

ECONOMIC MANAGEMENT AND PLANNING

**Case Studies of Selected
Commonwealth Countries**



COMMONWEALTH SECRETARIAT

ECONOMIC MANAGEMENT AND PLANNING
CASE STUDIES OF SELECTED COMMONWEALTH COUNTRIES

BAKUL H. DHOLAKIA
RAVINDRA H. DHOLAKIA

Indian Institute of Management
Ahmedabad (India)

Management & Training Services Division
Commonwealth Secretariat
London

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Preface

This book is the outcome of our fruitful association with a series of international programmes on Economic Management and Planning sponsored by the Commonwealth Secretariat, London and conducted at Indian Institute of Management, Ahmedabad during 1989-1993. The book contains 11 cases covering eight countries and focussing on a variety of issues in economic planning and policy. The choice of topics and countries has been governed primarily by the need for development of appropriate case material to meet the specific requirements of a newly designed international programme on Economic Management and Planning. We could undertake case writing effort on this scale mainly on account of the active support and funding provided by the Commonwealth Secretariat. We are grateful to Commonwealth Secretariat for providing necessary financial support for case material development. We are highly indebted to Dr. Mohan Kaul, Director, Management & Training Services Division, Commonwealth Secretariat, for valuable support and encouragement in this endeavour.

We are grateful to Dr. P.N. Khandwalla, Director, Indian Institute of Management, Ahmedabad and Dr. N.R. Sheth, former Director of the Institute for their interest in our work and also for ensuring the institutional support required for writing a book of this kind. We are also grateful to the participants of Commonwealth Programme on Economic Management and Planning in Developing Economies for their encouraging feedback on various case studies contained in this book. We would like to express our gratitude to the concerned Ministries in the respective Governments of the Commonwealth countries we visited for their cooperation and help in facilitating our task. Without the active support and facilities provided by many government officials in various countries, we would not have been able to undertake this case writing effort. We are highly grateful to the following officials for fruitful discussion and also for providing valuable insights and relevant information relating to the respective case studies contained in this book.

Planning As Development Management - Case of Commonwealth of Dominica

Dr. Cary Harris (Development Coordinator, MFD), Mr. Alick Lazare (Fiscal Advisor, MFD), Mr. Gilbert Williams (Financial Secretary, MFD), Mr. Raymond Austrie (Sr. Project Officer, EDU), Mr. George Buttler (Valuation Officer, EDU), Mr. Eisenhower Douglas (Development Economist, EDU), Mr. J.F. Casimir (Chief Statistician, MFD), and Mr. Thomas Fontaine (Statistician, MFD). Mr. Eliud Williams (Permanent Secretary, Ministry of Agriculture, for allowing to attend the Agricultural Sector Plan Committee Meeting.

Economic Planning in Tanzania - Framework and Possibilities

Mr. Mutalembwa, Mr. S. Odunga, Mr. A.Y. Mgumia, Directors, Planning Commission; Mr. R.M. Khijjah, Sr. Economist in Ministry of Finances; Mr. J.M. Komba, Government Statistician; and Mr. Rweyemamu, Assistant Director, Planning Commission, Government of Tanzania.

Planning in Consistency Framework : Malaysian Experience

Professors Nasaruddin Arshad, Abdul Rahim, Abdul Razak and Manjit Sidhu of University of Utara Malaysia; Mr. Hashim Mat Noor, Director, SEPU, Kedah; Mr. Haji Ariffin Ismail, Deputy Director, SDO; and Mr. S. Jagatheesan, Head, Planning and Evaluation Division, MADA.

Methodology of Planning and Planning Process in Kenya : The Case of the Sixth Plan 1989-93

Mr. Nduati Kariuki, Assistant Minister, Office of the Vice President and Ministry of Finance; Mr. Magari, Director of Planning, MPND; Mr. Njuguna Mwangi, CPO & Department Secretary, MPND; Mr. James Otieno, CPO, MPND; Mr. E.N. Njeru, Department CPO, MPND; Mr. Peter Ondieki and Ms. N.W. Muriithia, Principal Economists, MPND; Dr. A.Onyango, SPO, MPND; Dr. E. Odada, UNICEF; and Mr. W.E.O. Ochoro, University of Nairobi.

Urban Development Through Corporatism - The Case of Toronto Harbourfront.

Mr. David Clark, General Manager, HC; Miss Beverley Morley, Community Relations Director; Ms. Margarate Johnston, Assistant to Commissioner; and Mr. Gordon Garland, All from the Royal Commission; Professor Gene Desfor from the York University, and Professor Richard Stren, Director of Centre for Urban and Community Studies, University of Toronto.

Economic Policy Reforms : The Mauritian Experience

Mr. R. Bheenick, Director General, Ministry of Economic Planning & Development; Mr. Regis Yat Sin, Permanent Secretary, Ministry of Industry & Industrial Technology; Mr. A.S. Aboobakar, Deputy Director - MEDIA, Mr. R.L. Prabhu, Managing Director, Development Bank of Mauritius Ltd.; Mr. R. Padiyachy, Permanent Assistant Secretary, Ministry of Trade & Shipping; Mr. Raj Makoond, Deputy Secretary General, The Mauritian Chamber of Commerce & Industry, Dr. Azad Jeetun, Acting Director, Mauritius Employers' Federation; Mr. D. Zmanay, Director of Statistics, CSO; Mr. B. Goorah, General Manager, State Trading Corporation; Mr. K. Gupta, Principal Budget Officer, Ministry of Finance; Mr. Owasi and Mr. S.D. Bikoo, Bank of Mauritius; Mrs. Kalyani Upadhyaya, and Dr. S.S. Agarwal, MEDP.

Export Promotion Strategy and Trade Policy Reforms in Sri Lanka

Mr. P. Weerasekera, Secretary, Ministry of State for Trade & Commerce; Mr. L.F. Yapa, Director, Policy & Planning, Sri Lanka Export Development Board (SLEDB); Mr. S.A. Karunaratne, Director, National Planning Department, Ministry of Policy Planning & Implementation; Mr. H.B. Masinghe, Director, Promotion & Services, Board of Investment of Sri Lanka; Mr. M.R. Fernando, Controller of Exchange, Central Bank of Sri Lanka; Mr. M.B. Dissanayake, Chief Accountant, Central Bank of Sri Lanka; Mr. Asoka Dharmawardhane, Acting Director, Department of Commerce, Ministry of Trade & Commerce; Mr. Patrick Amarsinghe, President, National Exporters Association of Sri Lanka; Mr. J.N.V. Pereira, Director, Woodplex Ltd.; Mr. Keerthi Senarathne, Deputy Director, Investment Division, Ministry of Industries, Science & Technology; Mr. K.G.D.D. Dheerasinghe, Deputy Director, Data Processing Department, Central Bank of Sri Lanka; Mr. Ben Isaac, Deputy Director, Sri Lanka Customs; Mr. Sumith Abeysinghe, Deputy Director, Fiscal Policy Division, Ministry of Finance; Mrs. Jasoora B. Shiffar, Deputy Director, Policy & Planning, SLEDB; Mr. Codlin Abeyuriya, Commissioner, Department of Commodity Purchase, Ministry of Trade & Commerce; and Mr. P. Liyanarachchi, Additional Director, Budget Division, Ministry of Finance.

Issues in Monetary Management in Tanzania

Mr. Sunil Dalal, Sr. Advisor, Bank of Tanzania; Mr. N.N. Kitomari, Deputy Governor, BOT; Dr. C.S. Kemei, Manager - Research, BOT; Mr. Andres Rustia, Advisor, BOT; and Mr. Phillip Thomas, Consultant of the Banking Commission.

Issues in Monetary Management in Countries with Common Currency : The Case of Eastern Caribbean Central Bank

Mr. E. Liburd (Director - Research & Information); Ms. L. Bain (Economist); and Ms. S. Williams (Economist), all from ECCB; Hon. Richard Caines (Minister in Finance, and Member of the Monetary Council), ECCB; Mr. W. Lawrence (Permanent Secretary & Member, Board of Directors), ECCB; and Mr. Calvin Edwards (Budget Director, Ministry of Finance), all from St. Kitts and Nevis; Mr. A.B. Lazare (Fiscal Advisor to the Prime Minister, and Member of Board of Directors), ECCB; and Mr. G. Williams (Financial Secretary); Mr. A. George (General Manager), Dominica Banana Marketing Corporation; and Ms. P. Inglis (General Manager), Banque Francaise Commerciale, all from Dominica; and Mr. A. Lockhart (Local Representative), ECCB in Antigua.

Tourism Development in St. Kitts & Nevis : Problems and Prospects

Mr. Calvin Edwards, Budget Director in Ministry of Finance; Ms. Beverly Haris, Assistant Secretary in Ministry of Planning; Mr. Larkland Richards, Permanent Secretary in Ministry of Tourism; Mr. Harry Greene, Assistant Manager in Ministry of Trade; Mr. Jerome Thomas, Agronomist in Ministry of Agriculture; Ms. Sheila Williams, Economist in ECCB; Mr. Michael Hobson, Assistant Secretary in Ministry of Finance; Mr. Oliver Knight, Chief Statistician; and Mrs. Sylvain Henry, Statistician in Ministry of Development.

Role of Tourism Sector in Mauritian Economy

Mr. S. Fowdur, Principal Assistant Secretary; Mr. R. Sen, Tourist Officer; Mr. V. Haulder, Tourist Officer; and Mrs. C.K. Bhuckory, Deputy General Manager, all from Ministry of Tourism; Mr. R. Bheenick, Director General; and Mrs. Kalyani Upadhyaya, Economist; all from Ministry of Economic Development and Planning; and Mr. D. Zmanay, Director of Statistics, CSO.

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Indian Institute of Management
Ahmedabad, India

Bakul H. Dholakia
Ravindra H. Dholakia

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FOREWORD

Decision-makers in Commonwealth countries are faced with difficult policy choices in the context of a rapidly changing world economic environment. In order to assist Commonwealth developing countries in building key skills in macro-economic management, the Commonwealth Secretariat in collaboration with the Indian Institute of Management, Ahmedabad (IIMA), organised special training programmes aimed at senior Government officials from economic and planning departments. So far some 150 participants from 35 Commonwealth developing countries have benefitted from these programmes.

Case studies on macro-economic management and planning in various Commonwealth countries were prepared as teaching materials for these training programmes and are offered in this volume as a useful aid for others. They have been successfully tested in more than 4 international programmes at the IIMA, and they provide plenty of data and relevant information to generate meaningful debates and discussions among practising senior level government officials.

The cases focus on various aspects of reforms related to macro-economic policies, management and planning in a few selected Commonwealth countries. The cases demonstrate the extent of similarities in magnitude, nature, causes and intensity of economic problems faced by Commonwealth developing countries. The emphasis, however, has been more on the planning processes than on technical aspects of economic planning. The cases also highlight the issue of decentralisation, the environment and ecological concerns. We hope this publication will be useful to both training organizations and to the policy makers and planners from Commonwealth countries.

I am most grateful to Professors Bakul H. Dholakia and Ravindra H. Dholakia for their excellent efforts in preparing these cases. I would like to take this opportunity to thank the Director and the whole Economic Management Programme faculty of the Indian Institute of Management, Ahmedabad for their invaluable cooperation and contribution.

Mohan Kaul
Director
Management & Training Services Division
Commonwealth Secretariat
London.

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ABOUT THE AUTHORS

Bakul H Dholakia, Ph.D. (MSU), is currently the RBI Chair Professor of Industrial Economics at the Indian Institute of Management, Ahmedabad, India. His fields of specialisation are Industrial Economics, Economic Growth & Planning and Public Enterprise Management. He has been a consultant to several national and international organizations including the World Bank and Asian Development Bank. His publications include books on *Changing Efficiency of Public Enterprises in India*, *Economics of Housing in India*, *Sources of Economic Growth in India*, *Principles of Macroeconomics* (co-author), *Models of Economic Growth* (co-author), *Brackish Water Aquaculture Development in India* (co-author), *Fishery Sector in India* (co-author), *Energy Demand for Agriculture in India* (co-author), and *Regional Energy Demand Model and Analysis* (co-author), and several monographs and many research papers in professional journals in India and abroad.

Ravindra H Dholakia, Ph.D. (MSU), is currently Professor of Economics at the Indian Institute of Management, Ahmedabad, India. His fields of specialization are regional development and planning, international trade, input-output analysis, and labour economics. He was a post-doctoral Research Fellow at University of Toronto. He has also taught at MS University of Baroda and undertook several research and action research projects at Sardar Patel Institute of Economic and Social Research, Ahmedabad. He has been a consultant to several national and international organizations. Publications include books on *Regional Disparity in Economic Growth in India*, *Planning for Employment Programme in Sayla Block*, *Models of Economic Growth* (co-author), and *Planning for Rural Development: Issues and Case Studies* (co-author), *Regional Energy Demand Model and Analysis* (co-author) and more than 70 research papers in national and international journals.

Chapter 1

INTRODUCTION

I. Background

Developing commonwealth countries have several similarities. For their economic development, the paths chosen by them have also been very similar though not identical. This is because they shared the experience of being ruled over long period of time by foreigners with distinct exploitative imperialistic tendencies. As colonies, their rich resource base was used for the development and prosperity of the ruler's industries rather than the betterment of the local people. These societies with the psyche of the vanquished were forcibly made to accept even the production related choices of the rulers. Market mechanism and prices were deliberately distorted by the rulers to their own advantage. In the spheres of trade, production, consumption and distribution, the ruler's interference was a rule rather than exception. As a result, when these countries gained independence and formed their own governments, they found it easier to follow the same path. Philosophy of a high degree of government intervention in the economic life to achieve desired goals was readily accepted by the newly formed democratic governments in these countries. Detailed physical and financial economic planning and consequent expansion of public sector activities were found in the post-independence period in most of the developing commonwealth countries.

The small island colonies in the West Indies, which later became independent countries, did not experience the same degree of interference from the foreign rulers as the other bigger countries because of their special features of geographic smallness coupled with specificity of available scarce natural resources. These countries never had many production choices to begin with. Foreign rulers imported both the labour and capital to organize production on these islands. Some of these islands were not even inhabited when the foreign rulers first went there. The production and trade related decisions of the foreign rulers were, therefore, not seen as significant distortions and interference with the economic life in these colonies. When they gained independence, the local democratic government did not feel compelled to adopt the philosophy of economic planning. However, public sector activities were considered important to achieve their developmental goals. Planning of the public sector activities was, therefore, an important element of their macroeconomic management.

Thus, the experience of the developing commonwealth countries in the field of macroeconomic management and planning reveals a distinct similarity of approach. Details of economic philosophy and development strategy differ from country to country but the broad policy framework, institutional set up and general nature of the constraints operating on the macroeconomic management in these countries are very similar. Therefore, an effort to bring out relevant issues and problems faced by policy makers in the developing commonwealth countries is likely to be beneficial to the government officials working in these countries. If these issues and problems are considered while discussing the actual experience of different aspects of macroeconomic management and planning in these countries, the material can serve as very useful teaching aid. In view of the urgent need of training and upgradation of skills of government officials in the developing countries such material is likely to provide the basis for stimulating discussion, interaction, and experience sharing in a class room. At present there are very few such case studies readily available for class room use. The present book of case studies on selected aspects of macroeconomic management and planning in developing commonwealth countries is expected to make a modest attempt towards filling this gap.

In the following pages we have put together 11 case studies on various aspects of macroeconomic management and planning from different commonwealth countries.

II. Cases on Economic Planning

In the first part we present 5 case studies on experiences of economic planning and related themes. The first case study of the experience of Commonwealth of Dominica views economic planning as development management. The case focuses on the planning machinery, planning processes and their interlinkages with budget process in the small Caribbean Island. The case presents special features of the economy, development concerns and national goals, in the light of which, the planning process has to be viewed. The case clearly brings out the importance of political commitment, decentralized planning process, coordination and interaction among various government departments and agencies besides the macro framework for planning in a highly open economy. This case can be used for clarifying various concepts involved in economic planning in a democratic society.

The second case on the framework and possibilities of economic planning in Tanzania discusses the role of newly constituted Planning Commission in the planning process in the country. In the light of the limitations of the past planning systems and lack of clarity about the methodology of planning, possibility of using more sophisticated models of planning is examined. The input output statistics are generated in the country by their statistical office. The case illustrates use of input output statistics in planning with the help of the estimates already available for Tanzania. It also points out the limitations of the methodology. The case moreover, discusses decentralization of planning functions in Tanzania, particularly, for the framework and methodology used. This case brings out some of the issues involved in economic planning within a consistency framework in a largely closed economy.

The third case on Malaysian experience, on the other hand, examines economic planning in a largely open economy within consistency framework. The case provides the background on Malaysian economy and its development concerns to examine briefly planning models used in different Malaysia's Five Year Plans. In order to focus on the issues involved in planning within consistency framework, the planning process in Malaysia including the efforts of decentralization of planning functions are presented in the case. The sectoral allocations, both planned and realised, in different Malaysian plans are also considered. The case clearly brings out the role of planning processes vis-a-vis elegant planning models and sophisticated forecasting and planning techniques for testing internal consistency in deciding the ultimate structure of the plan.

The fourth case on the Kenya's Sixth Five Year Plan focuses on employment oriented planning and decentralised planning processes in the country. After providing the background of the Kenyan economy, the case goes into the methodology adopted in the Kenya's Sixth Plan for setting targets. A very interesting experiment of forward budgeting and rolling decentralised plan attempted successfully in Kenya is also discussed. This methodology ensures dovetailing all decentralised economic plans with overall macro plan and budget process. Since the main focus in Kenya's sixth plan is on employment generation the case provides an illustration of employment oriented planning put into practice.

The fifth case on Toronto Harbourfront Corporation presents Canadian experience in the field of urban development. In the decentralised planning or policy making, the urban dimension usually gets ignored. However, it represents one of the most important fields of developmental economic activity where decentralised decision making based on people's participation can play extremely useful role in achieving regional as well as national economic growth. The case briefly outlines a model emphasizing the role of human capital development and quality of life aspects in the growth of a city and hence the nation. It provides background information on the Toronto Harbourfront Corporation which was essentially the federal governments initiative to revitalise the inner city of Toronto. After

considering the special features of Toronto Harbourfront Corporation, the case briefly outlines the main events in the history of the Corporation upto 1991 when it was reorganized by divesting the real estate side of the Corporation. The case brings out various issues including the ones related to the roles of different levels of government, internal consistency of the institutional goals and objectives, nature and timing of privatization and the role of corporate structure in responding to changing environment.

III. Cases on Economic Policy Reforms

The case on Mauritian experience provides a comprehensive view of economic policy reforms under the structural adjustment programme. It considers in detail various reforms carried out in Mauritius in industrial policy, fiscal policy, trade policy, and monetary policy after discussing briefly the problems faced by the Mauritian economy at the time of undergoing the structural adjustment programme. Mauritius is one of the few success stories of IMF-World Bank's structural adjustment programme. The case discusses the experience of Mauritian Export Processing Zone in order to get insight into the management of the economic policy reforms. The case also considers the SWOT analysis of the export processing zone which is the critical element of the policy reforms programme in Mauritius.

The other case of trade policy reforms in Sri Lanka focuses on the export promotion strategy in the country. The case highlights Sri Lanka's exports of economic transition involving a distinct strategy shift from import substitution based development strategy to the export-led growth strategy. The case provides useful insights into the issues involved in the formulation and implementation of export-led growth strategy. After briefly discussing the background conditions under which Sri Lanka adopted policy of economic liberalization and restructuring of the economy, the trade policy reforms and export promotion strategy followed by the country are outlined. The case also presents the export performance and thinking on future scenarios in the field of trade policy in Sri Lanka.

IV. Cases on Monetary Management

The case on Tanzania discusses issues in monetary management as a part of the overall policy reform package adopted in Tanzania. As it is very well recognized, monetary policy plays a pivotal role in structural adjustment and economic policy reforms. The case reviews the existing financial structure in Tanzania and brings out problems in monetary management by examining efficacy of the instruments of monetary control available with Bank of Tanzania. The case highlights management of disinflationary policies targeting to bring down inflation rate from around 25 per cent to about 15 per cent per annum in the course of three years by following tight money policy. It raises important issues including the autonomy of the central banking in the economy.

The next case discusses issues in monetary management as faced by the Eastern Caribbean Central Bank. The Eastern Caribbean Central Bank is a common Central Bank to the eight Caribbean member countries and represents a unique case because the countries share the same currency as well as monetary policy. The case briefly provides historical perspective and highlights some important provisions in the Bank's Agreement having implications on the Central Bank's ability to control the financial aspects of the economy. Important features of the financial institutions and the financial structure existing in the region are also discussed. The effectiveness of the Bank's control and conduct of monetary policy is also appraised. The role of the special features of the economy in the region in the monetary management of the economy is also highlighted. This case provides a sharp contrast to the previous case on the issue of autonomy of Central Bank from the fiscal authority.

V. Cases on Tourism Development

The case on St.Kitts and Nevis examines problems and prospects of tourism development in a small Island economy with abundance of natural sites for tourist attraction. Since tourism has been perceived as an important concern of growth not only in the foreign exchange earning, but also in the economy as a whole, government policy regarding tourism development assumes significance in most of the countries. St.Kitts and Nevis is no exception. The case reviews the government's efforts to develop tourism in the two Islands of St.Kitts and Nevis. The case can be used to introduce and clarify various concepts involved in the tourism development in an economy. The issues of linkage of tourism activity with the rest of the economy as well as the one of import intensity of the tourism sector, besides the role of investments in infrastructural facilities to promote tourism are highlighted in the case.

The case on the role of tourism sector in Mauritian economy brings to the sharp focus the government's concern about environmental aspects, sustainability and quality of life considerations in tourism development policy. The concepts of tourists carrying capacity and optimal tourists flow in relation to the investments required in the infrastructural development are brought out in the case. It also provides quantitative estimates of the impact of tourism on the economy with help of the latest available information. It provides an illustration of additional application of the input output statistics used along with tourists survey results. The two cases on tourism development together provide valuable insights into the issues involved in formulating and managing policies for development of tourism industry.

PART I : ECONOMIC PLANNING

Chapter 2

Planning As Development Management - Case of Commonwealth of Dominica

1. Features of the Economy

Dominica is a small windward island country in the string of Caribbean islands. Its total area is 289 Sq.miles. Its population is approximately 79,000. The island gained political independence from the British rule in September 1978. Its topography is highly uneven with several valleys and mountains spread all over the island. There are so many rivers on such a small island that a visitor can choose a different river everyday of the year. All this coupled with thick forests, numerous falls and unpolluted environment make it the only nature island of the Caribbean and offers a unique tourism product. Although it does not have spectacular beaches, it is considered the divers' paradise. Tourism, however, does not play a major role in the economy of the island unlike most other Caribbean islands. Even the state of physical infrastructure like the road, communication, hotels, etc. is also not favourable comparable to other islands in the region. As a result, the total visitor arrivals in the island during the year 1990 was only around 50,000.

