

(H) BALANCE OF PAYMENTS AND EXTERNAL ASSETS**General**

Detailed statistics of Sri Lanka's balance of payments and external assets are available in Tables 44 to 48 in appendix II. Balance of payments data are largely derived from exchange control records of actual receipts and payments during the year, and are supplemented by information from other sources such as the Ministry of Planning and Economic Affairs and the Ceylon Petroleum Corporation, etc. These figures may differ from the statistics used in the foreign trade section which are based on Customs returns.

On provisional estimates the balance on current international transactions of Sri Lanka showed a deficit of Rs. 161 million in 1973 as compared to a deficit of Rs. 196 million in 1972. This deficit runs parallel with the declining terms of trade trend observed since 1965. But for the accelerated price increases for imports in 1972 and 1973, due largely to inflationary conditions and supply constraints abroad and to the uncertainty in the international monetary scene, the deficit for the year would have been considerably lower. Nevertheless, the 1973 outturn is a further improvement of the external accounts position since 1969. This continuing improvement has been managed by recourse to strict import policies governing both quantities and payments. It does not indicate any slackening of domestic demand. Merchandise trade, the major component of the current account of the balance of payments, was in deficit to the tune of Rs. 299 million as compared to Rs. 255 million in 1972. However, in view of a sharply increased surplus on account of invisibles transactions, which on a net basis brought in Rs. 138 million as compared with Rs. 59 million in 1972, the current account deficit was reduced to Rs. 161 million.

TABLE II (H) 1
Sri Lanka's Balance of Payments

Rs. Million

Year	Trade Balance	Net Invisibles including Transfer Payments	Balance on Current Account	Net Long-term Capital	Basic Balance
1957	- 95	- 100	- 195	- 18	- 213
1958	- 89	- 64	- 153	+ 8	- 145
1959	- 183	- 25	- 208	+ 32	- 176
1960	- 210	- 11	- 221	+ 22	- 199
1961	- 86	- 7	- 93	+ 11	- 82
1962	- 143	+ 3	- 140	+ 39	- 101
1963	- 161	- 7	- 168	+ 80	- 88
1964	- 193	+ 33	- 160	+ 8	- 152
1965	- 13	+ 72	+ 59	+ 58	+ 117
1966	- 344	+ 54	- 290	+ 137	- 153
1967	- 335	+ 46	- 289	+ 161	- 128
1968	- 380	+ 25	- 355	+ 224	- 131
1969	- 746	- 51	- 797	+ 275	- 522
1970	- 315	- 35	- 350	+ 184	- 166
1971	- 287	+ 71	- 216	+ 404	+ 188
1972	- 255	+ 59	- 196	+ 292	+ 96
1973(a)	- 299	+ 138	- 161	+ 195	+ 34

(a) Provisional

Source: Central Bank of Ceylon.

The implications of a current account deficit in the balance of payments on the economy must be assessed in terms of how the deficit was covered. In the absence of sufficient foreign exchange reserves, long-term capital inflow is the most desirable way in which this deficit can be covered. Such inflows in 1973 were more than sufficient to offset this shortfall resulting in a surplus in the overall balance of Rs. 36 million. Despite this favourable balance, Sri Lanka's dependence on short-term finance failed to register a decline. On the contrary, indebtedness on account of short-term and suppliers' credits (net of amortization) increased by Rs. 282 million. This source of finance, however, enabled Sri Lanka to achieve a modest increase in external assets (Rs. 125 million) in addition to a reduction in external banking liabilities (Rs. 112 million).

Trends in Detail

(a) Merchandise Account

The merchandise account of Sri Lanka's balance of payments recorded a deficit of Rs. 299 million in 1973. Although this may seem a further deterioration from the 1972 outturn, the annual figure conceals a marked upswing in export earnings which began in the middle of the year and continued strongly for the rest of the year. The level of imports continued to be governed principally by the need to ensure certain critical minimum levels of consumption in respect of essential foodstuffs and to prevent widespread production and employment cut-backs in manufacturing industry by making a reasonable amount of raw materials and other intermediate goods available to state and private industry. Over four-fifths of the deficit (Rs. 270 million) resulted in the first half of the year, and in contrast, the third and fourth quarters showed near balance between exports and imports.

