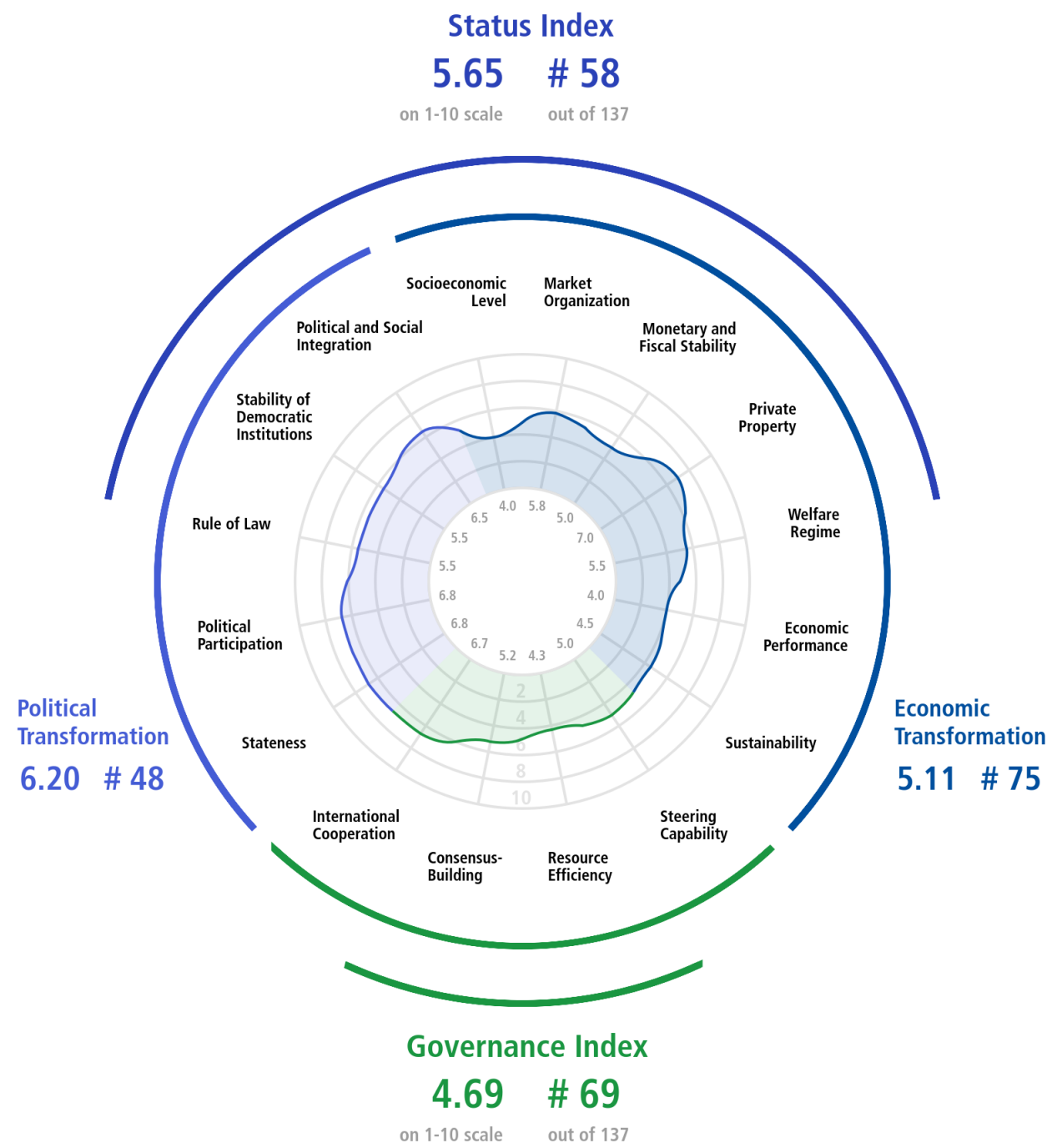


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Sri Lanka



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Key Indicators

Population	M	22.2	HDI	0.782	GDP p.c., PPP \$	14405
Pop. growth ¹	% p.a.	0.1	HDI rank of 189	73	Gini Index	37.7
Life expectancy	years	76.4	UN Education Index	0.754	Poverty ³	11.3
Urban population	%	19.0	Gender inequality ²	0.383	Aid per capita \$	6.9

Sources (as of December 2023): The World Bank, World Development Indicators | UNDP, Human Development Report 2021-22. Footnotes: (1) Average annual growth rate. (2) Gender Inequality Index (GII). (3) Percentage of population living on less than \$3.65 a day at 2017 international prices.

Executive Summary

The period under review witnessed significant economic and political upheavals that could have a lasting impact on Sri Lanka's democratic trajectory and economic stability. This period was underpinned by a crisis in governance, both in terms of the abject failure of the incumbents and the erosion of the population's confidence in governing institutions.

The COVID-19 pandemic severely impacted the economy, which was only starting to recover from the shock of the Easter Sunday attacks in April 2019. Even before the attacks, the economy had stagnated with low growth rates and low investor confidence. Despite the World Bank's classification of Sri Lanka as an upper-middle-income country in July 2019, investors remained circumspect due to substantial debt repayments due between 2019 and 2024, which put pressure on public finance and foreign reserves. Reduced global demand for Sri Lankan exports, supply chain issues and reduced tourist traffic also adversely impacted Sri Lanka.

Rather than taking remedial steps, the Sri Lanka Podujana Party (SLPP) government led by Gotabaya Rajapaksa continued on its disastrous trajectory of tax cuts, which significantly reduced government revenue, increased government spending, and utilized the Central Bank of Sri Lanka (CBSL) to intervene aggressively by directly financing fiscal expenditure while suppressing interest rates.

The government obfuscated and outright lied about the economic situation, even while people were stuck in fuel lines for days. Several individuals died waiting for fuel, facing 12-hour power cuts, a lack of essential medicine in hospitals due to U.S. dollar shortages, and rampant food insecurity owing to a shortsighted organic fertilizer drive that reduced crop yields. These mistakes culminated in large-scale citizen protests across the country.

The protests enjoyed widespread support. A survey revealed that nearly half of the respondents (48.5%) claimed that either they or a member of their immediate family had participated in the protests organized against those responsible for the economic crisis. The protests were peaceful for the most part, until SLPP supporters marched from the prime minister's office on May 9, 2022, and brutally attacked the protesters while the police looked on. The protests led to the removal of the CBSL governor, a political appointee with a checkered record, who strongly opposed approaching the IMF. Once this governor had left office, Sri Lanka sought an extended fund facility from the IMF. In April 2022, Sri Lanka also suspended debt repayments to preserve foreign currency reserves and maintain essential services.

The protests continued unabated and forced Prime Minister Mahinda Rajapaksa and President Gotabaya Rajapaksa, his brother, to resign in May and July 2022, respectively. This was an unprecedented event in Sri Lankan democracy, mainly because of the power the Rajapaksa family wielded in Sri Lankan politics and the power of the executive presidency.

Through this process, Ranil Wickremesinghe, the sole member of parliament from the United National Party, successfully positioned himself to assume the presidency and was elected by the parliament to serve the remainder of Gotabaya Rajapaksa's term. Immediately after taking office, Wickremesinghe declared a state of emergency and deployed the police and military to disperse protesters using force. Additionally, he launched a focused campaign portraying the protesters as anarchists and subversive forces, while presenting himself as a competent leader capable of restoring stability and fostering economic recovery.

During Wickremesinghe's presidency, Sri Lanka made progress in obtaining the IMF extended fund facility and met all IMF conditionalities except those relating to debt sustainability. The main issue in this regard is the unwillingness of the People's Republic of China (PRC) to provide guarantees on debt restructuring. Wickremesinghe pushed through several reforms, including reversing the disastrous tax policy of the previous president. However, he continues to crack down on civil liberties and is using IMF conditionalities as an alibi for extra-constitutional maneuvers to postpone elections. This is an extremely dangerous trend for both democratic governance and the economic recovery of the country. Postponing elections would trigger a popular backlash, particularly against the IMF, and could lead to further cycles of violence.

History and Characteristics of Transformation

The Democratic Socialist Republic of Sri Lanka is an island nation in South Asia, located in close proximity to India. From the 16th century onwards, it was under the colonial rule of the Portuguese, the Dutch, and the English, from whom it gained independence in 1948. The majority ethnic community in Sri Lanka is the Sinhalese (74.9%), while the Sri Lankan Tamils are the largest minority community (11.15%) and live predominantly in the northern and eastern provinces of the island. A significant portion of the Muslim community lives in the eastern province, but they are generally more evenly distributed across all nine provinces of Sri Lanka (9.3%). The Upcountry Tamil community lives predominantly in the central highlands of Sri Lanka (4.12%).

The United National Party (UNP) was the first political party to form a government in independent Sri Lanka. In the 1950s, SWRD Bandaranaike broke away from the UNP and formed the Sri Lanka Freedom Party (SLFP). The UNP and SLFP formed governments in turn between 1948 and 2015. Post-2015, the political party system became increasingly complicated with a faction of the SLFP breaking away to form the Sri Lanka Podujana Peramuna (SLPP) under the leadership of Mahinda Rajapaksa, who was president between 2005 and 2015 and under whose leadership the civil war ended in 2009. Gotabaya Rajapaksa, brother of Mahinda, won the 2019 presidential election. Ranil Wickremesinghe had been the leader of the UNP since 1994. After the 2019 presidential election, a large section of the UNP broke away and formed the party Samagi Jana Balawegaya.

Sri Lanka's post-independence history is marked by turbulent political contests over the nature of the state, several racial pogroms, two youth-led Marxist insurrections, and a three-decade-long civil war that ended in May 2009. The civil war was triggered by the secessionist claim first articulated by Sri Lankan Tamil politicians in 1976 and later adopted by armed insurgents. These secessionist claims arose from discriminatory policies implemented by Sinhalese politicians, which alienated many Sri Lankan Tamils. These policies included rendering a majority of the Upcountry Tamils stateless through the Citizenship Act in 1948 and making Sinhala the only official language in 1956. Additionally, Sri Lanka's first autochthonous constitution in 1972 ignored the representations made by Tamil-elected representatives, solidifying the unitary nature of the state and granting special constitutional recognition to Buddhism. The education standardization policies in the 1970s further restricted Tamil students' access to certain areas of university education.

The second republican constitution was enacted in 1978, establishing a powerful executive presidential system of government with limited separation of powers and a weak parliament. Both autochthonous constitutions were drafted by the governing party with limited input from opposition politicians and no participation from Tamil politicians.