Commonwealth of Dominica is a member of the CARICOM, Caribbean Development Bank (CDB) and East Caribbean Central Bank (ECCB). It therefore has the same currency unit as other east caribbean countries, viz. the EC dollar. Since it shares a common central bank, it also has a common monetary policy with the rest of the member countries. The EC \$ was initially (i.e. 1965 to July 1976) pegged to the pound sterling at the rate of £1 = EC \$4.8. Since July 1976, the EC\$ is linked to the U.S. dollar at the rate of U.S \$1 = EC \$2.70. This rate has not changed so far withstanding all the ups and downs in the regional economy as well as the world economy. The per capita GDP in Dominica is about EC \$4,000. Between 1978 and 1987, the economy grew at the rate of 4% p.a. in real terms. In 1988, the real GDP grew by 7.9% as a result of rapid growth in construction (30.6%), tourism (15.5%) and agriculture (6%). Hurricane Hugo devastated the economy in 1989 and it registered a decline of 1.4% in real GDP largely on account of 12.8% drop in agricultural output. In 1990 and 1991 the economy is limping back to normal. Dominica, like other windward islands is vulnerable to Hurricane disaster once in a while. In 1979 also, it suffered severely when Hurricane David had struck the island damaging buildings, physical infrastructure and agriculture. Such natural disasters totally destabilize the economy.

The structure of the Dominican economy has changed considerably between 1978 and 1990. The share of agriculture in GDP has reduced from around 37% to around 28%. Similarly, the share of manufacturing and construction increased from 11% to 15%. The service sector has also increased in its importance over last decade. However, the most important feature of the structure of the Dominican economy is its heavy dependence on a single crop, viz. banana. It is the largest employer of labour in the economy. Banana's share in the total export earnings of Dominica has been more than 70%. When we consider both the production and trade, banana contributed almost 37% of the income generated in the economy. The export of banana, moreover, is done through a long term (3 years) direct rolling contract with Geest Industries Ltd., one of the largest companies in the world banana market. No windward Caribbean islands can sell bananas to anybody else than the Geest as

per the contract¹. The Geest Industries Ltd also buys bananas from other countries in the dollar market where the banana are cheaper per unit of quality .

Like all other small island countries, Dominica also has an open economy highly dependent on its external transactions. Table 1 provides balance of payments for Dominica for the five years 1984-88. It can be seen that both the trade balance and the balance on current account are always in the deficit. These deficits are financed by a combination of foreign assistance programmes and loans from international and regional agencies. Among the imported goods in Dominica, manufactured goods account for about one-third value; food, beverages and tobacco about 22%; machinery and transport equipment about 20%; and chemicals about 14% of the value. Exports, on the other hand, are dominated by banana (72%) and toilet and laundry soaps (18%). In terms of the direction of trade, the share of the CARICOM countries is declining in exports and increasing in imports over the last five years. Currently, about 62% of the exports of Dominica are to U.K.; about 20% to the CARICOM countries and only 5% to U.S.A.; but 25% of the imports are from U.S.A.; 18% from U.K. and 27% from the CARICOM countries. Since EC\$ is pegged to U.S. \$ the predominance of export trade of Dominica with U.K. has serious implications of the dollar-pound parity in the international market on the trade balance of the country.

Although the external debt situation of Dominica is not precarious, the Debt/GDP ratio is rising from 35.9% in 1984 to 56% in 1989-90. Similarly, the ratio of Debt Service/Exports is quite low at 4 to 5%. The average interest rate on the external debt has been declining from 4.8% in 1984 to 2.6% in 1988. However, the existing debt amortisation structure is such that significantly higher debt service payments may start arising around mid-nineties.²

On the domestic fiscal front, the affairs of the government and public sector in Dominica are on the whole well-managed. The government has been exercising considerable restraint and discipline in its expenditures. On the current account, there has been a surplus which is rising significantly from EC\$ 6.1 million in 1984 to EC\$ 33.4 million in 1988. The deficit on capital account, on the other hand, has not been increasing over the same period. As a result, the overall deficit has reduced from EC\$ 46.6 million in 1984 to EC\$ 20.4 million in 1988. However, due to the devastating Hurricane Hugo of September 1989, the government revenue and expenditures were severely affected. The surplus on current account in 1990-91 budget was estimated only at EC\$ 12.3 million, whereas the overall deficit is estimated at EC\$ 93.3 million. The public sector in general in Dominica has been contributing positively to the total saving in the economy. The overall saving and investment rates in the economy have not been as high as other developing countries. Investment as percentage of GDP is around 22 to 23% and domestic saving are around 15%. The share of public sector investment in the total gross investment has been around 50% and the public sector surplus is around 4% of the total GDP. Since the expected growth rate of GDP is around 4% p.a. for the next 2 to 3 years, the incremental capital output ratio for the economy is around 6 which reflects low capital productivity.

1 These banana producing islands including Dominica have long lasting relation with the Geest Industries for over 40 years. In fact, the Geest were the largest owners of plantations in these islands once upon a time. As a result of all this, the infrastructure for marketing, packaging, weighing, processing, etc., at the ports are owned by the Geest Industries in the 4 windward islands. In Dominica, the Dominica Banana Marketing Corporation (DBMC) is created as a statutory body with monopoly power over the export of banana outside the Caribbean region. The contract for export of banana is between the Geest Industries and DBMC.

2 However, there have been efforts by the government to reduce this burden. As a policy, the borrowing is on very concessional terms and only for productive investments. Moreover, Canada has agreed to write-off their loans to Dominica and both France and China have agreed to restructure Dominica's debt on more concessional terms. Similarly, all future aid from U.K. will be on grant terms.

<i>Table 1</i>					
Dominica – Balance of Payments, 1984-88					
(US \$ million)					
	1984	1985	1986	1987	Prel 1988
Exports, Goods and NFS	36.9	38.3	53.9	59.5	67.9
Goods	25.6	28.4	43.4	48.0	55.6
Non-factor services	11.3	9.9	10.5	11.5	12.3
Imports, Goods and NFS	58.4	60.1	59.0	69.8	91.1
Goods	55.8	57.2	55.7	66.4	87.5
Non-factor services	2.6	2.9	3.3	3.4	3.6
Resource Balance (G&NFS)	-21.5	-21.8	-5.1	-10.3	-23.2
Net factor income	-3.2	-5.3	-6.1	-5.1	-3.4
Receipts	0.5	0.3	0.3	0.3	1.2
Payments	3.7	5.6	6.4	5.4	4.6
of which interest	1.9	1.9	1.9	1.8	1.7
Private transfers (net)	6.3	6.5	6.7	7.7	8.4
Current Account Balance	-18.4	-20.6	-4.5	-7.8	-18.2
Official transfers and grants	11.3	14.3	10.8	9.4	8.9
Net private direct investment	2.3	3.0	2.7	8.6	6.9
Net loans	4.8	4.5	4.2	5.4	3.5
Drawings	5.4	5.2	5.4	7.7	5.2
Amortization	0.6	0.7	1.2	2.3	1.7
Commercial Banks	3.0	-0.8	-2.9	-12.7	-9.9
Other	1.5	0.5	1.0	1.5	0.0
Capital Account	22.9	21.5	15.8	12.2	9.4
Errors and omissions	1.7	-1.5	-4.7	4.5	8.9
Overall Balance	6.2	-0.6	6.6	8.9	0.1
Change in Official Reserves	-6.2	0.6	-6.6	-8.9	-0.1
Net IWF	-0.3	-1.5	-0.6	-0.4	-2.1
Government foreign assets	0.2	-0.5	-1.8	-0.3	-0.1
Change in imputed reserves	-6.1	2.6	-4.2	-8.2	2.1

a) Estimates based on partial information compiled by Dominican officials
b) Imputed share of Dominica in the international reserves of the ECCB.
Source: Ministry of Finance, IWF estimates

Inflation in the economy is not very high. Price level rose by less than 20% during 1984-89. The unemployment rate in the economy is around 11% as per the 1989 estimate³. The unemployment rate among males is lower at 7% than among females at 17%. Wages are relatively low and male-female differentials are not substantial - only 28% difference in the median wages. The unemployment problem is more structural because there are severe labour shortages experienced in sectors like agriculture and construction. The skill level of the labour force is also very low. Although official estimates are not available, the overall literacy rate in the economy is likely to be very high. Estimates of life expectancy have also not been possible even with Census because such questions were not included in the Census questionnaire. From the health statistics, however, it is possible to estimate death rate, birth rate and infant mortality rate (IMR). The IMR has declined substantially from 27 in 1977 to 18.5 in 1987. Death rate has also declined from 7 in 1977 to 5.6 in 1987. Similarly the birth rate is reduced from 21.0 in 1977 to 19.8 in 1987. The level and the direction and rate of change in these indicators do imply that other socio-cultural welfare of the population is likely to be fairly high in Dominica.

In the next section, we discuss the major developmental concerns for future in Dominica. The third section is then devoted to outlining the planning process with a brief historical perspective. The fourth section reviews the role of Economic Development Unit (EDU) in managing economic development in Dominica. In the fifth section, we discuss the interlinkages of the planning process with the budget process and the fiscal policy. In the sixth and the last section, we discuss a few limitations of the planning process in Dominica.

II Development Concerns and National Goals

Considering the features of the Dominican economy discussed in the previous section, it is not very surprising that international agencies like World Bank and IMF in their review, do not see a very bright future for Dominica. This is largely because Dominica does not have a very sound base in the tourism sector unlike most of the OECS (i.e. Organisation of Eastern Caribbean States) countries. The future growth of Dominican economy is, therefore, constrained by domestic activities like agriculture, agro-processing and manufacturing. Banana's predominance in Dominican agriculture makes it more vulnerable to the international banana market. The balance of payments (BOP), import of essential commodities and the stability of the economy and the currency depend crucially on the banana exports. The developments taking place in the European Community in 1992 are therefore the prime concern for Dominicans.

The World Bank's projections of macroeconomic aggregates for the Dominican economy are summarised below in Table 2. According to these projections, which are based on the assumption of no banana shock after 1992, the growth of GDP in Dominica would be significantly decelerating, investment rate would be falling and the external debt-service would rise substantially during the mid-nineties. In order to tackle these problems, the country has to generate a current account surplus on BOP requiring a much higher rate of growth of exports than the projected.

If, however, there occurs a banana shock resulting from EC 1992, it might lead to (i) 50% fall in both the price and output of banana, (ii) considerable fall in the contribution of agriculture in real GDP, and (iii) fall in imports by one-half the fall in exports because the banana production in Dominica has a high import content. With banana-shock, therefore, the scenario is very gloomy for Dominica. The current account deficit on BOP, might reach U.S. \$70 million by 2000 A.D. and the debt-service/exports ratio might rise to 24% instead of 6% in 2000 A.D. The economy would be forced to restructure and adjust to such a rude shock but during the process, it may have to suffer severe cuts in the living standards and rising unemployment. The foremost national goal, therefore, is to try to avert the banana-shock and if it is somehow not possible to avert the shock, prepare the economy in such a way that it can absorb the shock with least possible cost. In the words of the Prime Minister, the national goals and objectives for policy making in Dominica are:

- a) To achieve a sustainable rate of economic growth;
- b) To reduce unemployment generally and specifically among target groups;
- c) To improve external competitiveness particularly in the productive sectors; and
- d) To reduce the vulnerability of the economy to external shocks.

3 The definition of unemployed persons was such that it included those who were (i) without work and (ii) available for and seeking work. Excluded from this definition are persons who did not seek work although were willing and able to work. If we include such "discouraged workers", the unemployment rate turns out to be 20.7%.

<i>Table 2</i>			
Dominica – Actual and Projected Macroeconomic Indicators, 1988-2000			
	Preliminary	Projected	
	1988	1989-94	1995-2000
	Real Growth Rates		
Gross Domestic Product	5.6	4.0	2.8
Gross Domestic Income	6.2	3.8	2.5
Consumption	5.6	3.8	2.4
Public	1.5	1.5	1.3
Private	7.3	4.6	2.7
Fixed Domestic Investment	5.6	2.0	0.6
Exports of G&NFS	5.6	5.3	3.6
Imports of G&NFS	5.6	4.0	2.2
	Shares of GDP(%)		
Gross Domestic Product	100.0	100.0	100.0
Gross Domestic Income	100.5	99.0	99.0
Consumption	86.6	86.6	84.0
Public	24.5	22.0	20.0
Private	62.1	63.0	64.0
Fixed Domestic Investment	23.0	22.0	19.0
Exports of G&NFS	45.8	48.0	51.0
Imports of G&NFS	55.4	55.0	54.0

These objectives, moreover, are sought to be achieved by following the strategy of (i) enhancing institutional capability to undertake programmes for improving economic performance; (ii) improving the investment and saving climate in the economy; (iii) diversifying the base of economic activity both within agriculture and into non-traditional areas; (iv) providing the requisite physical infrastructure; (v) upgrading physical facilities and encouraging skill formation for human resource development; and (vi) fostering people's participation and community involvement particularly in rural areas. The basic philosophy accepted by the Dominican government is to rely on the private initiative and enterprise to achieve these goals. The medium term economic strategy to facilitate the private sector investment, particularly the foreign investment, to promote growth of GDP and employment. Foreign capital is also welcomed because it brings new technology, entrepreneurial talent and competitive forces to compel the domestic industries to become more efficient users of the scarce resources. The role of the public sector is envisaged basically as the facilitator and provider of necessary infrastructural and institutional support for the growth of private sector activities. The involvement of the public sector in the directly productive activities would be confined only to those strategically crucial lines for achieving national objectives where the private initiative does not come forth. Thus, the public sector is seen more as a management tool or the policy incentive for private enterprise rather than an intervention to control and regulate market forces and thereby the private sector.

III Planning Process

In 1978 when Dominica got its political Independence, it was perhaps not well prepared for taking hard decisions to manage its resources to foster rapid economic development over longer time horizon. Perhaps it was not required. Moreover, in 1979 Hurricane disaster struck the island. Therefore the first five years saw restructuring and stabilization of the economy on ad hoc basis. A lot of sympathy was generated for the island and hence external aid was easily available. The special treatment it received from the U.K. and the U.S.A. made it complacent and dormant on long-term issues concerning its future path of growth. To put it simplistically, it used to take only a cable to U.K. or U.S.A. asking for a grant to carry out some project, e.g. building a road from point A to B, and it would be by and large accomplished. The need for systematic planning was hardly recognised upto 1983. Even the political philosophy in the country was hostile against the use of the term economic planning. The political lead, direction and commitment were lacking in these matters. The only long-term perspective on development of the country was provided in the *National Structure Plan for Commonwealth of Dominica, 1976-90* prepared in August 1976, i.e. before Independence. It was also not an economic plan as the term is commonly understood. Its focus was mainly on the spatial planning, i.e. the land-use and settlement planning for provision of infrastructure. However, its objectives and scope included some major economic concerns like employment growth, reduction of income disparities and related aspects of development strategy. In Appendix 1 below, we present the objectives, scope and the planning model of the Plan. In 1985, the National Structure Plan had to be revised on account of significant changes in development policies and availability of new data on socio-economic characteristics of the population from the 1981 Census. In Appendix 2, we present some excerpts from the *National Structure Plan (1985)* giving the objectives and goals of the Plan. The Plan emphasises that "Social and economic policies formulated at the national level can only be effective and successful if the spatial distributional implications of these policies are carefully articulated and fully incorporated into the planning process." (p.1). This assumes importance since, for the first time, the need for economic planning at national level in Dominica was recognised and some type of planning process was also envisaged.

The Ministry of Finance was expanded and renamed as Ministry of Finance and Development. Economic Development Unit (EDU) was created within the Ministry and a Development Coordinator with the same status as a Permanent Secretary was appointed as the head of the unit. We shall discuss the role of the EDU in the planning process in more detail in the following section. Currently we may note that it is the apex body responsible for plan formulation and monitoring in Dominica. Its approach to economic planning in the country as explained by the Development coordinator has been to manage economic development through specific projects from below rather than imposing a national economic plan from above. Economic planning is not considered a mechanical process but an interactive and participatory process where there is a scope for revision, modifications and alterations at every stage. Ideally speaking, it has to be a political process considering inputs from technocrats at various stages. Efforts at organizing such thoughts in the form of a Planning Manual or a Process Document are currently ongoing at EDU. What is most significant is the political support the EDU has been able to gain during the last 3 to 4 years for its approach and method of economic planning in Dominica. Essentially it is a sectoral approach based on project identification from below because the political direction and participation in the planning process was possible given the environment in Dominica only at the bottom level where the finance in terms of dollars and cents was discussed and understood. Thus, the capital estimates of projects have to be the starting point in the planning process. These projects have to be so chosen that they would fulfill the objectives and goals notionally agreed.

The currently existing planning process in Dominica started with an instruction from the Cabinet to various Ministries⁵ to prepare sector paper/plan in order to help improve the management of the sector and capital budgeting within the sector.

The steps in the planning process in Dominica are as follows:

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- 4 Dominica is a Republic headed by a non-executive President. Executive power is exercised by cabinet headed by a Prime Minister. Legislative power is vested in parliament. Government policies are elaborated and executed by Permanent Secretaries and Heads of Departments, Units and Sections.
 - 5 These Ministries are Agriculture; Trade, Industry & Tourism; Community Development and Social Services; Immigration & Labour; External Affairs; Legal Affairs; Education & Sports; Health; Communication, Works & Housing; and Finance & Development.

- 1) The concerned Ministry in each sector appoints a National Coordination Committee (NCC) under the chairmanship of the permanent secretary.
- 2) The NCC discusses and prepares terms of reference for the sector plan. Appendix 3 presents the terms of reference of agricultural sector plan in Dominica as a sample.
- 3) The NCC also decides whether outside assistance is needed in the preparation of the sector plan and if so from whom, e.g. Food & Agriculture Organisation (FAO) is identified to provide assistance/consultants to prepare sector plans for agriculture and forestry. Similarly, UNESCO is identified for education.
- 4) The NCC closely monitors and reviews the preparation of sector plans by the consultants. It looks critically at methodology including projections of output, income and employment generated. Similarly, it considers strategy questions like what types of products to produce - for internal consumption or exports? How should they be produced? With what technology? Who should produce? Public sector or private sector? When to produce? Where to produce? For whom to produce? etc. are considered within the sectoral strategy.
- 5) Once the sector plan document is finalised by the committee, it is submitted to the Cabinet for approval and necessary action. The document so finalised by the NCC is also expected to prioritize projects and activities according to what it thinks appropriate. The NCC is made up of representatives from the sector in question and other relevant sectors in government, one member from EDU and two private sector representatives selected by the concerned Ministry. Once the sector plan is submitted to the Cabinet, the NCC is dissolved.
- 6) The Cabinet would modify the sector plan if needed in consultation with anybody it chooses and approve the sector plan.
- 7) The approved plan proposal is implemented through Budgetary Process which is separate and distinct. Hence the priorities set out in the sector plan may or may not be followed in the annual budgeting for the sector.
- 8) The budget process puts all the sector plans converted into budget proposals together at the macrolevel.

The EDU as an organisation has a crucial role to play in the whole planning process including the final stage of dovetailing of the budgetary and planning processes.

IV Economic Development Unit (EDU)

EDU is an institution within the Ministry of Finance and Development. It is headed by Development Co-ordinator who reports directly to the Minister of Finance and Development. The other wing in the Ministry is the Finance Department headed by the Financial Secretary. Chart 1 below presents the organisational structure of EDU. There are currently 36 persons working in EDU; 14 are class A employees, 12 are class B employees and 10 are class C employees. Moreover, there is a separate organisation called Development & Planning Corporation (DPC) whose ex-officio chairman is the Development Coordinator. DPC is a separate statutory body working in close collaboration with the Physical Planning Division of the EDU. As such, there are three divisions in the EDU, viz. (a) Physical Planning; (b) Economic Planning and (c) Property Valuation. These divisions are made for carrying out specific and distinct functions assigned to EDU. Currently, the EDU performs the following functions:

- i) Project appraisal;
- ii) Provides assistance in sector planning;
- iii) facilitates external funding of projects and programmes;
- iv) administers development and building control;
- v) prepares inventory of property with values;
- vi) manages public sector investment programme (PSIP); and
- vii) provide technical assistance and advice to the political directorate.

More specifically, the Physical Planning Division is responsible for function (iv) listed above which basically aims at ensuring most efficient use of the country's land resources in all aspects of development; the Property

Valuation Division is responsible for function (v) listed above which is essentially required to develop a uniform and equitable property taxation system; and the Economic Planning Division performs the rest of the functions listed above except function (vii) which is performed by each of the divisions as and when required.

As can be seen from the organisational chart of EDU presented here, the Economic Planning Division is further divided into two sub-divisions viz. Project Development Sub-division (PDS) and Macroeconomic Analysis Sub-division (MAS). The PDS is headed by a Senior Planning Officer (SPO) and its main function is to facilitate management of PSIP. 5 Planning Officers (POs) each assisting different Ministries/sectors report to the SPO. These POs assist different Ministries in project identification and development. The PDS also provides information on donor funding, liaison on funding negotiations and administration and help in securing funds for specific public sector investment projects in various Ministries. The PDS is not directly responsible for implementation but is involved in it to the extent of implementation of plans, management information system connected to the project, external sources for finance for the project, monitoring and evaluation in collaboration with Ministries. The PDS maintains important data base on PSIP on computer. The basic source of the PSIP information is the Ministry of origin. The PDS assembles it and puts it in an organised way. There are four categories of PSIP:

- a) Funded out of external grants
- b) Funded out of external loans
- c) Funded locally by government revenues and sources
- d) Funded locally by government borrowings.

Data on expenditures by years and ongoing/proposed/conceived projects with project cost and funding agency is maintained and regularly updated on computer at EDU. It is interesting to note that all these data on PSIP on computer at EDU are in financial terms only. Physical targets and achievements are not maintained in the same way. Thus, what EDU monitors is the financial or expenditure performance only.

The main contribution of the PDS is in terms of techno-economic appraisal of capital projects of different Ministries and sectors. The PDS looks into the technical soundness of the project basically in terms of the following:

- a) clearly defined outputs and inputs;
- b) estimates of the quantities required of inputs and consequent quantity of output;
- c) location of the project;
- d) availability of technology;
- e) clear project design detailing the steps to achieve outputs;
- f) physical resource availability;
- g) skill requirement and
- h) supply of manpower.

