THE GULF CRISIS THE WORLD AND THE SRI LANKAN ECONOMY: SOME REFLECTIONS

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The Background

The Middle East is the natural crossroads of the "old world" or the Afro-Eurasian land mass and the new world – Europe. It is also the "land of the seven seas". Its main resource is oil. About two – thirds of the world's known oil reserves are in this area. Middle East is also a living mosaic of physical types, beliefs, systems, languages and cultures.

On August 2, the Iraqi army entered into the neighbouring Kuwait and occupied that tiny oil rich sultanate. Indeed as events unravelled from day to day at an alarming pace, it was crystal clear that no nation would be left untouched by this move. Saudi Arabia's rulers fearful that Saddam would attack them next agreed to an American request for troop deployment. Refugees began pouring across borders to Saudi Arabia, Syria, Jordan, Turkey, Sri Lanka, India, the Philippines, Pakistan and Bangladesh. Thus events in the Gulf is and will continue to affect Third World countries like Sri Lanka deeply.

The Beginning of the End of the Age of Oil

Iraq's invasion of Kuwait will go down in human history as the beginning of the end of the Age of Oil. A historic shift is in the air. Disorder in the Persian Gulf is looking more like the norm than the exception. The world is realizing that it cannot rely exclusively on Middle East oil. Therefore, the world will most likely respond to this crisis with a concerted hunt for alternatives, starting with non-OPEC oil. That's logical, because the dark goo that provides 39% of the world's energy, more than any other sources, will be a staple of the global economy for decades. Neither coal, which is the second largest energy provider with 28 % of natural gas, with 21% can quickly replace oil, particularly as a transportation fuel.

But explores aren't likely to find enough new oil resources to make OPEC a non factor in world energy. After the oil price hikes of the 70's, the industry mounted a rig-spinning exploration and development campaign outside OPEC that produced some new suppliers, nainly Mexico, Alaska and the North Sea. This together with conservation, brought down the prices of oil in 1986. But then the demand revived and non-OPEC countries oil production could not keep pace with this increasing demand. When oil consuming countries wanted growth, they had to draw once more from the wells of OPEC. And they have been returning in such numbers recently that cartel's spare capacity has dwindled from 12 million or 13 million barrels a day in the mid '80s to 4 million. Thus governments and consumers will probably become more willing to pay a premium for non-oil energy such as natural gas and coal, within their own borders, with a view to maximising control of their energy sources. The most likely consequence would be a long, slow ascendance of natural gas which is more available than oil and is evenly distributed globally. (See Table 1)

Table I
OIL VS GAS
WHO HAS THE MOST

Share of World Reserves in	Oil	Gas
Middle East	65.2%	30.7%
Latin America	12.5%	5.8%
USSR and E. Europe	5.9%	38.3%
Africa	5.9%	6.7%
Asia including Australia/NZ	4.5%	7.1%
North America	4.2%	6.5%
W.Europe	1.8%	4.9%

Source: Fortune 1990 Sept.

An U.N. embargo against Iraq-Kuwait, if effective will remote around 4 million barrels of crude and refined products a day from a world market that consumes about 65 million barrels a day. There is enough spare capacity in Saudi Arabia, the U.A.E. and Venezuela to make up the shortfall. Since there is a need to avoid dislocation, oil companies are raising oil prices and prices are likely to set around $ 25-30 per barrel for some time.

After that there are two possible outcomes.

(a) A relatively uneventful seige of Iraq followed by a peacefull resolution and a return to the status quo.

(b) A shooting war breaks out disrupting Saudi Arabia's production of 5 million barrels a day or the Emirates 2 million barrels or both. This would create the world's first serious crude oil shortage since World War II and drive prices to unpredictable heights.

The USA is the most drilled-up land on earth with 600,000 of the world's 900,000 producing wells. An average well produces about 15 barrels a day in the US vs 9,000 barrels a day in Saudi Arabia. Oil production fell in USA in 1989 by 6% and imports accounted for around 50% of US needs compared with less than 30% in 1985. The world can use several strategies to overcome the shortage of oil.

(a) Increasing exploration and development
(b) Stepping up conservation
(c) Switching to alternative fuels
(d) Develop national energy strategies and policies
(e) Promotion of natural gas as a fuel for fleets or cars and trucks
(f) Improve the gasoline efficiency of cars
(g) Raise tax on gasoline say at US 5 cents per year per litre for the next 20 years
(h) Boost research into alternative sources of energy
(i) Expand the strategic petroleum reserve.