In 1948, Sri Lanka was a state dependent on the plantation sector for much of its revenue. Sri Lankan politicians maintained the well-developed health care system that they inherited, and they vastly expanded secondary education by providing free public education (since 1943). On the other hand, they also inherited a weak industrial sector and had to make heavy investments in agriculture to reduce the country's dependence on food imports. A development model of import substitution and economic development through public sector companies was attempted until 1977. From 1977 on, market-oriented reforms were gradually adopted. Successive governments have pursued privatization, public sector reforms, and the liberalization of trade and capital movements to different degrees. The state remains actively involved in economic activities through state-owned enterprises and by providing services such as education and health care.

The BTI combines text analysis and numerical assessments. The score for each question is provided below its respective title. The scale ranges from 1 (worst) to 10 (best).

Transformation Status

I. Political Transformation

1 | Stateness

The state's monopoly on the use of physical force is unchallenged. However, the severe economic hardships that resulted from the severe economic mismanagement by the Sri Lanka Podujana Peramuna (SLPP)-led government resulted in large-scale civil protests. The focal location of the protests was the "Galle Face Green," the largest open space in Colombo, in front of the presidential secretariat.

Violence was unleashed on the protesters on May 9, 2022, when a mob of political affiliates of then-incumbent Prime Minister Mahinda Rajapaksa marched from the prime minister's office to the "Galle Face Green" and attacked the protesters, while being observed by the police. Violence spread across the country on the same evening, with houses of SLPP politicians in particular being attacked and burned. One SLPP member of parliament was killed by an angry mob. The prime minister resigned in the aftermath of the violence, which subsided the next day.

Widespread protests occurred again in July 2022, forcing President Gotabaya Rajapaksa to flee the country and eventually resign. Some protesters occupied the president's official residence and the presidential secretariat for several days during this period. This was after several declarations of states of emergency and a curfew, which were widely ignored by the public at large.

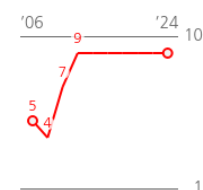
After President Rajapaksa fled, Ranil Wickremesinghe, who was made prime minister after Gotabaya's brother Mahinda Rajapaksa stepped down from that position, was elected president by parliament. The period immediately after Gotabaya Rajapaksa's departure saw the protests take a violent turn. This was used by President Wickremesinghe to justify a crackdown on protests throughout the country with the help of the police and military.

The manner in which the government used the security forces to crack down on protesters and return to the status quo highlights the extent to which the state continues to maintain a monopoly on the use of force since the civil war ended in 2009.

Question
Score

Monopoly on the
use of force

9



The right to citizenship is not denied based on ethnicity, religion, gender or political reasons, although citizenship through naturalization remains heavily regulated and difficult to obtain. Post-independence (i.e., after 1948) citizenship legislation rendered a significant section of the Upcountry Tamil community stateless. However, the legal issues relating to the community's citizenship have been resolved through legislation enacted between 1986 and 2009. Partly to generate revenue, the government now promotes dual citizenship, and the Tamil diaspora can now obtain such status more easily compared to during the Rajapaksa reign.

However, Sri Lanka continues to be a deeply divided society marred by ethnoreligious and linguistic tensions. Many of the ethnoreligious-linguistic fault lines, especially between the Sinhala-speaking Sinhala Buddhist majority and the Tamil-speaking Sri Lankan Tamil minority, which led to a 30-year civil war, continue to be a source of conflict even after the armed conflict ended in May 2009. Anti-Muslim sentiment, which permeated popular discourse in the aftermath of the Easter Sunday attacks, continues to linger. The government forcibly cremated all those suspected of dying of COVID-19 and only reversed the policy, which was widely discredited and seen as targeting individuals of Islamic faith, in March 2022.

These tensions, however, were overshadowed by the economic crisis that unfolded throughout 2022, and the protests that ousted the former president saw widespread support across ethnoreligious and linguistic divisions.

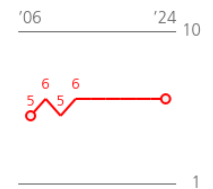
The questioning of the state's legitimacy can be observed among minorities for not being treated equally. This is especially the case for Sri Lankan Tamils and Upcountry Tamils.

The constitution specifies that "The Republic of Sri Lanka shall give to Buddhism the foremost place," although it also safeguards the freedom to have or adopt a religion of one's choice and the freedom to teach and practice one's religion in public or private. Sri Lanka's four major religions (Buddhism, Hinduism, Islam and Christianity) are all supported by state funds. Nonetheless, the dominant political view among the Sinhalese majority is that the Sinhala-Buddhist identity is inextricable from the national identity. Aggressive rhetoric by some Buddhist nationalists against Muslim and Christian minorities has continued during the review period. Buddhist monks (known as the Sangha) have historically enjoyed significant state patronage, including being consulted on major political decisions by elected representatives.

The prominence afforded to Buddhist monks on issues of government policy by the previous president has been reduced. However, Buddhist monks continue to be influential and vocal on important national policy issues. For example, they pressure the government not to implement several provisions of the constitution relating to devolution of power and not to reduce the excessive military presence in the Tamil-dominated north of the country.

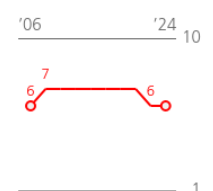
State identity

6



No interference of religious dogmas

6



Influential Muslim religious leaders continue to block reform of the Muslim Marriage and Divorce Act, despite several inconsistencies with basic human rights guaranteed by the constitution. The reforms aimed to enable female judges to sit in the specialized courts established by the act, increase the minimum age of marriage for women to 18 and, lastly, prevent polygamy.

With the bureaucracy and military being Sinhala-dominated, the vast majority of Sinhalese Buddhists support majoritarianism. While they may be embarrassed by how certain Buddhist monks behave, they nevertheless tend to support their monks' demands rooted in Sinhalese Buddhist majoritarianism.

Sri Lanka's administration is primarily controlled by the central government, with limited functions devolved to provincial councils established in 1987 and local authorities.

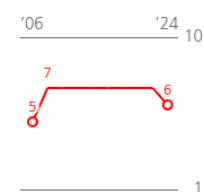
The country's administrative structures, especially those providing basic health and educational services to all regions, saw a significant deterioration during the review period. Sri Lanka experienced severe fuel shortages during the period, forcing the government to effectively shut down the country for some periods and subsequently to ration fuel. The health sector has been acutely impacted by shortages of essential medicine and human resources, and long-standing imbalances in the provision of these facilities were further exacerbated by the economic crisis. Sri Lanka has seen an exodus of trained health care professionals, such as nurses and doctors. The exact numbers are unknown as the government claims it does not collect this data. Furthermore, the adverse impacts of the economic crisis intertwine with the significant disruptions caused by the COVID-19 pandemic in the previous two years.

According to the World Bank World Development Indicators 2022, 92.2% of the population had access to at least a basic water source in 2020, 93.7% to at least basic sanitation, and 100% to electricity. However, the review period saw serious challenges to the supply of these services due to the severe economic crisis. Prolonged power cuts across the country, sometimes lasting for up to 12 hours a day, and the subsequent sudden and drastic increase in utility prices caused significant reductions in access to basic utilities, including electricity and water.

Additionally, choices made by the government in order to meet the reform conditions set by the IMF, including cutting government expenditure, have adversely affected the provision of government services and could potentially exacerbate existing problems.

Basic
administration

6



2 | Political Participation

National elections have been regularly conducted based on universal suffrage through multiparty contests, and election outcomes are respected. The last presidential and parliamentary elections were held in November 2019 and August 2020, respectively. Both elections were widely considered to be free and fair.

However, provincial council (second-tier devolved government) elections have not been held since 2014. This is due to an amendment to the election law enacted by then-Prime Minister Wickremesinghe's government in 2017, which made it virtually impossible to hold provincial council elections. No measures have been taken to date to rectify this legal impediment.

The terms of local authorities are due to lapse in March 2023. The election management body (the Elections Commission) had called for nominations and set the date of the poll for elections across the entire country as March 9, 2023. However, the government has repeatedly created roadblocks in this process and refused to release funds to government agencies for the election, citing the economic crisis. This despite funds being allocated to the March 2023 local government elections in the December 2022 budget.

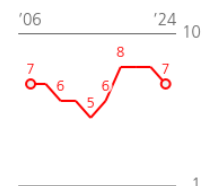
The structural changes that were made to the Elections Commission by the 20th amendment to the constitution during the previous review cycle have been reversed by a subsequent constitutional amendment. Thus, the president no longer has complete control over appointing the members of the Elections Commission. However, the Election Commission appointed by the previous president by the 20th amendment to the constitution remains in place until a new commission is constituted. Democratically elected officials are able to implement their policies. The president, who is usually directly elected by the people, wields extensive powers within the executive and over the legislature. President Wickremesinghe was elected by the parliament to serve out the remainder of Gotabaya Rajapaksa's term.

There are no extra-constitutional veto powers, but the military and Buddhist establishment are influential players. The Buddhist Advisory Council, established in the previous review cycle, has been effectively dissolved. Since 2001, political parties composed of Buddhist monks have played an important role in the parliament and the political process, despite having mixed results in elections. They continue to enjoy significant sway over the government on important national issues concerning economics and international cooperation.

With sweeping economic reforms likely to take place during the next year, the government could face increasing opposition from trade unions and the general public, including through large-scale citizen mobilization and protests. President Wickremesinghe's aggressive suppression of protests, his reluctance to hold elections before 2024 and his political limitations could all fuel such protests and mass mobilization.

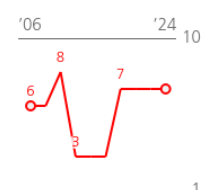
Free and fair elections

7



Effective power to govern

7



The review period saw several instances in which states of emergency were declared in order to restrict freedom of association and assembly, which are usually guaranteed by the constitution. These declarations were implemented without considering procedural safeguards placed in the constitution and were consequently all challenged before the Supreme Court, with cases ongoing as of February 2023.

Extensive surveillance was deployed in parts of the country and is routinely used as a deterrent to free association and assembly in the northern and eastern provinces. The practice of the police to obtain ex-parte orders from the magistrate's court, in order to prevent protests and demonstrations on the grounds of public nuisance, also intensified. However, there has been a notable pushback from the judiciary, which has refused many such applications by the police.

