PART I

WEIGHTS AND MEASURES

Conversion Factors

British to Metric Units

1 acre	=	0.405 hectares (ha)
1 pound (lb)	=	0.454 kilogrammes (kgs)
1 long ton (2240 lbs)	=	1.016 metric tons (mt. ton)
1 hundred weight (cwt)	=	50.802 kgs.
1 mile	=	1.609 kilometres (kms)
1 long ton mile	=	1.635 mt. ton kms
1 lb/acre	=	1.121 kgs./ha
1 cwt/acre	=	125.536 kgs./ha
1 pint	=	0.57 litres
1 imperial gallon	=	4.55 litres

Metric to British Units

1 hectare	=	2.471 acres
1 kilogramme	=	2.205 lbs
1 mt. ton (1000 kgs.)	=	0.984 long ton
1 metre	=	3.281 feet
1 kilometre	=	0.621 mile
1 mt. ton kilometre	=	0.612 long ton mile
1 litre	=	1.76 pints=0.219 imp. gallons
1 kg/ha	=	0.892 lb/acre

Paddy/Rice Conversions

1 bushel of paddy (46 lbs)	=	20·87 kgs.
1 mt. ton paddy	=	47.92 bushels paddy
	=	0.7 mt. ton rice
1 mt. ton rice	=	68.46 bushels paddy
	=	1.43 mt. ton paddy
1 bushel paddy/acre	=	51.55 kgs. paddy/ha

ECONOMIC PERFORMANCE, PROBLEMS AND POLICIES IN 1982

INTRODUCTION

In 1982, Sri Lanka's Gross National Product (GNP) at constant factor cost prices is estimated to have increased by 4.9 per cent. This represents a marginal improvement on the rate of growth in real GNP of 4.1 per cent attained in 1981. The real Gross Domestic Product (GDP), on the other hand, is estimated to have increased by 5.1 per cent as against the rate of growth of 5.8 per cent recorded in 1981. This is mainly because of the net outflow abroad of factor incomes in 1982 was lower than in 1981.

TABLE 1 · 1

National Income Statistics 1979—1982

Item	Amount Rs. Million				Growth Rate (%)			
	1979	1980 *(a)*	1981*(a)*	1982*(a)*	1979	1980	1981	1982
1. G.D.P. at Current Factor Cost Prices	49,782	62,246	79,337	91,643	23.0	25·0	27·5	15·5
2. G.D.P at Constant (1970) Factor Cost Prices	18,501	19,575	20,706	21,756	6·3	5·8	5·8	5·1
3. G.N.P. at Current Factor Cost Prices	49,542	61,814	77,625	89,674	23·1	24·8	25·6	15·5
4. G.N.P. at Constant (1970) Factor Cost Prices	18,430	19,456	20,257	21,246	6·4	5·6	4·1	4·9
5. Mid-year population (Million)	14·5	14·7	15·0	15·2	2·0	1 8	1·7	1·7
6. G.N.P. per Capita (Rs)								
(I) At Current Prices	3,424	4,194	5,179	5,904	20·7	22·5	23·5	14·0
(II) At Constant prices *(b)*	1,274	1,320	1,352	1,399	4·3	3·6	2·4	3·5

(a) Provisional
(b) Revised

Source: Central Bank of Ceylon.

Gross National Product in 1982 is estimated at Rs. 89,674 million at current factor cost prices and at Rs. 21,246 million at constant prices. The implicit change in the GNP deflator in 1982 is estimated to be 10.2 per cent and shows a marked decline from the deflator for 1981 which indicated a 19 per cent increase in prices for that year. Sri Lanka's population, according to tentative estimates made by the Registrar General's Department, rose by 1.7 per cent. When allowance is made for the increase in population, the real per capita income increased by 3.5 per cent as against the increase of 2.4 per cent in 1981. The per capita GNP at current prices was Rs. 5,904 or US $ 284.

An analysis of the sectoral performance of the economy as given in Table 1.2 shows that the decline in the rate of growth of real GDP in 1982 is mainly due to the lower rate of growth in agriculture, particularly in tea and paddy which recorded negative growth rates. The agricultural sector, as a whole, including forestry and fishing, grew only by 2.6 per cent in the year as against 6.9 per cent growth achieved in the previous year. Value added in the manufacturing sector also declined due to the lower output of tea that was processed. However, factory and other industries including industrial exports have increased by 9.1 per cent in 1982 over the previous year. The construction sector recorded a negative growth rate for the second successive year. The only sector to have registered a higher growth rate in 1982 was the services sector consisting of wholesale and retail trade, transport and other services where activity was largely sustained by the higher level of imports in 1982.

In terms of output, tea production suffered a severe set-back with a 10.6 per cent drop in production. Production of tea during the year amounted to 187.8 million kilograms as compared with 210 million kilograms in 1981. The fall in production appears to have stemmed primarily from the decline in average yield rather than the lower extent in bearing during the year. The decline in yield was closely linked to unfavourable weather conditions that prevailed during the first quarter of the year. Despite a drop in extent under tapping, rubber production improved marginally by 1 million kilograms to 125 million kilograms owing to the increase in average yield over the previous year. The average yield of 726 kilograms per hectare in 1982 was, however, well below the peak yield of 845 kilograms achieved in 1978. The coconut sector, however, continued its impressive record of growth with an 11 per cent increase in production of nuts. Production in 1982 was 2,510 million nuts. The data on export earnings of minor export crops indicate that production in this sector has dropped with the exception of coffee which recorded a 43 per cent increase in export volume.

