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Minimal impact seen from crisis in Sri Lanka

KUALA LUMPUR: The economic crisis in Sri Lanka will have very little impact on Malaysia, as bilateral trade between the countries is not huge in the larger context, say economists.

On Tuesday, a foreign news agency reported that crisis-stricken Sri Lanka had defaulted on its US$51bil (RM215.8bil) external debt, calling the move a “last resort” after running out of foreign exchange to import desperately needed goods.

The island nation is grappling with its worst economic downturn since independence, with regular blackouts and acute shortages of food and fuel.

Based on the Malaysia External Trade Development Corp or Matrade’s latest data, Malaysian exports to Sri Lanka were valued at RM3.02bil, while imports were at RM321.84mil in 2021.

To put that into perspective, based on the **Statistics Department’s** preliminary data, in terms of global trade, Malaysia’s gross exports in 2021 totalled RM1.24 trillion while gross imports came to RM987bil.

Centre for Market Education chief executive officer Carmelo Ferlito told StarBiz, “We have to put this in perspective. While the business between the countries grew at an important pace in the past decades, at the macro level, Sri Lanka is not one of the top trading partners for Malaysia.

“Some fallout can be perceived by individual businesses, which has developed ties with Sri Lanka, but I do not expect major repercussions.”

Based on the High Commission of Sri Lanka’s website, total trade between Sri Lanka and Malaysia had grown from US$547mil (RM2.3bil) in 2015 to US$941mil (RM3.98bil) in 2019.

In 2019, 51% of Malaysian exports to Sri Lanka were petroleum oils while Malaysia’s imports included apparel (24%), cereals and products (11%), and edible fish (10%).

Bank Islam Malaysia Bhd chief economist Mohd Afzanizam Abdul Rashid told StarBiz: “Judging from the trade numbers, it looks like Sri Lanka’s economic crisis is expected to have minimal impact on Malaysia.”

Mohd Afzanizam said: “What is more important is the lesson that we can learn from its crisis. Clearly, economic mismanagement precipitated by corruption is a recipe for disaster. If it is left unchecked, it could burst and become a self-inflicting crisis.

“I think we all can agree that resources are limited, and therefore, the politicians, government machinery and businesses would need to ensure every decision is done with transparency, value adding and fair for all. It’s a reminder for us actually whenever there is a crisis,” he added.

Meanwhile, data analytics and consulting company GlobalData, which is headquartered in London, pointed out that triggered by an acute shortage of foreign currency, ill-timed tax cuts, losses to tourism, a fall in foreign worker remittances, shortages of food and fuel and high foreign debt, Sri Lanka is currently battling the worst economic crisis since its independence.

In a recent report, GlobalData construction analyst Pooja Dayanand said considering this current turmoil, he forecasts the Sri Lankan construction industry to contract by 4.6% in real terms in 2022 against the previous projection of a 9.2% growth.

The weakness in Sri Lanka's tourism sector – which is the third-largest source of foreign exchange – is also expected to continue over the coming months, due to the ongoing Russia-Ukraine crisis, given that Russia is one of the largest tourism markets for Sri Lanka.

"The depleting foreign currency reserves, mounting debt and the continuing weakness in Sri Lanka's tourism sector are expected to limit public spending on infrastructural projects this year.

"Besides the economic catastrophe, the country is also witnessing a troubled political environment. This is expected to further weigh on investor confidence, thereby further affecting the Sri Lankan construction industry's output this year," said Dayanand.

The Sri Lankan construction industry, which is one of the biggest economic contributors and employment generators in the country, is also facing significant headwinds due to the shortage of cement.

The severe foreign exchange crisis has prompted the government to impose strict import control measures. This has led to the shortage of raw materials required to produce raw materials domestically.

Dayanand said: "The Sri Lankan government's decision to default on all its outstanding foreign debt could prevent a further deterioration of the country's financial position.

"Although it had sought debt relief from India and China, both countries offered more credit lines to buy commodities. However, the government's plan to seek financial assistance from the International Monetary Fund (IMF) and the World Bank could provide economic aid to bounce back."

Meanwhile, S&P Global Ratings has lowered its long-term foreign currency sovereign rating on Sri Lanka to CC from CCC. It also lowered its long-term local currency sovereign rating to CCC- from CCC.

"The outlook on the long-term ratings is negative," said the credit rating agency, adding that this reflected the high risk to commercial debt repayment in the context of Sri Lanka's economic, external and fiscal pressures.

S&P Global Ratings pointed out that although the central bank could technically create Sri Lankan rupees to meet upcoming obligations, doing so could have significant inflationary implications, with consumer prices already growing at a rapid 17.5% year-on-year in February.

"Sri Lanka's local currency debt also constitutes a considerable proportion of its overall indebtedness, and thus, its very high interest burden relative to revenues," said the credit rating agency.

S&P Global Ratings also noted that Sri Lanka's debt restructuring process was likely to be complicated and may take months to complete. "Failure to establish a sustainable government could further complicate and hinder progress in discussions with the IMF."

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