

# UNSTOPPABLE SRI LANKA



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His experience is diverse and his knowledge on the economy is immense. He has been a pillar of strength through economic turmoil, unwavering while steering the country towards calmer waters. The Government is able to make policy decisions knowing that each is substantiated and made with the best interests of the country at heart. Dr P B Jayasundera is the Secretary to the the Ministry of Finance and Planning and Secretary to the Treasury. He has been in the public

service for the last thirty years and has worked under different political and policy regimes while being true to his conscience and doing what is right. Dr Jayasundera spoke to Business Today on how the Sri Lankan economy survived the past turbulent economic environment, its recovery during the post war era, development endeavours and economic policy while staunchly believing that Sri Lanka will be unstoppable in its future economic journey.

**By Udeshi Amarasinghe**

**Photography by Menaka Aravinda**

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**The Government of President Mahinda Rajapaksa is completing four years this month. Can you tell us how the national economy has progressed during this time?**

President Rajapaksa's four-year term faced many challenges. In fact, his term began soon after Sri Lanka was shattered by the Tsunami and the LTTE had backtracked from peace talks. The country was demanding massive infrastructure development since the existing capacity of power generation, port operations, the road network and irrigation systems were lagging behind in the backdrop of the growing demand. Education and health sectors also had challenges due to inadequate teaching staff and medical personnel to be able to provide efficient services. Public unrest was high owing to marginalisation of the public sector.

In his approach to development, which was articulated in his manifesto popularly known as Mahinda Chinthana, which was later translated into a 10-year development framework after he was elected as President and had been discussed at length at several forums including Sri Lanka Development Forum held in Galle, emphasis was placed on (a) restoring peace and security which was lacking for the past three decades hampering our development prospects, (b) infrastructure development, which is an essential prerequisite for rapid development in the country (c) social and cultural development underscoring culture, arts, religion and sports required to create a value based society (d) agriculture and SMEs; the backbone of our economy that provide livelihood to a majority (e) promotion of value added industries and services and local entrepreneurship (f) widening of education and health services across the country and improved access to such facilities (g) empowerment of the rural and

plantation economy, (h) strengthening labour relations and productivity (i) private sector development by incentivising exports and competitive import substitution activities (j) promoting sound financial policies for a stable economic environment with a market friendly policy framework and (k) an environment friendly development – Nillapiruna Ratak.

There was a great demand from our own society to correct the emerging development imbalances in lagging regions and to narrow the widening gaps between rural and urban areas. In fact development had been mainly confined to the capital city. Even outer – Greater Colombo area was lagging behind. Therefore rural and provincial development became a priority.

**President Rajapaksa's four-year term faced many challenges...an economic regime was formulated** that was homegrown and nurtured with local values, addressing domestic needs – essentially a holistic approach to development.

Agriculture and domestic industries had been neglected in the backdrop of liberalisation, overlooking required safeguards for domestic entrepreneurs and industries and domestic value addition. Policy strategies had been overly biased towards import – export trade and consumption at the cost of production and investment on value creation in the domestic economy. The gradual erosion of the role of the public sector in essential service delivery particularly in the areas of education, health, agricultural extension services and distribution of essential commodities to the public was a concern since many agencies such as the CWE, Paddy Marketing Board had been marginalised. Policies were focused on trimming the public sector, placing a heavy reliance towards the private sector, particularly in 2002 – 2004 when Sri Lanka witnessed a dramatised neo-liberal policy regime towards liberalisation, privatisation and de-regulation, which did not receive much public support. It is in this backdrop that President Rajapaksa's economic regime was formulated using the experience of the past 30 years. It was homegrown and nurtured with local values, addressing domestic needs – essentially a holistic approach to development.

All issues and concerns that I reiterated were addressed in the ten-year development framework and a budgetary strategy was formulated to move the country forward on that basis. However, circumstances compelled the Government to engage in a war on terror, as the peace process did not gather

momentum and the LTTE did not show genuine commitment to peace talks. They increased violence on civilian targets such as the Kabithigollewa massacre and even prevented access to the Mavil Aru irrigation system, depriving water to innocent civilians. This compelled the Government to prioritise the battle against terrorism. Following the Mavil Aru incident, the Sri Lankan military forces engaged in a humanitarian operation that expanded to liberate the East in the first phase and subsequently the North, which in fact ended only in May, this year. A heavy investment was made to liberate the people affected by terrorism and to clear the geographical area, which was heavily laid with mines, to create a favourable investment climate in the country for long-term growth and development. The past four year expenditure on national security and defence which varied in the range of 3.5 - 4.5 percent of GDP per annum, has thus become a solid investment towards peace and development.

During the four-year period of President Rajapaksa's administration, the country has been freed from fear and uncertainty from the terror waged by the LTTE on people, national assets and the investment climate, achieving peace that successive Governments could not achieve during the past thirty years. Those Governments could not concentrate on long-term development programmes and in fact did not embark on any major development initiative since the Mahaveli multi purpose development scheme. President Rajapaksa did not compromise development, even when he decided to deploy security forces to liberate the East and the North. The Government simultaneously embarked on massive infrastructure development activities in power generation, ports, irrigation, airports, the highway network, bridges and public transport as regards to physical infrastructure and development of schools and hospitals, including recruitment of doctors, nurses, teachers and other professionals with respect to human resource development.

At this juncture when the President is completing four years in office, the country is witnessing the completion of a USD 455 mn - Phase I of the Coal Power Plant in Puttalam which will be expanded to generate 1000 MW, construction of the Upper Kotmale Hydro Power Plant with an investment of USD 300 mn, Hambantota Port in the South with an initial investment of USD 450 mn and the steady physical progress in the construction of the Colombo South Port Breakwater Project with an investment of USD 450 mn, with room for three further terminals in the coming years. Water supply schemes have been launched to augment urban water

supply in Colombo, Gampaha, Kandy, Galle, Ampara, Kurunegala and Jaffna. A large number of irrigation schemes including the abandoned Moragahakanda and Uma Oya irrigation schemes costing over USD 1500 mn is also under construction. Capacity augmentation of existing major irrigation reservoirs as well as new capacity creation through Deduru Oya, Weheragala, Kirindi Oya, Rambukkan Oya, Heda Oya and Uda Walawe left bank has commenced or completed. Even the Giant Tank in the newly liberated Mannar district has been fully rehabilitated. The country is also witnessing a massive bridge and road development programme at both national and provincial levels, involving massive investments. Improved roads and newly built bridges have connected many districts, resulting in less travel time and fuel costs have become a much talked of topic amongst travellers.

Rural development was a priority and a central focus in the Mahinda Chinthana - Development Programme towards reducing poverty. The President in this regard has not only placed emphasis on expanding welfare programmes, but also on providing infrastructure at rural level; consisting of rural roads built using durable concrete laying technology, rural electrification, drinking and irrigated water, transportation as well as health, education and livelihood programmes, to develop the rural economy. We can see these development activities taking place across the country. Access to electricity has increased to 83 percent and pipeborn water to 35 percent. The total tele-density is over 70 percent. Poverty Headcount Index has declined to 15 percent from 24 percent. The Human Development Index is 75. These are a few indicators showing the country's performance during the last four years. The credit should go to His Excellency the President, for adopting a strategy that is not confined to one or two aspects of the overall management of the country but to the totality of development and for being successful in balancing all these objectives.

President Rajapaksa was able to focus on several other initiatives such as taking IT and English to the rural community which have far reaching development prospects. Computer literacy was negligible at the time he assumed duties and now it is 50 percent, in just 4 years. We can proudly claim that even in rural areas there is improved access to telecommunications, televisions and computers. Greater awareness has been created on the importance of learning English and IT, even in the rural community. Over 600 Nana Sala's opened at rural level reflect how well these initiatives have embraced the rural economy. It is this seed

planted in our rural economy that will grow and help build a knowledge economy.

Education and health are two other areas that have achieved considerable progress in these four years. Sri Lanka can be proud of the state of national health facilities. Hospitals have been modernised with highly sophisticated equipment and strengthened with the assistance of experienced doctors, nurses and paramedical staff. Similarly, in education one of the urgent needs was to address the issues of those who do not succeed in gaining university entrance. During President Rajapaksa's past four years, Sri Lanka succeeded in establishing a university for vocational and skills education. Hostels and other educational facilities in the universities were improved and the annual intake was raised to 20,000 students. Universities located in distant areas are being given increased resources to upgrade and modernise their facilities. I would say that his four year term has laid a foundation to facilitate Sri Lanka transiting from an educated society to a knowledge and skills based economy.

President Rajapaksa as the Minister of Finance, guided and strengthened the Treasury and the Central Bank to manage the macro economic situation well, which task was not easy from the international perspective or in terms of the country's past experiences. This could be viewed as the most challenging periods. In December 2004, Sri Lanka was hit by the worst ever natural disaster, the Tsunami. Around 30,000 people killed and another 100,000 displaced, over 100,000 houses destroyed, schools, hospitals, hotels, fishery harbours and roads, badly damaged or destroyed in the coastal belt from Colombo to Jaffna. The country was able to rebuild completely without jeopardising macro stability. The phasing out of the US quota on garments was another challenge. Industries went through a tough time. Surging oil and fertiliser prices had a huge adjustment cost to the Government, industries and the people. We had to go through a period of high inflation. The country had to spend USD 3,200 mn in 2008 to import oil in comparison to USD 800 mn in 2005 imposing a severe strain on external reserves. The global food crisis, which raised food prices compounded our problems. Finally, there was the global financial meltdown in late 2008. In all these situations, President gave bold leadership for the required adjustments to maintain economic and political stability.

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President Rajapaksa's Government has been able to mobilise a substantial volume of foreign aid and loans, not only from donors but also from international capital market sources. This was possible since our country has a convincing and marketable story. During the President's term of office, in addition to mobilising well over USD 1,500 mn per annum from multilateral agencies such as the World Bank, the ADB and from our development partners world-over, the Government has been successful in raising large sums of foreign funds in the international capital market. This could not have been easy to achieve unless our economic policies are seen as right and credible. Government's economic and financial policies having gone through international financial institutions and rating agencies, is a test. This is indeed a major plus point.