Paddy production at 2,156,000 metric tons represented a 3.3 per cent decline from the output of 1981. This was, however, a temporary set-back which resulted from the drought conditions that adversely affected Maha production. Production in Yala 1982, however, registered a substantial increase of 12 per cent. On the whole, the minor food crop sector performed better during the year with a dramatic increase in the soya bean crop. Sugar production which showed a marginal improvement in 1981 dropped by 4 per cent to 22,783 metric tons. Meanwhile, the production of eggs and milk is estimated to have decreased by 7 per cent and 1.6 per cent respectively, while fisheries recorded an increase in output of 2.9 per cent.

While the agricultural sector was unable to maintain the impressive growth record achieved in 1981, industrial production overall increased by 9.1 per cent in real terms in 1982. This increase in output is in fact the highest increase recorded since 1978 and was the combined outcome of the expanded output of the public sector industry helped largely by the uninterrupted power supply during 1982, and the improved output of the export oriented private sector industry. Output of the private sector industries increased by 18 per cent while that of the public sector industries increased by 5 per cent. In view of the fact that more than 60 per cent of industrial output is contributed by the public sector, its growth rate though lower than that of the private sector was a major influence on the high overall growth in output of the industrial sector.

TABLE I . 2

Composition and Growth of GNP 1978—1982
(At (1970) Factor Cost Prices)

SECTOR	(Amount Rs. Mn.)					(Growth Rates)			
	1978	1979	1980 (a)	1981 (a)	1982 (a)	1979	1980	1981	1982
1. Agriculture, Forestry and Fishing of which:—	4,532	4,622	4,766	5,097	5,231	2.0	3.1	6.9	2.6
1.1 Tea	398	412	381	419	374	- 3.4	- 7.5	10.0	- 10.7
1.2 Rubber	225	223	194	181	182	- 0.9	- 13.0	- 6.7	0.6
1.3 Coconut	488	519	462	515	573	6.4	- 11.0	11.5	11.3
1.4 Paddy	1,116	1,132	1,267	1,313	1,269	1.4	11.9	3.6	- 3.4
1.5 Other (include subsidiary food crops, forestry and fishing) ..	2305	2,336	2,462	2,669	2,833	1.3	5.4	8.4	6.1
2. Mining and Quarrying	619	652	684	713	742	5.3	4.9	4.2	4.1
3. Manufacturing	2,541	2,659	2,681	2,820	2,955	4.6	0.8	5.2	4.8
3.1 Tree Crop Processing	840	877	791	851	806	4.4	- 9.8	7.6	- 5.3
3.2 Other	1,701	1,782	1,890	1,969	2,149	4.8	6.1	4.2	9.1
4. Construction	794	960	1,066	1,034	1,013	20.1	11.0	- 3.0	- 2.0
5. Services	8,915	9,608	10,378	11,042	11,815	7.8	8.0	6.4	7.0
6. G.D.P.	17,401	18,501	19,575	20,706	21,756	6.3	5.8	5.8	5.1
7. Net Factor Income from Abroad ..	- 72	- 71	- 119	- 449	- 510	—	—	—	—
8. G.N.P.	17,329	18,430	19,456	20,257	21,246	6.4	5.6	4.1	4·9

(a) Provisional

Source: Central Bank of Ceylon.

Sector-wise, the significant increases in industrial production were recorded in textile and garments and leather products, wood and wood products, fabricated metal products, chemical and petroleum products and paper and paper products. The increase in public sector production was to a large extent due to the uninterrupted operation of the oil refinery of the Ceylon Petroleum Corporation and the higher capacity utilization by most of the other corporations.

Evidently, the decline in the rate of growth of real GDP for 1982 can be attributed to factors which are of a non-recurring nature. Adverse weather conditions have in large measure contributed to the decline in tea and paddy production, which given its heavy weightage in total domestic production, has depressed the overall growth rate, partly through the adverse impact on the agro-processing industrial sector as well. However, there are clear signs that the economy has to perform better in the basic sectors such as agriculture and industry, if other ancillary activities which contribute in no small measure to national income are to have sustained growth prospects. Particular mention must be made of the need to increase the proportion of the GDP which is exported and its crucial importance in maintaining the country's balance of payments viability. The ratio of exports to GDP has been on a declining trend during the past few years and was 23 per cent in 1982.

During the year under review, the international economic environment continued to be adverse to the interests of primary producing countries, like Sri Lanka. Gloomy world economic outlook continued without any abatement in 1982 and world trade entered into the third year of almost zero growth. The growth rates of major industrial countries were even lower than their rates of growth in 1981. GNP at constant prices of 7 leading industrial countries, i.e., Canada, France, Germany, Italy, Japan, U.K. and U.S.A. recorded only a mere 0.1 per cent increase in 1982. The individualist policies adopted by these countries paid no heed to the fact that the crisis was a global one. Due to tight monetary and demand management policies, they were able to bring down the inflation rates to single digit levels on an average but unemployment rates were pushed up to double digit levels in a number of countries such as U.S.A., U.K. and Canada. Consequently, protectionist measures were strengthened thus causing further problems to developing countries like Sri Lanka. This together with the weak demand for primary goods following a slow down in manufacturing helped to intensify competition among primary producers and depressed primary commodity prices.

The strong impact of recession and unemployment led to a relaxation of monetary control, particularly in U.S.A. during the second half of 1982. The decline in interest rates in U.S.A. also led to a similar decline in international money market rates. While countries like Sri Lanka which had recourse to commercial credits in recent years benefited somewhat both from the lower interest rates and the less restrictive monetary policies, increased protectionism, however, became manifest on the international scene.