The outstanding feature of the merchandise account in 1973 was the departure from the stagnant trend of export earnings observed in recent years. Over the average for the last five years, export earnings increased by 17 per cent, to reach Rs. 2,346 million in 1973. In the light of the sluggish export performance in the several preceding years, this upturn represents a distinct break with the past. Rubber and tea from among the traditional primary export commodities and practically all minor exports subscribed to this change.

From among major exports only rubber and coconut products shared in the world boom in commodity prices in 1973; tea, Sri Lanka's main export, however, was one of the few commodities that did not benefit by the commodity boom. Nevertheless tea earnings did contribute to an increase in overall export income, rising from Rs. 983 million (on an exchange recorded basis) in 1972 to an estimated Rs. 1,069 million¹ in 1973. This was entirely due to an increase in the quantity exported. Rubber prices which were particularly depressed in 1972 when the

1. This figure may be somewhat lower than Customs data. The 1972 tea crop was affected by drought and the volume exported suffered in consequence. The effects of the drought wore off and the crop started picking up again during the course of 1973. Because of the time lag between physical exports of tea and eventual receipt of money (Exchange Control requirement is for receipts within 6 months) the entire value of the increased tea shipments may not be reflected in the Balance of Payments which is computed on an exchange recorded basis, whereas Customs data will indicate values as ascertained at the time of shipment.

Balance of

	Rupee		
	1 9 7 2		
	Credit	Debit	Net
1. Merchandise Account			
Exports (f.o.b.) ..	1,898		
Imports (c.i.f.) (own resources) ..		1,599	
(Aid Imports & Suppliers' Credits) ..		554	
Total Imports ..		2,153	
Trade balance (own resources) ..			(+ 299)
Trade balance (all imports) ..			- 255
2. Services Account			
Non-monetary gold ..	—	—	—
Port, transportation and insurance ..	154	61	+ 93
Foreign Travel ..	28	12	+ 16
Investment income ..	10	125	- 115
(i) Profits & dividends ..	1	23	- 22
(ii) Other (interest) ..	9	102	- 93
Government Expenditure n.i.e. ..	33	20	+ 13
Miscellaneous Services ..	83	105	- 22
Private transfers ..	24	50	- 26
Total Services ..	332	373	- 41
3. Total Current Account (own resources)	(2,230)	(1,972)	(+ 258)
Total Current Account (all items)	2,230	2,526	- 296
4. Capital Payments	—	995	- 995
Loans ..	—	125	- 125
Suppliers' credits ..	—	84	- 84
Short-term credits ..	—	570	- 570
Oil Compensation & ADB ..	—	—	—
Private Capital ..	—	8	- 8
I. M. F. ..	—	170	- 170
Bank borrowings ..	—	—	—
Other ..	—	38	- 38
Total Current & Capital Payments (own resources)			(- 737)
Total Current & Capital Payments (all items)			- 1,291
5. Financing			
I.M.F. Drawings ..	163	—	+ 163
Bank borrowings ..	12	—	+ 12
Bilateral balances ..	—	11	- 11
Suppliers' credits ..	52	—	+ 52
Short-term Credits ..	593	—	+ 593
External Assets ..	—	229	- 229
Commodity Aid ..	304	—	+ 304
Project & Other Aid ..	98	—	+ 98
Other Aid ..	13	—	+ 13
Grants ..	100	—	+ 100
Private Capital ..	10	—	+ 10
Other ..	107	—	+ 107
Special Drawing Rights ..	62	—	+ 62
Errors & Omissions ..	17	—	+ 17
Total financing ..	1,531	240	+ 1,291

(a) Provisional.
Figures have been rounded off.

