the downturn in the global economy, particularly after the September 11 terrorist attacks in the US, Sri Lanka's prolonged drought and resultant power cuts, the attack by the Liberation Tigers of Tamil Eelam (LTTE) on the country's main international airport in July last year and the uncertainties created by the unstable political situation.

Last year, growth in the agriculture and manufacturing sectors, which are heavily dependent on exports, was significantly hampered by the economic slowdown in the major industrial countries. Sri Lanka's total exports fell by 12.8 percent during 2001. The major industrial sectors to decline were apparel and textile by 8.5 percent, ceramics by 11.9 percent and petroleum products 11.3 percent.

Sri Lankan exports, particularly garments and textiles, have been hit by the emergence of regional trading blocs in Europe (with Turkey and Eastern European countries), and North America (with trade preferences for Caribbean and Sub-Saharan African countries). Increased competition from China and other low-wage countries, and increased insurance premiums on flights and ships destined for Colombo have also been factors.

Industrial production costs have risen due to higher lending rates and increased prices for imported raw materials, fuel and electricity. Severe power shortages during 2001 affected the industrial sector with power cuts of up to eight hours during last September-October. The agricultural sector suffered from the country's drought. Tourism declined by 16 percent in 2001, due to the continuing civil war and the worldwide downturn following the September 11 attacks in the US.

Overall investment slumped badly. Foreign direct investment fell by a massive 38 percent last year from 89,622 million rupees ($US896 million) in 2000 to 55,285 million rupees in 2001. Domestic investment severely contracted from 64,537 million rupees in 2000 to 24,679 million rupees in 2001.

The UNF government had hoped for new pledges of international financial assistance from the Sri Lanka Development Forum, the country's major creditors, when it met in Colombo during the first week of June. However, instead of receiving any aid, it received a series of lectures on the need for tougher austerity measures. World Bank Vice President Mieko said, "the focus of the Forum will not be on aid levels" but on economic reforms. "The economic situation remains precarious and the tasks ahead all the more urgent," she said.

Speaking at the Development Forum, IMF representative Jeremy Carter effectively pushed for the speeding up of privatisation by calling for the government to end open-ended subsidies and transfers to public institutions. He also demanded a cut in the Samurdhi program—a limited form of welfare relief—insisting it should only be available for the most needy people. Sri Lanka's Finance Minister K.N. Choksy responded by stating that the cost of the program would be slashed from 15 to 10 billion rupees.

The IMF had a Stand-By Arrangement with the previous government to provide $US253 million within 14 months to shore up Sri Lanka's foreign reserves. The first $130 million tranche was released last year when the Sri Lanka rupee was freely floated. As a result the rupee depreciated by 11.3 percent against the US dollar during 2001.

However, the IMF suspended further disbursements, claiming the PA government had failed to implement agreed economic measures. The second tranche of $60 million was only released in April after the UNP government took a number of measures in the February budget, including cutbacks to pensions, privatisation, the introduction of a value-added tax (VAT) and the floating of fuel prices according to the international market rate.

The government's policies have already had a severe impact on living standards. Over the past six months prices have soared. The official cost of living index, considered to be a conservative estimate, has jumped by 304 points since December—from 2,899 on average for 2001 to 3,203.7 in May.

Electricity charges rose almost 35 percent from April 1. Postage rates increased 25 percent in April. The price of petrol, diesel and kerosene has gone up four times since February. Water prices will rise between 25 and 50 percent in July. Bus fares were to increase by 15 percent on average from July 1. The cost of most imported items, including medicines, has increased due to the rupee's decline. The price of telecommunications and cooking gas has risen considerably over the past few months.

Privatisation is being accelerated. Under the Ceylon Electricity Board's financial restructuring plan, power generation is being sold off to the private sector in addition to electricity distribution. Ceylon Petroleum Corporation is planning to split refining and distribution so as to sell its filling stations sometime this year. Some of these are being offered to the Indian Oil Corporation as part of a recent agreement signed in India.

Other public sector entities slated for privatisation include port facilities, which are already owned by a public corporation, the railways and postal department. The government announced the removal of all limits on inward foreign direct investment in sectors such as construction, finance and utilities, opening up virtually the entire economy to international investors.

In addition, a new 10 percent withholding tax on savings that earn interest of more than 144,000 rupees (about $US1,500) will impact severely on significant numbers of workers, particularly contract workers in the Middle East or elsewhere who return to Sri Lanka and rely on their savings, and retirees who depend on interest earned on their bank accounts.

The government has frozen public sector salaries and suspended recruitment to the public service, provincial public services, local authorities, public corporations, statutory boards and all government-owned companies. Government has already changed the pension system to force all new public sector employees to contribute 8 percent of their salaries.

In line with IMF demands, the UNF is preparing major changes to the country's labour laws, in particular in relation to dismissals. Under the present Termination of Employment Act an employer has to obtain permission from the Commissioner of Labour before closing down a factory or institution and is liable to pay compensation. The government is preparing to do away with such binding clauses.

However, the IMF and World Bank are still not satisfied. An IMF team visited Sri Lanka in June for a final review of the measures associated with the Stand-By Arrangement. Expressing its dissatisfaction with the government's progress, the IMF team declared in a press release: "Important decisions are yet to be taken on financial sector and public enterprise reforms."

As with every other IMF demand, the UNF, with the support of the opposition parties, will rapidly fall into line. Those who will bear the brunt will be the Sri Lankan working class in form of rising levels of unemployment, higher prices and deteriorating social services.