

## ECONOMIC INDICATORS UPTO 1988

From the Public Investment Programme  
1982 - 1983.

### Domestic Resources and their Utilization

In terms of 1984 prices the GDP is expected to increase to about Rs. 155.4 billion in 1988, which is an increase of 6.9 percent per annum. Table I shows the domestic resource availability and the resource gap.

During the period 1984-88, the Government expects to achieve a structural transformation in resource utilization. Recent trends in the country have recorded levels of total investment averaging 28 percent of GDP. However, such levels of investment are unsustainable especially in the face of tight resource constraints. A substantial reduction in the ratio of investment to GDP has been achieved and during 1984-88, a further reduction of this ratio is envisaged - to about 25 percent of GDP from its level of 27 percent in 1984 (see Table 2). Further, restraints on public capital expenditures are expected to release resources for private sector development. Thus, the relative share of private sector investment is projected to increase and finally overtake public sector a capital spending by 1987 - 88.

In order to achieve the desired levels and structure of total investment, domestic savings are assumed to play a greater role than in the past. Both the public and private sectors are projected to contribute positively to this end. In fact, private savings are projected to grow faster and reach a level of 15.7 percent of GDP in 1988 as against 11 percent in 1984. (See Table 2). Net external inflow is projected to decline and this slack has to be taken up by the private sector.

#### Budgetary Outturn - 1984 - 88

Due to favourable developments in the prices of plantation crops, it has been possible to revise expectations about likely government revenue. It is expected that in 1984 approximately an additional Rs.1,500 million could

TABLE I

### Domestic Resources and the Resource Gap (Rs. Million)

	1983	1984	1988	Average Annual Growth Rate 1984-1988
1. GDP at current factor cost	111.3 (91)	127 (90)	155.4 (90)	6.9
2 Add indirect taxes less subsidies	10.9 (9)	14.4 (10)	18.0 (10)	10.6
3 Equals GDP at market prices	122.3 (100)	140.1 (100)	173.5 (100)	7.2
4 Exports of goods and non-factor services	31.9 (26)	41.3 (29)	52.8 (30)	10.6
5 Imports of goods and non-factor services	50.4 (41)	57.2 (41)	65.4 (38)	5.3
6 Resource gap	18.5 (15)	15.9 (11)	12.6 (7)	- 7.4

Note : 1 As percentages of GDP at market prices within brackets.

2 Figures for 1983 and 1984 are at current market prices while those after 1984 are at 1984 constant prices.

TABLE 2  
Total Resources and their Utilization  
(Rs. Billion)

	1983	1984	1988	Total 1984-1988
1 Total Resources	140.8 (115)	156.1 (111)	186.1 (107)	853.2 (109)
(a) GDP at market prices	122.3 (100)	140.1 (100)	173.5 (100)	783.4 (100)
(b) Net imports of goods and non-factor services	18.5 (15)	16.0 (11)	12.6 (7)	69.8 (9)
2 Total Utilization	140.8	156.1	186.1	853.2
(a) Consumption of which	105.3 (88)	118.6 (85)	142.3 (82)	650.3 (83)
- Private	95.6 (78)	107.9 (77)	129.5 (75)	592.2 (76)
- Public	9.7 (8)	10.7 (8)	12.8 (7)	58.1 (7)
(b) Investment of which	35.5 (29)	37.5 (27)	43.8 (25)	202.9 (26)
- Private	16.5 (13)	16.6 (12)	23.2 (13)	96.6 (12)
- Public	19.0 (15)	20.9 (15)	20.6 (12)	106.3 (14)
3 Financing of Investment				
(a) National Savings	20.2 (17)	24.4 (17)	33.6 (19)	145.9 (19)
(b) Foreign Savings	15.3 (12)	13.1 (9)	10.2 (6)	57.0 (7)

Note : 1 Figures in brackets - indicate percentages of GDP.

2 Figures for 1983 and 1984 are at current market prices while those after 1984 are at 1984 constant prices.

be collected from the ad valorem tea tax. Present export price trends indicate that this is an easily realizable target. In the case of the export duty on rubber, an increase of about Rs.350 million is expected in 1984. Import duties are likely to yield an increment to earlier budgeted figures amounting to over Rs.300 million. A further inflow of Rs.350 million is expected as contributions from the surplus of public corporations in accordance with a recent government decision. These and other factors are expected to increase government revenues by over Rs. 2,300 million in 1984. Total current receipts are projected to be around 22 percent of GDP during the period of 1984-88.

During the last six years the major part of capital inflows came in the form of official transfers and concessionary loans. This explained to a large extent how the country was able to step up investment expenditures and sustain comparatively large deficits in the balance of payments and in the government Budget. The strategy for the next five year period involves a progressive reduction of the resource gap and stabilizing investment expenditures at a level consistent with the growth targets spell out earlier. However some increases in foreign aid commitments and disbursements are required in the future.

