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CEYLON - TEMPORARY DUTY INCREASES

Request for Extension of Waiver of 21 January 1967

On 21 January 1967 the CONTRACTING PARTIES decided (BISD, Fifteenth Supplement, page 76) to waive the provisions of paragraph 1 of Article II of GATT to allow the Government of Ceylon to maintain in force until 31 December 1968 a number of duties temporarily increased above the level bound in Schedule VI - Ceylon. Most of these duty increases were originally authorized by Decision of the CONTRACTING PARTIES of 10 April 1961 (BISD, Tenth Supplement, page 35).

The following request for an extension of the waiver of 21 January 1967 has now been received from the Government of Ceylon.

I refer to item 14(b) of document L/3055 (Advance Agenda) for the twenty-fifth session of the CONTRACTING PARTIES of GATT. This waiver is due to expire on 31 December 1968. The Government of Ceylon now requests the extension of this waiver.

During the consultations held with the Committee on Balance-of-Payments Restrictions in November 1966, the Ceylon representative drew the attention of the Committee to the review of the tariff system which the Government of Ceylon had undertaken. This review has been completed, and the Government had on 2 August this year, introduced a complete revision of the tariff structure. As a result of this revision, duties have been imposed on twenty-nine additional items, in excess of the bound rates under GATT. The Ceylon Government now seeks in addition to the extension of the existing waiver, a waiver on these additional items. I am forwarding two notes entitled as follows:

1. Schedule VI: Ceylon - Introduction of the Brussels Tariff Nomenclature and revision of tariff structure on 2 August 1968, and request for a further extension of the waiver of 21 January 1967.

2. Ceylon: Request for an extension of waiver granted to Ceylon on 21 January 1967, and a request for a waiver on a further twenty-nine items on which duties were increased on 2 and 9 August 1968.

The latter note provides information on the balance-of-payments situation of Ceylon. These notes[1] are accompanied by statistical material as well as the relevant Government Gazettes.

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[1] One copy in English of each of these publications is being distributed to each contracting party.

Note 1

SCHEDULE VI: CEYLON - INTRODUCTION OF THE BRUSSELS TARIFF NOMENCLATURE AND REVISION OF TARIFF STRUCTURE ON 2 AUGUST 1968 AND REQUEST FOR A FURTHER EXTENSION OF THE WAIVER OF 21 JANUARY 1967

At the time the Committee on Balance-of-Payments Restrictions examined in November 1966, the request of the Ceylon Government for a further extension of the waiver and the Committee decided to recommend the extension of the waiver until 31 December 1968, the Ceylon representative drew the attention of the Committee to the review of the tariff system which the Government of Ceylon had decided to undertake.

This review has been completed and the Government, on 2 August 1968, has introduced a complete revision of the tariff structure. With effect from that date, the Government has adopted the Brussels Tariff Nomenclature (BTN) in lieu of the Standard International Trade Classification (revised) on which the Ceylon tariffs had hitherto been based. The adoption of the BTN has been accompanied by a substantial liberalization of tariffs particularly in regard to the import duties on items considered essential for development. At the same time import duties on items considered inessential or on items where domestic supplies or substitutes are available, have been increased for the purpose of either restricting inessential imports or giving protection to domestic industry. Full particulars of the new tariff structure are given in Ceylon Government Gazette No. 14813/2 of 2 August 1968 and No. 14814/1 of 9 August 1968, copies of which are annexed.[1]

The effect of this major revision in Ceylon tariffs on Ceylon's obligations to GATT as set out in Schedule VI, Parts I and II are given in the following statements which are also annexed[1]:

(a) Schedule VI - Ceylon - Part I - most-favoured-nation tariff.

(b) Schedule VI - Ceylon - Part II - preferential tariff.

(c) Schedule VI - Ceylon - items on which the rates of duty are bound both in Part I and Part II.

With regard to statements (a) and (b) above the items are identified under the BTN and the SITC (revised) and particulars are given in respect of each tariff item under the bound rate, the waiver rate, where a waiver has been granted, and the present duty, i.e. the effective duty after 2 August 1968. The value of imports of the various items in 1966 and 1967 are also given in order to estimate the volume of trade involved. It is important to recognize that in regard to a large number of items (ex items), Ceylon's obligation is in respect of part items only for which separate statistics are not available.

[1]One copy of each is being distributed to each contracting party.

The statement referred to at (c) above similarly analyzes the position in regard to the tariff items where the most-favoured-nation duty as well as the preferential duty is bound so that the margin between the two rates is also bound.

