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LETTER DATED 6 DECEMBER 1990 FROM THE PERMANENT REPRESENTATIVE OF  
SRI LANKA TO THE UNITED NATIONS ADDRESSED TO THE PRESIDENT OF THE  
SECURITY COUNCIL

I have the honour to forward herewith a revised memorandum on the economic difficulties arising out of the implementation by Sri Lanka of Security Council resolution 661 (1990) (see S/21710, annex).

This is submitted under the provisions of Article 50 of the Charter of the United Nations.

A copy of this was sent to the Chairman of the Working Group of the Security Council Committee established by resolution 661 (1990).

I would thank you to circulate this memorandum as a document of the Security Council.

(Signed) Daya PERERA  
Ambassador  
Permanent Representative

Annex

Revised memorandum, dated 30 November 1990, on the adverse economic and other consequences resulting from the imposition of sanctions under Security Council resolution 661 (1990)

On 5 September 1990, Sri Lanka submitted to the Security Council a memorandum covering the period ending 31 December 1990 setting out the adverse repercussions following the imposition of sanctions under Security Council resolution 661 (1990) (see S/21710, annex). However, as the problem seems unresolved and is likely to remain so for an indeterminate period, it has become necessary to revise the original memorandum. A revision was also necessitated by the fact that increases in the price of oil have exceeded original forecasts. This revised memorandum addresses both of those factors.

Sri Lanka has an open economy, which to a great extent depends on the performance of imports and exports, both of which are presently under severe stress owing to internal as well as external factors. The imposition of sanctions under Security Council resolution 661 (1990) has further aggravated this situation. This development will in turn lead to severe economic hardships as well as political and social instability.

Sri Lanka is currently engaged in combating terrorism and a substantial amount of its resources is being diverted for this purpose. Terrorism in Sri Lanka, which has threatened the well-entrenched democratic way of life and governance and the territorial integrity of the country, has retarded economic growth. The decline in resources for economic growth will in turn further weaken Sri Lanka's ability to counter this. Further, other priority sectors, which are equally important in providing the basic needs of the people, will be deprived of much-needed resources. A consequence of this would be continued political and social instability.

The adverse effects consequent on the observance of the sanctions are particularly felt in the following areas.

A. Export of tea

Tea is the second largest source of foreign exchange earnings and accounted for 15 per cent of total current account receipts in 1989. The Middle East absorbs approximately 55 per cent of tea exports. Iraq and Kuwait together accounted for around 12.15 per cent of the total exports and Iraq has been the second largest buyer of Sri Lankan tea. Consequent on the loss of the market in these two countries, Sri Lanka experienced a fall in tea prices owing to a lack of demand from a major buyer.

In the second half of 1989, the value of tea exported to Iraq and Kuwait was \$US 25.6 million and \$5.7 million, respectively. The general oversupply of tea on the world market will drastically reduce Sri Lanka's earnings from tea owing to a

decline in prices. In 1991, the decline in the tea export price from \$2 to \$1.20 per kilogram would imply a drop in earnings of \$37 million. In 1992 and 1993, prices are projected to remain 13 per cent below the originally expected price - about \$60 million less in total earnings than projected earlier. The indirect effects of a fall in prices would amount to another \$15 million per year.

#### B. Other exports and imports

The total value of other exports to Iraq and Kuwait in 1989 was around \$1 million. This market is completely closed to Sri Lankan exports since the eruption of the Gulf crisis. The loss of export markets can in no way be compensated for by a redirection of exports because of limited market accessibility and the prohibitive cost of breaking into new markets in an environment of protection.

#### C. Remittances by Sri Lankan expatriates in the Middle East

It is estimated that over 100,000 Sri Lankans were employed in Kuwait and a sizeable number in Iraq. While worker remittances from abroad are the third largest foreign exchange earner and were estimated at \$360 million for 1991, remittances from Kuwait and Iraq constituted a fair share of the total, estimated at about \$90 million annually.

The steady flow of remittances from these expatriates cushioned the adverse impact of the increase in oil prices.

This cushion no longer exists.

The loss of income-generating capacity from worker remittances cannot be limited to the dollar value of its loss. The sustenance of dependants, increases in national savings, enhanced investment activities and the growth of entrepreneurship at the small-scale enterprise level have now been greatly reduced. The impact can be seen in the decline in the activities of financial institutions as a result of the decline in savings and a reduction of their capacity to recover loans that have been financed on the understanding that there will be a steady flow of foreign remittances.