The implications of reliance on foreign aid and other forms of foreign borrowing on the future debt servicing commitments are under constant review. The external debt outstanding on account of commercial borrowing increased from SDR 81 million at the end of December 1980 to SDR 614 million at the end of September 1983. The total disbursed external debt excluding borrowings from the IMF and short-term debt, expressed as a percentage of GDP increased from 36 to 42. Given that, the increase in external debt occurred at a time when the international interest rates were high, it is very likely that the debt service payments will cause a considerable strain on the country's balance of payments in the coming period.

**TABLE 3** Balance of Payments 1983, 1984 & 1988 (1)  
(US \$ Million)

	1983	1984	1988
1. Merchandise			
(a) Exports	1056	1324	1678
(b) Imports	1920	2058	2361
2. Trade balance	-864	-734	-682
3. Non factor services (Net)	80	95	178
4. Factor services (Net)	-136	-168	-232
5. Private transfers (Net)	273	281	330
6. Current account balance	-647	-526	-408
7. Net aid disbursements	423	408	382
8. Direct foreign investments	38	43	50
9. Other MLT loans : Government	77	13	30
10. Other MLT loans : Private Sector and Public Corporations	74	111	20
11. Progress/Advance Payments	-17	-16	-17
12. Other financing items 2	52	-33	-68

Note: 1. Figures for 1983 and 1984 are at current market prices while those after 1984 are at 1984 constant prices.

2. Includes short - term borrowing errors & omissions valuation adjustments and changes in reserves.

**TABLE 4** Esports and Imports 1983, 1984 & 1988\*  
(US \$ Million)

	1983	1984	1988
1 Exports	1056	1324	1678
Tea Volume Mn. Kg.	158	190	200
Value	352	507	534
Rubber Volume Mn. Kg.	125	120	120
Value	121	142	142
Coconut Volume Mn. nut.	588	422	635
Value	59	72	108
Gems	41	46	67
Petroleum Products	115	141	187
Other Industrial goods	261	289	462
Minor Agricultural products	84	91	144
Other exports	23	37	35
2 Imports	1920	2058	2361
Rice Volume Th. mt.	147	50	0
Value	32	11	0
Wheat flour Volume Th. mt.	0	0	0
Value	0	0	0
Sugar Volume Th. mt.	315	200	145
Value	84	48	35
Wheat grain Volume Th. mt.	578	569	600
Value	99	98	104
Fertilizer Volume Th. mt.	192	305	387
Value	27	46	58
Petroleum (i) Crude Oil Th. mt.	1502	2055	2180
Value	332	450	477
(ii) Products Value	135	75	131
Other consumer goods Value	263	304	325
Other intermediate goods Value	444	481	627
Investment goods Value	514	539	598
Unclassified	11	6	6

Note: Figures for 1983 and 1984 are at current market prices while those after 1984 are at 1984 constant prices.

increase in paddy production which has taken Sri Lanka near to its goal of self-sufficiency in rice. Paddy cultivation provides employment to about six hundred thousand persons and occupies one fifth of the arable land of the country. Furthermore, paddy is predominantly a small farmer crop as there are more than 1.6 million parcels of cultivation of which about 74 percent are less than one hectare in extent. Therefore, increases in production as well as in the price of paddy tend to contribute to employment and income distribution in the rural sector. The production of paddy which in Maha and Yala of 1976/77 totalled 80 million bushels exceeded 118 million bushels in 1983/84. Much of this increase has been due to better production methods, improved seed varieties and greater utilization of inputs such as fertilizer rather than due to increase in the area cultivated. As a result, there has been a significant improvement in the average yield per acre which rose from 47.7 bushels in 1977 to 69.7 bushels in 1983. It appears that the price incentive has been a major factor which induced the farmers to increase production and a marketable surplus. The Guaranteed Price which stood at Rs.33 per bushel in 1978 was steadily raised to Rs.62.50 by 1983 while the open market price has risen to over Rs.75 per bushel over the same period.

