
New Trends in Foreign Direct Investment Inflows to Sri Lanka

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ABSTRACT

Foreign Direct Investment (FDI) has been used by developing countries as a tool to solve their economic problems in the recent past. The Sri Lankan governments followed different strategies to promote FDI after achieving independence in 1948. This paper provides an analysis the new trends of the FDI flows to Sri Lanka. Data were collected using secondary sources such as annual reports, websites and other relevant documents. Collected data analyzed using descriptive analyses methods. According to the study foreign direct investment (FDI) has been below expectations in 2010 and it has decreased in recent two years while FDI net inflows % of GDP was dramatically decreased. In addition main FDI Sources of Sri Lanka has changed the above period.

Keywords: Foreign Direct Investment, development, Economic growth

INTRODUCTION

Foreign Direct investment refers to an international investment made by a resident entity in one economy with the objective of establishing a lasting interest in an enterprise resident in another economy. There are three types of FDI, *Horizontal FDI*: Investment in the same industry abroad as a firm operates in at home, *Platform FDI*: a source country into a destination country for the purpose of exporting to a third country and *Vertical FDI*: it takes place when a firm through FDI moves upstream or downstream in different value chains i.e., when firm perform value- adding activities stage by stage in a vertical fashion in a host country. (Gupta.S, 2014)The foreign direct investor may acquire voting power of an enterprise in an economy through any of the following methods: by incorporating a wholly owned subsidiary or company anywhere, through a merger or an acquisition of an unrelated enterprise, participating in an equity joint venture with another investor or enterprise

Foreign investment can take place for many reasons, including take advantage of FDI. It can be an effective way enter into a foreign market. Some countries may extremely limit foreign company access to their domestic markets. Acquiring or starting a business in the market is a means for to gain access. FDI is also an effective way for acquiring important natural resources, such as precious metals and fossil fuels, oil etc. FDI is a means for to reduce cost of production if the labor market is cheaper and the regulations are less restrictive in the target foreign market, for example, it's a well-known fact that the shoe and clothing industries have been able to drastically reduce their costs of production by moving operations to developing countries.

FDI FLOW TO SRI LANKA

As a developing country, Sri Lankan government concerning to get attraction from foreign investor as a tool of economic development. During the British colonial period from 1815–1948, the United Kingdom was the major country of FDI in Sri Lanka. British FDIs focused on the development of tea plantation industry of the country. Fulfill the infrastructure requirements from plantation industry, British invested in banking sector, communication services and develop the railways and roads eg: investment in 1820 Colombo- Kandy road, 1831 Kandy- Mathale road, 1867 Colombo – Kandy railway. After achieving independence in 1948, Sri Lanka followed different strategies with changes in government until 1977. FDI flows were negligible as a percentage of GDCF (Gross Domestic Capital Formation) until the late 1970s. During the period of 1970-1977 the annual average inflow of FDI was only US\$ 0.5 million and it was around only 0.2% of GDCF.

After introduced open economic system in 1977, the FDI flows rapidly increased continuously until 1983. The annual average FDI inflows, as a percentage of GDCF, increased to 4.2% in the period 1978–1982(Thilakaweera B.H.P.K). In this period, government introduced several strategies to

promote international investor, those are offered the preferential tax rate and tax holidays establishment of foreign banks, removal of foreign exchange restrictions, establishment of Greater Colombo Economic Commission (GCEC). GCEC established and operated export processing Zones (EPZs), offered 100 percent foreign ownership in investment project, established Foreign Investment Advisory Committee (FICA) 1978, Free trade Zone and Board of Investment (BOI) 1978. In the 1980s with early liberalization, Sri Lanka attracted an annual average of US\$ 40 million in FDI flows, while large South Asian economies recorded lower FDI flows with respect to the size of their GDP (Thilakaweera B.H.P.K,

The impressive upward trend in FDI flow was disrupted by the escalation of ethnic problems into a civil war in 1983. Sri Lanka lost its investment potential due to the uncertainty created by the civil war. As an example, two electronic manufacturing giants, namely Motorola and Harris Corporation which obtained BOI approval to establish plants inside the Katunayake free trade Zone in 1982; withdrew their investment projects from Sri Lanka with the uncertainty created by the war.

Sri Lanka attracted significant FDI flows., with the trade and FDI liberalization in the early 1990s, power generation, telecommunication industry, infrastructure development, industrial sector were the important sectors which got attraction of foreign investor in that time, In addition, privatization program of government -owned enterprises has contributed to attracting considerable amount of FDI between 1990 and 2000((Athukorala and Jayasuriya 2004).

However the second half of the 1990s, FDI recorded a deceleration due to the external shocks and uncertainly political environment of Sri Lanka Civil ethnic problem was the affected reason for the FDI deceleration, it unable to attract much foreign direct investment on account of the war ,Sri Lanka has USD 550 million average FDI inflows during the period of 2006-2008, equivalent to about 2% from GDP(Sofat P,2009).

RESEARCH PROBLEM STATEMENT

After end of the civil ethnic problem Sri Lankan government hope to achieve its economic development. FDI is the one of key tool to solve main socio economic problems in order to achieving economic development. After introduced open economic system, Sri Lanka more liberalized it foreign policies and flowed several strategies’ to increase FDI flows. However Sri Lanka unable to achieve its FDI targets due to created uncertain environment from civil ethnic war. End of the civil war led to expectations of much higher FDI. However according to the previous FDI data, recent governments failed to get high amount of FDI inflows to the country. In this study attempt to identify the new trend of FDI inflows to Sri Lanka.