President Rajapaksa reigned this period successfully despite the Sri Lankan economy having been confronted with a major crisis due to the global financial meltdown since late 2008 and throughout this year. He has succeeded in maintaining stability. The Budget deficit was not permitted to go above 8 percent. In fact the Budget deficit has been moderately brought down despite pressures from the Tsunami recovery and reconstruction expenditure, development expenditure, war expenditure, rural development activities related expenditure, unparalleled increase in oil and fertiliser prices and associated costs on the Budget, the public and the business community and other challenges to our export industry. Government revenue was raised to 16 percent of GDP until that effort was confronted by challenges due to the recent global slowdown. Public debt to GDP was reduced from 103 percent to 81 percent last year. The macro economic situation has been good. This country has historically for the last 30 years experienced inflation well in excess of 10 percent. The President has been able to bring inflation down to a nominal 4 -5 percent, which is compatible with other countries. Unemployment has declined to 5 percent, reserves have been maintained at a very credible level and stability to our exchange rate regime has been restored without resorting to harmful controls. More importantly the overall economic growth has been maintained at well over 6 percent, except during the first half of this year due to the global setback. The country has progressed from USD 1040 per capita income to USD 2200 per capita income and has become a middle income country during President's term of office. Now that the war has ended and the much needed infrastructure is in place, Sri Lanka is poised for a

takeoff.

**You mentioned that the per capita income has increased from USD 1040 to approx USD 2200. If you could elaborate as to how this was achieved?**

The per capita income of Sri Lanka during the last five years has increased to USD 2200 and this increase is due to a fairly high growth rate, roughly about 6 percent experienced during this period. This growth can be attributed to all three sectors; agriculture, industry and services. The service economy is almost 60 percent of our GDP and that sector maintained a buoyant growth rate of around 6 percent. This sector consists of trade, banking and various other services, which contributed to this expansion. The last five years was a period that was fairly active in terms of property development, construction of roads, ports, electricity and irrigation schemes and provincial and rural infrastructure development. Further, agriculture blessed by very favourable weather conditions and due to the emphasis placed on agriculture by the Government remained buoyant. The policy shift from imports to local value addition helped to improve agricultural activities. It was also due to favourable prices created by the Government for agricultural products by removing the flour subsidy and other hidden incentives offered to imports. Agriculture also became an attractive engagement in recent years due to favourable farm gate prices for rice, maize, liquid milk, potato, onion, fruits and vegetables, provision of credit, fertiliser, quality seeds and planting material. Equally, in the industrial sector emphasis was given to domestic value adding activities using local raw material, as well as for exports. From the investment side there has been a growth in FDIs to around USD 750 mn per annum and domestic investment rising to near 28 percent. Industrial disputes remained at a very low level due to improved labour relations and best practices promoted by the Government. Productivity of the labour force also improved. These factors contributed towards buoyant economic activities during this period and resulted in a higher per capita income, lower incidence of poverty and unemployment.

The Per Capita Income Of Sri Lanka During The Last Five Years Has Increased To USD 2200 And This Increase Is Due To A Fairly High Growth Rate Of About 6 Percent Experienced During This Period In All Three Sectors; Agriculture, Industry And Services.

**Under President Mahinda Rajapaksa's Government many development programmes have been initiated especially infrastructure development**

**including extensive road networks and electricity, then another sector that is being developed are the harbours where Colombo South, Oluwil, Hambantota and the harbours in the North and East are being developed. Can you elaborate on these developments with regard to the Sri Lankan economy?**

For any developing economy to grow at a faster rate than 4 to 5 percent and be placed on a strong 8-10 percent growth path, availability of quality infrastructure is a must, in addition to political stability and peace. Without infrastructure no country can attract investment, reduce transaction costs and improve productivity. If you look at emerging economies like China, Vietnam, Korea, India or any fast growing country, you can see how rapidly infrastructure is coming up and how rapidly infrastructure feeds other investments in agriculture, industry and services. In fact growth is generated by infrastructure because the initial phase of infrastructure development involves massive constructions and business planning. Infrastructure development will create space for growth. In this context, our existing roads are insufficient. Twenty years ago it took only two hours to travel to Galle or Kandy from Colombo. Today, you need five hours, during normal traffic hours. Transaction costs have increased immensely by successive Governments neglecting road construction. Our existing ports are not capable of harbouring large vessels that the world is now manufacturing. The country needs sophisticated infrastructure in the ports sector to promote trade and investment and that is why five ports are being built at present. Sri Lanka is an international trade economy, being a player in global markets. Considering transshipment activities, roads have to be up to the mark, since international commodities would be brought down and certain goods would pass Sri Lanka as a transshipment centre, this will entail massive infrastructure development. The Colombo Port is being developed so that it can continue to maintain its international image as a transshipment port in Asia. The Colombo South Port where there is a 5 Km breakwater under construction, will bring with it larger capacity to accommodate modern day vessels.

The new Port being built in Hambantota is situated on an international shipping line. This Port will commence operations in 2011. This will bring industrial and bunkering facilities to our economy. Other Ports will also provide the required infrastructure. The Galle Port is being developed as a tourist Port. Here again the idea is the comparative advantage of the city to attract tourists. The Oluwil

harbour is being built to cater to the medium term needs of the fisheries sector and feed Trincomalee and Hambantota Ports. Then in the North we have the Kankasanthurai Port that will essentially facilitate trade in that area. Sri Lanka's port capacity is thereby being broadened. Their production capacity is also being broadened since investors are bound to check whether the country has required port facilities, be it for tourism or other services. In an industrial port an investor will look at whether ship building, ship breaking and maintenance services are available. All these facilities are being improved so that Sri Lanka can cater as a transshipment hub. Even now, we are offering many diversified facilities. Trincomalee being the world's deepest port is capable of commanding relocation of massive economic activities which other countries would not be able to accommodate. As such, building port facilities would mean the creation of diverse investment opportunities.

Electricity is another major area of importance. Functioning of a modern economy greatly depends on the availability of a quality electricity supply, its reliability and affordability. Here we need to create huge capacity. The country has embarked on expanding its coal based power to about 2000 MW. The Puttalam power plant will generate close to 1000 MW, in Trincomalee the Government is developing a 500 MW power plant. The country's hydro capacity is being developed to reach its maximum and other alternative energy sources are being promoted to ensure that required power supply is available in the country at all times. It is not only for household consumption but also for industrial and various other needs as well. In fact, Sri Lanka may be the only country in the region that experiences power-cuts very rarely, although we do not often speak of the same. If you look at India, Bangladesh and other countries in the region power cuts are common. Many countries are struggling to cope with their electricity demand.

Irrigation is another important area, since many parts in Sri Lanka are still without irrigation systems. In fact after the Mahaweli development scheme, the irrigation sector in this country has not had any major investment. The present Government has committed investments in major irrigation systems as well as in minor irrigation and tank rehabilitation. The Moragahakanda scheme will provide water to the Eastern and North Central Provinces. The Daduru Oya diversion is taking place, which will provide water to the North Western province. Uma Oya development project will provide water to the South and will generate about 50 MW power. Weheragala project was recently commissioned in the South which is

now providing water to the Hambantota District to augment the available capacity of water. This reservoir is similar to the Rajangana reservoir, which was built using local funds and local engineering skills. There are fourteen other irrigation schemes being developed to cater to various irrigation needs of neglected areas in the country including areas in the Northern and Eastern Provinces.

In addition, the Government has entered into a funding agreement with the World Bank to augment reservoir capacities of existing irrigation schemes like Parakrama Samudraya. The Giant Tank has been fully rehabilitated to accommodate an optimum capacity from the forthcoming Maha cultivation season.

Tourism is an area that the Government is promoting to attract private investments. Dedicated areas have been declared to build tourist resorts in Kalpitiya, in the East and in the South. The Government has targeted 2.5 mn tourists and therefore investments required for resorts, hotels, townships, convention centers, museums and art galleries, transport, health facilities, restaurants, shopping and recreation activities will be very large. The ongoing work towards building the Performing Arts Theatre in Colombo, a 1500 seating capacity Convention Center in Hambantota, the International Cinema and Tele Drama Studios at Ranminigama, the Sigiriya Museum and the Homagama International Stadium and Sports Complex will provide new opportunities in tourism, recreation and related services. In my view this has been a period where investment in infrastructure has been massive.

I see rapid progress in activities towards building a modern road network in this country... All this was done without ignoring the need to ensure connectivity to the rural areas.

Construction of an extensive road network is another important segment in the Government's infrastructure strategy. The traffic congestion in the capital city is being addressed through the construction of flyover bridges. It will take a few more years to convert urban traffic to function in a more modern and efficient manner. New roads are being built. Heavy investment has been made with long term funding arrangements from the World Bank, ADB, Japan, China, India, Korea, the EU countries and from Saudi and Kuwaitee Funds, to construct national and provincial roads. Huge investments have been mobilised from China and India for road construction in the North and East and even in the South. I see

rapid progress in activities towards building a modern road network in this country. The Katunayake expressway is under construction and the contract award is ready for the construction of the outer circular road connecting the Katunayake airport expressway to the Southern highway, under construction. The A9 road is to be developed as a major expressway and soon the North-South expressway would be a reality. Rehabilitation of a large number of national roads have been already completed and several other roads are in the construction stage. As I mentioned earlier, all this was done without ignoring the need to ensure connectivity to rural areas and as such rural access has been equally strengthened. 30 per cent of concrete roads constructed in rural areas have been through community contributions. Hence, there is a partnership between the community and the Government in building these roads.

Infrastructure is necessary in order to reduce transaction costs and enable reliable business planning, which in turn improves competitiveness. The required infrastructure must be in place if you are to remain competitive in the global economy. This is the aim of the current infrastructure development initiative called Randora, meaning – the golden gate way, being an integral part of the Mahinda Chinthana Development Horizon Towards a New Sri Lanka – to provide enhanced capacity to the private sector and production opportunities. The private sector will have greater business opportunities in port and shipping activities, tourism, agriculture, industries, trade, sports, banking, finance and construction. As the global crisis is coming to an end and recession is easing, investment will flow into the country and many of these areas are bound to become active.