However, the performance of the export oriented plantation sector over this period has not been as impressive as that of the domestic agriculture sector. There was only a slight improvement in the value added by tea, rubber and coconut production taken together, during the 1978-83 period. Compared with a negative growth rate of 1.7 percent recorded in the 1970-77 period even such a slight revival of the plantation crops was encouraging but it was not adequate to make any significant impact on the overall performance

**TABLE 2** SECTORAL GROWTH PERFORMANCE : 1970 - 77 AND 1978 - 83

	Value (Rs. Million)				(Average Growth Rates %)	
	1970	1977	1978	1983	1970-77	1978-83
1. Gross Domestic Product (Constant Prices)	13,187	16,078	17,401	22,816	2.9	6.0
2. GDP Per Capita (Constant Prices)	1054	1153	1226	1472	1.3	4.1
3. Agricultural Sector	3732	4299	4532	5492	2.1	4.1
(a) Export Crops	1191	1052	1111	1081	-1.7	0.5
(b) Paddy & Others	2541	3247	3421	4442	3.5	5.3
4. Manufacturing Sector	2197	2357	2541	3014	1.0	4.2
5. Construction Sector	744	619	794	1028	-2.6	8.8
6. Services Sector	6419	8288	8315	12,548	3.7	7.2

Source: Central Bank of Ceylon Ministry of Finance & Planning

of the agricultural sector. As the agriculture sector accounts for more than one quarter of the Gross Domestic Product of Sri Lanka its performance influences the overall growth rate of the economy, far more than any other sector. Furthermore, the production trends of plantation crops become even more important due to their relationship with the export earnings of the country. Approximately 50 percent of the total export income of the country is derived from tea, rubber and coconut which also covers 41 percent of the average land of Sri Lanka. The decline in production of these crops perhaps, can be cited as the most adverse factor that the Sri Lankan economy has faced after the energy 'crisis', in the nineteen seventies.

The liberalization of exchange and imports was intended to act as an impetus to the manufacturing sector by making freely available more machinery, equipment, raw materials and modern technology as

well as by helping to expend the infrastructure facilities such as energy, telecommunications and transportation. Nonetheless the performance of the industrial sector so far has not been upto expectations as the share of this sector still remains at about 14 percent of the GDP; although there are signs of increased capacity utilization by both public and private sector industries. For example, from an estimated capacity utilization in the industrial sector of about 60 percent prior to 1977 it moved up to 70 percent in the year following liberalization and thereafter has shown gradual improvement, stabilizing at an estimated 76 percent by 1983. The annual growth in the industrial sector which was limited to about 1 percent on average during the period 1970-77, improved to more than 5 percent per year since then. In addition to the increased capacity utilization, the new investments and expansion of existing industries would have also contributed to this growth. In regard to new investments the enterprises set up in the Free Trade Zone

under the GCEC appear to have been a major source of growth particularly in the 1980's. There are mixed and divergent views about the impact of liberalization on the industrial sector and the government has initiated measures to streamline the incentives structure, tariff systems and other forms of assistance to this sector keeping within the broad framework of the open economic policy.

Focussing on the services sector, it is possible to identify at least two main types which are closely linked with economic activities. They are firstly, the infrastructure facilities such as transport, communication and energy; and secondly, the trade and commerce activities. On the one hand the liberalization of the economy helped as a supply mechanism towards

expanding infrastructure facilities through imports of vehicles, equipment and technology. On the other hand, the pressure of demand for infrastructure started building up rapidly and strongly consequent to the upsurge of economic activities in a variety of fields following the liberalization in late 1977. For example, the demand for electricity which had maintained a modest growth rate of 7 percent in the 1970-77 period started growing at 12 percent in 1978 and 1979. Therefore, in addition to resorting to more expensive thermal power generation to supplement the hydro power capacity of the country, in order to increase the supply of electricity, demand management strategies also had to be adopted mainly through pricing policy to curb the rapid growth. Similar effort had to be made in relation to petroleum consumption which grew particularly along with the import of vehicles as the new registrations at the Motor Traffic Department rose by about 27 percent per year. The telecommunications and postal services sectors also experienced rapid pressure on demand emanating from the accelerated growth in

**Table 3 FOREIGN TRADE AND BALANCE OF PAYMENTS IN 1970, 1977, 1978 & 1983 (Rs. Million)**

	1970	1977	1978	1983
1. Trade Balance	- 316	+ 360	- 2,383	-20,304
1 (a) Exports	2016	6640	13,207	24,917
1 (b) Imports	2332	6280	15,600	45,221
2. Services Balance	- 103	+ 304	+ 119	- 1,287
2 (a) Receipts	237	923	1,942	7,959
2 (b) Payments	340	619	1,823	9,256
3. Transfers (Net)	+ 69	+ 612	+ 1,242	+10,416
3 (a) Private	6	122	342	6,400
3 (b) Official	75	490	900	4,016
4. Current Account Balance	- 350	+1266	- 1032	-11,186
5. External Resource Gap	-1124	- 860	- 4048	-32,760
6. Terms of Trade (1978 = 100) INDEX	106	102	100	44

Source : Central Bank of Ceylon

the economy. Hence, measures for expansion of supply and rationalization of demand had to be employed in regard to these sectors.

