

**TARIFFS AND TRADE**Committee on Balance-of-Payments Restrictions

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1989 CONSULTATION WITH SRI LANKA  
UNDER ARTICLE XVIII:12(B)Statement by Sri Lanka under Simplified  
Procedures for Consultations<sup>1</sup>

The following is the statement provided by Sri Lanka for the consultations.

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Balance of Payments for 1988

Sri Lanka's balance-of-payments position for the year 1988 was rather disappointing. The deficit in the merchandise trade account widened by 9 per cent, from SDR 525 million (SL Rs 20,005 million) in 1987 to SDR 574 million (SL Rs 24,512 million) in 1988. The deficit in the services account too widened from SDR 121 million (SL Rs 4,625 million) to SDR 126 million (SL Rs 5,403 million) in 1988. At the same time, the current account deficit expanded by 22 per cent, from SDR 265 million (SL Rs 10,093 million) in the previous year to SDR 324 million (SL Rs 13,841 million) in 1988. The current account deficit to GDP ratio, which is a basic indicator of the degree of weakness of a country's balance-of-payments position, increased from 5.1 per cent in 1987 to 6.2 per cent in 1988. Net non-monetary capital inflow, which is used to finance the current account deficit, fell by 11 per cent in 1988, thus leaving an enlarged overall deficit of SDR 101 million (SL Rs 5,000 million) to be met by drawing down on the external assets of the country.

Export earnings which had recorded an annualized growth of 10 per cent up to October 1988, declined sharply during the last two months of the year largely due to the escalation of civil disturbances. As a result, the rate of growth of exports was restricted to 2 per cent. Industrial exports stagnated recording just 1 per cent growth while gem exports grew by 27 per cent in 1988. The export earnings from tea and rubber increased by 3 per cent and 13 per cent, in SDR terms, respectively. Other agricultural exports recorded an impressive growth of 33 per cent which was entirely due to an increase in the volume exported. In contrast, earnings from coconut exports dropped by 44 per cent owing to 58 per cent fall in the volume of exports.

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<sup>1</sup>Material supplied by the Sri Lankan authorities.

Payment for imports increased by 4 per cent in SDR terms during 1988 as against a decrease of 5 per cent in the previous year. The import outlay on consumer goods and intermediate goods increased by 12 per cent and 4 per cent respectively while investment goods imports declined by 5 per cent during the year. The overall price movements in the international markets were adverse for Sri Lanka during 1988. The export price index rose by 1 per cent in SDR terms while import prices increased by nearly 9 per cent resulting in a deterioration of the terms of trade of Sri Lanka by 7 per cent during 1988.

The deficit in the services account increased from SDR 120 million (SL Rs 4,625 million) in 1987 to SDR 125 million (SL Rs 5,403 million) in 1988. This was largely due to an increased outflow on account of interest payments and the decline in the earnings from tourism.

Interest payments accounted for 39 per cent of total service payments and continued to be the single largest payment item in the services account. Interest payments and other service charges on external debt inclusive of the use of IMF credits rose from SDR 150 million (SL Re 5,721 million) in 1987 to SDR 165 million (SL Rs 7,052 million) in 1988. The increase in interest payments was mainly due to two main reasons namely, a rise in the external debt and an increase in international interest rates. Despite the rise in international interest rates, interest earnings declined in SDR terms due to the weakening of the external assets position of the country in 1988.

The downward trend in tourist receipts which started with the eruption of civil disturbances in 1983, continued during the year. Gross earnings from tourism declined from SDR 55 million (SL Rs 2,107 million) in 1987 to SDR 46 million (SL Rs 1,964 million) or by 16 per cent in 1988. The expenditure on travel abroad, on the other hand, increased marginally in 1988.

The port, transportation and insurance category of the services account showed a positive development in 1988. The surplus in this category rose from SDR 2 million (SL Rs 65 million) in 1987 to SDR 6 million (SL Rs 219 million) in 1988. This larger surplus was attributable to increased receipts from port services and Air Lanka passenger fares and a reduction in foreign payments by Air Lanka. Private remittances, major part of which representing inward remittances by Sri Lankans working abroad, continued to decline for the fourth consecutive year falling by 3 per cent in 1988.