These developments in the world economy exerted unfavourable effects both directly and indirectly on production, investment, exports and government revenue in Sri Lanka. Countries, including Sri Lanka, which are heavily dependent on international trade (Sri Lanka's exports and imports are 23 per cent of the GDP and 43 per cent of the GNE respectively), received a set-back by these adverse developments. A striking example of this is that while coconut production increased by an impressive 11 per cent, the consequential gain was almost fully wiped out by the drop in international prices. Export duty revenues were in fact 21 per cent lower than in 1981. The case of rubber provides an even more striking example. While the volume of exports increased by 17 per cent or by 19 million kilograms, export earnings declined by 20 per cent. The drop in export duty revenue was 47 per cent or nearly half the revenue of the previous year.

The effect of the international terms of trade continued for the fourth successive year to be adverse and declined to 38 in 1982 from 46 in 1981. Accordingly, Sri Lanka's loss from trade was 8 per cent of its GNP due to adverse terms of trade in 1982 compared with 7 per cent in 1981. Real national income after adjusting for the terms of trade is estimated to have increased by 3.6 per cent in 1982 as compared with the increase of 3.2 per cent in 1981.

One of the notable features of the economic performance in 1982 has been the significant abatement in the rate of inflation. After three successive years of high increases in the price level, the rate of increase in the general level of prices dipped to single digit figure. The average annual rate of increase in the Colombo Consumers Price Index (CCPI) was 10.8 per cent while the increase registered by the Wholesale Price Index (WPI) turned out to be even smaller at 5.5. per cent. The comparable increase in the previous year were 18 per cent and 17 per cent in CCPI and WPI respectively. This was brought about by many factors. The Government pursued a conscious and consistent policy aimed at controlling inflation by reducing the impact of budget deficits. The Central Bank continued its tight monetary policies thus leading to the success in demand management policies. Stability in prices of some of the imported goods due to lower inflation rates in the world contributed a fair share in support of the stabilisation policies pursued by Sri Lanka. The administered price adjustments associated with the withdrawal of consumer subsidies in the first few years of liberalization had been more or less completed and this was assisted by the stable exchange rate that existed throughout the year. In fact, the prices of wheat flour and sugar were reduced during the course of the year. Despite production shortfalls in the first half of the year, the availability of imports of rice at relatively stable prices helped prevent rice prices from rising significantly. Continuous surveillance of the impact of monetary and fiscal policies on the price level, however, cannot be relaxed on account of this moderation. Efforts to increase production, particularly food, will be called for if the hard won gains on the prices front are to be preserved in the future as well.

Largely as a result of the deceleration in the rate of increases in prices, real wages in both the organized as well as the unorganized sectors of the economy increased during the year. The introduction of a 'consolidated salary' with effect from 1st January 1982 and the continuation of the cost of living indexed allowances introduced in 1981 ensured that nominal wages of government employees increased at a higher rate in 1982 compared to the previous year. Their real wages, on the other hand, increased significantly by 19 per cent in 1982 as against a decline of 3 per cent in 1981. Although nominal and real wages increased in the organized private sector, where wages are governed by Wages Boards, the rate of increases in the government sector was higher than the rate of increases in the private sector. In the unorganized sector, the all island daily wage rates of male and female workers also increased in respect of all categories, the increases being most pronounced in the case of workers in coconut and paddy cultivation and for masons and carpenters. Real wages in these sectors too increased given the magnitude of the increase in money wages.

Available data on the employment front also indicate that the performance in 1982 was satisfactory. The total number of new employment opportunities created during the year in the organized sector, i.e. government departments, semi-government institutions and private sector enterprises contributing to the Employees' Provident Fund, however, showed a slight decline over 1981 and amounted to 34,000. The corresponding numbers in 1980 and 1981 were 18,035 and 40,622 respectively. The major share of this increase took place in the organzied private sector which increased its employment capacity by 25,625. The relative stagnation in public sector and the semi-government sector reflected the restraints exercised with regard to budgetary allocations and limitations on credit expansion in respect of semi-government sector.

While statistics on employment in the unorganized private sector are not available, official statistics of employment do not portray fully the extent of new employment generation that has taken place in recent years. However, there is reason to believe that employment in this sector has also increased in the last few years. This is due to several reasons. Firstly, the Sri Lankan economy by its very nature and state of development has a large unorganized sector. Secondly, quite apart from employment in the primary sector, the new economic opportunities generated by rising incomes which are the outcome of the increased rates of economic growth in the recent past, have resulted in diverse types of employment opportunities. Examples of such opportunities are the private transport sector and trade sector, especially retailing, where the full extent of such employment does not get reflected in the official statistics. Business concerns in these sectors do not, by and large, contribute to the Employees' Provident Fund, employing as they do casual labour and having a high turnover of employees.

Available evidence from the Central Bank's sample surveys on Consumer Finance of Households in 1978/79 and 1981/82 indicates that the rate of unemployment fell from 24.0 per cent of the labour force in 1973 to 14.8 per cent in 1978/79, and further to 13.1 per cent on the basis of very provisional estimates of the data in the 1981/82 survey. The results of this survey also seem to indicate that the unemployment problem has eased somewhat in the case of those with secondary and higher education.

While the deceleration in rate of increases in prices and the increase in both employment and wages in all sectors were noteworthy features, the economy continued to experience large increases in investment well beyond its capacity to generate savings locally. These higher levels of investment have generally been incompatible with the limited availability of real and financial resources. Consequently, foreign savings have had a large role to play in sustaining the high level of investment in 1982 as well. Domestic savings are estimated at Rs. 12.1 billion or 12.1 per cent of GDP in 1982 as against Rs. 9.9 billion in 1981. Investment, on the other hand, is estimated at Rs. 30.5 billion or 30 per cent of GDP. While there has been a marginal increase in the domestic savings ratio, it is still disappointingly low in relation to the investment level which continues to be around 30 per cent of GDP at current market prices. National savings have, however, been sustained by the rapid growth in net private transfers from abroad resulting from the larger flow of foreign remittances of Sri Lankans employed abroad. The ratio of National Savings to GDP has been increasing somewhat steadily and was 15.3 per cent of GDP in 1982.