The financial analysis of the project is carried out in terms of economic prices so that the viability of the project is assessed from the social viewpoint. The financial viability is checked only if the nature of the project demands e.g. Dominican Banana Marketing Corporation. The economic appraisal of the projects usually ignores the environmental costs and benefits. Similarly, the economic prices used in the analysis are derived by adjusting taxes and subsidies. The shadow wage rate is assumed to be 80% of the actual wages. The rate of return on capital is assumed to be at least 7% for the government projects and 12% for the other projects because these are the rates at which funds can be borrowed from the commercial banks. Net Present Value (NPV) and Internal Rate of Return (IRR) are used as the criteria.

In spite of such an elaborate exercise of project appraisal and the required skilled manpower available for doing it, it is clearly recognised that the ultimate investment decisions taken at the top level are political in nature - not necessarily dependent on economic return from alternative projects. As a result, process is modified. The decisions about the project selection out of alternatives as well as about their priorities are taken first. Then, they are appraised as a routine. Therefore, the project gets rejected, if at all, only when it turns out to be totally non-viable. In most cases, thus, the projects sent for appraisal to EDU enters the capital budget of the concerned Ministries. The process of sending the projects for appraisal to EDU seems to be more on account of fund hunting than testing economic viability of the proposed projects. In any case, this part of the planning process is extremely crucial because it links the sector plans with the budget process through EDU.

The Macroeconomic Analysis Sub-division (MAS) of EDU is in overall charge of providing the macroeconomic perspective to the economic development policy of the government. Its main task is to help different ministries in the preparation of their sector plans. Once these plans are made, the MAS is supposed to put them together to evolve a national economic plan by dovetailing the sector plans with one another. A three year national plan is on anvil. EDU will have to monitor and review the progress of the plan annually. The sector plan philosophy is based on the concept of planning from below. Capital projects and their budgeting in respective Ministries is the starting point. The national objectives and goals are arrived at by consensus. Projects to achieve these objectives are identified in the sector plan from the bottom. This is a learning experience for all involved in the whole process including the experts from international agencies like IMF who sometimes attend the sectoral coordination committee meetings discussing the sector plans.

Although there is a strong feeling about the need for a macroframework for the National Plan among a few officers in different Ministries including even EDU, the vision of the top official in EDU shared with conviction by other permanent secretaries in the Ministries does not consider it as a major constraint in the exercise. The presence of the member of the EDU in the meetings for sectoral plan preparation should ensure that the overall national development philosophy is not at variance with the sectoral strategies, but that they are internally consistent. As per the vision, the sector plans should not be merely the technical documents prepared and owned up by technocrats, but they should be people's choices reflecting political processes culminating into political commitments. Currently, however, outside consultants are preparing the sector plans. What is likely to emerge out of the sector plan exercise is at best a listing of alternative feasible strategies and programmes for the sectoral development. Within each scenario, priorities would be assigned by the technocrats. The EDU will have to consider all sector plans and give its feedback to each sector which may have to relook at its plan and revise it. Thus, as iterative method of closer and closer successive approximations is envisaged for national planning in Dominica. This model of planning from below in terms of physical flows of project proposals emanating from below is countered with budgetary financial flows in the opposite direction. These two flows and their consistent reconciliation completes the process. Its role in future is likely to be much more important than so far. This is because there has been a considerable achievement to the credit of EDU over the past 3 to 4 years, viz. (i) of late the term 'economic planning' is accepted as development management although the political philosophy is against the term 'planning'; (ii) Minister working in consultation with officials is accepted and also selectively practised; (iii) concept of project profiles with priorities is accepted and implemented; (iv) the need to synthesise sector plans is recognised by the Prime Minister; etc.

These achievements clearly focus on a very important role of EDU, viz. training and dissemination of information and technology. The permanent secretaries in different Ministries have to be taken into confidence and the whole methodology including iterative character of the process has to be explained to them. Whenever a new PS takes over, the process of training him has to start at EDU. The argument against not putting the methodology and the processes in writing is that informal things have better chance of acceptance than formal communications or written manuals because the latter usually provokes resistance and a tendency to negate among the participants. Similarly, the EDU also believes that sometimes it helps not to coordinate, e.g. the circular inviting the capital budget proposals which the EDU has to consider is sent independently and earlier than the routine finance department's circular. Thus, EDU does not view its role merely as a government sub-division in charge of preparing a plan, but it believes in managing the system to invoke participation and political commitment to the plan.

V Interlinkages with Budget Process

The budgetary process is a separate process taking place every year. The centre of this process is the Finance Department. Since both the planning function and budget function have to be consistent both internally and with each other, the EDU and Finance Department are put under the same Ministry. Both the functions have to rely on elaborate processes integrating the proposals of all the Ministries and public sector undertakings. The Finance Secretary who heads the Finance Department is in charge of the overall budgetary processes, though the preparation of budget is the task of the Fiscal Adviser to the Minister of Finance. The Fiscal Adviser also currently prepares an annual review of the functioning of the economy to be incorporated as the opening part in the budget speech of the Finance Minister.

The budgetary process deals with the recurrent expenditures and capital expenditures by different Ministries. The budget process consists of the following steps: To begin with, Ministry of Finance and Development sends a circular signed by FS and DC to various Ministries inviting their budget proposals. In this circular macro

targets are given, crucial assumptions about inflation, taxation etc. are outlined as a guideline, and specific instructions about capital estimates are given. Appendix 4 below presents summary of circular No.1 for 1991-92 dated January 17, 1991. It may be noted that the circular clearly distinguishes between the PSIP and the projects included in the capital estimates. The latter are financed out of the surplus on current account after meeting the debt repayments, whereas the former have to be financed out of external grants and borrowing and domestic borrowing. Therefore, while the PSIP projects can be included in the budget proposal without confirmed sources of finance, projects included in the capital estimates must have identified confirmed sources of finance.

The second step in the budget process consists of having the budget period meetings. These meetings are organised individually for each Ministry to discuss its budget proposal. The Budget Committee consists of representatives from Ministry of Finance, EDU and the relevant Ministry. The proposals for the recurrent and capital expenditures are discussed and kept pending for finalisation at the end. The third step in the process is to finalise the proposals already pruned in the initial discussion. This takes place in the Ministry of Finance and Development under the chairmanship of the Finance Secretary. Then, the finalised budget proposals are sent to the Cabinet for modification and approval. The Prime Minister presents the bill to the Parliament which approves it after discussion and modification if necessary. Generally, the Parliament does not modify the bill.

In this entire process, there are some important checks inbuilt so as to ensure consistency between the planning process and the budget process. First of all, the Permanent Secretary in various Ministries are basically in charge of preparing both the Plan proposal and the Budget proposal. Secondly, representatives from EDU are members of crucial sectoral committees in both the processes. Thirdly and most importantly, EDU has been given a very important control in the form of project appraisal function. Thus, the set procedure is that the projects have to be assessed/appraised by the EDU before it enters budget discussions. Further, the implementation plans must be submitted to EDU before the approved funds are disbursed. In this way, EDU can effectively monitor and ensure that deviations and departures from the approved plans are not taking place at the time of implementation. This is not a provision only on paper, but it is also used as a control when required. A departure in a livestock project was turned down recently by EDU and hence the funds never got disbursed.

As we have discussed earlier, the planning process works in such a way that only selected projects out of various alternatives are referred to the EDU. The selection of such projects takes place in the sector plan proposal. Out of these projects only prioritised projects are sent by the PS to the EDU for appraisal and fund hunting. When the EDU reports back, the projects with funding assistance would be included in the budget.

In this way the two processes are not expected to produce conflicting or inconsistent project priorities. The planning process is considered the fundamental process assigning priorities within the overall developmental strategy to achieve national goals. The budgetary process is the supplementary process to implement the plan. It is, however, argued that the actual operation of the two processes in Dominica does not ensure full consistency because the selection of the project for inclusion in budget proposal within each Ministry is not strictly dictated by the plan priorities but by the availability of external finance.

VI Limitations

There are several limitations of the economic planning exercise in Dominica. We briefly discuss them as follows:

1) *Lack of Macroframework*: Given the historical background of economic planning in Dominica, while one can appreciate the efforts of EDU to inculcate the culture of political participation in macroeconomic management in general and management of economic development in particular, the need for overall national economic development strategy cannot be overemphasised. Currently, the sector plan preparation lacks direction and guidance usually provided by the overall macroeconomic framework of the national plan. There is a good possibility that different sectoral plans would be prepared with entirely different - many a times internally conflicting strategies. Moreover, the macroframework is again not totally absent. As can be seen from Appendix 4, the circular inviting budget proposal does indicate overall budget ceiling for each Ministry. These ceilings are right now decided largely on historical pattern and partly on other considerations like foreign exchange implications, etc. If there exists a macro framework for the plan, the budget ceiling to Ministries could be used as an effective instrument. The macroframe may emerge over a period of time since Dominica has only recently started taking economic planning more seriously, but, at present at least this is a serious

limitation. This is also because without such a framework the internal consistency of sectoral targets, resource use pattern and potential interlinkages could seriously suffer.

2) *Lack of Coordination & Integration:* A very related aspect is that of coordination and integration of interdepartmental and intersectoral proposals. The sectoral planning committees are formed in such a way that it includes representatives from the related ministries - but in itself this may not ensure integration of the proposed plan which in any case is prepared by outside consultants. The coordination of targets in different sector also plays crucial role. In order to achieve this, iterative method of successively closer and closer approximation of planning is suggested. However, the practicability of such elaborate and time consuming processes raises doubts particularly in the context of the external consultants doing the job of preparing the sectoral plans within the framework of the given terms of reference (See Appendix 3 as an illustration). Even the rapidly changing environment would have an impact on the priority structure to convert the medium term plan into an exercise of contingency planning. Moreover, lack of coordination even among the EDU and the Finance Department is reflected in the fact that the proposals for loan borrowing are not brought in the debt-management system, converting the latter only into a debt-accounting system. Uncritical acceptance of debt-financed projects in the budget when the funding source is suggested by EDU is the example of such an uncoordinated system.

3) *Lack of Political Commitment:* The politicians are educated but not sensitised about the role they are expected to play in the planning process. There is ambivalence, lack of interest and lack of political directorate in the planning process in Dominica. Naturally, therefore, the sectoral plans do not become plans with political commitment. They remain merely as the technocrat's plans. People's representation and participation in the whole planning process remains superfluous. Currently, the sectoral committees include representatives from private sector, but they are appointed and not elected. Political representation on these committees is not yet achieved. As envisaged originally, the sectoral committees were to be consisting of representatives of people so that real issues and projects are freely debated and discussed. What was expected to emerge was only a sector paper and not plan. However, overenthusiasm to implement the ideas in the absence of permanent DC resulted in the current situation where the spirit of the process is ignored. Lack of political commitment and existence of external consultants are the major lacuna in the current planning process in Dominica.

4) *Lack of Decentralized Processes:* The political organisation of Dominica is such that it has a detailed structure of local government administered through thirty-two Village Councils, Portsmouth Town Council and Roseau City Council. Village improvements committees exist in every village and in several neighbourhoods in Roseau and Portsmouth. Several small projects including self-help schemes have been carried out with the assistance of these village councils. At district level, in all seven District Association of Village Councils exist who receive technical advice from the Department of Local and Community Development of the Ministry of Home Affairs and Housing. However, these councils have not been involved effectively in either plan formulation or implementation process. Coordinated and integrated development efforts at the district level do not exist in Dominica. The EDU officials feel that such decentralized planning processes would still take a long time because the processes even at central level are not yet in order.

5) *Lack of Statistics:* In terms of collection, compilation and estimation of basic statistics required for economic planning and economic management, Dominica is seriously lagging behind. Firm estimates of saving, investment, even literacy, etc. are not readily available in the statistical office. For such estimates, the country has to rely on external agencies like Caribbean Development Bank or World Bank or IMF. The statistical office which has meagre staff strength of only 3 persons is located within the Finance Department rather than EDU. Moreover, even the priorities of the statistics department are not properly fixed by higher authorities. As such, useful information does exist in the system but well directed efforts are lacking for collecting, compiling and presenting the data for planning purposes. With the result, planning without adequate data base is encouraged. This can result in serious distortion and wastage of resources.

6) *Lack of Skilled and Trained Personnel:* Dominica is a small island. It does not have general institutions of higher learning. The stock of skilled and trained personnel to carry out the planning or management jobs in the government service is extremely limited. This is recognised as an explicit constraint in the progress of planning in the country. Ability to comprehend abstract concepts and issues related to the economic management of the country's various sectors is seriously limited among the politicians as well as the bureaucrats. EDU's role in training personnel and disseminating information is therefore assuming significance as a precondition for successful planning processes.

7) *High Degree of Openness*: The smallness of the country makes it highly open economy dependent considerably on trade. Moreover, the structure of Dominica's trade also makes it more vulnerable to severe fluctuations resulting from the ever changing conditions in the foreign currency market. Dollar-Pound parity fluctuations can play havoc to Dominica. Since Dominica's currency (EC\$) is pegged to U.S.\$, it loses control over certain domestic policies like the monetary policy. Moreover, since it shares its currency with 6 other nations through ECCB, it also does not have any control over the foreign exchange rate policy. Thus, only fiscal policy and incomes policy are the instruments in the kitty for the Dominican government. Very long term or even medium term economic planning, therefore, has inbuilt limitations in such conditions. However, management of development responding to the environmental stimuli as is being attempted in Dominica is possible. What is required is much more understanding and commitment of people to achieve the desired goals in given time.

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Appendix 1

Excerpts from National Structure Plan, Dominica, 1976-90

The major goals and objectives of the National Structure Plan for Dominica are

- (a) Maximise the use of available land resources in a manner that will increase employment and reduce disparities in income, between rural and urban areas.
- (b) Develop a system of urban and rural settlements commensurate with the location of resources, in a manner that will permit provision of infrastructure and other facilities on an economic basis.
- (c) Improve existing level of infrastructure facilities and services to desirable standards and propose new facilities and services wherever needed, to facilitate optimum utilization of available resources.

The scope and purpose of the National Structure Plan for Dominica are as follows:

- (a) to propose an integrated physical structure of development taking into account spatial constraints, potentials and implications;
- (b) to formulate a generalized countrywide land use plan, which will identify areas of agricultural and settlement growth and communication network that is consistent with the development strategy;
- (c) to provide a set of development guidelines and recommendations for the use of land and the control of urban growth which will maximise production and social benefits and minimise costs;
- (d) to provide implementation recommendations including identification of priority projects and other special studies.

The elaborate planning models followed elsewhere for bigger countries have been simplified in the case of Dominica. A schematic diagram overleaf gives the planning model. (Figure 1.1)

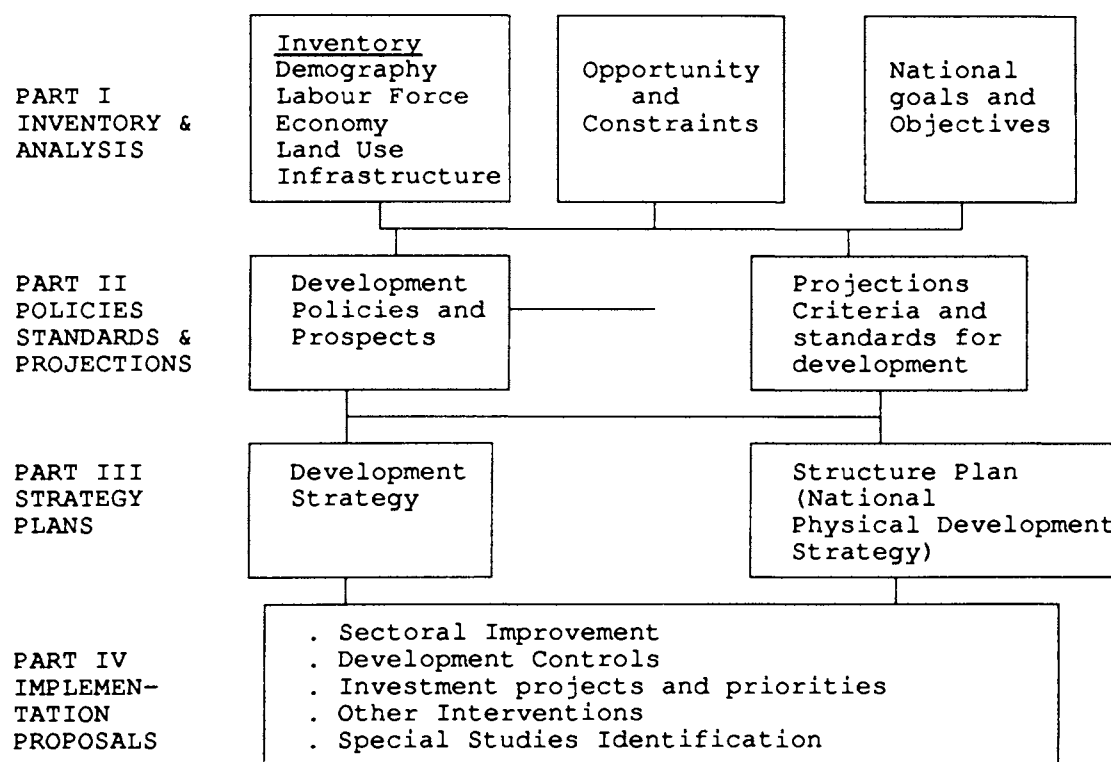


Figure 1.1 : Schematic Design of National Structure Plan for Dominica

Appendix 2

Excerpts from Dominica: National Structure Plan, 1985

1.3 An example of the effect which economic policies may exert on spatial development may be given by the case in which economic development policies emphasise rapid industrialization through the adoption of capital intensive technology. In the case of Dominica locational advantages would probably lead to many industries being located in the Roseau region. This would attract jobseekers from the rural areas to Roseau and accelerate the growth of the city. The rapid growth of the city would place a great strain on municipal and social services and produce the well known social problems associated with rapid urbanization in developing countries. Similarly, fiscal and tax policies may operate to encourage food imports and thus discourage food production in the rural areas of the country. This would, in turn, contribute to, at best, a stagnation in rural incomes, or lowering of rural incomes thus compelling young farmers or would be farmers to leave the rural areas for the city. On the other hand, the size and distribution of human settlements may facilitate or impede the delivery of services, thus affecting the design of social policy. For example, it may be difficult to achieve many objectives of social policy with a very dispersed settlement pattern while a more nucleated pattern of settlements connected by adequate communication networks would provide a better spatial configuration for the attainment of social objectives.

1.4 Given the fact that spatial and socio-economic patterns affect each other it is not enough that spatial planning merely responds to the effects of social and economic policies, solving problems of urbanization created in part by economic policies. It is essential that the spatial implication of alternative social and economic policies should serve as an essential input into the formulation of development policy if undesirable impacts of social and economic policies are to be avoided or, at least, mitigated, leading to the attainment of major social goals. Thus, to produce optimal results, economic and spatial planning should be an integrated process, each discipline benefitting from and reinforcing the other in a continuous process of interaction.

2. Objectives of the Structure Plan

A structure plan is a set of decisions regarding the long- term future of an area in terms of its economic, social and physical development. It sets out, in broad terms, long term policies for development of the area and provides a general framework for decision-making in the development process. Following the prescription set out in the authoritative manual, *Development Plans*, the Dominica Structure Plan will perform the following functions -

- a) interpret national development policies in spatial terms.
- b) establish policies for the spatial development of the nation commensurate with national, social and economic goals.
- c) indicate action areas, that is, priority areas where immediate action must be taken to solve pressing problems.
- d) provide a framework for local and area plans - the policies and proposals of the structure plan will form a general basis for more detailed planning on area and local level.
- e) provide a coordinated basis for the development of individual programmes by various sectors such as housing, roads, utilities, health and education.
- f) provide guidance for development control. The structure plan will propose general development policies for such areas as location of housing, community facilities, and industries.

3. The Goals of the Structure Plan

The overall goal of the plan is to improve the welfare of the people of Dominica and the major development goals to achieve the improvement in people's welfare are the following:

- 1) to develop policies which will ensure that the basic needs of the people are met.
- 2) to develop development strategies which are implementable within the context of physical and financial constraints.
- 3) to promote greater self-sufficiency in food production.
- 4) to increase the availability of basic goods and services to all the people.
- 5) to locate development strategy components in such a way as to promote the integration of urban and rural economies.
- 6) to propose strategies which increase opportunities for productive employment in urban and rural areas.
- 7) to propose a national human settlement policy which will maximise production and increase welfare throughout the nation and maintain an optimum balance in the use of land among competing uses especially between human settlement and agricultural uses.
- 8) to propose a planning process which will ensure the integration of a spatial policies with sectoral policies on a regular and continuous basis.

Appendix 3

Draft Terms of Reference for Agriculture Sector Plan (Dominica)

1. review of Performance of the Agricultural Sector
2. develop goals, objectives and strategies for the sector which will guide the sector's development during 1991 to 1994;
3. identify appropriate areas of emphasis on a sub-sector basis including linkages with Tourism, Agro-Industry, Forestry and Fisheries;
4. set targets for production, foreign exchange and employment;
5. identify appropriate support programmes in:
 - (a) Input, supply and credit
 - (b) Research and Development
 - (c) Training and Extension (including manpower requirements and training needs of the agricultural sector)
 - (d) Intra and Extra-regional infrastructure including marketing, roads, etc.
 - (e) Technology
6. identify major resource and institutional requirements to implement Capital Projects; and develop preliminary profiles to include cost estimates;
7. develop an implementation strategy for the Sector including the allocation of institutional responsibilities and interministerial/intersectoral linkages;
8. identify a monitoring evaluation and review mechanism for the Sector Plan.

Appendix 4

Financial Secretary's Circular No.1/91 To Permanent Secretaries of all Ministries dated January 17, 1991. Subject: Budget Estimates 1991/92

Salient Features

1. Macro targets are projected based on projected nominal GDP growth of 9.5% - Expenditure and Revenue target figures in EC\$ millions are given as it is given in the summary Table in budget. This is for keeping in view the overall macro constraint.
2. The Revenue projections are made on the basis of normal growth expectations without any changes in tax and duty rates.
3. Recurrent expenditures by each Ministry should be kept within the limits indicated for each of them.
4. Projected inflation rate of 4% is assumed - Each Ministry should keep price adjustments within 4% limit.
5. Recurrent expenditure proposals must include an updated description of the year's programme giving quantitative targets and past years performance wherever possible. Proposal for expenditure must bear direct relation to the targets indicated.
6. Since the amount of savings for capital financing projects is limited to only \$7.5 M. projects must be carefully prioritized.
7. Heads of Departments/Accounting Officers must identify carefully the source of financing for each capital expenditure project so as to access as much grant funding as possible.
8. Financing by domestic borrowing should be limited to as low a figure as possible so as to allocate a larger share of domestic savings to private investment.
9. Dates and times for scheduled discussion of budget submission will be advised.
10. The estimates reflect government's plan of operation in each Fiscal Year.
11. All projects included in capital estimates must have identified and confirmed sources of finance.
12. PSIP on the other hand may include projects without confirmed sources of finance.
13. All projects in capital estimates must be submitted along with the project profile or project document.
14. Development of Annual Estimates is a development management process which involves considerable discussions at the level of divisions, the originating ministry, the Ministry of Finance and Development and finally at the level of the Cabinet, before it is finalised.

