Sri Lankan government to unleash new austerity measures

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5 September 2013

Comments by a senior Sri Lankan government official to the *Sunday Times* last week are a signal that the government is preparing to intensify its assault on the living standards of working people.

Like other "emerging economies" in Asia, Sri Lanka is being hit by the continued slump in Europe, the US and Japan, compounded by the financial turmoil generated by the prospect of an end to cheap credit as the world's central banks wind back their quantitative easing policy.

The unnamed official warned: "The government, faced with a worsening budget deficit crisis, is to go in for deeper austerity measures and for the first time consider resorting to twin measures of cutting subsidies and increasing taxes to rein in rising costs."

The government's spokesperson specifically targeted social services, saying that "although it was difficult politically… measures will be taken to curtail the free welfare services." These measures come on top of one round of budget cuts after another by President Mahinda Rajapakse to meet the demands of the International Monetary Fund (IMF). Welfare programs and price subsidies have already been slashed, making life unbearable for the poor.

The official explained that the government was preparing these measures because its debt servicing cost has risen to exceed government revenue by 3 percent. If cuts were not made, he said, the government treasury would have to seek fresh loans, worsening its budget crisis.

Early this year, the IMF refused to consider a new loan program for the country and instructed the government to reduce the budget deficit by further cutting public spending. The government had already provoked resistance by working people by slashing subsidies for fuel, electricity and fertiliser.

Treasury Secretary P.B. Jayasundara declared in late July that a major component of the Rajapakse government's strategy was to reduce the budget deficit to 4 percent of gross domestic product (GDP) by generating a surplus of 2 percent of GDP in revenue.

Since then, the Sri Lankan economy has markedly deteriorated. During the first half of this year, exports declined by 4.5 percent and imports by 5.8 percent, compared to corresponding period last year. Even though the trade deficit improved by 7 percent compared to last year, mainly due to heavy falls in imports, including consumer goods, it still surpassed $4.5 billion.

The Sri Lankan rupee has depreciated by 7 percent so far this year—from 126 rupees to the US dollar in January to 136 rupees last week—increasing prices for all imported goods.

Central Bank governor Ajith Nivard Cabraal repeated the claim last week that the fall in the value of the rupee was just an "aberration." It is, however, in line with the falling value of currencies in other "emerging economies," such as India, Brazil and the South East Asian countries.

Fearing that the weak Indian rupee and Japanese yen could lead to higher vehicle imports, the Central Bank slapped a 100 percent margin deposit on opening a Letter of Credit to import cars and vans. The government also fears an outflow of capital from Sri Lanka to take advantage of the rising value of the US dollar.

The fall in the Sri Lankan rupee was triggered in early July as the US Federal Reserve hinted that it would taper off its quantitative easing policy, raising expectations of higher yields on US bonds.

This could also trigger a balance of payments crisis if speculative capital moves out of Sri Lanka and into US

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investments. The *Sunday Times* noted that a large portion of Sri Lanka's foreign reserves, about $3.5 billion, was in bonds purchased by foreign investors.

Unable to secure an IMF loan, the cash-strapped government is borrowing at high interest rates prices on global markets. The government's long-term loans during the first six months reached $918 million. Its foreign and domestic debt rose to 6.35 trillion rupees in first four months of this year, from six trillion rupees at the end of last year.

The international credit rating agency, Moody's, pointed out that the country's debt affordability—that is, debt to revenue ratio—was nearly 600 percent in 2012. "Sri Lanka's ratio is one of the highest amongst all emerging market countries that Moody's rates," the agency stated.

The international agencies recently issued warnings on the outlook for Sri Lanka's credit rating. Moody's changed its outlook from "positive" to "stable," foreshadowing a possible future downgrade. Standard and Poor's maintained its credit ratings for Sri Lankan debt, but commented: "We affirmed the ratings to reflect our view that Sri Lanka has weak external liquidity, moderately high and increasing external debt, and a weighty government debt and interest burden."

The government has already started to increase taxes as part of its austerity program. On August 23, onion and potato prices increased by 15 rupees, or nearly 20 percent, on the pretext that this would boost domestic production. Earlier, the government increased taxes on tobacco, cigarettes, liquor and ethyl alcohol.

In Sri Lanka, 80 percent of the country's tax revenue comes from working people, through regressive indirect taxes such as VAT, import duties and excise duties on food and other essential goods and services.

The tax hikes for working people are occurring as the government reduces the corporate tax rate to 28 percent and 12 percent for export industries. As well, generous tax holidays are offered to big business projects. For instance, the government has given a 10-year tax holiday and another 6 years at just 6 percent to a casino and gaming enterprise connected to an international tycoon.

There are fears in ruling circles that new austerity measures will provoke widespread opposition. Already, workers have been hit by a virtual wage freeze since 2006, imposed by the government with the assistance of the trade unions.

Expressing his concern, Treasury Secretary Jayasundera recently warned in a lecture, entitled "Government Strategy for the Industrial Development of Sri Lanka" and delivered to a big business audience, that the challenges following the end of the island's protracted civil war were wage hike demands and workers' unrest.

As it implements its austerity program, the government will use police-state methods to suppress any resistance by working people. Just last month, it unleashed an army operation on Weliweriya protesters who were demanding clean water, with soldiers cold-bloodedly killing three youth.

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