

THE ECONOMY

Some Notes on the Outlook of the Economy in 1977

Two problems are encountered in any attempt to forecast the prospects for the Sri Lanka economy for any given period—the difficulties of forecasting the weather conditions and the world market outlook. The economy depends heavily on agricultural production and weather conditions are an important determinant of the agricultural output. In 1976, for example, tea, coconut and paddy output recorded a drop beyond expectations owing to adverse weather conditions. What will be the weather conditions in 1977? This question cannot be answered in advance. Similarly, given the high dependence of the economy on the world markets, the behaviour of export and import prices (which are largely beyond the country's control) have a direct influence on our economic prospects. Export and import prices influence the real incomes and the capacity to import of the country. Here, again, there is not enough information for us to obtain a fairly accurate picture of the future world market outlook. Hence this forecast of the economic prospects for Sri Lanka in 1977 is necessarily a tentative exercise.

Growth Rate

The Finance Minister in his Budget Speech for 1977, anticipated an economic growth rate of around 4% in 1977 as against an estimated 2½% (provisional) that was realized in 1976. Whether a growth rate of this magnitude would in fact be realized will largely depend on the behaviour of agricultural output which accounts for around one-third of the total national production. If we can assume that the tea output (which declined in 1976) would increase to a level of around 480 million pounds, that the paddy output would increase to around 70-80 million bushels, and that the rubber output would show a further expansion by a substantial amount, a growth rate of 4% is perhaps not far off the mark. However, a failure of any one or more of these principal crops to realise the above target levels would lead to a lower growth rate. It would therefore be

more realistic to assume that the growth rate in 1977 would be in the range of say to 3½% to 4%. When allowance is made for a population growth of about 1½% the growth in the per capita national product would be around 2 to 2½%.

Plantation Output

In 1976, the production of tea recorded a decline to around 430 million pounds and the present indications are that the production should show some recovery in 1977. It is difficult to estimate the probable extent of the recovery. Much will depend on the improvements in the management practices if the tea estates vested with the government, fertilizer application and the weather conditions. A rough guess would be that the recovery would raise the production to about 450-60 million pounds. The rubber output which rose to around 350 million pounds in 1976 is expected to show a further improvement in 1977. Here the output level may reach a level of around 365-370 million pounds. The coconut crop which suffered heavily under the drought conditions particularly during the final quarter of 1976 is expected to show a poor performance upto about April 1977. A recovery in the crop is expected from about May but for the year as a whole the crop is expected to show an overall decline of around 300 million nuts.

Paddy Output

All available evidence points to a significant increase in the paddy crop in 1977. The crop which fell to a level of around 50 million bushels (or even below) in 1976 should rise to over 70 million bushels. The paddy crop in the North Central Province which was adversely affected by the drought for two consecutive years should show a marked increase with the availability of diverted Mahaveli water. Reports from all major paddy cultivating areas suggest a bumper Maha harvest. The GPS purchases which were around 12-13 million bushels in 1975 and 1976 should rise to around 25 million bushels this year.

Manufacturing Output

Manufacturing has contributed some 13% of the total national product in recent years. The factory output in this sector will largely depend on the availability of imported raw materials and hence the important factor here is the size of the foreign exchange resources allocated for the importation of raw materials. It is likely that more foreign exchange would be made available for this purpose during this year, relative to last year. The anticipated higher output of tea and rubber should also be reflected in a higher manufacturing output since tea and rubber processing activities are also included in manufacturing output. There will, however, be a decline in coconut processing activities.

Public Investments

According to the budgetary estimates, the net capital development expenditure of the government (adjusted for under-expenditure) in 1977 is Rs. 1,996 million. The major investment programmes envisaged for 1977 are as follows.

- (a) An amount of Rs. 300 million has been provided for projects under the Decentralised Capital Budget which will be spent on short-term projects at the district levels.
- (b) The DDC development programme for 1977-78 envisages the setting up of nearly 2,800 projects at a total capital cost of over Rs. 180 million. A substantial part of this programme is expected to be carried out in 1977.
- (c) Rs. 600 million has been allocated for the investment programme in the industrial sector, a substantial part of which will be spent on the Urea Fertilizer project. The other projects with substantial capital allocations are the stage II of the steel project, the second paper factory at Embilipitiya, projects for the manufacture of sheet glass, refractories and calcium carbide, a medium count cotton spinning mill and the expansion of caustic soda and chlorine production capacity.
- (d) Work will continue on the Mahaveli Project involving mainly land development and settlement and it is planned to settle 20,000 families in the newly developed land. The major irrigation project that will be undertaken this year is the Rs. 300 million Lunugamwehera project.
- (e) In the area of economic overheads the major allocations are for the purchase

of 600 more buses for the CTB, Samanalawewa project (with a power generation capacity of 120MW) and the rural electrification programme covering 200 villages.