#### Foreign Trade and Balance of Payments

Much of the activities in the services sector are in one way or other related to the export and import transactions and therefore it is more meaningful and useful to separately review the performance of foreign trade activities and their implications to the country's balance of payments position. It should be recalled in this context that one of the major objectives of the 1977 policy reforms was to encourage export-led growth in contrast to an import substitution strategy. Excessive protection through qualitative restrictions and high tariffs were considered not conducive to the growth of competitive trade and industry. Mean-

while it was also recognized that the transition from an inward looking controlled economy to an outward looking open economy could not be sustained without a rapid and sizeable increase in export earnings to finance imports. Therefore, continuous financing of imports through foreign aid and borrowings was not considered a feasible or desirable strategy. Nevertheless, in view of the poor performance of the export sector there was no other choice but to resort to foreign assistance for the maintenance of a liberal import policy.

The pent-up demand for imports due to the earlier system of controls as well as the fresh demand stemming from the growth dynamism resulted in a massive increase in imports since 1978. The average annual rate of expansion of imports during the 1978-83 period has been as high as 24 percent and the level of imports rose from SDR 819

million in 1978 to SDR 1796 million in 1983. In contrast to this, the increase in exports over the same period showed an annual average growth rate of only 9 percent, as export earnings increased from SDR 678 million in 1978 to SDR 988 million by 1983. Meanwhile the terms of trade declined drastically over this period. The outcome of these trends in imports and exports was the widening of the deficit in the merchandise trade account. (See Table 3). In the balance of payments the sub component known as the trade balance rose from SDR 144 million to SDR 808 million, reflecting a nearly six fold increase in the deficit in the merchandise account over the 1978-83 period.

The adverse impact on the balance of payments position resulting from the deterioration of the trade balance was mitigated to some extent, by the favourable trends in respect of the receipts in the services account made possible mainly by the inward remittances of funds by Sri Lankans working abroad, and earnings from tourism. For example the private transfers showed a 15 fold increase and amounted to SDR 255 million in 1978 compared with only SDR 17 million in 1978. Similarly, earnings from tourism which stood at SDR 44 million in 1978 rose to a peak level of SDR 133 million in 1982 before it declined to SDR 102 million consequent to the drop in tourist arrivals due to the July disturbances in 1983. However, the overall external resource gap in the balance of payments rose significantly from SDR 228 million in 1978 to SDR 1,312 million by 1983 necessitating that amount of finances from foreign sources.

#### Monetary and Fiscal Developments

The acceleration in economic activities in response to the policies introduced in 1977 stimulated both investment and consumption expenditure. Their consequences were

reflected in both monetary and fiscal policies. On the one hand, domestic credit creation and money supply grew at a rapid rate. On the other hand, the budget deficits and expansionary fiscal action expanded year after year. (See Table 4). These factors together contributed to inflationary pressures in the economy thereby necessitating a major task of stabilization.

The rapid growth in credit creation was particularly evident in 1979 and 1980 and total domestic credit increased by 43 percent and 70 percent, respectively. The rate of expansion in the Quasi Money\* supply during these years was as high as 49 percent and 41 percent. Hence the level of the country's money supply increased almost two fold between 1978 and 1980, rising from Rs.10,892 million to Rs.19,860 million. Since then more restrictive policies have been adopted to decelerate the rates of growth of credit creation and money supply. Yet, the Broad Money\*

supply level had risen to Rs.37,257 million by end of 1983 continuing to exert pressure on prices though at a somewhat reduced rate.

The expansions of money supply and credit creation, were to a great extent manifestations of budgetary management problems that emerged mainly as a result of a heavy public investment programme. For example, total public investment as a proportion of the GDP of the country more than doubled from an average of 7.7 percent in 1970-77 to 16.7 percent during the 1978-83 period. The share of the public sector in the overall investment level of the country amounted to more than 60 percent in the 1978-83 period compared with about 50 percent in the 1970-77 period. This reveals that despite the introduction of an open economic policy which was expected to be more dependent on private sector participation and the free market mechanism, the relative importance of the government,

Table 4

#### MONETARY AND FISCAL PERFORMANCE 1970, 1972, 1978 AND 1983

		(Rs. million)			
		1970	1977	1978	1983
1.	Government Revenue	2,736	6,686	11,688	25,210
2.	Government Expenditure	3,886	9,670	18,853	46,772
	2 (a) Recurrent	2,873	6,148	10,408	23,958
	2 (b) Capital	812	3,182	6,614	21,694
3.	Budget Deficit	1,150	3,074	7,165	21,562
4.	Narrow Money Supply	1,866	5,366	5,936	14,748
5.	Broad Money Supply	3,115	8,717	4,956	37,257
6.	Consumers' Price Index (1952 = 100)	138.2	203.2	227.8	474.2
7.	Wholesale Price Index (1974 = 100)		135.3	156.7	354.1

