

BOX 2

Improved Global Rankings: Steppingstone for Investors

The involvement of foreign investors has been notable in Sri Lanka’s mega scale development projects related to infrastructure and private sector ventures, particularly in the last decade. However, given the persistent gap between savings and required investment, difficulties in attracting enough foreign investments remain a major bottleneck that has slowed down Sri Lanka’s journey towards development. Such difficulties have had a multifaceted impact on growth, employment and income distribution. In the current context, the unforeseeable future bundled with the global pandemic has escalated the spectrum of challenges for Sri Lanka to address, including the need to reduce overdependency on debt creating foreign inflows, in order to sustain medium to long run economic growth and stability. Against this backdrop, the country has redoubled its efforts to attract foreign direct investments (FDIs) as a key source of non-debt creating inflows. In doing so, it is crucial to improve the investment landscape, which could be done by focussing on improving Sri Lanka’s global rankings (Table B 2.1), thereby enhancing the country’s viability as a preferred destination for investors based on different aspects of socio-economic conditions.

Table B 2.1
Selected Indices for Investors

Index	Sri Lanka (Latest Ranking)	Best
Ease of Doing Business Index (2020)	99/190	New Zealand 1/190
Global Competitiveness Index (2019)	84/141	Singapore 1/141
Corruption Perception Index (2020)	94/180	Denmark 1/180 New Zealand

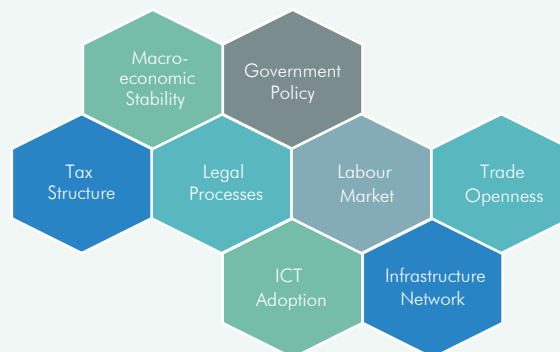
Sri Lanka was positioned at the 99th place out of 190 countries in the Ease of Doing Business Index¹ of the World Bank in 2020, advancing by one position from the ranking in 2019. An overall score of 61.8 was recorded covering 10 areas of focus. In terms of the Global Competitiveness Index² compiled by the World Economic Forum, Sri Lanka was positioned at the 84th place in 2019 out of 141 countries, and this was also an advancement of one place from the previous year. Both these reports highlight the areas of the economy, which hinder investor confidence and competitiveness. Based on the results, the followings could be highlighted as the key areas which require attention and timely redressal, not only to attract potential foreign investors, but also to facilitate domestic investments (Figure B 2.1).

Macroeconomic Stability

Maintaining macroeconomic stability, including low and stable inflation, is an important prerequisite for attracting investors. In a volatile environment, investors are unable to predict their future performance and profitability. During the past several years, with the support of prudent monetary

1 Ease of Doing Business Index is compiled by the World Bank. The latest report is available at <https://www.doingbusiness.org/en/reports/global-reports/doing-business-2020>
 2 Global Competitiveness Index is compiled by the World Economic Forum. The latest report is available at <https://www.weforum.org/reports/global-competitiveness-report-2019>

Figure B 2.1
Key Areas to Improve Investor Attractiveness



policy, inflation has been maintained in mid-single digits levels, although maintaining macroeconomic stability in terms of the performance of the external and fiscal sectors has been challenging. The country was positioned at the 118th place in 2019 in terms of macroeconomic stability in the Global Competitiveness Index, mainly due to low scores on debt dynamics. Strong commitment towards strict fiscal discipline, as envisaged in the national policy agenda, is key to improving the country’s standing on the global rankings.

Labour Market

Rigidities in the labour market is another concern of foreign investors due to mismatch of skillset, increasing cost of labour, unionisation and high compensation stemming from labour laws. Sri Lanka was ranked at the 118th position in terms of the labour market in the Global Competitiveness Index. This was driven by low scores on the ease of hiring foreign labour, internal labour mobility and redundancy costs. Investors face difficulties in terminating existing contracts under the prevailing labour laws. Further, labour mobility within the country is limited, thereby creating a lacuna in labour supply. While the protection of the workforce is essential, it must be understood that creating employment through attracting foreign investments and enhancing domestic investments is equally important. Ongoing government programmes for early identification of talent and promoting multiple vocational training programmes are expected to bear fruit in future, particularly as the country prepares for a high economic growth path. Labour market reforms will also support accruing benefits to the country with the establishment of the Colombo Port City and related development projects.