Exports

Present indications are that tea and rubber exports will continue to fetch high prices in 1977. The shortfall in supplies coupled with the high prices forecasts for substitutes such as coffee and cocoa should keep tea prices at a high level throughout 1977. In the context of higher petroleum prices and the resulting higher prices of synthetics, rubber prices are also expected to show a further improvement in 1977. It is difficult to forecast the probable extent of the price rise but the Finance Minister in his Budget Speech anticipated an average increase of 25 cents per pound in the f.o.b. prices of both tea and rubber. On this basis, the earnings from tea exports should be around Rs. 2000 million and rubber exports should fetch around Rs. 1000 million. Although the export prices of coconut products are expected to remain high, the export volume is expected to decline by at least 200 million nut equivalents, and hence the export earnings should record a decline. The export earnings from gems which recorded a substantial increase in 1976 are expected to show a further substantial improvement in 1977. The government expects an export level of around Rs. 300 million from gems in 1977. Exports of industrial manufactures are also forecast to show a sizeable improvement in 1977. The total exports are forecast to go up to about 4,700 million, which is an increase of around Rs. 350 million over the last years level. Tourist earnings are also likely to go up further and the services account of the balance of payments is expected to show a surplus of sizeable magnitude.

Imports

On the side of imports, the import prices of rice, flour and sugar should average considerably less than those of the previous year. Under the bilateral agreement with China, Sri Lanka will be purchasing 200,000 tons of rice at a price considerably below that paid in 1976. If the paddy crop should improve to the expected levels of around 70 million bushels, the import

volume of rice should record a marked decline in relation to 1976 imports. All this would mean a substantially lower food import bill in 1977 compared with 1976. However, a part of this benefit will be offset by the higher expenditure on petroleum imports as a result of the recent price increase by the petroleum producing countries by 5-10%. Depending on the source of imports, this should raise our petroleum bill by anything between Rs. 50 to over 100 million. The import bill which was around Rs. 900 million in 1976 should go up to about Rs. 1000 million in 1977. The rise in the petroleum prices should also lead to higher import prices of chemical fertilizer and higher costs for all imported goods. Given the inflationary situation in the industrialised countries (inflation is forecast to remain at a high level), the imported prices of raw materials and capital goods should remain high. Despite these, however, the higher export earnings coupled with the savings realised on food imports should raise the import capacity of the country above the last year's level. Furthermore, the government is expecting a higher level of foreign loans and aid this year particularly from such sources as the OPEC Special Fund and this should raise the country's capacity to import further. However, as in previous years debt servicing should absorb a fair portion of the country's export earnings. The higher import capacity should enable the government to increase the foreign exchange allocation for raw materials imports for industries.

Prices

At best the living costs may not rise sharply during 1977. Few prospects are seen, however, for lower prices. Among the locally produced commodities, the prices of coconuts should remain high during the first few months of the year with the prospect of prices coming down slightly by around May, tea prices to the local consumer should continue to remain high throughout the year and reflecting the higher paddy crop the open market price of rice should show a decline. The government has decided to import textiles and this should increase the availability of textiles to the consumers and thereby ease the existing shortages in the local market.

The government has already decided not to pass on the higher import cost of petroleum products to the consumer and has thereby prevented a potential inflationary trend via higher transport and manufacturing costs.

Employment

Certain measures have already been implemented since late 1976, to increase public sector employment. Absorption of about 7000 unemployed graduates and several thousands of Advance Level qualified persons into the teaching profession, recruitment of additional health personnel at middle level, and a substantial increase in the intake of various categories of trainees under the National Apprentice Board and for other vocational training centres are among the employment creation programme that have been implemented so far. Development programmes based on the land reform and the settlement schemes under the Mahaveli Project will be two other important avenues of employment creation during the year. The implementation of 2800 projects under the DDC programme during 1977-78 is estimated to create employment opportunities for about 82,000 persons. Despite these measures however, unemployment will continue to be the major problem in the economy in 1977. Although precise figures are not available, the number of unemployed persons in the economy can be estimated to be around one million or approximately 20 percent of the labour force.

Political Events

Finally, it may be noted that 1977 is an election year and that political developments could have substantial effect on the economic picture that will finally emerge. In the uncertain political climate that characterises an election period, the tempo of economic activity particularly in the public sector, may witness some slow down and the nature of the outcome of the elections should be an important factor that will shape the economic outlook during the final months of the year. Hence, besides factors such as weather conditions and the world market developments, a third important though uncertain element in the economic outlook in 1977 is the impact of political events.