M.Phil. in Economics

Impact of Financial Reforms in Sri Lanka from 1977 to 1997

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Abstract

This study brings together outcomes of financial reforms, and in particular financial liberalization in Sri Lanka from 1977 to 1997. The question addressed is whether the reforms had given adequate attention to interest rates liberalization and other elements necessary for the success of reforms with a long term perspective. Main finding of this study was that the interest rate liberalization helped to increase the institutional savings initially. But, in case of domestic savings, the effect of reforms was not impressive. On the other hand, private investment also recorded a slow growth, especially, long term productive investments were unable to attract funds, as the reforms failed to change the pattern of credit allocation of the financial institution. The role played by the Government was also unsatisfactory. Expansionary Government borrowings and the resultant inflation greatly affected the successful implementation of the reforms. Therefore, long – term finance of the commercial banks which could have gone to the private sector was diverted towards government sector. Meanwhile, strengthening private institutions also remained weak as prudential regulation and supervision during the early part of the reform period was lacking. It was not until the late 1980s that the economy realised the need for further reforms. The economic factors, non-economic factors such as governance could also have had influence on the financial reforms, as financial reforms are considered as s process rather than project. As meaningful results may take longer period, outcomes should be evaluated over a longer perspective.