The summary position with regard to the changes effected under Schedule VI, Parts I and II are examined below:

Schedule VI - Ceylon -
Part I - Most-Favoured-Nation Tariff

(rupees)

		No. of items	Imports	
			1966	1967
A.	Items on which there is no change in duties, i.e. at bound rate	12	72,354,527	62,725,353
B.	Items on which duties have been reduced from waiver rate to bound rate	6	9,558,726	9,623,988
C.	Items on which duties have been reduced from waiver rate but above the bound rate	10	31,142,365	20,026,871
D.	Items on which duties are at waiver rate	5 + (1)	6,809,625	7,718,877
E.	Items on which duties have been increased above the bound rate where there is no waiver rate	0 + (2)	316,227	312,254
F.	Items on which duties have been increased above the waiver rate	23 + (4)	23,670,373	43,816,397
G.	Items on which duties have been reduced below the bound rate	59	121,190,385	101,026,580
		115 + (7)		

( ) = Sub-items.

The total trade in all the 115 bound items in the most-favoured-nation schedule is Cey Rs 259 million in 1966 and Cey Rs 237 million in 1967. The rates of duty on fifty-nine items (G items) have been reduced to less than the respective bound rates. The trade in these items amounts to Cey Rs 121 million in 1966 and Cey Rs 101 million in 1967. In respect of further sixteen items (B and C items) duties have been reduced below the waiver rate and the amount of the trade covered by these items is Cey Rs 40 million in 1966 and Cey Rs 30 million in 1967. The extent of the changes in tariffs in these items underlines the degree of liberalization introduced recently. In regard to A and D items there have been no changes i.e. the duties are at the bound rate or at the waiver rate. The trade in these items is Cey Rs 78 million in 1966 and Cey Rs 70 million in 1967.

It is only in regard to twenty-nine items (E and F items) that duties have been increased in excess of Ceylon's existing obligations to GATT. These items include six sub-items resulting from the sub-division of the respective tariff items after the introduction of the new tariff structure in August 1968. The total trade in these items is Cey Rs 24 million in 1966 and Cey Rs 44 million in 1967. A separate table giving full particulars of the items where the duties have been increased either in excess of the waiver rate (twenty-seven F items) or over the bound rate when there is no waiver rate (two E items) is annexed. The increases in these tariffs have been accompanied by liberalizing import restrictions which applied earlier. Thirteen of these items have been placed on open general licence and four other items viz. grease BTN 22.10, lubricating oil BTN 27.10, superphosphates BTN 31.03 and muriate of potash BTN 31.04 are either entirely or at least almost entirely imported by State organizations which ensures that all essential requirements will be imported. All major items in these two categories (F and E items) have therefore been liberalized in one way or another.

An analysis of the most-favoured-nation schedule shows that almost 50 per cent of the items are duty free. The number of duty-free items before August 1968 was only nine, today the duty-free items number fifty full items and in addition seven part items which have resulted from sub-division of certain items (BTN 84.28 and 85.01) are also free. Duty-free treatment has been accorded to all items necessary for development, including machinery for agricultural and industrial development and chemicals and other essential development items.

In making these changes, consideration was given, wherever possible, to the request made by representatives of certain countries at the balance-of-payments consultations in November 1966, to reduce the duties on specified items of development. Thus the duties on rosin (BTN 13.02), inorganic gases, other, excluding chlorine (BTN 28.04), cranes and hoists and parts (BTN 84.22), conveying machinery (BTN 84.23), sewing machines, industrial (BTN 84.41) have been entirely eliminated and the duties on surgical and scientific instruments (BTN 90.23, 90.24, 90.26) have been brought down below the waiver rate of 40 per cent to 30 per cent. The Swedish representative had drawn Ceylon's attention to the duty increases in July 1966 on ceiling and flooring boards (BTN 44.13) from 45 per cent to 100 per cent. It has not been found possible to reduce the duty on this item. The duty on this item has, in August 1968, been increased to 210 per cent because this item is considered not essential as local substitute timbers are available. However, protection for the domestic supplies have been given only by way of a higher tariff and the import of this item has now been placed under the open general licence.

Schedule VI - Ceylon -
Part II - Preferential Tariff

The summary position with regard to the preferential tariff is as follows:

(rupees)

	No. of items	Imports	
		1966	1967
A. Items on which there is no change in duties, i.e. at bound rate	5	2,760,180	1,155,353
B. Items on which duties have been reduced from waiver rate to bound rate	3	1,048,748	835,058
C. Items on which duties have been reduced from waiver rate but above the bound rate	0	-	-
D. Items on which duties are at waiver rate	0 + (3)	1,589,875	2,258,284
E. Items on which duties have been increased above the bound rate where there is no waiver rate	0 + (2)	316,227	312,254
F. Items on which duties have been increased above the waiver rate	0	-	-
G. Items on which duties have been reduced below the bound rate	34	38,068,780	46,915,794

( ) = Sub-items.