TABLE II (H) 2

Payments 1971-1972

Million			U. S. Dollars Million					
1973 (a)			1972			1973 (a)		
Credit	Debit	Net	Credit	Debit	Net	Credit	Debit	Net
2,346			308			368		
	1,986			259			312	
	658			90			103	
	2,644			349			415	
		(+ 360)			(+ 49)			(+ 56)
		- 298			- 41			- 47
177	62	+ 115	25	10	+ 15	28	10	+ 18
59	10	+ 49	5	2	+ 3	9	2	+ 7
17	127	- 110	2	21	- 19	3	20	- 17
1	19	- 18	—	4	- 4	—	3	- 3
16	108	- 92	2	17	- 15	3	17	- 14
33	20	+ 13	5	3	+ 2	5	3	+ 2
103	115	- 12	13	17	- 4	16	18	- 2
48	46	+ 2	4	8	- 4	8	7	+ 1
437	380	+ 57	54	61	- 7	69	60	+ 9
(2,783)	(2,366)	(+ 417)	(362)	(320)	(+ 42)	(437)	(372)	(+ 65)
2,783	3,024	- 241	362	410	- 48	437	475	- 38
—	1,277	- 1,277	—	161	- 161	—	201	- 201
—	141	- 141	—	20	- 20	—	22	- 22
—	95	- 95	—	14	- 14	—	15	- 15
—	644	- 644	—	92	- 92	—	101	- 101
—	5	- 5	—	—	—	—	—	—
—	169	- 169	—	1	- 1	—	1	- 1
—	112	- 112	—	28	- 28	—	27	- 27
—	111	- 111	—	—	—	—	18	- 18
—	111	- 111	—	6	- 6	—	17	- 17
		(- 860)			(- 119)			(- 136)
		- 1,518			- 209			- 239
137	—	+ 137	26	—	+ 26	21	—	+ 21
—	—	—	2	—	+ 2	—	—	—
1	—	+ 1	—	2	- 2	—	—	—
240	—	+ 240	8	—	+ 8	38	—	+ 38
781	—	+ 781	96	—	+ 96	123	—	+ 123
—	125	- 125	—	37	- 37	—	20	- 20
210	—	+ 210	49	—	+ 49	33	—	+ 33
125	—	+ 125	16	—	+ 16	20	—	+ 20
—	—	—	2	—	+ 2	—	—	—
83	—	+ 83	16	—	+ 16	13	—	+ 13
6	—	+ 6	2	—	+ 2	1	—	+ 1
48	—	+ 48	18	—	+ 18	8	—	+ 8
—	—	—	10	—	+ 10	—	—	—
12	—	+ 12	3	—	+ 3	2	—	+ 2
1,643	125	+ 1,518	248	39	+ 209	259	20	+ 239

Source: Central Bank of Ceylon.

TABLE II (H) 3
External Resources and their Use

Item	Rupees Million				Percentage Share			
	1970	1971	1972	(a) 1973	1970	1971	1972	(a) 1973
A. Resources								
1. Merchandise exports f.o.b. ..	2,017	1,930	1,898	2,346	58	51	51	53
2. Services Account ..	234	333	332	437	7	9	9	10
3. Capital Inflow ..	382	628	525	424	11	16	14	10
of which:—								
(a) Loans ¹ ..	299	346	402	335	9	9	11	8
(b) Other Aid ² ..	—	152	13	—	—	4	—	—
(c) Grants ¹ ..	75	105	100	83	2	3	3	2
(d) Private Capital ..	8	25	10	6	—	—	—	—
4. Short-term Liabilities ..	829	903	989	1,207	24	24	26	27
(a) Gross drawings from the International Monetary Fund ..	57	83	163	137	2	2	4	3
(b) Special Drawing Rights ..	78	63	62	—	2	2	2	—
(c) Increase in balances in Bilateral Payments Agreements ..	—	—	—	1	—	—	—	—
(d) Bank borrowings ..	123	—	12	—	4	—	—	—
(e) Short-term Credits ..	434	658	593	781	13	17	16	18
(f) Suppliers' Credits ..	85	58	52	240	2	2	1	5
(g) Other ..	52	41	107	48	1	1	3	1
5. Decline in External Assets (net of Sterling Loans Sinking Fund) ..	—	—	—	—	—	—	—	—
Total ..	3,462	3,794	3,744	4,414	100	100	100	100
B. Use								
6. Merchandise imports c.i.f. ..	2,332	2,217	2,153	2,644	67	58	58	60
of which Aid ..	459	509	554	658	13	13	15	15
7. Services Account ..	364	367	373	380	11	10	10	9
of which								
(a) Investment Income ..	152	134	125	127	4	3	3	3
(b) Private transfers ..	23	40	50	46	1	1	1	1
8. Capital Amortization ..	126	132	133	146	3	3	4	3
(a) Official ..	113	96	125	141	3	2	3	3
(b) Private ..	13	36	8	5	—	1	1	—
9. Short-term Liabilities ..	605	976	873	1,131	18	26	22	25
(a) Repurchases from the IMF ..	161	145	170	169	5	4	5	4
(b) Decrease in balances in Bilateral Payments Agreements ..	75	57	11	—	2	2	2	2
(c) Bank borrowings ..	—	81	—	112	—	2	—	3
(d) Short-term Credits ..	282	614	570	644	8	16	15	15
(e) Suppliers' Credits ..	80	65	84	95	3	2	2	2
(f) Other ..	7	14	38	111	—	—	—	3
10. Increase in External Assets (net of Sterling Loans Sinking Fund) ..	39	89	224	121	1	2	6	3
11. Balancing item ..	— 4	13	— 12	— 8	—	—	—	—
Total ..	3,462	3,794	3,744	4,414	100	100	100	100