The macro-targets given in circular:

in EC \$ million	
Recurrent Revenue	138.2
Recurrent Expenditure	123.9
Salaries & Wages	(73.1)
Retiring Benefits	(6.5)
Goods & Services	(26.2)
Interest Payments	(8.2)
Transfers (In public sector with subventions etc.)	(9.9)
Current Account Balance	14.3
Less Debt Repayment	(6.8)
Local Contribution to PSIP	7.5
Capital Revenue	3.0
Capital Expenditure	58.3
Overall Deficit	47.8
Financed by:	
External Grants	20.5
External Loans	15.2
Domestic Borrowing	12.1

Chapter 3

Economic Planning in Tanzania - Framework and Possibilities

1. Introduction

After independence in 1964, the United Republic of Tanzania consisting of the mainland and Zanzibar had separate plans for the two upto 1981. The Tanzania Mainland implemented three medium term development plans: the first one from 1964-65 to 1968-69, the second one from 1969-70 to 1973-74 and the third one from 1976-77 to 1980-81. These three plans were part of the first long term perspective plan (1964-65 to 1980-81). The annual plans implemented during the period were a means to achieve the objectives and targets set for the medium term (five year) plans and thereby the perspective plan. Zanzibar on the other hand did not have a long term perspective plan nor medium term plans during this period. Thus, not only that both these major constituents of the United Republic prepared and implemented their plans separately but their planning organizational procedures were also different. However, the overall planning objective in both the cases was the same viz. improvement of the people's lives. Ever since the promulgation of the Arusha Declaration in February 1967, the guiding principles in the pursuance of this objective have been the ones of socialism and self-reliance.

The policy of socialism and self-reliance stresses the following:¹

- (a) Participatory decision making to give people effective voice in matters affecting their socio-economic development.
- (b) Public control over major means of production and exchange (land, financial institutions, industries, big estates, import-export trade, etc.)
- (c) Broad-based rural development, as most Tanzanians live in rural areas. The first step towards this objective has been villagisation, that is, grouping traditionally scattered peasants, households into organized settlements. This strategy offered the only quick approach to the provision of basic economic and social services to the majority of the population.
- (d) Self-reliance in national and local development efforts - to the greatest extent possible. External assistance (finance, expertise, etc.) in the implementation of projects deemed necessary for self-reliant growth in later years is not inconsistent.
- (e) Economic growth as essential for improving people's lives.
- (f) Equitable income distribution between worker and peasants as well as between other socio-economic groups.

Based on these principles, the first long term perspective plan involving both parts of the United Republic of Tanzania (Mainland and Zanzibar) was launched on 1st July 1981. Two medium term (five year) plans have been implemented so far. The first Plan was from 1981-82 to 1985-86. The Second Plan started from 1988-89 and would end in 1992-93. It is important to note that on 5th February 1977, the two political parties, viz. AFRO-SHIRAZI in the islands and TANU in the Mainland merged to form a single party - CHAMA CHA MAPINDUZI. The merger was prompted

¹ Reproduced from P.1 of *Long-Term Perspective Plan 1981-2000*, United Republic of Tanzania (1981).

by a serious consideration of the political situation and the realization that presence of two separate political parties dissipated efforts in the struggle for socialism and self-reliance.

In the present paper, we propose to examine the existing framework for economic planning and the possibilities for improving the planning practices in Tanzania. In the next section we outline briefly some of the well recognized weaknesses in the past planning approach and institutional framework existing in Tanzania which weakened the role of planning as a tool for effective management of the national economy. We, then, discuss in the third section, the role, functions and the structure of the Planning Commission which became operational in Tanzania with effect from July 1, 1989. In the fourth section, we briefly describe the planning process in Tanzania. The methodology followed so far in the preparation of plans is discussed in the fifth section. In the last two sections of the present paper, we discuss the possibilities of using input-output statistics to improve the planning practices in Tanzania.

2. Limitations of the Past Planning System

The planning system in Tanzania before July 1989 was not very well conceived in terms of its role, functions and linkages with the overall management of the economy. More precisely, the well recognized weaknesses of the planning system in Tanzania before July 1989² can be described as following:

- (a) The development plans mainly took the form of compilation of projects proposed at different levels in the regions and ministries submitted to the planning ministry for allocation of the government funds for implementation. As a result, the plan formulation and monitoring procedures emphasized only the monetary expenditures rather than the physical target component.
- (b) In the plan formulation and implementation, contributions of the implementing agencies and/or people themselves were not adequately harnessed.
- (c) Previously, the whole approach was isolationist in that each individual institution was concerned with soliciting the government funds for its own projects. This led to several inconsistencies and operational problems since vital inter-sectoral linkages could not be adequately taken into account.
- (d) The planning system defined its role only in terms of focussing on new investment projects. The management of already existing economic activity was not considered a subject of planning. As a result, there were no plan-based strategies for tackling such economic problems as shortages of foreign exchange, underutilization of capacity in industries, crop haulage problems, etc. which used to be ultimately handled through the 'crisis management' approach.
- (e) The system gave almost exclusive attention to projects at the pre-operational stage rather than at the operational stage also. The procedures for rationalizing development expenditures and operational costs were, therefore, not adequately developed.
- (f) On account of inappropriate planning methodology and processes, number of investment projects depending on the government funding increased tremendously in Tanzania which also led to thin spread of scarce resources over a wide range of projects resulting in poor performance and impact.
- (g) Mobilization of external investment resources was not systematic. Donor preferences rather than national priorities dictated the location and design of the projects. Appropriate planning centres properly guided by approved national plan were hardly consulted in the selection of projects for funding by external donors. This led to departures from national plan priorities and sometimes to the problems in management of external debt.

² See for instance, *Profile of the Planning Commission of the Union Government, United Republic of Tanzania, July 1989.*

3. Planning Commission

With a view to giving a new impetus to economic planning and to correcting the abovementioned weaknesses in the system, the Planning Commission was established by Act No.11 of 1989 passed by the Union Parliament in April 1989 in Tanzania. The Commission became operational from July 1, 1989. It is expected to make changes in the current planning and implementation system and bring about a more effective planning approach.

3.1 Functions of the Commission: The Planning Commission in Tanzania is made responsible for the management of the national economy and for supervising the planning process as well as monitoring the implementation of approved plans. More precisely, the functions of the Commission include:³

- (a) to assess the state of the nation's investment resources and advise the Government on their most efficient allocation and utilization. Those resources include: all foreign exchange resources; domestic finance and credit; Government Budget; external loans, grants and technical assistance; parastatal surpluses as well as physical and human resources.
- (b) to analyze trends in key economic variables, including balance of payments, money supply and prices, and advise the Government accordingly.
- (c) to analyze various existing policies, with a view to strengthening their implementation and to propose new policies where necessary and in the national interest;
- (d) to monitor the day-to-day performance of the various sectors of the economy and ensure that appropriate measures are taken to solve any operational problems that may have been identified in those sectors;
- (e) to issue guidelines on economic relations with other countries and international organizations;
- (f) to issue guidelines concerning the formulation of national plans particularly on the preparation of long term, medium-term and annual plans;
- (g) to oversee the implementation of plans for the purpose of achieving the most effective and balanced utilization of national resources;
- (h) to monitor the implementation of plans and take such measures as are necessary to ensure their successful implementation;
- (i) to advise the Government on changes that may be necessary in approved plans;
- (j) to monitor the implementation of Government decisions relating to planning and management of the economy;
- (k) to devise appropriate strategies for the development of science and technology in the country;
- (l) to analyze current social and economic problems with a view to recommending to the Government appropriate policies and measures to be taken in order to deal with such problems;
- (m) to develop national planning methodology as well as to ensure that planning units in ministries, regions and other public institutions are established and adequately staffed with qualified planning personnel.

3.2 Position and Powers of the Commission: The Planning Commission in Tanzania is placed directly under the office of the President as an independent department of the government. It is answerable to the Cabinet which, in turn, is answerable to the Parliament and the Party. However, all the ministries and the regions are required to report to the Commission. The Commission is the highest advisory body to the government. Thus, the Commission has the power.⁴

- (a) to give ministries, regions and districts any directive relating to planning and management of the economy as approved by the government;

³ As given on p.2 and p.3 of *The Profile of the Planning Commission of the Union Government, The United Republic of Tanzania, July 1989.*

⁴ Ibid.; p.4.

- (b) to direct and specify, in accordance with government decisions, priority activities in which investments may be made;
- (c) to approve changes in the implementation of plans;
- (d) to call for, from any institution, any information or statistics relating to planning and economic management generally;
- (e) to prescribe, as appropriate, national planning procedures.⁵

3.3 Structure of the Commission: The Commission consists of eight members, including the President who is the Chairman of the Commission. The other seven members appointed by the President include (i) the Vice-Chairman who is a full time member; (ii) three other full time members, and (iii) three part-time members including the Ministers for Finance of the Union Government. The Commission is aided by the Planning Commission Secretariat headed by the Secretary to the Commission. He is assisted by two Deputy Secretaries - one in charge of (a) Macro Planning Division, (b) External Sector Division and (c) Human Resource Planning Division; and the other in charge of (d) Regional Planning and Rural Development Division, (e) Agriculture and Natural Resources Division, (f) Industry and Minerals Division, (g) Economic Services Division, and (h) Social Services Division. The ninth division of Plan coordination and Monitoring Division is directly under the Secretary to the Commission. Moreover, there are two units viz. Planning Unit and Finance and Administration Unit in the Commission Secretariat to look after the compilation, analysis and storage of statistical data and the regular administrative chores of the Commission Secretariat.

Moreover, the following institutions are placed under the direct supervision of the Planning Commission in Tanzania: (a) Bureau of Statistics, (b) Price Commission, (c) National Productivity Council, (d) National Science and Technology Commission, (e) Rufiji Basin Development Authority, and (f) National Radiation Commission. There are several other institutions which provide important technical support to the Commission with close working relations. The commission can also develop contacts and consultations with various local and international organizations for harnessing useful expertise and experience in the field of planning. With such a major institutional change, it should be possible to make far-reaching significant changes in the national planning system in terms of methodology, processes and monitoring of economic development efforts in Tanzania.

4. Planning Process

As it is already noted, Tanzania has a single party democracy. Basic ideological differences among political leaders or the representatives of people on the decision making bodies at different levels do not exist in such a set up. The entire planning process in Tanzania to this extent is simplified by the existing political system. Before the Planning Commission was established, the approach to national planning in Tanzania was mainly sectoral. Since the Planning Commission has been established only recently, the approach and processes have remained more or less the same so far. The planning process effectively utilizes the existing politico-administrative structure at the regional levels. Every sectoral department/ ministry has vertical links at the regional and sub-regional levels. Such links are not sectorally interdependent but are sectorally independent. Moreover, in every ministry/department, planning entities/cells exist. At the regional and sub-regional levels, planning officers in different departments are in charge of planning the activities of their departments at the appropriate regional levels. However, at different regional and sub-regional levels, Tanzania has an elaborate political structure which is also utilized in the planning process through establishment of regional/sub-regional development councils which consider the proposals from planning officers in various departments working in the regions and consolidate them into a plan proposal at the respective regional levels. Such regional/sub-regional plan proposals are then sent to higher regional levels for their incorporation in their plans. Thus, plan proposals emanate from below in the planning process in Tanzania. People's participation is also seen to be taken into account through the development councils at

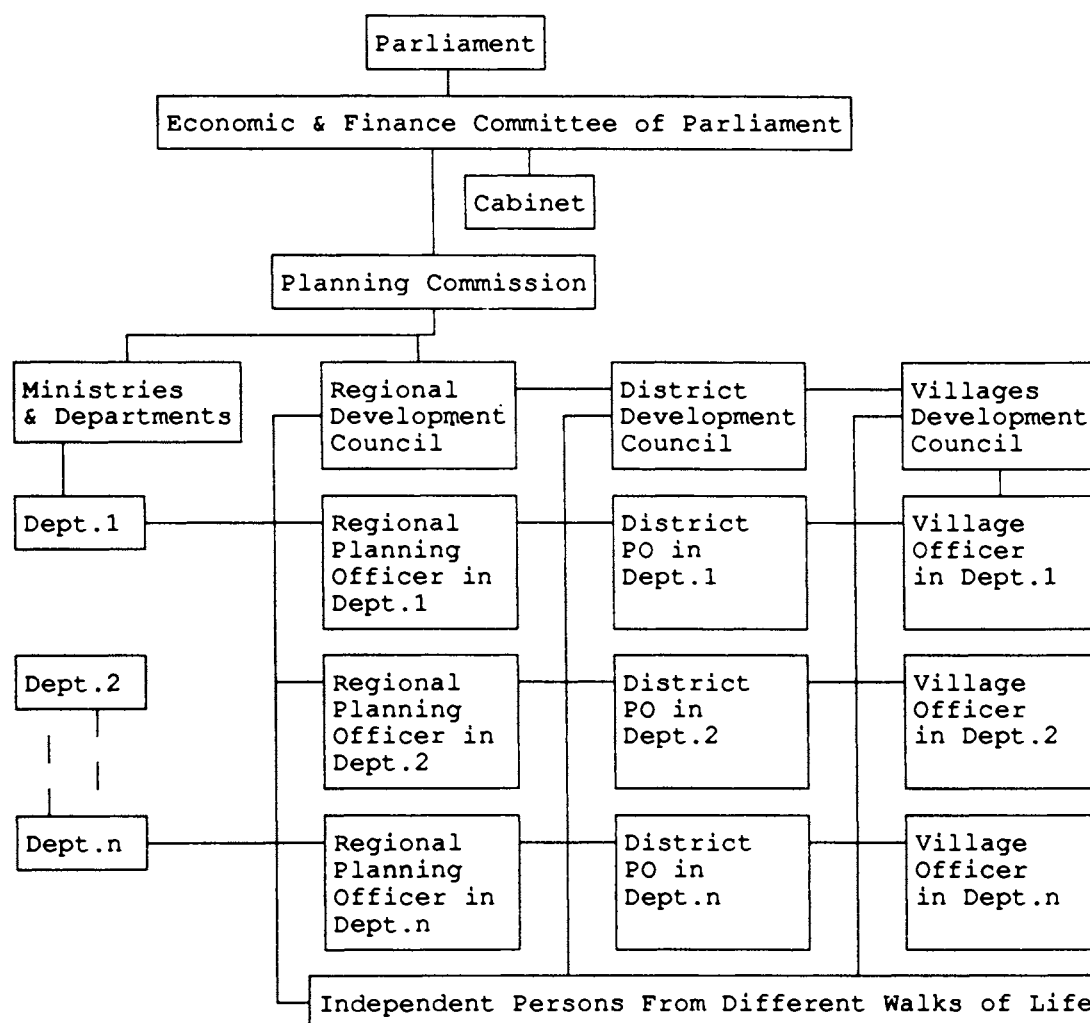
⁵ It may be noted here that so far (i.e. Oct.1990) the Planning Manual has not been prepared in Tanzania.

different levels. Schematically, the Planning machinery in Tanzania can be represented as in Chart 1.

At the national level, the planning process consists of the following steps. With the establishment of the Planning Commission, it prepares a tentative budget frame indicating financial priorities assigned to various sectors within the overall macroeconomic framework considering the estimates of some crucial parameters and constraints at the national level. This exercise is very similar to preparing an 'approach paper' for the plan. This budget frame is then put before the Cabinet for modification and approval. The Cabinet sends such a proposal after approval to the Ministry of Finance for raising adequate resources and to the Planning Commission for working out the details of the plan. At this stage, the Planning Commission gets the inputs from the regional and sub-regional units which are all put together to work out the details of the plan. After the details are worked out, the plan proposal is sent back to the Cabinet for its final approval. It is, then, referred to the Economic and Finance Committee of the Parliament for modifications and approval. The Committee then, sends it to the Parliament through the Finance Bill for specific financial allocation to different Ministries. The financial allocations are suggested by scheme and regions in different departments. Thus, the financial allocations are suggested by scheme and regions in different plan becomes a statutory document to be incorporated in the Finance Bill or the Budget. The Parliament is the final authority in the sense that it can amend or even reject an expenditure item in the proposed plan. Once the Parliament approves the plan, it gets implemented through various Ministries. The Planning Commission monitors the implementation generally by six monthly reports from every Ministry incorporating both the financial and physical components. The Planning Commission, however, does not enjoy any legal power to sanction against any particular department or ministry. Only the Economic and Finance Committee of the Parliament has such legal powers. The Planning Commission, therefore, relies heavily on this Committee for exercising its control.

At this stage, it is natural to inquire as to how overall macro constraints in terms of financial and physical resources could be considered in the planning process. In other words, if some overall consistency has to be observed in the national planning exercise, what mechanisms are provided in the process. This is a question pertaining more to the methodology of planning which we discuss in the next section.

Chart 1: Planning Machinery in Tanzania



5. Methodology of Planning

In the detailed discussions held with several officials in the Secretariat of the Planning Commission in Dar-es-Salaam, it was repeatedly emphasized rather apologetically that the planning methodology followed in Tanzania so far has not been very sophisticated. No systematic macro model of planning is followed. The broad methodology had tended to be based on learning from recent past experience. Thus, half yearly review of performance primarily meant for monitoring the implementation of the approved plan serves almost as a guide for future planning. Considering the discrepancies between the financial and physical achievements of the targets originally set, inquiring about the possible causes thereof, probing into the future prospects perceived and based on all these considerations trying to look ahead is the basic method of planning followed at the regional/sub-regional department levels. A list of physical projects proposals in each department at the appropriate geographical area unit level is formed which, then, gets prioritized through critical scrutiny and detailed discussions in the respective area development councils. Such a prioritized list of aggregate sectoral projects is then sent to the higher level of the geographical unit for its incorporation in the proposal of that geographical unit. As already noted above, the questions of overall consistency and recognition of macro constraints assume importance at this stage.

It can be seen from the above discussion that the process described so far is the 'bottom-up flow' which is mainly in the physical projects form. The macro-economic constraints and consistency requirements, on the other hand, are largely in the form of financial and physical resources. The Planning Commission passes on the idea about such constraints through tentative ceilings on financial resource availability in the form of guidelines to be followed to the regional/sub-regional levels. These are essentially 'top-down flows' in the planning process. These two flows have to be matched at different levels by dove-tailing the financial and physical components of the proposed plan of activities. In the process, the tentative financial resource ceiling prescribed earlier are adjusted considering the physical component of the plan of various geographical units and the stated national objectives and priorities. There is, thus, some degree of 'back and forth' exercise involved in the planning process. It is estimated that such an exercise takes about 6 to 8 months time. However, at the end of such an exercise a reasonably good sectoral allocation of resources based on decentralized decision making emerges.

The only substantial methodological questions that still remain are about the way of linking targets of overall growth with the availability of resources over time and about the criteria to allocate funds to different regions. The estimates of the resource availability - both external as well as internal - are worked out by individual components in the Treasury, Bank of Tanzania (BOT), Planning Commission and various financial institutions. Based on these estimates, an overall investment rate is estimated which presently works out to about 25% in Tanzania. The linkage of this estimate to the desired/target rate of growth of the economy over the plan period is basically a weak link in the whole exercise because, the estimates of incremental capital output ratio (ICOR) are considered so wild and unrealistic that they have been abandoned for planning purposes under the present circumstances. The link between the investment resource availability and the growth target in the economy over the plan period is based on some idealistic considerations based on distant past rather than current experience. The overall consistency of the macro plan, therefore, is not formally established. Intersectoral consistencies of plan targets are also not formally or even informally considered although some reasonably good estimates of a detailed Input-output Table (73 x 73 sectors) are available for Tanzanian economy for the year 1976. Although formally the employment generation aspect of the plan is not explicitly incorporated in the exercise, some aggregative estimates of labour productivity by broad sectors are considered but without any estimates of the labour and capital intensity of the activities.

Regarding the regional allocation of funds the methodology is again not very elaborate. Some broad criteria of regional weightage in terms of area, population and regional backwardness as revealed by the per capita regional incomes are considered for allocation of funds. Table 1 presents one such effort to use these indicators for actually allocating the funds to different regions. These criteria are only proposed and not yet accepted. They are meant to generate internal debate and discussion on the relevance and appropriateness of such a methodology so as to ultimately form a part of the Planning Manual. It is obviously recognized that several other considerations like preparedness of the region, nature of the proposed programme, donor's preference and counterpart fund considerations, etc. would modify such formula-based regional allocations of funds. However, they may serve as the first cut in the exercise. It is also currently debated in the relevant quarters in the Planning Commission to consider use of sectoral criteria like hospitals, dispensaries, primary schools, utilities like water, electricity, etc. to allocate funds to different regions by sectors (See Appendix A below). This might lead to some centralization of decision making but could prove very effective to address the national priorities in the fulfillment of plan objectives and targets.

Table 1								
Proposed Regional Resource Allocation in Tanzania based on Criteria of Income, Population and Area								
Regions	Per capita Income		Population		Area		Average Rank/Weight	Percentage of Resources to be allocated
	Amount in T.Sh. (1987)	Rank or Weight	in '000 (1988)	Rank or Weight	Km ²	Rank or Weight		
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
1. Tabora	684	17	1,036	9	76,151	19	15.0	7.2
2. Shinyanga	779	13	1,778	19	50,781	12	14.7	7.0
3. Dodoma	676	18	1,238	13	41,311	10	13.7	6.5
4. Mbey	1,012	9	1,476	18	60,350	14	13.7	6.5
5. Rukwa	598	20	695	3	68,635	17	13.3	6.3
6. Arusha	1,334	2	1,352	16	82,306	20	12.6	6.0
7. Lindi	704	16	647	2	66,046	16	11.3	5.4
8. Morogoro	1,196	3	1,223	12	70,799	18	11.0	5.3
9. Kagera	842	10	1,326	15	28,388	7	10.7	5.1
10. Mwanza	1,054	7	1,878	20	19,592	5	10.6	5.0
11. Iringa	1,120	4	1,209	11	56,864	13	9.3	4.4
12. Singida	814	12	792	5	43,341	11	9.3	4.4
13. Pwani	638	19	638	1	32,407	8	9.3	4.4
14. Mara	749	15	971	8	19,566	4	9.0	4.3
15. Kogoma	821	11	755	6	37,037	9	8.7	4.1
16. Ruvuma	1,081	6	783	4	63,498	15	8.3	4.0
17. Tanga	1,012	5	1,284	14	26,808	6	8.3	4.0
18. Mtwara	771	14	889	6	16,707	3	7.7	3.8
19. Kilimanjaro	1,037	8	1,109	10	13,309	2	6.7	3.2
20. Dar-es-Salam	4,235	1	1,361	17	1,393	1	6.3	3.0

Source: Planning Commission of Tanzania: "Mapendekezo ya Vigezo Vitakavyotumiwa Kugawa Rasiulimali Za Maendeleo Mikoani", Paper for internal circulation, 1990.

