

**INFRASTRUCTURE INVESTMENT
AND ECONOMIC GROWTH IN SRI LANKA:
FOREIGN INFLUENCE AND PATHWAYS TO SUSTAINABILITY**

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Sri Lanka is a lower-middle-income country situated strategically in the middle of the Indian Ocean. The country's population appeared to be 22.03 million people and a per capita income of USD 3,830 in 2023. While the country demonstrated significant potential in its early years, its growth has been curtailed by fiscal deficits, political instability, and a series of external and internal challenges. Key events, including the prolonged civil war, the 2004 tsunami, the 2019 Easter attacks, and the recent COVID-19 pandemic, have all posed substantial setbacks. With fiscal vulnerabilities persisting over the years, numerous factors have continued to impede its social and economic progress. Given this background, the main objectives of this study is to understand the long-term fiscal sustainability issue in Sri Lanka and to examine the pivotal role of infrastructure investment, public and private sector participation, and foreign direct investment (FDI) in Sri Lanka's economic development. This study employs both quantitative and qualitative approaches using time series data from 2000 onwards to analyze the 'crowding-in' and 'crowding-out' effects of public investment, the sustainability of fiscal policies, and the dominant role of foreign factors, particularly China, in infrastructure development. The study reveals that while foreign-funded infrastructure projects have supported post-war economic recovery, they have also heightened fiscal vulnerabilities and raised interest costs over the past decade. Additionally, it highlights that public-private partnerships (PPPs) have positively impacted critical sectors like healthcare, education, and telecommunications. However, inconsistent policies and high public debt have constrained more comprehensive economic growth. The study concludes with recommendations for improving fiscal management, fostering high-value industries, and promoting sustainable growth through balanced public-private partnerships and strategic foreign investments.

Keywords: FDI, PPP, crowding-in, crowding-out