**The past year has been quite turbulent with the war, and then fluctuations in oil prices and also the global financial crisis, can you tell us how Sri Lanka survived?**

The present global financial crisis is one of the worst ever economic crises that the world has experienced. In fact, when the crisis erupted with the collapse of Lehman Brothers many predicated that it will lead to a major economic depression, lasting for may be two to three years. Like a great storm, it destroyed much in its way. Firms closed, assets disappeared and people lost their jobs in the US, UK and other major industrial countries. Developing economies too suffered due to loss of exports. The crisis erupted due to several reasons, one being the collapse of the unregulated or less regulated financial institutions particularly in the USA and UK. That had a ripple effect globally. International trade and

financial relations of almost all countries were severely hampered. Secondly, the crisis occurred after three to four years of continuous rise in oil and commodity prices. In fact oil prices went up to USD 147 per barrel. The cost of oil imports alone in Sri Lanka rose from USD 800 mn per annum to USD 3.2 bn, in just four years. The cost of fertiliser, raw material and food imports increased by equal proportions. The trade deficit widened to almost USD 6 bn. That was the sheer size of the crisis on our external payments.

The collapse of the US financial system and the slow-down in consumer spending in the US and other industrial economies affected our exports. Certain exports such as ceramics, rubber products, and made-up garments went through a difficult time almost till September this year. Our exports so far have dropped by about 12 percent which is a very large amount in terms of foreign exchange. In fact people expressed fear of being laid off and were concerned about the financial stability in our own country. The reason as to why it didn't happen here is partly because our country had a well-managed macro economic situation despite pressures from conflict related expenditure. Our financial system is well monitored and regulated. The financial system stability is very much a priority concern of the Central Bank as the regulator. The Government formulated its fiscal strategy to bring down the Budget deficit in line with the fiscal responsibility framework that the Parliament has approved. There is a commitment on the part of the Government to keep the deficit in check by adjusting fuel prices and other outlays to moderate fiscal risks. A tight monetary policy stance was maintained to address inflationary pressures during this difficult adjustment phase. On the structural side, policy initiatives towards energy conservation and alternate energy usage as well as increased production in the local agriculture sector to ensure food security were taken into account. Trade policy was directed to sustain exports and safeguard domestic industries from lower import prices that prevailed during the crisis.

The Government was successful in moderating inflation systematically from around 28 percent year on year, to around one percent at present. Twelve month average inflation has declined to 4.5 percent from 23 percent last year. The Central Bank therefore has also reduced its policy rate to 8 percent, reflecting lower inflationary expectation. This still provides 3 - 4 percent real interest rate which may need closer monitoring. In a nutshell, policies adopted by the Government during President's first four year period giving emphasis to local

agriculture and SMEs, conservation and protection of environment, shifts towards alternative energy sources like coal, solar and hydro. In place of fuel based power generation and appropriate price adjustments and financial policies helped the country to manage the difficult global environment and its impact on Sri Lanka.

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**The Humanitarian Operation though undoubtedly incurred a large cost, its conclusion has been essential for the revival of the economy, can you elaborate on how this has contributed to economic growth?**

Everyone knows that thirty years of terrorism in this country was the main reason why Sri Lanka could not achieve an economic progress of more than what the country has been able to realise. Our economic performance was sub-optimum due to the war, which pre-empted the use of all resources available to the Government for development or for the benefit of the private sector, since much of the public sector resources were allocated to fight terrorism and provide security to the people. The private sector had to provide their own security to safeguard their establishments and property. Business sentiments were very unfavourable to engage them in a long term investment strategy. Tourism, which was one of the promising growth sectors in this country suffered heavily. Though the tourism industry started in the 1960s and gathered momentum in late 70s and early 80s, with the escalation of terrorist activities in Sri Lanka and consequent clashes between the Armed Forces and the LTTE, our tourism industry suffered immensely. Most of the tourists did not consider Sri Lanka a tourist destination anymore. Consequently, some of our neighbouring destinations became more attractive to tourists.

International trade suffered because insurance companies and bankers added a risk premium on trade transactions. The country had to meet war risk premiums, high costs on insurance and shipping. Bank charges were added to these costs, resulting in high transaction costs to Sri Lankan businesses. The country's geographical location advantage to develop shipping and aviation opportunities could not be exploited. If not for SriLankan Airlines, the country's aviations services could have even come to a grinding halt. Many airlines temporary suspended their services and in fact certain airlines withdrew altogether from Sri Lanka. Strategic economic centres were vulnerable to terrorist attacks and many

assets were destroyed. All these issues affected our economy and studies reveal the loss to be around 2 percent of growth in GDP, each year. That is a lot. The reversal of this trend is already visible, in itself is a major boost to our economy.

Ending the war has paved way for many opportunities. It is only now that people can say that expenditure of the last three years is in fact an investment. Those who thought it was a waste, can now realise how short-sighted they have been. The immediate challenge, after the war ended was to provide relief; food, medicine and medical care, shelter and sanitation to those affected. The entire Government machinery was mobilised to provide maximum welfare to the IDPs. The next task was proceeding with rehabilitation and resettlement. Managing this task was difficult as vast areas, which were entirely occupied by the LTTE had to be demined. Third is the reconstruction of the North to restore civil life and development. His Excellency the President appointed a high-powered Task force to carry out resettlement and reconstruction work on an accelerated basis to end thirty years of human suffering caused by the LTTE.

While engaging in demining operations, prioritising residential areas, farm lands, public places, access roads and railway lines, the Government also has to feed about 300,000 people, look after their basic needs, provide medical and humanitarian assistance and ensure security clearances for those in IDP camps, so that eventually they could move to their places of residence, that are cleared of land mines. On the President's directions, a Task Force has been setup to resettle a majority of the IDPs by January 2010. To date, the number of IDPs remaining to be resettled is about 157,400 from about 300,000. Prior to this, the Local Government Elections were held in liberated areas democratising local administration. The Task Force has also finalised a rehabilitation and reconstruction programme in the North. We, who live here clearly know and the international community also appreciate that from May 19, 2009 to date we have not seen any terrorism related incidents in the country. Since May 19, 2009, we have also witnessed a dramatic reduction in crime. This suggests that crimes would have had links with the activities of the LTTE. People are now able to move freely in any part of the country and we could see an increase in public movements. Domestic tourism is gathering momentum.

With the end of the war, Sri Lanka is experiencing a low inflation regime. Inflation has always been around 10 percent. Business climate has also improved and transaction costs are decreasing. Now the country is witnessing a dramatic

transition to a low interest regime. The recent reduction in the lending rate to around 12 percent for priority production sectors will stimulate economic activities. All this time we have been seeing high interest in the range of 20-30 per cent. The corporate sector is enjoying a bullish capital market. Capital gains have been near 100 per cent. Foreign investment inquiries are on the rise. Increased foreign investments in Sri Lankan Government Bonds is a reflection that the investment climate is becoming favourable. GDP growth outlook for the third and fourth quarters of this year indicate that the economy is bouncing back to near 6 percent growth by the end of the year.

**On The President's Direction, A Task Force Has Been Setup To Resettle A Majority Of The IDPs By January 2010. To Date, The Number Of IDPs Remaining To Be Resettled Is About 157,400.**

**The agricultural sector has seen a positive growth in the past year. What has been done to revive this sector?**

Agriculture is a vital sector for Sri Lanka as it constitutes 20 percent of our GDP as a primary activity. This agricultural base contributes towards manufacturing and service activities. Therefore there is a fair amount of contribution to tertiary activities such as services, trade, banking and finance. A greater percentage of our population also live in agricultural areas – in rural Sri Lanka. Looking at plantation agriculture other than the estates under the management of plantation companies, all agricultural crops such as tea, rubber, coconut, as well as minor agricultural exports crops are SME based. They are being encouraged with price incentives and subsidised inputs. In the plantation sector, incentives are also designed to promote high value added activities, industrial activities and finding new markets. Agricultural income is also tax free. In the non-plantation sector, paddy is a major crop. Fruits, vegetables and various other subsidiary crops, liquid milk and dairy production have also gained significant importance. Since Sri Lanka spends over a billion dollars on importation of food items, there is greater scope for local import substitution. This shift is not a move towards protection. Reversing subsidies on imported food items was essential as a policy strategy in favor of local production. In this context, one of the boldest decisions that President took was the removal of the flour subsidy and tax relief on maize imports for animal feed. All policy makers that I have worked for prior to this President, were reluctant to remove the flour subsidy. Successive Governments were committed to give flour at a subsidised price though it was a major

disincentive for rice production and many other agricultural crops.

President Rajapaksa took a firm position not to subsidise imported food items at the cost of local production. These policy initiatives facilitated to get the agricultural policy right. This Government not only removed the flour subsidy but also made it subject to import duty, like other commodities, to encourage local production. The President made the same decision for all major agricultural crops such as potatoes and onions, which can be cultivated in Sri Lanka. If this decision was not taken in a timely manner, inflation would have probably been lower, with no local investment in agriculture. During the initial years the farmers need a guarantee that their commitment to agriculture and their investments in agriculture will not be penalised for political gains. In addition, President Rajapaksa also promoted providing agricultural credit, seeds and planting material and guaranteed farm gate prices. The President also provided fertiliser and such other inputs at heavily subsidised prices. Agricultural extensions and marketing facilities were strengthened. During the last four years, many of the farmers got attractive prices for their produce, whereas there was a time that farmers lost control over their income after harvesting since they had to compete with unfavourable import prices. I do not think that any farmer is against imports, as long as there is a level playing field. Government policy has placed emphasis on sugar, dairy, milk, livestock, poultry and fisheries as well. Emphasis has been placed on increasing local liquid milk production and improving the dairy industry in which major investments are being made. We need to realise that this transformation would take time and cannot be achieved overnight.