Thus, the basic weakness in the planning exercise in Tanzania appears to be the lack of a macro-model or methodologically sound framework which would consider different macroeconomic constraints and the interdependent nature of economic activity in the national economy to derive the physical targets from the resource availability in a consistent way. We examine the possibilities existing in this regard in Tanzania in the next two sections of the paper.

6. Uses of Input-Output Statistics in Planning

The history of the estimation of the input-output (i.e. I-O) table for Tanzania dates back to the year 1957 when Peacock and Dosser published in the *Review of Economic Studies* the first I:O Table for the Tanzanian economy. It was for the year 1954 and considered 18 sectors only. Subsequently, for the year 1961, another table of 17 X 17 sectoral dimension was prepared for Tanzania by the National Statistical Office. The Bureau of Statistics constructed a more detailed table having 45 X 45 sectoral dimension for the year 1969 which was subsequently revised and updated for the year 1970. The latest I:O table for Tanzania published in 1986 considers 73 sectors but dates back to the year 1976. (The list of the 73 sectors is given below in the Table-5.) Availability of statistics and competence for estimation of the I:O Table do not seem to pose any serious problem in Tanzania as also in most

other developing countries. These estimates, however, have not been used so far in the national planning exercises in Tanzania. It was felt that failure to develop workable and suitable applications of the I:O technique was primarily responsible for not using such estimates for planning. A special national workshop was, therefore, organized in Arusha during February 1986 to consider utilization of the Tanzanian Input-Output Table for 1976.

The main uses of the I:O Table in general and the one for Tanzania in particular are thought to be in:

- (1) Checking consistency in national accounts and testing the accuracy of macro predictions;
- (2) Forecasting and projecting output; and
- (3) determining intersectoral linkages and thereby identifying the key sectors.

Let us take the Tanzania's I:O Table for the year 1976 to illustrate some of these uses. We may compress the table into only 3 sectors. These sectors are:

Sector I	Primary sector or Agriculture (1 to 26 sectors in the detailed Table)
Sector II	Secondary sector or Industry (27 to 58 sectors)
Sector III	Tertiary sector or Services (59 to 73 sectors).

Table-2 presented above is a very useful way of keeping the national accounts. The rows in the table shows the disposal of the sectoral output to intermediate use as inputs in different industries/sectors and to final use which is classified into 5 different categories like private consumption, government consumption, exports, fixed capital formation and changes in stocks. Every column in the table shows the break up of the gross output of the respective sector into the cost items like inputs from different sectors including imports, indirect taxes and subsidies, wages and salaries, depreciation and operating surplus. Thus, the I:O table as presented in Table-2 above is a very powerful way of describing and analyzing the structure of the economy. Since it is only an alternative way of maintaining the national accounts in which detailed transactions are systematically recorded, it provides a consistency check on the national accounts. The last two rows in Table-2, for instance, represent the consistent estimates of industrial break down of the GDP in the Tanzanian economy in the year 1976.

All the remaining uses of the I:O Table are possible only if some plausible assumptions are made about the sectoral interrelationships and the structure of the economy. To illustrate the concept, let us consider the first three rows and columns of Table-2. We may represent each column in the form of proportions (coefficients) of the respective industrial (sectoral) gross output. These proportions are called Input Coefficients since they represent the input requirements from different sectors to produce one unit of the given sector's gross output. Table-3 presents the Input Coefficients for the simplified Tanzanian economy for the year 1976.

Input-Output Transaction Table for Tanzania, 1976										
(In Million T.Sh.)										
	Intermediate use				Final Use					Gross Output
	Agriculture	Industry	Services	Total Inter.	Pvt.Cons.	Govt.Cons.	Exports	FCF	Stocks	
Agriculture	316.6	1511.2	672.1	2499.9	6769.9	-	1341.2	69.9	98.3	10779.2
Industry	245.4	1129.6	1614.5	2989.5	3584.4	-	1038.4	193.9	38.4	7844.6
Services	297.1	1411.2	4779.4	6487.7	5048.5	5447.2	2107.7	2177.4	-	21368.5
Total Inter. Inputs	859.1	4052.0	7066.0	11977.1	15402.8	5447.2	4487.3	2441.2	136.7	39892.3
Imports	155.4	1665.1	1616.5	(3437.0)	579.0	-	-	1662.2	-	5678.2
Import Duties	10.7	128.2	86.9	(225.8)	58.4	-	-	76.3	-	360.5
Other Indirect Taxes	66.7	41.8	54.7	(163.2)	964.4	-	497.5	738.2	-	2363.3
Subsidies	-104.1	-138.6	-12.5	(-255.2)	-	-	-	-	-	-255.2
Wages & Salaries	570.8	966.2	6044.0	(7581.0)	-	-	-	-	-	7581.0
Depreciation	354.6	217.0	676.8	(1248.4)	-	-	-	-	-	1248.4
Operating Surplus	8866.0	912.9	5736.1	(15515.0)	-	-	-	-	-	15515.0
Gross Output	10779.2	7844.6	21268.5	39892.3	17004.6	5447.2	4984.8	4917.9	136.7	72383.5
GDP at Factor Costs	9791.4	2096.1	12456.9	24344.4	-	-	-	-	-	24344.4
GDP at Market Prices	9764.7	2127.5	12586.0	24478.2	-	-	-	-	-	24478.2

Input Coefficients for the Tanzanian Economy, 1976			
Sectors	Agriculture	Industry	Services
Agriculture	$\frac{316.6}{10779.2} = 0.03$	$\frac{1511.2}{7844.6} = 0.19$	$\frac{672.1}{21268.5} = 0.03$
Industry	$\frac{245.4}{10779.2} = 0.02$	$\frac{1129.6}{7844.6} = 0.14$	$\frac{1614.5}{21268.5} = 0.08$
Services	$\frac{297.1}{10779.2} = 0.03$	$\frac{1411.2}{7844.6} = 0.18$	$\frac{4779.4}{21268.5} = 0.22$

If we assume that the interindustry structure of the economy as revealed by the input coefficients (e.g. as given in Table 3) remains stable or constant over the planning horizon, we can derive consistent projections or forecasts of the important macro aggregates over the planning horizon based on certain desired goals of the final use of output of different sectors. This can be illustrated by considering the following 3 equations obtained from each of the first 3 rows of Table 2 using the input coefficients as given in Table 3.

$$\begin{aligned}
\text{1st Row:} & \quad 316.6 + 1511.2 + 672.1 + 8279.3 = 10779.2 \\
\text{i.e.} & \quad 0.03(10779.2) + 0.19(7844.6) + 0.03(21268.5) + (8279.3) = (10779.2) \\
\text{i.e.} & \quad 0.03 X_1 + 0.19 X_2 + 0.03 X_3 + F_1 = X_1 \\
\text{i.e.} & \quad F_1 = X_1 - 0.03 X_1 - 0.19 X_2 - 0.03 X_3 \quad \dots(1)
\end{aligned}$$

Similarly,

$$\text{2nd Row:} \quad F_2 = X_2 - 0.02 X_1 - 0.14 X_2 - 0.08 X_3 \quad \dots(2)$$

$$\text{3rd Row:} \quad F_3 = X_3 - 0.03 X_1 - 0.18 X_2 - 0.22 X_3 \quad \dots(3)$$

Thus, there would be as many equations as there are sectors in the I:O Table. In our simplified version, there are 3 sectors and 3 equations. When we specify targeted values of the final use of sectoral outputs (i.e. F_1 , F_2 and F_3), we find the sectoral gross outputs (i.e. X_1 , X_2 and X_3) as unknowns from the 3 equations. The solution would be unique since there are 3 independent linear equations with 3 unknowns. In terms of matrix algebra, the system of equations can be written as:

$$\begin{aligned}
F &= X - AX \quad \text{where A is the input coefficient matrix} \\
F &= (I-A)X \\
(I-A)^{-1}F &= X \quad \dots(4)
\end{aligned}$$

We thus require inverse of (I-A) matrix and targeted values of F vector to get consistent predictions or forecasts of sectoral gross outputs. Table 4 presents the inverted (I-A) matrix for our simplified Tanzanian case of 3 sector economy.

Table 4				
(I-A) Inverse for 3 X 3 Tanzanian Economy, 1976				
	Agriculture	Industry	Services	Row Totals
Agriculture	1.0379408	0.2428819	0.0648317	1.3456544
Industry	0.0284627	1.1949602	0.1236547	1.3470776
Services	0.0464891	0.2851016	1.3130805	1.6446712
Column Total	1.1128926	1.72294337	1.5015669	4.3374032

The interpretation of the elements of the inverted (I-A) matrix as given in Table 4 becomes clear once we recognize that equation (4) above can also hold in incremental terms, i.e.

$$(I-A)^{-1} \cdot F = X \quad \dots(5)$$

Thus, if we consider a case where the final demand of agricultural produce increases by one unit with the final use in industry and services sectors remaining unchanged, the required change in gross outputs of all the 3 sectors would be given by the respective elements of the first column of Table 4, i.e. gross output in agriculture would have to change by 1.0379 units, in industry by 0.028 units and in services by 0.046 units. These numbers are derived by fully capturing all the intersectoral linkages existing in the economy. The concept of intersectoral linkages is very important in the economic planning not only to check the internal consistency of the plan but also to decide broad strategy of the plan and in identifying the 'key sectors' in the economy whose activation can generate significant spread effects in the rest of the economy. This would be the best strategy to use the available scarce resources most efficiently in an economy committed to achieving rapid economic development and transformation.

The I:O Table and the inverted (I-A) matrix can be used effectively to measure forward and backward linkages of a given sector in the economy. The direct linkages can be measured from the input coefficient matrix like the one given in Table 3; whereas the combined direct and indirect linkages of a sector can be measured from the inverted (I-A) matrix. Table 5 below gives the standard formulae for measuring different types of linkages and provides their estimates for each of the 73 sectors of the Tanzanian economy for the year 1976. Based on these values, it is possible to identify the seven most important 'key sectors' in Tanzanian economy as sector numbers: 6. Tobacco; 31. Grain Mill Products; 40. Textiles; 48. Fertilizers and Agrochemicals; 59. Electricity, 61. Construction; and 62. Commerce. A consideration of their import effects and income effects again as given in Table 5 clearly brings out that Commerce, Electricity, Tobacco and Textiles are far superior to other key sectors when import constraints are explicitly considered.

7. Possibilities of Using I:O Model in Tanzanian Planning

As we have already seen in the previous section, I:O statistics are compiled and prepared very competently in Tanzania. Lack of statistical network and the expertise needed to construct the I:O estimates do not appear to be the major deterrent in using I:O model for planning in Tanzania. However, it should be pointed out that the statistical network in Tanzania is not so developed that it can generate reliable I:O Tables quickly as and when required. As is the case in most of the third world countries, Tanzania can also generate the reliable I:O estimates only once in a decade and that too with a considerable lag between the collection of basic data required and the usable final I:O Tables. This is a major constraint because the economic structure as revealed by the available I:O table may not be relevant for the planning period for which it has to be used. Intelligent and informed guesswork is required to predict changes in the individual input coefficients before the I:O statistics could be used for planning under such circumstances.

Another major concern about the I:O model based economic planning is regarding the decentralization of the planning process. Regional I:O Tables can prove too costly for the developing countries and a generalized national I:O Table may not be relevant for planning at regional - i.e. states/provinces or district - levels in the case of most of the regions. The unresolved issue in this regard is to reconcile the regional planning in a decentralized framework with the national level planning based on a stringent consistency framework provided by the I:O model.

The officials in the newly formed Planning Commission in Tanzania are, however, hopeful of finding viable solution to these issues. Although currently, Tanzania does not have a well-defined macroplanning model based on internal consistency framework, the officials in the Planning Commission are seriously considering adopting an I:O model for national planning following the examples of countries like India and Kenya.

Table 5								
Measures of Intersectoral Linkages, Tanzania 1976								
Sector Name	Indices of Dir. Backward Links		Indices of Dir. Forward Links		Indices of Indir. & Direct Links		Indices of Dir. & Indir. Import Effects	Indices of Dir. & Indir. Income Effects
	Unwtd b1	Wtd b2	Unwtd f1	Wtd f2	Backwd B	Forwd F		
	1	2	3	4	5	6	7	8
1. Seed Cotton	0.1795	0.1007	0.5684	0.5609	0.8031	1.1904	0.0535	0.9465
2. Sisal fibre	0.1946	0.1012	0.3778	0.1565	0.8235	0.9671	0.0647	0.9353
3. Tea leaf	0.4089	0.0509	0.3289	0.1244	1.0503	0.9117	0.2161	0.7839
4. Coffee	0.0884	0.1241	0.0380	0.0350	0.7261	0.6739	0.0583	0.9417
5. Sugarcane	0.7660	0.1402	0.3619	0.1620	1.3761	0.9766	0.3768	0.6232
6. Tobacco	0.5844	0.1817	0.5689	0.3151	1.2183	1.1179	0.1544	0.8456
7. Cashew nuts	0.0379	0.0068	0.0870	0.0514	0.6855	0.7095	0.0045	0.9955
8. Pyrethrur	0.1567	0.0053	0.0535	0.0328	0.7939	0.6987	0.0212	0.9788
9. Maize	0.0569	0.1383	0.3609	0.3026	0.6924	0.9816	0.0157	0.9843
10. Wheat	0.2548	0.0379	0.2875	0.1458	0.8798	0.9299	0.2187	0.7813
11. Paddy	0.0670	0.0351	0.2190	0.1370	0.6992	0.8628	0.0141	0.9859
12. Other cereals	0.0321	0.0310	0.1418	0.0259	0.5699	0.7418	0.0008	0.9992
13. Legunes	0.0386	0.0631	0.0666	0.1117	0.6739	0.6970	0.0002	0.9998
14. Oil seeds	0.0991	0.0413	0.4219	0.2083	0.7187	0.9787	0.0000	1.0000
15. Plantains	0.0001	0.0001	0.0837	0.1081	0.6476	0.7114	0.0000	1.0000
16. Other horticult. crops	0.0498	0.0579	0.2147	0.1611	0.6862	0.7976	0.0062	0.9938
17. Coconuts	0.0001	0.0000	0.3899	0.3217	0.6476	0.9310	0.0000	1.0000
18. Other crops	0.0215	0.0349	0.0787	0.0847	0.6617	0.7143	0.0000	1.0000
19. Livestock	0.0731	0.2270	0.6238	0.3462	0.7238	1.1554	0.0318	0.9682
20. Fisheries	0.0409	0.0406	0.3090	0.3730	0.6885	0.8825	0.0094	0.9906
21. Forestry & Logging	0.0886	0.0764	0.4733	0.3618	0.7211	1.0766	0.0244	0.9756
22. Hunting	0.0671	0.0022	0.0035	0.0069	0.7190	0.6501	0.0826	0.9174
23. Stone quar. clay & sand	0.0191	0.0076	0.2709	0.3984	0.6653	0.8996	0.0196	0.9804
24. Salt mining	0.2501	0.0091	0.0069	0.0026	0.8778	0.6528	0.2308	0.7692
25. Diamond mining	0.1843	0.0553	0.0250	0.0027	0.8233	0.6698	0.0733	0.9267
26. Other mining	0.2318	0.0035	0.0777	0.0104	0.8560	0.7109	0.1185	0.9815
27. Sugar & Confectionery	0.5938	0.3104	0.3549	0.0880	1.3130	0.8894	0.2337	0.7663
28. Bakery products	1.0447	0.1835	0.0178	0.0130	1.8890	0.6612	0.2931	0.7069
29. Proc. meat & Dairy	0.3735	0.0869	0.1718	0.0554	0.9671	0.7923	0.3939	0.6061
30. Oils & fats	0.8098	0.2082	0.1063	0.0367	1.3795	0.7232	0.2931	0.7069
31. Grain mill products	0.8657	0.5595	0.5408	0.1063	1.3242	1.0075	0.2920	0.7080
32. Cann. fruits & Veggies.	0.8863	0.0456	0.0070	0.0051	1.5929	0.6529	0.2398	0.7602
33. Other food mfg.	0.5989	0.3540	0.0658	0.1344	1.2068	0.7123	0.1070	0.8930
34. Beverage Industries	0.4081	0.2359	0.0994	0.0824	1.0508	0.7367	0.2277	0.7723
35. Local brewing	0.4752	0.1142	0.0000	0.0000	1.0288	0.6475	0.0253	0.9747
36. Tailoring	0.7272	0.2130	0.0000	0.0000	1.3938	0.6475	0.1367	0.8633

Table 5 (contd)

	1	2	3	4	5	6	7	8
37.Other S.S.Industries	0.7853	0.9486	0.1015	0.0398	1.2464	0.7292	0.0494	0.9506
38.Tobacco mfg.	0.8082	0.5105	0.1101	0.0701	1.5929	0.7279	0.1708	0.8292
39.Cotton ginning	0.5375	0.5783	0.2361	0.2258	1.0839	0.9058	0.0431	0.7569
40.Textiles	0.4008	0.5113	0.8620	0.2650	1.0496	1.2636	0.1979	0.8021
41.Rope twine & cordage	0.5771	0.2127	0.1607	0.2289	1.1493	0.8526	0.1097	0.8903
42.Garment manufacturing	0.4042	0.1320	0.0300	0.0688	1.0492	0.6752	0.3487	0.6513
43.Leaner & leather prds.	0.6142	0.0886	0.2978	0.1311	1.1719	0.8794	0.3459	0.6541
44.Footwear	0.6890	0.1144	0.0007	0.0048	1.3991	0.6480	0.2277	0.7723
45.Wood & Wood prds.	0.4767	0.1274	0.2208	0.0916	1.1074	0.8426	0.2244	0.7756
46.Paper prng.& pub.	0.3979	0.2228	0.8735	0.5812	1.0412	1.5476	0.3894	0.6106
47.Chem.& Phar.ex agro.	0.5900	0.3730	0.3980	0.3247	1.2331	0.9569	0.3730	0.6270
48.Fert.& Agro.Chems.	0.3760	0.0929	0.4311	0.1772	1.0084	1.0790	0.4769	0.5231
49.Petroleum & Pet.prds.	0.0801	0.1070	0.8540	0.8287	0.7118	1.5176	0.7860	0.2140
50.Rubber products	0.3677	0.1268	0.0845	0.3001	0.9943	0.7975	0.4899	0.5101
51.Plastic products	0.3798	0.0512	0.2670	0.0879	1.0133	0.8524	0.3955	0.6045
52.Glass & Non-met.prds.	0.5335	0.0477	0.2680	0.0823	1.1406	0.8336	0.2700	0.7300
53.Cement	0.7660	0.1012	0.0922	0.1201	1.3276	0.7340	0.2554	0.7446
54.Iron steel & Non-ferr.	0.5307	0.2578	0.6734	0.4247	1.2670	1.4736	0.6161	0.3839
55.Fabricated met.prds.	0.6705	0.2253	0.3401	0.1531	1.3856	0.9183	0.3666	0.6334
56.Machinery & equips.	0.2857	0.0939	0.4866	0.1986	0.9214	1.0801	0.5018	0.4982
57.Trans.eqp. & repairs	0.2721	0.1541	0.3074	0.4382	0.9290	0.9700	0.5053	0.4947
58.Other manufacturing	0.2387	0.0262	0.2926	0.1072	0.8629	0.8921	0.2165	0.7835
59.Electricity	0.4126	0.1552	0.6800	0.3063	1.0007	1.2308	0.1392	0.8608
60.Urban water supply	0.5957	0.0994	0.1090	0.0964	1.2212	0.7485	0.2911	0.7089
61.Construction	0.4657	1.7221	0.4922	0.4146	1.0757	1.1373	0.2403	0.7597
62.Commerce	0.4379	4.0825	4.2520	2.8654	1.0147	4.6546	0.0893	0.9107
63.Hotels & Restaurants	0.7903	0.5772	0.1314	0.4576	1.3713	0.7739	0.1395	0.8605
64.Transport	0.1589	1.4001	1.7359	3.8072	0.7953	3.3758	0.1212	0.8788
65.Communications	0.2704	0.1277	0.2003	0.4229	0.9108	0.9741	0.1024	0.8976
66.Fin.institutions	0.1615	0.1856	1.8025	0.8278	0.8037	2.2799	0.1486	0.8514
67.Real estate	0.3121	0.2317	0.2280	0.2728	0.9685	0.9135	0.0896	0.9104
68.Business services	0.3583	0.1923	0.6749	0.5008	0.9842	1.4082	0.1279	0.8721
69.Pub.administration	0.4376	3.0285	0.0000	0.0000	1.0678	0.6475	0.1543	0.8457
70.Education	0.1594	0.3624	0.2627	0.2089	0.7919	0.9676	0.0924	0.9076
71.Health	0.1818	0.2656	0.0218	0.0121	0.8111	0.6676	0.2145	0.7855
72.Other services	0.3342	0.1920	0.2283	0.1304	0.9749	0.8589	0.3518	0.6482
73.Unspecified	0.1840	0.3098	0.7786	1.5495	0.8586	1.4247	0.5745	0.4255
Average Value	0.3674	0.3003	0.3674	0.3003	1.0000	1.0000	0.1915	0.8045

Note: Definitions of Indices are on the next page.

Definition of Indices

Direct backward linkages

$$bl_j = \frac{\sum_{i=1}^n X_{ij}}{X_j} = \sum_{i=1}^n a_{ij}$$

{ a_{ij} is the input coefficient in i-th row and j-th column.

Weighted direct backward linkages

$$b2_j = bl_j \cdot n \cdot \frac{X_j}{X}$$

Direct forward linkages

$$f1_i = \frac{\sum_{j=1}^n X_{ij}}{X_i}$$

Weighted forward linkages

$$f2_i = f1_i \cdot n \cdot \frac{X_i}{X}$$

Direct and indirect backward linkages

$$B_j = \frac{\frac{1}{n} R_j}{\frac{1}{n^2} \sum_{i=1}^n \sum_{j=1}^n r_{ij}} \quad \text{where } R_j = \sum_{i=1}^n r_{ij}$$

r_{ij} is element of the inverted Leontief-matrix in i-th row and j-th column.

