



Pathfinder Economic Alert

## **All the World is a Pond: We Cannot Afford to Opt Out.**

### **Emerging Political and Diplomatic Tensions**

The ongoing sessions of the UN Human Rights Council (UNHRC) have raised a number of issues regarding the conduct of Sri Lanka's international relations. The Pathfinder Foundation (PF) does not wish to get involved in areas of politics, diplomacy or human rights. However, the course of the country's international relations will have a crucial bearing on its economic prospects. There are serious concerns that have arisen about the policies and actions of the US, Europe and India, as well as some other countries that are likely to support the US sponsored Resolution. Sri Lanka already has advantageous economic relations with a number of these countries, or has the potential to do so in the future. Therefore, political, diplomatic or human rights issues need to be addressed in a pragmatic manner that best serves Sri Lanka's national economic interests, in a context of mutual respect. It is important not to let them have a negative impact on the economic arena in a manner that fundamentally compromises the country's future prospects.

### **Sri Lanka's Dependence on the World Economy: No Way Out**

In this context, it is useful to examine Sri Lanka's national economic interests at this particular juncture in the country's history, particularly in relation to the US, Europe and India. About 55% of Sri Lanka's exports go to the US and EU. Almost all apparel exports, US \$ 3991 billion which accounts for 41% of total exports are directed to these markets. In addition, US institutional investors hold 40% of the Sri Lankan bonds issued in international capital markets (\$ 3billion) and 80% of the domestic Treasury Bills and Bonds held by foreigners (\$3.4 billion). In addition, US institutional investors have also contributed to the net inflow of investment into the Colombo Stock Exchange in recent months. At a time when reliance on external borrowing has been increasing sharply and risks associated with the imbalance in the trade account have been elevated, Sri Lanka must ensure that its economic relations are further strengthened with the key markets. It is important to note that a loss of confidence on the part of US institutional investors and apparel buyers would have a very damaging impact on the economy.

The loss of GSP+ has already resulted in a loss of export earnings and domestic employment. Any further decrease in access to European markets will exacerbate this trend.

## **The Reality Whether We Like It or Not.**

India has now become a major source of investment and competitively priced imports. Furthermore, any realistic strategy to boost investment and exports in the medium to long term would have to place India too at its centre. In an increasingly multi-polar world characterized by rising regionalism, economic geography will inevitably gain greater importance. As a result, Sri Lanka's future economic prospects are closely linked to proximity to the large and fast-growing Indian market. This is a reality that cannot be escaped. Pursuing Sri Lanka's national economic interests makes it essential that bilateral economic relations with India are on a sound footing on the basis of mutual respect.

## **No Permanent Enemies but Economic Interests**

History is replete with instances of countries which were at war with each other subsequently establishing close and fruitful trade and investment relations. China and South Korea, which were subject to years of war and occupation by Japan, today maintain a high level of mutually beneficial relations. During the Vietnam War, the Americans killed and maimed hundreds of thousands of Vietnamese mostly through bombing and the use of chemical weapons, such as "Agent Orange." The Viet Cong retaliation was equally brutal until they drove away the foreign forces from the country. At the end of the Vietnam War, no one in US or Vietnam would have ever imagined the volume of American investment today enjoying special incentives granted by the Vietnamese government, which has laid out a red carpet for investors from its former enemy. During two World Wars, Germany and France, as well as other parts of Europe, waged brutal war. Today, they have joined together in the European Union, which goes beyond economic relations and pools sovereignty of individual countries for the common good. Of course, all these military confrontations, involved violence, a violation of norms and ethics and crimes against humanity. Notwithstanding these brutal past experiences, these countries are currently enjoying robust economic relations. The Americans, who bombed Hiroshima and Nagasaki killings hundreds of thousands of people during WW II, invested heavily in the Japanese economy during the 60's, 70's and 80's. They will continue to do so. Similarly Japanese investment in the US has been substantial. Trade between the two countries has also flourished. In addition, trade and investment is burgeoning between China and India and there is a growing relationship between the defense establishments of the two countries after many years of tense bilateral relations and a border war. All this demonstrates that it is well to remember the fundamental axiom in international relations: *countries do not have permanent enemies' only permanent interests.*

## **Recipe for Success: Economic Pragmatism**

The lesson to be learnt is that even if political or diplomatic differences, or even confrontations, are encountered with countries that are potential sources of trade, investment and tourism, it is important to tread cautiously so that the country's economic interests are not adversely affected.

Pragmatism rather than ideology or emotion should drive the country's international relations. That has been the recipe followed by all the successful countries in Asia.

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