The total trade in 1966 and 1967 in the forty-two items bound in the preferential schedule is Cey Rs 42 million and Cey Rs 49 million respectively. Duties on eight items in the schedule (A and B items) are now at the bound rates and in regard to a further three sub-items (D items) the duties are at the waiver rate. The total trade of these items in the preferential schedule and the duties on which are in conformity with Ceylon's undertaking to GATT are Cey Rs 5 million in 1966 and Cey Rs 4 million in 1967. On thirty-four items duties have been reduced below the bound rate. The trade in these items which cover a very substantial part of the total import trade of all items included in the preferential schedule, amounted to Cey Rs 38 million in 1966 and Cey Rs 47 million in 1967. Details of the duty changes affecting these thirty-four items in the preferential schedule are readily ascertainable from the statement referred to at (b) earlier. It will be seen that duties in respect of twenty-nine items have been eliminated. Prior to August 1968 not a single item in the preferential schedule, Part II was duty free (wattle bark extract, BTN 32.01 was covered by a waiver rate). All these are items essential for development. The balance, five items, are food items where the duties have been reduced to below the bound rate.

It is only in regard to two sub-items, agricultural machinery and parts, incubators for poultry (BTN 84.28), that the duties in the preferential schedule have been increased in contravention of Ceylon's existing obligations to GATT. The trade in these items which are also ex items, is however negligible.

Details of the bound rates, waiver rates and present duties on items, the duties on which are bound both in the most-favoured-nation and preferential schedules, are given in the annexed Table III.[1] The summary position with regard to these thirty items is as follows:

A = Number of items where the margin is not changed	7
B = Number of items where the margin is reduced	23 + (2)
C = Number of items where the margin is increased	0 + (3)
	30 + (5)

( ) = Sub-items.

The margin has been increased only in regard to three sub-items, viz. BTN 85.01, motors for non-industrial use. The margin has been reduced on twenty-three items and two sub-items by the elimination of duty on nineteen items and five sub-items and reducing the margin on one item (BTN 08.04, currants). The twenty-five items on which duties have been eliminated are all essential for development. It is, therefore, the need for according special tariff treatment for development needs that is the reason for altering the bound margins in the schedules. In fact the prime consideration which motivated the Government in adopting the new tariff structure in August 1968 is to accord special duty treatment for items which are essential for the country's development needs.

Bearing these considerations in mind, the Government of Ceylon brings to the notice of the CONTRACTING PARTIES the introduction of the new tariff classification with effect from 2 August 1968. Details of the new duties under the BTN classification are given in Gazette No. 14813/2 of 2 August 1968 and No. 14814/1 of 9 August 1968.

Further the Government of Ceylon requests:

1. An extension of the waiver of 21 January 1967 relating to Ceylon's temporary duty increases on certain items bound in the Ceylon Schedule for a further period of two years from 31 December 1968.

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[1] One copy is being distributed to each contracting party.

2. An additional waiver on the twenty-seven items (F items) in the most-favoured-nation schedule, the duties on which have been raised above the present waiver rate.

3. An additional waiver on the two items (E items) in the most-favoured-nation schedule the duties on which have been increased above the bound rate and on which there is no waiver at present.

A list of items referred to at 2 and 3 above is annexed.[1]

4. A waiver on the following two sub-items in the preferential schedule:

BTN 84.28 - Incubator, poultry
BTN 84.28 - Incubator, poultry, parts

where the duty has been, in each case, increased from the bound rate of 12 per cent to 40 per cent.

5. Also a waiver on the

(i) twenty-five items (B items in list where margins are bound) in which the margin has been reduced;

(ii) three sub-items (C items in margins list) in which the margin is increased.

The items referred to at 5(i) and 5(ii) are readily identifiable in the list of items where the duties are bound in both Parts I and II of the Ceylon Schedule and which is annexed.[2]

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[1]In Table I.a., a copy of which is being distributed to each contracting party.

[2]In Table III, a copy of which is being distributed to each contracting party.

Note 2

CEYLON: REQUEST FOR AN EXTENSION OF WAIVER GRANTED TO CEYLON ON 21 JANUARY 1967 AND A REQUEST FOR A WAIVER ON A FURTHER TWENTY-NINE ITEMS ON WHICH THE DUTIES HAVE BEEN INCREASED ON 2 AND 9 AUGUST 1968

1. Background to Ceylon balance-of-payments difficulties

The adverse trends in Ceylon's external payments situation which had been a feature for the past decade continued in 1967. Tables 1 and 2 give the essential statistics on Ceylon's balance-of-payments position.

