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Economic growth and economic management

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Sri Lanka's economic growth showed no sign of picking up in 1999. The GDP growth rate was 4.3 per cent, even lower than the 4.7 per cent growth in 1998 and far below the 6.3 per cent growth in 1997. As growth in 1995 was 5.5 per cent and in 1996 only 3.8 per cent, average annual growth in the last five years 1995-1999 is 4.9 per cent which is quite below the announced target of 7 to 8 per cent annual growth required for rapid rise in living standards.

Higher Growth of Developing Countries in 1999 over 1998

It is futile to make excuses for this unsatisfactory growth, particularly when such excuses do nor sound very convincing. In fact, there is a tendency to rationalize this mediocre performance by emphasizing that the growth rate of 4.3 per cent in Sri Lanka was higher than the all developing country rate of 3.3 per cent that year, and that her moderate growth in the context of a global economic crisis and depressed conditions is no small achievement. These excuses ignore, first, the fact that the developing countries did better in 1999 than in 1998. The Asian Development Outlook 2000 of the Asian Development Bank points out that the developing countries, as a whole, improved from 3.2 per cent in 1998 to 3.5 per cent in 1999. This was underpinned by the strong rebound in developing Asia where growth shot up from 2.3 per cent in 1998 to 6.2 per cent in 1999.

Countries which had negative growth in 1998 achieved significant positive growth, in 1999: Hong Kong, Indonesia, Malaysia, Philippines, Thailand and South Korea as shown in the table. These were the crisis-hit countries. Countries outside the epicentre of the currency crisis but slightly affected in 1998 too showed satisfactory growth in 1999: China achieved 7.1 per cent growth and India 5.9 per cent. If crisis-hit Asian countries recovered so dramatically, India and China which were slightly affected like Sri Lanka achieved high growth and developing countries overall improved their growth in 1999 over 1998, Sri Lanka's mediocre performance remains a puzzle.

Second, Sri Lanka's lacklustre performance in 1999 can hardly be attributed to global depressed conditions when world economic growth in 1999 was better than in 1998: World output grew at 2.5 per cent in 1998 but at 3.0 per cent in 1999. GDP growth in the industrial economies rebounded from 2.4 per cent in 1998 to 2.6 per cent in 1999. The US economy - Sri Lanka's principal export market - continued to perform strongly in 1999 with buoyant domestic demand. It grew at 4.0 per cent as compared to 3.9 per cent in 1998. Further, the rate of growth of world trade volume too increased from 3.6 per cent in 1998 to 4.0 per cent in 1999. Thus, the world economic environment being more favourable than in 1998 could not have slowed Sri Lanka's economic growth in 1999. On the contrary, it should have been conducive to higher growth as it was in the case of other developing countries.

Economic Growth of Asian Countries -- % Growth of GDP

Country	1996	1997	1998	1999
China	9.6	8.8	7.8	7.1
Hong Kong	4.5	5.0	-5.1	2.9
Taiwan	6.1	6.7	4.6	5.[illegible]
South Korea	6.8	5.0	-6.7	10.[illegible]
Indonesia	7.8	4.7	-13.2	0.2
Malaysia	10.0	7.5	-7.5	5.4
Philippines	5.8	5.2	-0.5	3.2
Singapore	7.5	8.0	1.5	5.4
Thailand	5.9	-1.8	-10.4	4.1
India	7.5	5.0	6.8	5.9
Sri Lanka	3.8	6.3	4.7	4.2
Japan	5.0	1.4	-2.8	0.6
USA	3.4	3.9	3.9	4.0

Source: Asian Development Outlook 2000 – Asian Development Bank and World Economic Outlook October 1999 – IMF Economist

