



This section of the Report presents a concise review of Sri Lanka, its physical features, demography and key economic indicators.

It also takes a brief look at the global economy during the period under review, which helps to place details of the Sri Lankan economy in context.

These details are presented to lend context and provide salient information about Sri Lanka to our readers, particularly our international audience.

Officially known as the Democratic Socialist Republic of Sri Lanka and also known as Ceylon, is located about 31 kilometres off the Southern coast of India. As a result of its location in the path of major sea routes, Sri Lanka is a strategic naval link between West Asia and South East Asia. Sri Lanka has also been a centre of Buddhism and culture from ancient times.

Sri Lanka is renowned for the production and export of tea, coffee, coconuts and rubber. It boasts a progressive and modern industrial economy with the third highest per capita income in South Asia. The natural beauty of the island's tropical forests, beaches and landscape, as well as its rich cultural heritage, places Sri Lanka high on the list of the world's top tourist destinations.

With the end of the 30-year bitter separatist war in May 2009 this island nation turns a new chapter in its history.

Physical Features

Total area	65,610 Sq. km.
Land area	62,705 Sq. km.
Capital	Sri Jayawardhanapura
Commercial Capital	Colombo

Demographics

	2009	2008	2007	2006	2005
Mid-year population (mn persons)	20.5	20.2	20.0	19.8	19.7
Labour force (mn persons)	8.1	7.5	7.4	7.5	8.1
Labour force participation rate (%)	48.7	50.2	49.8	51.2	48.3
Unemployment rate (% of labour force)	5.8	5.2	6.0	6.5	7.7

Source - Central Bank of Sri Lanka Annual Report 2009

Global Economy

The global economy is recovering at a moderate rate from a financial and economic crisis. Government policy responses have helped to set in motion the recovery process from the crisis. Countries worldwide are recovering at varying speeds, tepidly in many advanced economies and solidly in most emerging and developing economies. Among the advanced economies, the United States is off to a better start than Europe and Japan. Of the developing economies, Asia is recovering remarkably, while many European and some Commonwealth of Independent States are lagging behind.

Global growth is projected to reach 4¼% in 2010 and 2011. Advanced economies are now expected to expand by 2¼% in 2010, and by 2½% in 2011, following a decline in output of more than 3% in 2009. Growth in emerging and developing economies is projected to be over 6¼% during 2010-11, following a modest 2½% in 2009.

Source: World Economic Outlook (April, 2010).

Sri Lankan Economy

In the year 2009 Sri Lanka's economy grew by 3.5%. However further growth was hindered due to the spill-over effects of the global financial and economic crisis and the 30-year separatist war. The main contribution to this yearly growth rate is from the 6.2% growth rate of the final quarter. Also the second half of 2009 witnessed the end of the three-decades of war against LTTE. The return of investor confidence and a positive external outlook for the country, also contributed to this growth rate of 3.5%.

Sectoral Composition and Increase in Gross Domestic Product (GDP)

	As a Share of GDP (%)			Rate of Change (%)		
	2009	2008	2007	2009	2008	2007
Agriculture Sector	12.0	12.1	11.9	3.2	7.5	3.4
Industrial Sector	28.6	28.4	28.5	4.2	5.9	7.6
Services Sector	59.4	59.5	59.6	3.3	5.6	7.1
Gross Domestic Product (GDP)	100.0	100.0	100.0	3.5	6.0	6.8

Key Economic Indicators

	2009	2008	2007	2006	2005
GDP at Market Prices (Rs. bn)	4,769	4,312	3,540	2,898	2,423
GDP per capita (US \$)	2,053	2,014	1,617	1,421	1,241
GDP growth (%)	3.5	6.0	6.8	7.7	6.2
Colombo Consumers' Price Index (2002=100)					
Annual average	3.4	22.6	15.8	10.0	11.0
Colombo Consumers' Price Index (2002=100)					
Point-to-point-end period	4.8	14.4	18.8	13.5	7.4
Fiscal deficit (% of GDP)	-9.8	-7.0	-7.7	-8.0	-8.4
Current account balance (% of GDP)	-0.5	-9.3	-4.2	-5.3	-2.7