Export earnings from merchandise fell by a further Cey Rs 28 million to Cey Rs 1,646 million, the lowest in many years, while import payments at Cey Rs 1,997 million did not differ significantly as compared with 1966. The deficit on merchandise trade in 1967 amounted to Cey Rs 351 million (as compared with Cey Rs 344 million in 1966). Ceylon's earnings on invisibles account also fell markedly in 1967 while payments increased; consequently the invisibles surplus of Cey Rs 53 million in 1966 was reduced to Cey Rs 22 million in 1967. When the merchandise deficit is adjusted for the smaller surplus on invisibles account in 1967, the current account of Ceylon's balance of payments shows a deficit of Cey Rs 329 million in 1967, as compared with a corresponding deficit of Cey Rs 290 million in the previous year.

Ceylon's external reserves (net of Sterling Loans Sinking Funds) had declined by almost Cey Rs 126 million in the course of 1966, and in view of its low level it was impossible to conceive financing a current account deficit of the magnitude of Cey Rs 329 million out of these resources. In the event, however, Ceylon's ability to finance a volume of payments far in excess of currently earned income in 1967 was due to a larger inflow of aid and short-term borrowings abroad, mainly from the International Monetary Fund. If such resources were not available to the Ceylon economy in 1967, the only choice would have been to countenance a lower level of economic activity and a lower rate of economic growth. In fact the rate of economic growth in the past few years has been barely sufficient to cope with the annual increase in population and to absorb the increase in the country's work-force. An encouraging feature in 1967, however, has been the fact that increased amounts of external resources have been diverted to productive uses and conscious attempts have been made in framing the import budget, to change the composition of imports in favour of investment and raw material goods, as explained in greater detail in subsequent sections.

External resources and their use

In 1967, the total external resources available to Ceylon amounted to Cey Rs 2,393 million. This was Cey Rs 12 million less than the resources available in 1966. Since export incomes had declined to Cey Rs 1,646 million from Cey Rs 1,674 million in 1966, and as earnings from invisibles had declined from Cey Rs 204 million in 1966 to Cey Rs 198 million in 1967, the mobilization of external resources to a level approximating that of 1966 was made possible, principally as a result of an enhanced capital inflow. Long-term capital inflows increased from Cey Rs 226 million in 1966 to Cey Rs 261 million in 1967 and provided 11 per cent of Ceylon's external resources in that year, as compared with 6 per cent and 9 per cent in 1965 and 1966, respectively. Of this total, the value of loan finance increased from Cey Rs 173 million in 1966 to Cey Rs 212 million in 1967, while grants declined in value from Cey Rs 51 million in 1966 to Cey Rs 46 million in 1967. In fact, a noticeable feature of the pattern of capital inflows into Ceylon in recent years has been the increasing share of loans and the declining share of grants in total aid inflows, with corresponding implications for Ceylon's debt-servicing capacity in future years. Thus the share of loans in total capital inflows has increased from 55 per cent in 1965 to 82 per cent in 1967 while the share of grants has decreased from 45 per cent to 18 per cent, over the same period.

Another important facet of the financing of Ceylon's payments deficits in recent years has been the increasing resort to the accumulation of short-term liabilities, mostly with a maturity pattern of less than five years. The principal component of such short-term liabilities has been drawings from the International Monetary Fund, of which the outstanding total amounts to US$79.0 million; of this sum US$19.5 million consists of drawings under the International Monetary Fund's Compensatory Financing Scheme for fluctuations in export incomes. Drawings from the International Monetary Fund have continued to provide a substantial volume of external resources in the last three years; they amounted to US$22.9 million in 1965, US$30.2 million in 1966 and US$25.7 million in 1967. In 1967, Ceylon's external resources were further supplemented by increasing the indebtedness on bilateral payments agreements account by Cey Rs 80 million and short-term borrowings from foreign banking sources of Cey Rs 57 million. In sum, therefore, of the external resources available to Ceylon in 1967, only 77 per cent was obtained from earned resources while 23 per cent of resources were secured through various short- and long-term borrowing arrangements. This picture compares unfavourably with the years 1965 and 1966, when 89 per cent and 79 per cent respectively of Ceylon's external resources were secured from earned income. This however, was inevitable in the context of a pronounced decline in export incomes - principally due to a decline in average export prices - and a rise in imports necessitated by the need to increase the tempo of economic activity in the country, after the very low levels reached in 1964, which in itself was to a large extent due to a marked decline in import capacity, caused mainly by adverse movements in Ceylon's terms of trade.