Source: Central Bank of Ceylon

(a) Provisional.

1. Includes assistance received in the form of Project and Commodity Aid.

2. Currency Loan from the Peoples' Republic of China.

Figures have been rounded off.

average f. o. b. price sank to 93 cents a pound, made a very rapid recovery in 1973. The upturn in fact appeared in the closing months of 1972 and throughout 1973 prices rose strongly to close at Rs. 2.69 per pound f. o. b. in December. Overall earnings from rubber are estimated at Rs. 519 million, compared with Rs. 299 million in the previous year. While better prices account for the larger part of the increased earnings, some part is also due to a higher volume of shipments. Coconut prices, too, rose steadily during 1973, in keeping with the upward trend for most primary product prices; but earnings from coconut products fell in 1973 on account of certain restrictions on exports. Coconut oil exports suffered considerably owing to an export ban operative from 9th April, to 1st December, 1973. In the case of copra, there was a complete export ban from 15th February onwards running through to the end of the year. This export ban was the result of a sharp decline in domestic output of coconut following the previous years' droughts so that a need arose to ensure adequate supplies for local consumption. As a result, the bulk of exports in 1973 took the form of desiccated coconut.

Of the minor exports, precious and semi-precious stones, coconut products other than oil, desiccated coconut and copra, other agricultural products, industrial goods and bunkers showed marked increases in earnings when compared with earlier years. Exports of precious and semi-precious stones, in particular, showed a phenomenal increase rising from Rs. 8 million in 1972 to Rs. 130 million in 1973¹. The increase in earnings from gems as well as other minor exports was due to an increase in volume as well as in price. The increment in volume of exports could be attributed mainly to the very attractive incentives extended to this sector. For instance, all minor exports were entitled to the benefit of a 65 per cent domestic price enhancement by way of FEECs. In addition, gem exports were eligible for an income tax amnesty and a convertible rupee account facility of 25 per cent of their earnings. All other minor exports were allowed the convertible rupee account facility upto 2 per cent². Industrial exports enjoyed a further facility of a rebate on duties paid on raw material imports. It should be noted, however, that the increase in earnings from minor agricultural exports was largely due to sharply rising prices during the general commodity boom.

A factor which needs mention as a possible influence on Rupee export values is the frequent changes in exchange parities. Normally, when an exchange rate is depreciated, the local proceeds tend to increase without the foreign currency value of export proceeds going up. During 1973, frequent parity changes of the Sri Lanka Rupee caused it to depreciate against foreign currencies by about five per cent. However, as an explanation for the higher Rupee earnings, this has been of marginal relevance in 1973 as the bulk of the increase in export earnings is reflected in foreign currency terms: in US dollars, exports have increased from 308 million in 1972 to 368 million in 1973. In effect, this confirms the importance of the international price factor as the main influence on export earnings in 1973.

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1. The foreign exchange receipts, as distinct from the value of export contracts entered into during the year, are lower as the execution of all contracts has not been completed by the end of the year.
 2. Increased to 3 per cent with the Budget of 1973.

The value of Sri Lanka's imports increased by 23 per cent from Rs. 2,153 million in 1972 to Rs. 2,644 million in 1973. This is a sharp reversal of the declining trend of import values observed since the peak of 1969 following the liberalisation of imports in 1968. The increase did not imply a change in the policy of limiting imports to what the country could afford. Rather, it was the inevitable outcome of sharply increased prices which had to be paid for Sri Lanka's essential imports. While the price increases were spread over all items, the increases in respect of essential food items like sugar, flour, rice, milk foods and subsidiary foodstuffs were exceptionally large. Prices on the one hand were considerably higher than hitherto owing to a tight world supply position, which continued throughout the year, and on the other, due to a higher freight bill occasioned by several surcharges imposed by shipping lines in the wake of currency realignments.