Export Growth and Stock Prices in Asian Countries

Country	1996	1997	1998	1999	% Change in Stock Index between end of 1998 and 1999
China	1.5	21.0	0.5	6.0	-
Hong Kong	4.0	4.0	-7.5	-0.1	57.4
Taiwan	3.8	5.4	-9.5	6.8	1[illegible].0
South Korea	4.3	6.7	-4.7	10.1	7[illegible].0
Indonesia	5.8	12.2	-10.5	-7.4	6[illegible].8
Malaysia	7.1	1.2	-7.5	10.1	4[illegible].3
Philippines	17.7	22.8	16.9	18.8	[illegible].4
Singapore	6.4	-0.2	-12.2	2.6	6[illegible].4
Thailand	-1.9	3.8	-6.8	7.4	2[illegible].7
India	4.2	4.5	-3.9	10.0	6[illegible].8
Sri Lanka	7.6	13.3	3.4	-4.1	-[illegible].0

Source: Asian Development Outlook 2000

Recovery of Stock Markets in all Developing Countries

Third, stock markets of almost all Asian developing countries show a marked recovery in 1999 but not of Sri Lanka's. The CSE all share index which was 987 at the end of 1994 declined to 702 at the end of 1997; then it dropped to 597 at the end of 1998 and 573 at the end of 1999. In 1998, stock prices in most Asian countries dropped, e.g. Hong Kong, Singapore, Bangkok, Taipei, Bombay, Karachi and Colombo; only those of Kuala Lumpur, Manila and Seoul show a rise. In 1999, however, stock prices of all Asian countries rose: Seoul, Singapore, Jakarta, Bombay, Hong Kong and Karachi by as much as 50 to 75 per cent, Kuala Lumpur and Bangladesh by 25 to 50 per cent and Manila and Taipei 5 to 20 per cent. Both the countries which were directly hit by the East Asian currency crisis, i.e. East and South East Asian countries and those indirectly hit such as India and Pakistan experienced a marked upswing in their stock exchange: South Korea by as much as 75 per cent and India by 60 per cent.

Sri Lanka was the only Asian country whose stock prices declined — by 4.0 per cent — in 1999. This cannot be explained by adverse external factors for the same factors would have operated for other Asian countries as well but their stock prices boomed. Apparently foreigners had little confidence in the Sri Lankan stocks and in fact there was net outflow of portfolio investment in both 1998 and 1999, in contrast to net inflows in 1996 and 1997. As Sri Lanka received very little short-term capital, unlike East Asian countries, there were not much sudden outflows which destabilized the economy. This too was a major factor for the stability and high growth in 1997.

Economic Management

It is invariably the habit of authorities to take credit for good performance of the economy and to blame external factors for poor performance. When the year 1997 showed a high growth of 6.3 per cent the authorities attributed it to good economic management which made the economy resilient and insulated it from the highly uncertain global environment created by the East Asian currency crisis. When economic growth declined to low levels in 1998 and 1999 however, it was attributed to external factors: we were told the entire world economy was experiencing the worst economic crisis since the Great Depression in the early 1930s and the Sri Lankan economy was fortunate enough to achieve even 4.7 per cent growth in 1998 and 4.3 per cent in 1999. It is not revealed that the Indian economy confronting the same "sea of turbulence" achieved 6.8 per cent growth in 1998, even higher than the 5.0 per cent growth in 1997 and nearly 6 per cent growth in 1999.

The authorities do not seem to be perturbed by the downturn in the economy. On the contrary, they consider the low rates of growth as creditable achievements given the difficult environment, and that growth would have been even lower but for the good economic management which in the words of the Central Bank "helped to protect the economy to a large extent against the adverse spillover effects of the recent global economic recession". In their self-complacency, the authorities have kept the public wondering why the so called sound economic management failed to arrest the decline in growth in 1999 when all the crisis-hit countries of Asia did so and achieved higher growth in 1999 over 1998.

External Factors caused Economic Ups and Downs

The fact of the matter is good economic management had little to do with the high growth of the Sri Lankan economy in 1997 or in preventing even lower growth in the economy on account of the world economic recession with 1998 and 1999. The high growth in 1997 was mainly the result of rains which ended the drought of 1996 and converted the negative growth of minus 4.6 per cent in the agriculture sector in 1996 to a positive rate of 3.1 per cent in 1999 and the sharp rise of manufacturing on account of favourable external demand. Manufacturing output increased by 6.5 per cent in 1996, and 9.1 per cent in 1997. This marked increase in industrial and agricultural production resulted in a significant rise in exports growth from 7.6 per cent to 13.3 per cent in the same period.

