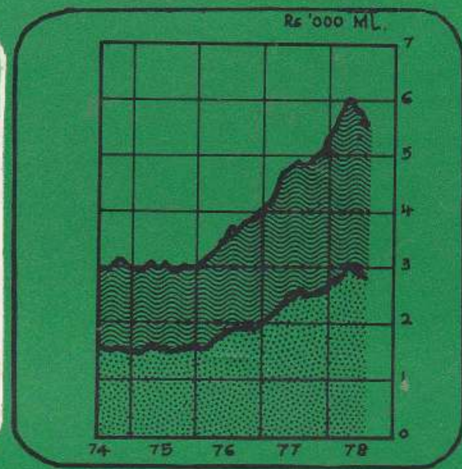
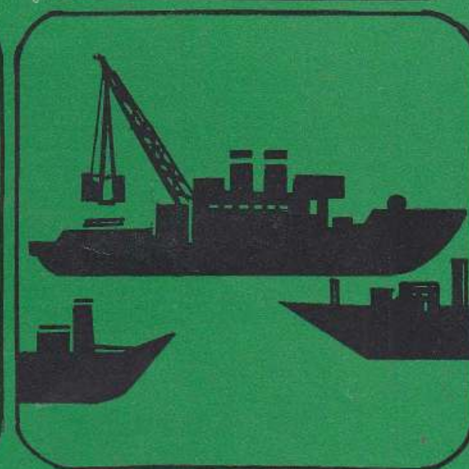
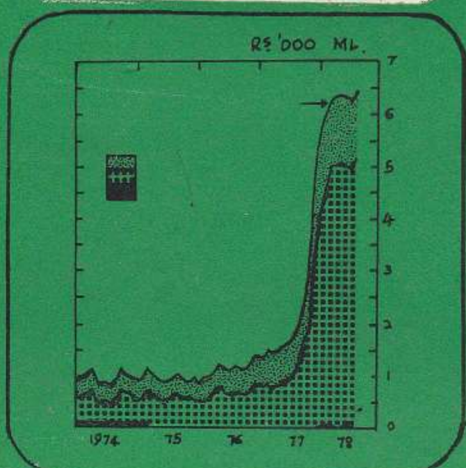
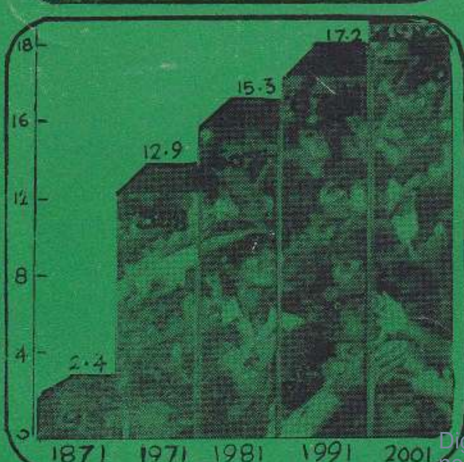
ECONOMIC REVIEW

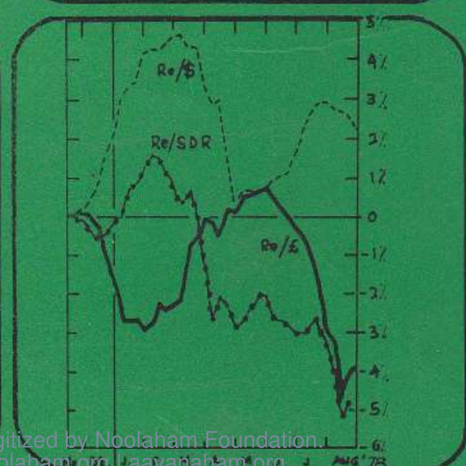
July/Aug 1978











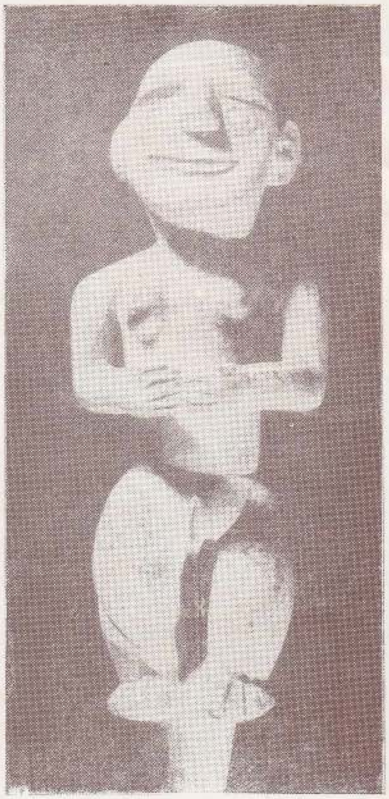
Sri Lanka's Economy

A People's Bank Publication

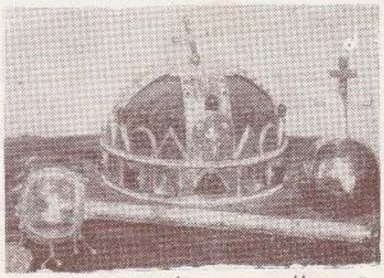
THE ANTIQUES DRAIN

Countries deprived of priceless cultural treasures now seek their return to the homeland

Down the centuries countless works of art and artifacts of all kinds have been carried away from their homeland. The flow of such priceless property has almost always been in one direction only, from the poor to the rich countries. A number of countries with outstanding artistic gifts have been deprived in this way of their entire cultural heritage. The richer their traditions the more their artifacts have tended to flow abroad. This explains why many countries are now feeling frustration and resentment — and are demanding the restitution of their works of art. As UNESCO's Director General has pointed out in a recent appeal (see page 17) art is for the whole world, but people who have been deprived of their cultural heritage have the right to demand the return of the objects that best represent their culture. Already some of these items (as illustrated on this page) have made the long voyage home. More often, however, it has been found that when one country approached another with a formal request for the restitution of a work of art taken away in unhappy circumstances the other country would listen politely and then regret that it is not in a position to take any action.



This chalk figure from New Ireland in the Bismarck Archipelago (Pacific Ocean) is one of a number of items returned in 1977 to the Papua New Guinea National Museum by the Australian Museum, Sydney. It was originally acquired by the Australian Museum by purchase.



The Hungarian coronation regalia have returned home once more. The crown was given to St. Stephen the first King of Hungary, in the year 1001 by Pope Sylvester II; the sceptre and the orb date from the 12th and 14th centuries respectively. Several times lost and even stolen during the centuries, these precious objects were stored at Fort Knox, Kentucky, after the Second World War. Following an agreement between the United States and Hungarian Governments the regalia were returned to Budapest early in 1978.

This pre-Columbian ceramic, produced sometime between 800 and 1200 A.D., was discovered in a tomb at Sitio Conte in Cocle province, northern Panama. The Peabody Museum at Harvard University (U.S.A.), has returned it to Panama under a ten-year renewable loan.

Already some items have made the long voyage home, like this 13th century statute of the Buddhist goddess Prajnaparamita from East Java which was returned, in April 1978, to the Museum Pusat, in Jakarta, Indonesia, by the Rijksmuseum voor Volkenkunde, Leyden, the Netherlands.

Detail from a stele dating from the late classical period (600-900 AD) of Mayan culture. This stele, which stands 240 cm high, was originally discovered at the ancient ruins of Piedras Negras, in north-western Guatemala. The stele, which was acquired by a United States Museum, was returned to the Government of Gpatemala in 1970.

ECONOMIC REVIEW

Volume 4 Numbers 4 & 5 July/August 1978

Published by the People's Bank,
Research Department,
Head Office,
Sir Chittampalam A. Gardinar Mawatha,
Colombo 2
Sri Lanka.

CONTENTS

COLUMNS

SPECIAL REPORT

FEATURES

Readers Please Note

We have combined two issues (July and August 1978) in order to catch up on our backlog in printing which had arisen through circumstances beyond our control. We assure all our subscribers, however, that the validity of their annual subscriptions would extend over 12 seperate issues.

NEXT ISSUE

- The Mahaweli Project — a discussion of current plans and problems and ways of achieving optimum economic and social benefits from Sri Lanka's biggest ever development project.
- Land Consolidation — a strategy in dry zone purana villages.
- Rural Banking in Sri Lanka — its beginnings, growth and significance.

COVER *A composite view of the Sri Lankan economy as seen by photographic artist Palitha Kannangara.*

THE ECONOMIC REVIEW is intended to promote knowledge of and interest in the economy and economic development process by a many sided presentation of views & reportage, facts and debate.

THE ECONOMIC REVIEW is a community service project of the People's Bank. Its contents, however, are the result of editorial considerations only and do not necessarily reflect Bank policies or the official viewpoint. Signed feature articles also are the personal views of the authors and do not represent the institutions to which they are attached. Similar contributions as well as comments and viewpoints are welcome.

THE ECONOMIC REVIEW is published monthly and is available both on subscription and on direct sale.

DIARY OF EVENTS

June

1 The government imposed a general ban on the import of all luxury motor cars.

Radio licence fees were increased to Rs. 25/- for the first broadcasting receiving set and Rs. 12/50 for each additional set.

3 A large West German multinational manufacturer of elasticated rubber extruded thread will be setting up a plant in the Katunayake Export Processing Zone in collaboration with Sri Lanka entrepreneurs, it was announced in the press. This is the second project to be approved for setting up in the Export Processing Zone, the first being the project of a Hongkong ready made garments manufacturer.

5 The Inland Revenue (Amendment) Bill containing incentives and reliefs for several areas of investment in the Export Processing Zone has been gazetted, according to a press announcement which carried the details.

8 A Free Trade Zone is to be set up 35 miles from Bangkok as part of a long term plan to promote exports from Thailand, according to the London *Financial Times*. The World Bank estimates that goods from this FTZ and the surrounding 400 acre domestic industrial estate should be worth about $ 200 million annually.

14 The World Food Council concluded a three day session in Mexico City sending out a call to all governments to allocate part of the resources freed by disarmament especially for food production and to combat widespread hunger and malnutrition.

16 The governing council of the United Nations Development Programme (UNDP) meeting in Geneva approved aid programmes for a total of $ 322.5 million in assistance to a dozen countries in Asia, Africa, Latin America and the Middle East.

20 A report on the world economic outlook issued by UNCTAD warned that the growth rate of developing countries was falling far short of the 6 per cent target established for the second development decade. The rate was expected to fall further to 4.6 per cent in 1978/79 and this reflected the effects of a general slow down in economic activity, stated the report.

22 The Board of governors of the United Nations Special Fund (set up in 1974) to aid the countries most seriously affected by the economic situation after the fuel price hikes decided that the Fund's activities should be suspended temporarily, due to a lack of contributions.

China is producing a new kind of chemical rubber tree stimulant that raises latex output by 10—30 per cent when the stimulant is injected into old rubber trees, stated a *Hsinhua* Bulletin.

23 Iran informed the United Nations Secretary General that $ 7 million was being diverted from its national defence budget to support the programmes of the International Year of the Child.

26 Work on the Rs. 569 million Lunugamvehera (Kirindi Oya) Irrigation and Settlement Project, which will help to irrigate 2,750 acres of irrigated land and 11,127 acres of existing fields in the Hambantota district, was inaugurated.

29 The Central Bank of Ceylon directed commercial banks not to increase the total of their advances to government corporations and statutory boards (other than financial and lending institutions) over the level of such advances outstanding as at June 29, 1978. The ceiling which is applicable to loans, overdrafts and local and import bills financed, was introduced with a view to restraining the expansion in money supply.

July

1 New bus fares, entailing a 10 cts. increase for every one rupee unit or part thereof in the prevailing fares, came into effect.

2 The National Savings Bank announced a new scheme to pay monthly interest on new Fixed Deposits over Rs. 5,000/- at the rate of 18.4 percent per annum.

3 In order to contain the fertilizer subsidy within limits, the Government announced a reduction in the subsidy from 75 percent to 50 percent in the case of the private sector, and from 50 percent to 25 percent to state-owned land management institutions.

7 An adhoc inter-governmental Working Group on the Problems of Corrupt Practices recommended that the U.N. Economic and Social Council convene a diplomatic conference to conclude an agreement against illicit payments in connection with international commercial transactions.

11 The Rs. 7 million Nilwala Ganga Drainage and Reclamation Scheme which will help to improve drainage of about 3,775 acres in the area between the Gin Ganga and Nilwala Ganga was inaugurated.

12 Two Agreements were signed between the Government of Sri Lanka and the International Development Association (IDA) for U.S. $ 21 million and U.S. $ 4.5 million for financing the proposed Tree Crop (Tea) Rehabilitation Project and the Tree Crop (Tea) Diversification Project, respectively.

13 The Central Bank relaxed marginally its ceiling imposed on June 29 on bank advances granted to Government Corporations and Statutory Boards by permitting a 5 percent increase in the overall ceiling.

31 The Paddy Marketing Board had purchased 23.5 million bushels of paddy from farmers, at Rs. 40/- per bushel, between January and July this year, according to figures compiled by the Paddy Marketing Board. On this basis the paddy farmers would have earned a total of Rs. 940 million from the PMB during the first seven months of this year.

SRI LANKA'S ECONOMY

A half yearly review

The economy in the first half of 1978 witnessed a process of adjustment to the package of economic reforms (Rupee devaluation and the liberal economic policy) introduced in the Budget of November 1977. After nearly two decades of economic controls and scarcities of imported goods, the economy has been opened to receive a liberal flow of imported goods, restrictions placed on private sector economic activity had been removed, and incentives in the form of a Free Trade Zone offered to attract local and foreign investment into export-oriented industries. The package of Rupee devaluation and the import liberalisation while removing scarcities in the economy by raising supplies both through higher imports and higher capacity utilisation in industry, required the evolution of a new (higher) set of price and wage levels as a part of the new economic picture that emerged. By mid 1978 there were signs that the economy was gradually approaching such a new price level with the rate of price increases slowing down in relation to the early months of the year. The prices that recorded the highest increases were those of imported goods and intermediates (which also have a high import content).

No estimates are available on the growth of overall production in this half year, but the official estimates project a growth rate of about 5.7 percent in the GNP for the year as a whole. If realized, this would be the highest annual growth recorded for the last decade. The estimated population in mid-1978 was about 14.2 million signifying an increase of about 1.7 percent over the level a year ago.

In contrast to 1977 when over half the increase in the GNP came from the agricultural sector, the manufacturing, construction and service sectors are expected to be the major contributors to the increase in the GNP this year. While the output of the agricultural sector is expected to increase by 5.7 per cent in 1978 as against 7.2 per cent in 1977, the corresponding increase in the manufacturing sector is expected to be 5.6 per cent in 1978 against an increase of only 1.1 per cent in 1977. The output of the construction sector is estimated to increase by 9.5 per cent in 1978, the trade and transport sectors by 5 per cent and the banking and finance sector by 21 per cent.

According to the provisional index of agricultural production computed by the *Economic Review* the overall production of principal agricultural crops (tea, rubber, coconut, and paddy) registered an increase of 7 percent over the first half of last year, and a 20 percent increase over the average level of 1975-76. This increase was largely a result of the substantial increase recorded in paddy production, the Maha harvest having reached a record level variously estimated at 59 million and 62 million bushels. The continued increase in paddy production since 1977 was a significant event carrying important economic consequences. For the first time it enabled the realisation of a substantial saving in the country's rice import bill and moreover, it also served to raise rural incomes in the paddy growing rural sector, thereby expanding the rural markets for what had been mainly urban consumer goods.

In the plantation sector only rubber production registered a sizeable increase. Coconut production, though showing an improvement over the 1977 slump, continued to remain below the past average levels, and tea failed to show an improvement over the last year's performance.

The production of many public sector industries recorded a distinct improvement over the half-yearly average levels of 1967-77. Sizeable production increases were recorded in cement, steel, ceramics, tyres, graphite and electricity. The greater availability of imported inputs enabled many private sector industries to raise their production levels and capacity utilisation. However, liberal import flows and the higher cost of imported raw materials created a slump in the local textile industry and a reduced level of activity also characterised such small-scale industries as safety matches. There was also a decline in gem production (as reflected in exports).

There was an acceleration in construction activity compared to the previous years. The improved supply and availability of building materials and the initiation of large scale development projects by the government were contributory factors. Economic activity in the transport sector was boosted by the substantial increase in the imports of vehicles and transport equipment. The higher level of activity evidenced in both public and private sectors led to the generation of new employment, though the exact number of new jobs created is not known.

Under the new exchange rate system introduced in November 1977, the exchange rates of the Rupee were daily announced by the Central Bank presumably on the basis of market developments. During this half-year, while the Rupee-US Dollar rate remained relatively stable, there was a depreciation of the Rupee against the Yen by nearly 15 percent and against the Mark by nearly 6 percent.

When measured in SDR terms, while export earnings of the first half of this year remained virtually constant, the import expenditure showed an increase of 4 percent. The ability of the country to limit the increase in the overall import bill despite import liberalisation was largely a result of the substantial savings realised on rice imports which declined by over 50 percent. The highest increases in imports were recorded by vehicles, transport equipment machinery and mechanical/electrical equipment, and the share of these imports in the overall import bill shot up to over 22 percent. There was also a sharp increase in the expenditure incurred by Sri Lankans on foreign travel. An increase of 380 percent has been registered in travel expenditure in the first half of this year when compared with the corresponding periods last year.

Despite the increase in the balance of trade deficit, the external assets registered an increase and the level of external assets at the end of June was almost equal to the total import bill of the first six months of the year. The commodity terms of trade of the first half of 1978 averaged 93.3 (1967 100) which was an improvement of about 15 percent over the average level of 1977, (which was 81).

PLANTATION PRODUCTION

The overall plantation production (as reflected in our index) showed a modest gain of 3 percent over the first half of 1977 but the production level was below the average level of 1975-76. While rubber production showed a distinct improvement over that of last year coconut production continued to remain below normal levels, with tea production showing a decline. Total export earnings from plantation produce during Jan.-June 1978 amounted to SDR 238 million which represented a decline of SDR 10 million or 4 percent when compared with the first half of 1977. As in the case of last year, export earnings from plantation crops continued to provide 74 percent of the total export income of the country.

The failure of the plantation output (in particular tea production) to show an improvement should be viewed against the background of the dislocations in management that resulted from the change-over of ownership from private to state hands under the Land Reform of 1975. There was a deliberate neglect of productivity by the former private owners in view of the Land Reform and a substantial decline in the quality of management characterised many organisations such as Cooperatives which managed a part of the plantations after the state take-over. The seriousness of such a management breakdown can be realised when it is noted that after the Land Reform, about two-thirds of the tea lands, nearly one-third of the rubber lands, and about one-tenth of the coconut lands are being owned and managed by the state. Since late last year, some significant steps have been taken by the government to improve the management of plantations. The institutional uncertainties that had surrounded the state-owned plantations have been removed by bringing the management of all estates under the umbrella of a single Ministry — the Ministry of Plantation Industries. Moreover, cooperative institutions which were ill-equipped and inexperienced to handle plantation management had been done away with, and the management of all state-owned plantations have been entrusted to two leading state agencies namely the State Plantations Corporation and the Janata Estate Development Board. Besides, some of the past management practices such as the visiting agents system and the role of superintendents have been restored with certain modifications.

A notable advance is also seen in the plantation sector. The sales of fertilizer to the plantations during Jan.-June 1978 amounted to 130,000 tons which was almost equal to the annual average fertilizer use in this sector during 1975-77. These developments and/or improvements in management and the increased fertilizer use, augur well for the future and should improve the production prospects in the plantation sector in the medium term. The production and export performance of each plantation crop during the first half of 1978 is briefly reviewed in the following section.