Direct and indirect forward linkage

$$F_i = \frac{\frac{1}{n} R_i}{\frac{1}{n^2} \sum_{i=1}^n \sum_{j=1}^n r_{ij}} \text{ where } R_i = \sum_{j=1}^n r_{ij}$$

Direct and indirect import effects

$$b_j = \sum_{i=1}^N \beta_i \cdot r_{ij} \text{ where } \beta_i = \frac{\text{Import sector } i}{\text{Total production sector } i}$$

Direct and indirect income effects

$$r_j = 1 - b_j$$

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Appendix-A

Criteria To Be Developed/Used in Future as Basis For Regional Resources Allocations

(Source: Planning Commission, Tanzania)

DATA

- i) Size
- | | | | |
|------------|-------|-----------------|----------------|
| Total area | ..... | km ² | 1.2.3.4.5,..20 |
| Land area | ..... | " |  |
| Water area | ..... | " |  |
- ii) Population
- | | |
|-------------|-------|
| Size | ..... |
| Density | ..... |
| Growth Rate | ..... |
- iii) Climate
- | | |
|----------------------------|-------|
| Annual Mean Rainfall(mm) | ..... |
| Annual Mean temperature C° | ..... |
- iv) Economic Growth
- | | |
|----------------------------------|-------|
| Regional Growth Domestic Product | ..... |
| Regional Per Capita Income | ..... |
| Growth Rate | ..... |
- v) Administrative Division
- | |
|---|
| Districts..... |
| Divisions..... |
| Wards..... |
| Villages..... |
| Total Registered villages..... |
| Villages Survey & with title needs..... |
- vi) Local Government
- | | |
|------------------------------|---------|
| Cities..... | No..... |
| Municipalities..... | |
| Townships..... | |
| Rural District Councils..... | |
- vii) Co-operatives Development
- | |
|---------------------------------|
| Unions..... |
| Village Primary Societies..... |
| Savings and Credit Society..... |
| Others..... |
- viii) Land Use
- | |
|-----------------------------|
| Arable Land..... |
| Land Under cultivation..... |
| Forest reserves..... |
| Pasture land..... |

- a) Crop Production
 - Cultivated land.....
 - Irrigated land.....
 - Area under permanent crops.....
 - Storage capacity.....
 - Main food crops.....
 - Main cash crops.....

- b) Livestock and Poultry Production
 - Cattle.....
 - Goats.....
 - Sheep.....
 - Pigs.....
 - Poultry.....

- c) Construction
 - Bulldozers, Graders and Caterpillars.....
 - Tarmac roads (Kms).....
 - Gravel roads (Kms).....
 - Earth roads.....

- d) Transport
 - Buses.....
 - Trucks (7 tons).....
 - Lorries.....
 - Vans, Pickups.....
 - Tractors.....

- e) Post and Telecommunications
 - Main post offices.....
 - Sub-post offices.....
 - Telephone lines (capacity).....
 - Telex lines (capacity).....

- f) Finance and Credit
 - Bank Branches.....
 - Insurance Branches.....

- g) Energy Consumption
 - Electricity : Domestic.....
 - Industrial.....
 - Wood/charcoal.....
 - Oil/Petroleum products.....

- h) Water
 - Rural Annual Water Supply Capacity.....
 - Number of rural people supplied with water.....
 - Urban water supply annual capacity.....
 - Number of urban people supplied with water.....

i) Health Facilities

Hospitals.....
Hospital beds/person.....
Dispensaries/person.....
Dispensaries.....
Health centres.....
Health centres/person.....
Doctors.....
Doctors/person.....
Trained Nurses.....
Nurses/person.....

j) Health Condition

Life expectancy(years).....
CBR per 1000.....
CDR per 1000.....
Infant Mortality rate.....

k) Education

Primary Schools.....
Secondary Schools.....
Vocational Training Centres.....
Emolument rate/Primary, Secondary.....
Literacy rate.....

Chapter 4

Planning in Consistency Framework: Malaysian Experience

I The Malaysian Economy

Malaysia covers a total land area of 329,758 sq.kms. It is made up of two distinct regions: Peninsular Malaysia (West Malaysia) covering an area of 131,598 sq.kms. and Sabah and Sarawak (East Malaysia) with a total land area of 198,160 sq.kms. These two regions are separated by about 540 kms. of the South China Sea. The Peninsular Malaysia is situated in the tropical region of the South-East Asia between 1°N to 7°N Latitude and 100°E to 104°E Longitude. Map 1 shows the location of Malaysia. Malaysia is a plural society with an estimated population of 17.77 million in 1990, comprising 61% Malays and other people (together, they are referred to as the Bumiputera community), 30% Chinese, 8% Indians and 1% others. The population is growing at 2.40% p.a. The country is well endowed with natural resources. Of the total land area, about 62% is forests, the bulk of which is exploitable timber, while most of the remaining land area is cultivated. Mineral resources are extensive and include both metallic minerals (such as tin, iron ore, bauxite and copper) and non-metallic resources (such as petroleum, natural gas, limestone and marble).

On the eve of Independence, Malaysia inherited from the British all the characteristics of a classical colonial economy. In 1957 Peninsular Malaysia was the world's largest producer of tin and the second largest producer of natural rubber, while Sabah depended largely on its timber and Sarawak on its petroleum, rubber and pepper for their prosperity. The country's commanding position over these commodities was the source of the prosperity which it enjoyed and placed it well to the fore amongst Third World nations; at the same time the nation was dangerously placed at the mercy of the fluctuations of the world market, particularly in tin and rubber. Malaysia has also become a leading producer of Palm oil, tropical hardwoods, cocoa and pepper. Malaysia's exports accounted for about 67% of the world's exports of palm oil and 20% of the global tropical hardwood exports. Table 1 summarizes important information on different aspects of the Malaysian economy for the last three years.

Since 1957 when the country gained Independence, Malaysian economy has been experiencing a sustained high rate of expansion. Over the period 1957-88, the nominal GDP grew at an average annual rate of 9.6%. Table 2 provides some information on the real GDP by expenditure category for selected years over the period 1960-88. As can be readily observed from the table, the economy experienced tremendous acceleration in its growth during the seventies. The growth of real GDP rose from an average of 3.3% during the sixties to 8.5% during the seventies. However, in the wake of the global recession, the growth again slumped to the average of 4.3% over the years 1981-86. However, after 1986, the economy has started recovering again with 6.2% p.a. growth achieved during 1986-88 and about 8.7% p.a. during 1989-91 (Table 1). Similar trends are obtained for consumption (both public and private), for investment (both public and private) and for imports in real terms. However, for exports and net factor payments, the trends were different. Exports in real terms grew at a high rate of 8% p.a. during the sixties but then decelerated during the seventies and mid-eighties. Only after mid-eighties, it has again picked up and started growing at more than 13% p.a. The net factor payment which is negative is on the other hand accelerating throughout the period.

Over the years, there are significant structural changes taking place in the economy. Table 2 reports data of sectoral shares in the real GDP for selected years during the period 1960-88. It is clear that

Table 1
Malaysia-Key Data and Forecasts

	1989		1990 ¹		1991 ²	
	\$ million	% growth	\$ million	% growth	\$ million	% growth
NATIONAL PRODUCT:						
Gross National Product in constant 1978 prices	68,621	9.6	75,049	9.4	81,107	8.1
Consumption expenditure: Public	10,920	7.6	11,559	5.9	13,019	12.6
Private	35,643	14.3	39,373	10.5	41,645	5.8
Gross fixed capital formation: Public	7,782	33.5	8,568	10.1	8,832	3.1
Private	13,430	31.0	16,836	25.4	18,439	9.5
Exports of goods and non-factor services	53,929	18.2	62,236	15.4	69,131	11.1
Imports of goods and non-factor services	49,440	30.2	59,152	19.6	64,698	9.4
Gross National Savings (at current prices)	29,602	4.4	33,794	14.2	36,968	9.4
Per capita GNP (at current prices, M\$)	5,558	9.8	6,147	10.6	6,638	8.0
DOMESTIC PRODUCT:						
Gross Domestic Product in constant 1978 prices	72,134	8.8	78,889	9.4	85,175	8.0
Agriculture, livestock, forestry and fishing	14,736	5.8	15,282	3.7	15,649	2.4
Manufacturing	18,089	12.0	20,947	15.8	23,670	13.0
Mining and quarrying	7,385	6.6	7,739	4.8	7,910	2.2
Construction	2,380	11.6	2,737	15.0	3,120	14.0
Services	30,370	8.6	33,248	9.5	36,269	9.1
FEDERAL GOVERNMENT FINANCE:						
Revenue	25,273		27,219		30,246	
Operating expenditure	24,832		25,993		29,040	
Current account surplus/deficit	+441		+1,226		+1,206	
Development expenditure (net)	5,701		8,023		7,134	
Overall deficit	-5,260		-6,797		-5,928	
Domestic borrowing (net)	2,474		3,793		--	
Foreign borrowing (net)	-1,016		-845		--	
Foreign debt service ratio (per cent)	4.4		3.5		--	
BALANCE OF PAYMENTS:						
Current Account	-473		-3,330		-4,022	
Merchandise balance f.o.b.	10,562		6,670		6,705	
Services balance	-11,243		-10,210		-10,937	
Transfers	208		210		210	
Long-term capital account	2,366		5,919		--	
Basic balance	1,893		2,589		--	
Overall balance	3,332		4,439		--	

	1989		1990		1991	
	\$ million	% growth	\$ million	% growth	\$ million	% growth
EXTERNAL TRADE:						
<i>Total Exports (f.o.b.)</i>	67,825	22.7	79,185	16.7	91,507	15.6
Rubber	3,949	-24.9	3,128	-20.8	3,243	3.7
Crude petroleum	7,883	28.9	10,190	29.3	10,407	2.1
Tin	1,161	27.4	800	-31.1	784	-2.0
Palm oil (crude and processed)	4,681	3.4	4,312	-7.9	4,340	0.6
Sawlogs	4,356	8.6	4,200	-3.6	4,203	0.1
Manufactures	36,592	36.3	46,654	27.5	57,571	23.4
<i>Total Imports (c.i.f.)</i>	60,858	40.6	77,265	27.0	90,912	17.7
Food, beverages and tobacco	4,846	20.1	--	--	--	--
Manufactures (SITC 6)	9,990	39.4	--	--	--	--
Crude petroleum and related products	2,606	22.1	--	--	--	--
Machinery and transport equipment	29,180	49.5	--	--	--	--
<i>Balance of Trade</i>	6,967		1,920		595	

Table 1(contd)

Production and Prices	1989		1990		1991	
	Volume	% growth	Volume	% growth	Volume	% growth
Production-						
Rubber ('000 tonnes)	1,419	-14.5	1,350	-4.9	1,400	3.7
Crude petroleum ('000 barrels per day)	588.9	8.7	626.4	6.4	640.0	2.2
Tin ('000 tonnes)	32.0	10.7	29.0	-9.4	27.0	-6.9
Palm oil ('000 tonnes)	6,057	20.5	6,550	8.1	6,800	3.8
Sawlogs ('000 cu metres)	39,709	5.3	40,000	0.7	38,000	-5.0
Commodity Prices						
	Price	% growth	Price	% growth	Price	% growth
Rubber, RSS 1 (sen per kilogramme)	262	-15.4	230	-12.3	235	2.2
Tin, Kuala Lumpur Tin market (\$ per kilogramme)	23.09	25.1	16.50	-28.6	16.50	0.0
Crude palm oil, Local Delivered (\$ per tonne)	822	-20.1	670	-18.5	680	1.5
Crude petroleum, average weighted price (US\$ per barrel)	18.29	19.5	22.00	20.3	22.00	0.0
	Index	% growth	Index	% growth	Index	% growth
Consumer Price Index (1980=100)	133.7	2.8	138.0	3.2	143.5	4.0
Producer Price Index (1978=100)	139.3	4.0	146.3	5.0	155.1	6.0

	1989 (End December)		1990 (End August)	
	\$ million	% growth	\$ million	% growth ¹
MONEY AND BANKING:				
Money supply (M2)	74,066.6	14.0	80,730.7	19.1
Money supply (M1)	21,248.7	17.6	22,883.4	19.1
Quasi money	52,817.9	12.6	57,847.3	19.1
Commercial Banks-				
Total deposits	74,849.0		79,372.5	
Total loans	67,141.7		73,628.2	
Liquidity ratio (per cent)	19.9		18.2	
Interest Rates (per cent per annum)-				
<i>Commercial Banks:</i>				
3 months fixed deposits	5.00		6.25	
Savings deposits	3.50		3.50	
Base lending rates	7.00		7.00	
Exchange Rates (equivalent in Malaysian Ringgit)				
1 US\$=	End December		End October	
	2.70		2.70	
1 Pound Sterling=	4.34		5.28	
100 Deutschemark=	159.92		178.05	
100 Yen=	1.88		2.09	
100 Singapore \$=	142.47		158.36	

	Thousands	% growth	Thousands	% growth	Thousands	% growth
LABOUR:						
Labour force	6,834.1	3.2	7,046.5	3.1	7,257.9	3.0
Employment-						
Total	6,350.9	4.3	6,603.4	4.0	6,839.8	3.6
Agriculture	1,957.9	2.6	1,975.0	0.9	1,985.7	0.5
Manufacturing	1,079.4	6.6	1,159.3	7.4	1,239.2	0.4
Government	846.6	0.3	850.2	0.4	853.9	0.4
Unemployment rates (percentage of labour force)	7.1		6.3		5.8	

Table 1 (contd)

INDUSTRIAL ECONOMIES	1989	1990	1991
	%growth	%growth	%growth
Real GNP: All Industrial countries	3.4	2.6	1.5
United States of America	2.5	1.3	0.1
Japan	4.9	5.1	3.7
West Germany	3.9	3.9	3.3
United Kingdom	2.2	1.4	0.5
Consumer Prices: All Industrial countries	4.4	4.8	1.5
United States of America	4.8	5.1	5.8
Japan	2.3	2.8	3.7
West Germany	2.8	2.8	3.7
United Kingdom	7.8	9.3	6.6

1: Estimates; 2: Forecasts; 3: Change from August 1989;
Source: Ministry of Finance, Government of Malaysia.

upto 1980, the secondary sector increased in importance considerably at the expense of both the primary and the tertiary sectors. During the eighties, however, the process seems to have slowed down. Moreover, the share of the tertiary sector has increased and remained stable at around 42% of real GDP. If we consider the share of major commodity producing sectors viz. Agriculture and Manufacturing, we find that the former has almost continuously declined and the latter has increased over the period 1960-88. Thus, the Malaysian economy is systematically transforming from the primary production based economy into rapidly industrializing country. Currently, about 17% of the total labour force in Malaysia is engaged in the manufacturing sector and about 31% in the agricultural sector.

	1960	1965	1970	1975	1980	1985	1986	1987	1988a
1. Total consumption	5506	7533	9227	12748	20083	24198	22441	22920	24265
a) Private	4540	5968	7310	9631	15249	18312	16481	16882	18071
b) Public	966	1565	1917	3117	4834	5886	5960	6038	6194
2. Total investment	1903	1510	2196	3936	8690	11180	9126	11407	13485
a) Private	865	836	1490	2454	5443	5254	3696	6763	7965
b) Public	228	674	706	1482	3247	5926	5430	4644	5520
3. Change in stocks	n.a.	n.a.	357	-266	-80	-814	-573	520	1162
4. Exports of goods and non-factor services	3596	7179	14109	20726	22365	19922	23429	25779	29784
5. Imports of goods and non-factor services	691b	198b	4868	6232	14917	18767	18260	19959	24463
6. Gross domestic product at purchasers' value	8889	9241	12308	17365	27885	35719	36162	37968	40771
7. Net factor payments	-236	-62	-355	-449	-974	-2756	-2509	-2469	-2824
8. Gross national product at purchasers' value	8653	9179	11953	16916	26911	32963	33653	35499	37947
9. % Share of GDP :									
a) Primary Sector	(43.7)	(40.4)	(37.2)	(32.2)	(32.8)	(30.4)	(31.6)	(32.5)	(31.6)
b) Secondary Sector	(11.7)	(14.5)	(17.3)	(20.2)	(24.6)	(24.3)	(25.0)	(25.9)	(27.2)
c) Tertiary Sector	(44.6)	(45.1)	(41.9)	(45.0)	(39.9)	(44.0)	(43.2)	(42.5)	(42.2)

Notes: a: Preliminary estimates; b: net export surplus; n.a. - not available
Source: Jomo, K.S. (1990), pp. 43-48.

II Development Issues and Concerns

Malaysia is a multiracial society. It inherited highly skewed distribution of income. While poverty was widespread and affected all ethnic groups, its incidence was disproportionately high among the Bhumiputeras. It was estimated that the per capita average income of Malays was half the income of Chinese community. The New Economic Policy (NEP) declared by the Malaysian government in 1971 which was to be effective till 1990, accorded the highest priority to eradicating poverty and reducing the racial imbalances in income, employment and ownership of assets. The NEP provided basically the perspective plan framework for the Malaysian second, third, fourth and fifth plans. Over these years, there has been considerable progress in reducing the interracial disparities and poverty particularly in the rural areas. However, a new set of economic issues have arisen now.

Rapid growth of manufacturing and consequent rising productivity of labour has surpassed wages. Despite a fall in relative wages and high rates of output growth, employment growth has been limited to around 3.5% over the past couple of years. Population and hence labour force, on the other hand, have been growing rapidly. As a result, the number of unemployed now estimated at around half a million people poses a serious problem for the policy makers. Moreover, the highest incidence of unemployment is found amongst the secondary school leavers and college graduates. The pattern of growth of manufacturing that emerged in Malaysia might be responsible for this. There are clearly two segments in manufacturing sector in Malaysia: a) outward oriented manufacturing and b) inward oriented manufacturing. The former which has replaced import substitution as the cutting edge of industrial growth has been dominated by electronic goods over the last 15 years. It, however, lacks linkages with the rest of the economy and heavily depends on the international environment. The inward oriented manufacturing has also grown rapidly over the past decade. The spectacular growth of this sub-sector was largely due to handsome fiscal incentives, high effective rates of protection and a large public sector participation. After the world wide recession, this segment has started showing its fundamental weaknesses in terms of low productivity growth, declining profits and excess capacity. Programmes of privatization and industrial restructuring have to be continued in order to revitalize the sector.

Malaysian agriculture so far has been a very dynamic sector. The major growth impetus came from palm oil and of late from cocoa and logs. Timber production has been buoyant but its rate of exploitation is much higher than the sustainable yield. Considerable environmental degradation is also becoming evident. In the medium term perspective, therefore, a fall in the logging output is almost inevitable. The rubber production also shows a declining trend of late. Food crops particularly paddy is no longer economic compared to the world prices largely due to higher wages and low productivity. A shift of rural labour force from the farm to the non-farm sector has depleted human capital in the agricultural sector. The need of the hour, therefore, is to increase farm productivity and obtain efficiency gains rather than increase acreage under cultivation.

On account of the recession of early eighties, the growth and employment in the Malaysian economy was artificially sustained through growing public expenditures. The government's share in the economy has almost become 40%. In the light of the increasing openness of the Malaysian economy, high public sector debt and deficits can no longer be sustained particularly when the growth of productivity in the sector has significantly slowed down. The government's role of late is shifting from the direct involvement to the indirect support of the growth in the economy. Public development expenditures have to be sharply curtailed. Domestic savings and borrowings only should finance the total public investment programmes. However, the total investment in the economy - particularly industrial economy - are promoted by encouraging greater participation of private sector, selective privatization, liberalization of licenses and foreign investment, etc.

The basic development strategy has been achieving growth and distributional goals through promotion of export oriented manufacturing and preserving the competitive advantage in the tree crop sectors. The components of such a strategy are diversification and development of internal linkages to

strengthen trickling down and multiplier effects of export growth. The role of private sector in achieving these objectives is pivotal because it can effectively manage technological upgradation and labour market with the help of government's flexible wage and exchange rate policies. The distributional objectives are considered the domain for government's active intervention. These interventions have to be so planned that maximum advantage of the efficiency gains from the liberalized markets and private sector are obtained on the one hand and the society's distributional and restructuring goals are achieved on the other hand.

III Planning Models

The first five year Malaya Plan (1956-60) was basically a rehabilitation plan and hence did not have any formal systematic approach or framework. The second Malaya Plan (1961-65) was, however, a more formal effort at planning with explicit targets for the output and employment growth. It was based on the Harrod-Domor macroplanning framework. The most crucial parameter to be considered was the incremental capital output ratio (ICOR). Given the value of targeted growth rate of income (4.5% p.a.) in the economy, the Harrod's growth equation was used to find the required rate of investment assuming the ICOR of 4:1. The required investment rate was 18% against the existing 12%. It implied nearly 67% increase in the real investment.

In September 1963, West Malaysia, Sabah and Sarawak came together and formed Malaysia. The first Malaysian plan (1966-70) had almost the same approach and methodology as the previous plan (1961-65). The real gross output was projected to grow at 4.9% p.a. With an assumed ICOR of 3.9, the investment rate required to fulfil the growth target was 19% of the GNP. Over the plan period, the employment growth was assumed to be 62.5% of the growth in output. In other words, the (total) income elasticity of employment was assumed to be 0.625. It was projected that employment would increase by 377,000 jobs in West Malaysia and 84,000 jobs in East Malaysia reducing the overall unemployment rate from 6% in 1965 to 5.2% by 1970.

The Second Malaysia five year plan (1971-75) was a major departure from previous plans both in the methodology and priorities. It was the first plan formulated in the overall perspective provided by the New Economic Policy (NEP). Its priority shifted significantly in favour of eradication of poverty by raising both the income levels and employment opportunities for all Malaysians irrespective of race. The aim of the NEP was restructuring of the Malaysian society by correcting the economic imbalances among the races and regions. The target for the real GNP growth was set at 6.8% p.a. with investment rate estimated at only 17.0%. There was no explicit mention of the ICOR approach to planning.⁶ The employment was targeted to increase at the annual rate of 3.2%. However, since the labour force was also expected to grow at the same rate, the unemployment rate was expected to remain unchanged at 7.3%. A macroeconomic model based on essentially Keynesian framework was used for forecasting the total supply and total demand by components. The policy variables were used as arguments in the functional relationships so that various policy options and their implications could be considered. Public consumption, public investment, exports and net factor payments abroad were considered exogenous while the private consumption, private investment, stocks, imports and indirect taxes and subsidies were considered endogenous. The consumption function was based on the Duesenbury's relative income hypothesis; the investment functions were based on the induced investment (for building and construction) and acceleration principle (for machinery and equipments); and the import functions had consumption and investment as determinants.

