7th International Conference of Multidisciplinary Approaches (iCMA), 2020
Faculty of Graduate Studies,
University of Sri Jayewardenepura,
Sri Lanka.
ISSN: 2386 – 1509

THE IMPACT OF FOREIGN DIRECT INVESTMENT INFLOWS ON PUBLIC DEBT IN SRI LANKA

Weerakoon A.M.K.

Department of Economics and Statistics, Faculty of Arts,
University of Peradeniya, Sri Lanka
araliya.weerakoon@gmail.com

Abstract
Public debt is assumed to benefit a developing country like Sri Lanka to get extra funds to invest in economic growth. Foreign Direct Investment (FDI) is an important avenue to transfer technology, diversify exports, reserve foreign exchange, increase government revenue, resolve the public debt problem, and promote economic growth. Public debt is made more secure than FDI by buying government bonds, but the high level of public debt has resulted in harmful effects on the Sri Lankan economy. It is vital to reallocate FDI into productive investments that need to be undertaken. Sri Lankan government's debt to GDP was increased by 76.9% while FDI inflow was increased only by 17.3% in 2017. The relationship between FDI and public debt has not been explored in Sri Lanka. Hence, the main objective of this research is to analyse the impact of FDI on public debt in Sri Lanka using econometric techniques. Time series data from the period of 1978 to 2017 was used for the research. The two main variables FDI and public debt were measured in US dollars million while inflation rate and openness were measured as percentages. The study adopted Augmented Dickey-Fuller (ADF), Auto-Regressive Distributed Lag (ARDL), and Error Correction Model (ECM) tests to check the Stationarity, Long-run, and Short-run relationships respectively. According to test results, there is a significant positive impact of FDI on public debt at 1 % significance level in the long -run as well as in the short-run while inflation and openness do not have impacts on public debt. Therefore, the government of Sri Lanka should implement proper policies; to maintain the sustainability of public debt service and improve ways which are vital for attracting FDI to manage public debt at a desirable level while maintaining the inflation rate at a standard level to enhance FDI.

Keywords: Foreign Direct Investment (FDI), Public Debt, Inflation, Openness, Economic growth