Over the year, the Import price index (1967=100) increased from 158 to 209 and within this, the food index rose from 173 to 233. As a result, there was in fact a reduction in the volume of imports, which is borne out by the import volume index (1967=100) declining from 88 in 1972 to 79 in 1973. With critical minimum levels of consumption imports being a first charge on available resources, and with price escalation greater in the case of bulk food items, food imports in 1973 increased their share from 44 per cent to 52 per cent. Imports of intermediate and capital goods therefore suffered reductions in their respective shares, declining from 26.9 per cent and 27.2 per cent to 24.2 per cent and 20.7 per cent, respectively.

(b) Services and Transfers

The services account of Sri Lanka's balance of payments has traditionally been in deficit. The years 1965 to 1968 provide an exception but this is explained very largely by the restrictions imposed on certain classes of payments e.g. the moratorium on profits and dividends. The re-emergence of the deficit from 1969 onwards not only conforms to the previous trend but in addition was reinforced by the backlog of payments withheld in the preceding few years. In this background, the surplus of Rs. 57 million resulting from transactions on the services account in 1973 without the need for additional restrictive measures on payments is an encouraging sign. Statistically, the total outpayments on services has remained at much the same level as could have been envisaged from the historical trends. But the receipts show a marked increase over the previous levels and it is here that the primary source of the surplus lies. Specifically, the receipts on other transportation account (mainly port services, excluding the supply of bunkers to ships and aircrafts) and travel, evidence notable increases totalling Rs. 54 million. Besides, smaller gains all-round have added another Rs. 51 million.

TABLE II (H) 4
Changes in Major Sectors in the Services Account
1972 and 1973

	Rupees Million							
	Credit			Debit			Balance	
	1972	(a) 1973	Change	1972	(a) 1973	Change	1972	(a) 1973
Port, Transportation and Insurance ..	154	177	+ 23	61	62	+ 1	+ 93	+ 115
Foreign travel ..	28	59	+ 31	12	10	- 2	+ 16	+ 49
Investment Income ..	10	17	+ 7	125	127	+ 2	- 115	- 110
(i) Profits and Dividends ..	1	1	—	23	19	- 4	- 22	- 18
(ii) Interest ..	9	16	+ 7	102	108	+ 6	- 93	- 92
Government Expenditure ..	33	33	—	20	20	—	+ 13	+ 13
Miscellaneous Services ..	83	103	+ 20	105	115	+ 10	- 22	- 12
Private Transfers ..	24	48	+ 24	50	46	- 4	- 26	+ 2
Total ..	332	437	+ 105	373	380	+ 7	- 41	+ 57

Source: Central Bank of Ceylon

(a) Provisional

The growth of tourist traffic, which was interrupted by the state of civil unrest in 1971, continued its upward trend at a sharply increased rate in 1973, the earnings of that year being well over double that of 1972. This increase is the outcome of both an increase in the number of tourists visiting the country as well as an increase in earnings per tourist. The number of tourists visiting Sri Lanka increased from 56,047 in 1972 to 77,888 in 1973, an increase of 39 per cent. This development went hand in hand with the expansion of the infrastructural facilities set up to cater to and attract a high volume of tourist traffic. Judged by the occupancy ratios and the rapid achievement of break-even points in the operation of tourist hotels, there seems to be scope for the provision of higher capacity to accommodate growing demand. However, an element of uncertainty has been introduced into international tourism by the impact of the energy crisis on air-line traffic.

Receipts from port expenditure (ship chandling, harbour dues, repair facilities) which have been consistently high in recent years have shown a further increase in 1973, registering a net surplus of Rs. 114 million as compared to a surplus of Rs. 100 million in 1972.

