

EFFECT OF ASIAN CURRENCY CRISIS ON THE RUBBER INDUSTRY OF SRI LANKA

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Sri Lanka is the 7th largest natural rubber producing country in the world. In 1997 out of the 106,000 MT of Natural Rubber produced, nearly half (45%) have been consumed locally for making value added products like Solid tyres, Pneumatic tyres and tubes, latex based dipped products and footwear *etc.*

In general, the economy of Sri Lanka has not been adversely affected by the currency crisis that occurred in the South East Asia (SEA) starting on the 2nd July 1997; compared to other SEA countries due to following factors :

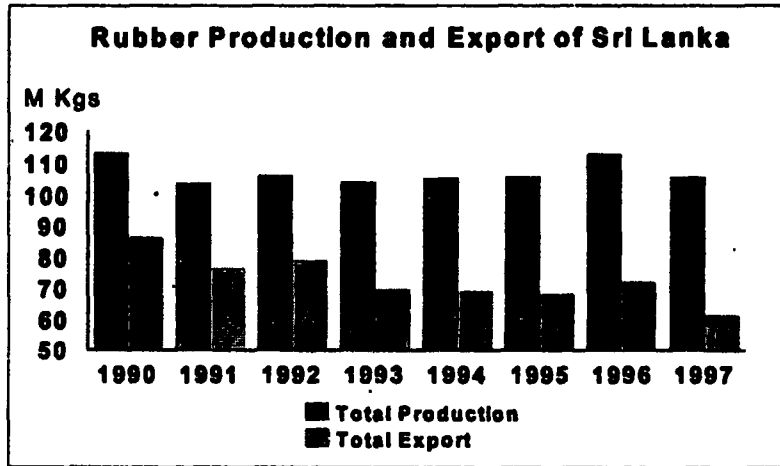
- a. Majority of foreign investments in Sri Lanka were not confined to SEA countries only like Korea, Taiwan, Malaysia and Indonesia.
- b. Sri Lankan rupee was allowed to devalue gradually over time as a floating currency.

Among the SEA countries, Malaysia had been the largest recipient of Foreign Direct Investment (FDI) during the past decade followed by Indonesia, Thailand, South Korea and Philippines. In comparison to US \$ Mn 32348 and 18198 received by Malaysia and Indonesia respectively the investment in Sri Lanka in terms of FDI is not significant at all. Total FDI attracted by Sri Lanka between 1985 and 1996 amounts to just over US\$ Mn. 800 only. A further amount of US\$ Mn 85 has been invested in Sri Lanka during the 1st half of 1998. Hence, the distribution of FDI between these Asian countries clearly explains the reason as to why Sri Lanka did not experience a noticeable impact of the Asian financial crisis.

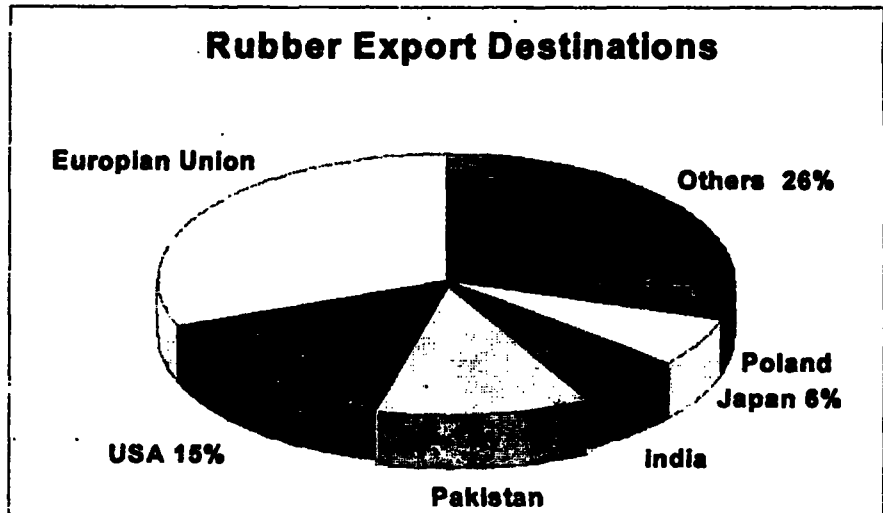
Other issue that needs to be investigated is that the nature of International borrowing and capital account convertibility adopted in Sri Lanka. Owing to the borrowing restrictions enforced by the Sri Lankan monitoring authorities, opportunities given to the private sector for borrowing money from the lending organizations in International financial market is limited. Further, the capital convertibility becomes important only if Sri Lanka has substantial foreign investments. One of the reasons for less foreign investments in Sri Lanka during the past decades is the war that is going on from 1983 and if not for that definitely there would have been very much more foreign investments in the country by now and the