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Rural agriculture benefited from infrastructure development. Today, the majority of the Sri Lankan society enjoys access to electricity. Most of the areas have telecommunication facilities and good roads. President Rajapaksa's novel concept of Maga Neguma, where all villages are empowered with basic infrastructure at rural level has helped farmers to benefit from commercial activities that are taking place in urban areas. The number of tractors, machinery and equipment, packaging material, refrigeration facilities and other new technologies associated with agriculture is amazing. There are also increased investments towards

growing fruits, vegetables and export agriculture. The large corporate private sector companies as well as individuals have taken to agriculture in response to the new agricultural policy of this Government. There is also a growing interest in the out-grower model through which many small holders are considerably benefited.

**You said that you would not call the Sri Lankan economic policy as protectionism but Sri Lanka seems to be moving towards import substitution and hence the agricultural sector has been able to progress. What are your thoughts on this and how viable is this in the long term?**

Well, I explained that the initiatives taken by this Government in the agricultural sector were aimed at correcting major price and tax distortions created by past economic policies and should not be viewed as a move towards a protectionist policy; Liberal imports subject to normal duties and taxes and other safeguards are permitted. Even during the worst global economic crisis, this country did not resort to import barriers and export controls. There were no trade restrictions. Sri Lanka still conserves free trade agreements with India and Pakistan and liberal trade regimes where duties and taxes are maintained at more liberal levels. Sri Lanka can still claim that it is the most liberal trade regime in the South Asian region. The exchange rate regime is very flexible with no restrictions on current account transactions. There are no exchange controls or credit controls. Sri Lanka has been guided by global economic principles. True enough that the Government adopts safety standards that are required either for health, consumer welfare, security or environmental reasons. Neither protectionist measures have been adopted nor have policies been reversed. All I said was that the policies which were biased towards imports have been realigned to support efficient domestic production.

As a result, local farmers can compete internationally. Our producers export fruits and vegetables and a small quantity of rice. Paddy producers are now well positioned. Farmers have ventured into maize cultivation. Sometimes I wonder how we can be a proud nation when we cannot even manufacture animal feed. 100 per cent of our animal feed requirement had been imported in 2005. It has been reduced to 50 per cent since Sri Lankan farmers are now growing maize and such other products. Of course, during the harvesting season there are certain safeguards being introduced like in any other country, being mindful of difficulties that would accrue to farmers in marketing their products at stable

producer prices. There is a considerable investment being made in the milling and processing industries and also in storage capacity expansion. These policies need to be pursued to ensure deserving benefits to such investors.

Looking at viability aspects, think of two areas other than agriculture. Let us analyse Sri Lanka's viability of import substitution. I use that term directly. Number one is energy; now what was the structure here? The power generation strategy, was to rely basically on the use of fuel, which is not a material available locally. Recent price developments of oil have shown how vulnerable our system is, to international supply conditions and prices. In addition to the huge cost, the use of oil has a tremendous adverse impact on the environment as well. At the time when President Rajapaksa resumed office, Sri Lanka relied on fuel based technology for almost 65 percent of power generation. Therefore, is it wrong to move towards alternative and affordable energy sources to replace fuel imports?

Due to politics and various other sensitivities, previous leaders were reluctant to give the green light to set up a coal power plant or proceed with the Upper Kotmale hydro power project. These projects were suspended and did not gather momentum for nearly 25 years, despite the fact that there was funding available to commence them. However, President Rajapaksa gave his approval to go ahead with the coal power plant in Puttalam and the Upper Kotmale hydro power project.

Incentives have been provided through policy initiatives for people to adopt alternative energy sources like solar, windmill and mini hydro. We are gradually reducing import of oil for power generation. This strategy is consistent with our Green Environment policy strategy as well. It is an extremely valuable policy and the entire world is supporting this strategy. We will be able to cut down oil imports by half when this strategy succeeds. On average we now spend approximately USD 2.1 bn, on the basis of USD 70 per barrel for the importation of oil. By resorting to alternate energy, imagine if we can save one third of 2.1 bn dollars? That is 700 mn dollars. This would be a very large saving.

We are importing close to USD 800 – 900 mn worth of food items. Imagine if most of these products are produced here, with the required technology, quality planting materials, fertile land and irrigation schemes put in for productive use with proper extension and marketing arrangements put in place. The local economy could replace food imports altogether and a huge value added food

industry can be developed. With the liberation of the North and East, prospects for increased production in agriculture, livestock and fisheries are very strong. Newly liberated districts like Mannar, Killinochchi, Batticaloa and the Eastern Province will add to agricultural production due to which our country can reduce most of its food imports. The fisheries sector is in fact exploiting its potential after thirty years because the Eastern and Northern coastal belt is now available for fishing. Then livestock is another important area. Import substitution can be focussed on these areas.

There is a fair amount of growth in the tourist sector. The country is eyeing a 2.5 mn tourists market in the medium term. Expansion in the tourist industry means demand for food, vegetables, fruits, electricity, domestic industrial products, furniture, recreation and all such domestic activities means greater scope for local production.

In my view protectionism is where you impose import controls or banning imports. The Government has not done that. Even today we import such as potatoes; onions and chilies, peanuts and bees honey. No restrictions have been imposed and competition prevails. What the Government is doing is creating an incentive structure to enable the domestic economy to grow. In the long term, this economic strategy is extremely viable. It needs hard work and commitment from both public and private sectors to create farming friendly systems and procedures and related institutional arrangements.

**The service sector and the industrial sector showed moderate growth last year, how are these sectors faring this year?**

Well, the growth in the service sector slowed down reflecting global slow down in trade and investment. During the second quarter of this year the service sector grew only by one percent. The industrial sector grew by about 3.5 percent and the agriculture sector by 4 percent. As I said before, export growth declined by 12 percent and import growth declined by 30 percent. The decline in motor vehicle and consumer durable imports is substantial. Since Sri Lanka is a trade dependent nation, global trade flows matter for economic performance. The gradual disappearance of terrorist financing and tight regulatory controls on unauthorised finance companies and credit operations also seem to have had some impact on the service economy. Tight monetary policy we followed to counter inflation curtailed demand for formal credit. In the agricultural sector,

the drop in tea production due to the drought in the first quarter and the global impact on industrial activities also affected the economy adversely. The economy also went through some adjustments due to the impact of high oil prices that prevailed during last year. Cumulatively, these have slowed down the economy.

Neither Protectionist Measures Have Been Adopted And Nor Have Policies Been Reversed... The Policies Which Were Biased Towards Imports Have Been Realigned To Support Efficient Domestic Production.

Now we have approached an immediate post war transition period in which business sentiments have improved. Following the decline in inflation, financial system has been able to move on to a low interest rate regime in which credit growth will gather momentum. The global economy is on a recovery path, which is a plus point because Sri Lanka is an open economy that is heavily dependent on exports, remittances, tourism and capital flows. Tourism and capital markets are bullish. Sri Lanka exported almost USD 8 bn worth of goods in 2008 but this is expected to decline in 2009 to around USD 7.4 bn. Therefore we need the international economy to recover fast to get back our export growth. Sri Lankan imports in 2008 was to the tune of USD 13 bn which is also projected to decline below USD 9 bn largely due to the decline in oil and fertiliser prices as well as the drop in motor vehicles and consumer durable imports. These activities need to get back to normal levels. Since remittances are improving, imports will increase and low interests will stimulate spending. As a result the service economy will bounce back. The construction industry which slowed down during the past 12 months is poised to a recovery. Northern reconstruction activities and revival of the fishery industry and other livelihood activities as well as banking and financial expansion in the North will make a further impetus to the growth in all sectors. With all these put together I feel that during the last quarter of this year the service economy will bounce back and the economy will grow by 5-6 percent.

**Looking at the city landscape we find many apartment buildings, some of these have been abandoned even before completion and many of these are empty. Not only is this sore to the eyes, it reflects badly on the country. Can you tell us why there is no control on such property development ventures?**

The property boom that took place during the last few years happened in an insecure environment when we were saddled with terrorism. Global economic

deterioration made this worse. Only sectors that operated with targeted markets or clientele base managed to do well. Some of our tea, cinnamon, apparel and tourism industrialists have graduated to such scales of operations. Being capable of withstanding various adversities, many such investors have built state of the art hotels, factories and farms in the country. Similarly, property development also took place in this backdrop. Then the global situation took a turn for the worse in 2008-2009. In addition to the problems we already had, the global economy collapsed. Therefore the construction industry suffered a severe setback. As a result certain investors felt that they could not go ahead with their projects and suspended. There are others who completed construction and are operating at under-utilised capacity. Now that the war is over, the world recession is ending and the country is transiting to a low inflation, low interest rate regime construction industry ought to bounce back. The period ahead is a period of construction in which our economic capacity could be exploited to the maximum, giving best returns on investments. I feel that Sri Lanka will experience a construction boom that will change its landscape.

**Moving on to the infrastructure in the plantation sector, for the first time since independence, concrete roads are being constructed in this sector. Can you elaborate on the infrastructural development done in this regard?**

The plantation sector is a Government priority in terms of developing lagging regions. According to poverty indicators in the country, one of the concerns that the Government had was high incidence of poverty in the plantation areas despite there being better employment opportunities. The Government has given highest priority to improve living conditions of the plantation community by improving their educational and health facilities and at the same time, providing access to roads, electricity and drinking water. Like the rest of the rural development initiatives, the plantation community has been integrated with the overall development initiatives and that is why you see concrete roads and rural electrification schemes being implemented in the plantation areas as well.

**In your interview with Business Today in June 2008, you spoke about the nation being integrated with the rest of the world, especially, the trade agreement with India, Pakistan, the SAARC region and also China, USA and Europe, can you tell us how this has expanded since then?**

Sri Lanka is a liberal economy. We conduct trade with almost every country. Our

presence is reflected in the best performing markets in the world. If we start from tea, Sri Lankan tea has penetrated into almost all tea drinking nations. We are present in the Middle East, Russia, East Asia and Europe, Australia and the Far East. Our value added tea brands such as Dilmah, Mlesna and Tea-Tang have captured global tea markets. In fact I have been told that these local brands have become leading brands in those markets. Small manufacturers are also venturing into branding their value added varieties of tea such as Heladiv. They are gradually diversifying their markets and competing with popular international brands. Ceylon tea cannot and should not go forever as bulk tea to international markets. We must make more value addition here and fetch best prices.