Large-scale citizen mobilizations occurred during March and July 2022, in spite of attempts by the executive to curtail freedom of assembly. However, with President Wickremesinghe taking office, the police and military have been deployed to disperse protests with the use of force. One of the first decisions of President Wickremesinghe upon taking office was to clear protesters occupying the Galle Face Green protest site through the use of military force. His administration has also targeted individuals perceived as protest leaders through the Prevention of Terrorism Act. This allowed the police to hold individuals without required charges or evidence for up to 12 months and is also used as a deterrent to other citizens.

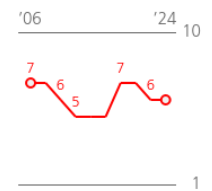
Freedom of association is guaranteed to trade unions, both in the constitution and through acts of parliament, although this has been restricted through the use of emergency laws. Additionally, the surveillance of civil society activities, especially in the northern province, continues unabated.

Freedom of expression is protected by the constitution. The review period saw the arrests of and investigations into several internet-based media outlets and their journalists, as well as a one-day deactivation of social media to prevent citizens from organizing protests. However, this was circumvented by citizens using virtual private networks (VPNs).

There is no official government censor. However, mainstream media practices a policy of self-censorship as evidenced by the lack of reporting on certain issues, particularly in relation to the security forces. State media is fully controlled by the government and has been for several decades. Private media institutions became more critical of the government following the economic collapse and resulting nationwide protests. However, partisan political agendas continue to permeate private media institutions, which are controlled by a select few individuals with their own political ambitions.

Association / assembly rights

6



Freedom of expression

7



Law enforcement continues to use the prohibition of incitement to war in the International Covenant on Civil and Political Rights (ICCPR) Act, No. 56 of 2007, and the provisions of the Prevention of Terrorism Act (PTA), to arrest and detain persons expressing legitimate political opinions, especially on social media. These laws provide for long detention periods at the discretion of the executive, with little judicial oversight. The threat of arbitrary arrest and prolonged detention without charge under these laws incentivizes self-censorship.

The Right to Information (RTI) Law was enacted in 2016. Attempts were made to compromise the independence of the RTI Commission. However, the RTI Commission has resisted these attempts and continues to function in a robust manner.

3 | Rule of Law

Due to the large-scale protests, which led to the resignation of the former president, parliament moved to repeal the 20th amendment to the constitution. In October 2022, parliament enacted the 21st amendment to the constitution, which reverted the constitution to the status quo that existed under the 19th amendment to the constitution.

The 21st amendment reduced the powers of the president to make key appointments to institutions that are envisaged as checks on executive power. These institutions include independent commissions such as the Human Rights Commission of Sri Lanka and important appointments such as judges of the higher judiciary, the attorney general and the auditor-general. The president's power is limited by his dependence on the approval of a multiparty body known as the constitutional council prior to making such appointments. An important change from the 19th amendment to the 21st amendment is that the president gains more power over the prime minister.

All four constitutional amendments since the year 2010 have undone the changes made by the previous amendment. Sri Lanka has thus oscillated between reducing the power of the presidency and drastically increasing it. This trend also explains part of the difficulties in ensuring meaningful checks and balances in the Sri Lankan constitution.

The appointment procedure for the judiciary was severely compromised by the 20th amendment to the constitution, which gave the president sole discretion to make appointments. Despite these changes in the previous cycle, all appointments to the higher judiciary made by President Gotabaya Rajapaksa during the present review cycle were based on seniority from among career judges and officers of the attorney general's department.

Separation of powers

5



Independent judiciary

7



Furthermore, these changes to the appointment procedure were reversed in October 2022, toward the end of the review period, with the president now being required to obtain approval from the constitutional council for a nominee prior to any appointment being made. There are no specific qualifications required to be appointed as a judge of the Supreme Court or Court of Appeal. However, such appointments are only made from among career judges, officers of the attorney general's department and, on occasion, lawyers who are not from the attorney general's department.

The jurisprudence of the Supreme Court has been mixed, with several prominent examples of it asserting itself against executive overreach, especially in cases involving corruption and the abuse of public resources. However, the Supreme Court and Court of Appeal have mostly continued to be deferential to the executive on issues relating to national security, law and order.

The oscillation between different appointment procedures has made it difficult to analyze the long-term trajectory of the judiciary. The executive and parliament continue to have disproportionate influence over the judiciary, especially in relation to the impeachment of judges and post-retirement appointments.

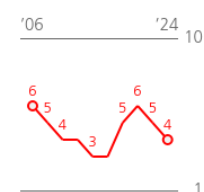
Lastly, judicial corruption remains an issue in Sri Lanka. It was highlighted by Sugandhika Fernando, a young Sri Lankan lawyer who produced a whistleblowing video in 2018, whose allegations ranged from drunken lawyers and officers in court administration to the payment of bribes to judges to influence their verdicts.

Over the past several decades, Sri Lanka has seen little successful prosecution and conviction of high-level political figures on corruption charges. There is, however, the widespread perception that senior politicians in successive governments have been corrupt. Problematically, very few have been prosecuted, with even fewer of these cases resulting in convictions. For instance, a senior minister was convicted by a trial court of threatening a businessman and demanding money to “evict unauthorized occupants of a land,” and to provide approval to refill the land. Pending appeal, the minister continued to retain his portfolio and was appointed to a senior position in the government's parliamentary caucus.

In January 2023, the Supreme Court upheld the conviction of the former chief of staff of former President Maithripala Sirisena under the Bribery Act, for soliciting a bribe of LKR 100 million and accepting LKR 20 million from a foreign investor. In a separate case, the Supreme Court ordered former President Maithripala Sirisena to leave the official residence he had allocated to himself, until the court concluded hearing a petition that challenged the legality of Sirisena allocating these premises to himself. While these are all positive developments, they remain the exception, and little progress has been made on corruption cases, even where related parties have been successfully prosecuted in other countries.

Prosecution of
office abuse

4



During the review period, government officials were accused of being involved in various scams, including deals involving vaccines and medications during the COVID-19 pandemic. This was a major issue for those whose protests led to the ousting of Prime Minister Mahinda Rajapaksa and President Gotabaya Rajapaksa in 2022. The fact that such corruption took place when most Sri Lankans were suffering without essentials underscored the degree of impunity that individuals in power enjoy.

The Sri Lankan constitution recognizes several civil and political rights and provides an enforcement mechanism against their violation by the executive and administrative functionaries. However, the constitution does not explicitly guarantee the right to life or the right to privacy. Protections against non-state actors are provided by criminal law. Furthermore, the constitution prohibits discrimination based on race, religion, language, caste, sex, political opinion, place of birth or any one of such grounds and grants equal access to justice and due process. Problematically, despite the aforementioned provisions, the constitution does not explicitly recognize the right to nondiscrimination based on sexual orientation, and the existing criminal law prohibits consensual same-sex relations between adults.

The long delays in the court system limit its effectiveness in addressing grievances. The ambitious plan to modernize the court system and reduce delays, promised by the government during the previous review cycle, has seen limited progress.

As mentioned previously, the ICCPR Act, No. 56 of 2007 and the PTA continue to be disproportionately used for prosecutions and detentions of ethnic and religious minorities. In the aftermath of the Easter Sunday attacks, hundreds of Muslims were arrested and many remain in custody without charge. The government made some cosmetic changes to the PTA during the review period, which have failed to address the main problems with the act.

Custodial torture remains a serious concern, with the systemic and well-documented use of torture by the police and the Supreme Court. However, very few successful prosecutions have taken place of individuals accused of perpetrating torture.

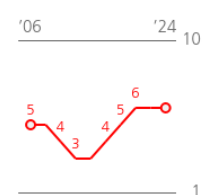
4 | Stability of Democratic Institutions

Sri Lanka has a highly centralized system of government in which the central government plays a dominant role. Within the central government, a strict hierarchy exists, and the president wields disproportionate power over the other arms of government.

Provincial councils, regional units exercising devolved power and subject to the overriding control of the central government, have not functioned throughout the country since 2019. The central government appears determined to postpone elections for local government institutions, which are otherwise required by law to take place in March 2023.

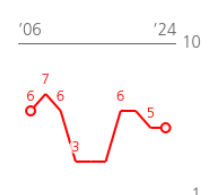
Civil rights

6



Performance of democratic institutions

5



The judicial system continues to be plagued by delays and a backlog of cases, which was further aggravated by COVID-19-related closures. Despite large allocations of money to the Justice Ministry to upgrade infrastructure and human capital in the judicial system, these transfers could not be utilized due to the economic crisis, and many initiatives that were initiated in the previous review period were abandoned.

Sri Lanka has a long-established public service. However, it is politicized and often subservient to the president's directives. Centralized decision-making, dominated by the executive president, can be seen as a cause of the economic crisis in Sri Lanka. Decisions by the former and incumbent president together with their confidants, such as a ban on nonorganic fertilizer and the refusal to seek IMF assistance in a timely manner, contributed significantly to food shortages, with the World Food Programme estimating that 30% of the population was left food-insecure and requiring humanitarian assistance.

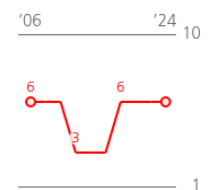
The period of review saw a significant undermining of the idea of a “strong technocratic leader” able to address the problems faced by the country. The concept is a founding myth that has been used to justify the existence of a strong executive presidency in Sri Lanka. The historical failings of President Rajapaksa and the ensuing economic chaos strengthened the discourse around the need to ensure checks and balances and to strengthen democratic institutions. The most prominent example of this was pressure exerted by large-scale public protests on parliament to undo the undemocratic changes made by the 20th amendment to the constitution.

Sri Lanka's constitutional history suggests that the recent undermining of this myth is likely temporary. However, the degree to which the president was able to adversely impact the economy provides strong evidence in support of a move toward a system of government with stronger checks and balances. Unfortunately, this momentum was not seized upon, and the succeeding president enacted only small-scale reforms to the presidency. He successfully managed to resist calls for more robust reform, such as abolishing the executive presidency. Thus, the incumbent president continues to wield significant power.

Sri Lankans have mixed feelings about the need for a strong executive. Buddhist nationalists and arguably many within the military are strongly in favor of it. There is also dissatisfaction with the electoral system. That being noted, there is a commitment to changing governments using democratic mechanisms. Some have warned that the instability stemming from the recent economic crisis could motivate the military to assert itself in politics, but this is unlikely to happen if the security forces continue to receive high budgetary allocations.