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situation in the country as a result of SEA financial crisis would have been much worse.

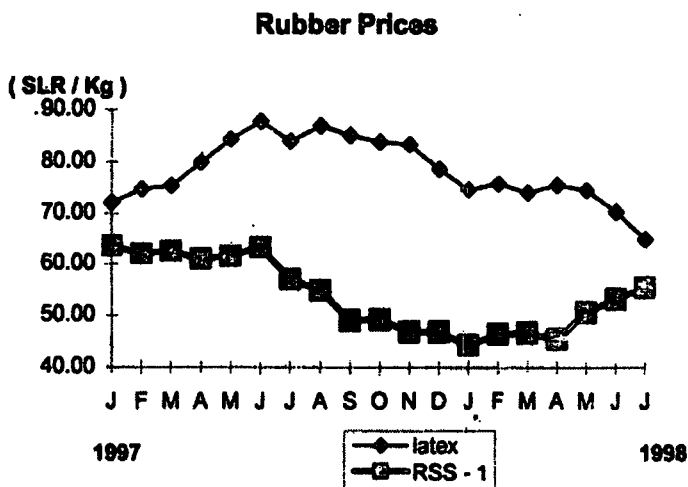


Out of the 19.7 billion US\$ invested in Malaysia investments from Japan alone is 8.2. bn US\$. In Indonesia out of 48.3 bn US\$ total investment, 22.0 bn US\$ is from Japan. In Thailand, out of 61.7 bn US\$ investment, 37.9 bn US\$ is from Japan. But in Sri Lanka, out of the total investment though South Korean component is about 20%, the balance 80% is evenly distributed among all countries in the world.



However, due to the possible drop in both export revenue and FDI, the possibility of Sri Lankan economy getting affected in the future remains fairly strong.

As a result of the currency devaluation in major rubber producing countries in the world viz. Thailand, Indonesia and Malaysia, the effective farm-gate price paid to their rubber farmers rose rapidly and hence they produced more rubber since July 97 than the anticipated target figures for 1997. Releasing of buffer stocks kept in Thailand during this period to ease their economic problems worsened the situation for rubber and as a result the rubber production recorded a surplus of over 10% by the end of 1997. Hence, the global rubber price dropped rapidly until May 1998, recording a figure of Rs. 45.00 per Kg. for average grades of RSS from the figures above Rs. 65.00 recorded before July 1997. Similarly in the case of other industries like the garment industry and commodity export industries, the revenue fell far below the expected targets. Due to the financial hardships faced by South Korea, Malaysia, and Hongkong, a fall in foreign investment in Sri Lanka too, is expected.



Eventhough the total rubber production in the country dropped from 112 000 MT to 106 000 MT in 1997, the amount of latex crepe produced out of the total production remained even slightly above the production in 1996. This was mainly due to the attractive premium price paid for this top quality commodity in the world market which has already reached Nitch status. In order to maintain this position for this commodity in the world market, RRI owned "Dartonfield Estate" gained ISO 9002 in the middle of 1998 while few other crepe factories in the country are already very close to gain this important standards registration. However, Sri Lankan authorities have taken all necessary precautions to prevent an over supply situation of latex crepe rubber in the International Market. The environment safe water soluble

bleaching agent introduced to the crepe industry by RRI Sri Lanka is now exported to both India and Indonesia by Chemanex Ltd.