Many nations will be considering similar options in the years ahead and their collective actions is likely to create massive changes in the energy business. The oil industry will embark on its last great hunt, BP estimates that of the 1,300 sedimentary oil basins in the world, 300 remain unemplored because they were too remote or because politics, had placed them off limits.

Both conditions are changing. Technology is bringing far off basins such as those of ocean beds of upto a mile within reach.

Table II

OIL GIANTS

EXXONS	–	US$ Revenue 86.6 billion Profits - $ 3.5 billion
(US)		Source of Crude Imports 22% OPEC, 29 % Angola, 6% Oman, 16% Colombia, 17% Others
MOBIL	_	Revenue – US$ 51 billion Profits – US$ 1.8 billion
(US)		Sources of Crude Imports – 33% OPEC, (12% from Iraq) 32% Canada, 11% UK, 24% Mexico
ROYAL DUTCH SHELL (UK/Neth)	–	Revenue – US$85.5 billion Profits – $6.5 billion Sources of Crude imports 56% OPEC, (22% from Iraq) 19% Mexico, 17% Yemen, 6% Canada, 2% Others
BRITISH PETROLEUM (UK)		Revenue – US$ 49.5 billion Profits – $3.5 billion
		Source of Crude: 86% OPEC (all from Nigeria) 8% UK, 2% Zaire, 4% Colombia

Source: Fortune 1990 Sept.

Table III

WHERE THE OIL FLOWS

Exporter	Proved Reserve (Mln Bbls)	Main Markets
Mexico	54,100	US 52% Spain 16% Japan 6% France 5% Brazil 2%
Canada	6,800	US 96% Japan 0.7% N'lands 0.2%
Venezuela	58,100	US 44% N. Antiues 15% Germany 9% Canada 3%
Ecuador	1,400	S. Korea 33% US 23% Puerto Rico 16% Panama 5%
Colombia	2,000	N. A
Argentina	2,300	N. A
Nigeria	16,000	49% US 11% Spain 8% Germany 6% France 6% N'lands 36% Italy 26% Germany 10% Spain 9% France 8% Greece
Angola	2,200	N. A
Egypt	4,300	N. A.
Algeria	8,400	33% Italy, 15% Spain, 14% Germany 10% US 7% France
Gabon	720	31% France 27% N'Lands 11% Brazil 10% US 3% Korea
Saudi Arabia	255,000	14% Japan 25% US 6% France 5% Baharin 5% Singapore
Iraq	100,000	US 16% Brazil 11% Turkey 11% Japan 7% USSR 7%
Iran	92,000	N'lands 14% Japan 12% 9% Italy Turkey 7% Belgium 7%
UAE	98,100	Japan 47% Italy 7% Singapore 7% US 5% S. Korea 5%
Kuwait	94,500	Japan 27% N'lands 17% US 12% Italy 9% Brazil 4% S. Korea 4%
Qatar	3,200	Japan 58% France 11%

Source: Fortune 1990 Sept.

Table IV

IMPORTS OF OIL

Country	Annual Amount (Millions of bbls)	Imports as a% of total Consumption
Brazil	223	53
Chile	30	86
USA	2,421	45
Germany	674	97
France	483	96
Italy	461	93
N'lands	352	94
Spain	338	97
Belgium	172	99
Sweden	104	95
Czechoslavia	120	99
Poland	110	99
Hungary	62	82
Japan	1,191	99
S. Korea	261	100
Singapore	252	100
India	130	38
Philippines	74	97

Table V

Iraq's and Kuwait's main oil importers

US	imports	7%	of its oil from Iraq	2%	from Kuwait
Brazil	,,	38%	,,	5%	,,
France	,,	9%	,,	0	,,
Italy	,,	13%	,,	–	,,
N'lands	,,			14%	,,
Spain	,,	10%	,,		
Belgium	,,	8%	,,	–	
Japan	,,	–	,,	6%	,,
S. Korea	,,	–	–	4%	,,
Singapore	,,	–	–	2%	,,
India	,,	20%	,,		
Philippines	,,			10%	,,

Source: UN / OPEC Publication Oil & Gas
Journal International Energy Agency

The Gulf Crisis and Sri Lanka

With this background a Third World developing country like Sri Lanka which is totally dependent on imports of oil and gas and exports of tea and on migrant workers earnings would find it difficult to meet the sudden economic and social catastrophy created by the Gulf crisis.