Source: Central Bank of Ceylon

especially in the field of investment, had not diminished during the post-liberalization era. Although, the government embarked on a massive investment programme mainly consisting of lead projects such as Accelerated Mahaweli Development Scheme, the Housing and Urban Renewal Programme and the Greater Colombo Economic Commission as well as other development projects, it has not been able to generate adequate budgetary savings to finance such programmes. The provision of financial incentives to the private sector and the low export performance affected the tax revenue of the government. Meanwhile, despite the scaling down of certain subsidies public expenditure kept rising rapidly due to the massive investment outlays and cost escalations. Therefore, while foreign assistance was sought for financing investment projects the remaining budget deficits had to be bridged by resorting to an expansionary fiscal policy. The resulting implications on money supply through the issue of Treasury Bills and borrowing from the banking sector were reflected in inflationary trends.

The upshot of all these trends described above, coupled with the adverse effects of the balance of payments which necessitated the depreciation of the exchange rate, was an upsurge in the domestic price level. The Colombo Consumers' Price Index (1952=100) which is popularly known as the Cost of Living Index which stood at 203.2 in 1977 rose dramatically to 318.2 in 1980 and 474 in 1983. In other words the rate of inflation in a given year has varied between 11 percent and 26 percent during the 1978-83 on an year to year basis. Similarly the movements in the Wholesale Price Index (1974=100) indicated a two fold increase from 156.7 in 1978 to 354.1 by 1983. During the entire six year period 1978-83 the consumer price index appears to have risen by about 15 percent while the wholesale price index has grown at an average of 17

percent per year reflecting both excess demand pressures and cost-push effects.

### Emerging Trends in 1984

The performance of the economy in the first half of 1984 seems to suggest that the scenario of economic development in Sri Lanka might take a somewhat favourable turn this year. This hope tends to

appear from certain key trends that have emerged which, if sustained and strengthened, should enable Sri Lanka to ease some of the difficulties described in the preceding sections of this review. These trends are mainly related to balance of payments and budgetary management. The final impact of these favourable developments should be felt in terms of an improved economic growth rate and reduced rate of inflation while

**Table 5 EXPORT EARNINGS**

Item	1983	Rs. Million (SDR Million in brackets)		
	June	January to June	June	January to June
1. Agricultural Exports	1,233.4	6,428.3	1,056.8	10,045.2
1.1 Tea	(50.1) 700.8 (28.4)	(261.7) 3,592.5 (146.3)	(40.4) 714.3 (27.3)	(381.1) 6,953.1 (263.8)
1.2 Rubber	230.5 (9.4)	1,280.3 (52.1)	180.7 (6.9)	1,830.3 (69.4)
1.3 Coconut	184.5 (7.5)	760.9 (31.0)	74.5 (2.9)	563.4 (21.4)
1.3.1 Kernel Products	143.5 (5.8)	517.1 (21.1)	42.0 (1.6)	288.0 (10.9)
1.3.2. Others	41.0 (1.7)	243.8 (9.9)	32.5 (1.2)	275.4 (10.5)
1.4 Minor Agricultural Products	117.6 (4.8)	794.6 (32.4)	87.3 (3.3)	698.4 (26.6)
2. Industrial Exports	730.5 (29.7)	4,055.0 (165.0)	995.7 (38.1)	6,098.4 (231.4)
2.1 Textiles and Garments	385.6 (15.7)	2,142.7 (87.2)	644.6 (24.6)	3,304.3 (125.4)
2.2 Petroleum Products	246.3 (10.0)	1,226.3 (49.9)	210.8 (8.1)	1,861.7 (70.8)
2.3 Others	98.6 (4.0)	686.0 (27.9)	140.3 (5.4)	932.4 (35.4)
3. Mineral Exports	77.5 (3.2)	481.6 (19.6)	48.2 (1.8)	482.0 (18.3)
3.1 Gems	55.2 (2.2)	388.4 (15.8)	31.4 (1.2)	383.7 (14.6)
3.2 Others	22.3 (0.9)	93.2 (3.8)	16.8 (0.6)	98.3 (3.7)
4. *Others	109.8 (4.5)	283.3 (11.5)	78.6 (3.0)	448.4 (17.0)
Total Exports	2,151.2 (87.3)	11,248.2 (457.9)	2,179.3 (83.3)	17,074.0 (647.8)

Source : Customs, Sri Lanka,  
State Gem Corporation,  
Ceylon Petroleum Corporation

\* Includes re-exports

possibly contributing to a modest expansion in employment. At the same time however, there are key production sectors that are the cause for concern due to their unanticipated decline in performance so far this year. These trends should be arrested and remedial measures must be taken to prevent further deterioration in the years to come.

