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Economic recovery not adequately broadbased - CB

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The Central Bank says that though economic activity turned around from negative to positive growth which was encouraging, the recovery was not adequately broad based.

The Central Bank in its 2002 review said that the Agriculture sector recovered significantly, but not completely, with the improvement in weather conditions. The growth in the Agriculture sector was 2.5 per cent in 2002, compared to a contraction of 3.4 per cent in the previous year. The industry sector continued to shrink during the first half of 2002, but regained some growth momentum during the latter half, recording a 1.0 per cent growth in 2002, due to both domestic and global factors, compared to a contraction of 2.1 per cent in 2001. The comparatively low performance in the Industry sector raises concerns, as this sector is crucial for the creation of employment opportunities and influences activities in the Services sector, as well as future economic growth. The Services sector, which contracted marginally by 0.5 per cent in the previous year, thrived in 2002, with a growth of 6.0 per cent, responding well to the increased demand for services such as trade, transport, communication, financial services and tourism, arising mainly from the improved security situation both locally and internationally. The overall recovery reported in 2002 was clearly centered on the performance in the Services sector which contributed 80 per cent of the GDP growth, claiming 53.6 per cent of total GDP in 2002, compared to 52.5 per cent in 2001. The demand for services arose mainly from domestic consumers. Suppliers who had excess capacity responded quickly to this increase in demand. In contrast, activities in the industry sector took a comparatively longer time to regain their growth momentum owing to the inherent nature of such activities. For example, generally, the recovery in export manufacturing and in the construction industry take relatively longer, as the decision making process and obtaining required material inputs take more time. Slower recovery in the Industry sector will hinder longer term growth prospects which are dependent on construction sector activity and manufacturing.

On the expenditure front, GDP at current market prices was estimated at Rs. 1,585 billion compared with Rs. 1,407 billion in 2001, recording an increase of 12.6 per cent in nominal terms. This increase was explained to a lesser extent by increases in real economic activity and, to a larger extent, by the increase in the general price level. The overall inflation as measured by the GDP deflator was 8.3 per cent, in comparison to 12.4 per cent recorded in 2001. The comparatively lower inflation was mainly induced by the increase in local production to meet demand and improved macro economic stability. Accordingly, GDP per capita for 2002 is estimated at Rs. 83,382, an increase of 11.0 per cent over the previous year's Rs. 75,133, which surpasses the combined increase in inflation and population growth, indicating an overall improvement in living standards, on average. In US dollar terms, per capita GDP increased by 3.7 per cent, from US dollars 841 to US dollars 872.

In 2002, Gross Domestic Product (GDP) grew by 4.0 per cent, recovering convincingly from the contraction of 1.5 per cent reported in 2001. The recovery was a gradual process. During the first half of the year, GDP grew by 1.7 per cent (0.5 per cent during the first quarter and 3.0 per cent during the second), reviving from the contraction of 3.9 per cent experienced in the latter half of the previous year. In the second half, the growth was 6.1 per cent (5.9 per cent in the third quarter and 6.2 per cent in the fourth quarter), partly due to the statistical effect of a low base in the previous year.

The growth in 2002, over a performance that plummeted in the previous year, was driven by several factors. The security situation, which improved with the uninterrupted continuation of the cease-fire that came into effect in late February, boosted consumer demand, as well as the shift to positive perceptions and attitudes, both domestically and internationally. The world economy that experienced difficulties in the previous year, regained some of its growth momentum in 2002, though at a slower pace than earlier projected. The partial recovery in markets that are of major importance to Sri Lanka, namely, USA, Europe and the Middle East, was particularly important for recovery in the domestic economy. Benign weather conditions after a severe drought that had prevailed in 2000/2001 supported the recovery in agriculture, while the discontinuation of power cuts impacted positively on industry and services. Meanwhile, the removal of the war risk insurance surcharge on sea and air travel improved external trade and tourist activities. Further, a decline in interest rates, commensurate with the deceleration in inflation, and improved fiscal discipline that minimized expansionary government borrowing, created a conducive macro economic environment for growth in 2002. However, under-performance of the world economy, and the wait and see attitude of investors watching the political cohabitation between the Parliament and the Executive Presidency and the progress of the peace process initiated early in the year dampened the potential for economic growth beyond the long term average of 5.0 per cent per annum.

Meanwhile, Gross National Product (GNP), defined as GDP adjusted for net factor income from abroad (NFIA), grew by 4.1 per cent in real terms, in 2002, compared to a contraction of 1.3 per cent in 2001. The growth in GNP was higher than that in GDP due to the better performance of NFIA. NFIA, though continuously negative, improved in US dollar terms in 2002 owing to the decline in factor payments and increases in factor receipts. Interest earnings improved in 2002 owing to the increase in gross reserves while interest payments on foreign borrowings fell due to the decline in interest rates in international markets.