Commitment to democratic institutions

6



5 | Political and Social Integration

Overall, internal party organization is undemocratic and dependent on personalities and patronage. Parties are organized in such a way that change in leadership is difficult to achieve. The review period saw a significant realignment between political parties. The United National Party (UNP), which was reduced to just one seat in parliament at the 2020 election (having been the main party in government from 2015 to 2019), reclaimed an important role in national politics with its one member of parliament, Ranil Wickremesinghe, appointed as prime minister and subsequently as president after Rajapaksa's resignation. This was preceded by an informal alliance between the Sri Lanka Podujana Peramuna (SLPP) and the UNP.

Clientelism plays an important role in political party structures and the perceived role of national politicians. In the case of members of parliament (members of parliament), clientelism is also responsible for the large excess of staff in government departments and state-owned enterprises, which is a cause of significant pressure on public finance.

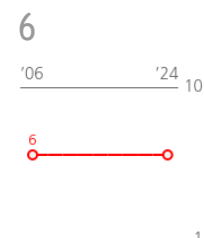
Sri Lanka's polity remains significantly divided along ethnoreligious identities. The dominance the SLPP enjoyed among Sinhalese voters has waned, although this does not mean majoritarian sentiment has weakened. The economic situation and the reforms being enacted by the government to qualify for IMF assistance have caused significant volatility in the political system. For example, it has made the president and the SLPP, which commands a majority in parliament, highly unpopular. While this may offer the main opposition parties a chance to do much better when national and local polls are held, their leaders do not seem to have credible alternative programs that could revive the country's economy.

Buddhist monks are the most influential group representing social interests within the political system and possess the ability to organize citizens around political projects. Trade unions also play an important role in political discourse. Most political parties have their own affiliated trade unions, which form an important part of their political strategy.

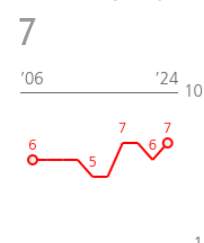
Sri Lanka has seen active participation by non-governmental organizations (NGOs) both at the national and local level. These NGOs, such as local welfare societies and youth societies, come in different shapes, sizes and political affiliations. They are a useful forum for organizing at the local level and lobbying local governments.

There was increased demand for the work done by NGOs during the review cycle, with an ever larger cross-section of the population being engaged around issues of corruption and governance. The protest grounds at Galle Face Green, which saw the participation of a wide range of groups including Buddhist monks, student organizations, former military personnel and relatives of those who were "disappeared" during the final stages of the war, provided an important forum to share ideas on many different issues.

Party system



Interest groups



The large-scale protests observable in the last few years saw significant cooperation among diverse interest groups. Indeed, the economic crisis helped highlight the widespread degree of associational life in the country, thanks to farmers, teachers, and others – especially from rural areas – protesting against scarcity and government policies.

However, it remains to be seen whether this cooperation will dissipate once the more severe economic problems, namely food and energy shortages, begin to ease.

An overwhelming majority of Sri Lankans (79.2%, according to a survey in September/October 2022) indicate that democracy is preferable over any other kind of government. While continuously reaffirming their support for periodic free and fair elections, respondents often express significant support for “experts” (62%) and “a strong leader” (55%) who can make decisions on what is best for the country without eyeing re-election. Initially, former President Gotabaya Rajapaksa was promoted as the embodiment of all these characteristics; however, he was the first president in Sri Lankan history to be forced to resign due to large-scale protests charging him as one of the main causes of the ongoing economic crisis.

Sri Lanka has experienced peaceful election-based transfers of power for more than 75 years since independence, with regular high voter turnout. However, frustration prevails over the inefficiency and corruption among elected representatives. As per the aforementioned survey, confidence in democratic institutions, such as parliament, and the legal system remains low.

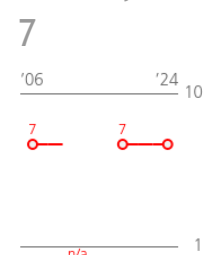
While impunity and a relative breakdown in the rule of law made Sri Lanka an illiberal democracy for a long time, the economic crisis has made it a dysfunctional illiberal democracy. Sri Lankans favor the democratic process; yet they disapprove of the way this process has unfolded during the period under review.

There are active local and national self-help organizations among all groups based on religious and social affiliations. These organizations actively step in to fulfill the functions otherwise provided by the government, including the provision of emergency relief during natural disasters and the mobilization of resources to augment government expenditure. These practices are observable particularly in relation to health care, education and small-scale rural infrastructure projects.

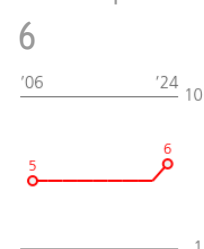
Levels of trust seem to be based more on cultural and professional affinities than on a common bond of citizenship. Thus, Sri Lanka’s main ethnic groups, Sinhalese and Tamils, each have a great amount of bonding social capital but considerably smaller amounts of bridging social capital. However, these self-help initiatives, which avoid politically sensitive issues, do provide a useful platform for interethnic and interreligious solidarity.

The economic crisis has seen citizen groups organize to remedy government shortcomings in the provision of essential services. There has been an increase in community kitchens to serve the most vulnerable sections of society, as well as citizens collectives to procure and provide essential medicines to government hospitals. The large-scale protests also provided an opportunity for citizens to

Approval of democracy



Social capital



collaborate and provided a space to engage in uncomfortable conversations about Sri Lanka's post-independence history, which are otherwise neglected by the administration. In May 2022, for the first time in Colombo, a commemoration event was held to remember those who passed away during the last stages of the civil war.

II. Economic Transformation

6 | Level of Socioeconomic Development

Sri Lanka remains the frontrunner in South Asia in terms of its score on the U.N. Human Development Index (HDI), registering an index value of 0.782 in 2021. In the private sphere, ethnicity does not appear to hinder individuals' access to economic opportunities, although it is worth noting that approximately 90% (official statistics are not available) of those employed by the government come from the majority community. Individuals face notable disadvantages when it comes to economic opportunities due to the unequal allocation of resources across different geographical regions and the urban-rural divide. This geographical divide poses a significant obstacle to realizing economic prospects.

The most recent Gini Index data is from 2016. However, data compiled by Sri Lanka's Department of Census and Statistics indicates that the poorest 20% of households account for 5% of total household income, while the richest 20% account for over 50% of the total household income. Women's participation in the labor force remains lower than that of males. Sri Lanka's Gender Inequality Index score marginally dropped to 0.383 in 2021, continuing a downward trend since 2019.

As identified in the previous review, a large percentage of Sri Lanka's population is classified as "near-poor." According to the World Bank, high inflation of 64.3% year-on-year in August 2022 and the significant contraction of the economy by 9.2% in 2022 would disproportionately impact low-income earners. World Bank estimates in 2021 indicated that more than 500,000 people fell into poverty due to the COVID-19 pandemic, with poverty projected to remain above 25% over the next few years. Children in Sri Lanka are also increasingly vulnerable to poverty. For instance, some have fainted in schools due to malnutrition, and other poverty-related indicators have remained at high levels.

President Wickremesinghe has stated that he hopes that Sri Lanka will recover to its 2019 GDP level by 2026.

Question
Score

Socioeconomic
barriers

4

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Economic indicators		2019	2020	2021	2022
GDP	\$ M	89015.0	84440.5	88496.5	74403.6
GDP growth	%	-0.2	-4.6	3.5	-7.8
Inflation (CPI)	%	3.5	6.2	7.0	49.7
Unemployment	%	4.7	5.2	5.2	6.7
Foreign direct investment	% of GDP	0.8	0.5	0.7	1.2
Export growth	%	1.7	-29.6	10.1	10.2
Import growth	%	-3.5	-20.1	4.1	-19.9
Current account balance	\$ M	-1843.4	-1083.0	-	-
Public debt	% of GDP	82.6	96.7	102.7	115.5
External debt	\$ M	56117.9	56299.5	56592.1	-
Total debt service	\$ M	6240.5	5223.3	4731.0	-
Net lending/borrowing	% of GDP	-6.4	-13.4	-11.7	-
Tax revenue	% of GDP	10.9	7.8	7.4	-
Government consumption	% of GDP	9.0	10.4	9.5	7.2
Public education spending	% of GDP	-	1.6	1.5	1.2
Public health spending	% of GDP	1.5	1.9	-	-
R&D expenditure	% of GDP	-	-	-	-
Military expenditure	% of GDP	1.8	1.7	1.9	1.4

Sources (as of December 2023): The World Bank, World Development Indicators | International Monetary Fund (IMF), World Economic Outlook | Stockholm International Peace Research Institute (SIPRI), Military Expenditure Database.

7 | Organization of the Market and Competition

The state permits 100% foreign investment in any commercial, trading, or industrial activity, except for a few regulated sectors such as air transportation, coastal shipping, and military hardware. The latter are subject to approval by relevant government agencies.

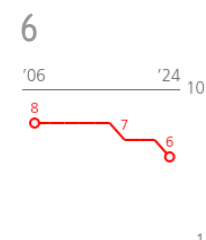
In the context of an ongoing foreign exchange crisis, the government prohibited a greater number of imports. Additionally, caps were implemented on the retail price of various goods and services, and a state of emergency was declared in 2021 to purportedly prevent the hoarding of rice and paddy. However, the state of emergency was terminated after a brief period of time.

In 2022, significant changes were made to permit foreign participation in the power and energy sector in response to the country's foreign exchange crisis. In 2021, the government established a new regulatory mechanism that applies exclusively to the Colombo Port City Special Economic Zone (CPCSEZ). The Colombo Port City Economic Commission Act creates a parallel system of administration within the CPCSEZ by suspending many regulations and restrictions related to policy fields such as foreign exchange controls, labor, and employment conditions. These regulations and restrictions remain in place in other parts of Sri Lanka. This creates disparities between businesses based inside and outside the CPCSEZ. Businesses set up outside the CPCSEZ, especially local ones, face a significantly more complex licensing and regulatory framework, which puts them at a disadvantage.

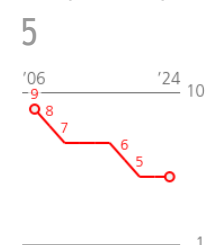
According to estimates from the International Labour Organization, informal workers account for approximately 67% of the workforce, highlighting the significant contribution of the informal sector to the national economy. Price setting is predominantly determined by market forces. However, the government often imposes price controls on essential food items.