Obviously the large gap between national savings and investment continues, as in the past, to be financed, as shown in Table 1.3 below, by foreign savings. However, the proportion of the net concessional aid during recent years has been going down and the country has had to resort to more expensive commercial credit as well as run down its reserves to finance the balance. The continuation of this process would depend critically on the continued inflow of foreign aid since the utilization of commercial credit as well as reserves for the purpose has obvious limits. The prospects for concessional aid under the present grim world economic prospects are not very encouraging at present and a sustained effort to increase the domestic savings ratio has to be made if investment is to be sustained at the current level, without undue pressures both on the price level and the balance of payments.

TABLE 1.3

Investments — Savings 1978—1982
(As percentages of GDP at Market Prices)

Category	1978	1979	1980	1981	1982*
Gross Fixed Capital Formation ..	20.0	25.3	31.3	27.4	30.1
Public[1]	7.2	7.3	7.1	4.9	5.0
Private (including Public Corporations) ..	12.8	18.0	24.2	22.5	25.1
Changes in Stocks	0.1	0.5	2.4	0.4	0.2
Total Investments = Total Savings(local & foreign)	20.1	25.8	33.7	27.8	30.3
Gross National Savings	15.5	14.8	14.0	14.3	15.3
Public	-1.4	0.2	-3.8	-1.7	-1.7
Private	16.9	14.6	17.8	16.0	17.0
Foreign Savings[2]	4.5	11.1	19.8	13.5	15.1
Net Concessional Aid[3]	9.2	8.5	8.4	9.2	8.3
Use of Reserves	-4.4	-1.5	4.5	0.5	1.1
Net Commercial Borrowings ..	-1.0	2.1	4.9	3.5	4.9
Others (Net)[4]	0.7	2.0	2.0	0.3	0.8

* Provisional. Source : Central Bank of Ceylon.

1. Net budgetary Capital Expenditure
2. Equals Current Account deficit in the balance of payments adjusted for net official transfers.
3. Includes IMF Trust Fund, Concessional Loans and Grants.
4. Includes direct foreign investment, SDR Allocations and errors and omissions.

The failure of the domestic savings ratio to increase over time has to be also viewed in the context of the low annual growth in per capita gross domestic income which has been largely the result of the deterioration in the terms of trade since 1978. Policies to stimulate the growth of financial savings have been, by and large, successful with the rate of increase in time and savings deposits positively responding to high nominal rates of interest. However, it would appear that, on the whole, policies to encourage total savings through mobilization of financial savings, successful in a narrow sense, have been off-set by declines in savings elsewhere.

It is significant that the contribution of the Government by way of a current account surplus to the domestic savings effort has been negative in recent years. Coming as it does in the wake of a programmed withdrawal of subsidies, it does seem that efforts have not yielded results. It is true that the international economic environment has taken a heavy toll on government revenue, which is heavily dependent on export tax revenues. The need to reduce duties and maintain producer incentives, has had a large impact on the Government's capacity to generate savings. However, Sri Lanka has witnessed very large increases in investment since 1978 and the direct beneficiaries of such investment, associated largely with investment in infrastructure projects, will have to contribute their share to government revenue. This is essential if the public sector were to contribute its due share to the national savings effort. In this context, it is to be noted that revenue as a percentage of GDP at market prices has shown a declining trend even if one were to exclude export duty revenues.

Both Gross Domestic Capital formation (GDC) and Gross Domestic Fixed Capital formation (GDFC) registered increases of 29 per cent and 30 per cent in 1982 respectively. The rate of increase in GDFC of the private sector and the public corporations has been higher than that of the GDFC in the government sector. While the former increased by 32 per cent the latter increased by 21 per cent. There was a significant increase in the imports of capital goods in 1982, of which ships and aircraft were an important component, which increased the import content of GDFC from 32 per cent in 1981 to 37 per cent in 1982.

Total resources available to the country consisting of the GDP and import of goods and non-factor services at 1978 prices increased by 4.1 per cent in 1982 compared with 5.1 per cent in 1981. The availability of resources to the economy as in the previous year was reduced by a decline in the rate of increase in the import of goods and non-factor services and resulted in a marginal increase in the share of resources from domestic production. On the utilization side, consumption increasing at a much lower rate than in 1981 still absorbed 61 per cent while Gross Domestic Fixed Capital formation and exports accounted for 18 and 21 per cent respectively of the total resources available to the economy.

The year under review saw the continuation of the demand management policies that had helped in a large measure to remove in 1981, the disequilibrium that developed in 1980. The significant feature in monetary management in 1982 was the monetary and price stability that was sustained during the year. A slower growth in domestic credit and a decline in external banking assets (net) resulted in monetary growth in the year under review being broadly on targetted lines. Domestic credit which had expanded by 81 per cent in 1980 and had decelerated to 33 per cent in 1981, further decelerated to 25 per cent by the end of 1982. The main impetus to monetary expansion came from domestic credit, both to the government and to the private sector, although a gradual deceleration was evident in the rate of growth of credit to both sectors.

The expansionary impact of the increase in domestic credit was somewhat off-set by the decline in external banking (net) assets which declined once again by Rs. 568 million compared with declines of Rs. 3,177 million and Rs. 690 million in 1980 and 1981, respectively. Although the fall in external banking assets helped to moderate the adverse monetary repercussions of the increased domestic credit it resulted in increased pressure on the balance of payments. Reflecting these changes, broad money supply (M2) rose by 25 per cent compared to an increase of 23 per cent in 1981. Narrow money supply (M1), however, rose by 17 per cent as against a much lower increase of 6 per cent in the previous year.