Gulf Crisis and Foreign Aided Projects

Kuwait along with Japan and the World Bank has funded the tertiary irrigation works in Zone 3 to 6 in System C of the Mahaweli. The total loan works out to Rs 8.4 billion (US$ 263 milion) of which Kuwait has already disbursed KD 9.4 million and a sum KD 3.5 million is yet to be received from the Kuwait Fund. The loan is valid till 1993. Japan has loaned through the OECF £7,700 million, £ 2,950 million as loan/credit and Rs 3,300 million as Food Aid. Nearly 95-100% of this has been used. The IDA has disbursed Rs 4,068.15 million (73.3 SDR million) as loans of which 67% has been used and 24.5 million SDR are remaning to be used.

68% of the loan from Kuwait Fund has been used. Loan funds are used to complete downstream irrigation infrastructure in zone 3 and 4, development of blocks 409 and 410. D Canals and F Canals in Zones 5 and 6. Rough levelling, jungle clearing, on farm development improvements to the drainage system, water management training, O & M settlement of 17,200 new farm families are planned under this loan. The benefit accrued so far have been in paddy cultivation in Zones 3-6 from Yala 1988. The area cultivated has increased from 7,711 ha in Yala 1988 giving a yield per ha of 4.1 tons and a production of 30,179 metric tons of paddy to 9,825 ha in Maha 1989/90 with average yeilds of 4.7 per tons/ha yielding 43,869 metric tons of paddy. Other field crops includes 400 ha in Yala 1989 with chillies (140 ha), red onions (65 ha), cowpea, green gram, big onions (35 ha). There were about 9,342 farmers in Yala 1989 cultivating these crops. The Gulf Crisis makes the disbursement from Kuwait of KD 3.5 million doubtful but the shortfall may be financed by one of the other parties. If Kuwait as a country is wiped out and Iraq only treats it as a province Sri Lanka has no obligation to pay back its KD loan to Iraq since Iraq has no commitment under the loan. If it is written off Sri Lanka could gain by about KD 9.4 million.

Gulf Crisis and the Tea Market

Sri Lanka produces about 207million (1989) to 213.3 million (1987) kgs of tea from an area of 222,000 ha. High grown tea constitutes 35.7% of the total production, low growns 40.04% and medium growns 24.15%. Nearly 204.2 million kgs of made tea are exported, earning Rs 13,663.9 million (SDR 296 million). The value added as a percentage of GDP is 4.5 of total tea exports. Middle Eastern countries take in 58.26% (1989) of the total volume compared to 62.62%

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South Asian refugees in Jordan camp: Hunger had become an urgent factor

in 1988. This as a percentage of value is 55.17% (1989) compared to 59.50% in 1988. Volume wise the Middle East takes in 118.9-137.6 million kgs. Iraq takes in 24,166,000-33,958,000kgs or 12-16% of the total volume of export and 10-13% of the total value of exports. Kuwait imported 2,1-3.0 million kgs of tea which was 0.98-1.49% of the total volume or 1.20-2.15% of the total value. Thus as a result of the trade embargo the demand for nearly 172 million kgms of tea will (earning 15% of the total value of exports of tea) will fall. The value of the total export of tea to Iraq is Rs. 1.4 billion. Therefore we might have to look for new market as even reduce production.

The Gulf Crisis will undoubtedly affect our macro economic development. It will reduce our foreign exchange earnings and thereby affect our import capacity and the Balance of Payments. Increases in oil prices will affect our energy scenario and transport and production cost. It will also affect the cost of living adversely. Taken with the cost of the war in the North and East of Sri Lanka the effect of the Gulf crisis will be disastrous. The