The inadequacies in the legal framework relating to anti-competition and antitrust laws, which were highlighted during previous review periods, persist. The Consumer Affairs Authority, a member of the International Competition Network, was designed to enhance consumer protection by regulating trade and prices of goods and services, to safeguard traders and manufacturers against unfair and restrictive trade practices, to promote competitive pricing, and to ensure fair competition between traders and manufacturers of goods and services. However, the government has admitted that this regulatory framework is completely inadequate, using these weaknesses as grounds for imposing a state of emergency in September 2021. Additionally, the Consumer Affairs Authority is composed of members directly appointed by a minister, which greatly hampers its ability to act independently.

Market organization



Competition policy



The Public Utilities Commission of Sri Lanka (PUCSL) has faced significant controversy, primarily due to the actions of its chairperson. The chairperson has been in constant conflict with the government over the widespread extended power cuts that have been in effect since January 2022, as well as the increase in electricity prices. The PUCSL's standing as a regulatory body has been severely compromised during this time, both by the chairperson's conduct and the government's undermining of its decisions.

Subsidies over extended periods have played a significant role in contributing to the ongoing economic crisis. The government's attempt to reduce – or even remove – such subsidies and to increase taxes is also a major reason for the continued protests.

Additionally, trading related to certain commodities, such as rice and sugar, is controlled by individuals with strong connections to influential politicians. In addition to the evident practices of clientelism, some of these groups operate in a manner resembling a cartel.

The simple average of the most-favored nation applied total tariffs increased to 9.5% in 2020 from 9.3% in 2019. However, as explained during the last review period, imports into Sri Lanka continue to be subject to several other charges. These para-tariffs make Sri Lanka a de facto protectionist country, hampering international trade.

In response to the worsening foreign exchange crisis, the government prohibited several types of imports. The number of restricted items has decreased over time but many remain in place. Additionally, there were specific periods during which existing foreign reserves were insufficient to import even basic necessities.

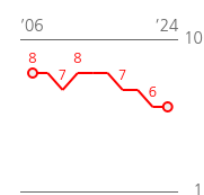
Sri Lanka employs a range of nontariff measures to protect local industries from external competition. These measures include the imposition of import quotas and standardization requirements.

With the onset of the COVID-19 pandemic and the pressures on the foreign currency exchange rate, the government imposed prohibitions on importing certain categories of products. These prohibitions were accompanied by more onerous conditions on other imports. Following the resignation of Gotabaya Rajapaksa and the election of Ranil Wickremesinghe as president, the government decided to abandon its previous import substitution policy. Instead, it pledged to liberalize foreign trade by gradually eliminating para-tariffs and implementing other measures.

The banking sector in Sri Lanka, which comprises licensed commercial banks (LCBs) and licensed specialized banks (LSBs), dominates and accounts for the highest share of the total assets in the financial system. The bank capital-to-assets ratio declined to 6.8% in 2020.

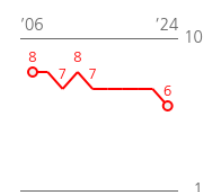
Liberalization of foreign trade

6



Banking system

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In terms of the Banking Act and the Monetary Law Act, the central bank is responsible for licensing new LCBs and LSBs, conducting continuous supervision and examination of banks, enforcing regulations, and providing directions, orders, and guidelines to banks under the aforementioned laws. Up until the last few months of the period under review, the office of the governor of the central bank had been highly politicized and partisan, which undermined its independence.

The bank's ratio of nonperforming loans to total gross loans increased to 4.9% in 2020. The banking sector has maintained capital adequacy ratios (CAR) well above the minimum regulatory requirements throughout 2020. As of September 2022, the banking sector reported a tier 1 CAR of 12.4% and a total CAR of 15.3%.

Exposure to central government and state-owned enterprise debt remains high, including both rupee (LKR) and foreign currency-denominated debt. This poses significant risks for the banking sector as the central government undergoes a debt restructuring process and exacerbates the adverse effects of economic contraction and failing private sector businesses. As part of this process, the government is being requested to restructure domestic debt, which could have drastic implications for the domestic financial sector.

High interest rates, economic contraction, and macroeconomic rebalancing efforts, such as higher tax rates, would all impact the ability of businesses and individuals to repay loans. Thus, the central bank projects a further increase in nonperforming loans (NPLs) in the financial sector.

The Colombo Stock Exchange (CSE) comprises 290 companies representing 19 GICS industry groups as of January 31, 2023. The market capitalization was LKR 3,881.14 billion.

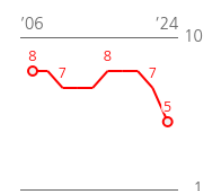
8 | Monetary and fiscal stability

In the first half of the review period, the central bank of Sri Lanka (CBSL) intervened aggressively through direct financing of fiscal expenditures while continuing its policy of suppressing interest rates. Between March 2020 and March 2022, central bank holdings of government securities increased by 2000%.

Year-on-year inflation, based on the national consumer price index, was 70.2% in August 2022. According to World Bank data, however, it was 64.3%. Inflation has been on the rise since the beginning of the review period, and the central bank responded with only minor interest rate hikes. As these responses were completely inadequate, the central bank resorted to a 7% increase in interest rates by April 2022, when inflation had risen rapidly.

Monetary stability

5



The high inflation rate was a result of several internal and external causes, including the central bank's aggressive direct financing of fiscal expenditures and inadequate responses vis-à-vis price increases.

Owing to the impact of the COVID-19 pandemic, Sri Lanka experienced a decrease in foreign currency inflows to the country. In 2020, the country lost access to international financial markets due to repeated credit rating downgrades. These circumstances should have prompted a reassessment of government policy; however, the government continued to use reserves to service external debt and aggressively defend the exchange rate. Official reserves dropped from \$7.6 billion in 2019 to less than \$400 million (not counting the currency swap – equivalent to \$1.5 billion – with China) in June 2022.

In response, the central bank, without any notice and before the government had announced it was approaching the IMF, adjusted the exchange rate limit in March 2022. This policy reversal saw the Sri Lankan rupee (LKR) depreciate from approximately LKR 200 in February 2022 to over LKR 350 per \$1 by May 2022.

The period leading to the exchange rate reversal saw accusations of incompetence directed at the central bank governor. There was a strong sense that monetary decisions were not being made in the best interest of the country.

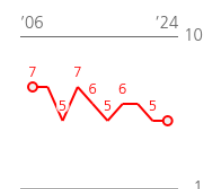
The government's budgetary policy has changed significantly during the period under review, when the macroeconomic impacts of the significant tax income and consumption tax cuts offered by the government were fully realized. In addition to the significant reduction in government revenue due to tax cuts, government expenditures also increased during this period. Salaries and wages paid by the government, which accounted for approximately 58% of government expenditure in 2021, increased by 11% between 2020 and 2021, further imperiling the government's fiscal position. The primary account deficit amounted to 6% of GDP in 2021, and the overall budget deficit increased to 12.2%. By the end of 2022, Sri Lanka's total public debt was equivalent to \$83.6 billion.

The government amended its strategy in the last quarter of 2022, implementing an increase in consumption tax in October 2022, and announced a reversal of the income tax policy to take effect on January 1, 2023. These increases have been necessary, but they are also directly linked to the IMF Staff Level Agreement reached in September 2022. The agreement sets a target of achieving a surplus primary account balance of 2.3% by 2025.

In addition, the government must reform state-owned enterprises (SOEs). The largest 52 SOEs reported a before-tax loss of LKR 86 billion in 2021, representing a significant strain on the national budget. Although institutions such as the Ceylon Electricity Board and the Ceylon Petroleum Corporation have been subject to government reforms such as cost-reflective pricing, there is much more that needs to be done to reduce inefficiencies and corruption.

Fiscal stability

5



9 | Private Property

There is no constitutional right to property, so private property ownership is regulated through civil law, or more precisely, through statute law, the Roman Dutch common law, or personal laws when applicable. The plethora of sources of civil law can lead to confusion and cause uncertainty. Private land ownership is limited to 50 acres per person through the Land Reform Law. Furthermore, the Land (Restrictions on Alienation) Act places restrictions on the transfer of freehold title lands to foreigners, foreign companies, and certain institutions with foreign shareholdings in Sri Lanka.

Court proceedings in litigation to vindicate property rights are slow. The rights, title and interest in land can only be transacted through a deed, a specialized legal instrument with specific formalities required to be completed to confer validity.

Local Authority Regulations, the Urban Development Authority Law, and the Town and Country Planning Law regulate the use of private property located in different parts of the country. The Land Acquisition Act provides the legal basis for the government's acquisition of private land for a "public purpose." The Requisitioning of Land Act grants the president the power to authorize a designated competent authority to take possession of any land for a time determined by the president. In theory, this time period can be extended indefinitely. Both land acquisition and requisition processes are subject to the safeguards guaranteed in the constitution.

The private sector plays an important role in the economy, and the government allows 100% foreign investment in any commercial, trading or industrial activity, except in a few regulated sectors.

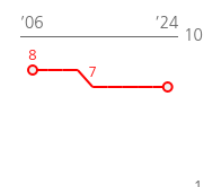
The procedure for incorporating, operating, and winding up private companies is regulated by the Companies Act of 2007.

Sri Lanka has a substantial number of state-owned enterprises (SOEs), totaling 527 in 2019. Most state-owned enterprises have been incorporated either by an act of parliament or as a company. In the case of the latter, the privatization process would be relatively straightforward in theory. However, if a state-owned enterprise is incorporated by an act of parliament, the procedure would necessitate parliamentary action and would be considerably more complex.

The government claims that Sri Lanka will have to reform or privatize state-owned enterprises (SOEs) as part of conditionalities in the IMF program. To date, no clear mechanism has been decided on for this, and ad hoc committees have been appointed to facilitate the process. Thus far, the process has not been transparent, which raises serious concerns relating to corruption. Sri Lanka has a history of corruption surrounding the privatization of SOEs, with little accountability.

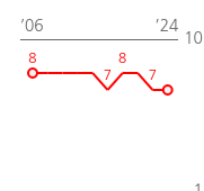
Property rights

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Private enterprise

7



10 | Welfare Regime

The state provides a number of poverty alleviation and welfare programs targeting low-income households and the rural population. The “Prosperity” program (known as Samurdhi) includes a subsidy and social security fund for low-income families across the country.

Measures taken for macroeconomic stabilization include increased indirect taxes and cost-reflective tariffs for the power and energy sector, which resulted in an overall price increase of 78% in 2022 and another increase of 66% in February 2023. These measures, coupled with high inflation and a contracting economy, have disproportionately impacted low-income earners and have resulted in a sharp reversal of Sri Lanka’s progress in reducing poverty.