Of the external resources of Cey Rs 2,393 million available to Ceylon in 1967, as in previous years, more than four fifths was used for the purchase of merchandise imports. Thirteen per cent of such imports were financed out of aid, as compared with 11 per cent in 1966 and only 7 per cent in 1965. However, in 1967, the orientation in the import programme was more marked towards investment goods and raw materials, both in terms of expenditure out of owned and aid resources. The effects of such changes in the pattern of imports on the structure of production were evident in increases in output for home use, both in non-export agriculture and in industrial production. For example, there was a marked increase in 1967 in the import of agricultural inputs such as fertilizer, tractors, and other transport equipment, machinery and industrial raw material. Quite apart from the fact that increased aid inflows in 1967 facilitated the import of investment and raw material imports, considerable relief was also obtained on capital account since the volume of resources devoted to servicing old loans and payments on invisibles account were moderate in 1967. In the case of payments in respect of invisibles, while there were increases in outflows in respect of investment income, and interest payments, they were offset somewhat by a fall in migrants' transfers. There was also a marked decline in the volume of resources devoted to the amortization of old loans; this was however, mainly due to the fact that there was a substantial decline in 1967 in the payments due on drawings from the International Monetary Fund.

2. The devaluation of the rupee

The decision to devalue the Ceylon rupee by 20 per cent on 22 November 1967, arose partly as a result of long-term factors that had resulted in an over-valuation of the Ceylon rupee, and partly as a result of the devaluation of the United Kingdom pound in November 1967. From the long-term standpoint, the expansionary impact of the monetary-fiscal imbalance which had continued for some time in Ceylon had resulted in the imposition of severe import and exchange controls on the one hand and bred circumventions through the over-invoicing of imports and under-invoicing of exports, on the other, with a consequent loss in foreign exchange.

Rising domestic prices and costs, particularly in the export sector had also tended to diminish progressively Ceylon's competitive capacity. It had therefore, been increasingly appreciated that both with a view towards restricting the demand for imports, providing added incentive to import substitution, agriculture and industry and with a view towards affording some relief to exporters, an adjustment of the overvalued exchange rate appeared to be necessary. It was felt that the devaluation of the United Kingdom pound would have sooner or later brought out the weakness in Ceylon's exchange rate into sharper focus, with adverse consequences for export income.

3. The position in 1968

Table 3 gives details of Ceylon's balance-of-payments position for the period January-June 1968.

The deficit in the merchandise account in the first half of 1968 provisionally estimated at Cey Rs 306.8 million shows a substantial increase over the deficit of Cey Rs 183.8 million in the first half of 1967. However, an interpretation of the figures must make due allowance for the difference between the exchange rates in the first half of 1968 and those prevailing in the first half of 1967 as a result of the devaluation of the rupee in November 1967. For example, the value of imports in 1968, in rupee terms, will rise by about 7 per cent over the pre-devaluation amounts, in the case of those imports arising in the United Kingdom, or in other countries which devalued to the same extent as the United Kingdom, while imports from monetary areas which did not devalue will show an increase of up to 25 per cent in value over the pre-devaluation amount. This applies to exports as well, where prices are externally determined. The regional pattern of trade for 1966 and 1967 indicates that approximately 28 per cent of exports were to the United Kingdom and about 21 per cent were from the United Kingdom.

Table 3 gives the statistical breakdown of Ceylon's balance of payments for the first half of 1967 and 1968. According to provisional estimates the export earnings at Cey Rs 885.5 million registered an increase of Cey Rs 72 million in the first half of 1968 over the corresponding period in 1967. The value of imports in the first half of 1968 at Cey Rs 1,192.3 million was Cey Rs 195 million in excess of the value of merchandise imports in the same period of 1967. Hence the balance on visible trade in the first half of 1968 showed a deficit of Cey Rs 306.8 million as compared with a deficit of Cey Rs 183.8 million in the corresponding period last year.

The invisibles account which was in surplus in the first half of 1967 turned into a deficit of approximately Cey Rs 3 million during the first half of 1968. This is mainly attributable to a sharp fall in the amount of grants and gifts in kind received in 1968. It is noteworthy that, in the pattern of capital inflow into Ceylon in recent years, the share of loans in total aid inflows has been increasing, with grants declining significantly, with corresponding repercussions on Ceylon's debt-servicing capacity in future years. The share of grants in total capital inflows has decreased from 24 per cent in the first half of 1967 to 9 per cent during the first half of 1968.

The deficit in the invisibles account is also partly attributable to a fall in the receipts on the port transportation account, due to fewer number of vessels calling at the Port of Colombo on account of the closure of the Suez Canal from June 1967, and also the continued releases out of funds held back on account of the moratorium on profits imposed in July 1964.

In sum total, therefore, the current account showed a substantial deficit amounting to Cey Rs 310 million in the first half of 1968 as compared to a deficit of approximately Cey Rs 179 million in the first half of 1967. The capital account of the balance of payments in the first half of 1968 showed a surplus of Cey Rs 137 million as compared with a surplus of Cey Rs 60.6 million in the first half of 1967.