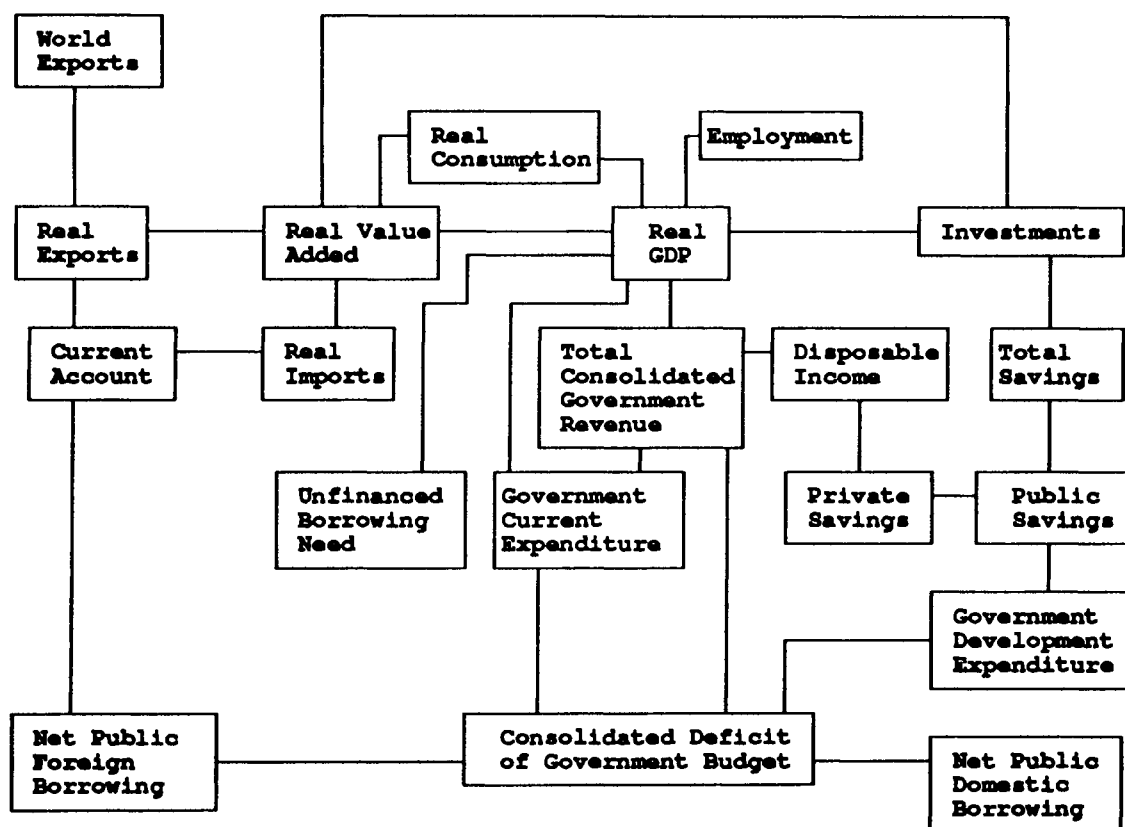
⁶ The implicit ICOR turns out to be 2.5 - so exact a figure that one suspects that it was perhaps implicitly assumed by the planners to calculate the overall national investment targets. The actual ICOR for the previous plan (1966-70) turned out to be 2.6 against the assumed ICOR of 3.9. This is because the actual growth of GNP was 6% p.a. and the investment rate averaged at 15.8%.

In the Third Malaysian Plan (1976-80), the two-gap macroeconomic framework was used for deriving consistent demand- supply projections. It is basically an extension of the simple Harrod-Domor framework to consider the question of consistency between aggregate demand and supply in the light of the external trade balance and internal resource gap. Thus, the two-gap framework explicitly addresses the question of financing the plan in a consistent manner. In order to further test the internal consistency of the estimates, an Input-Output Table for the West Malaysia was used.

The fourth (1981-85) and fifth (1986-90) Malaysian five year plans were based on the general equilibrium model of the economy. An Input-Output framework was used as the fundamental system but the sectoral outputs were constrained by availability of the human and physical capital. The private consumption was linked to the factor incomes generated out of the production process explicitly considering the employment of factors and the rates of factor rewards. Through the demand and supply of factors of production, the income distribution was generated. The detailed model has 259 endogenous variables and 31 exogenous variables. Several of these variables represent sectoral disaggregation.

An overall framework of the basic model indicating the direction of processes and causalities assumed in the model is sketched in Chart-1. From the chart, one can readily see the important place accorded to the volume of world exports in the whole framework. It is seen as the most primary variable affecting almost all important aggregate in the whole Malaysian economy. The quantitative estimate of this model would capture the sensitivity of the economy to changes in the external environment and thereby bring out the issues involved in economic planning in a consistency frame for an open economy like Malaysia.

Chart 1: Framework of the Macro Model



Source: Imakoa H. et al (1990) and Economic Planning Unit, Malaysia

The model is solved through iterative process and as such involves a huge econometric exercise. To begin with, the output prices are determined with the help of given rates of profits and wages. With the output prices available, output levels are solved on the assumption of competition in the markets. Given the level of output and the production technology in form of production functions, demand for the factors of production are determined. However, the implicit rates of factor prices may not be clearing all the markets. The market clearing rates are therefore re-fed into system to repeat the whole exercise. This is an iterative process. The system is further constrained by the output levels representing the sectoral targets which are checked for their internal consistency through the Input-Output table. The level of investment would be varied until the employment targets are fulfilled. The prices - both for product and for factors are assumed to be fully flexible. As a consequence, the model provides an efficient solution where the profit rates, product prices and wage rates ensure full utilization of capital and labour. However, the whole system is highly susceptible to the forecasts of external environmental variables which are obviously not within the control of the planners.

IV Planning Process in Malaysia

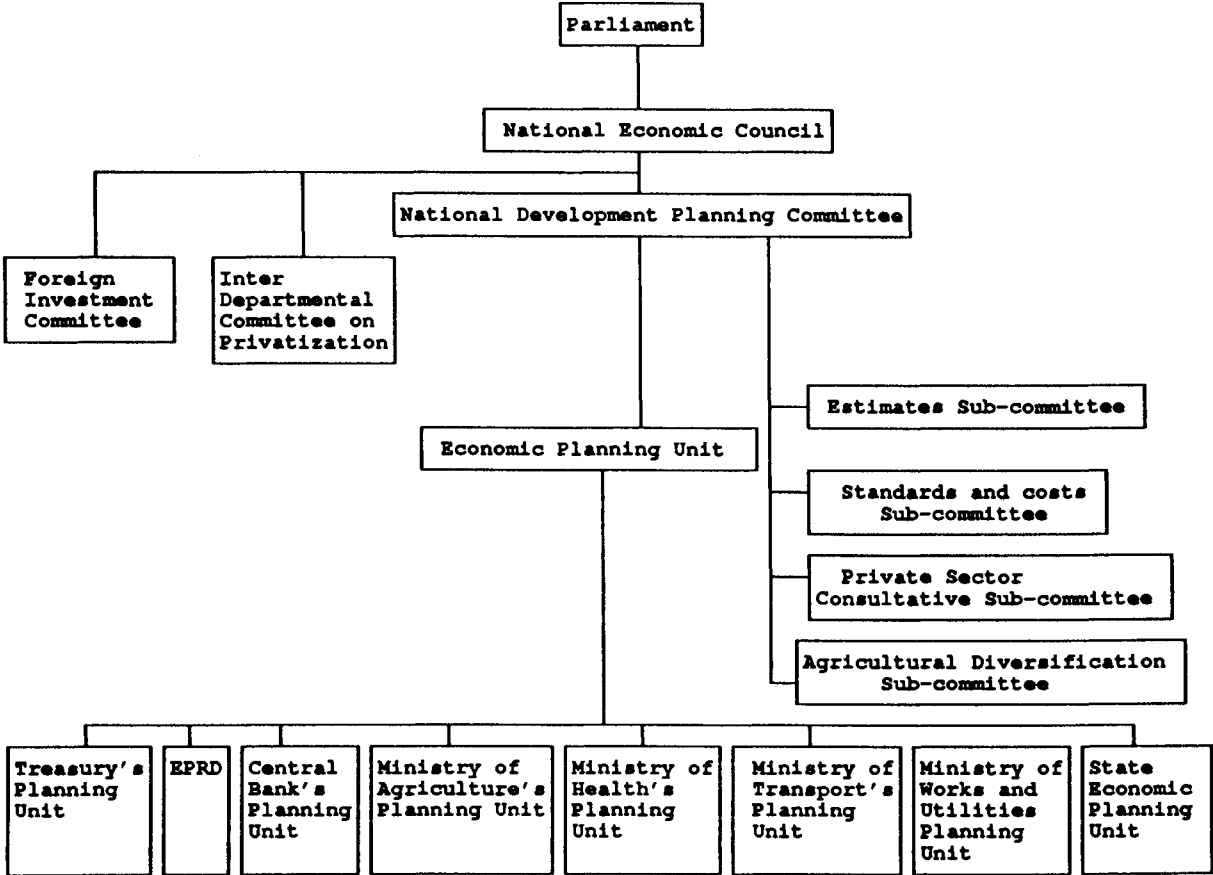
There are three regional levels of economic planning in Malaysia viz. Centre, State and District. Chart 2 presents the organizational set-up of the Malaysian planning machinery at the central level. As can be seen from the chart, the supreme authority is the Parliament. The National Planning Council (NPC) consists of senior ministers from the cabinet. It is responsible for matters pertaining to the major public policy decisions affecting the national economic development. The National Development Planning Committee (NDPC) which consists of senior bureaucrats is responsible for formulation and review of all plans for national development. It also makes recommendations on resource allocations to the sectors and projects. The Foreign Investment Committee (FIC) also made up of senior bureaucrats considers applications from the private sector and foreign investors willing to invest through acquisition of assets, mergers or takeovers of business entities. The members of Inter-Departmental Committee on Privatization (IDCP) are again senior bureaucrats not only from the government secretariats and departments but also from important governmental agencies. The Economic Planning Unit (EPU) is the central staff agency of the government that acts as a secretariat to the NPC, NDPC, FIC and IDCP. Chart-3 outlines the internal organizational structure of EPU and briefly describes the functions of the division and sections.

At the state level, the planning and implementation machinery in Malaysia is briefly outlined in the Chart 4. There is a constitutional distinction between state and federal powers. For revenues, the states typically depend on the centre. The constitution also provides a formula agreed by all states for sharing the revenues. The state governments also have their own sources of revenue like land, estates, entertainment, etc. It is, however, not very substantial since the base is narrow. In terms of sharing responsibilities also the federal government plays a major role, e.g. defence, internal security, health, education, industrial development, other infrastructural development responsibilities, etc. are with the federal government. The tourism, socio-cultural and religious powers and land and natural resources are constitutionally under the jurisdiction of the state governments.

The State Executive Council (SEC) is the final authority at the state level. It is headed by the Mantri Besar (Chief Minister) and has 8 councilor members and 3 members from state level bureaucracy. The planning functions at the state level are carried out by the State Economic Planning Units (SEPU) which is directly responsible to the state government but work very closely with the federal agencies, particularly EPU. The SEPU basically coordinates all the activities related to planning at the state level as shown in the Chart-4 through its linkages with several committees. The SEPU's main task has been to collect, collate and combine proposals from various departments of the government and forward the same to the centre (EPU). At the centre, a detailed scrutiny of the projects takes place with the help of respective ministries. There are well-defined criteria for each sector/programme on which the scrutiny and pruning take place at the centre. For facilitating the formulation of plans at the state level, the centre does provide prior information on financial ceiling to the state

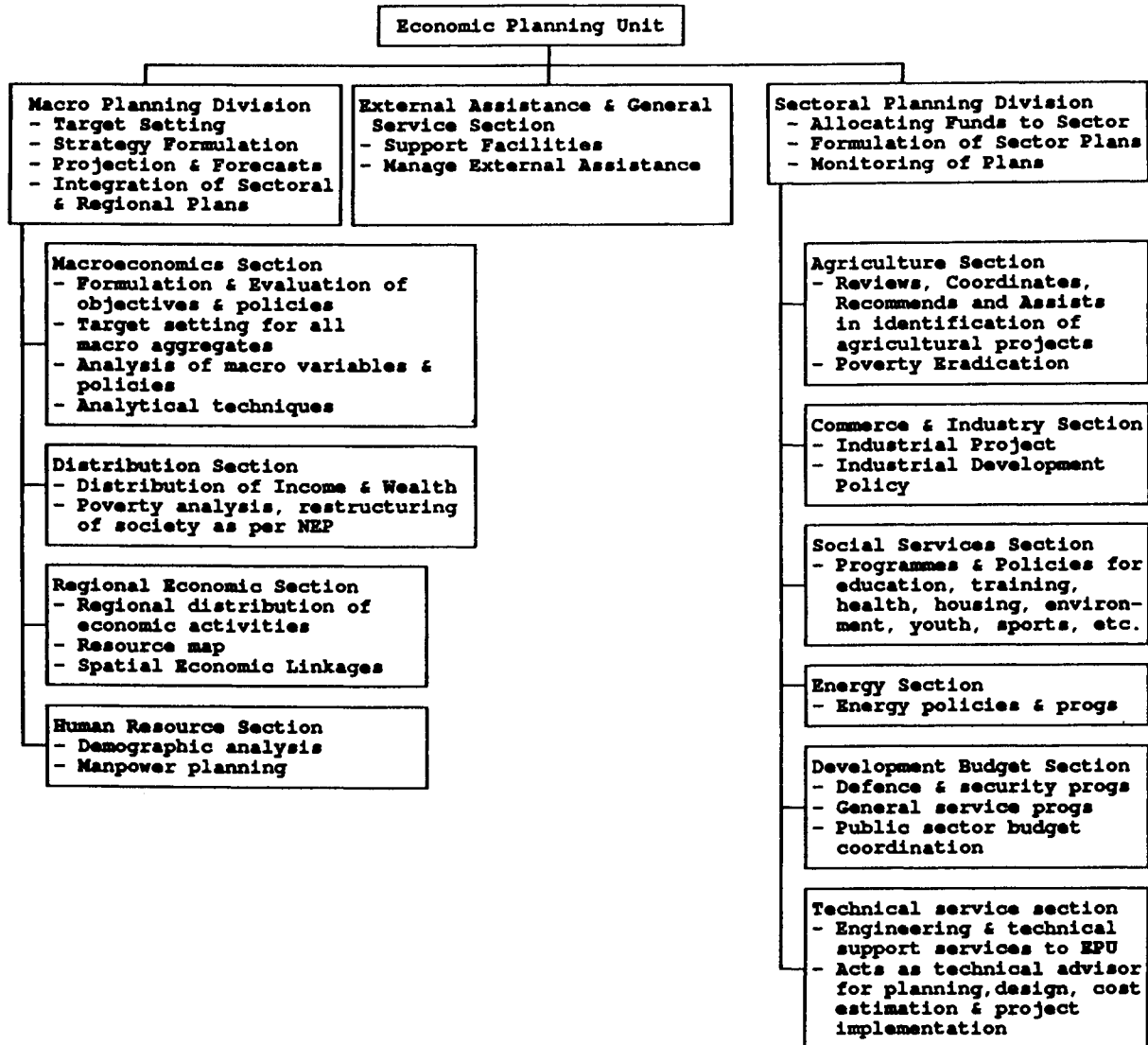
governments. However, the latter do not consider it relevant for their planning exercise. Thus, the top-down financial flows are essentially ignored. The bottom-up physical flows of project/scheme proposals have to be, therefore, dovetailed only at higher levels of planning. Thus, prioritization of projects/schemes takes place first at the state government department level and then at the SEPU level within a sector. In this process, inputs from Ministers and people's representatives are considered through various committees. The intersectoral priorities are, however, decided only at the national level. The entire process has so far been harmonious.

Chart 2: Organizational Set-up of Malaysian Planning Machinery in Phases



At the national level, the EPU is not entirely responsible for the final intersectoral priorities. It is merely a recommendatory body. The NDPC is ultimately responsible to formulate and review all the plans. It is the NDPC which is responsible for the allocation of resources. The targeted goals and objectives and the recommended allocation of resources based on the priority structure emerging at the EPU may substantially change at NDPC. In order to minimize technical complications, the NDPC insists on consensus in order to introduce such changes. It may use its own discretion in this regard and can refer such matters regarding plan proposals directly to the NPC or cabinet for approval.

Chart 3: Internal Organizational Structure of EPU



The lowest planning level in Malaysia is the district as noted earlier. At the district level the main area of concentration is social development. The administration at the district is headed by a District Officer (DO). He is usually drawn from the public service cadre. The qualifications required for DO are 10 years of working experience and graduate degree in any discipline. He is most important functionary in the whole process at the district level. The personnel capabilities impose the major constraint because both in terms of quality i.e. skills and quantity i.e. manpower there is genuine scarcity. The main function of DO is coordination among sectors and departments on all aspects. There are three main areas which a DO has to look after.

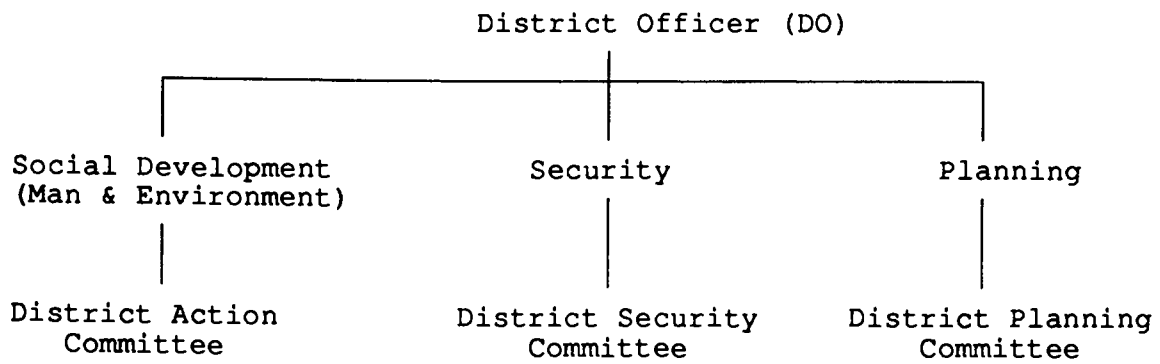
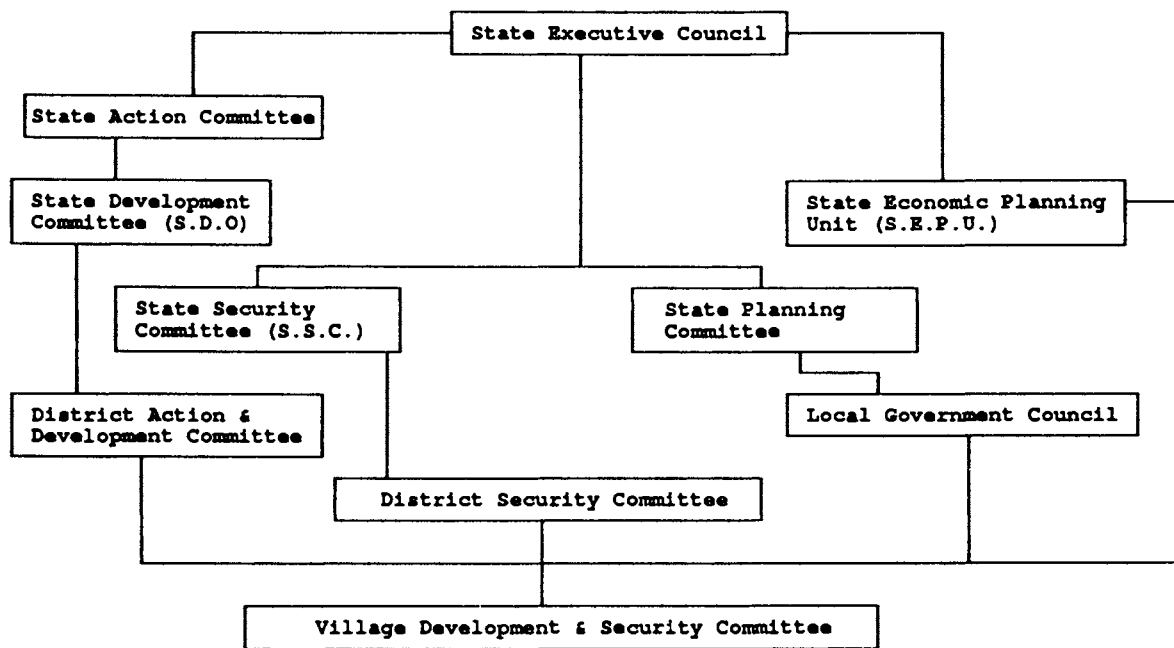


Chart 4: State Level Planning and Implementation Machinery



DO is also responsible for the implementation of some direct plan programmes and projects because some funds flow from the P.M.'s Department through SDO to DO for implementation. In such projects/programmes/schemes, technical sanction is not needed. For the rest of the programmes, the DO has limited powers of technical sanction for minor projects, say not exceeding M\$ 50,000. The DO is in charge of coordinating all agencies and departments at the district level for implementation and formulation of five year plans. The District Planning Committee assists DO in prioritising project proposals received from below. These priorities are, however, within each sector. Intersectoral priorities are left to the state and higher levels of planning.

The levels below the district are Mukim (Block) and Kampung (Village), but planning functions are hardly carried out at that level. The Village Development and Security Committees are proposed and are also functioning in some states. The members in these committees are all appointed and not elected. They are selected from different walks of life so as to adequately represent the people. Ethnic considerations are also taken into account. These committees and the ones at higher levels are currently seen as substituting hard data⁷ required for prioritization. The main argument for the existing arrangement is that the districts are not very big after all and are more or less homogeneous in a given state. Therefore a DO whose term is normally 3 to 4 years and who is invariably a local person, hardly finds any problem of familiarity with local conditions. The prioritization and selection of projects and schemes by DO and DPC is, therefore, considered to serve the same purpose as people's participation.

V Sectoral Allocations

Sectoral priorities in the public development expenditure in different plans in Malaysia are summarized in Table 3. The table shows the sectoral allocations originally planned as well as obtained actually when the plans were implemented. The whole economy is divided into three broad sectors: a) Economic sector which includes agriculture, infrastructure and industry; b) social sector

⁷ The Data Bank project at District level is currently under progress.

which includes education, health, housing and other services; and c) General sector which comprises of administration and security.