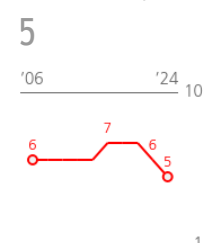
The government’s response has been to promise direct cash transfers to the most vulnerable and a strengthening of the social safety net. However, little has been done on either of these fronts other than ad hoc announcements. Payments of Samurdhi and elders’ benefits have been subject to significant delays due to a lack of funds. It is a program that is also mired in corruption, with many who should not qualify for aid using political connections to access it.

According to the International Labor Organization’s World Social Protection Report (2020 – 2022), 44.6% of the labor force were active contributors to a pension scheme, and 66% of the population are covered for essential health services. The Asian Development Bank reports that the Sri Lankan government spends 3.2% of the country’s GDP on social protection (excluding health), while the World Development Indicators record that 1.9% of GDP is spent on health.

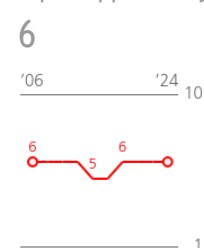
The constitution guarantees the right to nondiscrimination on the basis of race, religion, language, sex, and political opinion. However, there are no protections against discrimination based on sexual orientation, and consensual same-sex relations remain criminalized. This creates specific disadvantages and vulnerabilities for LGBTQ+ persons, including being targeted by law enforcement for bribery.

With some notable exceptions, disparities in access to education, public health, and public services are more pronounced regionally than across ethnic or religious divides. Geographical disparities are primarily due to imbalances in economic growth and disparities in the allocation of public funds due to political considerations. Conflict-affected areas suffer from acute economic hardships; specifically, disparities created due to prolonged displacement and landlessness create barriers to accessing public services.

Social safety nets



Equal opportunity



Large segments of the Upcountry Tamil population have suffered statelessness for more than 40 years. This community still encounters obstacles when it comes to accessing health care, education, and public services due to inadequate infrastructure facilities and limited economic prospects. Moreover, Upcountry Tamils residing in Sinhala-speaking administrative regions face an additional challenge: a scarcity of Tamil-proficient public officials.

Female literacy rates and life expectancy rates continue to be higher than those for males. Female enrollment in Sri Lanka's education sector is higher than male enrollment across age groups. However, according to statistics from the University Grants Commission, female participation in science, technology, engineering, and mathematics (STEM) is very low compared to that of their male counterparts. Furthermore, women's participation in the labor force, at 33.6% in 2021, remains significantly lower than for men.

11 | Economic Performance

The per capita GDP, calculated by the central bank at the current market price, was \$3,815 (provisional) in 2021, indicating a significant decline from a peak of \$4,077 in 2017.

As per World Bank statistics, the economy contracted by 4.1% in 2020 and experienced a modest recovery with a growth of 2.5% in 2021. Thereafter, however, political instability caused a contraction of 4.8% in the first half of 2022, which was visible across all major sectors of economic activity.

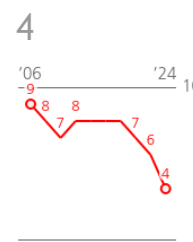
Inflation reached an unprecedented 64.3% (year-on-year) in August 2022, according to World Bank data, representing a staggering increase from 7% in 2021. The unemployment rate increased from 4.3% in 2019 to 5.4% in 2021. However, this does not include data for 2022, during which the most significant impacts of the economic crisis were observed.

Public debt stood at 103% of GDP in 2021 and has continued to increase over a long period of time. Sri Lanka's public debt has been assessed as unsustainable by the IMF. In response to this assessment, Sri Lanka announced an external debt service suspension in April 2022. Currently, it is engaged in a debt-restructuring process with its creditors.

The COVID-19 pandemic and the impacts of Russia's invasion of Ukraine posed external shocks that adversely impacted the Sri Lankan economy, with considerable public debt repayments due in the next decade. The government led by the Sri Lanka Podujana Peramuna (SLPP) made ill-advised tax cuts that reduced tax revenue to 8.1% of GDP in 2020, down from 12% in 2018. This decline in tax revenue, combined with the depletion of foreign currency reserves and the government's refusal to seek assistance from the IMF until the second half of 2022, sent the economy into free fall.

Because of the economic crisis, the island has recently been downgraded from an upper-middle-income country to a lower-middle-income country.

Output strength



12 | Sustainability

Sri Lanka continues to experience the effects of severe weather events such as extended periods of drought, frequent flooding, and heightened vulnerability to tropical cyclones originating in the Bay of Bengal.

Sri Lanka has several policies relating to environmental protection and sustainability, the implementation of which remains sporadic and uneven. As in the previous review period, despite public campaigns on environmental protection, encroachment on natural reserves and deforestation continue at an accelerated pace. Air and water pollution have worsened in urban areas, as have industrial contaminants and the unrestricted disposal of untreated sewage pollute freshwater. Recycling of garbage in urban areas remains inadequate.

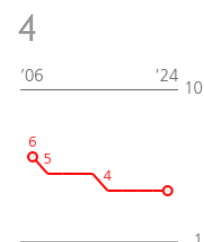
Sri Lanka's electricity grid is primarily powered by coal and thermal power plants. The rapid increase in global oil prices during 2022 led to a push toward greater renewable energy production. However, no significant tax incentives to encourage renewable energy use were forthcoming. In the previous period of review, there were several proposals for such incentives, but it seems that they either did not materialize or were withdrawn to bolster government revenue in response to the economic crisis.

Sri Lanka offers free primary and secondary education in public schools, leading to a consistently high U.N. Education Index of 0.754 (2021). Female enrollment surpasses male enrollment at all education levels. The adult literacy rate, for those aged 16 and over, stood at 92.4% in 2020. The government also provides free university education, although resources for incentives and support for students are constrained. Consequently, the gross tertiary enrollment rate for the academic year 2020/21 was 21.6%, with approximately 43,800 students in absolute figures.

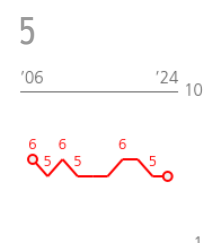
Low levels of government funding for higher education continue to be a problem. Unfortunately, this is likely to become only more acute with deep government spending cuts. Based on available data, public expenditure on education remained below 2% of the GDP in 2019 (1.9%). To increase this share, there is room for greater private sector participation in education. While private sector participation is rising, regulatory and monitoring mechanisms related to private sector institutions remain weak.

The emphasis on research and development in tertiary educational institutions is very low. This has contributed to Sri Lanka being ranked only 85 in the Global Innovation Index in 2022.

Environmental policy



Education policy / R&D



Governance

I. Level of Difficulty

Sri Lanka enjoys an advantageous geographical location near international shipping lines and in close proximity to India. Its labor force is highly literate and benefits from publicly provided free health care and primary and secondary education. The basic, though inadequate, system of transport has been improved in recent years by considerable investment in ports, airports, roads and railways, but these investments have been predominantly debt-driven and financed by commercial interest rates.

Sri Lanka had made considerable gains in reducing extreme poverty over the last three decades. However, there is a significant percentage of the “near-poor” population who are particularly vulnerable to economic shocks. The economic crisis in 2022 saw a marked increase in poverty, exacerbated by some of this “near-poor” population falling into poverty. At the end of 2022, the average worker was earning only around \$100 a month. Approximately 20% of students attend school without having breakfast. School dropout rates have drastically increased and threaten school closures. As per the World Food Programme, around 70% of Sri Lankans have been forced to eat less due to the economic crisis, which is closely connected to the rising poverty rates.

Sri Lanka is highly vulnerable to the impacts of climate change. According to the World Bank, historical records indicate that floods and droughts are increasing, resulting in an increased risk of landslides during the monsoon season and rendering a large part of the island drought-prone from February to April. Extreme heat and an increased incidence of flooding threaten human health and adversely impact agricultural yields. The adverse impacts of climate change are expected to disproportionately impact the poorest and most marginalized communities, exacerbating poverty and inequality.

The World Bank estimates Sri Lanka’s GDP will contract by 9.2% in 2022. Sri Lanka ended 2022 in receipt of an IMF-approved loan, at the cost of being highly dependent on the island’s creditors agreeing to restructure their existing loans.

Even after the IMF loans are approved and the government has been able to borrow additional money, the country will need to deal with loss-making SOEs and reduce the size of its military. These will be politically very unpopular and threaten the country’s stability.

Structural
constraints

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Sri Lanka enjoys a long civil society tradition dating back to British colonial rule. Many of the early organizations that advocated for self-government and independence from British rule were also advocates for other social and cultural issues, and some of these organizations later transformed into political parties. In recent years, particularly during and after the civil war, a culture of organized NGOs has emerged that has taken an active role in advocating for human rights. Organizations from the north and the east have continued to function under difficult circumstances due to militarization and a lack of resources and have been at the vanguard on issues of accountability and justice.

Decades of armed conflict and polarization have prevented the emergence of strong civil society associations that effectively cut across ethnoreligious cleavages and enhance bridging social capital. In this regard, many groups that would typically function as civil society may not promote tolerance and pluralism, given that they espouse ethnoreligious and nationalist sentiments framed by an exclusivist ethos.

Sri Lankan civic society is characterized by a keen interest in politics and governance and high levels of participation during elections. Peaceful protests across Sri Lanka between April and July 2022 forced the former president's resignation due to economic mismanagement. However, the protests lost momentum after his resignation and, unfortunately, some groups engaged in protest turned violent.

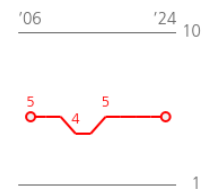
Electoral politics in Sri Lanka remain a divisive force. The existing deep divisions across ethnoreligious and linguistic fault lines continue to be exploited for electoral gain. Despite the conclusion of armed hostilities more than 10 years ago, the political conflicts that fueled the armed conflict remain unresolved. Additionally, new conflicts emerged after the end of the civil war, particularly involving the Muslim minority. In connection to this, the Easter Sunday attacks created significant tensions between Muslims and Christians. The suicide bombers who participated in the attack were easily radicalized, at least in part due to the sporadic attacks on the Muslim community since 2013. Also, important to consider is the failure of the state to prevent the attacks or hold the perpetrators accountable.

Tensions continue to grow across the northern and eastern provinces vis-à-vis allegations of militarization, attempts of forced demographic relocations by the government, and the failure to ensure accountability for atrocities committed during the war or to allow memorialization efforts. In turn, the pushback from Tamil civil society and political actors further drives polarization in the south of the country.

