

GENERAL AGREEMENT ON TARIFFS AND TRADE

RESTRICTED

BOP/W/87
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Limited Distribution

Committee on Balance-of-Payments Restrictions

1985 CONSULTATION WITH SRI LANKA
(SIMPLIFIED PROCEDURES)

Background Paper by the Secretariat

1. This paper has been prepared in accordance with Paragraph 7 of the Declaration on Trade Measures Taken for Balance-of-Payments Purposes (BISD 26S/205) to assist the Committee in taking the decision referred to in paragraph 8 of the Declaration. It updates the paper prepared for the 1983 consultation (BOP/W/72).

I Sri Lanka's previous consultations

2. The last full consultation with Sri Lanka took place on 22 June 1971. At that consultation, the Committee recognised that Sri Lanka's then existing balance-of-payments difficulties warranted the use of quantitative restrictions on imports. The Committee urged Sri Lanka to consider additional measures to increase foreign exchange earnings, particularly through promotion and diversification of exports, and expressed the hope that the improvement in the balance-of-trade then apparent would continue, so as to enable some easing of the stringent restrictions placed on imports essential for the further development of the economy (BOP/R/58, paragraph 27).

3. Subsequently, consultations under simplified procedures were held in 1973, 1975, 1977, 1979, 1981, and 1983.

II. Sri Lanka's trade policies and main changes since the last consultation

4. Since 1977, the government of Sri Lanka has pursued an economic policy which, inter alia, has reduced administrative controls, cut back previous trade and payments restrictions, and begun a reform of tariff policy. Although the country is still heavily dependent on the exports of its traditional crops of tea, rubber and coconut products, serious attempts are being made to increase exports of "non-traditional" products; some significant headway has already been made in the areas of garments, shellfish, wood articles, gems and certain chemicals.

5. Generally, imports may be made without prior licensing. However, specified items subject to import licensing include rice, infant milk food, milk powder, onions, drugs, medicaments and narcotics, disinfectants, insecticides, fungicides and herbicides, yarn of man-made fibres, slag, ash and residues from metal manufacturing, concrete blocks encasing industrial

waste, retreaded or worn tyres, marine engines, newsprint, colour photocopies, and motor vehicles, for which licences are issued on a "no-exchange" basis and for vehicles less than three years old. In addition, a number of products including dried chillies, potatoes, refined petroleum products, certain chemicals and explosives, caustic soda, hessian and consumer utility textiles and used clothing remain reserved for import by government departments or state corporations. Prior approval is also required for imports of certain types of machinery for foreign or local investment, of a value over SLRs 700,000 per consignment.

6. Since the last consultation, control of imports has generally been effected through restrictive credit policy, rather than by direct controls. In particular, private sector credit was subject to quantitative and other restrictions, leading to a reduction in its growth from 34 percent in 1983 to 14 per cent in 1984. Imports of consumer goods fell consequently; the slow growth of private investment in 1983 and 1984 also affected imports of capital goods.

7. A first stage of import tariff reform undertaken in November 1984, following a comprehensive review of the tariff structure by the Presidential Tariff Commission, led to a general revision of the structure of effective protection and a nominal tariff structure generally up to a maximum of 60 to 75 per cent. A number of consumer and intermediate products previously subject to low tariffs up to 7.5 per cent, including medicines, books, infant foods, chemicals, fertilizers and seeds, have been exempted from duty, while tariffs on iron and steel, machinery, motor vehicles and agricultural materials have generally been reduced substantially; machinery for firms exporting more than 50 per cent of output was exempted from duty. Higher tariffs were introduced on products which are competitive with local industry or agriculture, including full cream milk powder, rice, sugar, and sanitaryware.

8. The number of items subject to export licensing has been greatly reduced over the period since 1977. The 20 items now subject to such licensing (mainly natural resource products and pharmaceuticals) are shown in Annex B of the Sri Lanka statement (BOP/251). Export taxes on traditional plantation exports were reduced in the 1985 budget with a view to reducing obstacles to increased production and, in the case of rubber, compensating for declining international prices.

III. Recent trends in Sri Lanka's economy and foreign trade

9. In 1983 and 1984, overall economic growth, as expressed by estimates of real GDP, remained at around 5 per cent, similar to that of 1982 but somewhat lower than the average registered in the period since 1977. Preliminary estimates suggest that the growth rate may have increased slightly in 1984. Growth in 1984 was largely due to the robust performance of Sri Lanka's traditionally dominant export product, tea, but, unlike in 1983, manufactures (particularly clothing for export) contributed strongly to the growth rate with an overall output increase of some 10 per cent, aided by increased domestic production of petroleum products and electricity. Growth in 1984 was, however, constrained by the weaker performance of non-tea agriculture,

particularly in rice paddy and coconuts, by sluggish construction activity and falling tourist receipts. Domestic consumption, which had increased at 5.5 per cent in 1983, is estimated to have grown at less than 1 per cent in 1984. Consumer price inflation (as measured by the Central Bank cost-of-living index) which was around 11 per cent in 1982 and 1983, increased to 17 per cent in 1984. The value of the Sri Lanka rupee against the United States dollar, its intervention currency, declined by 5 per cent during 1984, less rapidly than in 1983; this was, however, insufficient to prevent the rupee from appreciating both in nominal effective and real effective terms as the dollar's international value increased.

10. After a sluggish performance in 1983, export earnings increased by 38 per cent in United States dollar terms in 1984, to reach almost \$1.5 billion, about half of the expansion stemming from increased volume. Sri Lanka's major foreign exchange earner, tea, accounted for two thirds of the total increases in exports. The bumper crop allowed a 29 per cent rise in the quantity of tea exported which, combined with booming prices, pushed up tea exports to a record \$0.6 billion, about three-quarters above the 1983 level. Other agricultural exports, though also benefiting from higher unit values, did not do as well in 1984: while rubber exports stagnated in volume and earnings were up 7 per cent (to over \$130 million), value increased - if any - were only marginal for exports of coconut products and of most minor agricultural commodities because of sharply reduced volumes. Though still relatively small, exports of shrimps and of rubber manufactures achieved above-average growth in 1984. More importantly, sales of clothing increased 47 per cent and their share in total exports rose to 20 per cent.

11. The total import bill fell to below \$1.9 billion in 1984, a decline of 3-4 per cent from the previous year. However, import volume was 3 per cent up over the very high level reached in 1983, when volume had increased by 20 per cent. The value of food imports, which had been among the fastest-growing items in 1983, fell substantially in 1984 (despite higher wheat imports), mainly as a result of plummeting international sugar prices and a strong reduction in sugar and rice import needs. In value terms, significant declines were also recorded for imports of consumer manufactures, petroleum and investment goods. Fertilizers were among the few items whose imports increased in 1984.

12. In 1984, Sri Lanka's trade deficit in dollar terms was the smallest since 1978 (around \$400 million f.o.b./c.i.f. or some \$240 million f.o.b./f.o.b.), reduced from some \$870 million (f.o.b./c.i.f.) in 1983. Although net receipts from tourism in 1983 and 1984 declined substantially from their 1982 level, and remittances from nationals working abroad grew considerably more slowly than in the period 1980-82, the current account was virtually in balance in 1984 compared to a deficit varying between \$450 million and \$650 million since 1980. As a result of the substantial surplus in the overall balance of payments, Sri Lanka's international reserves (excluding gold) increased to some \$510 million by the end of 1984, almost equal to the record 1979 level.