Our manufacturers are also exporting biscuits and chocolates with brand value. Damro, is a local household and office furniture company and is a major exporter to India, Australia and many other destinations. Industries such as Nature's Secrets engage in cosmetic and beauty care products has attracted several global destinations. Similar progress has been shown by local Arurvedic product manufacturers as well. I just mentioned a few of these names to show how our economy is evolving in a globally competitive environment.

Then our apparel, ceramic, gem, jewellery and rubber product industries have gained a fairly niche market access. These industries show active presence in US, Europe and are now penetrating into Japan and looking for opportunities in China and various other countries. Our industries are not looking at the low end of the markets where several other nations are competing. It is indeed encouraging, our manufacturers are looking at the middle and upper segments of the markets. Incentives have been geared towards that. The tax regime as well as the exchange rate regime is very much in support of exports to promote global integration.

**With India we have the Indo - Sri Lanka Free Trade Agreement for bilateral trade. Both sides are moving in that direction with increased trade volumes. Sri Lanka has an FTA with Pakistan as well. Though we do not have FTAs with US and Europe, we have liberal trade access in those markets.**

Now the country's labour force is moving up the ladder to semi and high skilled categories. Particularly professional services such as legal, medical, business management are growing, internationally.

Even the rubber manufacturing industry is targeting the European and US markets. In fact, Loadstar was a very vibrant tyre manufacturing company prior to the crisis, supplying products even to the airline industry. Even in this small way, our country has integrated with the rest of the world.

The country's labour force has integrated with global markets rapidly. In fact about one million people are working overseas. They remit almost USD 3.2 bn per annum to Sri Lanka. Earlier, Sri Lanka was prominent in the unskilled category, now the country's labour force is moving up the ladder to semi and high skilled categories. Particularly professional services such as legal, medical, business management are growing, internationally. President Rajapaksa's Government has introduced a series of tax incentives to promote offering professional services internationally. Here too, I feel that Sri Lanka is quite well integrated.

With our increased new capacity, in terms of infrastructure, stability, sound policies that the Government is continuing and the likely investments in tourism, alternative energy, agriculture, manufacturing, urban development and various other related activities, Sri Lanka will have greater integration in global trade and finance. I prefer not to label whether the country will be a finance, shipping or a bunkering hub but the fact that all these facilities being available here is bound to make Sri Lanka a unique development centre in the region. Further prospects for IT and enabling services and industries, financial services, shipping, medical services are also great. When business bounces back, the prospects for SriLankan Airlines to promote catering, maintenance, engineering, training facilities for pilots and service personnel are very high. Sri Lanka is a pleasant place to live compared to many cities in the region. I'm sure that most of us would agree with this view.

Similarly, the Government has systematically built up its policies to create a knowledge and skill based economy because we are a very literate society. We have shifted from being a literate society to an educated society. From an educated society we are moving towards a knowledge and skilled society. Our doctors have revamped our medical services and in our own way we have succeeded in attracting investments to this area. Both Government and private hospitals have developed modern capacity, to make the services attractive to users. Likewise our engineers, architects, accountants and lawyers are expanding the scope of their services. In the next ten years these services will be available from here to the rest of the world, without our people having to go abroad to

provide such specialised services. Instead, there will be people visiting Sri Lanka to obtain such services.

Our story is not similar to countries that are still talking about unskilled cheap labour. Sri Lanka will be basically adopting middle and upper scale skills and knowledge based industries. Agriculture will also be knowledge based. That is the direction the country is moving under President Rajapaksa's administration.

With Our Increased New Capacity, In Terms Of Infrastructure, Stability, Sound Policies...Sri Lanka Will Have Much More Integrated Global Trade And Finance.

### **How did Sri Lanka widen its scope in global trade and investment?**

During the last four years, I have seen an active involvement of the Government under the President to expand our trade and investment relationships beyond our traditional partners. The President's visit to Iran revived our long standing trade and investment relationship. For example till his visit no Sri Lankan Government was able to secure a facility extending more than thirty day credit, although 70% of our crude oil is imported from Iran. It was only after the President's visit that Sri Lanka acquired seven month credit facilities. In addition through this bilateral relationship, the President was able to secure large investments for projects such as the Uma Oya project, which Sri Lanka was not able to start because of funding constraints. Further, funds were also secured for power projects for rural electrification. On the trade side, Iran agreed to facilitate Sri Lankan exports to Iran.

The continuous development assistance for Sri Lanka's development programmes was secured during the President's visits to Japan. The relationship with India enabled the Government to enhance development assistance for railways as well as for hospitals, schools and vocational training institutes in the Plantation area. The recent support extended for humanitarian assistance and development of infrastructure in the Northern Province has raised the Indian contribution significantly.

Russia has become a very strong partner in development and we have been able to secure funding assistance as well as markets access for our products in Russia.

Chinese assistance to Sri Lanka was enhanced in support of mega infrastructure projects that was commenced recently. Ties with the Middle East expanded with

President's visits to those countries. The Kuwait, OPEC and Saudi Funds have expanded their contributions for our development. In fact the three agencies together have committed to the Moragahakanda funding arrangement and the Japanese Government will be funding the any remaining activities. Ties with Middle East have also promoted tourism, foreign employment and exports, particularly for tea. President's visits to Libya promoted export and employment opportunities for Sri Lanka.

Recently the President visited Vietnam, again a long standing friendly country of Sri Lanka with whom we had not built partnerships so far. Burma and several other countries were visited by the President to promote trade and cultural relations. The scope of trade and investment between Pakistan and Sri Lanka has been widening through Free Trade Agreement, investment promotions, technical and security cooperations.

South Asian countries like Bangladesh, Nepal and Bhutan have accepted President's unique contribution as a leader of SAARC. Korea is another active partner supporting our development and has provided employment opportunities for over 20,000 skilled workers and has also extended financial assistance for infrastructure development. Singapore's involvement, in security, trade and investment promotion has also contributed immensely. The President is engaged in building ties with South American countries. Of course new relationships are being built while consolidating relationships with traditional donors like US, Europe and others with whom Sri Lankan trade and investment ties have been increased. Liberal trade and exchange rate regimes and the credible payment mechanisms practiced by the Sri Lankan banking system have contributed to promote global financial transactions as evident from the two successfully concluded Sri Lanka Government Bond issues. It is for the first time Sri Lanka showed its presence in the international capital market. International rating agencies have given financial ratings reflecting the country's sophistication as an emerging economy.

**Could you elaborate on the trade agreements between India and Sri Lanka, because this has made a significant impact on our economy?**

India and Sri Lanka are neighbours. Both countries gained Independence almost at the same time and can be considered as model democracies. The political relationship between the two countries is very strong. Trade, investment and

technical cooperation are also very strong. It is based on this historical relationship that the Indo-Sri Lanka Free Trade Agreement was formulated. India is a large country. When a country enters into a Free Trade Agreement with a large country, the small country is always uncomfortable but in our case India allowed Sri Lanka to feel comfortable. Our agriculture and several other industrial products were not open to free trade. In that environment too the trade volumes of both countries have increased. Of course there are some problems. Certain industries have been affected but both countries have managed the difficult transition. Some of the Indian businesses were affected when our exports were sent to India and some Sri Lankan businesses were affected when they entered our market. This trade agreement has contributed towards the expansion in investments and trade between the two countries.

India and China are no longer poor countries. They are recording high economic growth rates. During the last 20 years China and India have been growing at over 10% and China has become the third largest world economy. Brazil, Russia, India and China - BRIC has become a powerful world forum. India is no longer being looked at by world powers as a poor economy. It is a vibrant economy in South Asia. Indonesia, Vietnam and many other East Asian countries are growing too. Smaller but rich countries such as Singapore and Hong Kong are very strong and stable. Asia is growing and Sri Lanka is contributing its share to this 'Asian lead'. After all, in terms of per capita income, Sri Lanka is a lead economy in South Asia. In that context, Indo- Sri Lanka free trade keeps our ties and businesses together.

**The Political Relationship Between The Two Countries Is Very Strong. Trade, Investment And Technical Cooperation Are Also Very Strong. It Is Based On This Historical Relationship That The Indo-Sri Lanka Free Trade Agreement Was Formulated.**

**Moving on to inflation, the consumer inflation rate peaked to 28.2% in June 2008 and decelerated considerably to reach 2.9% in April 2009, can you explain the reasons behind these fluctuations?**

As I explained earlier, there are several reasons for the high inflation experienced at the beginning of this Government's administration. Firstly, the Government adopted policies to shift the import dependent economy to a production economy. Thus the wheat flour subsidy, duty and tax concessions on several imports had to be removed. This initiative to provide remunerative prices for local producers

engaged in the production of liquid milk, maize, paddy, potatoes, onions and similar items resulted in high consumer prices. Secondly the oil prices rose dramatically and Sri Lanka had to make corresponding adjustments in domestic prices which resulted in high transportation costs. Adjustments were very difficult. It was more difficult for the ordinary people and fixed income earners. There are a large number of motorcycle users and over 400,000 three wheeler operators. For them an extra cost of Rs 500 - 1,000 was a large burden. Then public transport - 70% of bus operations being done by private bus operators had to adjust to revised fuel prices. The cost of goods transportation largely done by lorries and trucks also increased. Electricity and water tariffs increased because of high energy costs. The global food crisis resulted in high food prices. Thirdly, the volatile security situation was another factor that affected the cost structure. Security restrictions were also in force.

The challenge for the Armed Forces was to ensure security in the rest of the country while fighting in the terrorist occupied areas. Their biggest success was being able to provide security to the rest of the country without any incidents. Internal movements, particularly of goods and services and transportation involved additional transaction costs. Fourthly, tight global and financial conditions resulted in high interest rates. Therefore cost of funds was very high. Domestic production was not sufficient to meet the demands. Government expenditure was high largely because certain subsidies had to be accommodated within the Budget because the entire adjustment could not be done through prices. The fertiliser subsidy for example was a major expenditure item in our national Budget, where at one time the Government subsidised 95% of the fertiliser prices. All these factors contributed to inflationary pressure in the economy.