The decline in overall economic growth in 1998 was mainly on account of a marked drop in the rate of growth of manufacturing output - from 9.1 per cent in 1997 to 6.3 per cent in 1998 - and also a decline in that of agricultural production - from 3.0 per cent in 1997 to 2.5 per cent in 1998. Consequently, export growth dropped sharply from 13.3 per cent to 3.4 per cent. The year 1999 saw an upturn in agriculture but it could not offset the further fall in the growth rate of manufacturing - from 6.3 per cent to 4.4 per cent - and the consequent fall in exports growth - from 3.4 per cent minus 4.1 per cent. The East Asian economic crisis and its contagion effects apparently did not affect Sri Lanka in 1997 but their impact was felt in 1998 and 1999.

If the drought was the principal cause of the decline in economic growth in 1996 and the rains combined with boom in manufacturing, the main causes of recovery and high growth in 1997, the persistent fall in the rate of growth of manufacturing - from 9.1 per cent in 1997 to 6.3 per cent in 1998 and further to 4.4 per cent in 1999 - was the crucial factor behind the downturn in the economy in 1998 an 1999. Manufacturing contributes 17 per cent of GDP and industrial exports constitute about 75 per cent of the total exports. The slowing down of the growth rate of manufacturing inevitably resulted in slowing the pace of export growth. Sri Lanka's exports as mentioned earlier, grew in dollar terms by 13.3 per cent in 1997 but by 3.4 per cent in 1998; in 1999 they fell - for the first time in many years - by 4.1 per cent. While the decline in exports growth in 1998 was caused by a drop in the volume of exports, that in 1999 was caused by a fall in export prices (in dollar terms) by 10 per cent in spite of an increase in export volume. Actually, export prices had risen in 1997 and 1998 - both, agricultural and industrial - but both declined in 1999.

Poor Performance of Textiles and Garments

Textiles and garments constitute Sri Lanka's principal export accounting for about 53 per cent of the country's total exports in 1999. Textiles and garments exports which had risen in dollar value terms every year in recent times, declined by 1.4 per cent in 1999, in spite of an 8 per cent increase in export volume because of a drop in export prices by 9 per cent. Over 60 per cent of Sri Lanka's textiles and garments exports go to the USA - the largest market - and Sri Lanka's textiles and garments exports to the USA which had increased by 3.4 per cent in 1998 declined by 1.2 per cent in 1999 on account of a fall in export prices by 7.3 per cent - a sign perhaps of increased competition from existing exporters with depreciated currencies and new exporters. The key to Sri Lanka's economic growth, thus lies in the demand and price for its textiles and garments exports to the US market. High growth appears difficult without a rise in export prices in the American economy. This is the crucial problem in the Sri Lankan economy and our efforts should be to retain and expand our market in the US and to secure better prices without dissipating our energies on minor export markets.

Economic Management Played No Role

The high growth in 1997 and the low growth in 1998 and 1999 were mainly the result of external factors - climatic factors such as rainfall and the demand and prices for our exports, particularly textiles and garments in the US market. Good rainfall and buoyant demand for exports would have raised the economic growth rate in 1997 in any case; economic management had no hand in it. The lower demand and lower prices for textiles and garments in the US market caused lower growth in the Sri Lankan economy in 1998 and 1999 and economic management could not prevent it and did not cushion its impact. The mediocre economic performance in 1998-1999 is a matter not for self-congratulations but for a serious study of why economic growth dropped in 1999 when almost all the Asian economies and developing countries in general achieved higher growth in spite of an unfavourable external environment. If the high growth in 1997 was due to good economic management was the mediocre growth in 1998- 1999 due to poor management?