

THE IMPACT OF DIRECT FOREIGN INVESTMENT ON ECONOMIC GROWTH IN SRI LANKA

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Globalization offers an unprecedented opportunity for developing countries to achieve faster economic growth through trade and investment. As a result of this rapid globalization process, the integration of developing countries with the global economy increased sharply in the last few decades due to the lowering of barriers in trade and investment. Foreign Direct Investment (FDI) provides much needed resources to developing countries such as capital, technology, managerial skills, entrepreneurial ability, access to markets etc. These are essential for developing countries like Sri Lanka to industrialize, develop, and create jobs to reduce the poverty situation in their countries. In this context, most developing countries have recognized the potential value of FDI and have liberalized their investment regimes.

Since the beginning of its liberalization process Sri Lanka has offered attractive investment opportunities for foreign companies and has adopted a number of policies and provided generous incentives to attract foreign direct investment into the country. The country seems to offer perhaps one of the most liberal FDI regimes in South Asia. As a result, during the last decade FDI inflows in Sri Lanka has increased considerably by 8.5 in 1990 to 15.0 in 2000 as a percentage of GDP while Indian experience was 0.5 to 4.1 in the same period.

Against this backdrop, this paper focuses on the FDI-led growth hypothesis in the case of Sri Lanka, a country which has become one of the major FDI recipient countries in South Asia. The methodology involves estimating a econometric model (Distributed Lag Model) based upon macro time series data and response of civil society, foreign firms in and around Palallekele Industrial Zone. Their result shows that there is a positive relationship between FDI and economic growth in Sri Lanka. Its analysis increases the confidence in the belief that FDI accelerates GDP growth. Perception of the civil society regarding the impact of FDI is positive and net attitudes of foreign firms toward FDI reveals that the investment climate has not improved in Sri Lanka due to lack of good governance, corruption, political instability and disturbance, bureaucratic inertia and the poor law and order situation.