Table VI

Country Classification of Tea Exports and Percentage Share : Middle East

Country	(Volume Mln Kgs)				% of Total Volume				Value (Rs, Mn)				% of Total Value			
	1986	**1987**	**1988**	**1989**	**1986**	**1987**	**1988**	**1989**	**1986**	**1987**	**1988**	**1989**	**1986**	**1987**	**1988**	**1989**
Iraq	22.7	29.7	33.9	24.1	11	15	15	12	822	1382	1627	1403	8.9	12.9	13.2	10.3
UAR	40.4	37.7	35.4	33.8	19.4	18.7	16	16	1671	1900	1830	1974	18.06	17.84	14.8	14.4
S. Arabia	12.9	14.4	14.6	11.9	6.2	7.2	6.6	5.8	787	974	1001	1069	8.5	9.1	8.1	7.8
Syria	13.4	9.6	11.4	10.0	6.4	4.8	5.2	4.9	466	396	501	476	5.0	3.7	4.1	3.4
Iran	10.0	15.9	12.3	12.6	4.8	7.9	5.5	6.2	412	817	722	890	4.4	7.7	5.8	6.5
Jordan	4.3	3.5	5.1	3.9	2.1	1.8	2.3	1.9	233	224	319	220	2.5	2.1	2.6	1.0
Kuwait	3.1	2.1	2.1	3.0	1.5	1.0	0.9	1.5	175	149	148	294	1.9	1.4	1.2	2.1
Yemen	4.1	4.5	6.2	4.5	1.9	2.2	2.8	2.2	152	207	313	253	1.6	1.9	2.5	1.8
Libya	–	–	7.3	6.4	–	–	3.3	3.2	–	–	433	448	–	–	3.5	3.2
Others	8.6	7.8	9.2	8.4	4.1	3.9	4.2	4.1	374	423	424	520	4.05	3.97	3.4	3.8
Grand Total	207.8	201.1	219.8	204.2	100.0	100.0	100	100	9253	10653	12299	13664	100.0	100.0	100.0	100.0

Source: Central Bank

Table VII

Direction of Trade

	Exports					Imports (Rs Million)				
	1985	1986	1987	1988	1989	1985	1986	1987	1988	1989
Iraq	1468.5	8429	1394.0	1627.6	1406.8	2.0	101.2	103.3	76.8	356.5
Kuwait	263.2	215.4	198.0	206.9	352.9	242.6	53.4	116.6	186.2	199.4

Source: Sri Lanka Customs,Central Bank of Sri Lanka

Budget deficit in 1991 is expected to be 9% of GDP compared to 10% in 1990. The budget estimate for 1990 was Rs 103 billion (US$ 2.6 billion) compared to Rs 139 billion (US$ 3.4 billion) in 1991. The revenue in 1991 is estimated at Rs 72 billion (US$ 1.8 billion) which brings in a budget deficit of Rs 67 billion (US$1.6 billion). Part of this gap is to be financed through revenue and other through loans and foreign aid. But if the Gulf Crisis results in a drop of tea reserves the budgetary gap would increase. Meanwhile the foreign exchange income that Sri Lanka received from 100,000Sri Lankans in Kuwait and 35,000 in Iraq will also be affected.

Other non-traditional exports to Kuwait and Iraq will also be affected leading to problems in these sectors.

Gulf Crisis and Remittances from Abroad

The net private transfers between 1986-1989 showed an increase from Rs 7.883 million (SDR 242 million) to Rs 10,844 million (234 mn). This consisted mainly of the remittances by Sri Lankans working abroad. The remittances are in the region of SDR 263 million. 150,000 Sri Lankans who lived in Kuwait were remitting around US $ 100 million. There were about 40,000 Sri Lankans in Iraq. There are a fairly large number in Saudi Arabia, Oman, Quatar, UAE and Iran, and if the Gulf crisis continues, they too are likely to return to Sri Lanka. This could result in a decrease in foreign remittances. In 1991 the loss in foreign exchange from remittances will be in the region of US $ 400 million, which is equal to Rs. 16 biilions.

This will have adverse consequences on the following:

(1) The Balance of Payments
(2) The urban property and real estate market
(3) The dependent families
(4) The purchasing power of these dependent families
(5) The returnees will have problems of adjustments and finding lucrative employment.

At the time of Gulf Crisis occured there were 30,000 foreigners from the developed Kuwait and Iraq. They were:

Gulf Crisis and other Imports

The Gulf Crisis will undoubtedly have impact of the imports of consumer, intermediate and capital

Table VIII

Nationality	In Kuwait	In Iraq	Total
American	2,500	600	3100
British	4,000	700	4,700
French	290	270	560
Japanese	278	230	500
Soviet	880	7,830	8,71
Other European	-	-	3,17

Source: Newsweek Aug. 27, 1990

The victims of the Gulf War from Third World countries included.

Table IX

	Indian	Pakistani	Bangladesh	Sri Lankans
Pre-invasion number in Kuwait	172,000	90,000	70,000	90,000
Pre-invasion number in Iraq	10,000	8,000	15,000	n.a
Number in Jordan (Sept. 4)	22,500	10,000	28,000	16,000
Evacuated through Jordan	14,000	9,000	1,500	1,000

Source: Economist Sept 8, 1990

Sri Lanka imports about Rs. 8,716 million of petroleum which amounts 10 - 14% of our total import bill.