The latest Annual Report (1984) of the World Bank for instance, is optimistic about Sri Lanka's prospects for a better economic performance. This Report notes that "most economies in the South Asian Region which are heavily dependant on the performance of their large agricultural sectors benefitted from the gathering recovery in the major industrial countries". In regard to Sri Lanka, the Report comments that "by early 1984, there were signs of improvements because tea prices remained very strong with resulting improvements in public revenues and the foreign exchange position." Among the other factors that the World Bank Report points to as being in Sri Lanka's favour, are the effective energy conservation measures that have been adopted and the initiation of policies to improve the tree crop sector's performance. This Report also anticipates that "a major boost to the economy should come in 1984 when the country's five year power crisis will be relived by the commissioning of the first major dam under the Accelerated Mahaweli Programme."

In light of the such emerging trends in the Sri Lankan economy in 1984, it can be safely assumed that the economic growth rate in the current year would surpass what was achieved in the past year. In 1983 the economy suffered a set back due to both external and internal factors and the growth rate decelerated. For example, as against an average growth rate of 6 percent during the 1978-83 period, the GDP in 1983 rose by only 5 percent. The main reasons for the lower performance were the adverse effects of the July disturbances on industry, commerce, trade and related activities as well as the reductions in the levels of production and export earnings of tree crops which suffered due to the world recession and local drought conditions in the

past two years. Two other major sectors of the economy, namely, manufacturing and construction also performed comparatively poorly in 1983. There are reasons to believe that most of these sectors have revived in 1984 and that the overall growth performance should improve. The economy should also benefit from the better international economic climate in general during 1984.

#### Export Prospects

The most favourable feature of the economy in 1984 so far, has been the tea price boom which contributed to a better than anticipated increase in export earnings. Compared with the first half of 1983, during the January to June period this year, export earnings have shown an improvement of 41 percent in terms of SDR, which rose from SDR 458 million to SDR 648 million. While the most important source of this increase was earnings from tea exports, the contributions of rubber and industrial exports were also noteworthy. (See Table 5). Compared with a Rs. 3,593 million - equivalent of SDR 146 million - earnings from tea in the first half of 1983 in the corresponding period this year tea exports have generated Rs. 6,953 million or SDR 264 million, recording a dramatic increase of 81 percent, in SDR terms. Earnings from rubber have registered a growth rate of 31 percent over the same period increasing from SDR 52 million to SDR 69 million. Meanwhile, industrial exports (led by textiles, garments and petroleum products) also showed an increase of 40 percent, rising from SDR 165 million in the first half of 1983 to SDR 231 million in the same period this year. Some other important export items, however, including coconut, gems and minor agricultural products experienced declines in their earnings in the first half of this year in comparison with the corresponding period last year.

The hope for a better performance in export earnings in 1984 can however be based on the continuing tea price boom. Production levels

in the tea industry efficiently responded to the price incentives and the forecasts for the remaining part of this year as well as for next year in regard to tea should be favourable. The current high prices fetched by tea in the international markets have been attributed to the imbalance between the supply and demand consequent to the drop in production in 1983, followed by the decline in stock position since then. The ban on tea exports imposed by India due to the need to meet local consumption requirements in view of her shortfall in production on the one hand, and also the upsurge in demand for tea in the consuming countries, mainly in the context of high coffee prices, appeared to have contributed to the imbalance in conditions in the tea market. The FOB price of tea appreciated from Rs.44.82 (SDR 1.82) per kilogram in the first half of 1983 to Rs.77.23 (SDR 2.93) in the same period this year. These prices reflected an increase of 72 percent in rupee terms and an improvement of 61 percent in SDR terms. It is note worthy that Sri Lanka could take advantage of the deficit supply situation and respond to attractive world market prices by expanding production and exports.

The volume of tea exports by Sri Lanka in the first half of 1984 amounted to 90 million kilograms compared with 80 million kilograms during the corresponding period in 1983. Over the same two periods, the production level of tea reflected an increase of 37 percent, from 85 million kilograms to 117 million kilograms. It appears that a good part of this production increase came from the small holders of tea who were able to derive a higher producer margin than the state plantation sector. It is obvious that though the tea price boom would contribute to higher gross earnings the margin that accrues to producers would depend on their cost of production. The cost of production of the public sector plantations rose appreciably since the wage revisions were effected in the middle of this

year while the tea small holders would not have been subject to the same cost increases. However, the continuation of the attractive price level, coupled with favourable weather conditions so far this year have been a boon to tea growers, and the chances are that 1984 as well as 1985 should turn out to be quite successful years for Sri Lankan tea exporters.