Fighting inflation was not easy, the immediate instrument available was through monetary policy because it can influence credit expansion. The method in which this can be done is by tightening monetary policy to influence interest rates. That is why the Central Bank had to engage in open market operations to mop up the liquidity in addition to raising policy rates. Despite the war, the Government also had to manage development and welfare expenditure by maintaining high revenue efforts to moderate the deficit and lessen the borrowing demand. Private sector expansion had to be moderated to curtail the otherwise high demand pressure. Those were the policies at a macro level that the Government could

adopt. Nevertheless those alone cannot counter short term inflation arising from fuel price adjustments or due to other structural reasons.

However the continuation of those policies in the short term helped to moderate demand. In the medium term several other decisions such as increasing production and efficiency, reducing transaction costs are important. Ending of the war and associated cost reductions too contributed to bring down the inflation to a moderate level in recent months.

In the medium term several other decisions such as increasing production and efficiency, reducing transaction costs are important. Ending of the war and associated cost reductions too contributed to bring down the inflation to a moderate level in recent months.

**The Central Bank continues to tighten the monetary policy stance through the control of reserve money growth, can you tell us the rationale behind this?**

Any Central Bank will be concerned about inflation. Its primary responsibility is to ensure price stability. Domestic demand was high due to high Government expenditure and private sector credit demand. In this environment the Central bank basically conducts monetary policy through market instruments targeting reserve money. Interest rates and exchange rates reflect reserve money movements. Therefore when the inflationary pressures are obvious to the monetary authorities they use the policy rates and various other policy instruments available to influence the same. Therefore from the Central Bank's point of view and as far as their share of responsibility is concerned, inflation is constantly addressed. That is why the monetary policy road map explains how the Central Bank shapes the liquidity movement. Because of these actions, inflation is no longer a near term concern. This is why currently the policy rate of the Central Bank is maintained at 8 percent as compared to 12 percent a year ago because the underlying inflation has declined to around 4-5 percent. However the bank maintains a relatively high positive real interest rate as a precaution to ensure that inflationary pressures are satisfactorily neutralised.

**In September 2009, the rate of inflation decreased to 0.7%, from 0.9% in August, this year, as measured by the point-to-point change in the Colombo Consumers' Price Index (CCPI) but this is set to increase at a**

**more subdued level, can you explain why this is?**

Yes, the Central Bank has setup their reserve targets in the road map that they follow each year to stabilise liquidity conditions in the country. Despite the journey being difficult, they have managed to get through and the domestic demand pressure has been moderated. In the meantime the international commodity prices have been moderated although there are international pressures on oil prices again. Oil prices remained around USD 70 per barrel in recent months and as such there was no pressure on prices. The Government has managed to ensure that agricultural production continues to remain high. In recent times, particularly with the liberation of the East, the contribution from this province to the national economy is on the rise. There is an increased supply of fish production. We see goods coming from the North as well. In fact fish prices have gone down. Fruit and vegetable prices are reasonable, right now the most expensive commodities are sugar and lentils, both these commodities are heavily imported and their prices are not favourable. Most of the consumer items have remained at fairly stable prices and the Government has kept to its policy to maintain price stability even of fuel and gas. The Government has also revitalised the CWE and Coop City networks, Retail Dedicated Economic Centres and Cooperatives to intervene in the market and provide essential commodities at affordable prices for less income earners. Taxes were imposed when imported prices were low and reduced when the prices were high, as a cyclical measure. Towards the end of the year there is a seasonal pressure on food prices and this reflects inflation in November and December. Nevertheless, the overall inflation is expected to be around 5 -6 percent which is quite reasonable.

**Any Central Bank Will Be Concerned About Inflation. Its Primary Responsibility Is To Ensure Price Stability.** The Domestic Demand Was High Due To High Government Expenditure And Private Sector Credit Demand.

**The banks cut their interest rates during the last few days, if you could elaborate on this?**

Yes, of course the Central Bank has been consistently bringing down its policy rates in line with the decline in inflation. However as I mentioned earlier, the Bank maintains a fairly high positive return on the policy rate itself. Call market rates have stabilised around 8 percent. Market interest rates on Treasury Bills and Bonds have declined to a range of 9 - 12 percent from 16 - 18 percent. This

too is in line with the moderation of inflation and domestic liquidity conditions. In response to this the banks have introduced several cuts in their lending rates. The core inflation, which will guide monetary policy actions is around 4-5 percent and the Central Bank's desire is to keep that below 6-7 percent. That is fairly an acceptable rate of inflation. Of course the world economic recovery and the revival of domestic economic activities will also influence these movements. Food prices are very crucial in relation to inflation. This is why the policy rate is still maintained at around 8 percent.

The entire interest rate structure will fall in line with that. Anyone can deposit their money on a daily market at 8 percent. Treasury bills for a three month period are going at 9 percent and one year bonds are going at around 11-12 percent. Therefore savings are more secured at that range with a positive rate of return. Banks are adjusting their lending rates on that basis as high interest rates are no longer justifiable considering huge positive returns to banks. Generally real interest rates should be around 1.5 to 2 percent. The banks are now moving in that direction and one can see a clear transition to a lower interest rate regime. Of course the banks will have to adjust gradually because some of the deposits they have raised are at very high rates so they are gradually realigning deposit rates in line with Treasury Bond and Treasury Bill rates. 12 percent rate on fixed deposit is a good return considering 5-6 percent inflation

Deposit rates cannot reduce substantially because the country needs to retain savings. Therefore fixed deposit rates may remain at 12-13 percent. Accordingly the banks may structure their lending rates in the range of 8-9 percent to 14-15 percent for priority sectors and high interest rates for consumption based credit. Banks also need to curtail their operational costs and margins, through efficiency gains.

Lending rates will also depend on security. If a loan is secured, the rates will be lower. With regard to pawn broking, the People's Bank has announced that they will lend at 14 percent that is because they are secured loans. If it is unsecured it may be 16-17 percent and could be even higher if they are for consumption purposes. Agricultural and industrial loans are also moving in that direction and penal rates are being relaxed. The application of new rates on the remaining balance of existing loans will provide relief to a large number of borrowers. Leasing and finance companies are also likely to adjust their rates downwards in the coming weeks which will be a boost particularly to SMEs. In the next several

months the country will see a movement towards a low interest rate regime. As the environment is conducive, the financial regime will have to balance between savings and investments. The Central Bank and the Government will have to ensure that inflation is managed at single digit level, to promote both savings and investments.

**Consumer items have remained at fairly stable prices and the Government has kept its policies to maintain the price stability even of fuel and gas.** The overall inflation is expected to be around 5 -6 percent which is quite reasonable.

**If we are to move on to the loan that we received from the IMF, many predicted that Sri Lanka would not receive this loan, what actually turned things around?**

Well, although there was some speculation that Sri Lanka will not secure the IMF loan, the Sri Lankan officials guided by His Excellency the President and also the IMF technical staff, managed to design a sound financial programme to secure the Standby Facility that Sri Lanka was eligible. That programme was very well designed in respect of Government's concerns. There have not been conventional conditionalities attached to the programme. It has been designed well within the Government agreed budget, which had already been approved by Parliament for 2009. It has been well within the broad framework of the Fiscal Responsibility Act and the broad objectives that the Government has committed to bring down inflation and build external reserves at a time the global economy is going through a serious financial crisis. Thus the Government was quite optimistic. The Central Bank and the Treasury were very confident that they can secure the Fund Standby Facility. The IMF Mission which was here was also of the view that Sri Lanka needs IMF assistance. Sri Lanka itself had shown during the past four years its capacity to face economic vulnerabilities and ability to manage difficult conditions without resorting to protectionist policies or working against market practices. In that background, the role of the IMF was essentially to facilitate the smooth functioning of the international payment system of the country. That is why the full quota was approved for the benefit of the country to build reserves to a satisfactory level. The programme was also consistent with the monetary policy road map of the Central Bank.

**Why is it important for the loan to go directly into Central Bank Reserves,**

## **rather than finance budget expenditures?**

Well, the need of the hour was to build international reserves. Sri Lanka's official reserve of over USD 4 bn, prior to the crisis declined in a very short period of time to around USD 1.2 bn. That level of reserves was not sufficient to meet unforeseen situations in the context of the fragile global financial outlook. Technically, Sri Lanka's Balance of Payments in 2009 was not as bad as in 2008, because the projected decline in our exports was lower than the decline in the cost of imports. The biggest saving was from oil. The saving from oil imports was at least USD 1.5 bn. That was a buffer. Though some predicted that remittances would decline, they did not decline either. In fact, remittances continued to grow. Then, certain imports such as motor vehicles that required heavy payments declined. Raw material costs, machinery and equipment costs also declined, which resulted in savings in foreign exchange. However, in order to restore confidence in the system, the country needs to build up reserves and stabilise exchange rates. That is why the IMF favourably looked at Sri Lanka's justifiable reasons for fund support.

Generally, the IMF Standby Arrangement is to support Central Bank Reserves. The IMF and all financial institutions including private financial institutions know that Sri Lanka has never defaulted a single loan. Not only that our banking system has not defaulted even a Letter of Credit. That much commitment has been made by the Sri Lankan Government to meet its international obligations whether it be debt, or contractual. The Country has maintained that credibility throughout.

Therefore it was important to strengthen our Reserves to sustain our commitment to safeguard a credible international payment system. The budgetary needs are looked after through other development assistance and funding arrangements. In addition to the increased utilisation of official development assistance the Government also floated USD 500 mn Sri Lanka Bonds. International rating agencies gave a higher rating with a positive outlook on the country's economy and finance.

Since the Standby Agreement was approved, the country's reserve position has shown a turn around. Of course ending the war was a major contributory factor to this turn around. Investments in Government bonds by foreign funds, the new quota allocation by the IMF and the gradual recovery of the economy and improvements in the Balance of Payments have helped to establish a strong

Balance Sheet for the country. The Central Bank is projecting near USD 6 bn reserves towards the end of the year.