The major feature of commercial banking activities was the improved liquidity position of the banks. The significant improvement in the liquidity of banks evident since the latter part of 1981 continued into the year under review. The banking system reacted to the improved liquidity by reducing interest rates on deposits by 2-5 per cent in the middle of the year. However, there were no changes in the interest rates on Central Bank accommodation to banks, the deposit rates offered by the National Savings Bank and the rate of interest on the rupee securities issued by the Government.

The moderate expansion in major monetary variables experienced in 1982 did not call for any significant monetary policy changes during the year. The policy measures that were introduced and intensified during the previous years were continued through the year under review, notwithstanding the deceleration in the rate of price increase. There were no changes in the Bank Rate of 14 per cent or the penal rates ranging from 21 to 30 per cent, which applied to accommodation above that made available at Bank Rate. The statutory reserve requirements of 14 per cent on demand deposits and 6 per cent on time and savings deposits remained unchanged during the year. On the other hand, efforts were directed towards mitigating the adverse effects of the high interest rates on priority sectors in an attempt to use monetary policy to stimulate the supply in the economy.

The need to ensure adequate medium and long-term credit to the export sector and to increase the active participation of commercial banks in project financing was recognized. The quantum of refinance provided from the Medium & Long-term Credit Fund (MLCF) of the Central Bank for export projects was raised from 80 per cent of project cost to cover the entire project cost with effect from January 1982. The refinance as well as the on-lending margins were also reduced slightly. The amount of refinance for pre-shipment credit made available at the concessionary rate of 12 per cent was also increased marginally. The growth of credit to this sector, however, failed to meet the targets envisaged in the National Credit Plan for 1982, towards which the Central Bank continued to work for the second successive year.

TABLE 1.4

Monetary Magnitudes 1977—1982

(Rs. Million)

	1977	1978	1979	1980	1981	1982
Changes in Domestic Credit	**1,464**	**1,662**	**3,624**	**11,286**	**8,330**	**8,483**
Increase in Net Credit to Government	– 278	– 1,126	1,057	6,052	3,817	4,361
Increase in Credit to Government Corporations	615	693	984	776	365	190
Increase in Credit to Co-operatives	509	205	– 439	– 86	93	– 54
Increase in Credit to other Private Sector	618	1,890	2,022	4,544	4,055	3,986
Change in Net External Banking Assets	**3,597**	**1,884**	**1,218**	**– 3,177**	**– 690**	**– 568**
Change in Total Assets and Liabilities	**5,061**	**3,546**	**4,842**	**8,109**	**7,640**	**7,915**
Increase in Broad Money Supply (M2)	2,396	2,175	4,166	4,803	4,587	6,063
Increase in Other Labilities (Net)	2,665	1,371	676	3,306	3,053	1,852

Percentage increases in Monetary Magnitudes

	1977	1978	1979	1980	1981	1982
Percentage increase in total Domestic Credit ..	20.2	19.1	35.0	80.7	33.0	25.3
Percentage increase in total Assets and Liabilities ..	66.4	28.0	29.9	38.5	26.2	21.5
Government as percentage of total Domestic Credit Increase ..	– 19.1	– 67.8	29.2	53.7	45.9	51.5
Non-Government as percentage of total Domestic Credit Increase ..	119.1	167.8	70.8	46.3	54.1	48.5
Percentage increase in-Broad Money Supply(M_2) ..	38.0	25.0	38.3	31.9	23.1	24.8
-Narrow Money Supply(M_1) ..	28.8	10.6	29.2	22.9	6.3	17.3

Source: Central Bank of Ceylon.

One of the developments that caused a great deal of concern to the Central Bank was the decline in rural credit. During the year, the total amount of credit extended to the rural sector declined marginally by 2 per cent. Yet, this credit disbursed under the Comprehensive Rural Credit Scheme (CRCS) by People's Bank, the rural banks, the Bank of Ceylon sub-offices and by the Hatton National Bank, as well as other loans to the rural sector extended by these institutions have not shown a growth commensurate with the increased level of activities which the rural sector has experienced in recent years. This trend is suggestive of an increased dependence on other more expensive sources of credit.

The decline in credit is also due to the high rates of default which continue to be an unsatisfactory feature of rural lending. In 1982, only a little over half the amount disbursed during the 1981/82 cultivation year was renewed. Although the drought had a serious impact on the repayment capacity of many farmers, and highlights the need for an efficient crop insurance scheme, the rehabilitation of the defaulters who, through their ineligibility to borrow had contributed to the decline in credit to the rural sector, engaged the attention of both the Central Bank and the Rural Credit Advisory Board (RCAB) . The re-scheduling scheme for cultivation loans granted under the CRCS from January 1977 to June 30, 1981 was initiated by the RCAB in the previous year and was implemented by the Bank of Ceylon which commenced the consolidation and re-scheduling of loans under this scheme in 1982. The People's Bank, however, has yet to implement this scheme. Unless the two state banks involved in rural lending make a concerted effort to implement this scheme, a segment of credit-needy farmers who are non-wilful defaulters will not have access to credit in the future.

The year 1982 witnessed a higher level of activity in the Capital Market of Sri Lanka with respect to new share issues. During the year ended 1982, there were 19 new share issues totalling Rs. 371 million as against 13 such issues amounting to Rs. 285 million during the previous year. The highest number of new issues in 1982 was in respect of Hotels & Travels, followed by investments in the Engineering, Motors & Industries categories. There was some evidence that the fiscal incentives provided for broad based ownership of companies and for increased investor participation were beginning to show results. As in 1981, the peak activity in the primary issue market was during the first quarter of the year which coincides with the last quarter of the income tax year. Almost all the shares were issued during this period. Except for three share offerings in December 1982, the lists of the other 16 companies were closed by the end of the year. Most of these issues were fully subscribed or underwritten before the closing of the respective lists. The increasing volume of new share issues as well as the broad basing of existing companies are indicative of the badly needed revitalization of the capital market which had been stagnant for a number of years.