The gross receipts from private transfers amounted to SDR 262 million (SL Rs 11,194 million) in 1988 compared with SDR 270 million (SL Rs 10,324 million) in 1987. The official grants rose marginally from SDR 139 million (SL Rs 5,311 million) in 1987 to SDR 142 million (SL Re 6,077 million) in 1988. While project grants amounting to SDR 94 million (SL Rs 4,006 million) accounted for 66 per cent of the total official transfers, commodity grants accounted for the balance. Thus, the combined transfer receipts from private and official sources declined marginally, in SDR terms, in 1988.

Usually, a significant portion of the deficit on goods and services is met out of the net transfer receipts. However, in 1988, the net transfer receipts were sufficient to meet only 54 per cent of the deficit on goods and services, as compared with 59 per cent in 1987. As a result, a larger current account deficit amounting to SDR 324 million (SL Rs 13,841 million) emerged to be financed out of net non-monetary capital inflows and the use of external assets.

Following the declining trend observed since 1983, net inflow of foreign capital fell by 11 per cent, from SDR 218 million (SL Rs 8,408 million) in 1987 to SDR 193 million (SL Rs 8,232 million) in 1988. The decline was primarily due to a sharp reduction (55 per cent) in net capital flows to the private sector and increased amortization of official loans. Net capital flows to the private sector amounted to SDR 29 million (SL Rs 1,223 million) in 1988. Disbursements of long-term foreign loans to the government on the other hand, increased from SDR 265 million (SL Re 10,162 million) in 1987 to SDR 286 million (SL Rs 12,243 million) in 1988. However, amortization payments by the government also rose by 9 per cent from SDR 112 million (SL Rs 4,261 million) to SDR 122 million (SL Rs 5,234 million), thereby reducing the net resource availability in the form of official capital flows to SDR 164 million (SL Rs 7,009 million) during the year. Altogether, the net capital flows from different sources were sufficient to finance only 60 per cent of the widened current account deficit in 1988, leaving an overall deficit of SDR 101 million (SL Rs 5,000 million) for financing by drawing down on external reserves.

Sri Lanka's external assets position came under heavy pressure in 1988, resulting in a depletion of external assets during the year. The gross external assets at the end of the year was SDR 393 million (SL Rs 17,482 million) as compared with SDR 415 million (SL Rs 18,134 million) at the end of the previous year.

The Sri Lankan rupee, which had been depreciating in nominal terms against all major currencies since 1985, appreciated by 10 per cent against the Indian rupee, 4.3 per cent against the Deutsche mark and 5.2 per cent against the French franc in 1988. However, it continued to depreciate against the United States dollar, the intervention currency, by 6.9 per cent, the pound sterling by 3.2 per cent and the Japanese yen by 5.3 per cent in nominal terms. Against the SDR, the rupee depreciated only by 2.3 per cent reflecting the strength of the United States dollar against the SDR in 1988.

Sri Lanka's total outstanding external debt rose from SDR 3,372 million (SL Rs 144,889 million) at the end of 1987 to SDR 3,679 million (SL Rs 162,548 million) at the end of 1988, or by 9 per cent in SDR terms and 12 per cent in rupee terms. The ratio of total external debt to GDP increased from 65 per cent in 1987 to 70 per cent in 1988.

The total debt service payments increased from SDR 383 million (SL Rs 14,538 million) in 1987 to SDR 399 million (SL Rs 17,018 million) in 1988. This reflects an increase of 4 per cent in total debt service payments in 1988, which was wholly due to a sharp rise in interest

payments. The total debt service payments as a ratio of exports of goods and services increased from 27.7 per cent in 1987 to 28.8 per cent in 1988. The increase in the debt service ratio was attributable to both higher debt service payments and the sluggish growth in exports. The overall debt service payments as a ratio of total current receipts, excluding official transfers, also rose from 23.2 per cent in 1987 to 24.2 per cent in 1988.