In order to help the small holders who were badly effected by the 25-40% price decline in sheet rubber and the farmgate price paid to them for their latex by the centrifuged latex manufacturers, a cess of Rs.5.41 levied on raw rubber exports was abolished by the Government of Sri Lanka from May 1998. This along with the gradually declining rupee value against the US Dollar helped the small holder to withstand the sharply declining rubber prices at least to some extent. Central Bank of Sri Lanka is maintaining a 10% depreciation of the rupee in 1998 compared to the 7.4% depreciation maintained through out 1977.

Rubber products industry

The local rubber products manufacturers had to compete with manufacturers in South East Asia, when the domestic rubber prices in such countries fall sharply due to the currency crisis. For instance, during the period between Jan - Aug. 1998, the price of sheet rubber and centrifuged latex of SEA origin was nearly Rs.25 per kg. below Sri Lankan prices. This is a reduction of over 40 - 50% of the price of the main raw material used in the local rubber products industry. It was at this juncture that the local rubber products manufacturers, particularly the gloves manufacturers were interested in importing both concentrated latex and dry rubber from SEA countries at low prices. However, the Government of Sri Lanka intervened and prevented importing substantial quantities of natural rubber, which could have otherwise adversely affected the local rubber plantation industry in the long-run. The total quantity of latex imported up to August 1998 has been less than 500 MT; which is less than 2.5% of the annual latex consumption in the country for dipped products manufacture. Dry natural rubber has not been imported at all during that period. Hence, the importation of latex had no negative impact on the domestic dry rubber latex price, as some of the people claim.

As a result of the recognition of the rubber products industry as a "*Thrust Industry*" in 1997, there was a considerable interest among products manufacturers to expand their product industries and hence even despite the currency problem, rubber consumption in the country has increased by 2.2%. However, due to the low price of rubber products introduced to the market by SEA countries, manufacture of Industrial Solid tyres, Pneumatic tyres and tubes and the footwear industries stepped down their production out put by 0.8% 27.6% and 23.5% respectively during 1997. In terms of quantity, the decline in consumption of rubber in the three sectors have been 104 MT, 1684 MT and 1610 MT respectively. Even with these figures, the decline in rubber consumption in the Pneumatic tyres and tubes industry by 1684 MT was merely due to the close down of the Kelani Tyre factory as a result of an industrial dispute.

In the remaining rubber product sectors, there had been a sharp increase in rubber consumption particularly in the Tyre retreading, flooring, dipped products and latex foam industries where the rubber consumption has increased by 17.5%, 28.5% and 36.0% respectively. There is also a remarkable 23.7% increase shown in the other rubber products industries such as the tubing and hoses industry and rubberized coir mattress industries, there by increasing the net natural rubber consumption by 2.2% over the previous year. Based on this positive response shown by the present rubber products industries after gaining thrust industry status, the government of Sri Lanka is now considering strongly to extend more incentives for the rubber products industry to promote further expansion of the existing factories and to set up new rubber based industries. This will be one of the best ways for Sri Lanka to nullify the possible indirect effects of the SEA currency crisis on the economy of the country.

NR CONSUMPTION BY DIFFERENT SECTORS

A summary sheet 1996 Vs 1997

Product type	No. of companies		NR consumption (MT)				
	1996	1997	1996	1997	Change over previous year		
					Quantity	%	
1. Tyre retreading	26	28	4600	5404	804	17.5	
2. Industrial solid tyres	3	3	12900	12796	(104)	(0.8)	
3. Pneumatic tyres & tubes	5	5	6100	4416	(1684)	(27.6)	
4. Footwear	10	13	6860	5250	(1610)	(23.5)	
5. Flooring	5	7	2700	3465	765	28.3	
6. Other rubber products	6	14	3,990	4,934	944	23.7	
7. Latex dipped products	16	25	19230	20100	870	4.5	
8. Latex foam	3	4	3970	5400	1430	36.0	
9. Total	74	99	60350	61685	1335	2.2	

Figures in parenthesis indicate negative values