Sri Lanka's Prospects in 1979

The year 1978 was in many ways a transitional year for Sri Lanka's economy — a transition in the main from a controlled to a liberalised economy. This year (1979) should witness the completion of this transition in most spheres of economic activity with the economy clearly shifting from various controls and restrictions on private enterprise that characterised the past several years and with an increased role for the market mechanism in the determination of resource use and development. In 1978 the economy was able to achieve a growth rate of over 8 percent. At the same time the transition to a liberalised economy required the establishment of a new (higher) price level resulting in an inflation rate of about 16 percent. All indications are that in 1979 too, the economy would continue to show a growth rate higher than the past levels of the 1970s and the rate of inflation too would continue to be high. The economic growth in 1979 would largely be a result of the higher output of industry, trade, transport and construction rather than of agriculture.

As in the case of most other countries, particularly those in the Asian region (see Foreign News Review), the impact of the regular and at times erratic increases in oil prices by producer countries is bound to be felt in 1979 by Sri Lanka too. Much will depend, however on the extent to which such price increases will have to be borne by the consumer in the course of this year. There is no doubt that increased local oil prices will inevitably lead to a need for adjustment in the entire price structure, and major changes in government's budget to cover whatever deficits that arise.

Agriculture

In the agriculture sector, there is no basis to expect any significant increase in the output of any of the major crops. The 1978/79 Maha paddy crop is estimated at 63 million bushels compared with 62 million in the previous Maha. The crop could have been bigger if not for the cyclone damage (particularly in the Eastern province). The size of the Yala crop this year would probably be in the range of 28-30 million bushels. On this basis the total paddy crop harvest this year would either be at the same level of last year (91 million bushels) or at best would show some marginal improvement. In this context it is unlikely that rice imports would show a further decline this year. In fact it is very likely that the volume of imports would be close to 200,000 tons as against 166,000 tons last year. On the other hand wheat flour imports are expected to record some decline this year, reflecting the slight decline in demand following the price increase of August last year and the relative stability in the market price of rice which will continue to be an important feature in 1979 as well.

Overall plantation output is unlikely to show any significant increase. Tea production (which was 199 million kgs. in 1978) is officially estimated to rise to about 209 million kgs. this year. But it is doubtful whether this expected increase could in fact be realized. The recorded production in the first quarter of this year (49 million kgs) shows no improvement over the corresponding period last year. Tea prices in 1979 are expected to record an average somewhat below the 1978 level and this price decline in the context of the relatively high level of export taxation and the rise in production costs could lead to an erosion of the profit margins of tea producers.

The rubber industry has entered a price boom since the beginning of this year and with synthetic rubber prices indicating a sharply rising trend (as a result of the petroleum price hike) the rubber boom is expected to accelerate further in the coming months. This should raise the profit margins of rubber producers and if weather conditions remain favourable rubber production is certain to show an increase. In the first quarter of this year, the production (at 38 million kgs.) had remained roughly at the same level as that of the corresponding period last year.

Coconut production is officially forecast to show a decline reflecting (a) the cyclonic damage to about 30,000 acres of coconut in the Eastern Province and (b) the effects of the weather conditions. It may be noted, however, that coconut lands in the Eastern Province had never made any significant contribution to the total coconut production of the country since productivity of such lands had been far below the average level. Assuming that the decline in the crop would be around 10 percent, the production this year should be around 2,000 million nuts. The volume of coconut oil exported in the first quarter of this year showed a decline over the same period of 1978 but this was more than offset by an increase in the export volume of desiccated coconut.

In the case of subsidiary food crops, the year 1979 is unlikely to show any significant change. The Government's attempts to balance the producer and consumer interests by the maintenance of buffer stocks is likely to result in relatively stable market prices for most of these crops. If such buffer stocks are built up through imports (which are generally cheaper than the local products) domestic prices tend to get stabilized at a lower level thereby reducing producer margins. The policy measures adopted in the agrie cultural sector continue to reflect conflicting objectives, particularly between the need to assure reasonable prices to the consumer and remunerative prices to the producer.

Fisheries and Livestock

Among the other primary activities, the fisheries and livestock industries should show some output increases this year. The fishing fleet in the Eastern Province was damaged by the cyclone but despite this factor fish output is expected to show a fair improvement particularly in view of the new incentives being offered to the fisheries sector. Fish production in the first quarter of this year is estimated at 39,347 tons compared with a production of 35,800 tons in the first quarter of 1978.

The increase in the purchase price of milk and the reduction in animal feed prices effected in November 1978 are expected to improve the level of milk production during 1979. The Milk Board's collections during the first two months of the year had shown an increase of 8 percent over the same period last year. (The increase was 5 percent in January and 12 percent in February). This increase probably reflects the impact of improved incentives being made available to the producers.

Mining and Quarrying

The output of the mining and quarrying sector which recorded a substantial expansion last year is expected to show a still higher rate of growth this year due principally to the increasing production of bricks, tiles, sand and quarrying and this is a reflection of the boom in construction activity.