The moderation in the monetary expansion experienced during the year was due both to the continuance of the tight monetary policies and to a reduced expansionary impact of budgetary operations. While recourse to bank borrowing for purposes of financing the budget increased marginally in absolute terms from Rs. 3,917 million in 1981 to Rs. 4,006 million in 1982, there was a decline in the ratio of bank borrowing to GDP from 4.6 per cent in 1981 to 4 per cent in the year under review. The expansionary impact of the budget was, however, less in 1982 largely due to a build-up of cash balances which occurred during the year. The overall budget deficit, however, increased from 17.5 per cent of GDP in 1981 to 20.2 per cent in 1982. This was due to the increase in expenditure during the year of 23 per cent being very much higher than the increase in total revenue of 10 per cent. Revenue as a percentage of GDP declined from 19 per cent in 1981 to 18 per cent in 1982, the lowest ratio during the last decade. Expenditure particularly capital expenditure during the year, however, ran at well below budgetted levels presumably due to the uncertainties that had prevailed on account of both the Presidential Election and the Referendum held during the year.

TABLE 1.5

Fiscal Magnitudes 1977—1982

Rs. Million

	1977	1978	1979	1980	1981	1982*
Revenue	6,686	11,688	12,730	14,068	16,228	17,809
Expenditure	9,760	18,853	21,521	30,343	31,094	38,097
Recurrent including Advance Accounts ..	6,578	12,239	12,531	16,489	17,729	19,230
Current Deficit / Surplus +	+ 108	- 551	+ 200	-2,421	-1,493	-1,421
Capital Expenditure- ..	3,182	6,614	8,991	13,854	13,373	18,867
Overall Budget Deficit ..	3,074	7,165	8,791	16,274	14,861	20,289
Fanancing-						
Foreign	1,779	4,454	4,237	6,735	8,208	9,270
Domestic Non-Bank ..	2,009	2,486	3,902	2,484	2,779	7,248
Domestic Bank ..	- 224	167	680	7,126	3,917	4,006
Use of Cash Balances ..	- 492	58	- 28	- 72	- 38	- 235
(As a Percentage of G. D. P. 1977—1982)						
Revenue ..	18.4	27.4	24.3	21.1	19.1	17.8
Expenditure	26.8	44.2	41.1	45.6	36.6	38.0
Recurrent including Advance Accounts ..	18.1	28.7	23.9	24.8	20.8	19.2
Current Deficit / Surplus+ ..	+ 0.3	- 1.3	+ 0.4	- 3.6	- 1.8	- 1.4
Capital Expenditure ..	8.7	15.5	17.2	20.8	15.7	18.8
Overall Budget Deficit ..	8.4	16.8	16.8	24.5	17.5	20.2
Financing						
Foreign	4.9	10.4	8.1	10.1	9.7	9.2
Domestic Non-Bank ..	5.5	5.8	7.4	3.7	3.3	7.2
Domestic Bank ..	- 0.6	0.4	1.3	10.7	4.6	4.0
Use of Cash Balances ..	- 1.4	0.1	- 0.1	- 0.1	- ...	- 0.2

*Provisional

Source: Central Bank of Ceylon.

On the whole, government budgetary operations indicated a mild reversal of the improvement witnessed in 1981. This reversal, however, largely attributable to unfavourable developments in the international environment led both to a decline in government revenue and in receipts of foreign aid, below anticipated levels. The actual revenue of Rs. 17,809 million was 8 per cent below targetted levels while of the expected foreign finance of Rs. 14,198 million, only two thirds of this amount or Rs. 9,270 million was received in 1982.

There was, however, a significant increase in the borrowed resources mobilized through the non-bank captive sources, particularly the National Savings Bank, but such increases were not enough to off-set the short-fall in revenue as well as in foreign finance. The advance account operations of the Government, however, showed an inpayment after several years, largely as a result of the reduced level of stocks of the Food Commissioner during the year. Notwithstanding this improvement the current account of the budget registered a deficit. It is significant that in 1981 the current account excluding the large net-outpayment in advance accounts showed a surplus. The adjustments in the aggregate level of expenditure that these developments called for were insufficient and the overall budget deficit increased as a ratio of GDP. In addition, increased recourse to 'captive' sources pre-empted part of the resources that would have been available for private sector investment activities.

TABLE 1 . 6

Summary of Balance of Payments 1977—1982

Rs. Million (SDR million in brackets)

	1977	1978	1979	1980	1981	1982(a)
Merchandise Exports	6,640 (651)	13,207 (675)	15,282 (759)	17,603 (818)	20,507 (903)	21,434 (934)
Merchandise Imports	6,290 (622)	15,600 (819)	22,570 (1,121)	33,915 (1,576)	36,123 (1,596)	41,902 (1,826)
Non-Factor Services (Net)	+ 457 (+44)	+ 356 (+18)	+ 979 (+48)	+1,290 (+60)	+1,950 (+85)	+2,094 (+91)
Factor Services (Net)	− 153 (−15)	− 237 (−12)	− 239 (−12)	− 432 (−20)	−1,712 (−75)	−1,968 (−86)
Private Transfers (Net)	+ 123 (+12)	+ 342 (+17)	+ 754 (+37)	+2,260 (+105)	+3,918 (+172)	+5,170 (+225)
Current Account Balance (b)	+1,266 (+117)	−1,032 (−75)	−3,556 (−177)	−10,912 (—507)	−8,342 (−375)	−11,793 (−515)
Non-Monetary Capital (Net)(c)	+ 326 (+32)	+2,600 (+133)	+3,306 (+164)	+6,585 (+306)	+7,691 (+341)	+9,885 (+431)
Aid disbursements (Net) (b)	+1,243 (+119)	+3,906 (+200)	+4,451 (+221)	+4,685 (+217)	+6,343 (+300)	+7,278 (+317)
Short-term finance (Net)	− 237 (−22)	− 40 (−2)	+ 1 (−)	+2,604 (+121)	+ 386 (+17)	− 63 (−2)
Other Non-Monetary Capital	− 190 (−18)	− 366 (−19)	+1,093 (+54)	+1,577 (+74)	+4,080 (+160)	+6,049 (+263)
Change in net International Reserve financed by monetary movements	−3,313 (−153)	−1,861 (−65)	− 793 (−35)	+2,967 (+166)	+ 405 (+26)	+1,149 (+24)