TABLE I INDICES OF AGRICULTURAL PRODUCTION — PRINCIPAL CROPS *

Crops	1973-76	1977	1978
Tea	100	103	93
Rubber	100	100.6	111
Coconut	100	74.2	87.6
Plantation Crops	100	95	90
Paddy	100	148	160
All Principal Crops	100	117	130

* *Computed by Economic Review* (provisional).

TABLE 2 TEA: PRODUCTION AND EXPORTS

	Production (Million kg)	Colombo Auction Sales Vol. (m.kg)	Colombo Auction Average Price (Rs)	Exports Vol. m.kg	Exports Value Rs. mn.	Exports Unit value per Kilo
1975-76						
First Half (avg.)	110.7	94.7	12.26	99.2	832.8	8.40
Second Half (avg.)	94.5	82.7	18.73	107.6	1082.5	10.06
1977						
First Half	114.0	95.9	14.67	92.7	1648.4	18.70
Second Half	94.6	90.8	18.00	92.9	1951.3	21.00
1978						
First Quarter	49.4	48.2	8.66	39.3	1261.6	32.26
Second Quarter	60.1	45.1	7.88	51.4	1786.7	34.94
Second Half	109.5	93.3	14.50	90.6	3048.5	33.64

Tea

Tea production in the first half of 1978 at 109.5 kg was lower than in the corresponding period of 1977 by 4.5 kg or nearly 4 percent. This decline was mainly reflected in the production of high and medium grown teas. The low growns have shown a modest increase in production. The quantity sold at the Colombo auctions also showed a decline of nearly 3 million kg. and the quantity exported declined by 2 million kg. The average auction price too declined when compared with the first half of 1977. The monthly average auction price having reached a peak level of s. 18.31 per kilo in February declined in the subsequent months. The average price in June stood at Rs. 11.08 which reflected a decline of 39 percent from the peak level recorded in February. On the other hand, the average export price (f.o.b.) showed an improvement throughout the first six months of this year rising from Rs. 27 per kg. in December 1977 to Rs. 38.38 per kg in June 1978, showing an increase of 35 percent. While in Rupee terms the average export price for tea in the first half of this year recorded an increase of about 180 percent over the corresponding period last year, in SDR terms there was a decline of about 5 percent. Thus, the higher rupee value was largely a reflection of the devaluation of the Rupee rather than an upward trend in prices in real terms.

Rubber

Unlike tea, the production of rubber in he firs half of 1978 showed a distinc improvemen when compared wih he corresponding periods of 1975-77. Production at 79.4 kilos represented an improvement of 11 percent over the corresponding figure of 1977, and the export volume registered an increase of nearly 5 million kilos or 8 percent. The export earnings in Rupee terms more than doubled but in SDR terms there was only a marginal increase of SDR 1 million. (SDR 60.3 million in 1978 compared with SDR 59.3 million in 1977). Rubber exports accounted for 18.6 percent of the total export earnings as against 17.5 percent last year. The average export value per ton at Rs. 13.75 represented a more than 100 percent increase compared to the level of the corresponding period last year, but there was a slight decline when measured in SDR units.

TABLE 3 RUBBER: PRODUCTION AND EXPORTS

	Production (Mn. Kilos)	Local Price RSS I (Rs. per kilo)	Local Price Crepe No. 1 (Rs. per kilo)	Volume Mn. Kilos	Total Value (Rs. millions)	Average Value Rs. per kilo
1975-76						
1st Half (avg)	75.4			78.2	366.9	4.56
2nd Half (avg)	80.1			70.6	415.2	5.88
1977						
1st Half	71.8	4.25	5.14	78.9	525.0	6.99
2nd Half	75.5	4.79	5.13	55.7	397.0	7.13
1978						
1st Quarter	38.2	5.84	6.06	42.1	590.3	13.92
2nd Quarter	41.2	6.66	6.88	41.6	560.3	13.54
1st Half	79.4	6.20	6.47	83.7	1150.6	13.75

Coconut

Coconut production showed a recovery from the worst ever slump recorded in 1977 but the production level continued to remain considerably below the past average level. The estimated production in the first half of 1978 was 1,004 million coconuts compared with an average production of 1,146 million nuts in the corresponding periods of 1975-76. (Both coconut oil and desiccated coconut production remained considerably below the average level of 1975-76. Though the export volume recovered relative to the 1977 level it was only about half the average level of of 1975-76). Coconut production in 1978 is now estimated to reach 2,250 million nuts as against an annual average of 2,458 million nuts in 1975-76.

Total earnings on the export of all coconut products during the first half of 1978 amounted to Rs. 516.2 million as compared to Rs. 200 million for the same period last

TABLE 4 COCONUT: PRODUCTION AND EXPORTS

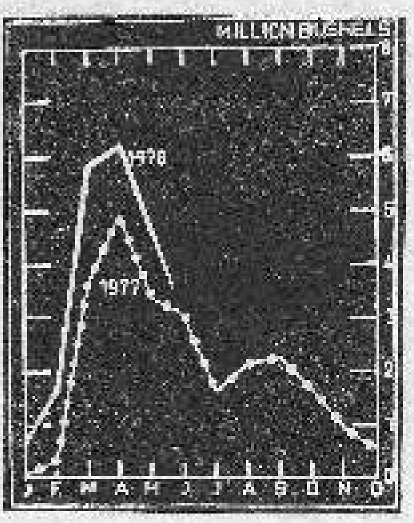
	Production Coconuts (mn. nuts)	Production Oil (tons)	Production D.C. (tons)	Exports Total Volume (mn. nuts) equivalents	Exports Total Value (Rs. mn)	Exports Unit Value per Rs.
First Half of:						
1975	1,184	20,342	31,252	336	188	0.52
1976	1,107	21,407	45,547	380	140	0.37
1977	851	11,324	18,576	107	126	1.18
1978	1,004	14,673	22,449	198	360	1.81

* Provisional estimates.

year. This reflects an increase, in rupee terms of about 158 percent in 1978 over that of 1977. The major share of these earnings came from D.C. exports which contributed about Rs. 230 million or 45 percent of the total earnings. Fibre exports brought in about Rs. 126 million or 25 percent and coconut oil exports around Rs. 123 million or 24 percent of the total.

Paddy Production

Among the principal agricultural crops, the most significant production increase was in paddy. The estimated Maha production at 61.6



the Guaranteed Price Scheme
Paddy purchases in 1977-78 under

million bushels represented an increase of 12 percent over the Maha of 1977 and 46 percent over the Maha of 1976. This higher production was largely a result of the higher harvested acreage estimated at 1.39 million acres, an increase of 11 percent over the previous Maha crop. The increased paddy production led to a sharp increase of 42 percent in the purchases of paddy under the G.P.S. The purchase volume at 21.8 million bushels was the highest so far recorded for a Maha season in recent history. The high GPS purchases of paddy, the decline in the Food Commissioner's requirements of rice to be issued under the ration scheme (as a result of the withdrawal of rice ration books from about half the population), and the availability of high stocks of imported rice (as shown by the high level of imports in 1977) led to a substantial drop in the rice imports. The import volume in the first half of 1978 (about 100,000 tons) was only about one third of the half yearly imports of rice during the year 1976-77. The higher paddy production also served to raise rural incomes in the surplus paddy producing areas (notably in the Dry Zone districts) thereby expanding the market for urban goods in these areas. This high production should continue into the Yala season, with production estimated at over 30 million bushels, as against an annual average of about 23 million bushels for the last three years.

TABLE 5 PADDY PRODUCTION & RICE IMPORTS

	Maha Crop (million bushels)	Gross Harvested Area (Million acres)	GPS Purchases (million bushels)	Rice Imports (tons)
First Half of:				
1975	34.5	0.88	7.9	323,900
1976	42.3	1.05	10.2	244,800
1977	54.9	1.25	15.4	385,205
1978	61.6*	1.39	21.8	100,130

* *Also estimated as 59.08 million bushels*

TABLE 6 PRODUCTION OF SELECTED INDUSTRIES

	1976 Full Year	1977 Full Year	1978 First Half	% Change in 1978 over 1976—77 average half-yearly level
1. Electricity (mn. kwt)	1183	1217	672	+ 14.2
2. Petroleum				
(a) Petrol (tons)	99306	109348	57508	+ 13.5
(b) Furnace oil (tons)	513673	545349	299399	+ 13.1
(c) Diesel oil (tons)	364364	368438	201621	+ 10.0
3. Steel (tons)	26205	24808	18867	+ 43.8
4. Cement (tons)	438449	376641	290706	+ 45.3
5. Chemicals (tons) (caustic soda)	1546	1516	854	+ 11.5
6. Tyres (number)	180887	155474	113126	+ 41.2
7. Paper (tons)	17276	19429	16053	— 9.6
8. Ceramics (tons) (Crockery)	2383	3909	1811	— 37.6
9. Graphite (tons)	8007	3723	7031	20.2
10. Ilmenite (tons)	54952	34092	10710	— 51.9
11. Salt (tons)	134749	47080	40732	3.5
12. Sugar (tons)	22513	22316	11431	2.4
13. Hardware (number) (mammoties)	199476	384720	140947	— 2.7
14. Textiles (million metres)	107.8	106.2	51.70	— 2.3
15. Processed Milk (pints)	23202	25210	15019	19.2
16. Plywood (sq. ft.)	47582	38612	10056	— 71.3
17. Gems (export value) SDR million	29.5	24.2	12.6	— 7.4

INDUSTRIAL PRODUCTION

In general, the industrial sector showed a higher production performance compared with the corresponding periods in the previous two years. In the public sector significant production increases were recorded by electricity, petroleum, cement, steel, ceramics, graphite, chemicals (caustic soda), and tyres. The enhanced availability of raw materials and other inputs as a result of the import liberalisation, and the relative industrial peace that characterised this period were among the factors contributing to the higher level of industrial production. There were, however, industries which recorded production declines in the face of the import liberalisation. The most important among them were the textiles and such small scale industries as toys, glassware, safety matches all of which had to face competition from better quality imported products and assembly industries such as radios, fans and electrical items. There was a tendency for some of these manufacturers to move towards trade or direct import and distribution of the items they previously assembled locally.

The textile industry, particularly the handlooms, suffered adversely as a result of import liberalisation and the institutional changes in the yarn import and distribution policy. While the price of yarn almost doubled, the final output could not be marketed owing to the competition from the better quality foreign products. On the otherhand, the export-oriented garments industry continued to record production increases. During the first half of 1978, nearly 4 million pieces of garments valued at Rs 156 million were exported as against 5.2 million pieces valued at Rs. 94 for the whole of 1977. Among the projects approved for the Free Trade Zone are several garment manufacturing projects which should raise the garment export capacity of the country sharply in the coming year.

The production in the gem mining industry (as reflected in gem exports) showed no increase during the period under review. Although the value of gem exports in rupee terms (Rs. 238 million) rose by 35 percent over the first half of last year, when measured in SDR terms, there was a decline of about 13 percent.

CONSTRUCTION

The implementation of a number of large scale development projects (accelerated Mahaweli project, Free Trade Zone, Greater Colombo development scheme and the five-year housing construction programme) and the increased economic activity in the private sector, led to an expansion in construction activity. The increased availabilities of key building materials such as cement (a 45 percent increase in production) was also an important factor in the higher level of construction activity. However, the prices of most building materials such as sand, timber, metal and bricks registered sizeable increases which raised the cost of construction; in particular the timber shortage became a constraint on construction activity and this compelled the Government to permit the import of timber for more important projects planned for construction. Moreover, the large scale outflow of construction workers to Middle-eastern countries caused shortages of carpenters, masons and other skilled personnel and the local wages for such skills have recorded substantial increases in recent months. The construction activity in the public sector, though continued at a higher level than in 1977, showed a shortfall in relation to the targets. The average performance has been about 74 percent of the construction targets set for the first half 1978, as seen in table 7 below.

TABLE 7 CONSTRUCTION ACTIVITY IN THE PUBLIC SECTOR: The Performance of Selected Agencies

Agency	January-June 1978 Target (Rs. Millions)	Performance	% of the target achieved
1. Dept. of Buildings	62.6	46	73.5
2. State Engineering Corp.	63.9	38.4	61.0
3. Dept. of National Housing	26.4	19.8	74.8
4. River Valleys Dev. Board	27.9	25.4	90.6
5. State Development and Construction Corp.	24.6	15.0	61.2
6. Dept. of Highways	11.2	15.5	137.9
7. Irrigation Dept. (Major works)	25.6	16.2	63.5
8. Decentralised Budget for irrigation works at rural	31.0*	23.4	75.5
Total (1 to 8 above)	280.2	197.7	72.5

* 50% of 1978 allocation

TRANSPORT AND TRAVEL

A substantial increase was recorded in the imports of vehicles and transport equipment and this led to higher output and employment in the transport sector. The vehicle population of the country (registered with the Commissioner of Motor Vehicles) rose from 203,771 in July 1977 to 213,078 in June 1978 which is an increase of nearly 10,000 vehicles. This was the highest increase recorded for a 12-month period in many years. The position as at June in the previous two years was 1976—193,054; and 1976 — 196,760. The greater part of the increase during the past one year took place in the first half of 1978. Of the total increase during the past one year over 3,000 were private cars, nearly 2,200 were tractors, and nearly 1,500 were lorries. Substantial increases which were recorded in lorry and tractor imports, in particular, would have led to enhanced employment opportunities in the transport sector. The public transport sector also recorded a higher level of activity as seen by the higher operated mileage of the CTB which rose by 14 percent over the first half of 1977 and the higher passenger mileage (which rose by 17 percent). The Port Cargo Corporation registered sizeable increases in the cargo handled, import cargo by 7 percent and export cargo by over 5 percent.

TABLE 8 TRANSPORT: SELECTED INDICATORS

	First Half 1977	First Half 1978	Percentage Change
1. Vehicle Population: of which:	196,760	213,078	+ 8.6
Private Cars	91,559	94,631	+ 3.3
Lorries	35,077	36,514	+ 4.1
Tractors	21,370	23,535	+ 10.1
2. C.T.B. Operations:			
Operated Km. (millions)	194.4	220.8	+ 13.6
Passenger Km. (millions)	7,659	8,936	+ 16.7
3. Port Cargo Corporation Cargo handled (Thousand Tons)			
Import Cargo	1,047	1,120	+ 6.97
Export Cargo	508	535	+ 5.31

Tourism

An estimated 83,604 tourists visited the country during the first half of 1978, and this represented an increase of 22 percent over the

TABLE 9 FOREIGN TRAVEL: SELECTED INDICATORS

	First Half 1977	First Half 1978	Percentage Change
1. Receipts from foreign travel			
Rs. millions ..	[illegible]	360	+ 155.5
SDR millions ..	15.2	18.3	+ 20.4
2. Payments for foreign travel			
Rs. millions ..	13.7	139	+ 914.6
SDR millions ..	1.5	7.3	386.7
3. Net earnings from foreign travel (1-2):			
Rs. millions ..	123.3	211	+ 71.1
SDR millions ..	13.7	11.0	− 19.7
4. Tourist Arrivals (Number)	76,875	93,604	21.8
5. Passport Issues (Number) ..	20,014	53,053	+ 165.1
6. Foreign Travel by Sri Lankan residents (Number)	30,710	57,313	+ 86.6

first half of 1977. The gross earnings from foreign travel thus registered an increase of 20 per cent. The visitor room strength of the country as at June 1978 was 4,900 and approval had been granted for nine more hotel projects with a room strength of 577. An important development in the first half of this year has been the substantial increase in the number of Sri Lankans travelling abroad on holidays, business, pilgrimage and for employment. Statistics on the number of Sri Lankans travelling abroad show that over the first six months of 1977 and 1978 there has been an almost 90 per cent increase. From 30,710 in 1977 it rose to 57,313 in 1978. A further indication is provided by the number of passport issues. 57,848 passports have been issued during the first half of 1978 and this number represents a considerable increase at 165 percent over the first half of 1977 and 39 percent over the second half. A good part of these new passport holders could be assumed to be prospective migrants to Middle Eastern countries. The expenditure of Sri Lankans for travel abroad amounted to Rs. 139 million (or 7.3 million SDR) and this represented an increase of 387 percent over the corresponding period last year. When allowance is made for the outflow of this expenditure, the net foreign exchange earnings from tourism amounted to only SDR 11 million which represented a decline of 20 percent from the net earnings of the corresponding period last year. However, the remittances from migrants to Middle Eastern countries are likely to show a significant increase this year. Rough estimates are that Rs. 25 to 30 million were being remitted per month by the Sri Lankans working abroad.

BTN No.	Item	Increase in Rs. million	Increase in SDR million	Increase in %
86-89	Vehicles and Transport equipment	550.6	21.5	154.5
84-85	Machinery, Mechanical apparatus, and Electrical equipment	515.5	14.6	61.6
28-38	Chemical & Allied Products	790.5	10.2	17.3
16-24	Foodstuffs, Beverages and Tobacco	315.1	6.39	33.4
1-5	Animal Products	245.9	5.9	44.4
73-83	Base Metals & Products	168.8	5.1	28.8
68-70	Stone, Plaster, Cement Asbesto & Allied	210.9	3.03	18.8
90-92	Optical, Photographic and	45.9	1.42	76.2
	Scientific instruments	50.2	1.07	96.3
94-98	Miscellaneous Manufatures	19.4	0.8	163.8
	All Imports	3,755.8	14.73	4.3

EXTERNAL TRADE AND PAYMENTS

In rupee terms, the value of exports and imports more than doubled but this was primarily a result of the devalued Rupee value. In SDR terms, the exports valued at SDR 327 million remained virtually unchanged from the level recorded in the first half of 1977, while the import value at SDR 360 million registered an increase of only 4 percent. The unchanged export earnings (in SDR terms) was a result of the increases in the earnings from rubber, coconut and industrial exports being offset by a decline in the earnings from tea, gems and minor agricultural crops. On the other hand,

TABLE 10 BALANCE OF MERCHANDISE TRADE

	Exports		Imports		Balance of Trade	
	Rs. million	SDR*	Rs. million	SDR*	Rs. million	SDR*
1st Half 1977	2937.1	326.5	3127.1	347.6	-190	-21.1
1st Half 1978	6244.7	327.2	6874.9	360.3	-630.2	33.0

* *SDR value was Rs. 8.9965 for the first half of 1977 and Rs. 19,0860 for the first half of 1978.*

TABLE 11 EXTERNAL ASSETS AND EXTERNAL DEBT

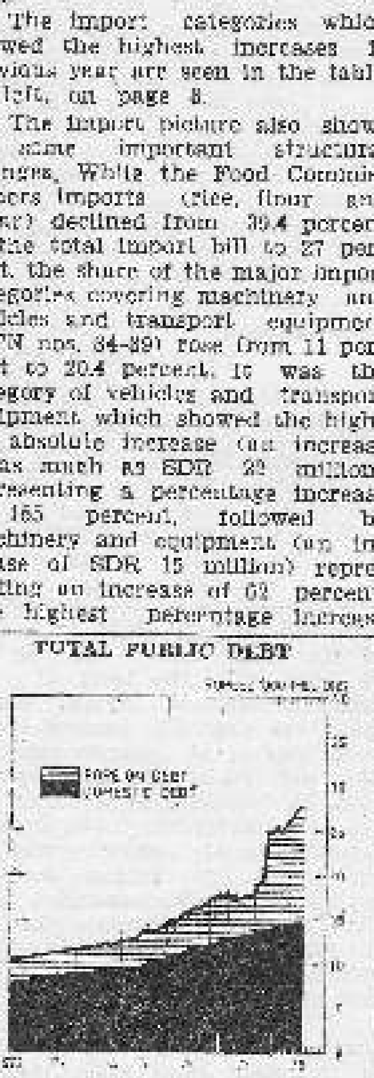
	External Assets Rs. Mn.	External Assets SDR Mn.	In terms of months imports	External Public Debt Rs. mn.	External Assets as % of Public External Debt
End June 1977	1602.7	189	3.5	4412	36.3
End Dec. 1977	5573.6	300	5.5	10,827	51.5
End March 1978	6356.0	329	6.0	11,359	56.0
End June 1978	6167.5	316	6.0	12,692	48.6

the modest increase recorded in the import bill (in SDR terms) despite the import liberalisation was a result of the large savings realized on rice imports which declined by as much as 72 percent in value and by 73 percent in volume. Foreign exchange savings on account of this reduced level of rice imports (relative to the first half of the previous year) was as much as SDR 45.4 million. This saving enabled the country to accommodate a good portion of the increases recorded in the rest of the import bill, and to contain the rise in the overall import bill to only SDR 15 million or 4 percent.