Besides the new public construction work planned for this year, there will also be added construction activity in connection with the rehabilitation after the cyclonic damage of November 1978.

Power

It may be noted that some important projects such as the Maduru Oya dam project and the Bowatanne power project received a setback as a result of the cyclonic damage. The Bowatenne project which will provide for a 40 MW hydro-power plant would now be completed only in early 1980 and not in 1979 as originally planned. The existing power supply situation has become critical with the rapid growth in consumption and emergency measures are being planned to meet a possible crisis situation anticipated in early 1980.

Industry

Production in the industrial sector is expected to maintain the momentum it gained in 1978, following the policies of import and exchange liberalization.

The increased imports of machinery, equipment, spares and raw materials are expected to continue and lead to a further rise in factory output this year. Another indication of increased industrial production in 1979 is evident in the large numbers of new industrial units which were granted approval during 1978 and in the first three months of this year.

The Ministry of Textile Industries alone approved 1,315 units in 1978 with an anticipated investment of Rs. 454.3 million and an estimated employment of 20,153. The bulk of these new investments is expected to materialise during 1979.

The Ministry of Industries and Scientific Affairs also approved as many as 1,070 new units during 1978. These are expected to have a total investment of Rs. 606.5 million of which the foreign component would be Rs. 503 million. The estimated employment potential in these units is 23,191. During the first three months of this year a further 213 units received approval from the Ministry of Industries and Scientific Affairs.

Many of the new industrial units approved over the last 15 months are expected to commence production in the course of this year. In addition, nearly 29 units in the Free Trade Zone are also expected to be in production by the end of 1979. All indications are that the overall increase in the country's factory output would provide an important contribution to GNP growth this year.

No major public sector industrial projects are expected to be completed this year. All major industrial projects presently under implementation, namely the urea fertilizer, nylon, steel stage II, and refractories projects, are expected to be completed only in 1980.

Banking and Finance

In the banking and financial sphere, a major problem the monetary authorities would have to face this year is to restrain monetary expansion. The enhanced level of economic activity and the rise in prices and wages are bound to put pressure on the banking system for credit expansion. During January-March this year alone the money supply increased by Rs. 815 million or 14 per cent over the level at the end of 1978. By comparison, during the whole of 1978 the money supply rose by only Rs. 570 million.

The rate of inflation in the economy (which was about 16 percent last year) is unlikely to show a marked decline. In January, the Government raised the excise duties on tobacco and liquor which resulted in an increase in prices of these items to the consumers. The series of price increases announced by the petroleum exporting countries should lead to a rise in the local prices of petroleum products. One alternative suggested is that the Government should effect price increases, particularly for kerosene and diesel which are at present heavily subsidised. A rise in price of diesel could bring about a general rise in transport costs—particularly commercial transport, resulting in vegetables and other foodstuffs going up in price. Increases in the cost of petroleum and diesel oil could push up the cost of production in the plantation industry and manufacturing industrial sector, and would also inevitably result in the increase of costs on all development projects. For instance, an estimate of the likely increased cost of the country's biggest development project, the Mahaweli Development Project, (if petroleum prices move up by about 50 percent from the existing Rs. 20/- per gallon and also if diesel prices were increased) foresees the overall cost of the accelerated programme going up from the present Rs. 12-15 billion to over Rs. 18 billion.

Other proposals being considered to face the upheavals in the economy caused by increasing petroleum prices and global inflation are possibilities of a reduction in the consumer subsidy on wheat flour and substitution of the rice ration by food coupons to be followed by another round of wage and salary increases. Much would depend, however, on the extent to which the economy can bear these subsidies. But given the Government policy of maintaining buffer stocks for certain important food items and the improved rice supply position in the local market, the prices of most food items are unlikely to show any sharp increase during the year.

Trade

The balance of trade should continue to show a deficit this year and the size of the deficit would in all probability be larger than last year. In the first two months of the year, the import bill exceeded the export earnings by as much as Rs. 1,140 million. The total import bill this year is expected to be higher than last year. The export earnings should also rise but would lag behind the growth of import expectations. The anticipated decline in tea prices should adversely effect export earnings from tea but this is likely to be offset by the high earnings from rubber. If the trend seen in 1978 and the first quarter of 1979 continued for the rest of the year, export earnings from gems and ready-made garments should also record a considerable increase.

The official target for garment exports this year has been set at Rs. 750 million as against an actual export value of Rs. 414 million last year. The export value of garments during the first quarter amounted to Rs. 142 million. During the first quarter of 1979 tourist arrivals (77,592) showed an increase of 18 percent over the corresponding period in 1978 and this is an indication that earnings from Tourism should show a definite rise during the year.

The bulk of the trade deficit will be financed by foreign borrowings and also by drawing on the external assets built up over last year. The external assets which stood at Rs. 7,500 million at the end of 1978 fell by Rs. 300 million in the first two months of the year.