When the USD 500 mn loan was realised, the Government did not use it for day to day consumption expenditure. In fact, the Government very prudently used about USD 168 mn out of USD 500 mn to settle the loan raised by the Government a few years ago from the FCBU at high interest. This reduced our foreign currency debt by that amount.

In addition, the Government had to settle some of the Letters of Credit which were opened to meet various obligations of the Government. The Government also reduced its working overdraft balance, in both Bank of Ceylon and People's Bank from about Rs 70 bn to Rs 54 bn which reduced the cost of funds on Government finance.

All in all, the whole idea of IMF support was to stabilise the external financial environment of Sri Lanka and maintain high reserves and restore confidence in the country's financial and payment system. At the same time it was vital for the Government to re-engineer its own fiscal operations to move into a low cost interest rate regime, which I articulated earlier. In addition, we are seeking development assistance from the World Bank, the Asian Development Bank and other such institutions in support for development. Both the World Bank and ADB are working closely with us to provide emergency credit for Northern rehabilitation and development work. Support from bilateral arrangement for Northern development is also encouraged.

**Moving on, the World Bank has also signed agreements recently to finance post conflict programmes. What has been the response from the International community in general in terms of loans and grants to revive the Sri Lankan economy and fund post conflict programmes?**

There is quite a positive response from almost all countries for Sri Lanka's development efforts despite rhetoric in the media. The World Bank is working towards providing USD 150 mn funding assistance to reconstruct and rehabilitate the Northern Province. Government has shown a remarkable progress in the resettlement of IDPs. People have returned to the liberated areas including Mullaithivu and Killinochchi. People are also returning to the Mannar District because de-mining in the entire Giant Tank area has been completed and

resettlement has begun. In the next several weeks, the numbers returning will continue to rise.

Prior to the return of IDPs basic infrastructure such as access roads and community facilities were provided. Livelihood support and other development assistance is also being provided and it is in this context that the World Bank and Asian Development Bank have committed for their support. The Asian Development Bank is also contributing to build infrastructure and a road network complementing the reconstruction work supported by other development partners such as Japan, India, China, Korea and the European Union. Many other development partners such as Australia and the UK have also extended their support for rehabilitation and demining activities in the North. In brief, support for post war reconstruction in the Northern Province remains strong.

In addition, our own Government has incurred substantial expenditure to mobilise the required machinery, technology and equipment for the accelerated demining programme. In fact, Sri Lankan Security Forces have deployed over 1,000 soldiers for demining activities. The expenditure under the Defence Ministry can no longer be considered as military expenditure. Security personnel are now engaged in resettlement and reconstruction activities. The Government has imported a large consignment of machinery and construction equipment for use in Northern reconstruction work. The Government has taken a lead in Northern rehabilitation and reconstruction work and the domestic private sector has also shown their commitment to participate in this programme.

**GSP plus has been making news the past few days, can you tell us the reasons behind the crisis?**

GSP plus unfortunately has become a political issue rather than a trade issue. The Sri Lanka Government from the very beginning indicated that they should not be subjected to any investigation by outside parties on matters coming under the governance structure of Sri Lanka. The Government has gone on record that the humanitarian operations conducted to liberate people in the North and East from LTTE terror has been done in accordance with the laws of the land.

As far as trade is concerned all the best practices that the EU is committed to, is available in Sri Lanka. Our industries are committed to best practices in labour laws, gender, environment, human rights, work ethics and factory conditions. As I

understand the current debate regarding GSP plus revolves around a report compiled by two consultants based on information provided by various NGOs. Our industrialists and private sector who are working closely with European partners would testify how onesided the content of the report is. The Government has put the record straight.

Therefore Though I Think It Is A Challenge, Industries Will Go Through These Difficulties And Come Out Of It. That Is Why GSP Plus Should Not Be Withdrawn Because Industries Will Survive.

Sri Lanka's trade, investment and diplomatic relations with the European Union does not rely on GSP plus alone. It is much wider. The entire global community was aware that Sri Lanka was fighting a war against terrorism. In fact there is a global agenda to fight terrorism and Sri Lanka being a country that suffered heavily from terrorism worked closely with the international community to defeat it. In this context, it is unfortunate that trade issues are being mixed up with National Security issues. Now that the thirty year war has ended and the economy is poised to a rapid recovery GSP plus can be complementary to the development process. I can't think of any economic rationale for obstructing that process, which will improve the livelihood of many citizens particularly the poor who have suffered for decades. I hope that these economic considerations and the factually correct position will eventually guide the ultimate decision making regarding trade issues.

**If GSP plus concessions are removed, will the Sri Lankan export industry be able to survive?**

It will be difficult, because, as I said Sri Lanka has gone through an extremely tough time. The impact of the global crisis itself was worse than the possible withdrawal of the GSP plus. The oil shock that this country went through is unparalleled to any other economic problem because the country had to spend USD 3.2 bn as against USD 800 mn that Sri Lanka spent few years ago.

At the same time, Sri Lanka fought a thirty year conflict which was not an easy task. Our factories, our establishments, our work force, our entrepreneurs and the Government had to work under extremely difficult conditions. The tourism sector was very vulnerable to security conditions and the industry was never able to exploit its full potential. Yet, the tourism industry survived with 400,000

tourists coming in to the country. Sri Lanka's tourism industry has shown that the country has the capacity to survive adversities. Companies like Loadstar which expanded its reach very rapidly by raising the country's value added rubber exports to a significant level suddenly became vulnerable and in fact had to scale down its operations – a very painful adjustment. Still Loadstar is back in business, having made adjustments. Despite difficulties, the Sri Lankan economy, its entrepreneurs and industries have shown remarkable resilience. Sri Lanka's apparel industry showed how well it could adjust to meet challenges of competitive global trade, when the US removed the export quota a few years ago. Therefore though I think it is a challenge, industries will go through these difficulties and come out of it. That is why GSP plus should not be withdrawn because industries will survive and will even shift its direction if necessary. The European economy is an important partner for our economic development; the US is equally an important partner for our economic development. These are big markets for our exports. It is not only about trade but also about investment. Many European countries are contributing for development in Sri Lanka. The British Government extended credit for flyovers. Our joint venture with British company De La Rue is here in Biyagama, printing currency not only for Sri Lanka but to the rest of the world as well. In fact 80 percent of their currency markets are outside Sri Lanka. The Arugam Bay bridge was funded by the US. That is the bigger picture as far as trade, investment and finance are concerned. American and European banks have been in operation here for a long time. I feel that we should value these relationships.

In the end, Sri Lankan industries will have to operate in a globally competitive environment. Sri Lankan industries are competing with Bangladesh, Vietnam, Indonesia and China. These are countries, which are producing virtually the same products that our exporters are producing. Therefore competition, at the end of the day, is the hard reality. The Sri Lankan industries will face it although it will be difficult. Sri Lanka should not be permitted to go through that difficulty by global partners, particularly by our friendly partners because this is the time Sri Lanka is poised to takeoff. That is inevitable because infrastructure is in place, peace has come our way, global economy is recovering, political stability has come in a big way and the country is looked at very favourably as a growth centre in the region. Therefore I'm sure the withdrawal of GSP plus is not going to be the biggest constraint for growth. However, we can enjoy a comfort margin if we secure GSP plus.

If you permit the technically required lag for an investment decision then such investments are in place... Already new attractions have come from the hotel sector, alternative energy projects, property development, agriculture and manufacturing.

**What is being done to convince the EU, that Sri Lanka is actually conforming to International law and hence the concession should not be removed?**

Our sincere commitment from the part of the Government is evident because everyone can see the time and effort being devoted to Northern rehabilitation, reconstruction and development. The progress made in demining and the preparation for resettlement, restoration of schools and health facilities and the number of people who are being released daily by the Ministry of Nation Building and the Presidential Task Force are given wide publicity. This is verifiable.

As regards to the Government commitment to continue with GSP plus concessions, our Ambassador in Brussels is actively providing all the clarifications regarding various concerns. In addition, the President has appointed four senior Ministers to look into any issues that the EU may need further clarifications on how best these issues could be resolved without compromising our sovereign rights in conducting our own affairs.

**Since the end of the war and the economic climate is improving we were expecting more investments to come into the country. But that has not happened. Why is that?**

Well, investment is something that you cannot expect overnight. In the debt market, investments have already been realised. Sri Lanka's reserves have improved not only from the IMF resources. The IMF so far has released only USD 322 mn. The second tranche is due but reserves are already near USD 6 bn. That is because people have placed confidence in the Sri Lankan economy.

There is a surge in the stock market. All corporate entities have taken a lead. Market participants are active and are enjoying a sizable turnover. Share prices have increased by over 100%. Many listed companies have enjoyed huge capital gains over the last few months. Market capitalisation has reached near one trillion from 490 bn last year. The market had a daily turn over of almost a billion rupees. Response in the real economy is taking place and excess capacity seen in

many sectors in the Sri Lankan economy being rapidly utilised. Room occupancy in most hotels is on the increase. Hotel rates have increased. Turnover is large. If you permit the technically required lag for an investment decision then such investments are in place. In fact a large number of investment inquiries are being responded to. They are quite ambitious investment proposals which cannot be hurriedly cleared. Already new attractions have come from the hotel sector, alternative energy projects, property development, agriculture and manufacturing.

### **How will Sri Lanka maintain the peace dividend?**

The peace dividend was actually reflected on May 19, 2009 itself. From that day onwards there have been no terrorist incidents. That is the biggest peace dividend that the entire world was looking for. While seated here we don't think whether a bomb will hit us or a nearby building anymore. Staff in the Treasury can still remember how this building itself was affected by three separate terrorist incidents; one when the terrorists bombed the Central Bank, another when terrorists attacked the World Trade Centre and last year a suicide attack near Hilton Hotel in which one of our employees lost her life. That feeling of insecurity is not there anymore. The relief is evident from everyone's faces.