The import categories which showed the highest increases in previous year are seen in the table, at left, on page 8.

The import picture also showed some important structural changes. While the Food Commissioners imports (rice, flour and sugar) declined from 39.4 percent of the total import bill to 27 percent, the share of the major import categories covering machinery and vehicles and transport equipment (BTN nos. 84-89) rose from 11 percent to 20.4 percent. It was the category of vehicles and transport equipment which showed the highest absolute increase (an increase of as much as SDR 22 million) representing a percentage increase of 165 percent, followed by machinery and equipment (an increase of SDR 15 million) representing an increase of 62 percent. The highest percentage increase

TOTAL PUBLIC DEBT



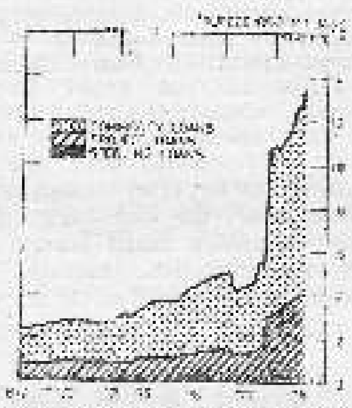
Source: *Central Bank of Ceylon*

was recorded by miscellaneous manufactures (184 percent increase) although the absolute increase was quite modest (being less than SDR 1 million).

The balance of merchandise trade showed a deficit of SDR 33 million which represents an increase in the trade deficit of over 50 percent in relation to the first half of 1977. The higher trade deficit was of course a result of the increased flow of imports while export earnings (in SDR terms) remained virtually constant.

Despite the higher balance of trade deficit, the external assets of the country rose by a significant amount. Compared with a level of SDR 189 million at the end of June 1977, the country's external assets at the end of June this year amounted to SDR 316 million, representing an increase of 67 percent. Compared with the position at the end of 1977, there was an improvement of nearly 10 percent by the end of March, which dropped to about 5 percent by end June. The external assets in June were almost equal to the first half of 1978 which represents a substantial build up of assets when it is noted that in most previous years of the 1970's, the external assets could finance only about two to three months of imports. Since the balance of trade was in deficit, the higher level of external assets was a result of an increased inflow of foreign capital and aid. It may be noted that the external public debt rose by 17 percent during the first six months of 1978. Measured in relation to the external debt, the level of the external assets throughout the first half of 1978, has been equivalent to about 50 percent of the external public debt, as against a picture of less than 30 percent that characterised the previous years of the 1970's.

THE FOREIGN DEBT



Source: *Central Bank of Ceylon*

Another healthy element in the foreign trade picture of the first half of 1978, was the noticeable improvement in the country's commodity terms of trade reflecting an increase in the import purchasing power of a unit of exports. The commodity terms of trade which have continuously dropped from 1967 (which is the base year, 1967=100), upto 1975 when they reached the lowest level at 46) showed some improvement in the subsequent two years, and by December 1977, they had recovered to the 1967 level of 100. During the first half of 1978, the monthly terms of trade fluctuated between a low of 78 and a high of 103, averaging 93.3 for the period as a whole and this represents a substantial improvement over 1977 when they averaged 81. The improved terms of trade largely reflects the rise in the export price index of tea.

TABLE 11 CHANGES IN THE COMMODITY TERMS OF TRADE

(1967=100)

	Export Price Index	Import Price Index	Terms of Trade
1967	100	100	100
1975	189	411	46
1976	239	383	62
1977	382	471	81
1978 Jan-March	684	748	92
1978 April-June	715	761	96
1978 1st half	701	757	93

Source: *Central Bank Trade Indices*

However, the trends in the first half of this year seem to indicate that the balance of payments would record a deficit of about SDR 122 million (Rs. 2,432 million) as compared with a surplus of SDR 121 million (Rs. 1,250 million) in 1977. This turnaround is primarily attributable to the larger inflow of non-food imports and also to an estimated decline of about 4 per cent in export earnings.

Making allowances for short-term capital repayments, the balance on the services account and private transfers, the balance of payments for the whole of 1978 is officially estimated to record an overall deficit of SDR 14 million.

EXCHANGE RATE MOVEMENTS

Since the exchange rate reform of mid-November 1977, the external value of the Sri Lanka Rupee has been announced daily by the Central Bank presumably on the basis of the supply and demand picture for various currencies in the local foreign exchange market. An analysis of the exchange

TABLE 12 THE VALUE OF RS. 100 IN FOREIGN CURRENCIES

	Rupees 100 is worth					
	Yen,	D.M.	£	Indian Rs.	U.S. $	SDR
End June 1977						
(a) Official Rate	2878	32.9	7.99	121.5	13.73	11.73
(b) FEEC inclusive	2840	19.9	4.84	73.6	8.32	7.14
End Dec. 1977	1638	13.4	3.34	53.9	6.41	5.30
End June 1978	1504	13.3	3.43	52.7	6.36	5.13
Percentage Change:						
(i) June '77 to June '78 at						
(a) Official Rate	-66.4	-59.9	-57.1	-56.7	-53.8	-56.6
(b) FEEC Rate	-44.8	-32.7	29.1	-28.4	-23.9	-28.2
(ii) Dec. '77 to June '78	-14.8	-6.9	+2.7	- 2.4	- 0.9	- 3.2

rate changes during the first half of 1978 reveals that while the Rupee-US Dollar parity rate has changed only marginally, there has occurred a significant depreciation of the Rupee in relation to the Japanese Yen and a modest depreciation against the German Mark. The extent of the depreciation of the Rupee against the Yen has been nearly 15 percent and against the German Mark about 6 percent, while against the dollar the depreciation has been less than 1 percent. Thus, the outcome of the operation of the new system of exchange rate determination in the first half of this year has been the maintenance of a highly stable relationship with the US Dollar and a variable relationship with the Yen and Mark in particular. It may be noted in passing that this observed stability of the Dollar-Rupee rate has occurred during a period when the value of the Dollar has continuously declined, particularly against the Yen and the Mark, in world money markets. If we could assume that changes in the exchange rates have been announced by the Central Bank on the basis of the supply and demand for foreign currencies in the local market, then it could be said that the depreciation of the Rupee against the Yen essentially reflected a situation where the demand for Yen continuously outstripped the supply of Yen (meaning that imports from Japan were taking place far in excess of the exports to Japan) while stability of the dollar value reflected that the demand for dollars has remained roughly in line with the dollar supplies.

In relation to the official exchange rates that existed in June last year, the exchange rates prevailing at the end of June this year represented a depreciation of 86 percent against the Yen, 60 percent against the Mark, and 54 to 57 percent against the Pound Sterling, US Dollar and the Indian Rupee. However, when measured against the FEEC-inclusive exchange rates of June 1977 (which were the effective rates for most foreign trade transactions), the end June 1978 rates reflected a much lower degree of depreciation, namely 45 percent against the Yen, 34 percent against the Mark, 28 to 29 percent against the Pound and the Indian Rupee and 24 percent against the US Dollar. The depreciation of the Rupee against the SDR (the international monetary unit, the value of which is linked to a basket of key currencies) during the year ended June 1978 was nearly 57 percent (using the official rate of the Rupee a year ago) and 28 percent (using the FEEC-inclusive rate).

TABLE 13 MONEY SUPPLY (Rupees million)

	(1) Currency	(2) Demand Deposits	(3) Money Supply (M1 = (1) + (2))	(4) Percent Change	(5) Savings & Time Deposits	(6) Money Supply (M2 = (3) + (5))	(7) Percent Change
End of Period							
June 1977	2626	2322	4964	— 2.3	7116	12980	
December 1977	2782	2574	5301	+11.8	6716	12717	—16.8
March 1978	3042	2959	6066	+ 8.6	6037	11403	+11.5
June 1978	2928	2926	5847		4897	9844	— 2.1

MONEY SUPPLY AND INTEREST RATES

The money supply, narrowly defined to include only currency and demand deposits (denoted by M1), stood at Rs. 5,864 million at the end of June 1978. This level represents an increase of 9.3 percent over the end of the December 1977 level. The increase in the money supply was confined to the period January — April when an increase of 12 percent was recorded. A decline set in during May which continued into June mainly due to a drop in the country's external assets.

The increase in the money supply during the first six months of 1978 was largely a result of (a) a rise in the external assets of the banking system and (b) an expansion of commercial bank credit to the private sector, public corporations and co-operatives. The high level of bank credit to finance GPS purchases was an important factor in the commercial bank credit expansion. With a view to restraining the expansion in money supply, the Central Bank directed commercial banks not to increase the total of their advances to public corporations and boards over the levels of such advances outstanding as at June 28th. This ruling was marginally relaxed in mid-July to permit an increase in this overall ceiling; and was due to be further relaxed.

The money supply, broadly defined to include not only the currency and demand deposits but also savings and time deposits (denoted by M_2), stood at a level of Rs. 12,980 million at the end of June 1978. The level of this broad concept of money supply (M_2) was thus 121 percent higher than that of M_1 (narrow concept). Moreover, during the first half of 1978, M_2 increased at a faster rate (at 14 percent) than the increase recorded in M_1 (which was 9.3 percent). The reason for the higher rate of M_2 expansion was the continued increase in the savings and time deposits which recorded an increase of 18 percent during the first half of 1978.

The high level of savings and time deposits (at Rs. 7,118 million at the end June 1978) was an important source of secondary liquidity in the economy. High interest rates continued to attract funds into the savings and time deposits of the commercial banks and the National Savings Bank, and the increase in this flow of savings in the first half of 1978 amounted to Rs. 1,079 million.

The Central Bank rate on advances to commercial banks (Bank Rate) continued unchanged at 10 percent since August 1977. The market rate for Treasury Bills continued at 9 percent since November 1977. The commercial bank lending rates ranged from a minimum of 13 percent to a maximum of 20 percent. The banks and private finance companies continued to offer high rates for savings and time deposits. The National Savings Bank offered 8.4 percent for savings deposits and 12 to 18 percent for fixed deposits ranging from 6 months to 18 months.

The financial operations of the Government sector were a significant factor in that they helped to exert a contractionary influence on the money supply. Further, most of the factors that caused the money supply to increase during the first half of 1978 are expected to exert a negative influence during the second half. Thus, the Central Bank has estimated that the money supply would increase by about 12 percent in 1978, as against 35 percent in 1976 and 29 percent in 1977.

PRICES AND WAGES

The period under review witnessed significant price increases for many commodities, but there is no reliable index to measure the impact of these price changes on the cost of living. The Colombo Consumers Price Index is a defective barometer of consumer price changes and its shortcomings are well known. During the first half of this year, this 'defective' index registered an increase of 11 percent. This increase was largely a result of the inclusion of the open market price of rice in the calculation of this index since February this year, when the rice and sugar rations were withdrawn from families earning Rs. 300 or more per month. As a result of this change, the food sub-index (which has a weight of 62 percent in the overall Index) registered a sharp increase of 13 percent in February. Apart from this, no other significant price changes are reflected in this Index. For example, clothing prices have remained constant, and the two groups fuel and light and miscellaneous commodities (which together have a weight of 25 percent in the Index) registered price increases of only about 1 percent. But this picture is hardly realistic since significant price changes did take place in each of these commodity groups.

A more realistic indicator of price change is provided by the Wholesale Price Index computed by the Central Bank. However, this index measures prices at the primary marketing level (that is, at the first commercial transaction in the chain of sales of the product) rather than at the retail level. Hence the prices covered by this index are mostly producers' prices (in the case of locally produced goods) and the import prices of imported goods. The Wholesale Price Index having shown an increase of 3.2 percent during January-March, declined by 3.5 percent during the next three months (April-June), so that for the six months as a whole there was no increase. Within the overall index, however, several important categories of commodities showed significant price increases. The price increases were highest in the case of imported goods (an increase of 26 percent) and intermediate goods (an increase of 14 percent). The sub-category of textiles and footwear (which is an important consumer item group) rose by as much as 23 percent and this stands sharply in contrast with the picture depicted by the Colombo Consumer Price Index where the Clothing index had remained constant for the first half of 1978. Among the intermediate products which showed relatively high price increases are paper products (+17%), non-metallic products (+13%), metal products (+15%) and fuel and light (+17%). However, the rate of price increase recorded for most commodity groups during April-June was much lower than in the first three months of the year. This may be an indication that by mid-1978 most prices having worked through the adjustment process necessitated by the devaluation, import liberalisation and other policy reforms were

TABLE 14

CHANGES IN PRICES AND WAGES

	June 1977	Dec. 1977	March 1978	June 1978	Percent Changes Dec. '77 to June '78	March '78 to June '78
1. Colombo Consumer Price Index 1952=100	205.9	204.6	221.6	227.0	+ 11.0	+ 2.4
of which Food Sub-index	205.3	203.1	230.1	238.3	+ 17.3	+ 3.6
2. Wholesale Price Index (1974=100)	142.8	152.2	158.7	152.6	+ 0.4	— 3.5
of which:						
(a) Imported Goods	86.0	111.6	130.1	140.9	+ 26.3	+ 8.3
(b) Intermediate Goods	107.7	141.4	146.9	161.0	+ 13.9	+ 9.6
(c) Textiles and Footwear	155.1	186.4	228.1	240.5	+ 22.6	+ 5.4
(d) Paper Products	115.5	118.5	128.3	138.8	+ 17.1	+ 8.2
(e) Non-metallic Products	152.8	220.6	263.1	249.2	+ 13.0	— 5.3
(f) Metal Products	91.9	106.1	105.9	121.2	+ 15.3	+ 14.4
(g) Fuel & Light	178.7	215.5	232.6	251.2	+ 16.6	+ 8.0
3. Minimum Wage Rate Index Numbers 1952 = 100						
(a) Central Govt. Employees	237.2	275.2	275.2	275.2	—— No Change ——	
(b) Govt. School Teachers	182.9	203.9	203.9	203.9	—— No Change ——	
(c) Workers in Wages Boards Trades	309.3	402.0	424.5	438.2	+ 9.0	+ 3.2

approaching their new equilibrium levels.

There was speculation, however, that the pressure on prices would continue for sometime in view of the excessive monetary expansion of the past two and a half years, since monetary expansion reacts on prices with a time lag; and the need for monetary restraint would persist for some time before pressure on prices could be relieved.

Beginning from around late 1977, there was a spectacular rise in urban land and property values, particularly in and around Colombo. In some parts of Colombo, the extent of the increase in land values has been as much as 100-300 percent. While a good part of the explanation of these price trends has to be sought in the activities of real estate speculators, the inflationary trends, high interest rates and liquidity in private hands, and the increased business activity in the private sector were further factors that contributed to this land price inflation.

The wage increase of Rs. 60 (maximum) granted in December 1977 raised the minimum wage rate index of Central Government employees by 18 percent, and those of government school teachers by 11.5 percent and the workers of Wages Boards Trades by nearly 11 percent for the next six months. While the wage rates of all government employees remained constant those of the Wages Boards Trades recorded an increase of 8 percent. It could be assumed that the increase in the living costs that followed went to offset a substantial portion of these wage increases. The erosion of the real wages led to a demand by many trade unions for higher wages and the government was expected to make adjustments in wages and salaries in keeping with the living costs in the 1979 Budget to be introduced in mid-November.

MANPOWER AND EMPLOYMENT

The number of unemployed persons at the end of 1977 has been estimated to be over one million or over 20 percent of the labour force in the country. In view of this high rate of unemployment, the government has attached high priority to new employment generation. In the medium and long-term, the government expects to absorb the unemployed manpower by the implementation of major development projects such as the accelerated Mahaveli Development Scheme, Greater Colombo Development Scheme and the Investment Promotion Zone.

No data are available on the extent of employment creation during the first half of this year or on the number unemployed at the end of the period under review. However, scattered data available suggest a fair expansion of employment in this period. In the public sector the main course of new employment has been the filling up of vacancies in the existing cadres of various public sector institutions. The number of vacancies filled upto the end of June has been reported to be over 120,000 and the number of vacancies reported as available for filling as at the end June, according to the Ministry of Plan Implementation, was over 130,000. A new scheme for the placement of unemployed persons in public sector jobs (called the Job Bank Scheme) was inaugurated and it is expected to provide 130,000 jobs (at the rate of 1,000 persons per electorate) under this Scheme during 1978. The government has also appealed to the private sector to increase its workforce by 10 percent, which it is anticipated would lead to the creation of about 50,000 jobs in this sector.

The enhanced level of economic activity in the private sector evidenced throughout this period would have led to a sizeable expansion in employment opportunities. Unofficial estimates suggest an increase of the order of about 20,000 during the first six months of this year. The number of jobs advertised in the daily papers (mainly skilled, managerial and technical jobs) was more than 8,000 during this period and this represents a considerable increase over the figures of the previous year. Liberalisation of the imports of raw materials, machinery and spares, by enabling the private sector industries to achieve a higher capacity utilization, would have led to some employment expansion. Moreover, the policy of import liberalisation would have had a direct effect on the employment generation in the import, wholesale and retail trade. Higher tourist traffic (outflow as well as inflow), substantial increases in the imports of lorries, vans and tractors, and the higher level of construction activity were further factors that would have contributed to the employment expansion.

TABLE 15

REGISTRATION OF COMPANIES

Year	No of Companies Registered
1965	220
1966	181
1967	208
1968	215
1969	279
1970	240
1971	141
1972	201
1973	355
1974	349
1975	224
1976	205

Monthly Registrations Nos.

	1977	1978
Jan.	22	32
Feb.	23	12
March	40	43
April	18	26
May	17	45
June	28	55
July	15	50
Aug.	20	58
Sept.	27	58
	220	400

A further indication of the expanding business activity is evident from the numerous applications being received by the Registrar of Companies for the registration of new businesses. Some of these applications have even come from established businesses which were hoping to make use of the tax concessions granted to new companies set up after the budget of November 1977. The major part, however, are reported to be new concerns which in 1978 averaged 45 registrations per month as compared with a monthly average of 25 in previous years. The total number of new business registrations in 1978 was expected to exceed 500. (See table).