#### Import Capacity

Despite the low growth rate of exports during the past several years, the country's capacity to import has not been seriously affected due to the availability of foreign aid. However, a modest deceleration of the demand for imports was witnessed in the first half of 1984. This might be an early indication of the gradual saturation of the import demand which accelerated ever since the economy was liberalized in 1977. In view of the preference of the government not to admit any new major investment projects and also in view of the projected completion of major on going capital intensive projects, it is possible to envisage a further deceleration in the demand for imports furthermore, the increased flexibility in the exchange rate adjustment should result in the rate approaching a realistic level thereby discouraging the non-essential and less productive imports. The projected low growth in imports therefore, should arrest any further deterioration in the balance of trade in 1984, particularly in view of the already improved export performance. See Table 6.

Import payments in the first half of 1984 had reached Rs. 22,988 million or SDR 872 million, reflecting an increase of 6 percent in SDR terms. Taking into consideration the slight reduction in the overall import bill in 1983, compared with the previous years import expenditure, in 1984 too it could also either decline marginally or not increase significantly. Another important feature that has emerged during the 1980's is the change in the composition of imports. This trend has been reinforced in the first half of 1984 with imports consisting main-

Table 6

CLASSIFICATION OF IMPORTS				
Category	Rs. Million (SDR Million in brackets)		Percentage of Total	
	January to June		January to June	
	1983	1984	1983	1984
1. Consumer Goods	5,936.2 (241.7)	4,876.3 (185.0)	29.5	21.2
1.1 Food and Drink		2,741.8	2,150.0	13.6
1.1.1 Rice	(111.6) 452.5 (18.4)	(81.6) 197.9 (7.5)	2.2	0.9
1.1.2 Flour	33.1 (1.4)	10.3 (0.4)	0.2	.....
1.1.3 Sugar	1,042.9 (42.5)	508.2 (19.3)	5.2	2.2
1.1.4 Milk and Milk Products	479.6	326.2 (19.5)	2.4 (12.4)	1.4
1.1.5.1 Fish - dried	87.1 (3.6)	174.9 (6.6)	0.4	0.8
1.1.5.2 Fish - other	57.0 (2.3)	148.3 (5.6)	0.3	0.6
1.1.6 Food - other	589.6 (24.0)	786.3 (29.8)	2.9	3.4
1.2 Textiles and clothing	1,206.0 (49.1)	1,329.9 (50.5)	6.0	5.8
1.3 Other Consumer Goods	1,988.4 (81.0)	1,395.4 (52.9)	9.9	6.1
1.3.1. Motor cars and cycles	307.4 (12.5)	106.4 (4.0)	1.5	0.5
1.3.2. Radio Receivers and Television	440.5 (17.9)	241.4 (9.2)	2.2	1.1
1.3.3. Rubber Tyres and Tubes	80.5 (3.3)	109.3 (4.2)	0.4	0.5
1.3.4. Medical and Pharmaceutical Products	247.1 (10.1)	234.2 (8.9)	1.2	1.0
1.3.5. Other	912.9 (37.2)	704.1 (26.7)	4.5	3.1
2. Intermediate Goods	8,902.1 (382.4)	11,284.0 (428.1)	44.2	49.1
2.1 Fertilizer	240.7 (9.8)	423.6 (16.1)	1.2	1.8
2.2 Petroleum	3,787.5 (154.2)	5,407.5 (205.2)	18.8	23.5
2.3 Chemical Elements & Compounds	431.8 (17.8)	525.0 (19.9)	2.1	2.3
2.4 Dyeing, Tanning, and Colouring Materials	122.7 (5.0)	136.3 (5.2)	0.6	0.6
2.5 Paper and Paper Boards	421.9 (17.2)	314.8 (11.9)	2.1	1.4
2.6 Wheat and Meslin	951.4 (38.7)	1,282.7 (48.7)	4.7	5.6
2.7 Other	2,946.1 (119.9)	3,194.1 (121.2)	14.6	13.9
3. Investment Goods	4,974.9 (202.5)	5,387.1 (204.4)	24.7	23.4
3.1 Building Materials	472.1 (19.2)	388.8 (14.7)	2.3	1.7
3.2 Transport Equipments	1,227.6 (50.0)	1,023.5 (38.8)	6.1	4.4
3.3 Machinery and Equipments	2,429.6 (98.9)	2,793.1 (108.0)	12.1	12.1
3.4 Other	845.5 (34.4)	1,183.6 (44.9)	4.2	5.1
4. Unclassified Imports	303.9 (12.4)	1,442.0 (54.7)	1.5	6.3
Total Imports	20,117.1 (819.0)	22,988.3 (872.1)	100.0	100.0