Source - Central Bank of Sri Lanka Annual Report 2009

The annual average rate of inflation which is measured by year-to-year change in Colombo Consumers' Price Index (CCPI) was 3.4% by the end of 2009 compared to 28.2% in June 2008. This is the lowest inflation rate recorded since 1985. The low inflation rate enabled Central Bank of Sri Lanka (CBSL) to relax its monetary policy stance to support the domestic economy. This is clearly evident by the gradually lowered policy interest rates during the year.

A further decline in market rates was observed following a request made by the Government in October 2009 to the state-owned banks to bring down their lending rates. The Average Weighted Prime Lending Rate (AWPR), the rate at which Licensed Commercial Banks (LCBs) lend to their prime customers, showed a marked decline of over 800 basis points to 11.12% at end December 2009. The Average Weighted Lending Rate (AWLR), has gradually declined during the year, with a marked decline observed in the final quarter of 2009.

Interest Rates

	2009	2008	2007	2006	2005
(Percentage per annum at end-year)					
Treasury Bill rate -					
91 days	7.73	17.33	21.3	12.76	10.1
364 days	9.33	19.12	19.96	12.96	10.37
Commercial Banks -					
Weighted average - prime lending rate (AWPR)	10.91	18.5	17.95	15.19	12.2
Weighted average - deposit rate (AWDR)	8.01	11.63	10.31	7.60	6.2

Source - Central Bank of Sri Lanka Annual Report 2009

During the first 4 months of the year witnessed heavy foreign exchange outflows due to the critical stage of the internal conflict. This exerted pressure on the exchange rate. However, since May 2010 with the end of the conflict and improved investor confidence there was a large inflow into the country exerting pressure on the exchange rate to appreciate. The intervention strategy adopted by the Central Bank helped to maintain a stable exchange rate to a great extent.

Exchange Rates

	2009	2008	2007	2006	2005	2004
Annual average Rs./US\$	114.94	108.33	110.62	103.96	100.50	101.19
End-year Rs./US\$	114.38	113.14	108.72	107.71	102.12	104.61

Source: Central Bank of Sri Lanka Annual Report 2009

The gross official external reserves increased to its highest level ever recorded of US\$ 5,097 mn by the end 2009. This was mainly due to the receipt of the first two tranches of the IMF-SBA facility amounting to US\$ 652 mn in June and November 2009. Further, the receipt of the proceeds from the second international sovereign bond issue of US\$ 500 mn in October 2009 was another contributory factor.

Standard & Poor's (S&P) and Fitch Ratings revised Sri Lanka's sovereign rating outlook from 'stable' to 'negative' within days of the end of the conflict, reversed it once again to 'stable' and further to 'positive' in October 2009. S&P affirmed the long-term foreign currency Issuer Default Rating (IDR) at 'B'.

The recovery of Sri Lankan economy was further evident from the significantly high surplus of the Balance of Payment (BOP) by US\$ 2,725 mn. This surplus was due to lower trade deficit which contracted to US\$ 3,122 mn in 2009 from US\$ 5,981 mn in 2008 by 47.8%. And substantially high financial flows like worker remittance which grew by 14.1% to US\$ 3,330 mn in 2009 compared to US\$ 2,918 mn in 2008.

After the end of 30-year long civil war, Colombo Stock Exchange (CSE) Indices increased rapidly creating new records. Market capitalisation at the Colombo Stock Exchange reached record high on 06th October 2009 as it reached the Rs. 1 tn mark for the first time in Sri Lanka's history. All Share Price Index (ASPI) closed the year at 3,385.6 points, the highest level recorded in CSE history. The ASPI recorded a growth of 125.3% for the year 2009. Milanka Price Index (MPI) closed the year at 3,849.4 points, the highest level reached by the MPI since May 2007. The index recorded a growth of 136% for the year 2009. The share market also achieved the highest turnover for a given year by generating Rs. 142.5 bn for the year 2009.