There were also signs of increased activity in the Investment Promotion Zone area and according to latest official information 40 projects had been approved with a total investment of Rs. 1,600 million on these projects and employment potential in them of 26,000. The construction of infrastructure facilities in this zone were underway and was providing direct employment to considerable numbers. Several tube wells had been sunk and the internal roads relating to Phase I of the project were completed. The increased economic activity that has been stimulated through this project and several other major schemes, it is hoped, would ultimately generate the new employment opportunities which is expected to be the principal thrust of the government's future economic and social policy.

China's New Long March

China has launched on a course of "modernisation", a new policy that can have major repercussions on the balance of economic and political forces of the entire world and Asia in particular. Its diplomatic offensive between May and August, with no fewer than five key members of the Chinese hierarchy embarking on extended tours covering every major continent, climaxed by the signing of the China-Japan Peace and Friendship Treaty on August 12; its shopping for new military hardware in the capitals of Europe; its ambitious targets for agricultural mechanisation which it hopes would help eventually in providing surpluses for exports which will in turn pay for other programmes; its large scale imports of foreign technology and virtual invitation to foreigners to develop the country on the party's behalf; and its open acceptance of the profit motive in banking and other business sectors are all clear indications that China intends moving quickly out of its earlier isolation from the mainstream of the world economy.

When China's Chairman Hua Kuo-feng addressed the Fifth National People's Congress in Peking in March this year he visualised a Chinese economy in the year 2,000 where

> "the output per unit for major agricultural products would reach or surpass advanced world levels, and the output of major industrial products approach, equal or outstrip that of most developed capitalist countries". Such ambitious goals and the path China would take to reach them have been the subject of much discussion and interpretation ever since. Sceptics keep asking whether "revisionist socialism is really right for China" or whether it was possible for China "to buy its way towards a vision of self-reliance".

Chairman Hua Kuo-feng in his report to the Fifth National People's Congress thus set out quite clearly his new targets:

> In agricultural production, the highest possible degree of mechanisation, electrification and irrigation will be achieved. There will be automation in the main industrial processes, a major increase in rapid transport and communications services and a considerable rise in labour productivity. The results of modern science and technology on a broad scale will be applied, extensive use of new materials and sources of energy will be made, and the major products and the processes of production will be modernised. The economic and technical norms must approach, equal or surpass advanced world levels.
>
> The ten years from 1976 to 1985 are crucial for accomplishing these gigantic tasks. In this interval, China is to produce 400 billion kilogrammes of grain and 60 million tons of steel. Every year between 1978 and 1985, the value of agricultural output is to increase by 4 to 5 percent and industrial output value by over 10 percent. The increase in the output of major industrial products during this time is expected to far exceed that of the past 28 years......The state expects to have built or completed 120 large-scale projects, including ten iron and steel complexes, nine non-ferrous metal complexes, eight coal mines, ten oil and gas fields, thirty power stations, six new trunk railways and five key harbours".

"There are only 22 years left to the year 2,000. In such a short period of time, can this formidable task be accomplished", he asked.

Where speculation has been most rife is how far this task could be accomplished; and even more what its repercussions would be not so much for the rest of the world as for China. Chairman Hua, emphasising what has come to be known as the "drive for the four modernisations", stated that China's goal was to modernise agriculture, industry, national defence and science and technology, catch up with advanced world levels and surpass them both economically and technically. There is no doubt that China is today in the midst of a major modernising movement and emerging from a period of self-imposed isolation. In its drive for the four modernisations China is calling for universal education, urging the people to write letters to newspapers and to government if they wish to voice their grievances. An indication of this policy came in the Chairman's call to raise the scientific and cultural levels of the entire Chinese nation. In his address at China's National Science Conference on March 24, Chairman Hua commented,

> "the most powerful base and inexhaustible source of strength for the modernisation of science and technology in our country are the masses of the people in their hundreds of millions who, fired with enthusiasm, are determined to do away with blind faith, emancipate their minds, rid themselves of inferiority complex, call up the courage to break new ground and to think, speak and act, and exert themselves in study and work."

China's modernisation drive has moved on to sending out innumerable technical delegations overseas and welcoming foreign technicians, and to paying emphasis to the need for rules and regulations in enterprises, and stressing the importance of developing a legal code. All this and more have been done in the name of the "four modernisations" of agriculture, industry, defence and science and technology. How China hopes to meet the challenges, as visualised by Chairman Hua of propelling his country into the ranks of modern industrialised nations by the end of the century, appears to be through select borrowing from the capitalist countries.

Capital equipment imports from abroad will certainly play a major role in China's new production drive. Following its early initiative in this direction there is speculation that China's shopping list would range from transport equipment to power plants including various types of Western gadgetry. For instance, its recent purchases of off-shore drilling rigs from U.S. companies and its commitments of more than U.S. $ 5 billion for imports which includes several steel mills, one of which is a 6 million ton Japanese facility to be built near Shanghai; and also West German skills and equipment needed to build five new deep coal mines and modernise another, plus two large opencast mines, together with the factories to build the machinery for these projects estimated to all cost nearly $ 4 billion, seem only the begining.

With all these activities on the import front many important issues could arise. According to some observers, "Peking's long standing posture of rigid fiscal conservatism will almost certainly be incapable of dealing with the large financial burdens imposed by multi-billion dollar buying. And the country's technological infrastructure, long neglected in the wake of the post-Cultural Revolution emphasis on ideological purity and economic egalitarianism, seems similarly unable to cope with the requirements of a large influx of sophisticated plant and technology." There is little doubt that the manner in which China's leadership meets these twin challenges will decide the precise direction the import programme would take, and in the end the result of the entire modernisation drive.

Following three consecutive deficit of trade years Peking registered two impressive surpluses and this perhaps has given China's leadership sufficient confidence to move forward on the import front. A major part of the U.S. $ 8 billion capital equipment to be purchased from Japan will be financed through its exports of oil and coal. But there would yet be a part of its imports upto 1985 that would have to be paid for by other means. The Chinese Import and Export Corporation has therefore adopted international practices in trading with other countries. China's Foreign Minister Lee Chiang was very specific about China's method of payment when he said recently; "our imports should be based on the ability to pay. Only if we have the ability to pay can we increase our imports. That is to say, only if we increase our exports simultaneously can we import more goods. No matter what forms of payment we adopt cash, instalment, fairly long-term deferred payments, compensation by our own products, or other prevailing forms in international trade, we hold that all these forms should be based upon our ability to pay immediately or within a specified period of time. Other forms which deviate from this principle are unacceptable to us". In several cases the Chinese shopping missions have hinted that they may be prepared to adopt more conventional forms of financing and possibly pay in hard cash through foreign banks.

As important as financing arrangements will be the problems associated with the absorption of modern and advanced technology. China by some estimates is said to be nearly two decades behind industrialised countries in certain advanced branches of science. One explanation is that educational disruptions over the past decade have eliminated an entire generation of young people from the technology man-power pool and many of those from the previous generation who have to fill the middle and senior management positions find themselves out of touch with international developments over the last decade. Furthermore, with shortages and obsolescence of equipment the gap has widened. One solution is the sending of more Chinese abroad for training and the increasing of scientific and technological exchanges with the industrialised countries. But as contacts increase between Chinese and foreign scientists, Chinese and foreign students, Chinese and foreign officials, inevitably doubts will be raised about various features of the Chinese system. The new leaders are now moving in the direction of giving scientists a free hand in their work, and are encouraging intellectuals to give vent to their creativity, freedom to study religion and philosophy, to discuss the merits of capitalist features, to read previously forbidden books — this is bound to lead to questioning of previously unquestioned tenets. These modernisation measures in China today contrast strongly with the inward looking attitudes that prevailed during most of the last decade.

Analysts point to a repetition of history when reviewing the periods during which China has introduced foreign technology and new industrial plants. Such periods have always been either preceded or followed by political struggle favouring or opposing the ideological stance behind the imports. Striking similarities in events towards the end of the last century have been noted by some observers. The current events seem reminiscent of measures proposed back in 1898 by the reformer Kang Yu-wei. At that time, Kang acting as Emperor Kuang-hsu's adviser, called for a reform of the educational system, with separate schools being set up to study overseas subjects, politics and medicine. One decree encouraged private citizens to make suggestions to the government. Another called for high officials to tour foreign countries. A third called for the improvement and simplification of legal codes. Kang also called for promotion of agriculture, industrial and commercial development.

The proposed solutions, too, are said to be similar, but Kang's reform movement failed because the Empress Dowager, Tzuhsi, felt that the measures were too drastic, and threatened China's cultural heritage and cultural values. She stepped in, seized the reigns of power from the young emperor and Kang had to flee for his life. That reform movement was aborted. The outlook for China's present-day modernisation drive, however, appears to be much brighter. Though there are people who undoubtedly feel that the post-Mao leadership may be going too far or too fast, there is no Empress Dowager who can seize power. Mao's widow, Chiang Ching, who could have played such a role, was arrested and will not be in a position to exert any political influence. The only forces that could emerge to oppose China's present policies are the essentially conservative ones who see the present policy direction as a threat to the country's Marxist - Leninist-Maoist heritage.

Another particular area where the new policy could have a sig-

TENG FOR FACING REALITIES

At a news conference in Tokyo, China's Vice-Chairman Teng Hsiao-ping, asked for "help from all industrialised countries in the modernisation of China".

...Mr. Teng said, "we are backward and we must not close our eyes to the truth. It is a stupid person who behaves as if he were handsome when in fact his face is ugly".

Mr. Teng said the $ 20 billion, eight-year trade agreement with Japan concluded earlier this year is just the beginning.

That sum must be doubled and tripled", he said.

(Reported in the Asian Wall Street Journal) nificant impact is the emphasis on the need to increase profits and accumulate more funds, spelt out clearly in a recent address by China's Chairman:

> "In the struggle to eliminate the pernicious influence of Lin Piao and the "gang of four", we must carry out widespread education throughout the Party and among all economic, financial and trade workers on the need to strengthen economic accounting, pay attention to economic results, increase profits and exercise strict financial supervision, so as to accumulate production greatly and accumulate more funds for socialist construction".

The *ASIAWEEK* of July 21, 1978 commented cynically on the impact this policy was having on the financial sector in Hongkong, when it stated:

> Deals deemed consistent with socialist ideals were most favoured by Peking's thirteen banks in the free enterprise British territory. Now, profit, it seems, is the main priority by order of the Chinese government.

Reports circulating in Hongkong last week made it clear that Peking is giving its banking comrades in the international financial centre much more flexibility on their capitalist operations. News of this development emerged only days after statements at the top levels of the Chinese government which indicated strongly that Peking is ready to accept some form of foreign loans instead of relying on deferred payments for overseas capital purchases........ China's tiptoeing down the road of financial revisionism to help fund its ambitious modernisation programmes comes as no surprise to capitalist circles in Hongkong. And such news, of course, is welcome, particularly by the stock market which is in the midst of its biggest rally since the 1973 share boom went bang.

What caused most excitement — and a prompt eight-point gain on the Hang Seng Index — was the initial report that Peking had actually issued a directive to its financiers in the colony to adopt "capitalist methods" to boost profits. Whether Peking was so explicit is not clear. Certainly, the banks were urged to raise earnings and implement more efficient cost control to contribute to the "four modernisations" programme which China has set itself for the rest of this century".

One fact stands out in the whole process and that is by taking [on] China down the road to modernisation, the present leadership is, in effect travelling down a path from which there seems to be no turning back. Many crucial questions keep cropping up, however, as China's drive to acquire the trappings of modernisation get under way.

Foreign technology is respectable again, but will there by a backlash if progress is not swift?

In turning its farms towards mechanisation and the rush to modernise will Chairman Mao's tears of China's poorer peasants being left behind finally materialise?

How exactly does the Chinese leadership plan to finance its innumerable modernisation projects?

In implementing the new policies will the agricultural and industrial workers get caught out by the new ideological shifts?

As the country develops and education becomes more widespread will the Chinese people, like those in other countries, expect a higher standard of living (a greater share of the cake), more material comforts, free time, travel and a greater say in the way decisions that affect their lives are made?

China's entry into the mainstream of the international economy could also provide a much needed boost to a currently sagging world economic and monetary system. There appears to be greater hope that the Japanese yen has been crashing for international currencies, particularly the U.S. dollar, may now be curbed. U.S. pressures compelled Japan to cut back on her exports of industrial products. Japan's answer was to confine her exports largely to plant and technology and now she is first on the scene in the enormous Chinese market where there exists the world's largest concentration of potential consumers. For the other industrialised nations that hope to follow suit the prospects seem bright.

> SIGNS OF THE TIMES
> *SOME RECENT NEWSPAPER HEADLINES:*
>
> *"The Bank of China to open a branch at Luxembourg".*
>
> *"France secures $ 700 million missile order from China".*
>
> *"Shanghai Curio and Antique Shop resumes business".*
>
> *"Unit of PANAM, International Hotels, to build chain of hotels in China."*

The hierarchy in power in China today is certainly aware of the problems and implications of their new policy and appear confident that the solutions are within their grasp.

In Peking Vice Premier Keng Piao, a member of the Politburo, talked of them candidly with a group of visiting American journalists. Vermont Royster, a Wall Street journalist who accompanied the delegation states in a report that Keng agreed for example, that China would have the problem of rising expectations, the more so the more it succeeded in raising the standard of living. The Vice Premier conceded quite frankly that such moves as sending young Chinese students abroad carried with it some "risks". They expect to "lose" some of them, who once abroad will not return. But it is a risk that must be accepted, he said, if China is to move forward. He thinks the risk is minimal because great care will be taken in choosing the students from among those with a proven loyalty to China and patriotism for their country.

As for those rising expectations among consumers, he expressed confidence that China's production can keep up with them if the modernisation program for both industry and agriculture, does not slacken. Unlike the Soviets, he said, the Chinese are not overemphasising the development of heavy industry at the expense of either agriculture or light industry.

They are all tied together, he explained. If agriculture is not run well it will hurt industrial development and agriculture cannot be improved without industrial development; neither can it be improved if the people who must work hard to bring that about do not see some rewards for their labour in improved living conditions.

The major task for China, in his view, is to catch up everywhere and to accept whatever risks are necessary.

The problem of class divisions — i.e. the separation of intellectuals, government functionaries and managerial personnel from the mass of people — is to be resolved by one of the practices left over from the Cultural Revolution. That is the practice of government officials, college professors, managerial personnel and the like being forced to spend periodic times working among the people as farm or factory workers. "To go to May 7th schools", as the catch-phrase has it, referring to those first launched by Chairman Mao.

The Plunder of National Treasures

In the May and June 1975 issues of the *Economic Review* we had two incisive columns on the antiques drain from Sri Lanka. These two articles directly or indirectly led to a series of newspaper articles and reports, broadcasts, seminars and academic resolutions in the months and years that followed. It was in this sense of the verbal response created that these turned out to be among the most influential pieces this journal produced that year. However, at the level of action those two articles, as well as numerous other responses thereafter continue to remain ineffective. Hence this attempt to re-emphasise the seriousness of the problem.

Following on our May 1975 article, the newspapers reported that a Three-man Committee consisting of the Commissioner of Archaeology, the Director of Museums and the Commissioner of National Archives was engaged in drafting recommendations for a check on the traffic in antiques. Numerous newspaper reports subsequently have repeated that legislation was around the corner and recently a Cultural Delegation from India (which is far more advanced in these matters than Sri Lanka) assured the Sri Lanka authorities that India would be giving us as much technical help as possible in stemming the flow of antiques.

Judging from the record of the last three years of implementing some sort of regulation on the outflow of antiques, it becomes clear that what is required is not so much foreign assistance, although this would be valuable, but a will to do what needs to be done. Our own lethargy takes place within the context of much international success in stemming the flow of antiques in other countries. The current issue of "Courier", the UN organ on cultural matters, devotes a high degree of attention to these successes, not only in stemming the outflow but even of returning antiques already spirited away. Thus the Director General of UNESCO has made a stirring appeal "for the return of an irreplaceable heritage to those who created it." Several countries even without a long recorded heritage and authenticated antiques that we are heirs to have taken steps in this direction. For example, one African country is attempting to recover four ivory masks removed in 1897 by members of a punitive expedition. The articles that follow, as well as our photo coverage draw attention to some of these facts. We also have included some previous correspondence in the national newspapers on this matter to highlight some of these facts.

HOW IT WAS DONE THEN
Through The Archaeological Commissioner himself

The following appeared in the "Ceylon Standard" dated 15th June, 1908:-

"............... A few days ago Mr. Bell Archaeological Commissioner had allowed the District Engineer to remove certain stones from the buildings which are recognized as ancient Buddhist Colleges. A complaint regarding this was made by the High Priest, before Mr. Brayne, Police Magistrate, who ordered the work to be promptly stopped, but after communicating with the Archaeological Commissioner who said that the High Priest had no right whatever to the land in question or the stones there and that they were the property of Government and that he would personally hold himself responsible for the removal of the stones, presumably for mending roads, the District Engineer was allowed to resume the removal of stones, which was done in such a manner as to cause annoyance to the Buddhist Community. The stones were broken up into small bits on the spot and then removed by cart-loads. This has caused great dissatisfaction among the resident Buddhists as they found that they were quite powerless to check this act of vandalism owing to the high official status of the officers concerned".

"The Ceylon Morning Leader" in its editorial of the 14th September, 1907, on "The Archaeological Commissioner" says:

"The Commissioner is in the unfortunate position of having no restraints of that kind, — if we exclude the Buddhists, who from time to time, raise the cry in the wilderness that their sacred idlers are being unnecessarily invaded....

The work of the Archaeological Commissioner has been a term incongruous to the Government and the public alike.

We want a return for the expenditure of over Rupees 300,000/- something the wide world is expecting from the favoured spot of Archaeological work — we want the detailed report of the Archaeologist with all its invaluable sidelights on the history of Ancient Ceylon".

In the midway between the Dagoba and the bund there lie the ruins of Mahapasuma and Suniset. Pirivenas or Oriental Colleges.

It was from this precincts of the former that the coolies of the Public Works Department removed stones; and those shown in Plate XLIV are some that were left unbroken through the interference of Buddhists. These were photographed by a representative of Messrs. P. Skeen & Co., Colombo, on the 17th November 1907, at our request. From the words of the Archaeological Commissioner in page 78 you could very well understand the despotic attitude this servant of His Majesty has assumed. His authority appears to be something higher than that of the Court of Law! We know that he is one of the oldest civil servants but it is gross violation of British Justice to reduce these sacred stones to metal and to say that the remains of religious edifices in the Sacred City do not belong to the Buddhists.

If the sacred precincts are allowed to be devastated in this manner, in a short time the Buddhists will have very little evidence to maintain their long enjoyed rights and privileges, and the lovers of antiquities who visit this city of Ruins and Ruins will be disappointed".

HOW IT IS DONE NOW
Through the Tourist Trade

Many of those vendors who up to a few years ago were selling books for local pilgrims (Vandana Poth) at the main centres of pilgrimage — namely the ruined cities — have now switched over to selling antiques to tourists. Among these antiques are some very rare specimens (judged on stylistic grounds) which have been obtained from temples throughout the Island. According to information supplied by these vendors themselves there is a systematic ring of suppliers — at least three mudalalis — who comb the country's temples and supply the tourist trade with antiques. There is also a brisk sale of rare palm leaf manuscripts (Pus Kola Poth). This latter trade has reached such ridiculous heights that instead of

A Plea for the Return of an Irreplaceable Cultural Heritage to those who created it

An appeal by UNESCO's Director-General

One of the most noble incarnations of a people's genius is its cultural heritage, built up over the centuries by the work of its architects, sculptors, painters, engravers, goldsmiths and all the creators of forms, who have contrived to give tangible expression to the many-sided beauty and uniqueness of that genius.