Therefore, Ceylon's "basic balance" which reflects the country's net external position on both commercial and long-term capital transactions, showed a deficit of Cey Rs 173 million in the first half of 1968. The basic deficit for the comparable period in 1967 was Cey Rs 118.3 million. The deficit in 1968 was financed primarily by accommodations at the International Monetary Fund both under the facilities for compensatory financing of fluctuations in export earnings as a result of which Ceylon became eligible to draw US$19.3 million in April, and under the normal lending policy of the Fund which enabled Ceylon to draw a further US$10 million within the period under review.

Increased indebtedness on the bilateral payments agreements account also significantly contributed towards financing the deficit in the first half of 1968. Consequently, the gross external assets in the first half of 1968 declined by only less than Cey Rs 3 million.

The trade balance on commercial transactions also showed an adverse movement in the first half of 1968 as compared to the corresponding period last year. On commercial transactions the trade balances increased from Cey Rs 102.4 million in the first half of 1967 to Cey Rs 180.0 million in the first half of 1968 indicating that in 1968 a much higher value of imports had to be financed from own resources and short-term borrowings.

Detailed trends in exports and imports

The performance of tea and rubber exports in the first half of 1968 has been disappointing despite the devaluation of the rupee. Although the average f.o.b. prices of all teas in the first half of 1968 stood at Cey Rs 2.50 per lb. as compared to the Cey Rs 2.24 per lb. in the first half of 1967, this was partly due to the automatic upward adjustment of prices to devaluation. In fact, the Central Bank Trade Indices for exports show an upward trend in tea prices even before the devaluation, when the index rose from 75 in August 1967 to 79 and 83 in September and October, respectively. Despite the slight improvement in prices, the value of tea exports fell substantially (by Cey Rs 42.2 million) because of interruptions in the outflow of tea exports following a prolonged strike among dock-workers and mercantile employees.

Compared to the first half of 1967 rubber has fared badly in the corresponding period of 1968. The Central Bank Indices for rubber export prices indicate that the index for the first half of 1968 was only 74 compared to 88 in the corresponding period of 1967. The apparent improvement in rupee prices of rubber exports in 1968 can be attributed largely to devaluation. In terms of overall earnings of rubber, the trade data revealed a substantial drop in the first half of 1968 as compared to that of the same period in 1967. Despite the labour unrest referred to earlier, rubber exports in the first half of 1968 showed only a marginal drop in volume. Earnings, however, amounted only to Cey Rs 142.4 million in the first half of 1968 as compared to Cey Rs 168.3 million in the first half of 1967 in view of the decline in prices.

Prices fetched by the three coconut products, desiccated, copra and oil, have on the whole been appreciably better in the first half of 1968, compared to the performance during the corresponding period in 1967. On the average in terms of the nut equivalent the prices fetched have increased by almost 70 per cent in 1968 over the prices ruling in 1967. The volume according to trade data has also increased by 17 per cent in the first half of 1968, compared to the volume in the corresponding period in 1967. This exceptional situation is however not expected to continue, because of the resumption of interrupted supplies of competing oils from Nigeria, as internal disturbances subside, and the increase in supplies from Indonesia.

The factors behind this export performance which fell short of expectations can largely be attributed to factors beyond Ceylon's control. That is, general over-supply of tea in the world market with increased supplies coming from new regions, such as East Africa in the case of tea, and the stagnant world demand for natural rubber - both exercising a depressing influence on the prices of tea and rubber respectively.

Import payments have registered a substantial increase in the first half of 1968 as compared to the same period last year. This has occurred in spite of a fall in the volume of all imports from 97 in the first half of 1967 to 92 in the first half of 1968 as measured by the Central Bank Trade Indices. Within this broad category the volume index of textiles and intermediate goods was higher in the first half of 1968, while the volume index in respect of all other categories fell in 1968. Import prices however have increased sharply in 1968 over the 1967 first half level. This is shown in the table below:

June 1967 and 1968 Indices (1958 = 100)

	Food and drink	Textiles	Other consumer goods	Intermediate	Investment	All
June 1967	110	105	117	96	260	130
June 1968	160	117	188	115	366	182

The price increase has been sharpest in the case of the food and drink category and the investment goods category. In fact the increase in the world price of rice from around £ 50 per ton in 1967 to £ 70 per ton in 1968 has robbed Ceylon of the potential savings in foreign exchange resulting from significant increases in the local production of rice. Another cause contributing to the higher level of import payments in the first half of 1968 as compared to the first half of 1967 has been the higher freight payments due to the closure of the Suez Canal since June 1967. Freight rates were revised upwards by 15-25 per cent. A further factor causing import values to be higher in the first half of 1968 over the 1967 first half level has been the increase in rupee prices on account of devaluation.