Based on the above assumption, the impact of the loss of remittances, excluding indirect repercussions, is expected to be \$53 million in 1990. The overall impact in 1990, 1992 and 1993 is expected to be \$207 million, \$193 million and \$125 million, respectively.

#### D. Price of crude oil

The anticipated increase in the cost of crude oil imports over the estimate made prior to the Gulf crisis, despite a 9 per cent reduction in volume, is \$58.4 million for 1990. The average price of Sri Lanka's crude oil imports for the

balance of the year is estimated at \$32 per barrel, which is more than 50 per cent higher than the prices prevailing during the first half of the year. This increase is mainly a result of a shortfall created by the removal of Iraqi and Kuwaiti oil from the market. The average for 1991 is assumed to be \$29 per barrel. In 1991, the impact will be felt fully and the bill for crude oil imports is expected to go up from \$246 million to \$377 million. The impact of this increase in 1991 is expected to be \$131 million. The oil price shock has several indirect effects on other prices. Apart from an increase in import prices, there will be a general rise in local costs. Transportation costs have already risen. Marginal enterprises are likely to go out of business and industrial production will slacken.

#### **E. Inflation and economic growth**

Sri Lanka is already experiencing inflation, an average annual rate of 16.7 per cent. The impact of the escalation of the price of oil on Sri Lanka's import prices will add further pressure on inflation and raise the cost of industrial production. In the context of continuing inflationary pressure, the monetary policies will no doubt remain tight but this will lead to slower economic growth.

#### **F. Socio-economic conditions**

With the large-scale return to Sri Lanka of displaced workers from the Middle East, the high unemployment rate in the country, estimated at around 18 per cent, will be further aggravated. This could result in a reduction in the quality of life of lower-income groups of the population owing to the considerable reduction in remittances received from family members employed overseas. There could also be an adverse social impact on account of readjustment problems faced by the workers returning from the Middle East who have become accustomed to a different lifestyle based on high-income levels enjoyed overseas. The cost of rehabilitating the returning migrant workers is still to be fully determined. The cost of the repatriation of Sri Lankan workers from the Gulf financed by external assistance has not yet been fully determined, but is estimated to be \$25 million. In addition to this, Sri Lanka has up to now incurred expenditure amounting to \$5 million.

#### **G. Overall economic situation**

Sri Lanka is currently in the process of implementing an economic restructuring programme in collaboration with the International Monetary Fund (IMF), the World Bank and other multilateral donor agencies. The recent escalation of terrorist activities is already adding pressure on the operation of the restructuring programme. Compliance with resolution 661 (1990) will take these programmes further off course. The restructuring programme was based on the optimistic estimates of the earnings from tea exports and expatriate worker remittances, as well as the continuation of normal trends in respect of fuel prices, etc. The unexpected fall in foreign exchange earnings combined with the increase in the price of imports will have severe adverse implications on the

balance of payments and economic stability of Sri Lanka and thereby impose severe constraints on the working of the programme.

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The cumulative effect of compliance with the Security Council resolution is not easily quantifiable. The invisible and indirect consequences and the time-span are equally important in gauging the overall effect of the sanctions on society as a whole.

Further, the impact of sanctions on an economy such as that of Sri Lanka, which is experiencing severe constraints, will be far more damaging than on a strong or larger economy capable of absorbing losses arising out of compliance with the sanctions.

Sri Lanka has been severely affected by the Gulf crisis because of several factors. Apart from the loss of a growing and lucrative tea market and the loss of remittances from migrant workers, the savings and investment capabilities of Sri Lankans have been reduced owing to reduced income generation. Additionally, the negative multiplier effects of the loss of income have an adverse impact on small-scale enterprises, finance companies and wholesale and retail businesses. Further, the returnees from Kuwait and Iraq will add to the unemployment problem, with adverse social consequences. Above all, the upsurge in oil prices puts tremendous pressure on the balance of payments, which is already under severe strain. The oil price increase alone is expected to increase Sri Lanka's external payments by as much as 20 per cent of export earnings. In addition, the increased air fares, together with higher insurance costs, will reduce tourist income while increased freight charges will raise prices of imports to Sri Lanka.

On the above basis, the impact of the Gulf crisis during the period from August 1990 to the end of 1993 is expected to be well beyond \$1 billion. With all the ongoing readjustment efforts, the economy is not in a position to absorb a loss of revenue of this magnitude and to continue with its economic programmes, even at minimum levels, unless substantial economic assistance is made available to cushion these losses. If this assistance is not forthcoming Sri Lanka will suffer irreparable political, economic and social consequences.

Hence, the Security Council is requested to take immediate action to facilitate the mobilization of resources from bilateral, multilateral and other sources.

