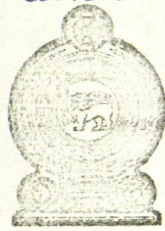


Subject filed on Sri Lanka : UK relations May 79



PRIME MINISTER'S
PERSONAL MESSAGE
SERIAL No. T 64 A/82

President of Sri Lanka

29th March, 1982

(Under cover letter 2.4.82)

My dear Prime Minister,

The 18th Meeting of the Sri Lanka Aid Group convenes in Tokyo on July 8th and 9th, 1982. At these meetings, the donor community and representatives of my Government participate in a frank exchange of views on Sri Lanka's economic situation and its external assistance needs. May I take this opportunity to thank you and your Government for the close interest you have shown in our development programs and the generous assistance you have rendered in support of them. We have found the views expressed by your delegation at past meetings very helpful in determining our priorities. This letter is intended to keep you personally informed of the impact of recent economic trends on our development strategy and on our external assistance needs. I trust that this will help you formulate your own development assistance programs to Sri Lanka in the light of our changing needs.

You will recall that during 1980 the economy had come under enormous pressure from a sharp deterioration in our terms of trade just when our development programs were acquiring momentum. Inflation rose sharply and our balance of payments position worsened. We responded to these developments through a series of stabilisation measures designed to reverse the trends that had set in during 1980.

The Rt. Hon. Margaret Thatcher, M.P.
Prime Minister,
United Kingdom of Great Britain
and Northern Ireland.

I will not burden you with the nature and details of these policies, since these have been described in documents circulated to you by my Government, the World Bank and the International Monetary Fund. What I do wish to indicate to you is that these stabilisation policies have met with success. The performance of the economy improved considerably during 1981 despite a further deterioration in our terms of trade, particularly in the form of unexpectedly low tea prices. The extent of the adjustment achieved in 1981 has been somewhat larger than we thought it possible to bring about. Strict budgetary discipline combined with substantial reductions in many of our development programs have enabled us to greatly reduce the size of the overall budget deficit and to decrease the dependence of the budget on inflationary bank borrowing. A more desirable budgetary outcome together with strict monetary and fiscal policies enabled a substantial reduction in the rate of inflation and a marked improvement in the balance of payments.

That this was achieved without any sacrifice in terms of economic growth, which recorded an increase of 5.8% was a considerable achievement. This turnaround enabled us to meet the Fund's performance criteria the final purchases under the SDR 260 Mn. arrangement. I understand Sri Lanka is one of the few countries to have successfully completed an Extended Fund Facility Arrangement.

While developments during 1981 are a source of considerable satisfaction to us, we are now entering an even more difficult period and one in which we look to you for understanding and assistance. The major expenditures on development which we have undertaken are beginning to peak in 1982 and 1983. In order to prevent

the overheating of the economy, my Government has decided that no new projects would be commenced until 1984. Only those already in our Investment Programme 1982-86 will be considered. At the same time, however, we are faced with the first serious setback to our food production since 1977. A drought of unprecedented severity affected much of the country in January and February this year. This has had a marked impact on agricultural production in the country. Despite this unforeseen dry spell, we estimate only a modest decline in rice production, which reflects the remarkable success our policies have enjoyed in raising rice yields. Nevertheless, the drought has forced us to abandon our plans not to import any rice during 1982. We have been compelled to import 200,000 tons of rice. At the same time, widespread relief has to be given to hundreds of thousands of farmers whose main source of income has been seriously jeopardized by the drought.


The drought, coinciding as it does with the peaking of expenditures in the public investment programme, has placed a great strain on our domestic and external resources. We are at the same time anxious to ensure that the momentum of our development effort does not slacken. We are, as we have demonstrated in the past, prepared to make whatever adjustments that appear feasible and necessary, short of imposing excessive hardships on our people or of sacrificing our firm commitment to a liberalized economy, free of controls and restrictions.

To make this possible, I must once again urge donor countries who have been generous to us in the past, to assist us in overcoming our present difficulties. In

particular, I would urge you to consider increasing your support to on-going projects which have now become under-financed because of cost over-runs. The quick disbursing food and commodity aid pipeline is rather small at the moment, and needs urgent replenishment. In providing such assistance, I would also urge careful review of procedures so as to permit a quick use of such assistance. We would naturally be particularly grateful for any untied assistance that you are able to provide.

With my warm personal regards,

Yours sincerely,


(J.R. Jayewardene)
PRESIDENT