People are travelling around the country. Many people say that you can't reach the Arugam Bay beach or the Nilaveli beach without advance bookings. There is an increase in the number of tourists coming into the country. Already hotels are full and people are beginning to consider that Sri Lanka is a place to visit. Though our people probably don't notice, fishing restrictions in the North and East are no longer there and fishing activities have resumed to normal scale. There is an increase of fish supply in the market. The people in the North and East have got their livelihood back. Many people in the East are engaged in agriculture and livestock as well.

There is a massive construction plan as I spoke of earlier. When the Manampitiya bridge was opened last year by the President everybody thought that that would be the longest bridge which connected the North Central Province to the East. Earlier this month the President commissioned the bridge in Kinniya which has become the country's longest bridge now. Everyday the country is witnessing some thing unique in progress. Before the construction of such bridges, ferries were used extensively. People can witness development happening in their

neighbourhood. In another few months, the Mannar bridge will be opened and that will connect a previously conflict affected area. It is for those who are living in those areas that the peace dividend is vital.

Approximately half of the IDPs have returned to their homes and many are planning to do so. Livelihood activities for those who are returning as well as those who are living in conflict affected areas are being developed.

The public saw yet another aspect of peace dividend when the State Banks took the leadership to introduce a low interest rate regime. That means funds are available for house building, business development and trade, at low interest rates. The saving from rate reduction is almost in the range of 6 - 8 percent. That is a huge relief and an incentive particularly for the SMEs to revive their businesses and livelihood. Similarly, housing construction, agriculture, livestock and other activities for which loans are now available at low interest rates will be a peace dividend. The accelerated infrastructure development that can now take place in the North after thirty years will also be a peace dividend. The machinery including hundreds of construction equipment, earth moving machines and trucks that have been imported to the tune of USD 150 mn and seen in Galle Face last week have now been dispatched to the North. The people are now getting used to a new life instead of seeing T56 rifles, hand grenades and suicide jackets. Therefore the peace dividend is already there. Imagine the impact of creating 45,000 new room capacity in the tourism sector alone, boosting construction activities with related services and backward linkages.

Development is inevitable as a conducive environment has been established. The corporate world cannot complain. As I explained before the turnaround in the stock market and the capital gains enjoyed by them will expand further once their investment portfolios begin to expand into diverse economic activities in the future. Above all, we live in a very peaceful environment and that is a sustainable peace dividend.

**The private sector is feeling the weight of both direct and indirect taxes. But from another side we find that many people including professionals are evading taxes. What are your thoughts on this?**

The operation of a multiplicity of taxes on narrowly focused areas of taxation for each tax has made our tax system complex. This has evolved over a time period

due to increased reliance on tax concessions and tax holidays for the provision of various consumer relief and investment incentives. The country's economy is largely SME based. Agriculture is a small holding other than those managed by the 20 plantation companies. Most export industries enjoy concessions. The country's service economy other than banking and financial institutions, telecommunications and selected commercial activities are essentially small holdings in nature. Professional services which have expanded in the field such as medicine, accountancy, engineering and law are largely individually managed and only very few firms have been established as organised services. The domestic manufacturing industries are subject to high taxes while those established with BOI incentives operate in a very low tax regime. Although the country's income has increased from less than USD 300 per capita to little over USD 2,000 at present, there is no commensurate growth in income taxation. The country's tax system relies largely on complex indirect taxes to raise revenue. They too rely on a selected range of commodities such as liquor, cigarettes, motor vehicles and consumer durables for revenue. Most indirect taxes have targeted specific objectives such as infrastructure development, domestic value addition and consumer relief in addition to maintaining a higher revenue effort.

As you know, the system has expanded at a time the country was preoccupied with a struggle to defeat terrorism. Tax holidays and various concessions had to be offered to compensate the unhealthy business climate that prevailed due to the war, lack of infrastructure and several other shortcomings. Although certain steps have been taken to modernise the tax system by moving towards VAT, adequate investments have not been made to introduce the required technology and human resource capacity building. As a result the VAT system itself has been confronted with many problems. This complex system, the weak tax administration, the SME based economic activities and high taxes have also contributed to both tax evasion and avoidance, which you are referring to.

Sri Lanka Is Likely To Hit USD 5000 Per Capita Income. That Is In Per Capita Terms Similar To Malaysia Today. The President Has Laid A Solid Foundation For This Journey...This Is Why I Say That The Graduation To A Solid Middle Income Country Is Unstoppable.

There is no simple way that Sri Lanka can avoid the operation of a multiplicity of taxes since the country needs to essentially address certain concerns through taxes. Firstly, custom based taxes are necessary to provide certain acceptable

safeguards and protections. Then the country needs personal income tax since taxation should eventually shift towards income taxation in line with capacity to pay. Sri Lanka has a fairly organised corporate economy and prospects are improving for the growth in that sector. That should justify a standard corporate income tax system. The country's indirect taxes should be developed in line with VAT principles to ensure that only consumption is liable to such taxation. As there are specific commodities such as liquor, cigarettes, motor vehicle etc. that need to be treated differently from general consumption commodities, there is a necessity to use excise tax as well. There is also a widespread interest in conserving the environment and hence environmental related taxes are globally promoted. On these considerations, even the simplest tax system we could adopt would involve 7- 8 different taxes, each servicing a unique purpose.

Sri Lanka also needs to move towards a low tax rate structure. Sri Lanka's prospects in expanding banking and financial services as a major growth sector requires to place them on a much lower tax regime than the present system which imposes nearly 60 percent. The Government has also recognised the need to narrow down the gap between highly taxed economic sectors and activities and sectors in the economy that enjoy tax holidays. With regard to consumption taxes, excise taxes have weakened the revenue growth and hence the country needs to move toward a much more efficient low tax rate structure with a wider base so that compliance would become easy. Such a tax system will also promote investment and growth and hence would be favourable for long term growth in Government revenue. The country could move towards such a system as previous constraints such as the war and absence of infrastructure are no longer relevant for our development. Recognising these aspects, His Excellency the President has appointed a Presidential Commission on Taxation to go in to all such aspects of revenue administration, which would address issues involved in defining the tax rates and the base, required for tax administration in Customs Inland Revenue Department and Excise Department examination of national and provincial linkages and also the prospects for non tax revenue sources. I am sure that the Taxation Commission will provide us a framework that can be used as a guide to formulate a new tax regime that will make our economy vibrant and that will also promote a buoyant growth in Government revenue. As Sri Lanka is looking forward to a post-war development strategy with the forthcoming Budget, revenue reforms could be a major area of emphasis so that people could look forward for better economic prospects with a lesser tax burden. Development of

such a system would be necessary to address complex questions you raise on tax evasion.

**You have worked under different policy regimes during your career, you were able to adapt and deliver the goods. Can you tell us about this experience and how you managed to do what you felt was right?**

I have gained much experience during the last thirty years working under different leaderships, seniors and also under different policy and political regimes. However, I have never been subjected to undue influence and I have always worked to the best of my professional ability. I continue to upgrade myself professionally and I maintain very honest, sincere commitments to the work I am entrusted with. Most of us have developed ourselves with the opportunities we received from free education and other facilities in the system, which many tend to take for granted.

I received my professional discipline from the Central Bank from which I proceeded to the US to complete my postgraduate studies. Since then I worked at the Central Bank for a longer period where we had very inspiring superiors from whom we learnt a lot. Then I came to the Ministry of Finance where I worked under equally competent seniors. Of course at the Ministry I work closely with political leaders whom I enjoy working with. I always make decisions according to my conscience. If I am not convinced then I won't do it. I consider that Sri Lanka can prosper and the public service can do much to realise it. I believe in being Sri lankan and myself.

**I Have Gained Much Experience During The Last Thirty Years Working Under Different Leaderships, Seniors And Also Under Different Policy And Political Regimes. However, I Have Never Been Subjected To Undue Influence.**

**With 2010 just around the corner what can Sri Lanka look forward to?**

2010, I would say is a year of take off. It begins with Sri Lanka transcending from the status of a lower middle-income country to the high end of a middle-income country. In the immediate five years of post war Sri Lanka, the country is likely to hit USD 5000 per capita income. That is in per capita terms similar to Malaysia today. The President has laid a solid foundation for this journey.

The President has removed many negatives – terror on our society and lagging infrastructure issues are subjects of the past. The commitment for a new Sri Lanka and a value based Sri Lanka are all in place. Such leadership will take the country to a fairly high level of income. In that journey we will see a much more prosperous rural Sri Lanka which will be connected with urban Sri Lanka through roads, electricity, telecommunication, schools, hospitals and other facilities. All Sri Lankans will have access to electricity, quality drinking water and quality education. Every Sri Lankan family will have at home at least some form of a vehicle. Every Sri Lankan will have a TV, access to a computer, fridge and other basic facilities. This is an unstoppable process of development considering the foundation laid by the President during the last four years. The President has made bold investments. The difficult and politically costly decisions made by President Rajapaksa have basically paid dividend to the country because not only did the war end, but also new power plants, ports, roads, new schools, hospitals and stadiums are ready for economic use. Policy strategies for the development of agriculture, livestock, fisheries, industries and SMEs are all ready, which means a solid foundation is in place. Everything was done simultaneously. This is why I say that the graduation to a solid middle income country is unstoppable.

It is not only in the economic front that the country is moving forward, the society is moving towards being a caring society. The President is very sensitive towards that – a value based, caring society is his central theme. That is why he is fighting against the use of drugs, discouraging smoking and alcohol consumption while promoting culture, arts, religion and sports. Some may think that the President is committed only to roads, ports, electricity and irrigation. That is not so. Building international stadiums and sport complexes and convention centres, cinemas, studios, art centres and places of worship also are initiatives of the President. In Hambantota in another year's time the country will see a 1500 seating capacity Convention Centre. Towards the end of next year a Performing Arts Theatre in Colombo and an international stadium and a sports complex will be opened and that will entail a large number of recreational and sports activities for the new generation. The President is taking the new generation to the next level with IT and English initiatives. The benefits will not be seen today but the new generation will grow with IT, English and modern infrastructure which means they will be global citizens. To me the future of Sri Lanka is very promising.