Compared to the imports in the first half of 1967, imports in the first half of 1968 indicate that a proportionately large amount has been financed out of aid. The value of imports tied to aid increased from Cey Rs 81.4 million in the first half of 1967 to Cey Rs 164.1 million in the first half of 1968.

These movements in export and import prices have continued to result in a deterioration of Ceylon's terms of trade from 64 in June 1967 to 56 in June 1968.

Ceylon was able to finance a volume of payments far in excess of currently earned incomes in the first half of 1968 without running down the reserves too much, chiefly as a result of larger inflows of aid and borrowings from the International Monetary Fund as well as increased indebtedness to the bilateral payments agreement partners, particularly China. If such resources were not available to Ceylon, the only choice would have been to countenance a lower level of economic activity and a lower rate of economic growth. This would have caused a setback to the stabilization programme under way for some time. However, it is disturbing to notice the higher import bill being absorbed by price increases rather than by volume increases, particularly relating to imports of intermediate and investment goods.

Foreign Exchange Entitlement Certificate Scheme - Vide Gazette No. 14,800/3 of 5 May 1968[1]

Since about 1960 when foreign exchange reserves fell to low levels as a result of the continuous deterioration in the balance of payments, the par value of the Ceylon rupee was maintained only by increasing the stringent trade and currency controls. After six to seven years of such administrative controls it was generally felt that they tended to act as a drag on growth. It was partly for this reason that the Government with effect from 6 May 1968 introduced the Foreign Exchange Entitlement Certificate Scheme, under which certain foreign exchange receipts and payments were diverted via a certificate market. The following are the main objectives of the Scheme:

1. to introduce some flexibility in respect of the country's import requirements by introducing a gradual reform of the import licensing system;

[1]One copy is being distributed to each contracting party.

2. to give a stimulus to all exports of minor products which qualify for certificates;

3. to reduce the volume of foreign exchange transactions in the black market by providing a more attractive rate for tourists and certain other items of foreign exchange earnings which are believed to be a source of finance for the black market;

4. to absorb a part of the heavy liquidity-overhang in the economy.

As the Scheme has been in operation for only two months in the first half of 1968 it is too early to make an objective judgment on its impact, not only because it requires time for the stabilizing forces to emerge but also because interruptions to foreign trade in the second quarter of 1968 due to strikes in key sectors would have distorted the picture.

Foreign reserves

The gross external assets of Ceylon at the end of June 1968 at Cey Rs 446.1 million showed an increase of 80.4 million over the June 1967 figure. This apparent improvement was in large measure due to the revaluation of assets consequent to the devaluation of the rupee in 1967. External assets net of Sterling Loan Sinking Funds amounted to Cey Rs 402.3 million at the end of June 1968. The principal additions to reserves in the first half of 1968 apart from earnings were drawings from the International Monetary Fund amounting to approximately Cey Rs 176 million. The major capital repayments were an amount of Cey Rs 57.1 million paid to British banks in settlement of short-term borrowings and a repurchase of Cey Rs 23.8 million from the International Monetary Fund on account of earlier drawings. In view of:

(a) capital repayment due on account of oil compensation;

(b) settlement in sterling of amounts in excess of swing limits under payments agreement;

(c) further repurchase obligations to the IMF;

(d) repayment of long-term capital and interest (which item is becoming increasingly heavier)

there is likely to be continued pressure on Ceylon's external assets.

Along with the measures taken by the Government to adjust the external payments situation, major steps have been taken to increase production of import substitutes, particularly in respect of food; and with this end in view the monetary and fiscal policies of the Government have been appropriately geared to maximizing domestic output in order to limit the pressure on the payments situation. Despite the far-reaching measures adopted to relieve the continued pressure on balance of payments, there is considerable cause for anxiety in view of the magnitude of the impact of external factors on the domestic economic scene. In view of the tight foreign exchange position now facing the country and in view of the need to limit the use of the country's scarce resources, it would be difficult to anticipate further liberalization of the trade and payments regulations in the absence of a substantial improvement in the terms of trade and/or in the size and content of official and private long-term capital, except such rationalization of import policy as is feasible within the Foreign Exchange Entitlement Certificate Scheme.