The vicissitudes of history have nevertheless robbed many peoples of a priceless portion of this inheritance in which their enduring identity finds its embodiment.

Architectural features, statues and friezes, monoliths, mosaics, pottery, enamels, masks and objects of jade, ivory and chased gold — in fact everything which has been taken away, from monuments to handicrafts — were more than decorations or ornamentation. They bore witness to a history, the history of a culture and of a nation whose spirit they perpetuated and renewed.

The peoples who were victims of this plunder, sometimes for hundreds of years, have not only been despoiled of irreplaceable masterpieces but also robbed of a memory which would doubtless have helped them to greater self-knowledge and would certainly have enabled others to understand them better.

Today, unbridled speculation fanned by the prices prevailing in the art market, incites traffickers and plunderers to exploit local ignorance and take advantage of any connivance they find. In Africa, Latin America, Asia, Oceania and even in Europe, modern pirates with substantial resources, using modern techniques to satisfy their greed, spoil and rob archaeological sites almost before the scholars have excavated them.

The men and women of these countries have the right to recover these cultural assets which are part of their being.

These men and women who have been deprived of their cultural heritage therefore ask for the return of at least the art treasures which best represent their culture, which they feel are the most vital and whose absence causes them the greatest anguish.

This is a legitimate claim; and UNESCO, whose constitution makes it responsible for the preservation and protection of the universal heritage of works of art and monuments of historic or scientific interest, is actively encouraging all that needs to be done to meet it.

The return of cultural assets to their countries of origin nevertheless continues to pose particular problems which cannot be solved simply by negotiated agreements and spontaneous acts. It therefore seemed necessary to approach these problems for their own sake, examining both the principle underlying them and all their various aspects.

This is why, on behalf of the United Nations Educational, Scientific and Cultural Organization which has empowered me to launch this appeal:

I solemnly call upon the governments of the Organization's Member States to conclude bilateral agreements for the return of cultural property to the countries from which it has been taken; to promote long-term loans, deposits, sales and donations between institutions concerned in order to encourage a fairer international exchange of cultural property, and, if they have not already done so, to ratify and rigorously enforce the Convention giving them effective means to prevent illicit trading in artistic and archaeological objects.

I call on all those working for the information media — journalists of press and radio, producers and authors of television programmes and films — to arouse worldwide a mighty and intense movement of public opinion so that respect for works of art leads, wherever necessary, to their return to their homeland.

I call on cultural organizations and specialized associations in all continents to help formulate and promote a stricter code of ethics with regard to the acquisition and conservation of cultural property, and to contribute to the gradual revision of codes of professional practice in this connexion, on the lines of the initiative taken by the International Council of Museums.

I call on universities, libraries, public and private art galleries and museums that possess the most important collections, to share generously the objects in their keeping with the countries which created and which sometimes no longer possess a single example.

I also call on institutions possessing several similar objects or records to part with at least one and return it to its country of origin, so that the young will not grow up without ever having the chance to see, at close quarters, a work of art or a well-made item of handicraft fashioned by their ancestors.

I call on the authors of art books and on art critics to proclaim how much a work of art gains in beauty and truth for the uninitiated and for the scholar, when viewed in the natural and social setting in which it took shape.

I call on those responsible for preserving and restoring works of art to facilitate, by their advice and actions, the return of such works to the countries where they were created and to seek with imagination and perseverance for new ways of preserving and displaying them once they have been returned to their homeland.

I call on historians and educators to help others to understand the affliction a nation can suffer at the spoliation of the works it has created. The power of the fait accompli is a survival of barbaric times and a source of resentment and discord which prejudices the establishment of lasting peace and harmony between nations.

Finally, I appeal with special intensity and hope to artists themselves and to writers, poets and singers, asking them to testify that nations also need to be alive on an imaginative level.

Amadou - Mahtar M'Bow

palm leaf books being sold whole, pages are cut into small strips and sold to tourists as souvenirs for about Re. 1/- per small strip.

At these traditional centres of pilgrimage antiques are openly sold for foreign currency by these vendors and there is a considerable profit in this business. A former General Manager of the Anuradhapura Preservation Board who visited Anuradhapura a few weeks ago after an absence of nearly five years found that there has been a sharp rise in the standards of living of these vendors arising from this trade.

The sale of antiques also goes on either directly or indirectly at almost all the leading hotels in the country. Thus the foyer of the Inter Continental Hotel has a very prominent display and advertisement for a well known antique dealer in Colombo. Similarly there are antique boutiques at many of the leading hotels in Anuradhapura, Colombo, Bentota and Negombo. In the rare event of antiques not being sold in the hotel premises itself, there are often shops adjoining the hotels (and which form part of the hotel complex) which specialise in this trade.

Most of the antique shops in Chatham Street and Queen Street in the Colombo Fort area specialise almost exclusively in the sale of antiques to tourists.

Men in robes whom he would hesitate to call bhikkhus were behind some of the antique rackets discovered recently, the Secretary to the Ministry of Cultural Affairs told a press conference recently. He said that stringent measures would be adopted to arrest the outflow of antiques from Sri Lanka.

A few months ago the Police in Anuradhapura arrested a dealer on suspicion of possessing stolen antiques. Inquiries, however, revealed that the antiques were sold to this dealer by the Chief Priest of a not so remote temple. There is also evidence to indicate that tourists are made offers of antiques even from well known temples, as well as from museums.

Apart from sales to tourists who come to the country for a few weeks, there is a much more systematic sale to foreign experts, diplomats and the like who are here for a longer stay.

It is worth repeating, in the present context what the *Review* urged in June 1975 when we stated "clearly a very broad policy on antiques must be evolved. This should include not only new legislation and tighter methods of control but also a complete re-appraisal of what is historically valuable. The development of popular awareness through education and propaganda and the establishment of local antiquities registers are vitally necessary. The registration of dealers, the encouragement of local collections and the formation of small provincial museums should be combined with a renewal of craft skills and the reproduction of antiques for sale and export. Incidentally, much of this is already being done. It only needs systematisation and encouragement".

COMMODITIES

SPICES

Downward trend

The downward trend in spice exports experienced during the first quarter of 1978 continued into the second quarter of the year with cinnamon and cloves being most affected. Exports of these two commodities further dwindled by 10 percent and 72 percent respectively in comparison to the same period in 1977. Cardamoms, nutmeg and mace however performed better. Total spice exports during April — June 1978 declined by 25 percent over the same period last year. January to June this year. Pepper exports during the first half of 1978 amounted to 677 metric tons. This is a significant achievement compared with the same period in 1977, when pepper exports were negligible. An improvement in the local pepper crop together with an increased availability of red chillies (for which pepper is a substitute) thus reducing local consumption of pepper to a minimum were two factors responsible for this favourable increase. Cloves and cinnmon on the other hand registered declines of 59 percent and 26 percent in quantities exported this year compared to January—June 1977. A poor crop of cloves indicated by the complete absence of this commodity at the Colombo Produce Auctions (except for small quantities on three occasions) was mainly responsible for the poor performance

TABLE 1. EXPORTS OF SPICES JANUARY — JUNE 1978

	April—June 1977 metric tons	April—June 1978 metric tons	% over 1977	Jan.—June 1977 metric tons	Jan.—June 1978 metric tons	% over 1977
Cinnamon (Quills & Chips)	1237.10	753.45	— 39.90	2718.60	2020.09	— 25.70
Cardamoms	15.30	30.54	+ 100.00	50.90	61.08	+ 20.00
Pepper	—	162.91	—	—	677.09	—
Cloves	330.90	91.64	— 72.30	707.60	290.18	— 59.00
Nutmeg & Mace	10.20	162.91	+1500.00	76.40	213.81	+ 180.00
	1593.50	1201.45	— 24.60	3553.50	3263.25	— 8.20

Source: *Customs Returns and Central Bank Monthly Bulletin*

The half yearly performance for all spices, however, registered a smaller decline of only 8 percent over 1977 figures. An improved performance of nutmeg and mace and cardamoms resulted in an increase in the export volume of these commodities by 108 percent and 20 percent respectively during

(Continued on inside back cover).

TABLE II. SPICE EXPORT EARNINGS JANUARY — JUNE 1977—1978

	Jan.—June 1977 Rs. million	Jan.—June 1978 Rs. million	% over 1977	Jan.—June 1977 mill. SDRs	Jan.—June 1978 million SDRs	% over 1977
Cinnamon	31.60	59.10	+ 87.00	3.51	3.10	— 11.80
Cardamoms	7.80	17.00	+ 118.00	0.87	0.89	+ 2.80
Pepper	—	20.10	—	—	1.05	—
Cloves	31.70	21.60	— 31.90	3.52	1.13	— 67.90
Nutmeg & Mace	1.20	5.50	+ 358.30	0.13	0.29	+ 116.50
	72.30	123.30	+ 70.50	8.04	6.46	— 19.60

Source: *Customs Returns and Central Bank Monthly Bulletin*

The Cost of Foreign Aid to Developing Countries

Nihal Kappagoda

Nihal Kappagoda who is at present Vice-President, International, of the International Development Research Centre (IDRC) in Canada, examines here the "cost of foreign aid" in both economic and political terms and focuses on the problems that recipient developing countries face in absorbing foreign assistance. He was the Director of External Resources at the Ministry of Planning and Employment in Sri Lanka from 1970 to 1973, and draws profitably on his personal experiences. Many of these experiences are shared, in various forms, by other developing countries. His background of direct involvement in managing a developing country's external resources gives this paper special relevance in the debate on the 'debt issue'. This paper is based on a talk delivered to the Society for International Development (Ottawa Chapter) on December 13, 1977. The views are essentially those of the author and not necessarily representative of the I.D.R.C.

The need for enhanced transfers of foreign exchange resources to finance the development efforts of Third World countries in the post-1973 period has brought into focus once again the problems that recipient nations face in absorbing foreign assistance. The international community responded positively to the acute balance of payments problems that arose in these countries in 1973 and after, but in concentrating on the volume requirements that increased five-to six-fold annually on a global basis some of the qualitative aspects of foreign aid did not receive the same attention. The costs to recipient nations of absorbing increasing amounts of foreign aid continue as in the past, in spite of international efforts to reduce them. This paper discusses some of the major problems that have been encountered by recipients and the progress that has been achieved in the 1970s to alleviate these problems, mainly through the initiatives of the countries of the Development Assistance Committee (DAC) of the Organisation for Economic Co-operation and Development (OECD).

THE REPAYMENT BURDEN

The debt service problem has been discussed at virtually every international gathering convened during the past decade to discuss economic problems of developing countries. It figured high on the agenda of the 1976 meeting of UNCTAD IV in Nairobi and at the Conference on International Economic Co-operation (CIEC, the North South dialogue) that was concluded in the summer of 1977. The high levels of resource transfers to developing countries that have taken place since 1973 brought into sharper focus the need for international action on the debt question, because much of the borrowing since that time has been on hard terms from non-official sources, thereby increasing the repayment burden of developing countries. As seen from Table 1, private capital flows constituted 57 per cent of the total net flow of resources from Development Assistance Committee (DAC) countries in 1976 compared to 49 percent in 1972, and during this period, annual transfers from official sources increased by only 61 percent compared to 134 percent from private sources.

There is no danger to an economy from a high level of borrowing even on hard terms, provided these funds have been used to build up the capacity to repay such debts. Specifically, a country borrowing heavily will experience a debt problem if it has not adopted policies that have generated a high rate of growth of foreign exchange earnings through exports of goods and services or if it has not adopted import substitution programs that will achieve real savings in foreign exchange expenditures. If a country's economic policies are not geared to achieving these objectives and it

TABLE 1. Net flow of resources from DAC countries and multilateral institutions to developing countries (millions of U.S. $)

	1961-66 Average	% of GNP	1970	% of GNP	1972	% of GNP	1973	% of GNP	1975	% of GNP	1976*	% of GNP
Official Development Assistance	5936	0.44	6831	0.34	8538	0.33	9351	0.30	13630	0.36	13740	0.33
Other official flows	333	0.33	1140	0.06	1546	0.08	2483	0.08	3020	0.08	3490	0.08
Private capital	2902	0.20	7761	0.30	9609	12842	12481	0.41	23330	0.61	22440	0.56
Total	10092	0.75	15711	0.77	19683	0.78	24620	0.79	39910	1.05	39610	0.90

* Preliminary.

Sources: *Tables 1, 2, 3, 4 of Statistical Annex, Development Co-operation, 1976 Review: OECD, and page 25, Annual Report, 1977: World Bank.*

TABLE 2. Global structure of current account balances
(billions of U.S. $)

	1967-72 Av.	1970	1971	1972	1973	1974	1975	1976
Industrial countries	10.2	10.1	13.4	9.4	11.1	-11.2	18.6	-1.4
Major oil exporters	0.7	0.3	2.1	1.7	6.2	67.4	34.7	41.0
Other nonoil-producing countries	-9.8	-8.6	-11.0	-8.9	-9.6	-43.8	-53.0	-41.0

Source : *Annual Reports, International Monetary Fund.*

faces a sharp decline in export earnings or an increase in import prices, then the debt problems could become very acute because of higher borrowings needed to maintain import levels, if the additional resources have not been obtained on concessionary terms.

The benefit of a loan to a recipient is often measured by the grant element of the loan, which is the difference between its face value and the present value of the amortization and interest payments discounted by an appropriate rate of interest. This should normally be the rate at which capital could be borrowed by developing countries in international capital markets. Except to the high income developing countries, this rate of interest is often an academic concept, as they have no access to these markets. As a working rule, therefore, the grant element is estimated by discounting the repayment stream by 10 percent. For example loans that are extended by the International Development Association (IDA), which are interest free and repayable in 50 years including the grace period of 10 years, have a grant element of 90 per cent compared to 100 per cent for outright grants.

Recognizing the need for international action on the debt problem of developing countries, the DAC adopted a recommendation on financial terms in 1972 for Official Development Assistance (ODA)*. To fulfill these conditions, each member country was expected to reach and maintain an average grant element for their ODA commitments of at least 84 per cent. However, countries whose ODA commitments as a percentage of Gross National Product were well below the DAC average would not be considered as having met the target for financial terms. Further, in recognition of the problems of the least developed countries, it was agreed that ODA to these countries should preferably be in the form of grants and that the average grant element of all commitments from a given donor should either be at least 86 percent for each least developed country over a 3 year period or at least 90 percent annually for the least developed countries as a group.

*ODA is defined as resource transfers to developing countries and multilateral institutions provided by official agencies with the main objective of promoting the economic development and welfare of developing countries; it is concessional in character and has a grant element of at least 25 percent.

Problem Worsens for Developing Countries

Since the adoption of this resolution on financial terms in 1972, considerable progress has been made in softening the terms of ODA. In 1975, the overall grant element of all ODA was 88 percent, much above the target of 84 percent. There is no question that positive steps have been taken by individual countries to meet this target, but the overall debt problems of developing countries have worsened by the greater increase in export credits and bank lending since 1972. The increasing financial requirements of non oil producing countries, which were brought about by higher oil prices, shortfalls in food production, and higher import prices in general, are illustrated in Table 2. which presented the global structure of current account balances.

In contrast to the softening terms of ODA, the terms of the total flow of resources have hardened in the 1970s due to the declining share of ODA and the growth of Euro-currency lending of surpluses generated by oil-exporting countries, the terms of which have hardened. If one examines the non oil-producing countries, it is seen (Table 3) that the total debt outstanding increased by nearly two-thirds from 1973 to 1976 and this was accompanied by an increase in the proportion of commercial debt in total debt outstanding from 48 percent to 56 percent and in debt service payments from 67 percent to 77 percent.

If we next examine the debt outstanding in terms of the income groups (Table 4). it is seen that three-fourths of the debt up to the end of 1974 had been incurred by countries whose per capita incomes exceeded US $ 200. The shift in the debt structure toward commercial debt on harder terms is common to all income categories but was most pronounced for those countries whose per capita incomes exceeded $ 375. Debt on commercial terms now represents the bulk of their total debt, which is an indication of their credit worthiness. as well as their ability to raise funds in international money markets. Even in poorer countries with per capita incomes of less than $ 200, commercial and other debts on harder terms accounted for 45 percent of total debt outstanding and for two-thirds of their total debt service payments. but this group of countries accounted for only 13 percent of total debt service payments in 1974. In 1975. debt service payments to DAC countries on ODA loans were only 19 percent of the total by all developing countries. These statistics show that the prob-

TABLE 3. Reported debt and debt services of non oil-producing countries
*(billions of U.S. $)**

	1973	1974	1975	1976
Total outstanding	79.0	96.8	116.3	129.0
Commercial debt (%)	48	52	54	56
Debt Service	9.1	11.8	15.0	17.8
Commercial debt (%)	67	72	75	77

* Excludes nonguaranteed private bank lending.
Source: *Table 11—4, Development Co-operation, 1976 Review: OECD*

TABLE 1. Debt outstanding at end of 1974 and debt service (millions of U.S. $) by income group

	Debt	(%)	Debt Service	(%)
Least developed countries	4967	(4)	329	(2)
Under $200*	23653	(20)	1604	(10)
$200-374†	8114	(7)	1012	(7)
$375-699	17333	(15)	2049	(13)
$700-999	17611	(15)	2270	(16)
$1000 and over	30137	(26)	4700	(30)
Total non-oil-producing developing countries	96040	(82)	11752	(76)
Oil producers	20517	(18)	3723	(24)
Total	117305	(100)	15485	(100)

*Excludes Indonesia,
†Excludes Nigeria

Source: *Table 34 of Statistical Annex, Development. 1976 Review: OECD.*

lem is not with official flows but with private lending on commercial terms that has responded more to the increasing needs of developing countries than official transfers.

Several countries have experienced acute external positions brought about by excessive debt service payments, and debt relief of one form or another has been extended in some 50 countries since 1970. Included in these debt-relief operations have been multilateral arrangements within the framework of the Paris Club for Chile and Zaire and within the framework of the World Bank consortia for India and Pakistan. The writing off of debts has been on the agenda of various international conferences including the UNCTAD IV and CIEC but to date (Dec. 13, 1978) unilateral action has been taken only by Canada, which wrote off $ 254 million of foreign debt with a present value of $ 25 million owed to her by the poorest developing countries to whom she provides assistance, and by Sweden, which agreed to write off debts totalling $ 238 million. Unfortunately, Canada did not follow through and failed to provide new aid to those countries on grant terms. International action on debt relief has been under consideration for some time, but the inability to obtain the support of the Eastern European Bloc for such action, among other reasons, has made it impossible to arrive at a general agreement covering groups of developing countries. Nevertheless, the serious debt service situations of many developing countries make it imperative for the international dialogue to continue.

THE TYING OF AID

The practice of tying foreign aid to donor sources began at the end of the 1950s in response to the balance of payment difficulties donor countries were experiencing at the time. This was the case with the United States when she began in 1959 to tie supplies financed by development loans to U.S. sources, and she even went further and ensured that funds remitted to meet local costs of projects, were subsequently used for imports from the U.S. In the same way, the United Kingdom began to tie her assistance to U.K. supplies in 1963. This action on the part of donor countries that had balance of payment deficits also led to similar actions by surplus countries, such as the Federal Republic of Germany, due to pressures exerted by export lobbies who found their markets threatened by the actions of deficit countries.