The transfer payments account of the balance of payments, which consist in the main of private migrant transfers into and out of the island and receipts of grants-in-aid, have consistently assisted the balance of payments since the end of the 1950s, when exchange control curtailed private transfers abroad. The more important item, grants-in-aid, which invariably offsets the outflow on private account has not shown a trend behaviour influenced as it is by the aid policies and balance of payments position of the donor countries rather than by the local need for balance of payments support. In 1973, grants-in-aid amounted to Rs. 83 million, as against Rs. 100 million and Rs. 105 million in the two

previous years. Private transfers on the other hand, particularly those inward, have shown evidence of an increase. This again was largely the outcome of official policy which sought to increase and channel through the official sector remittances from nationals employed abroad through further incentives in addition to the FEEC rate, namely the special accounts scheme. This scheme, which came into existence in February, 1971 in pursuance to a proposal made by the Minister of Finance in his Budget Speech, was intended to mobilise small savings from nationals employed abroad by granting concessionary treatment with respect to voluntary remittances made by them. There was also a requirement under the Passport (Regulation) and Exit Permit Act under which nationals securing employment abroad were required to remit up to 10 per cent of their earnings. The higher level of private inflows was associated with equally high outflows, owing to the faster rate of repatriation of non-citizens under the Indo-Ceylon Agreement.

The transfer payments account together with the services account comprise the invisibles component of the balance of payments. The balance on invisibles account can either aggravate or minimise the unfavourable outturn on merchandise transactions, depending on whether the invisibles account is in deficit or in surplus. During the period 1964-1968, the invisibles account exercised a moderating influence on the adverse trade balance to produce a lower overall deficit on current account. In 1969 and 1970, its role was reversed and larger deficits than were indicated by merchandise transactions occurred, largely owing to increased outflows on account of investment income, due partly to relaxation of the moratorium and partly to increased service payments on the rising external debt. Since 1971, however, the invisibles account assumed its former role of modifying the adverse effects of the trade balance. The year 1973 marks a further improvement in this favourable trend when it showed a sharply increased surplus. This surplus amounted to Rs. 138 million as compared with surpluses of Rs. 71 million and Rs. 59 million respectively in 1971 and 1972. In view of the improved performance on invisibles account, the adverse effects of the increased merchandise deficit were mitigated and the current account deficit reduced to Rs. 161 million.

(c) Capital Account

In 1973, Sri Lanka had to finance a resource gap of Rs. 1,518 million. While this was a continuation of the pattern observed since 1969, when resource gaps of over Rs. 1,000 million emerged, the 1973 figure is the highest ever recorded. The major contributory factors were the higher outlays on imports and the rising debt service payments, particularly on short and medium-term debt, and, to a lesser extent, repayment of bank borrowings and building up of external assets

TABLE II.(H) 5
Modes of Financing the External Resource Gap 1972-1973

	1972		1973 (a)	
	Rs. Mn.	% Share	Rs. Mn.	% Share
Resource Gap	-1,291		-1,518	
Financing	+1,291	100.0	+1,518	100.0
1. External Assets	- 229	-17.7	- 125	-8.2
2. Foreign Bank Borrowings	12	1.0	—	—
3. I.M.F. Drawings	163	12.6	137	9.0
4. Bilateral Trade Balances	- 11	- 0.9	1	0.1
5. Short-term Trade Credits	593	45.9	781	51.4
6. Supplier's Credits	52	4.0	240	15.8
7. Commodity Aid	304	23.6	210	13.8
8. Project Aid	98	7.6	125	8.2
9. Other Loans and Lines of Credit	13	1.0	—	—
10. Grants	100	7.7	83	5.5
11. Private Capital	10	0.8	6	0.4
12. Other	107	8.3	48	3.2
13. Special Drawing Rights	62	4.8	—	—
14. Errors and Omissions	17	1.3	12	0.8

Source: Central Bank of Ceylon

(a) Provisional

In the current context of the external accounts situation facing Sri Lanka, long-term capital is the most appropriate form of finance to bridge the resource gap. Private long-term capital has not been a significant source of finance in recent years. The inflow of long-term official capital which fell from the peak figure of Rs. 494 million in 1971 to Rs. 415 million in 1972, suffered a further setback in 1973, declining to Rs. 335 million. When allowance is made for repayments on past borrowings amounting to Rs. 141 million, the net inflow declined to Rs. 194 million. The reduction is wholly reflected in commodity aid, which fell by as much as Rs. 94 million over the level obtained in 1972. One important reason for this drop had been certain delays in the signing of aid agreements in 1973. Although the Aid Group meeting was held in March, 1973 the bulk of the agreements was signed only towards the end of the year. This meant that actual disbursements started quite late. It is also partly explained by the cut-back in aid commitments in the previous year (1972)¹ which resulted in the spillover for 1973 being reduced.