Table X

Year	Value Rs Million	Value is SDR Million	%of total Imports
1987	87,116	128.7	14.4
1988	7,839	183.3	11.0
1989	8,376	181.3	10.4

Source: Central Bank of Sri Lanka

Fertilizer is mainly inaqauic petro Chemical based. therefore the price of fertiliser too will go up. Imports have been as follows:

Table XI

Year	Value Rs Million	Value in SDR Million	% of total Import
1987	1,299	34.1	2.1
1988	2,476	57.9	3.5
1989	1,755	138.0	2.2

Source: Sri Lanka Customs

Any increase infertiliser prices are going to have a direct impact on productivity.Sri Lankals requirement of crude petroleum is'9 - 14 million barrels. Fertiliser imports are 355,000 - 556,000 metric tons.

Table XII

Crude oil imports have been as follows:

	1983	1984	1985	1986	1987	1988	1989
Quantity MN Bbls	11	13	12	12	13	14	9
Value Rs Mn	7,832	9,542	9,486	5,296	78,121	6,726	5,896
C & F Rice R/Bbl	714	751	777	439	544	484	628

Source: Sri Lanka Customs

Main Source of crude oil for Sri Lanka is Iraq and this is bartered for black tea. Therefore, Sri Lanka will have to find new sources of supply.

goods from economies which themselves have problems due to the Gulf Crisis. The cost of production in these countries would have gone up and fuel price adjustments would be reflected in shipping and handling charges. Thus, import cost will go up and this will add to the already high level of inflation. The composition of imports reveals that 26.1% are consumer goods of which 16.4% are food and beverages. Intemediate goods constitute 56.6% of which the prices of petroleum (10.4%) textile and clothing (12.4%) and wheat (6.2%) would increase. Investment goods constituting 15.0% of the total imports cover machinery and equipment (7.8%), transport equipment (2.3%) and building materials (1.2%) The final result will be an increase in the cost of living which will adversely affect the quality of life of the people. There will be an increase in freight and insurance by about US $ 50 million in 1991. This is going to increase the cost of imports and will result in a decrease in imports. There will also be a decreased demand for Sri Lankan exports, particularly manufactured goods because of the increased recession in developing countires as a result of the gulf crisis. High rates in insurance will bring about an imbalance in banking transactions.

Gulf.Crisis and Tourism

Tourist industry has been experiencing a downward trend since 1983 (due to the ethnic conflict or later the JVP insurgency). This has been further aggravated by the current war in the North East. There was a marginal improvement in 1989 and 1990 the Gulf War will affect this adversely. Airline and shipping costs are going to increase. So are other related local costs like transport, hotel and food charges. The tourist arrivals which stabilised at 101,910 in 1989 will dwindle down to about 80,000-90,000 and income from tourism would level off to about Rs 2,000 million from Rs 2,749.5 million in 1989. The average spending of tourist per day which increased from Rs 848.71 in 1985 to Rs 1,396.00 cts in 1989 will dwindle to around Rs 1,000-2,000 tourist per day.

The Gulf Crisis and Socio-economic Problems

The Gulf Crisis is sure to have rippling effects on our socio-economic structure and aggravate as already adverse situation. The majority of the returning migrant workers will swell the already large goal of unemployment and underemployed.

The returnees will find it difficult to fit into other places of employment since **no contingency plan for returnees from abroad has been formulatd.** There are no self employment projects and the banks have not come out with any plan to create employment for returnees.

The boom in the property market and the demand for durable is likely to dwindle. Increase in uneployment and servere inflation will aggravate a number of social and economic problems. Therefore, the government should come up with a contingency plan to meet this crisis.

The Gulf Crisis and Alternative Development Strategies for Sri Lanka

Sri Lanka can adopt several strategies to overcome the above described scenario resulting from the Gulf Crisis.They are:

(a) Stepping up production of food items domestically
(b) Stepping up energy conservation measures
(c) Switching to alternate fuels
(d) Development of hydro-power
(e) Promotion of natural gas fuel fleets in Sri Lanka
(f) Improve gasoline efficiency of cars
(g) Re-cycle the used oil through filteration and re-processing
(h) Raise the price of gasoline annually
(i) boost research into alternate energy sources
(j) Explore potential areas for oil
(k) Build a 3 month buffer stock in each province to meet any contingency.

No government can do anything unless the population is ready and willing to cooperate. But to find a solution can only be an alternative contigency plan for energy. ■