One reason for tying assistance to commodities produced in donor countries is the existence of surplus stocks or excess capacity in industries. This was undoubtedly the motivating factor behind the origins of the PL 480 food aid program in the United States and was effectively an attempt to minimise the real cost of aid to the donor. To the recipient, however, the costs are high because of support prices maintained internally in donor countries for agricultural produce. A realistic method of valuing such assistance would be to price the quantities at a notional "world market price" had these supplies been released to the market.

In spite of these higher costs, it has to be conceded that the existence of surplus stocks or excess capacities often results in additional resources being channeled to developing countries. Strong export lobbies in developed countries influence governments to extend credits to support sagging industries that have excess capacities or to dispose of surplus stocks that have arisen due to wrong market expectations and in such cases, aid is necessarily tied. Further, credits are given for the explicit purpose of export promotion of developed country products. In all these cases, the reasons adduced against tying would apply, but had it not been for export promotion or other policy objectives of developed countries, these additional resources would not be available.

Another reason for tying aid is the preponderance of project aid in total aid extended by developed countries. This is due to the mistaken belief that project aid is used more efficiently by recipient countries. But concentration on this type of assistance often results in the implementation of projects that are not often of high priority and leads to an incorrect allocation of resources for investment. There is also the cosmetic effect that a project is better identified with the donor than commodities whose use is more dispersed throughout the economy and not easily identifiable. Once a decision is taken to provide project aid there is even a greater reluctance to untie aid, because a project is better identified with the supplier of equipment and services than with the donor providing funds.

It bears repeating to mention what is often stated about the efficient use of external resources. It is the soundness of an annual import program within the context of a country's development plan that is important and not the financing of individual items or projects in such a program. Commodity aid provides greater flexibility in the use of aid and often leads to minimizing the costs resulting from the tying of aid to donor sources.

Basically, the direct costs of tying arise from paying FOB prices that are higher than world market prices. There could be two reasons for this. First, suppliers in donor countries, realizing that the goods are financed under aid programs and that the recipient country has no choice but to make this purchase under aid, charge a monopoly price. This would be minimized to the extent that it is possible to invite worldwide tenders and then select a supplier from the donor country and to the extent that there are a number of suppliers to introduce an element of monopoly pricing but the situation is worse when there is only a monopoly supplier in the donor country. Second, the cost of production in the donor country may be higher than from the traditional source, which is the main reason why purchases were not made from the donor country originally. This arises often in cases where imports are diverted from traditional sources. The tying of shipping and insurance to donor sources also adds to these costs.

The Additional Costs Can Vary

The additional costs, of course, vary from country to country and depend on the multiplicity of donors, the volume of assistance from traditional sources of supply, the possibilities of competitive bidding, and the goods that could be purchased using aid funds. There are in addition indirect costs that cannot be easily quantified. These result from the use of aid for low priority items due to the dictates of donor countries, the distortions in the price structure (which is, in any event, complicated in a developing country), and the administration costs of managing a tied-aid program where disbursements have to be controlled to ensure the correct sourcewise procurement procedures laid down by donor countries. Accordingly, the real value of foreign assistance is reduced, and the disbursement procedures required to ensure source-wise tying result in waste and delays in the transfer of resources and also dampen the expansion of trade, especially between developing countries.

Theoretically one could minimize the cost of tying aid by inviting international bids for commodities and projects and selecting the cheapest source, provided that adequate assistance is available on time to finance the imports. An accurate estimate of the cost of tying could only be obtained by international bidding conducted on a freely competitive basis, which condition is unlikely to be fulfilled in practice, and it is probable that these costs are not less than 20 percent. The knowledge of the availability of tied funds could result in monopolistic pricing by suppliers from donor sources and indifferent bids from other suppliers. Another factor that has to be borne in mind in project financing is that the recipient often lacks the technical expertise to negotiate cost reductions.

International discussions, mainly by the DAC, on untying aid began in the mid 1960s. By the early 1970s agreement had been reached only on untying contributions to multilateral institutions by DAC countries, which did not effectively change earlier practice though it represented a moral commitment by the group as a whole and in 1975 these funds constituted 28 percent of total ODA. Progress towards untying bilateral loans has been limited and to date 10 DAC countries have collectively signed the agreement on untying bilateral development loans permitting procurement in developing countries. Following the impetus given by UNCTAD IV and CIEC fresh initiatives have been taken toward untying but the progress made in quantitative terms is unknown at the present time.

Apart from joint action by DAC, some countries have taken individual initiatives toward untying aid. By 1970, the United States authorized procurement in almost all developing countries and increased the premissible foreign content of aid-financed goods. The Federal Republic of Germany also removed many restrictions on capital project aid and technical assistance equipment around this time and Canada too decided that up to 20 percent of bilateral aid could be used for purchases in developing countries or to meet local costs. In 1975, the U.K. decided to permit procurement in countries whose per capita incomes were less than $ 200, whilst Japan also took legal measures that were necessary to facilitate untying aid

The position regarding the financing of local costs has been more liberal. Donors such as Sweden and Norway permit all their bilateral project aid to be spent on local costs. Others permitted it for the poorer countries when directed to agriculture and social development projects. In some cases, local costs are financed for particular recipients as in the case of France for the francophone countries.

These have been the recent changes in the developed countries of the West. Amongst the centrally planned economies, only China has permitted the financing of local costs or provided united assistance in the form of cash grants to some developing countries. The costs of tying aid are even greater in the case of these countries as we deal with a monopoly supplier in the donor country, whose prices are fixed by considerations not apparent to those outside and price reductions are almost impossible to achieve.

DISBURSEMENT PROCEDURES

The timing of agreements and disbursement procedures are often key elements in the effectiveness of aid programs to a recipient country and delays in these processes add to the cost of aid to the recipient. In the initial phase of a country's development, particularly those that were colonized by the metropolitan countries, foreign aid was obtained mainly from one country. As these countries developed, both politically and economically, and took their place in the international community, the reliance on a single donor decreased in importance and recipient countries began to deal with a multiplicity of donors whose procedures and practices differed considerably. This process was evident even in the 1970s when the number of developing countries obtaining more than 50 percent their total bilateral and multilateral assistance from a single country decreased from 43 in 1970 to 30 in 1974.

As a result of the multiplication of donors interested in assisting a single recipient, action was taken ni the late 1950s to set up coordinating mechanisms of one type or another by multilateral institutions such as the World Bank, beginning with the consortia set up by the World Bank for India and Pakistan in 1958 and 1960 respectively. The Bank also set up other coordinating mechanisms such as consultative groups and aid groups for discussing foreign aid requirements of recipient countries individually, and this certainly helped countries facing acute balance of payments problems as it enabled the total foreign exchange requirements of a recipient to be looked at by the donors as a group on an annual basis. But this still left the negotiation of agreements by each donor to an independent process determined by the internal approval procedures of donor countries for approving aid allocations to individual countries.

A development that improved the timing of agreements was the introduction of country programming by many DAC countries such as Canada, Denmark, Finland, France, Germany, New Zealand, Norway, Sweden, Switzerland, and the United Kingdom. In spite of this, the availability of funds was yet dependent on budgetary appropriations approved by the legislatures in the donor countries and only limited action has been taken to provide developing countries with the multiyear commitments.

For example, the Australian authorities permit commitments 1 year ahead of 75 percent of current aid levels, 50 percent 2 years ahead, 25 percent 3 years ahead, and 10 percent 4 years ahead. In the case of Canada, I understand that allocations for the main recipients, which number around 30, carry forward commitment authority of 75 percent for each of the 4 succeeding years.

It is true that the coordinating mechanisms and the country-programming exercises of donor countries have improved the timing of agreements, but the improvement has only been marginal. Aid decisions are yet made independent of the overall coordinating mechanism and the uncertainty regarding the timing of agreements increases the difficulties of managing a country's foreign exchange budget. The delays in this process should not be underestimated, and this led the Pearson Commission to report (in 1969) that in the case of United States Development Loans the checklist of statutory provisions required at that time before a loan can be approved had reached 68 separate items. Ideally, developing countries require information in advance of the total quantum of aid that would become available annually and the commodities and projects for which these funds could be used. It is for this reason that the Pearson Commission recommended that the aid appropriation period of donors should be extended to at least 3 years and that appropriated funds could be carried forward for several years. Agreement could be reached in advance of the quantum of aid and the items to be purchased and the signing of agreements should not affect the utilization of aid provided the disbursement procedures of donor countries permit reimbursement of expenditure incurred prior to the signing of agreements. This is often not the case and in the case of many developing countries, it would not be a feasible alternative as they do not have adequate foreign exchange resources or access to short-term lines of credit to permit advance purchases.

Cause for Delays

Apart from the timing of agreements, the disbursement procedures of donor countries also result in considerable delays. Where a country has a multiplicity of donors, the detailed disbursement procedures of each country have to be mastered by the coordinating agency in the recipient country, as well as by the licencing authority and the importers receiving allocations under each program. The realization of this problem led the Pearson Commission to comment: "Hard pressed and frustrated administrators on both sides may some times be pardoned for wondering whether their programs will fail because they will run out of carbon paper".

The negotiations on the list of items that could be permitted under each program often result in protracted bargaining between the donor and recipient: the latter is more interested in financing items that would have a greater impact on the country's development and permit quicker disbursements, whereas the former often has to balance export promotion interests in the donor country with the development needs of the recipient country. This varies from donor to donor and it depends on the influence that export lobbies exert on these governments. The next delay is the approval of individual contracts. Often tenders have to be called in the donor country and after a decision is taken on each one, the prior approval of the aid agency in the developing country is required and payment for each contract is made direct to the supplier. Some donor countries have permitted the reimbursement of expenditure, upon submission of documents for goods that have been shipped and payments made, for items agreed upon between donor and recipient. Even after following these elaborate procedures and gaining approval for a purchase, the US-AID audit could call upon the recipient country to refund the amount disbursed for an item purchased using a U.S. Development Loan if any irregularity is later discovered.

Not all the blame is on the donor country. The recipient countries also have elaborate licencing arrangements that have to be dovetailed with the procedural requirements of the donor agencies. Often, in the interests of equity, aid allocations are distributed amongst numerous importers making it necessary for each of them to master the procedures of each donor agency. It also reduces the real value of aid eliminating the possibility of obtaining discounts on bulk purchases and reductions in shipping costs that could be achieved by bulking. It is perhaps difficult to imagine the delicate balancing act performed by many administrators in developing countries who are called upon to administer these aid programs. Often imports of critical commodities are financed on aid and delays in their arrival have a chain effect on the economy that cannot be avoided in the short run. For example, delays in fertiliser imports financed by aid effects the entire food production effort of the recipient country and it is often not possible to overcome this problem by purchasing commodities from abroad at short notice, either because it is physically impossible to affect shipments within a short time period or the foreign exchange resources needed to finance such purchases are not available at the time.

POLITICAL AND ECONOMIC COMMITMENTS

The influence by donor countries on the domestic policies of recipients has been dealt with extensively in many publications but more critically and not altogether impartially in books such as Teresa Hayter's "Aid as Imperialism" and Cheryl Payer's "The Debt Trap: The IMF and the Third World." I think it is necessary to look at specific examples to understand the full implications of the so-called leverage effects exerted by donors and for this purpose I will quote some examples from Sri Lanka.

In the preceding sections, I dealt briefly with the role coordinating mechanisms have played in expediting the flow of resources to developing countries. It is however, normal for donors belonging to consortia, consultative groups, or aid groups to base their decisions on foreign aid to developing countries on the framework of economic policies adopted by the country concerned, as analyzed and presented by the agency sponsoring the co-ordinating group. It is normal for growth-oriented economic programs to receive the endorsement of donor countries by pledges of higher volumes of assistance. However, in these analyses, the World Bank and the International Monetary Fund, which have been responsible for sponsoring most of the co-ordinating groups, emphasize the impact of domestic policies on private enterprise, the operation of market mechanisms, the promotion of private investment both domestic and foreign, all of which are important for the creation of a capitalist society. It is relevant to question whether much of this is applicable to a society that is backward and based for the most part on a subsistence economy. Even the World Bank has now modified its position on the pursuit of growth-oriented development and has over the last few years turned its attention to basic human needs such as nutrition, health care, education and housing by its support for integrated rural development projects. But nevertheless, the orientation and thinking of these institutions are based on the operations of the market place. For example, subsidies are often an integral part of government programs for the distribution of the basic necessities to the masses in developing countries and this is anathema to these institutions and no opportunity is lost to pressure developing countries to elimiate them in the interests of increasing investment for growth. A recent example was the attempt by the Government of the Arab Republic of Egypt to remove subsidies on a series of basic necessities as part of a Standby Agreement with the International Monetary Fund signed in 1977, and it led to widescale disturbance in Cairo and finally of the withdrawal of the measures.

No one could really quarrel with the prescription made to divert more resources for investment in the interest of achieving higher growth rates, but it has to be understood that such policies often have to be implemented within the framework of democratic political institutions. The pressures such systems exert on the political leaders in developing countries can never be understood by Western societies and it is largely brought about by the access that people have to the political leadership in these countries. In such a situation the elimination of subsidies and other welfare-oriented policies have to be gradual and implemented with the full support of the masses. Otherwise these pressures can only be controlled by changing the political systems to autocratic ones, employing repressive tactics. This again is unacceptable to the Western societies, which emphasize, as U.S. President Carter's human rights program does, human liberties and this is an area of conflict based on different conceptions of political institutions and the process of development.

Specific Policies Insisted Upon

The need for sound economic policies as a general precondition for providing foreign assistance cannot be questioned as it is in the interest of the recipient country to use the additional resources generated through foreign aid programs as effectively as possible. But nevertheless, one questions the need for specific economic policies that are insisted upon by donor countries before providing aid. Here I would draw a distinction between commodity assistance and project assistance. In the former, sound overall economic policies are more justifiable preconditions than in the latter where the feasibility of the project and its priority in the country's development plan should be the main concern. The need for project assistance should be judged on the merits of the proposal rather than the overall framework of economic policies or the political institutions under which these policies are being implemented.

An additional cost to a recipient in the case of project aid is the need to hire foreign consulting firms to execute projects, the cost of which are debited to the loans, to satisfy the donor countries regarding their implementation. This often leads to the justifiable accusation of neocolonialism against the donor as many developing countries possess qualified technical personnel to supervise the implementation of projects, though they may lack the experience of working as a team within the framework of a consultancy organization. In a similar way the practice of the World Bank and the Fund in placing staff in developing countries to monitor the implementation of programs is questionable.

One important aspect of the leverage effects is that often the preconditions imposed impinge on the sovereignty of developing countries. Here, I would like to use an example from Sri Lanka where in early 1970 the World Bank provided assistance for a major diversion project and insisted on including two clauses that were objectionable; first, that that Government appoint as the Chief Executive and the Deputy of the statutory body responsible for the project, persons who were both competent and experienced and acceptable to the Bank; and second, that prior approval of the Bank be obtained before changing any legislation governing the statutory body. This agreement created serious political problems in the country and became a major issue in the general election that year. The Government that negotiated the loan agreement was defeated and the new Government renegotiated these clauses, which were subsequently deleted and substituted by clauses whereby the Government undertook to merely inform the Bank of changes in the management and legislation.

One would have expected these experiences to have settled the issue for all time as far as Sri Lanka was concerned but it came up once again two years later with the Asian Development Bank. The ADB is, after all, a regional institution and is expected to be more sympathetic towards the aspirations of Third World countries. Nevertheless, they insisted on consultation when changes in top management of another statutory body was contemplated as a precondition for providing assistance. Explanations to the negotiating team of the experience with the World Bank on the diversion project proved to be of no avail and the Government broke off negotiations, which was the first occasion in the history of the Bank, up to the time, that a recipient country had taken such action. Subsequently, negotiations were resumed and the offending clause deleted by the substitution of a Side Letter whereby the Government undertook to inform the Asian Development Bank of any proposed changes in the top management.

These are particular instances but they nevertheless point to the need for recipient countries to be constantly aware of the danger of acceding to such conditions as they constrain the recipient to a course of action that is both unpalatable internally as well as being a commitment made for a long period of time.

SACRIFICE OF LONG-TERM DEVELOPMENT OBJECTIVES

The rationale for negotiating foreign aid is to increase the import capacity to a level necessary to achieve a given rate of growth as laid down in the country's development plan. At the same time, it often enables the recipient to avoid taking harsh economic decisions that would be politically unpalatable in the short run. One could provide examples of cases where actions to curtail imports of agricultural products could develop the capacity to grow these items locally. In the short run, the internal prices rise and provide the necessary incentives to increase production locally but at the same time the increase in prices leads to demands for high wages, which, if granted, could set off an inflationary spiral. However, the availability of foreign aid in the form of agricultural products that can be grown locally or cash grants that would enable the importation of these items sacrifices the long-term development interests of the country because of the predisposition of many governments to reduce internal prices for short-term political gains. One could point to similar examples in the other sectors but the adverse effect is most often felt in the agricultural sector.

Food aid, whether provided under emergency conditions such as famines and natural disasters or provided for balance of payments reasons, has an impact on domestic production in recipient countries. Emergency food aid is a necessary response of the international community to meet national disasters such as famine, earthquakes, etc. Nevertheless, there are examples of cases where due to a lack of coordination amongst donors or an inadequate assessment of needs to overcome such disasters, the farming communities in the disaster areas have been adversely affected. The uncoordinated efforts in the Sahel and in Bangaladesh are now historical facts. A recent example quoted in the New York Times of 6 November 1977 relates the experience of Guatemala, which received emergency food supplies from the United States after the earthquake in 1976. At the time of the disaster, most agencies operating in the country recognized that adequate supplies of food were available but building materials were in short supply. In spite of this assessment, food aid arrived and damaged the financial prospects of the small individual farmers living in the highlands of Guatemala City who found the prices for their produce had declined sharply due to the availability of aid supplies. It had the further adverse effect of weakening the financial structure of farmer cooperatives in these highlands regions and is a good example of aid sent with the best of intentions, but misplaced and damaging to the recipient because advice from the local level was not accepted.

If one looks at the food aid provided as balance of payments support a similar situation emerges. It represents surplus stock purchased from aid allocations at high prices due to the support provided by donor governments internally to agricultural products. The consumer in the donor country often pays more because of aid purchases, which are added to the demand of consumers in donor countries. These food supplies are then sold in the recipient country reducing the prices of local supplies and substitutes, thereby damaging the long-term interests of farming communities in recipient countries whilst benefiting the urban consumers. If one looks at the entire picture from the source of production in the donor country to the consumer in the recipient country, it is the farmer in the donor country and the urban consumer in the recipient country who benefit at the expense of the consumer in the donor country and the farmer in the recipient country. Clearly, this does not promote development in the Third World, although food aid provided in this manner affords immediate balance of payment relief to recipient countries. It is not in their long-term interests to rely on food aid on a continuing basis, year after year.

Here again, I would like to quote an example from Sri Lanka whose staple food is rice. There have been numerous attempts made to grow other food crops such as sorghum, maize, millet, cassava, and yams, but in the past, these efforts have been launched during periods of drought as an emergency measure to switch consumption from rice to other cereals that require less water for production. Such a situation arose in the financial year 1974-75 and due to the lack of rain during the period preceding the main cultivation season it was abundantly clear that there would be a substantial shortfall in the local production of rice. Faced with this situation, the Government launched a major production program to encourage farmers to grow other food crops and due to balance of payments difficulties during this period, the distribution of imported wheat flour was also restricted. Around March 1975, the US offered 100,000 tons of wheat flour, which they asked the Government of Sri Lanka to ship before the end of the fiscal year on 30 June 1975. In anticipation of these additional supplies, the Government of Sri Lanka liberalized the distribution of flour from the month of April 1975 onward, as this coincided with a festival period in the country. This was unfortunately the harvest period for the other food crops that had been grown and the farmers suffered catastrophic losses in income. A major extension effort by the Agriculture Department received a setback as the farmers required considerable persuasion to grow these other crops and the country's long-term development prospects were seriously damaged.