The short-fall in the flow of grants and long-term capital meant that the burden of financing the major share of the resource gap fell on short-term and medium term sources as in the previous years, but on a larger scale. Altogether resources to the tune of Rs. 1,021 million were obtained from short-term sources (short-term credits and suppliers' credits), while a further sum of Rs. 137 million came from the I. M. F. During the year repayment of short-term credits (short-term credits and suppliers' credits) amounted to Rs. 739 million, which meant that on a net basis short-term credits increased by as much as Rs. 282 million in 1973, as compared with a

¹ In 1972, aid commitments by the Consortium members decreased by Rs. 148 million over the previous year to Rs. 296 million.

decrease of Rs. 9 million in 1972. Although this by itself appears to be rather disquieting, it needs to be looked at from a background where external assets have risen by Rs. 125 million and external banking liabilities reduced by Rs. 142 million.

In 1973, resources available from the I.M.F. were confined to a drawing of Rs. 137 million under the Scheme for Compensatory Financing of Export Fluctuations. Unlike in the previous year, facilities were not available under stand-by agreements or the allocation of Special Drawing Rights. A sum of Rs. 12 million was credited to the I.M.F. as charges payable in rupees. On the other hand, repurchases on past drawings amounted to Rs. 169 million. In the event, net indebtedness to the I.M.F. decreased by Rs. 20 million, as compared with an increase of Rs. 12 million in 1972.

The foregoing analysis of the capital account transactions in 1973 highlights the underlying weakness of Sri Lanka's external accounts position as it has evolved since 1968, when the major part of the external resource gap came to be financed from short-term and medium-term sources. As service payments on past borrowings are a first charge on current foreign exchange earnings, the ability to sustain a critical level of imports depends on the negotiation of fresh deferred payments facilities.

In assessing the prospects for 1974, long-term assistance of the scale and at the time required is unlikely to reach Sri Lanka both due to problems within donor economies and normal procedural delays. Therefore recourse to short-term assistance may be unavoidable. While past reports have referred to the undesirability of increasing recourse to short-term credit, Part I of the present Report draws pointed attention to the disadvantages and dangers inherent in such situations.

2. External Assets

TABLE II (H) 6
External Assets of Sri Lanka*

	Rs. Million				
	Dec. 1971	Dec. 1972	Dec. 1973	Change 1971/1972	Change 1972/1973
Government ..	12.4	53.7	3.3	+ 41.3	- 50.4
Government Agencies and Institutions ..	62.3	67.3	70.7	+ 5.0	+ 3.4
Central Bank ..	238.2	285.4	480.5	+ 47.2	+195.1
Commercial Banks ..	185.2	320.3	296.7	+135.1	- 23.6
Total ..	498.1	726.7	851.2	+228.6	+124.5

* Adjusted for China account balances

Source: Central Bank of Ceylon

The gross external assets of Sri Lanka increased by Rs. 124.5 million in 1973 as shown in the foregoing table. This is a continuation of the trend observed in 1972, when the assets increased by as much as Rs. 228.6 million. Gross external assets at the end of 1973 stood at Rs. 851.2 million, and this was

the highest recorded since 1960. This increase is almost entirely due to an increase in the assets of the Central Bank by Rs. 195.1 million, whereas those of the government and the commercial banks have decreased by Rs. 50.4 million and Rs. 23.6 million, respectively. The decrease in the assets of the government was mainly the result of a decrease in the balance due to Sri Lanka under payments agreement account with the People's Republic of China.

The rise in external assets is explained only in small part by the improvement in the balance of payments. As the increase occurred at a time when the terms of trade continued to be on a downward path, it was achieved through a sacrifice in the import volume, on the one hand, and a further accumulation of short-term obligations, on the other. Short-term liabilities of the government¹ registered an increase of Rs. 253 million in 1973, but the liabilities of the Central Bank and commercial banks declined by Rs. 72 million and Rs. 70 million, respectively. On a net basis, therefore, Sri Lanka's short-term obligations increased by Rs. 111 million in 1973.