Government Policies

Economic and foreign policies of the Government have a direct bearing on foreign investor perception about the country. A stable and strong government with consistent policies will always be beneficial to establish a solid foundation for investor relations. Further, frequent reversals of the stance on existing or ongoing foreign investments



will tarnish the image of the country as an investment destination. In addition, one of the most common criticism of many governments around the world is corruption. Sri Lanka was ranked at the 94th position in the Corruption Perception Index³ in 2020 among 180 countries, whereas Denmark and New Zealand jointly have been ranked the least corrupted nations. Therefore, in establishing an investor friendly environment, strengthening the ongoing efforts to curtail corruption too is a decisive factor.

Tax Structure

A simple and effective tax system will increase the country's attractiveness for doing business. Frequent changes in the tax structure of Sri Lanka have been a critical issue faced by investors in terms of long term planning. As per the Ease of Doing Business Index in 2020, the number of tax payments by a corporate per year in Sri Lanka was 36 and the average time spent on paying taxes has been 129 hours per annum placing the country at 142nd position under paying taxes. Tax system of Sri Lanka was recently updated with a more simplified structure and the Government is keen on maintaining the current tax policy for the medium term to support the businesses. Modernisation of return submission and other services with the use of technology will help simplifying the tax systems and in turn will motivate the taxpayers to honour the tax obligations without evading. Further, the ongoing efforts to increase the use of technology in paying taxes, which was enabled through the Revenue Administration Management Information System (RAMIS), will also be beneficial. While a considerable amount of work is left to be completed, authorities are on track to bring in necessary reforms to simplify the system and improve doing business indices.

Trade Openness

Complexity of the tariff structure, prevalence of non-tariff barriers and lack of border clearance efficiency have led to very low trade openness rank of 140th position out of 141 countries in the Global Competitiveness Index. Sri Lanka's lacklustre performance in relation to regional trade blocs has been disadvantageous in connecting to global supply chain networks. In line with Government policy, all the foreign trade agreements are being revisited and necessary adjustments are expected in order to improve the bilateral trade balances with Sri Lanka's key trading partners.

Information and Communication Technology (ICT) Adoption

Sri Lanka has continued to embrace the latest technologies related to communication. However, industrial ICT adoption is not at a commendable level. The state sector usage of ICT systems is not in par with the private sector, although there have been notable improvements during the pandemic. In the Global Competitiveness Index, the country was ranked at 107th position for ICT adoption, with comparatively low usage of broadband, fibre and internet technologies. Sri Lanka has produced world class IT professionals and firms that engage in global projects. Therefore, improving the ICT systems in-house would be feasible as well as rewarding for the local talent while also reducing brain drain. Designated IT industrial zones (IT

Parks) and other targeted projects through Public-Private Partnerships have recently contributed to improve the overall level of IT adoption, and strengthening these efforts will be beneficial for investment.

Legal Processes

In terms of enforcing legal contracts, Sri Lanka was ranked at the 164th position in the Ease of Doing Business Index with an average time of 1,318 days for resolving a legal matter. Steps have been taken in the recent past to use technology for expediting the judicial processes. Preliminary work is underway to introduce e-courts and expedite the longstanding cases within a strict time frame. However, there is still a considerable progress required to improve legal processes. Releasing lands for various projects is also a tedious task for investors, due to rigidities in the land registration process and outdated laws related to land ownership. Therefore, the legal system needs to be restructured to facilitate investment. Establishment of an arbitration centre and additional Commercial Courts to resolve urgent business and investor cases would also be beneficial in improving the overall efficiency of the legal system.

Infrastructure Network

Infrastructure is one crucial element that holds together all other elements facilitating investment. A good road network and other modern commuter transport solutions, state-of-the-art seaports and airports and the provision of utilities without delays and interruptions are crucial to attract investment. During the past decade, Sri Lanka has accelerated improving the infrastructure network, hence positioning itself at the 61st place in the Global Competitiveness Index in terms of infrastructure. However, still there are concerns regarding road connectivity, efficiency of transport services and access to utilities. Addressing these concerns will contribute to attracting potential investors.

Way Forward

With unparalleled locational advantage, Sri Lanka's potential as an investment destination has been well recognised, as evidenced by the positive responses received from the global investor community, at various investor fora, roadshows and many other promotional activities carried out by Sri Lankan authorities to attract FDIs to the country. However, such positive responses have not resulted in sufficient investment inflows due to the weaknesses discussed above. The Government has already initiated a programme to improve the country's ease of doing business conditions, which will complement enhancing Sri Lanka's position in global rankings. Provision of 'One-Stop Shop' facilities for investors would support the Government's endeavours to entice investors. Meanwhile, the establishment of the Colombo Port City Commission is expected to provide a doing business environment that is in par with investment hotspots around the world, thereby raising the prospects to enhance the FDI inflows to new heights. While overcoming the complex challenges associated with the COVID-19 Pandemic, efforts must continue to address the identified weaknesses with a focussed approach, to establish the necessary steppingstones required for sustainable relationships with strategic investment partners.

³ Corruption Perception Index is compiled by Transparency International. The latest report is available at <https://www.transparency.org/en/cpi/2020/media-kit>