#### Prospects for 1989

The balance-of-payments position for 1989 is expected to deteriorate sharply as a result of a worsening in the merchandise trade account and the services accounts. The estimated deficit in the current account excluding official transfers is expected to expand from SDR 454 million in 1988 to SDR 567 million in 1989. Accordingly, the current account deficit as a percentage of GDP would increase from 8.7 per cent in 1988 to a little over 10 per cent in 1989. Although an increase is expected in net non-monetary capital inflows, the overall balance is expected to indicate a deficit of about SDR 150 million.

Earnings from exports are expected to increase by 5 per cent while expenditure on imports would rise by about 7 per cent in 1989. Thus, the resulting trade deficit of SDR 633 million indicates an 11 per cent increase over the previous year. Substantial reduction in the volume of tea exports and a drop in the exports of petroleum products were the main reasons for the relatively slow overall growth in the exports sector. On the imports side, consumer goods imports, particularly rice, sugar and wheat grain are responsible for the increased expenditure.

The services account is expected to record a larger deficit of SDR 155 million in 1989 as against a deficit of SDR 120 million in 1988. This higher deficit is mainly due to a reduction in the earnings from tourism and increased payments on Sri Lankans travelling abroad. Net private transfers are expected to decline from SDR 238 million in 1988 to SDR 223 million in 1989 while net official transfers are estimated at SDR 144 million in 1989 or 6 per cent lower than in 1988.

Inflows of net non-monetary capital are expected to increase from SDR 193 million in 1988 to SDR 279 million in 1989 or by 45 per cent. Net non-monetary short-term capital inflows to the private sector is expected to increase from SDR 10 million in 1988 to SDR 91 million in 1989 while government long-term net non-monetary capital inflows are estimated to increase from SDR 190 million in 1988 to SDR 201 million in 1989.

Debt service payments in respect of both private and public sector loans including IMF transactions are estimated to decline from SDR 413 million to SDR 384 million. The debt service ratio, as a result, would decline from 29 per cent in 1988 to 27 per cent in 1989. The debt service payments as a ratio of total receipts from goods, services and private transfers is expected to fall from 25 per cent in 1988 to 23 per cent in 1989.

TABLE 1

Balance of Payments 1987-1988

Item	SDR million		Rupees million	
	1987 <sup>a</sup>	1988	1987 <sup>a</sup>	1988
1. Trade balance	-525	574	-20,005	-24,512
Exports	1,077	1,093	41,097	46,764
Imports	1,602	1,667	61,102	71,276
2. Services, net	-121	-126	-4,625	-5,403
Receipts	307	293	11,721	12,524
Payments	428	419	16,346	17,927
3. Goods and services, net	-646	-700	-24,630	-29,915
4. Transfers, net	381	376	14,537	16,074
Private	242	234	9,226	9,998
Official	139	142	5,311	6,076
5. Current account balance (3+4)	-265	-324	-10,093	-13,841
6. Non-monetary capital, net	218	193	8,408	8,232
Direct investment	45	41	1,727	1,732
Private long-term, net	-10	22	437	-947
Private short-term, net	30	10	1,217	438
Government, long-term, net	153	164	5,901	7,009
Inflows	265	286	10,162	12,243
Outflows	112	122	4,261	5,234
7. Valuation adjustments	-	-	1,841	7
8. SDR allocations	-	-	-	-
9. Errors and omissions	-25	30	-1,957	603
10. Overall balance	-72	-101	-1,801	-5,000
11. Monetary movements	72	101	1,801	5,000
Exchange rate SL Rs/SDR			38.10	42.76
Ratios to GDP in percentages				
Trade account			-10.17	-11.01
Current account			-5.12	-6.21
Current account without grants			-7.81	-8.94

<sup>a</sup> Revised

Note: All transactions in the Monetary Sector are converted at end of the year exchange rates.

Source: Central Bank of Sri Lanka