

## Large fiscal and current account deficits



### General Information

GDP	USD59.4 billion (World ranking 69, World Bank 2012)
Population	20.33 million (World ranking 57, World Bank 2012)
Form of state	Republic
Head of government	Mahinda Percy RAJAPAKSA
Next elections	2016, presidential and legislative



### Strengths

- Sound economic growth, despite the currency crisis of 2000/2001 and global downturn in 2009
- Tourism revenues and workers' remittances provide hard currency inflows
- Economic policies are broadly supportive of business and economic growth

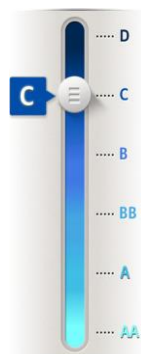
### Weaknesses

- Ethnic tensions remain a threat to stability and growth prospects
- Fractured nature of the political system, with generally weak coalition governments
- Vulnerability of export base (42% textiles and clothing)
- Relatively strong inflationary pressures
- Large fiscal deficits and high public debt
- Banking system weaknesses
- Large current account deficits since 2011

### Country Rating

C3

#### Country Grade



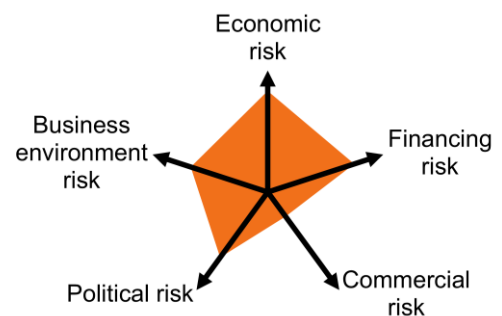
High risk

#### Country Risk Level



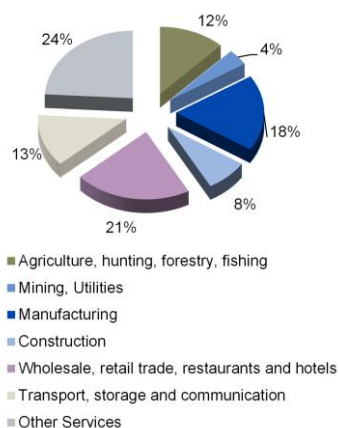
Low risk

### Risk Dimensions



## Economic Structure

### GDP breakdown (2011)



Sources: UnctadStat, IHS Global Insight, Euler Hermes

### Trade structure (% of total, 2011)

Exports	Rank	Imports
United States	21% 1	24% India
United Kingdom	11% 2	16% China
Italy	6% 3	7% Singapore
Belgium	5% 4	7% Iran (Islamic Republic of)
India	5% 5	5% Japan

Exports	Rank	Imports
Articles of apparel & clothing accessories	42% 1	19% Petroleum, petroleum products and related materials
Coffee, tea, cocoa, spices, and manufactures thereof	17% 2	11% Textile yarn and related products
Rubber manufactures, n.e.s.	7% 3	10% Road vehicles
Non-metallic mineral manufactures, n.e.s.	5% 4	5% Non-metallic mineral manufactures, n.e.s.
Miscellaneous manufactured articles, n.e.s.	4% 5	3% Specialised machinery

## Economic Forecast

	2009	2010	2011	2012	2013f	2014f
GDP growth (% change)	3.5	8.0	8.2	6.3	6.3	6.8
Inflation (% end-year)	5.0	6.8	4.9	9.2	8.0	6.5
Fiscal balance (% of GDP)	-9.9	-8.0	-6.9	-6.5	-5.8	-5.5
Public debt (% of GDP)	86.1	81.9	78.5	79.3	79.9	78.0
Current account (% of GDP)	-0.7	-2.3	-7.9	-5.8	-5.7	-5.2
External debt (% of GDP)	42.4	42.7	40.5	48.7	49.3	50.7

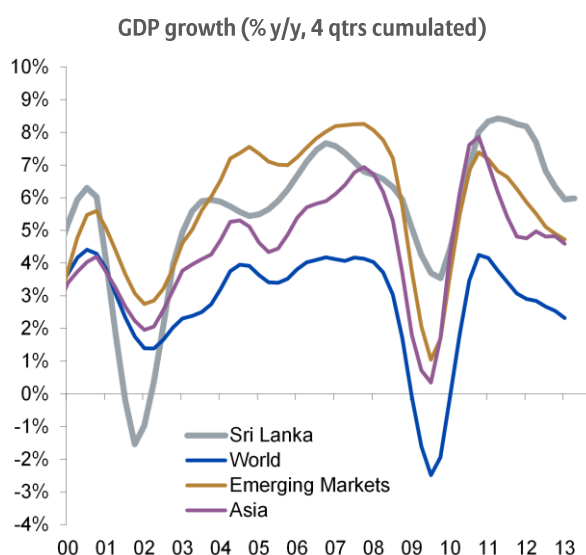
Source: IHS Global Insight, national sources, Euler Hermes