The economic and 2022 protests masked ethnoreligious tensions, at least temporarily. They enabled people to come together across the class and ethnoreligious divide to protest against the government.

Civil society traditions

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Conflict intensity

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II. Governance Performance

14 | Steering Capability

The period under review saw two different presidents in office, albeit both at the head of SLPP-led governments. President Gotabaya Rajapaksa's government was considerably more ideologically coherent and came to power promising technocratic efficiencies. However, in practice, it was responsible for haphazard policies, brash decision-making and the subsequent regular reversal of such decisions. President Ranil Wickremesinghe has been more successful in setting and sticking to strategic priorities over the last six months, especially in fulfilling actions that Sri Lanka had agreed to implement in return for the IMF approving financing under an extended fund facility.

The public service is highly politicized, with key government positions staffed by political appointees. Career public officials are incapable of making independent decisions due to the politicized nature of public service. The technical competence across the public service has been compromised by generations of political appointees entrenching themselves within the government, as well as recruiting and providing jobs for constituents on political considerations. Cabinet portfolios are not scientifically apportioned but are primarily based on political expediency rather than the government's goals. Decision-making is highly politicized and driven by political actors, often based on short-term gain. There are very few institutional mechanisms to develop long-term plans, and even the ones that do function are routinely sidelined. Often, such policies are not only discontinued but even reversed by the succeeding government.

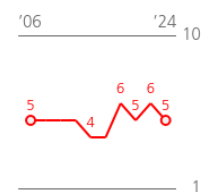
President Wickremesinghe has promised a 25-year development plan, on which limited information is available except for the immediate objective of stabilizing the economy, increasing private sector investments in strategic sectors and liberalizing trade. However, thus far, his tenure has been driven by IMF conditionalities.

Several political initiatives taken by President Gotabaya Rajapaksa's government were reversed during the period under review. Rajapaksa's commitment to a market economy was unclear, with several policy decisions reflecting different ideological dispositions. As highlighted in the previous review period, a deeply nationalistic policy agenda, the past human rights record, existing geopolitical realities and the state of the economy all complicated the government's ability to manage domestic economic expectations based on its populist rhetoric. Clientelism and corruption were major roadblocks in fulfilling its promise of technocratic efficiency. Rajapaksa's background made him more comfortable working with military officers, who were inexperienced civilian administrators, and ill-equipped to navigate the bureaucracy of the public service.

Question
Score

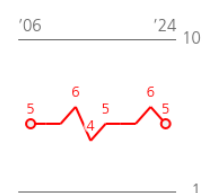
Prioritization

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Implementation

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When Wickremesinghe took over as president, widespread protests at the time forced him to move the parliament to repeal the 20th amendment to the constitution, which undermined the separation of powers and accountability of the president. However, as a politician with over 40 years of experience, he successfully resisted calls for more meaningful reform that would reduce the powers of the presidency and create more accountability mechanisms. Wickremesinghe's administration has successfully pushed through policies to meet IMF conditionalities, including an increase in tax revenue and spending cuts, cost-reflective pricing mechanisms and initiating efforts for the privatization of SOEs.

President Wickremesinghe and his main backers in parliament are ideologically heterogeneous. This tension, coupled with the injudicious crackdown on public protests, raises concerns as to whether he can see through his own strategic priorities.

As in the previous period of review, the government has touted innovation as a key policy platform, both in terms of simplifying governmental processes and as a method of driving economic growth. However, progress remains very limited.

President Wickremesinghe seems unwilling and unable to learn and adapt from his own past experiences. He has been prime minister on several occasions and has tried to push through reforms; however, he was undermined primarily by the political forces affiliated with or in support of the SLPP. Since his inauguration, President Wickremesinghe has gone to great lengths to appease the SLPP and protect the party and its leaders from accountability. By doing so, he is imperiling his own policy objectives.

President Wickremesinghe also relies on the status of the economy and the need for an IMF bailout to push through reforms. By directly linking reform efforts to IMF conditionalities, he is not building the domestic constituencies needed to sustain reform efforts. On the other hand, the economy's dire situation has enabled him to push through policies such as tax increases that would not have happened otherwise.

At times, the president's overconfidence causes him to overreach, which is a major impediment from a personal standpoint. His political dependence on the SLPP also limits his ability to achieve his reform objectives, such as increased private sector participation and greater trade liberalization. Wickremesinghe's previous tenures as prime minister were characterized by his willingness to allow input and expertise from domestic and international experts. However, these mechanisms have yielded limited results during his presidency.

Policy learning

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15 | Resource Efficiency

The civil service is overstaffed, and the appointment of new public officials is politicized. The cost of salaries and wages increased to 5% of GDP in 2021 and constituted 58% of the government's expenditure. In an attempt to rectify this issue, the government reduced the retirement age of public sector and semi-governmental employees to 60 years. Accordingly, over 20,000 employees in the public sector were entering retirement by the end of 2022.

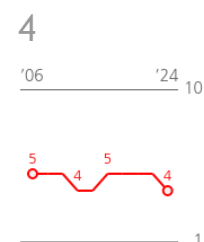
Sri Lanka's budget deficit increased considerably during the review period, mainly due to low government income and increased expenditure. Sri Lanka's public debt was assessed as unsustainable by the IMF. While the auditor-general's department was subject to executive control during the previous review period, the 21st amendment enacted during this review period increased its independence. Successive governments have continued to undermine the Fiscal Management Responsibility Act, a law designed to compel the government to report on and explain budget deviations. This has resulted in unaccounted and underreported deviations, with no corrective measures being taken in practice.

Government spending is not rational. Military spending per capita is disproportionately high and continues to rise, a decade after the war. Government spending on health and education remains at comparatively low levels in contrast with defense spending. The military engages in a variety of commercial activities often competing with local businesses and the agricultural sector, especially in Northern Province. The annual budget presented for 2023 has not meaningfully increased spending for the health and education sectors.

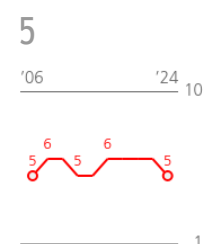
There are significant areas of overlap between the spheres of authority of the central government and provincial councils. This is the result of an unwillingness to effectively devolve power and has led to inefficient allocation and utilization of resources. Rather than rationalizing devolution structures and creating procedures to reduce duplication, these inefficiencies are used as justifications to avoid devolution and increase centralization.

Meaningful and transparent consultation and coordination remain a challenge for the government, as they have been for several decades. Prioritizing quick decision-making has made this even more challenging, as trade-offs between policy goals and their impact continue to be insufficiently considered. Rapid decisions often lead to zero-sum analysis and inadequate efforts to prioritize sustainability and the understanding of long-term impacts. A good example is the former president's decision to dictate an immediate shift from synthetic to organic fertilizer in the agricultural sector without consideration for short-term impacts, as well as local and international market conditions. The move had disastrous consequences for the economy and food security, and while the decision was eventually reversed, it did much to undermine public confidence in the government.

Efficient use of assets



Policy coordination



The allocation of functions to different ministries is driven by political bargaining and expediency, as opposed to a rational allocation of responsibilities and functions. This impedes coordination and adequate policy implementation.

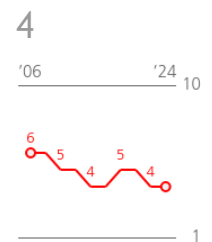
For almost 20 months during the review period, the 20th constitutional amendment was in operation, which effectively undermined the Commission to Investigate Allegations of Bribery or Corruption (CIABOC), as well as abolishing the National Audit Commission (NAC) and the National Procurement Commission.

The 21st amendment to the constitution reestablished the NAC and the National Procurement Commission. The NAC has important responsibilities in implementing the National Audit Act, which include the ability to impose fines on public officials for losses caused by fraud and negligence. Following the 21st amendment, the president's powers in appointing the auditor-general and members of the CIABOC have been limited. The National Procurement Commission is supposed to introduce transparency to procurement processes but has never been fully operational. Procurement processes remain opaque and vectors for corruption.

In 2022, the government enacted a law to regulate election expenditure. The law was rushed through and followed a haphazard process. It has serious shortcomings, such as making monitoring expenditure increasingly difficult and imposing insufficient punishment for violations. However, being the first law enacted to regulate election expenditure, it does provide a much-needed mechanism to monitor this issue.

CIABOC remains ineffective in dealing with corruption at the highest level of government, mainly due to a lack of resources and investigative skills to deal with complex cases of corruption. It has also had only limited success in dealing with low levels of corruption. For the year 2021, CIABOC completed investigations into 2464 cases, of which only 62 cases were filed in court. Out of these 69 cases concluded in 2021, most of which dated from previous years, only 11 resulted in convictions.

Anti-corruption
policy

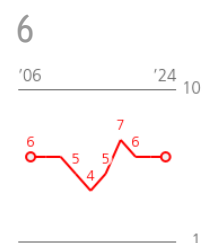


16 | Consensus-Building

Intractable differences exist between the Tamil political parties that represent the northern and eastern parts of the country and the national-level Sinhala political parties concerning the nature of the Sri Lankan state and devolution of power. These differences have been the source of conflict since Sri Lanka gained independence from colonial rule in 1948. Decades of conflict, the brutal end to the civil war and broken promises on political compromises have created deep divisions. No meaningful efforts at reconciliation have taken place.

The period under review saw another swing in public opinion on issues of democratization. Whereas during the previous review period, the dominant position seemed to be in favor of concentrating more power with the presidency to govern and fewer checks and balances, a significant change occurred in favor of curtailing the powers of the president due to the rule of President Rajapaksa. These sudden swings in public opinion have been common in Sri Lankan politics since 2000.

Consensus on goals



The mass mobilization of citizens provided an opportunity to build a consensus to abolish the executive presidency, to halt this oscillation and to build solidarity between different ethnic groups. However, since being elected president, Wickremesinghe has cracked down on protests and gatherings and impeded any such opportunity. He also successfully resisted pressure to make far-reaching changes to the institution of the presidency.

Comparatively, there is considerable convergence on economic policy issues, at least among the main political parties. Nevertheless, important differences persist. There is broad agreement on the need for a market-based economy with state welfare and subsidies. Party affiliation is not dictated by significant ideological differences. There is broad agreement on the need for IMF assistance and the reforms accompanying the loans, but that does not foreclose the possibility of parties taking different views purely for electoral gain. Leftist parties have embraced a more anti-capitalist rhetoric that may be better received by the electorate especially in rural areas, in light of the economic crisis and resource scarcities.