Conclusion

In dealing with this subject under five headings, I have not assigned any priorities to them. The repayment burden is the one that persons interested in international development are familiar with and it is readily quantifiable. Nevertheless, the others are real costs that reduce the value of foreign aid to the recipient. Perhaps I have introduced a note of pessimism to the foreign aid effort, but my main purpose is to draw attention to the need to improve the qualitative aspects of aid, at a time when the volume of resource transfers is increasing sharply. Both aspects are important and should continue to receive the attention of the international community in the interests of Third World development.

A Future for Sri Lanka's Desiccated Coconut Industry

S. A. C. M. Zuhyle

The declining trend in desiccated coconut production, while market prices kept rising, has been a clear indicator of the crisis that beset Sri Lanka's coconut industry. The obvious solution is to eliminate the problems that retarded increased production, argues S. A. C. M. Zuhyle who is an assistant manager at the Coconut Processing Board in Colombo.

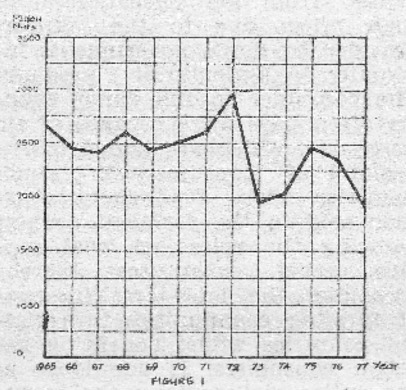
Coconut production has been fluctuating between 2,400 and 2,700 million nuts per year with the unusual increase to 2,963 million nuts in 1972, to a drop of 2,031 million in 1974 and an exceptional 1,825 million nuts in 1977 owing to a record drop in output. The fluctuation in production is characterised by weather conditions, variations in the application of fertiliser and foreign market conditions for exportable coconut products such as desiccated coconut, fibre, oil, charcoal and copra. Both 1972 and 1974 had been remarkably unusual years. Within the period 1965-77 due to favourable weather conditions that prevailed in 1971 and the substantial fertilizer application on coconut lands in 1972, nut production increased to a record figure of 2,963 million nuts. On the contrary, the steep drop to the level of 2,031 million nuts in 1974 was characterised by the drought that prevailed in that year, and the negligence of the estates by management, on the eve of nationalization of the estates which were brought under the Land Reform Commission.

It is clear, as illustrated in figure 1, that the trend line is declining, which indicates a falling production.

Following the trend, the nut production for 1980 and 1990 could be estimated at 2,374 and 2,230 million nuts respectively. Comparing the forecasted figures with the actual production figures of 1975 (2,447 million), a drop of 3 per cent in 1980 and a 9 per cent drop in 1990 is expected. This fact has to be considered against the increasing local consumption by our growing population.

LOCAL CONSUMPTION

Local consumption of coconut is estimated to be 125 nuts per person per annum. Considering the population projections for the future (based on a study by Gavin W. Jones & S. Selvaratnam) the projected consumption of coconuts for the period 1973-1990 must steadily increase. On the same basis the percentage of domestic consumption of nuts in 1980 is estimated to increase to 71.5 per cent of total production and in 1990 it would be 79 per cent of total production which would leave only 28.5 per cent in 1980 and 21 per cent in 1990 for the purpose of industrial production and export. If the decline in the availability of nuts (for industrial purposes) is left unchecked, it would result in a serious curtailment of desiccated coconut production thereby directly affecting the country's exports.



Coconut Production in Sri Lanka 1965 — 1977

D.C. EXPORTS

Sri Lanka desiccated coconut is mainly exported to the continental market while the U.S.A. market is monopolised by the Philippines. (1977 witnessed a dramatic breakthrough by the Philippines with the U.K. and European markets as the recent data shows. A large part of the usual demand that Sri Lanka was unable to meet was captured by the Philippines). In terms of quantity, 65 — 70 per cent of the purchases are generally made by the principal buyers in Western Europe such as the United Kingdom, the Federal Republic of Germany, France, Netherlands and Spain. However, the variations in market conditions in such countries seriously affect the local desiccated coconut trade due to this concentration and dependence on only these markets. When the contracted buyer decides to purchase less, say due to increase in the price of sugar — (i.e. sugar is a complementary item for the end-use of desiccated coconut), our sales naturally drop. To a large extent therefore, the Sri Lanka desiccated coconut industry is at the mercy of these purchasing countries. For example, in 1975, when Australia decided to purchase most of its desiccated coconut from the Philippines for internal reasons, our sales there dropped from 1,321 long tons in 1974 to 183 long tons in 1975.

Due to various governing factors, such as market conditions, variations in demand for confectionery in the buyer countries etc., the world desiccated coconut export market varies. However, apart from the world market conditions the local conditions such as the availability of nuts, (depending on the nut production) and conditions in the consuming countries of our desiccated coconut, exports had been fluctuating between 300-400 million nuts (converted to nut equivalent on the basis of 300 lbs. per 1,000 nuts — though the out-turn per 1,000 nuts varies, depending on the seasonality and on a regional basis, an average of 300 lbs is observed to be a justifiable rate). Considering the thirteen year period 1965—1977, one could observe an exceptional rise up to 517 million nuts in 1968 and an unusual drop of 285 million nuts in 1973.

The highest ever export of desiccated coconut, approximately 70,000 tons, bringing in about Rs. 164 million and contributing a then record foreign exchange earnings in 1968, was indeed an unusual occurance. (The Rs. 323 million earned in 1977 was also an exceptional occurance). The unusual situation in 1968 was caused by the unfavourable weather conditions in Philippines in that year resulting in a short supply of coconuts. As a result the principal buyer of Philippine desiccated coconut, the United States, purchased 13,000 cwts. of desiccated coconut from Sri Lanka while due to increased demand, Canada and the European countries too purchased increased quantities. (This situation appears to have been reversed, in favour of the Philippines, in the U.K. and European markets in 1977).

The lowest ever production of 38,000 tons of desiccated coconut in 1973, was a severe set-back caused by the prolonged drought in 1972 and the curtailment in the application of fertilizer. The coconut pest

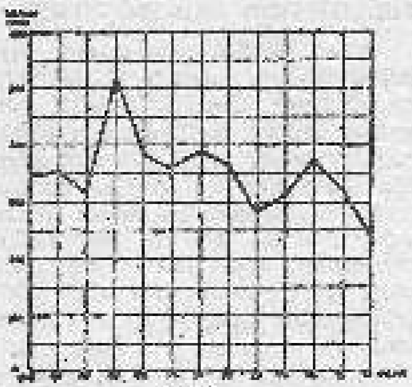


Figure 2

Desiccated Coconut Exports by Volume
1965 — 1977
(Nut equivalent in million nuts)

which attacked the plantations also caused a drop in nut production which in turn affected desiccated coconut production. Yet, in this particular year the low volume of desiccated coconut produced did not affect foreign exchange earnings which remained as high as Rs. 119 million. Apart from these two unusual years the production on the whole shows a declining trend and the future of the exports, according to the present trends, could be a threat to the entire coconut industry.

The fluctuation in export performance and declining trend is pictorially shown in figure 2. From this trend it could be estimated that desiccated coconut exports in 1980 and 1990 would be 323.9 and 293.9 million nuts respectively. These estimated figures with 1975 exports reveal approximately a 12 per cent drop in 1980 and a 21 per cent drop in 1990 which is a dangerous declining rate from the point of view of the industry.

Table I SRI LANKA EXPORT OF DESICCATED COCONUTS
(nut equivalent in million nuts) — 1965—1977

Year	1965	1966	1967	1968	1969	1970	1971	1972	1973	1974	1975	1976	1977
Quantity	345	362	316	317	382	300	300	287	265	316	375	315	240

MARKET PRICE OF DESICCATED COCONUT

The export prices for the Sri Lanka desiccated coconut has been fluctuating on an upward trend. Apart from times of exceptionally varying market conditions it has always shown this rising trend since 1968.

Table II AVERAGE MARKET PRICE PER POUND OF DESICCATED COCONUT
(1965 — 1977)

Year	1965	1966	1967	1968	1969	1970	1971	1972	1973	1974	1975	1976	1977
Price per lb. Rs. cts.	.52	.47	.42	.79	.56	.64	.67	.71	.80	1.41	.90	1.57	2.88

Considering the movements of prices over the years one could observe that desiccated coconut prices are in an upward trend with attractive prospects in the future; yet falling nut production, as observed earlier, poses a threat to the upward trend in earnings.

two major exporting countries. This trend is characterised by the increasing demand in the buyer countries. But as it was noted earlier there is a contrasting picture in that the local export of desiccated coconut has been on the decline over the years. If the necessary steps are taken, however, the declining local production trend could be arrested and production geared to meet increasing world demand.

PRODUCTION CAPACITY

The desiccated coconut industry is mainly located in the coconut triangle with about 83 out of 86 mills being located in that area.

Table III DESICCATED COCONUT EXPORTS OF SRI LANKA AND THE PHILIPPINES (in nut equivalents) — (1965 — 1977)

Year	1965	1966	1967	1968	1969	1970	1971	1972	1973	1974	1975	1976	1977
Exports in nut equivalents (million nuts)	840	850	780	1052	752	807	815	847	880	790	867	882	968

A study of the Sri Lanka's desiccated coconut production and exports would be incomplete if not compared with the trend of the other major exporting country Philippines. Market conditions, such as demand for desiccated coconut, production and supply etc., is a determining factor for Sri Lanka exports. Nevertheless, the trend of the world production is also undoubtedly an influencing factor. For a complete study and forecast of the future of desiccated coconut in Sri Lanka, the trend of the combined Sri Lanka-Philippines production, as shown in Table 3, is of much relevance.

Considering the trend line of exports of both major desiccated coconut producing countries the possible increase of exports for 1980 and 1990 is 982.4 and 1,132.4 million nuts respectively, which shows a steady increase in exports by the

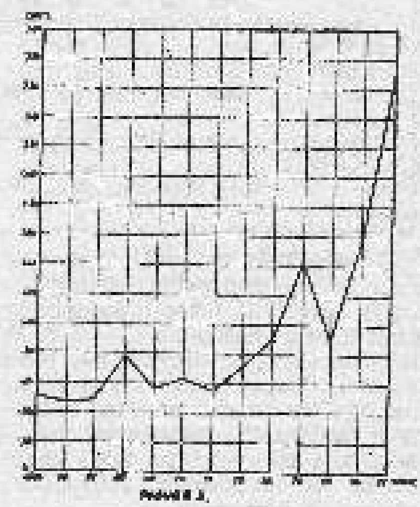


Figure 3.

Market Price of Desiccated Coconut
— Average price, rupees per lb.
1965 — 1977

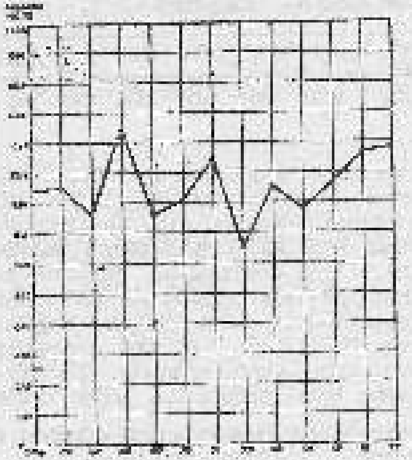


FIGURE A.

Desiccated Coconut Exports of Sri Lanka and the Philippines 1965 — 1977
(Nut equivalent in million nuts)

Though most of the desiccated coconut mills are conveniently located in the coconut growing area, the mills are never worked at maximum capacity. If maximum utility is obtained at a reasonable estimation of 230 days work per year, 73,000 tons of desiccated coconut could be manufactured (computed on the basis of an out-turn of 300 lbs. of desiccated coconut per 1000 nuts.) The total nut requirement would be approximately 545 million per annum. The actual production from 1965-77 had been far below the maximum capacity.

The principal machinery used in the desiccated coconut mills are largely those desiccators which were discarded from the tea factories (except for a few mills which are using driers). As such, the machinery constantly breaks down and the managements face difficulties in obtaining spare parts which are not readily available in the market. Hence, the parts have to be turned out or searched for among the dismantled machines. This process involves a loss of several days work and contributes to a curtailment in production.

A good part of the coconut production gets transferred to the local consumption market since coconut production is heavily subject to seasonal fluctuations during the unfavourable (lean) seasons. During the lean period, coconuts fetch a very high price and as such, purchasing nuts at high prices becomes uneconomical for mill operators. Moreover, among the buyer countries desiccated coconut fetches a very high price during a particular season and at other times prices remain low. When desiccated coconut prices are low and nut prices are high it becomes more economical for the miller to either close down the mill or minimise his operations.

Administrative difficulties, labour problems etc., though not seasonal

Table IV D.C. PRODUCTION AND PERCENTAGE OF TOTAL ESTIMATED CAPACITY PRODUCED

Year	1965	'66	'67	'68	'69	'70	'71	'72	'73	'74	'75	'76	'77
D.C. Prod: in nut. equiv. m. nuts	345	332	315	517	382	367	390	367	288	315	375	345	240
% of the total capacity	63	68	58	94	70	66	72	67	52	58	69	63	44

It was only in 1968 that the boom for the desiccated coconut industry occurred where production reached near maximum capacity. At all other times production has been less than 75 per cent of full capacity. The desiccated coconut industry is faced with a number of drawbacks and as such, the mills could not be in continuous production. Some such handicaps are:

1. Bad machinery;
2. Uneconomic operation;
3. Administrative difficulties;
4. Labour problems.

or regular are other factors which affect production. For an increase in production one of the fundamental requirements is satisfactory mechanical working of machinery which could be achieved by modernising the existing machinery.

Another conditional factor for increase of production is the expansion of the market. The hitherto hardly tapped markets for Sri Lanka such as the U.S.A. and the Middle East countries can make a substantial contribution with regards to this aspect. Producing desiccated coconut according to the requirements of these countries would enable market expansion, particularly in the case of the United States market where extremely high hygienic standards are required. Production in conformation to these requirements would help increase production, utilizing the presently un-utilised capacity.

LAND EXTENT UNDER COCONUT CULTIVATION AND ITS UTILITY

The coconut plantations are mainly concentrated in the so called 'Coconut Triangle' (with the apexes Chilaw, Negombo and Kurunegala) which also extends along the coast line up to Hambantota, and are scattered in blocks in the eastern coast and in the Jaffna peninsula. Apart from these, small plots are sprinkled over some parts of the central highlands as a mixed crop.

According to the 1962 Agricultural Survey Report, the extent under coconut cultivation as at 1st July 1962 was 1,152,418 acres. The breakdown is as follows: —

Holdings under 50 acres — 843,626 acres
Holdings of 50 acres and above — 308,792 acres

This was one of the only reliable estimates of the extent of acreage available. Subsequently certain amounts of land have been brought under cultivation while certain coconut lands have been taken up for road construction, building sites, overhead wiring etc. On the other hand 20,000 acres of uneconomic citronella lands and 20,000 acres under colonization schemes have been brought under cultivation. The acreage added to the coconut cultivation is not sufficient to offset the land that has gone out of production. Hence the existing land keeps contracting. Further the last five year plan did not provide for an increase in the acreage under cultivation and according to the plan the existing acreage at 1,150,000 was given as a stable figure.

NUT EQUIVALENT OF EXPORTS

The quantity of desiccated coconut manufactured out of 1,000 coconuts varies from season to season, regional wise. During the lean period the out-turn per 1,000 nuts is greater than in the season when the crops are high in yield. Regionally coast line estate nuts are larger and provide a higher poundage than those of the interior lands. On this basis it has been observed that the out-turn per 1,000 nuts varies from about 280 lbs. to 350 lbs. Hence for purposes of computation of relative figures, for desiccated coconut, poundage per 1,000 nuts is rated as 300.

On this basis is also computed the estimated nut equivalent of desiccated coconut exported from 1965-77, as shown in Table V below.

either intensive or extensive cultivation, particularly the high yielding hybrid varieties. Such an action, and immediate action, would help to meet the increasing demand for desiccated coconut and enable Sri Lanka to remain a strong partner or competitor in the world desiccated coconut export market.

RELATED ECONOMIC AVTIVITIES

By-products of the desiccated coconut industry namely, shell charcoal and parings contribute a considerable amount to the economy.

exported except for a small portion which is retained for local industry.

Copra is another product which has necessarily come to stay with desiccated coconut production. As a result the high quality requirements for desiccated coconut, laid down in regulations by the Coconut Processing Board, all the coconuts purchased for processing could not be utilised for making D.C. In the case of nuts which are germinated or split open, if the possibility of contamination exists, such nuts are not permitted in production of desiccated coconut. Such rejections total up to a considerable quantity in desiccated coconut mills each day and they are sent for copra curing and oil milling.

Table V COCONUT PRODUCTION IN RELATION TO DESICCATED COCONUT EXPORTS

Year	1965	'66	'67	'68	'69	'70	'71	'72	'73	'74	'75	'76	'77
Nut prod. in millions	2601	2465*	2431	2601	2440	2316	2610	2963	1940**	2032	2437	2330	1921
D.C. Equiv. in million nuts	345	353	315	517	392	360	390	387	295	315	275	345	240

Source: * Coconut Cultivation Board
** Central Bank of Ceylon

According to Coconut Research Board sources the national average production per acre is 2,500 nuts. Taking this standard into consideration we find that the quantity of desiccated coconut exported in the form of nut equivalents as obtained from the acreage of coconuts cultivated is given in Table VI.

From Table VI we find that approximately 150,000 acres of coconut land are directly feeding the desiccated coconut export market.

REPLANTATION

The increasing rate of consumption at 125 nuts per head per year, also taking into consideration the growing population, would leave little and possibly no hope for exporting desiccated coconut in the 1990's. The only possible solution for the challenging phenomena is

my. While shell charcoal is exported in raw form and also in the form of activated carbon, parings is made use of for the manufacture of oil which is mainly used up by the soap industry, and the poonac received from this is utilized for the manufacture of poultry and cattle food. Fibre processing is another industry which goes hand in hand with the desiccated coconut industry. Though fibre mills do not necessarily operate alongside desiccated coconut mills, in some cases the fibre mills are located in the desiccated coconut manufacturing areas. The husks of the nuts which are used in desiccated coconut manufacture, find their way into the fibre mills where they are processed into various grades such as hackled, bristle, mattress and omit fibre. All these fibre products are

Most of the desiccated coconut mills in the island also have set up an oil mill which process all copra obtained from the rejected nuts and the parings. Copra unlike parings is graded into No 1 and No. 2.

Oil extracted from No. 1 is either used for export purposes or for local consumption while the oil manufactured from No. 2 copra is sold in the local market for domestic use and sometimes for the purposes of soap manufacture and other industrial uses.