## Economic Overview

Annual real GDP growth decelerated from around +8% in 2010-2011 to +6.3% in 2012, as a result of a sharp slowdown in external trade activity and some monetary tightening. Real exports contracted by -1.9% in 2012 (+10.8% in 2011) and real imports by -4.6% (+27% in 2011). Details on domestic demand are not available, but private consumption is a key growth driver, fuelled by rising incomes and workers remittances. EH forecasts annual GDP growth of about +6.3% in 2013, as global demand remains subdued, and an acceleration to +6.8% in 2014.

Headline inflation accelerated from 4.9% at end-2011 to 9.2% at end-2012 and 9.8% y/y in February 2013, before easing to 6.1% y/y in July 2013. The key policy interest rate was accordingly raised from 7% at end-2011 to 7.75% in April 2012. From December 2012 to May 2013, the rate has been cut in two steps to 7% as inflationary pressures have declined. Private sector credit growth has fallen from unsustainably high 35% y/y at end-2011 to reasonable 9% y/y in May 2013.

Public finances are very weak and remain a cause of concern. Fiscal deficits have always been large, recording an annual average of around 8% of GDP in 1990-2010. More recently, the annual deficit is estimated to have declined somewhat to 6.9% of GDP in 2011 and 6.5% in 2012 and is forecast to decrease to just below 6% in 2013-2014. Public debt has slightly fallen from a record high of 103% of GDP in 2001 but

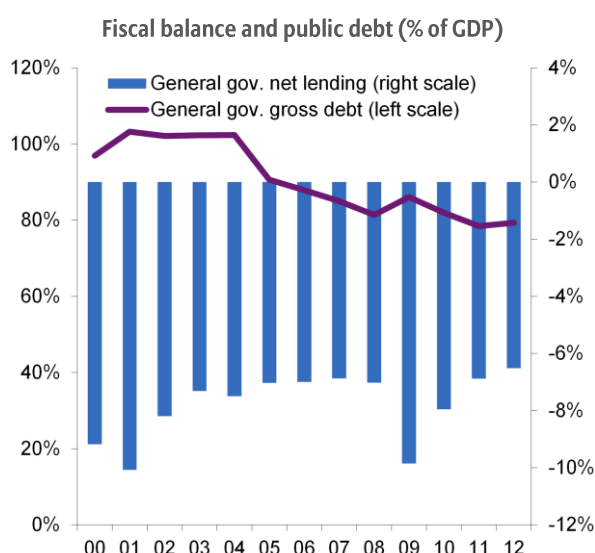


Sources: IHS Global Insight, Euler Hermes

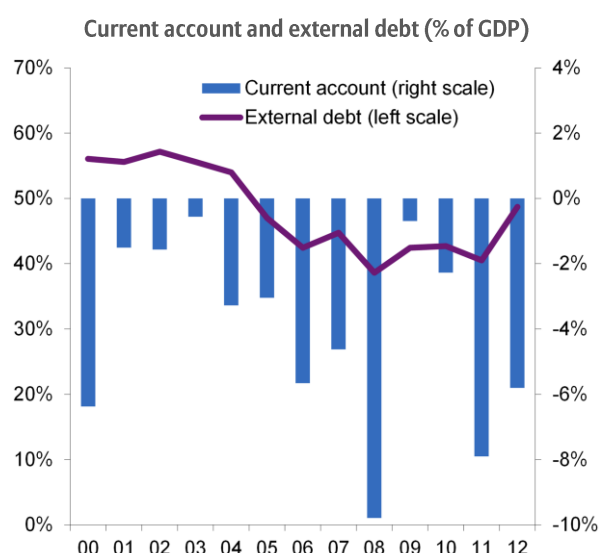
## Economic Overview (continued)

has remained high overall at around 80% of GDP currently. Moreover, the debt structure has deteriorated as the share of external public debt has risen to almost 50% from 40% in 2008.

The external position is also weak. The current account deficit widened markedly to 7.9% of GDP in 2011 and remained large at an estimated 5.8% in 2012. The reason was a sharply deteriorating trade deficit while net workers' remittances inflows reached around 8% of GDP. EH forecasts the current account deficit to remain above 5% of GDP in 2013-2014. Gross external debt is relatively high at around 50% of GDP or 150% of export earnings. Foreign exchange reserves have recently fallen from USD7.1bn in August 2012 to USD5.8bn in May 2013, such that import cover has declined to just below three months.



Sources: IHS Global Insight, Euler Hermes



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