Capital Markets

	2009	2008	2007	2006	2005
All Share Price Index	3,385.60	1,503	2,541	2,722.40	1,922.20
Milanka Price Index	3,849.40	1,631.30	3,291.90	3,711.80	2,451.10
Value of shares traded (Rs. mn)	142,463	101,454	104,985	105,154	114,599
Market capitalisation (Rs. bn)	1,092.10	488.8	820.7	834.8	584
Market capitalisation (% of GDP)	23	11	23	28	24

Source: Central Bank of Sri Lanka Annual Report 2009

Sri Lankan Social Infrastructure Development

Sri Lanka's life expectancy and adult literacy rates which measure the social development are well ahead of the other countries at the same income levels. Between 1980 and 2007 Sri Lanka's Human Development Index (HDI) rose by 0.58% annually from 0.649 to 0.759 today. The HDI for Sri Lanka is 0.759, which gives the country a rank of 102nd out of 182 countries with data. Human Development Index (HDI) which looks beyond GDP to a broader definition of well-being. The HDI provides a composite measure of three dimensions of human development: life expectancy, adult literacy and purchasing power parity (PPP).

The life expectancy and adult literacy rates even when compared with the high income countries are well ahead. Although social infrastructure is not up to international standards, Government continues to support its long-standing policy of providing free health for the public in every Government hospital. The Governments' commitment to continue the free education system has provided Sri Lanka with a high literacy rate.

Population and Vital Statistics

Age distribution (%) (2009) -	
0-14 years	26.3%
15-64 years	67.4%
65 years and over	6.3%
Population density (2009)	326 persons per sq. km.
Infant mortality rate (2006)	10.0 per 1,000 live births
Dependency ratio (2006)	48.3%

Expectation of life at Birth (2007)

Male	70.3 years
Female	77.9 years

Literacy Rate (2008)

Overall	91.30%
Male	92.80%
Female	90.00%

Human Development Index (2007)

Ranking among 182 countries	102
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Poverty

Population below US\$ 1 a day (1990 - 2005)	5.60%
Population below US\$ 2 a day (1990 - 2005)	41.60%

Future of Sri Lanka

The future of Sri Lanka looks very positive after the end of 30-year long civil war which hindered the development in this country. The Northern and the Eastern Provinces which were affected most carry two thirds of country's coastal and maritime resources and about one-third of the country's fertile land. There is tremendous potential for the development of the agriculture and fisheries activities and related industries in these areas. In order to rehabilitate and resettle Internally, Displaced Persons (IDPs) and to develop infrastructure in the said provinces the Government has initiated two province specific programmes; Nagenahira Navodaya (Eastern Revival) in the Eastern Province and Wadakkil Wasantham (Uthuru Wasanthaya/ Northern Spring) in the Northern Province.

With the increased investor confidence the Sri Lankan economy is anticipated to recover steadily. A higher growth of 7-8% is expected in the medium term which requires investment of around 30% of GDP. Although, the trade deficit is expected to widen in the medium term, the anticipated increase in migrant workers' remittance is expected to ease the deficit in the external current account.

Sri Lanka is amongst the 16 beneficiary countries of the GSP+ facility arrangement, which is a special arrangement granting duty free access to EU markets. The GSP+ facility allows businesses in Sri Lanka to export 7,200 items to the EU which is worth around 900 mn Euro to Sri Lanka in terms of export earnings. Further, the garment industry provides direct employment to nearly 300,000 people. In December 2008, Sri Lanka's eligibility for the next term beginning from 2009 was renewed subject to a review by the EU.

In February 2010, the EU member countries temporarily suspended the GSP+ facility to Sri Lanka effective after 6-month grace period.

However, recently the Government commenced engaging the EU in an effort to win back the withdrawn GSP+ facility. There is little doubt that the withdrawal of GSP+ will impact the garments sector.