RESEARCH OBJECTIVES

Based on the problem statement the objectives of the study as follows:

Identify the new trends in FDI flows to Sri Lanka with special reference of post war period

Identify the evolutions and strategies used to get attraction for FDI after independent period in Sri Lanka

DISCUSSION

New Trends in FDI Flows to Sri Lanka

Civil war was the main obstacles to get attraction on FDI until 2009. While the end of the civil war led to expectations of much higher FDI. However FDI slightly increased until 2015 and decreased after 2015 As indicates Table 1 and Figure 1

Table1. *FDI flows to Sri Lanka 2012-2016*

Year	FDI (US\$ Million)
July2012	201
January 2013	283
January2014	386
January 2015	388
January 2016	309

Source: <http://data.worldbank.org/indicators>

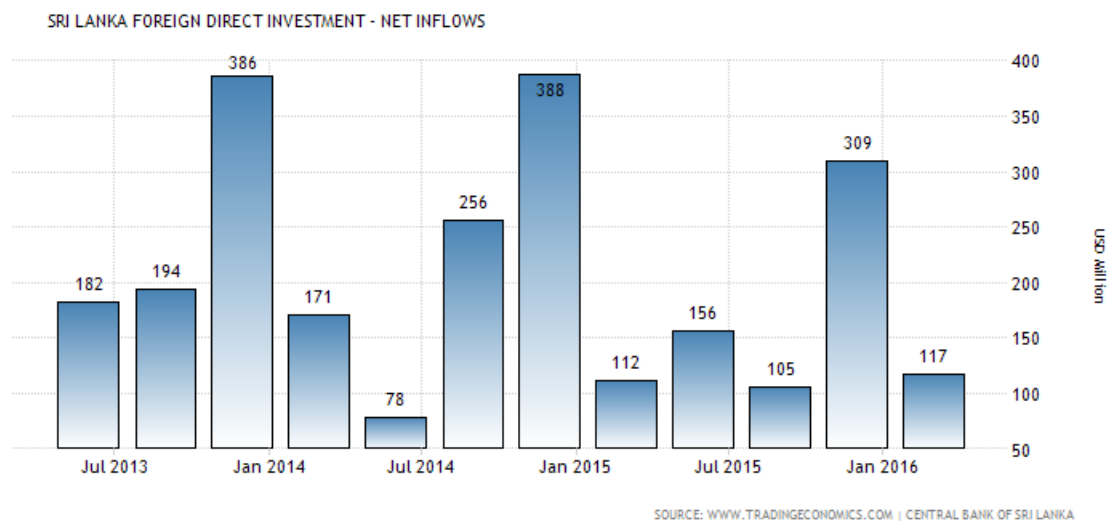


Figure1. FDI flows to Sri Lanka 2013-2016

Sri Lanka Foreign Direct Investment, Net inflows (% of GDP)

Foreign direct investment; net inflows (% of GDP) in Sri Lanka was last measured at 0.8 in 2015. According to World Bank data as shown in table 2, the contribution of FDI to gross domestic products rapidly decreased after 2008. Board of Investment of Sri Lanka expected the significant contribution to GDP by FDI inflows with peaceful environment due to end of civil war. However, contribution of FDI net inflows to GDP showed downward trend as indicated in the table 2.

Table2. Foreign direct investment, net inflows (% of GDP)

Year	FDI net inflow % of GDP
2008	1.86
2011	1.5
2012	1.4
2013	1.3
2014	1.2
2015	0.8

Source: <http://data.worldbank.org/indicators>

Table 3 presents the top sources of FDI flow to Sri Lanka. Netherlands is the main sources for FDI flows as followed by U.K, Malaysia, Switzerland and Mauritius are the other important source for FDI flows. Before 2014 China was the one of main country which invest in the many projects in Sri Lanka. However with the government changes, importance of the china as a main sources, has been changed.

Table3. Top Sources of FDI Flow to Sri Lanka in 2014

Country	Amount	Percentage from Total Inward
Netherlands	1851	21
U.K	1131	13
Malaysia	841	09
Switzerland	829	09
Mauritius	783	09

CONCLUSION

As a developing country, Sri Lankan governments flowed different strategies’ to increase FDI flows to after achieving independence in 1948. FDI used as a tool of economic development and solution for economic issues which facing by governments. Civil ethnic problem was the main barrier to get attraction from foreign investors after 1980. While the end of the civil war led to expectations of much higher FDI flows to Sri Lanka. Recants government was expected to get high

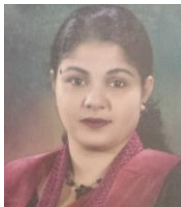
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amount of FDI inflows from different countries due to created peaceful environment. After 2010. However, Peace and security were necessary conditions, but not only sufficient conditions to attract foreign investment to recent past There are many factors that have to get attract FDI. It is important to ensure an attractive investment environment. Consistent macroeconomic policies and government polices, good governance, economic stability, guarantee of property rights, rule of law and absence of corruption are among the conditions required to attract FDI. Consistency and predictability in political stability and economic policies are preconditions to attract FDI.

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