Table 1

CEYLON'S BALANCE OF PAYMENTS

(Cey Rs million)

	1957	1958	1959	1960	1961	1962	1963	1964	1965	1966	1967
1. Exports (total) f.o.b.	1,669	1,624	1,773	1,796	1,707	1,763	1,708	1,767	1,909	1,674	1,646
2. Imports (total) c.i.f.	1,764	1,713	1,958	2,006	1,794	1,906	1,869	1,960	1,922	2,018	1,997
3. Trade balance:											
(i) of total	- 95		-185	-210	- 87	-143	-161	-193	- 13	-344	-351
(ii) of which commercial transactions	- 45	- 11	- 49	-127	- 5	- 47	- 27	- 39	+128	-119	- 89
4. Net invisibles (including gifts in kind)	-100	- 64	- 23	- 10	- 7	+ 3	- 7	+ 33	+ 72	+ 53	+ 22
5. Balance:											
on current accounts (net of 3(i) and 4)	-195	-153	-208	-220	- 95	-140	-168	-160	+ 59	-290	-329
of which balance on current account on commercial transactions	-127	-119	- 66	- 63	- 48	- 81	- 78	- 82	+136	-132	-117
6. Net long-term capital	- 18	+ 8	+ 32	+ 22	+ 11	+ 39	+ 80	+ 69	+ 58	+137	+160
7. Basic balances (net of 5 and 6)	-213	-145	-176	-198	- 84	-101	- 88	- 92	+117	-153	-169
8. Net short-term capital	- 1	+ 32	---	- 24	+ 93	+ 42	+ 42	+ 33	+ 3	+ 53	+269
9. Errors and omissions	---	- 16	+ 1	+ 29	- 19	+ 31	+ 4	- 8	- 6	- 22	+ 31
10. Change in total external assets (increase +)	-214	-129	-175	-193	- 9	- 28	- 42	- 51	+114	-122	+131
11. Total external assets at end of period	1,062	933	734	541	532	504	462	351	440	318	449
12. Assets (excluding Sterling Loan Sinking Funds)	973	838	655	458	441	407	359	305	408	282	407

Source: Central Bank of Ceylon.

Table 2

EXTERNAL RESOURCES AND THEIR USE

	Cey Rs million			Percentage share		
	1965	1966	1967	1965	1966	1967
A. Resources						
1. Merchandise exports f.o.b.	1,909	1,674	1,646	81	70	69
2. Current invisibles	199	204	198	8	9	8
3. Capital inflow:	141	226	261	6	9	11
of which:						
(a) loans	77	173	212	55	77	81
(b) grants	64	51	46	45	23	18
(c) private capital	-	2	3	-	-	1
4. Short-term liabilities:	109	175	288	5	7	12
of which:						
(a) gross drawings from the International Monetary Funds	109	144	123	100	82	43
(b) increase in bilateral payments agreement balances	-	31	80	-	18	28
(c) borrowings from foreign banks	-	-	57	-	-	20
(d) others	-	-	28	-	-	9
5. Decline in external assets (net of Sterling Loan Sinking Funds)	-	126	-	-	5	-
Total	2,359	2,405	2,393	100	100	100
B. Use						
6. Merchandise imports c.i.f.	1,922	2,018	1,997	81	84	83
of which: aid	142	224	258	7	11	13
7. Current invisibles:	199	213	224	8	9	9
(a) investment income	4	26	34	2	12	15
(b) migrants' transfers	31	32	30	16	15	13
(c) interest payments	22	21	31	11	10	14

Table 2 (cont'd)

	Cey Rs million			Percentage share		
	1965	1966	1967	1965	1966	1967
B. Use (cont'd)						
8. Capital amortization or repatriation:	75	114	71	3	5	3
(a) private	3	8	8	4	7	11
(b) official	16	30	45	21	26	63
(c) repurchase and gold subscription at the International Monetary Fund	56	76	18	75	67	26
9. Short-term liabilities	69	62	-	3	2	-
10. Increase in external assets (net of Sterling Loan Sinking Funds)	103	-	125	5	-	5
11. Balancing item	-9	-2	-24	-	..	..
Total	2,359	2,405	2,393	100	100	100

Table 3

CEYLON'S BALANCE OF PAYMENTS

(Cey Rs million)

	First half 1967	First half 1968[1]
Exports f.o.b.	-813.5	- 885.5
Imports c.i.f.	-997.3	-1,192.3
Trade balance	-183.8	- 306.8
Services	- 4.8	- 8.1
Private transfers	- 11.3	- 11.0
Official transfers	21.0	15.9
Net current invisibles	4.9	- 3.2
Net current account	-178.9	- 310.0
Net long-term loans	59.7	138.2
Net private capital	0.9	- 1.2
Basic balance	-118.3	- 175.0
Financing account		
Short-term liabilities	161.3	176.6
IMF position	106.9	158.0
Central Bank	3.2	- 23.8
Commercial Banks	10.4	10.7
Other	40.8	31.7
Change in external assets	- 46.4	2.4
Errors and omissions	+ 3.4	- 6.0

[1]Provisional.

(Increase -)

Notes: Grants under United States Public Law 480 Counterpart Funds included in official transfers. Other gifts in kind pro-rated. Changes in external assets are mainly in respect of holdings of Central Bank and Commercial Banks.

Source: Central Bank of Ceylon.