The Convertible Rupee Account Scheme

The Convertible Rupee Account Scheme was an additional incentive to step up exports of a 'non-traditional' nature, particularly of gems, and to induce such earnings to flow through official channels. Under this scheme exporters of 'non-traditional' or minor export products and some services are permitted to credit a percentage of their earnings to a convertible rupee account,² which they can utilise for the payment for imports against licences issued by the Controller of Imports and Exports and to effect certain other invisibles payments, such as for foreign travel, with the prior approval of the Controller of Exchange. Gem exports were the first to qualify for this facility, with effect from 11th July, 1972 and 25 per cent of such earnings was allowed to be credited to the convertible rupee account. From the beginning of 1973, this facility was extended to cover exports by individuals of paintings, sculpture and other original and individual works of art, literary and scientific writings and material for publication abroad, and earnings from professional and consultancy services. In the case of other minor exports the share qualifying for convertible account facility was 2 per cent of gross earnings from the beginning of the year to 2nd November, and 3 per cent thereafter.

The number of Convertible Rupee Accounts opened with the authorised dealers up to the end of December, 1973 was 709 and the total credits amounted to Rs. 54.2 million, while the debits were Rs. 22.6 million. Of the various categories, gem exports have been the strongest contender for the convertible account facility accounting for Rs. 46.5 million or 85.8 per cent of total credits. Other non-traditional exports and tourism accounted for Rs. 6.8 million and Rs. 0.9 million respectively. The spectacular increase in earnings from gem exports in 1973 (Rs. 130 million) as compared with the magnitudes in any previous period indicate that the convertible account facility has provided a strong boost not only for increasing the export volume but also for routing such exports through official channels.

1. Defined to include short-term credits, Suppliers' credits and Crown Agents, debit balance.
2. Credits include the value of FEECs earned.

The overwhelmingly large share of debits to Convertible Rupee Accounts consists of payments for imports. Of the total debits amounting to Rs. 22.6 million, Rs. 19.1 million is in respect of imports, while foreign travel and local expenses absorbed Rs. 3.0 million and Rs. 0.5 million, respectively. On the basis of import licences issued by the Controller of Imports and Exports for the period 1.3. 1973 to 31.12.1973, it is observed that the bulk of the import payments has been for industrial raw materials and trade quota items; payments for the former amounted to Rs. 5.7 million and for the latter Rs. 8.7 million. Convertible rupees utilised for the importation of motor vehicles amounted to Rs. 3.5 million or 17 per cent of the import licences issued. Thus, it is evident that the major part of convertible rupees arising from this scheme has been utilised for developmental purposes rather than for consumption.

(b) External Debt¹

Service payments on the external debt of Sri Lanka amounted to Rs. 512.6 million in 1973 compared with Rs. 480.2 million in the previous year. (see table II (H) 7). The debt service in 1973 consisted of Rs. 404.2 million in amortization and Rs. 108.4 million in interest remittances. Comparable figures for 1972 were Rs. 378.3 million and Rs. 101.9 million, respectively.

TABLE II (H) 7
Service payments on the External debt 1969-1973

	(Rs. million)				
	1969	1970	1971	1972	1973
1. Debt Service payment ..	282.3	453.4	410.2	480.6	512.6
(a) Amortization ..	213.9	353.7	306.1	378.3	404.2
(b) Interest ..	68.4	99.7	104.5	101.9	108.4
2. Earnings on export of goods & services ..	2,162.8	2,253.3	2,244.2	2,205.9	2,733.3
3. Debt Service ratio (1 as % of 2) ..	13.1	20.1	18.3	21.8	18.8

Source: Central Bank of Ceylon.

Out of the 1973 amortization, Rs. 263.7 million or 65.2 per cent comprised repayments of debts with a maturity of 1-5 years. In 1972 such repayments totalled Rs. 253.8 million or 67.1 per cent of that year's amortization.

The total debt service ratio (amortization and interest payments expressed as a percentage of earnings on export of goods and services) was 18.8 per cent in 1973 compared with 21.8 per cent in 1972. The decline in the ratio in the year under review was mainly the result of an increase in the country's export earnings.

1. Data in this section may differ from those provided in the section on Public Finance due to the inclusion of external indebtedness of non-government financial institutions such as the Central Bank in this note.