Another by-product obtained comes in the form of coconut water which otherwise goes waste. The

Table VI ACREAGE CULTIVATED AND EXPORTS OF DESICCATED COCONUT

Year	1965	66	67	68	69	70	71	72	73	74	75	76	77
D.C. Export (nut equiv)	345	353	315	517	392	360	390	387	295	315	275	346	240
Acreage expected (in '000s)	138	149.9	186	306.8	152.8	144	166	146.8	114	126	150	138	96

water is collected in a tank and left for a few weeks. Out of the sediment oil is extracted. This oil is really not obtained from water, but from the oil in the water. Such oil is used by the small soap manufacturers while the refuse which is called the "sediment poonac" is used as poultry food. The by-products of the desiccated coconut industry do not only contribute in large measure to the economy, but also generate many economic activities in the areas where the desiccated coconut mills are located.

The industrial processing of the above coconut shell products has become a major export industry in recent years with about 25,000 to 30,000 metric tons of these items being manufactured each year to meet the country's growing export demand. Coconut shell charcoal is the most important of these by-products, accounting for nearly Rs. 21 millions in foreign exchange earnings in 1977.

The local shell supplies come mainly from the DC industry while a small percentage is supplied by the copra manufacturers. About 10 to 15 percent of the total 600 million shells supplied is used up by domestic demands, mainly for fuel purposes, while the balance 80 to 85 percent is fully absorbed by the export trade.

The desiccated coconut industry as stated earlier employs a large amount of old machinery. As such, the maintenance and repair activities are very high. Hence this industry generates a considerable amount of mechanical engineering activities and certain establishments are now specialising in the mechanical activities related to the industry.

FOREIGN EXCHANGE EARNINGS

Coconut is the third largest foreign exchange earning cash crop of Sri Lanka and contributes significantly by means of its various industrial processing activities such as D.C. fibre, oil and charcoal manufacture. Unlike the other products of the coconut industry, however, desiccated coconut has always been contributing a steady percentage of the foreign exchange earnings. Except for the boom year of 1968 and a very favourable year in 1974, the contribution made to the foreign exchange earnings has been consistent at 4—5 per cent.

The increase in production of 25 per cent would result in a considerable increase in the amount of foreign exchange earnings.

CONCLUSION

Over the years the desiccated coconut industry has come to stay as an established part of our industrial sector. This industry, concentrated in the coconut triangle, has many tangible effects on the economy of the country. Foremost is that desiccated coconut exports are bringing substantial and steady foreign exchange earnings into the country. In addition to its own contribution of about 4½ per cent of the total foreign exchange earnings it also contributes by means of its earnings from the by-products earnings from charcoal, activated carbon, fibre, oil and copra to contribute a sizeable portion of the country's foreign exchange earnings. The desiccated coconut industry and the other charcoal, fibre and oil industries located in the coconut triangle generate further economic activities to a considerable degree. Many of the areas in which these industries are located are observed to be areas of "full employment" where most employable persons are directly or indirectly engaged in the activities of these industries.

The desiccated coconut industry which has provided a wide range of socio-economic benefits needs greater attention. It has been observed that coconut production is on the decline and on current estimates by 1980 and 1990 only about 28.5 per cent and 21 per cent respectively of local production would be available for industrial purposes. The effect of declining nut production is matched with the declining export of desiccated coconut; in nut equivalent terms in 1980 this is estimated to be 328.9 million nuts and in 1990 to be 293.9 million nuts.

Table VII FOREIGN EXCHANGE CONTRIBUTIONS FROM DESICCATED COCONUT EXPORTS

Year	1965	66	67	68	69	70	71	72	73	74	75	76	77
% of country's total export earnings	4	4	4	8	5	5	5	4	4	7	5	4	5

The declining nut production and consequently desiccated coconut production presents a contrasting picture when compared with the upward market price of desiccated coconut over the period under review. The satisfactory upward trend in prices could be coupled with the increasing demand in international markets and exports, particularly of the Philippines. It may thus be observed that the world market is becoming a promising place for the desiccated coconut trade while local conditions are not satisfactorily geared to meet the world demand and tap fully the available resources.

By the beginning of this year trade circles felt strongly that Sri Lanka's export trade in desiccated coconut, despite the high unit price earned in 1977, had reached a stage requiring immediate action to ensure its survival. Until about 1969 Sri Lanka exported almost the same volume of desiccated coconut as the Philippines, but thereafter this declined and in 1977 Sri Lanka's exports were only about 30 percent of those of the Philippines, and her total earnings were 40 percent lower compared to the Philippines. The trade was of the view that as long as Sri Lanka remains a marginal supplier, merely to bridge the gap between international demand and supply, a high unit price is assured for her produce. But the Philippines and other newly emerging suppliers will before long increase their supply to wipe out the gap between demand and supply and there will be no need for marginal suppliers to participate in the trade.

One solution to meeting the increasing demand and maximising our foreign exchange earnings in what would turn out to be a very competitive market is to launch a programme for steadily increasing nut production over the years to come and feeding the desiccated coconut mills with more industrial grade coconuts. An increase in production within the limited resources available would be possible only by means of intensive cultivation with a high yielding variety of coconuts.

A Case for Up-dating Banking Legislation and/or Practice Regarding Collection of Cheques

R. Suntheralingam

Mr. Suntheralingam, who has several years of practical experience as a manager in the People's Bank, expresses his personal suggestions here on measures to facilitate collection of cheques. It is emphasised that these opinions are not those of the People's Bank or in any way the official viewpoint. The two footnotes are not those of the author but are the views of authoritative persons who have discussed Mr. Suntheralingam's suggestions. They are included at the end of this paper with the hope that they would stimulate the discussion on this subject.

Among the many services Banks are called upon to perform, one of the traditional services is collection of instruments for payment to customers' accounts, largely in the form of cheques. When customers of a Bank deposit cheques drawn on other Banks (or on itself too) this Bank serves as a collecting agent or if it had already given value for the cheques the Bank functions as a Collecting Banker.

The Bills of Exchange Act of 1882 in England and its parallel Act in our country gives protection to the paying bank under its provisions when the Bank acts in the bonafide capacity and pays the Collecting Banker. The relevant sections of both these Acts is quoted below:

"When the Banker on whom a crossed cheque is drawn in good faith and without negligence pays it, if crossed generally, to a Banker and if crossed especially, to the Banker to whom it is crossed or his Agent for collection being a banker, the Banker paying the cheque and if the cheque has come into the hands of the payee, the drawer, shall respectively be entitled to the same right and be placed in the same position as if payment of the cheque had been made to the true owner thereof".

This is the current legal position in our country.

Before we proceed further, let us analyse the customer content and the type of work and responsibility involved in the collection of cheques.

The Banking sector in our country is at present composed of the two state-owned Banks (Bank of Ceylon and People's Bank), branches of six Foreign Banks, one locally owned Commercial Bank and a Commercial Bank with mixed ownership.

The Banking sector caters to the following sections in our economy — the Government sector, the Co-operative sector, the Corporation sector and the private sector. The last one is composed of big business establishments, petty traders, craftsmen, etc, and individuals who have accounts which are termed personal accounts.

Though statistically it may not be possible to prove by direct reference, it is true to say that the Government sector, Government sponsored sector, Co-operative sector and big business (business managed by professionals) are the major customers of the Bank. The major part of the work is handled on their behalf.

When cheques drawn on other Banks are deposited by the customers, the Collecting Banks are expected to collect the proceeds as expeditiously as possible. Cheques are deposited by the customers either over the counter or by mail. Either way the cheques have to be received, acknowledged, and scrutinised. Here the scrutiny is not done as is done by the paying Banker. As for the Collecting banker, among other things, the major question that has to be resolved is that of conversation; i.e. legally defined as "wrongful interception of goods belonging to another" or alternatively as "an unauthorised act which deprives another of his property permanently or for an indefinite time". In layman's language, a cheque ostensibly meant for 'A' should not be credited to 'B' even if 'B' comes into possession and presents it however long-standing and honourable a customer 'B' may be. When the Banker scrutinizes, he sees to it that he does not collect a cheque purportedly meant for 'B' into 'A's account.

Once the officer is satisfied as to the existence of reasonable grounds to believe that there is no obvious attempt at conversion, he guarantees the fate of proceeds wherever relevant. Suppose the cheque is a direct credit, i.e, the cheque is drawn payable to 'A' and he is called upon to collect the proceeds to the credit of 'A's account, he assures the paying banker that the proceeds will be credited or if he intends crediting it before the fate is known or before the lapse of the number of days of waiting, then he assures in the form of a confirmation that the payee's account has been credited. In case of a negotiated cheque it is at the most on the assurance of the beneficiary customer, preferably on the guarantee of another disinterested customer, that the collecting Banker guarantees the fate and uses the obvious words to that effect. The signature is placed on the reverse of the cheque, in the appropriate places stamped, and the credit voucher or slip is also signed in the appropriate place.

These cheques, looking at it from the point of view of a Branch in Colombo, would consist of broadly speaking cheques drawn in Colombo branches and cheques drawn on outstation branches.

Cheques drawn on Colombo branches have to be cleared through the Central Clearing chaired by the Central Bank. This is done twice a day. All cheques received upto — say 10 a.m, or thereabout — will be sent to the Central Clearing around 11 a.m. on the same day and all others will be sent on the morning before 8 a.m. the succeeding day.

The Colombo cheques received unto 10 a.m. if they are to be expeditiously cleared, must be sent that day by 11 a.m. In order to do that the Bank has to receive, acknowledge, scrutinise, guarantee fate, sort them, list them, tally them, schedule them and be in time at the Central Clearing lest the Bank staff be "shut out". Outstation cheques have to go through the same process and be ready to catch the post by 2 p.m. the latest.

This rush exists because, though the Bank is legally entitled to keep the cheque for an additional day, it opts to clear it the same day to be of invaluable service to its customers. The major delay is caused by the necessity for satisfying the conditions regarding guaranteeing the fate, assuming that the other contributory factors such as sufficient staff and machinery are available. Statistically speaking the number of cheques handled by the Banks in the process of collection of cheques is not readily available. A crude attempt has been made to arrive at the dimensions involved by taking a sample of the number of cheques handled over a period of five consecutive days by one of the Branches of the People's Bank situated in Colombo which may be regarded as one of the largest Branches. This, in no way will reflect the full effect of the amount of work involved but would at least give an indication of the number of signatures the officers are called upon to place, and if necessary sanction were granted, the amount of time that could be saved and thus enable the expeditious collection of cheques. (See Table).

Is there a necessity for the collecting Banker to guarantee the fate of cheques? The paying Bank's responsibility ends when that Bank pays the collecting Bank. They need not and cannot keep track of the fate of the proceeds thereafter. That is the factual as well as the legal position. In such a situation why should there be a time consuming practice of guaranteeing the fate of proceeds.

The relevant Section 80 of the Bill of Exchange Act 1882 quoted above spells out the position clearly.

In the United Kingdom the Cheques Act 1957 sought to dispense with the necessity for endorsement but succeeded in achieving one thing, it dispensed with the necessity for calling for endorsement and of guaranteeing of fate when the cheque is credited to the payee's account.

COLLECTION OF CHEQUES FOR FIVE DAYS

	COLOMBO CLEARING		OUTSTATION CLEARING		TOTAL COLLECTION	
Date (1)	No. of Cheques (2)	Amount (3)	No. of Cheques (4)	Amount (5)	No. of Cheques (6)	Amount (7)
					(2+4)	(3+5)
78.05.29	1,927	28,859,052.20	1,512	7,349,163.72	3,439	36,208,215.92
78.05.30	1,802	7,224,028.72	972	6,390,766.48	2,774	13,315,993.85
78.05.31	2,154	10,708,076.40	1,827	7,607,917.45	3,981	18,315,993.85
78.06.01	2,512	22,081,885.69	1,923	6,707,138.13	4,435	28,789,023.82
78.06.02	2,421	47,665,142.01	1,451	5,029,625.99	3,872	52,694,768.00
Total	10,816	116,538,185.02	7,685	33,084,611.77	18,501	149,622,796.79

The Authority on Commercial Banking (Sheldon) summarises the position as follows:

"The Cheques Act 1957 (and certain statutory instruments) do not mitigate the severity of this position (i.e. need for endorsement) but they do take the vast majority of cheques and indeed the vast majority of Banking instruments outside their purview. The paying Banker does not incur any liability by reason only of the absence of or irregularity in endorsement (Section 1, 2) and the collecting Banker is no longer negligent by reason only of his failure to concern himself with the absence of or irregularity in endorsement of an instrument".

The relevant section of the Cheques Act 1957 are quoted below:

Paying Banker: Section 1 (1)

When a Bank in good faith and in the ordinary course of business pays a cheque drawn on him which is not endorsed or is irregularly endorsed, he does not in doing so, incur any liability by reason only of the absence of or irregularity in endorsement and he is deemed to have paid it in due course.

Collecting Banker: Section (4) (3)

A Banker is not to be treated for the purpose of this section as having been negligent by reason only of his failure to concern himself with the absence of or irregularity in endorsement of an instrument.

Why should we emulate the English example? The reasons are not far to seek. First and foremost the bulk of the business of banking is done on account of the Government departments, Corporations, Co-operatives and big business. None of these organisations accept negotiated cheques in discharge of debts by whoever has dealings with them. In other words, cheques drawn in their favour; or their account only are made not negotiable. (The seemingly innocent long rope meant for the intrepid interceptor) and payable to them only are accepted by them. Again these cheques are credited to their respective accounts and not negotiated or transferred to other accounts. The cheques deposited by the National Savings Bank and other similar institutions too fall within this category.

The major time consuming work or chore that could be avoided is in the process of guaranteeing fate; other items of work like scrutinising, of vouchers, tallying, listing etc. cannot be avoided.

What is required now is to dispense with the necessity for perusal of the reverse of the cheques when the proceeds have to be credited to the account of the ostensible payee. If this is permitted the officers can dispense with the practice of guaranteeing fate when collecting cheques meant for the payee to the credit of the payees. In case of planned conversion by the customer the collecting Bank has recourse to its customer provided he has acted bonafide and without negligence.

From the point of view of the customers too, they need not waste their time writing credit instructions on the reverse of every cheque that is received.

It may not be out of place to quote the relevant extracts from the Circular dated 23rd September, 1957 issued by the Committee of London Clearing Bankers —

"Broadly the effect of the Act (i.e. the Cheques Act 1957) is that on and after that date paying Banks need not concern themselves with the endorsement or absence of endorsement upon any cheques or analogous instrument and the same applies to collecting banks unless ostensibly there is or has been, negotiation of the cheque or instrument for which purpose endorsement is still required". The intention of the Act is to relieve customers from the task of endorsing instruments which

TABLE III.	SPICE PRICES JANUARY — JUNE 1977—1978					
	Av. Public Auction Price Jan.—June 1977	Rs./Kgm. Jan.—June 1978	Av. F.O.B. Price Jan.—June 1977	Rs./Kgm. Jan—June 1978	Av. F.O.B. Price Jan.—June '77	(SDRs) Jan.—June 1978
Cinnamon	13.60	16.49	11.57	30.40	1.40	1.60
Cardamoms	211.47	202.88	165.45	278.33	17.85	14.64
Pepper	30.67	28.75	—	28.15	—	1.48
Cloves	80.73	117.00	44.54	72.64	4.80	3.82
Nutmeg	37.74	31.20	17.36	22.96	1.87	1.21
Mace	35.88	25.64	—	—	—	—

Source: Sunday Produce Reports and Customs Returns.

A case for updating....

(Continued from page 32)

are to be collected for the payee's account and to save them and the Banks the trouble caused by the return of a large number of such instruments for correct endorsement".

The time consuming process could be dispensed with if there is legal sanction by legislative enactment or even a decision or arrangements between the members of the Association of the Clearing Banks with the concurrence and approval of the Central Bank.

Apart from these legal issues that may arise, if the Banker is to dispose with the practice of examining the reverse of a cheque made payable to an account holder in a situation where the account holder has more than one account, crediting to a different account against the wishes of the account holder may lead to unnecessary litigation.

1. As regards Section 1 of the Cheques Act (1957) which has not yet been tried in courts, the authorities on banking law, while conceding that the object of the Act is to eliminate the need for endorsement, have pondered whether Section 1 protects against irregular endorsements only in cases in which it is not asked for but nevertheless appears. Where it is called for it would seem that the former protection under the Bills of Exchange Ordinance is still available. Where an endorsement is required it must still be regular for although the section gives protection in respect of an irregular endorsement, the instrument might not be considered paid in the ordinary course of business and it is doubtful if the section would be available. Since the banks have established a course of business and since this Section has not been tried and tested in the courts the question has been raised whether the established course should be departed from.

2. As far as Section 4 (3) which protects the collecting banker is concerned even this section has received little judical consideration. There have been doubts raised for instance as to the definition of true owner. Further the words used in Section 4 (1) (d) of the Cheques Act (1957) are sometimes at variance with Section 82 of the Bills of Exchange Ordinance. Some authorities have argued that there is nothing in the Cheques Act to show beyond doubt that the law has not been changed in this respect. With the advent of the Cheques Act the bankers position is still not free from doubt, by reason of the wording of Section 4 1 (b) there appears to be a confusion which did not exist before. This is made more difficult as the Act does not provide any definitions. There is, however, a People's Bank Circular 369/75 Addendum (1) — **General Instructions issued by the Bank** which states as follows:

> "Cheques crossed 'Account Payee Only' should also be honoured by the paying banker if they purport to have been correctly endorsed by the payees". However, where there is no evidence of 'Account Payee Only' crossing instructions being complied with, cheques should be returned unpaid calling for confirmation of fate of proceeds, from the Collecting Bank, Returning of such cheques calling for confirmation of fate should be regarded purely as a courtesy extended by the Paying Bank to the Collecting Bank'.

of clove exports. (Details in Table I).

The total value of spice exports in June 1978 amounted to Rs. 14.9 million. This brought the total earnings for the first half of the year to Rs. 123.3 million as against Rs. 72.3 million in the corresponding period in 1977. The increase of Rs. 51.0 million or 70.5 percent is reflected mainly in the increased earnings from the export of cinnamon quills whose contribution was Rs. 58.0 million or 47.2 percent of total spice export earnings during the period, despite a fall in export volume by 26 percent. Earnings from nutmeg and mace and cardamoms too recorded substantial increases of over 300 percent and 100 percent respectively over earnings during the same period last year. Earnings from pepper and cloves were around Rs. 20.0 million each amounting to approximately 32 percent of the total spice earnings.

Although in rupee terms the performance of Sri Lanka spices shows a major increase when evaluated in terms of SDRs (Special Drawing Rights), total earnings from spice exports amounted to SDRs 6.46 million during the first half of 1978, which amounts to a drop of 20 percent over the corresponding period in 1977. Further, in SDR terms the earnings from individual spices such as cinnamon dropped by 19.3 percent and of cloves by 68 percent. However, nutmeg and mace recorded an increase of 117 percent, primarily due to higher export volumes while cardamoms showed a small increase of 2.8 percent. (See table II).

Despite the sharp increase in export values of most spices recorded in rupee terms during the first half of 1978, in real terms there was a drop of almost 20 percent as against earnings from the corresponding period in 1977.

A fall in the price of spices in the world market during the year has further contributed to a drop in export earnings. Except for cinnamon all other spices recorded declines in their FOB prices (reflected by lower SDR values) this year as against prices during the first half of 1977. (Table III). If this trend continues export earnings from spices could decline appreciably this year. However, one can hope that during the next six months there would be an arrest in this downward trend and that by end of 1978 we would have recovered from this unfavourable situtíon.

Registered as a Newspaper at the G.P.O.

Price 2/25

Printed by the Associated Newspapers of Ceylon Ltd at Lake House, D. R. Wijewardene Mawatha, Colombo 10.