Some Key Indicators

	1977	1978	1979	1980	1981	1982(a)
Terms of Trade	102	100	72	58	46	38
Net Petroleum Imports	867 (83)	1,459 (75)	2,707 (134)	5,034 (234)	6,592 (291)	8,994 (391)
Current Account deficit as a percentage of GDP	—	3	7	18	11	13
Net Aid disbursements as a percentage of GDP	4	10	9	9	10	9
Gross International Reserves	5,573 (306)	7,477 (371)	9,652 (475)	6,766 (296)	9,222 (387)	10,956 (466)

(a) Provisional

(b) Includes Net Official Transfers.

(c) Excludes Net Official Transfers.

Source: Central Bank of Ceylon.

One of the disconcerting developments during the year was on the balance of payments front. While the overall deficit registered of SDR 24 million (Rs. 1,149 million) was marginally lower than that of 1981, the trade and current account deficits expanded sharply in 1982. The deficits in both merchandise and current accounts were the highest on record being SDR 892 million and SDR 515 million respectively. The current account deficit as a percentage of GDP was 13 per cent and represented a deterioration from the previous year's level.

Adverse terms of trade continued to plague the external payments position in 1982 for the fourth year in succession and contributed to an increased imbalance in the merchandise trade account. While the deterioration in the current account was also due to the sluggish world demand for Sri Lanka's traditional export products as manifested in the declining terms of trade, it was due in equal measure to higher import procurement. While a good part of the higher imports was aid financed, imports nevertheless grew by 14 per cent as compared with a one per cent increase in 1981. On the other hand, export performance in 1982 with a rate of growth of only 3.4 per cent in SDR terms has been disappointing. While it is true that the reduced world demand depressed the prices of our exports and the export volumes suffered due to adverse production trends, the deceleration in the rate of growth of exports in the face of the ever increasing demand for imports, calls for urgent action to increase production for exports with an equal emphasis in the still unexploited areas of import substitution.

Despite the large merchandise and current account deficits, the overall deficit in the balance of payments was confined to a small magnitude largely due to increased receipts from private transfers, consisting essentially of remittances of Sri Lankans employed abroad and the larger net inflows of capital in the form of direct investment and long-term foreign loans which were largely concessional. Private transfers in 1982 amounted to Rs. 5,789 million (SDR 252 million) or Rs. 1,359 million (SDR 57 million) more than what was received in 1981. Net inflows of capital were Rs. 9,885 million (SDR 431 million) in 1982 as compared with Rs. 7,691 million (SDR 341 million) in 1981. Nevertheless, the year, witnessed a further decline in the country's net external assets although there was an increase in gross external assets by 20 per cent to Rs. 10,956 million (SDR 466 million). The increase in gross external assets was brought about by the increased accumulation of liabilities by both the Central Bank and the commercial banks. Gross external assets at the end of 1982 were adequate to finance about 3 months imports.

The slow rate of growth in exports as well as the increase in debt service payments (including those on drawings from the IMF and Public Sector Suppliers' Credits), the latter being largely the result of the increase resort to commercial credits in the recent past, resulted in the debt service ratio increasing to 15.2 per cent from 13.3 per cent in 1981. The debt service ratio excluding IMF transactions also increased from 6.8 per cent to 9.5 per cent over the same period.

The most disturbing feature of the balance of payments developments in 1982 has been the singular lack of dynamism displayed by the export sector. The underlying principle behind the economic reforms of 1977 was the pursuit of an outward looking growth strategy which was to be sustained initially by foreign savings and thereafter by the achievement of balance of payments viability in the medium-term through an expansion of the export sector. The fact that the export sector almost stagnated in 1982 and the current account deficit was as high as 13 per cent of GDP while the debt service ratio also increased meant that the time horizon within which balance of payments viability could be achieved has been further extended, while the time available for remedial action has been correspondingly shortened.

In the context of an adverse international climate where an increasing number of countries are facing unmanageable debt servicing problems leading to complex debt rescheduling programmes, the need for reaching balance of payments viability in the shortest possible time period becomes a matter of paramount importance for continued and sustained economic expansion within the framework of a liberalized economy. In this context, while demand management policies can help in providing the necessary favourable climate for savings, investment and exports and in enhancing the effectiveness of the adjustment process, Sri Lanka's balance of payments problem is more fundamental in character to be overcome merely by the pursuit of demand management policies alone. The situation warrants corrective action in the form of strenuous efforts at promoting exports and the pursuit of policies which are conducive to export growth. These matters should receive the most urgent attention of the Government.