source : Customs, Sri Lanka; Food Commissioner's Department; Ceylon Fertilizer Corporation and other major importers; Ceylon Petroleum Corporation; and Central Bank of Ceylon

ly of intermediate and investment goods. For example, compared with 30 percent in the 1983 January to June period, the proportion of consumer goods in the total imports have further dropped to 21 percent in the corresponding period this year. Accordingly, the share of intermediate goods consisting of items such as fertilizer and petroleum have risen from 44 percent to 49 percent over the same period while the ratio of investment goods including machinery and equipment have remained relatively stable. The capacity expansion effects of such imports, that have already been used in capital formation in the country, should enable a greater output in the production sectors of the economy in the years to come.

#### **Growth Potential of Different Sectors**

On the basis of the performance in the first half of 1984, it appears that the paddy sector which was responsible for much of the improvements in the agricultural sector in the 1978-83 period has fared poorly this year. As against an increase of 15 percent in 1983 over the previous year's production level, the first half of this year registered a significant decline in paddy production, in relation to the first half of last year. The main reason for this has been the adverse weather conditions that prevailed in the early part of 1984 even causing floods in some major rice growing areas. Similar problems appear to have caused poor harvests in the case of subsidiary food crops in the first half of this year which might eventually contribute to a decline in the growth rate of the overall agricultural sector.

The industrial sector which grew at a marginal rate of only one percent in 1983 over the level of production of the previous year seems to have revived in the first half of 1984. This trend was also evident in the growth of industrial exports while the public sector industries reflected an increase in the output level. For example, the output index of some public sector industries (1977 = 100) which remained almost static at 102 last year, is estimated to have risen to

121 in the first half of this year. This improvement was mainly a result of the recommissioning of the refinery of the Petroleum Corporation which had been closed down for repairs during the early months of last year. The other public sector industrial ventures which recorded improvements in production in the first half of this year have been the State Distilleries Corporation and National Textiles Corporation whose output grew by 21 percent and 10 percent respectively, compared with the same period last year. In regard to private sector industries the main contributions to production increases are expected from the industrial establishments in the Katunayake Investment Promotion Zone. With the rehabilitation of the industrial ventures affected by the July disturbances there might be a further impetus to growth in the private sector industries in the second half of 1984. As a result of the improved energy situation, with the strengthening of the national grid by adding the Mahaweli hydro power (i.e. with the Victoria power project providing an additional 210 MW), there should be a further impetus for the expansion of the industrial and commercial sectors. The increased availability of hydro-power should also enable some saving in the petroleum consumption due to the possible reduction in use of thermal power. Similarly, the completion of on-going infrastructure facilities such as telecommunications, and expansion of commercial space and transportation service etc, should widen the investment opportunities in industry and commerce thereby inducing a higher rate of growth in the other sectors of the economy in 1984.

In the context of these trends that have emerged in the first half of 1984 and also taking into consideration the trends in the growth in money supply, credit creation and developments in government finance so far this year, it is possible to predict a reduction in the rate of inflation in 1984. One indicator already is the Colombo Consumers' Price Index, which in the first six months of

this year had a growth rate of about 8 percent compared with an increase of more than 10 percent during the same period last year. In terms of the wholesale price index, the growth rate in prices have been only 3 percent in the January to June 1984 period as against a more than six times higher growth rate of 19 percent during the same period last year. Assuming these trends would continue in the second half of the year, it should be possible to experience a lower rate of inflation in 1984 compared with the rates of 14 percent and 25 percent that were revealed by the Consumers' Price Index and the Wholesale Price Index, respectively, in 1983.

In the first half of this year, the broad money supply increased by 7 percent consequent to the improvements in external assets in view of the higher tea prices. Domestic credit creation, however, declined by 2.4 percent during the January to June, 1984 period reflecting the tight monetary policy adopted to curb inflationary pressures. Meanwhile, it is anticipated that the budgetary outlook in 1984 would be satisfactory due to both improved revenue performance as well as better expenditure management. The tea boom and higher rubber prices have also contributed towards an increase in the export duty revenue of the government in the first half of this year. The modest growth in government expenditure coupled with a sizable increase in revenue should enable a surplus in the current account thereby contributing to arrest a further expansion in the overall budget deficit in 1984. This should in turn, mean a reduction in expansionary sources of financing thereby helping to curtail the inflationary impact of budgetary policy, in the current year.

If the trends that emerged by mid 1984 should continue it is possible to predict that a combination of greater price stability, more stable conditions for economic growth and more employment opportunities should be realized towards the end of 1984. The international economic environment, indicating a moderate economic recovery in the western industrial countries, also seems to favour such an outcome for Sri Lanka in 1984.