The Sri Lankan political system is significantly shaped by actors opposed to pluralism and to politics that is inclusive from an ethno-religious standpoint.

The SLPP controls a working majority in parliament and, as such, will likely control the government until the next election. President Wickremesinghe can call for parliamentary elections anytime after February 20, 2023, without consulting members of parliament.

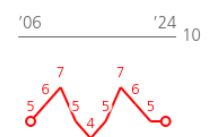
The government has promised several reforms to the Prevention of Terrorism Act, anti-corruption legislation and proceeds of crime law. This is primarily in response to domestic protests, international pressure and IMF conditionalities. However, the extent to which these reforms will be enacted remains to be seen, as the SLPP majority in parliament could potentially dilute them.

President Wickremesinghe promised recently to fully implement provisions of the constitution relating to the devolution of power. However, Buddhist monks, including the leadership of the different sects, vociferously and unequivocally object to these initiatives, in parts even violently by setting fire to parts of the constitution outside the parliament.

While it is likely that President Wickremesinghe will be able to enact economic reforms with partial support from the SLPP, it is much less likely that he will be able to – or even be willing to – enact reforms relating to democratization and the devolution of political power.

Anti-democratic
actors

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President Wickremesinghe has repeatedly stressed that his main priority is stabilization of the economy. However, he seems unable or unwilling to engage in building consensus on necessary economic reforms and is actively trying to undermine opposition parties and their proposals. For their part, opposition parties have also shown a lack of strategic vision to deal with the economic crisis at hand. Implementing economic reforms based on IMF conditionalities already creates disproportionately adverse impacts on vulnerable groups. Despite the rhetoric of targeted welfare and assistance to those most affected, little has been done in this regard. In light of large-scale citizen protests in 2022, it is not unlikely that further mass mobilizations could occur during the next year.

Regarding ethnic conflict, former President Rajapaksa operated under the premise that the end of the armed conflict represented the end of all political conflict and that any remaining grievance could be resolved through economic development. President Wickremesinghe has made limited overtures on this front, especially in relation to the devolution of power under the existing constitutional framework. However, no substantive action has been taken to date.

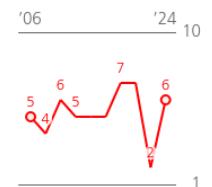
Sri Lanka does not have a culture of meaningful public consultation, and public consultations designed to capture diverse views and concerns have been difficult to implement for successive governments. When consultations do occur, they are mostly only a matter of formality and rarely influence decision-making. A notable exception to this was the process by which the Personal Data Protection Act, which was enacted in 2022, allowed for broad stakeholder input throughout the process.

Robust civil society participation is essential to building a consensus on necessary economic reform and ensuring such reforms have public support. However, the government does not seem to be interested in such a mechanism. The main opposition party, SJB, proposed a mechanism named the Council of State to discuss matters of national importance, which included nonpoliticians and a mechanism to enable citizen participation in decision-making. However, this was outright rejected by the government, which promised its own mechanism but has not delivered anything to date.

Successive governments have co-opted civil society actors for various positions within government. However, once co-opted, those individuals become part of the government and can no longer be categorized as representing civil society.

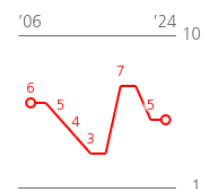
Cleavage / conflict management

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Public consultation

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Former President Rajapaksa was uninterested in pursuing postwar reconciliation efforts, and his government's actions exacerbated existing divisions. His government rejected the U.N. Human Rights Council resolution 46/1 in March 2021 and the subsequent report presented by the Office of the High Commissioner for Human Rights (OHCHR). His government continued to undermine the Office on Missing Persons, initially appointed to investigate the disappearances of thousands of Sri Lankans.

In this context, the OHCHR has continued collecting, collating, searching and analyzing large quantities of data from multiple sources to preserve material and support accountability efforts. As per the comprehensive report published by the OHCHR in October 2022, efforts are underway outside Sri Lanka to ensure accountability for international crimes, and the OHCHR will be evaluating requests to share information relevant to specific individuals.

During Wickremesinghe's tenure as prime minister (2015 – 2019), some efforts have been made to address reconciliation, however, progress has been very limited to date. There is some possibility of progress but given Wickremesinghe's reliance on the SLPP for parliamentary support and his own aversions to issues relating to accountability, it is unlikely that any meaningful progress will be realized in the short term.

17 | International Cooperation

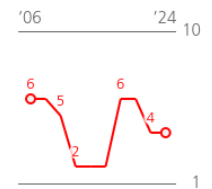
The Rajapaksa-led government reneged on several commitments made to foreign governments regarding investment and financing, which damaged Sri Lanka's relationships and credibility with these international partners. This included an agreement with the Japan International Cooperation Agency (JICA). The manner in which these projects were terminated left relations with Japan strained. Furthermore, the decisions by the government to not seek financial assistance from the IMF in order to deal with debt repayment and balance of payment issues led to severe foreign exchange shortages and consequently shortages and price hikes of essential goods like fuel and medicine.

With the new president, there has been a reversal of many such decisions. Sri Lanka has sought IMF assistance, with an emphasis on debt sustainability, which has required negotiations with bilateral lenders. In the short term, Sri Lanka had to negotiate with the World Bank and Asian Development Bank to repurpose existing loans to cover the costs of importing essentials. President Wickremesinghe claims to have repaired the strained relationship with Japan.

President Wickremesinghe has promised a 25-year road map to develop Sri Lanka and a blueprint for recovery from the current economic crisis. However, very little is known about the details of the plan. The new government has appeared open to input from international partners, with key bureaucrats from the United States, Germany

Reconciliation

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Effective use of support

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and India visiting Sri Lanka regularly. In the past, Sri Lanka has been unable to harness the benefits of such foreign support because of policy inconsistencies motivated by short-term political benefits, which undermined this support and assistance.

The Sri Lankan state's image as a credible partner within the international community has diminished, primarily because of the conduct of successive governments in relation to the U.N. Human Rights Council (UNHRC) process. Different Sri Lankan governments have taken contradictory approaches of confrontation and cooperation. However, even when the government has made promises to cooperate with the UNHRC, such as between 2015 and 2019 when Wickremesinghe was prime minister, it has failed to deliver on anything it has undertaken to deliver.

Sri Lanka had pledged to reform its Prevention of Terrorism Act (PTA) as part of its negotiations to obtain the European Union's GSP+ trade facility. Successive governments have repeatedly failed to deliver on this promise. With the new scheme for GSP+ coming into effect in 2024, Sri Lanka's past broken promises have come into sharp focus again. Even as they pledge to replace it with a new national security law, President Wickremesinghe's government has continuously used and abused the PTA to deter public protests.

The previous period of review highlighted how the government led by then President Rajapaksa reneged on several commitments and canceled at least two major infrastructure projects, which were part of bilateral agreements. These actions and the manner of cancellations strained bilateral relationships (with India and Japan) and raised concerns regarding Sri Lanka's international credibility.

The state continues to have poor compliance with core international human rights law (IHRL) conventions, most of which are not being incorporated into the domestic legal system. However, compliance with International Labour Organization (ILO) conventions remains high.

Credibility

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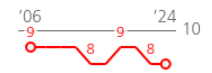
Sri Lanka has good relations with its neighbors in South Asia and enjoys close economic and cultural ties with all countries in South Asia. The relationship with India remains complicated due to Sri Lanka's close ties with the People's Republic of China and Sri Lanka's inability to adhere to the Indo-Sri Lanka accord of 1987, especially regarding ensuring a functioning system of provincial councils. However, India did provide considerable assistance to Sri Lanka in 2021/2022, by providing a credit line to facilitate purchases of essential commodities and by supporting Sri Lanka's efforts to enter into another IMF program.

Sri Lanka continues its close relationship with the People's Republic of China, which is Sri Lanka's largest bilateral creditor. As such, China is an important actor in restoring debt sustainability in order to access an IMF program. The People's Republic of China has not provided specific and credible financing assurances to satisfy this requirement, even as other bilateral creditors have provided such assurances.

Sri Lanka is an active member of the South Asian Association for Regional Cooperation (SAARC) and continuously engages with the Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation (BIMSTEC).

Regional cooperation

8



Strategic Outlook

During the review period, many of the concerns expressed about Sri Lanka's economic situation in previous years materialized. In the short term, Sri Lanka has secured a temporary respite from the acute fuel shortage and extensive power cuts and is on track to receive an IMF extended fund facility (EFF). However, key concerns and challenges remain.

Regarding economic recovery, the IMF EFF program aims to restore macroeconomic stability and debt sustainability, while also accelerating structural reforms of the economy. The government needs to achieve a broad local consensus on economic reforms to ensure that these reforms benefit all parts of Sri Lankan society. Failing to do so will result in more protests and violence. To achieve this consensus, the country needs the president to act as a consensus builder instead of being led by the preferences of a single political party and its interests. The IMF and other international partners should also demand governance reforms that address high-level corruption as part of the overall reform package. The IMF should be transparent about the conditions for its assistance and make them public, as long as they do not affect debt restructuring negotiations.

Transparency should also be a central priority for the government in the interest of reconciliation and avoidance of violence. The culture of impunity in Sri Lanka has strong roots in the lack of accountability for past violence, such as during the civil war. The government needs to ensure credible accountability and further employ truth-seeking mechanisms, as it promised to do in 2015.

Concerning devolution of power, the government should take the lead in building a political consensus for greater devolution to address historical demands, ensure balanced regional development, and ensure greater checks and balances through vertical separation of powers. By emphasizing the strong safeguards against secession and the indivisibility of the state, it should assuage fears of devolution held by the Sinhala majority.

Regarding democracy and the rule of law, the government needs to recognize the significance of democratic institutions in maintaining and promoting growth and stability. The government should safeguard fundamental rights and civil liberties and cease its excessive crackdown on protests. Governments must ensure timely elections, as the historical denial of the people's right to vote has resulted in violence in Sri Lanka. Bilateral and multilateral partners should continue to engage with the government regarding the importance of democratic institutions and counter the government's attempts to undermine such institutions by blaming conditions imposed by the IMF.

With regard to climate change and sustainable development, the government's rhetoric on climate change must be matched with action. The government must ensure that the remaining forest cover and sensitive ecosystems of the country are protected when engaging in development and agricultural activities. The impact of climate change has been observed in Sri Lanka. Thus, the government must play an active role in mitigating these impacts. Special emphasis is required to prepare for more frequent natural disasters and communicable diseases.