The year under review also witnessed a further intensification of Sri Lanka's problems concerning the energy sector. The increased demand for the principal sources of energy stemming from the expanded economic and social activities as well as the increase in oil prices during 1981 have resulted in a rapidly rising import bill for crude oil and petroleum products. The value of petroleum imports in SDR terms increased by 20 per cent in 1982. Oil imports constituted 67 per cent of Sri Lanka's total earnings from non-petroleum exports for 1982 as against 56 per cent in the previous year. While the increase in demand for electricity had to be met through additional thermal generation and hence, higher petroleum imports, the value of petroleum exports which had during the past few years been increasing, also declined by 4 per cent due to increased consumption of exportable oil products, viz., heavy diesel and naptha. As a proportion of total export earnings, the net oil import bill increased from 32 per cent in 1981 to 41 per cent in the current year. The growing demand coupled with higher prices exerted severe pressure on the balance of payments as well.

The state of the balance of payments of the country and Sri Lanka's experience during the decade of the energy crisis emphasize the need to reduce her dependence on oil imports in the quickest possible time. Short-term policy options are equally important and should be aimed at improving efficiency in the use and conservation of energy. In this context, the establishment of Natural Resources, Energy and Science Authority in June 1982 is an important step in creating the necessary institutional framework for the formulation and implementation of such policies. The functions of this Authority include among other things advising the Minister regarding the policies concerned with all aspects of energy requirements of Sri Lanka as well as plans for the overall development of energy resources and measures for optimal use and conservation of energy.

The important structural change in Sri Lanka's imports during recent years has been the increasing share of intermediate and investment goods. While increased production of rice and of other subsidiary food crops has contributed to the decline in the share of consumer goods imports, this process should be accelerated. There still exists a great deal of unrealised potential in the agro-based industrial sector both for purposes of import substitution as well as for exports. With the opening up of the lands under the Mahaveli Scheme, there will be ample scope for the growing of crops other than paddy. It is also necessary that the increased production of paddy that could be expected from these developments does not suffer by way of depressed prices due to pronounced increases in supplies. Consideration will have to be given to the export potential in rice, if the encouraging momentum in rice production is to be sustained in the future. The major emphasis, however, has to be on conservation of fuel, if there is to be a sizeable impact on the large and growing import bill. It is also important that the large investments made in the shipping and airline sectors, essentially through foreign commercial financing, be made to pay their way, if they are not to increase the debt service burden as well as cause problems for the government budget.

Even with all these measures on the import front, the imports necessary to sustain the Sri Lankan economy will continue to be high and there is no escape from a policy of accelerating exports. The prospects of an increasing debt service burden, peaking of the inflow of private remittances and the bleak outlook for concessional aid add a sense of urgency to this task. However, the task of accelerating exports is not going to be easy in the present international environment. Sluggish growth coupled with rising rates of unemployment in the industrial countries has meant restrained demand for imports in these countries. In addition, recessionary conditions in the industrial countries have also led to the strengthening of protectionist tendencies. Apart from their impact on exports, the present fiscal and monetary policies in such countries resulting in high nominal and real rates of interest will add to Sri Lanka's debt service burden, even in respect of borrowings made from international lending institutions. Notwithstanding the adverse climate, efforts directed towards increasing the export volumes of the plantation crops, tea, rubber and coconut, perhaps provide the best immediate prospects for augmenting the country's export earnings in the short-term. While the declared policy of the Government to confine tax holidays in the future essentially to export oriented ventures, is a desirable step, the rationalization of Sri Lanka's tariff structure could also provide the necessary climate for new export and import substituting ventures to be set up.

It is now five years since Sri Lanka initiated its program of economic reforms designed to liberalize the economy and put it on the basis of an outward looking strategy. The past five years have seen considerable progress. The most notable success has been in respect to the country's ability in breaking out of the low investment and low growth pattern of the pre-1977 period. As observed in last year's annual report, it is unfortunate that Sri Lanka's export oriented growth strategy has had to be tried and tested in an entirely hostile international economic environment. Yet, the fact that economic growth continued to be sustained in the face of adverse developments is remarkable. The doubling of petroleum prices which led to substantial increases in the import bill, the recession which reduced the demand for exports, government revenue and, to some extent, aid flows, and international inflation which led to the continuous deterioration in the terms of trade and to cost escalations of the public investment program of the country are just three of such developments which had an overwhelming impact on the country's saving and investment record and on its balance of payments and budgetary performance. Nevertheless, Sri Lanka's growth rate of real GDP has averaged 6.2 per cent over the last five years. Both the public sector, through the public investment program, as well as the private sector, which was freed of most controls, have contributed to the growth effort which has also been accompanied by significant gains in employment.

While sector-wise the most impressive real growth was achieved in the agricultural sector, particularly in paddy, and to some extent in the industrial sector too, the lack of progress in the tree crop production and the export sector in general has been disappointing. In addition, the high levels of investment in the face of an inadequate increase in domestic savings, though sustained by concessional aid flows, have also meant increased resort to foreign commercial borrowing, a draw down of reserves and a depreciation in the exchange rate. The impact domestically of increased levels of investment has been the increase in the rate of price increases, escalating costs of investments and, in the face of continued inflationary trends, the lack of any significant increases in savings, implying a shift of resources from investment to consumption. The pursuit of effective demand management policies, however, has helped to restore the equilibrium somewhat in recent years. The adjustment process aimed at ensuring sustainable deficits in the current account of the balance of payments and in the budget necessarily called for policies which continued to demand heavy sacrifices from the people. There are clear signs that this adjustment momentum has to be maintained in the future as well, if the country is to benefit from its present economic strategy. The acceleration of the rate of growth in exports which was one of the major objectives of the economic and exchange rate reforms has not materialized. While this is difficult to achieve in the present international economic environment, it must nevertheless continue to be an important objective particularly in the light of the growth rate in imports as well as the declining trend in the country's terms of trade.

Developments in the various sectors during the year are discussed, in the sections to follow in greater detail.