	FFYP		SFYP		IMP		2MP		3MP		4MP		5MP	
	Plan	Actual	Plan	Actual	Plan	Actual	Plan	Actual	Plan	Actual	Plan	Actual	Original	Revised
Economic sector	69.2	78.9	68.8	66.5	59.0	63.3	71.6	72.3	59.3	64.0	60.6	75.3	76.0	76.2
Agriculture	23.1	23.6	25.5	17.7	23.2	26.3	23.1	21.7	20.8	22.1	16.4	11.8	17.2	16.0
Infra-structure	44.7	54.0	42.1	46.6	33.9	33.7	32.8	34.1	24.8	26.6	29.8	36.2	44.7	43.2
Industry	1.4	1.3	1.2	2.2	1.9	3.3	15.7	16.5	13.7	15.3	14.4	27.3	14.1	17.0
Social sector	18.5	14.4	22.8	15.6	21.4	17.8	14.0	13.7	17.6	17.2	21.7	13.5	13.1	17.2
Education	8.3	6.3	12.1	8.9	10.3	7.8	7.4	6.9	6.9	7.3	9.3	6.3	8.1	12.5
Health	4.3	2.3	6.7	3.8	4.2	3.5	2.2	1.8	1.7	1.5	1.6	1.0	1.0	1.5
Housing	5.9	6.8	3.7	2.6	4.6	4.9	2.3	2.4	5.5	6.1	8.3	5.3	2.9	2.2
Other services	n.a.	n.a.	0.3	0.3	2.3	1.6	2.1	2.7	3.5	2.3	2.5	0.8	1.1	1.0
General	12.3	6.7	8.4	17.9	19.0	18.9	14.4	14.8	23.1	18.8	17.7	11.2	10.8	6.6
Admini- stration		6.7	4.1	6.3	2.8	3.2	3.6	3.6	2.8	2.2	1.8	1.1	4.0	1.6
Security	n.a.		4.3	11.6	16.2	15.7	10.8	10.4	20.3	16.6	15.9	10.1	6.8	5.0
TOTAL	00	100	100	100	100	100	100	100	100	100	100	100	100	100

Notes: n.a. - not available; FFYP: First Five Year Plan; SFYP: Second Five Year Plan
 1MP: First Malaysian Plan; 2MP: Second Malaysian Plan; 3MP: Third Malaysian Plan; 4MP: Fourth Malaysian Plan; 5MP: Fifth Malaysian Plan
 Source: Jomo K.S. (1990); p.108.

From Table 3, it can be readily seen that there have been frequent shifts in the emphasis on different sectors in the planned allocation of resources in Malaysia over the entire plan period. The first Malaysian plan (1966-70) allocated considerably higher proportion of resources to security cutting the allocation drastically to the economic sector. In the second plan (1971-75) a significant shift in allocation of resources occurred in favour of industry from 1.9% in first plan to 15.7% in the second plan. This shift was, however, at the expense of both the social sector and security. In the third plan (1976-80) allocation to the economic sector was significantly reduced to accommodate increases in security and the social sectors - largely housing and other services. The most affected economic sector during the third plan was infrastructure which rose sharply during the fourth plan (1981-85) but only at the expense of agricultural sector. The social sector continued to receive higher and higher priority, but this time, it is in education and housing. The allocation of resources to security fell relatively. In the fifth plan (1986-90), the security allocation fell sharply to only 6.89% and allocation to the economic sector increased sharply to 76% with infrastructure receiving a substantially higher priority (44.7%) as compared to the fourth plan (29.8%). The social sector again sharply declined in the fifth plan allocation with the major reduction falling on the housing sector. This brief description of trends in the resource allocation among sectors in the Malaysian plans clearly suggests that, barring a clear shift in favour of industry in the second plan (1971-75) which was then maintained subsequently, no long term consistent and persistent strategy for planned intervention in

the functioning of the economy is discernible. Planning in Malaysia appears to be more a matter of short term responses of the government bureaucracy to the changing environment and the problems created by it.

This impression is further strengthened when we compare the actual allocations among sectors with the planned allocations in each of the plans. In almost all Malaysian plans, the actual or ex-post priorities turned out to be considerably different from the planned or ex-ante priorities assigned to different sectors. The only exceptions to this are the second Malaysian plan (1971-75) and to some extent the third plan (1976-80). When we consider this question in the light of the discussion on the planning process in Malaysia, the deviations of the ex-post priorities from the ex-ante priorities are hardly surprising. What it suggests is that considerable discretion is used and changes take place at the stage of implementation of the plan. Table 4 presents the percentage plan fulfilment by sectors for each of the Malaysian plans. Except the second Malaya plan (1961-65) and the fourth Malaysian Plan (1981-85) all other plans suffered from partial fulfilment of the overall plan expenditure target. The percentage of the plan expenditure target fulfilment varied considerably from sector to sector not only across the plans but also within a given plan.

Table 4 Public Development expenditure - Performance in Plans (%)							
	Plan Fulfilment: Actuals as % of Targets						
	FFYP (1956-60)	SFYP (1961-65)	IMP (1966-70)	2MP (1971-75)	3MP (1976-80)	4MP (1981-85)	5MP (1986-90)*
Economic sector	97.4	119.3	99.1	96.0	73.4	188.4	71.5
Agriculture	85.6	85.93	102.5	89.9	72.3	109.1	66.7
Infrastructure	101.4	136.5	92.9	99.4	72.8	184.4	68.9
Industry	76.3	218.9	167.2	100.6	76.3	287.0	85.8
Social sector	65.3	84.2	77.1	94.2	66.2	94.0	94.0
Education	63.8	91.0	70.0	88.5	71.9	102.6	110.8
Health	25.4	70.3	77.4	76.7	58.1	97.0	104.2
Housing	96.8	86.8	98.6	97.8	75.7	96.8	53.5
Other services	--	96.7	65.7	76.3	44.2	51.0	63.9
General	--	261.9	93.0	93.1	55.7	96.0	43.3
Administration	46.0	189.7	109.3	94.3	53.9	90.7	28.6
Security	--	330.0	90.2	92.7	55.9	96.8	51.9
State government	--	--	--	--	--	--	--
TOTAL	87.6	123.3	93.2	95.8	68.1	164.4	71.4

* Plan Revisions as % of originals.
Note: Abbreviations as in Table 3.
Source: Jomo K.S. (1990); pp.106-107.

VI. Concluding Remarks

The above discussion of the planning experience in Malaysia raises some issues. Planning in a consistency framework does not mean following elegant planning models sophisticated in econometric

estimation with inbuilt checks for testing internal consistency. The planning processes play an equally important, if not more dominant, role in deciding the final structure of the plan. Sophisticated forecasting and planning techniques largely serve as the pre-condition for ensuring consistency. Ultimately, it is the planning process containing a large number of non-quantifiable variables that determine the final shape of the plan. It is perhaps for such reasons that most of the Malaysian plans have preferred not to reveal details of the methodology used for making the forecasts of the macro aggregates as well as for deriving the sectoral allocations of the public development expenditures. Apart from the considerations of the nature of uncertainty and tentativeness attached to such forecasts e.g. forecasts for ICORs or for exports (which represent more the judgements of the planner than any logical derivation), the aspects of flexibility and subjectivity would also have weighed in such decisions. Unless the planning processes are appropriately designed and strengthened, the plan in practice may differ substantially from the plan on paper. Under such circumstances, the issue of whether or not long term or medium term economic planning in an open economy like Malaysia is desirable and advisable, becomes highly relevant.

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Chapter 5

Methodology of Planning and Planning Process in Kenya The Case of The 6th Plan 1989-93

1. Background

Kenya achieved the Independence in 1963. It has a democracy with a single party political system. Geographically, Kenya is spread over 583 thousand square kilometers, about 75% of which is classified as desert, semi-desert or arid bush. Kenya's population was estimated to be 22.1 million in 1987, but its growth rate of 3.7% p.a. is considered one of the highest in the world. And yet, Kenya has achieved miraculous results in terms of the basic quality of life indicators like adult literacy, life expectancy and infant mortality. Literacy rate increased from 20% to 50%, Life Expectancy from 44 years to 58 years and the Infant Mortality Rate declined from 126 to 72 since independence. The percapita GNP in 1987 in terms of U.S. dollars was estimated at \$330. Like most of the developing countries, Kenya's economy is heavily dependent on agriculture which employs more than 70% of the total labour force and accounts for less than 30% of the domestic income. The industrial base of Kenya is considered relatively strong and diversified employing around 10% of the labour force and contributing around 18% of domestic income. Table 1 provides annual growth rates of real GDP (at 1982 prices) in the important sectors of the Kenyan economy over the years 1972 to 1987. It clearly brings out important characteristics of the Kenyan growth experience in the past.

It can be seen from the table that the rate of investment in Kenya is reasonably high at around 25% since mid-seventies. The trends moreover, clearly indicate that the foreign savings are relatively declining and the national savings are increasing over time. The gross national savings represent investments financed by households, domestic corporations and the government. Like most other countries, in Kenya too, the trend in the government sector's contribution to national saving is a serious matter of concern because it is declining since 1980 and of late has become negative.

The trend in Kenya's public debt since Independence is presented in Table 3. Since 1974, there has been a considerable increase in the government budget deficit although, of late, its growth rate is significantly reduced. Thus, during 1974 to 1978, the budget deficit increased by 25.31% per annum; during 1978 to 1982, it increased by 20.56% per annum; and during 1982 to 1987, it increased by only 5.36% per annum. In absolute terms, however, it remained as high as 6.1% of the GNP in 1987. The total public debt in Kenya has also been increasing at an alarming rate of 16.69% p.a. since independence and at 20.50% p.a. since 1974. The composition of the total public debt is also changing rapidly with the proportion of the foreign debt rising from 46% in 1978 to 76% in 1987. Thus, the foreign debt has become more than 3 times the domestic debt in Kenya. This has serious implications on the economy's debt service charges. As the table shows, the service charges on external debt as a percentage of the total exports of goods and services (excluding factor incomes) increased from 1.65% in 1964 to 18.38% in 1987. Thus, almost a fifth of the total export earnings are required to merely service the external debt in Kenya. Similarly, the ratio of external debt to the GNP has also become alarming and stood at 36% in 1987. This has become one of the most critical issues in the economic development of the Kenyan economy.

Another critical issue is of inflation. Kenya showed remarkable price stability in the initial phase of 9 years after independence. But the oil price shock of 1973 leading to the world-wide inflation forced the Kenyan economy into the spiralling inflation from 2.6% in 1972 to 9.6% in 1973, 15.3% in 1974 and 15.6% in 1975. Rate of inflation remained high around 10% between 1976 and 1981. But again second oil crisis accompanied by widening budget deficit to fight the recession forced the economy into an all-time high inflation rate of 22% in 1982. Since then, however, concerted

government efforts assisted by favourable international economic environment have significantly checked the inflationary pressure though the inflation rate is most likely to be around 10% of late. Table 4 presents percentage increases in consumer prices for the years 1983-87.

Table 4 brings out an important feature of the Kenyan inflation in recent years. Although the inflation in the Kenyan economy favoured the rich upto the year 1984-85, of late, it appears that the poor are protected from the inflation. However, the rich continue to experience lower level of inflation than the middle income group. The worst sufferer of inflation is the middle income group. The distributional impact of inflation in Kenya during the recent years is thus, ambiguous.

Another important issue in Kenya's economic development is the employment creation and wages. Tables 5 and 6 provide the information on structure of employment and changes in wage employment and real earnings over the recent years. Table 5 clearly reveals that the employment growth in Kenya has been remarkably high at 7.87% p.a. during 1984-87. The most spectacular growth of employment has taken place in the small scale enterprise (SSE) sector which has grown at the rate of 33% p.a. The slowest growing sector in terms of employment in recent years in Kenya is the private modern sector. The share of SSE in the total employment in the Kenyan economy has increased from 10.37% in 1984 to 19.35% in 1987. The shares of all other broad sectors in the total employment over the years 1984-87 have declined. In order to create employment to absorb the fast growing labour supply the policy emphasis on SSE seems to have worked in Kenya in the initial period. The labour productivity and future potential of this sector, however, raise serious concern.

The real earnings of the wage-employed in Kenya in the recent years as revealed by Table 6 do not show a very encouraging trend. If we take the inflation rate relevant to the middle income group into account (See Table 4), we find that real earnings of the workers have declined during most of the recent years in Kenya. On the other hand, a conscious interest rate policy followed by the Central Bank of Kenya ensured that the real interest rates in Kenya remained positive during the period. In real terms then, labour is becoming cheaper and capital costlier in recent years in Kenya.

Any account of Kenya's economy cannot be complete without explicit reference to its unique Harambee movement. It is a self-help movement operating concurrently with official development programmes since Independence. The movement has been responsible for mobilization of large quantities of capital resources providing for a wide variety of basic needs. The emphasis in Harambee has been more and more on social development projects like education, health, etc., rather than on economic development projects like transport and communication, agricultural ventures, etc. The Harambee projects accounted for 11.8% of Gross Fixed Capital Formation between 1965 and 1984. Table 7 provides information on the movement's progress in Kenya over 1965 to 1984. It is considered an important vehicle to decentralise planning process effectively in Kenya because the participants' contributions in the movement take the form of cash, labour, materials and professional services. All segments of the society, governments and even foreign agencies are involved in the movement.

Having described briefly the background for the Sixth Development Plan of Kenya, in the next section, the approach to the plan including the main objectives is discussed. The third section, then provides the details of the targets set along with some discussion on the methodology adopted in the Plan. The fourth and the fifth sections consider the planning process and the issues in decentralization of planning in Kenya since the major theme of the Sixth Development Plan of Kenya is "*Participation for Progress.*"

2. Approach to the 6th Plan

Kenya's Sixth Development Plan is formulated in the framework provided by the Perspective Plan for the period 1984-2000 as outlined in *Sessional Paper No.1 of 1986 on Economic Management for Renewed Growth*. The basic development philosophy of this plan is consistent with the one contained

in *Sessional Paper No.10 of 1965 on African Socialism and Its Application to Planning in Kenya* which clearly spelt out the goals and objectives of development planning in Kenya. These goals and objectives include social justice, human dignity, freedom from want, disease and exploitation, equal opportunities for all and high and growing percapita incomes, equitably distributed. Although the broad development philosophy remains unchanged, the Sixth Plan proposes a major re-orientation of policy and priorities particularly in certain key areas as compared to the previous plans.

First of all, the Sixth Plan is based on incorporation of the structural adjustment process. The major thrust during the Sixth Plan would, therefore, be on redressing and reshaping those previous policies and strategies which emphasised: (1) import substituting industrialization, (2) concentration of more economic activities in major towns at the expense of rural areas; (3) government's role and involvement in even commercial activities where the private sector could be more efficient, and (4) development of modern wage paying sector in general and public sector in particular for generating employment.

The second important point of departure in the 6th Plan from the previous plans is the basic approach regarding the management and decision making in public affairs. The conventional centralised decision making at the headquarters in Nairobi has proved inefficient. In order to correct this situation, therefore, the Sixth Plan emphasises decentralization of the planning process on the lines suggested in the Blue Book on *District Focus for Rural Development* and the *Budget Rationalisation Programme*. Thus, decentralised planing in Kenya is adopted as a basic approach to improve efficiency in management of public affairs and utilization of manpower and capital resources.

The third distinctive aspect of the Sixth Plan in Kenya is its integrated approach to planning. The Sixth Plan, unlike its predecessors, seeks to address particular issues rather than to discuss the specific activities of individual ministries or sectors. It implies not only that a limited set of issues is addressed at a time but also that all arms of the government ensure improved communication, acceptance of common goals and cohesion of efforts in seeking to resolve these issues. Thus, such an approach entails viewing development issues inter-sectorally and is expected to facilitate on-going and timely examination of possible constraints to development and initiate steps towards overcoming such constraints. The Integrated Approach to planning also has clear methodological implications. For instance, it implies that appropriate relative price signals are given in order to induce all participants to make the desired choices, and that careful attention is given to the time-phasing of economic activities so that they follow a logical, sequential pattern. In other words, internal consistency of the production and consumption targets of different sectors over time has to be ensured in the Integrated Approach to planning. There is a feeling among the government bureaucracy that the integrated approach is not new in Kenya. It has been already applied in the District Development Planning which is based on complementarity between the ministries whose approaches are sectoral, and the districts where various sectors are brought together for rural development activities.

As we have already discussed in the previous section, the main problems before the Kenyan economy are (i) high growth of population giving rise to a rapid growth of labour force, (ii) public debt both internal and external; (iii) inflation; and (iv) low percapita income. The main objectives of the Sixth Plan are, therefore: (1) Employment creation, (2) Improved management of human and financial resources, (3) Achieving rural-urban balance in development, (4) Expansion of agricultural production so as to move toward the self-sufficiency in food production, (5) More efficient and faster industrialization, (6) Preservation and development of natural resources, and (7) Enhancement of public welfare. The Integrated Approach to planning to be followed in the Sixth Plan would imply that only these areas considered to be of primary importance to the development of Kenyan economy will be addressed by all sectors and that the Plan would not attempt to cover all the difficulties that the country is likely to encounter over the plan period.

3. Targets Set In The Plan

The process of converting broad objectives into precise goals and targets to be achieved over the plan period is a crucial step in the exercise of national planning. The way these targets are set becomes important methodologically. Usually, all the plans must ensure that different targets are: (1) internally consistent with each other; and (2) reasonably achievable or feasible given certain plausible assumptions about the behavioural responses of the economy to its most likely economic environment. In order to ensure the consistency and feasibility of various plan targets, usually one or the other type of macroeconomic model is followed. In the Sixth Plan of Kenya, a simple Harrod-Domor model provides basis for consistency framework at an aggregate level whereas the standard macroeconomic model of an economy based on simultaneous equations is used to derive disaggregated targets. The latter are, however, checked for their internal consistency by using an old (1967) Input-Output Table updated for the year 1986.¹ It is important to note here that econometric estimates of parameters based on past data are only one of the essential inputs in deriving the targets. Judgement, intuition and hopes of the planners are also inbuilt in numerous targets. It is only for this reason that the planners consider the targets set in the Sixth Plan as somewhat ambitious.

The whole target setting exercise in the Sixth Plan begins with the population and labour force growth. Population growth depends on life expectancy, total fertility rate and death rate, the most crucial parameter being the fertility rate. Currently the total fertility rate in Kenya is around 8 children which is the highest in the world. If it is assumed to remain unchanged, the growth of population in Kenya would be 4.3% p.a. other things remaining the same. However, the family planning programme in Kenya is expected to make a dent and as per the perspective plan (1984-2000), the total fertility rate in Kenya is targetted to come down to 5.6 children which would bring down the population growth rate to 3.7% p.a. In the long run, such a reduction in the population growth would save the national resources from feeding and educating the additional children, for direct investment in further growth. The Sixth Plan takes the population growth rate to be 3.7% p.a. The rate at which the living standards of the people can be improved over the plan period is considered to be 1.6% p.a. This is the most important target of the Plan. It implies the annual growth rate of 5.4% in real GDP.

Persistently high growth rate of population has implications on labour supply in the economy. Taking 40% as the labour force participation rate, the perspective plan (1984-2000) estimates that the labour supply in Kenya would be growing at the rate of 4.0% p.a. To accommodate such a huge increase in the labour supply without raising the unemployment rate is the most challenging task before the planners in Kenya. It is more so because the concept of unemployment is closely linked to the productivity. Not only that people must find jobs, but that the jobs should be sufficiently productive to yield adequate incomes. The overall target of the income growth in the economy of 5.4% p.a. implies that average productivity per worker in the Kenyan economy can increase by 1.2% if the employment has to increase by the targetted 4.2% p.a. Growth of labour productivity is attributed to improvement in the efficiency of workers, growth in the level of capital employed per worker, increased availability of land and materials and general technological progress. A moderate increase of only 1.2% p.a. in the overall labour productivity over the plan period, therefore, implies that significant shifts in the structure of economy from low productivity (traditional) sectors to high productivity (modern) sectors are ruled out. Thus, rural employment (defined as the sum of non-wage agriculture, farm and rural non-farm employment) and small-scale enterprises would play a major role in generating new employment over the plan period. This is also dictated by the overall resource constraint on the economy. It is estimated that a job in the modern sector requires approximately K£ 16,000. At that rate, even if Kenya maintains a high investment rate of 25%, it can generate only 1.4 million new jobs in next 15 years as against the total requirement of 6.5 million new jobs. On the other hand, a job on small farms or in very small-scale industry and services or in self-employment takes only a fraction of K£ 16,000 per worker required in the modern sector.

¹ The I:O Table is updated using the RAS method - a popular non-survey technique. A comprehensive revision of the I:O Table for Kenya based on the Survey data for the year 1990 is currently being carried out.

At this juncture, it is important to get some idea about the productivity of investment² in the Kenyan economy assumed by the planners. The perspective plan clearly notes that "for the past decade savings have been invested in much lower productivity uses - it has required nearly six units of new capital to produce one new unit of output - and consequently Kenya's GDP has grown at just over 4 per cent a year. Thus a fundamental task becomes evident: to accelerate Kenya's growth, it will be necessary to increase substantially the productivity of investment." In other words, the Incremental Capital Output Ratio (ICOR) in the past decade in Kenya was around 6. The planners have, however, calculated the requirement of investment resources for achieving growth target of 5.4% p.a. on the assumption of the overall ICOR of 4.3 which represents a substantial improvement in the productivity of investment in the system. In this context, it is interesting to note that the planners feel that instead of using an observed ICOR, it is better to use targeted ICORs based on judgement considering the available historical evidence. They also prefer the assumption of constant ICORs to the variable ones over the planning period. In terms of the data base on capital, estimates of the capital coefficient matrix as used in the dynamic I:O model are not available in Kenya, though the Planning Ministry does have an estimate of Fixed capital stock by sectors. It is, however, not officially published. Based on this estimate and the data from the national accounts, targeted Incremental Fixed Capital Output Ratios (IFCOR) for different sectors in the economy are worked out which are presented in Table 8 along with other targets of the Sixth Plan.

Table 8 also provides sectoral decomposition of the GDP growth targets which are derived by using the most recent statistical evidence on the demand for the sectoral outputs arising in and outside the economy. In this exercise the planners use their judgement about likely changes in the past trends, new developments and the "desired" direction of changes in demand for sectoral outputs. Once these sectoral targets of GDP growth are derived, the sectoral allocation of fixed investment is obtained by using the sectoral IFCORs. Based on the available fixed investment and a judgement about the general technical progress likely to take place in different sectors, a forecast of the growth in average labour productivity during the plan period is derived which is also presented in Table 8. Ultimately, the target growth of employment in each sector is derived by using the targeted growth of labour productivity and real GDP growth. It is important to note that during the Sixth Plan period, positive growth is projected in both labour productivity and employment in all the sectors of the Kenyan economy.

The financing of the Sixth Plan in Kenya is constrained by the structural adjustment programme. The resources for the Plan are expected to be raised from (1) the domestic savings from the private sector and the government sector, and (2) foreign savings. The private sector saving includes savings from the household sector and the private corporate sector. The government sector saving is basically the excess of current revenues over current expenditure of the government. The foreign saving is the excess of the imports of goods and non-factor services over their exports. Table 9 presents the projections/targets of the plan finances.

It is clear from the table that the structure of resources raised for the Plan is expected to undergo substantial changes which are consistent with the structural adjustment programme. The foreign savings as a proportion would be declining largely on account of reduced imports. The imports are expected to increase by 5% and exports by 5.8% in volume during the plan period. The domestic saving rate is expected to rise over the Plan period again on account of increased government savings which are expected to be brought about by increased current revenue through improved tax collection coupled with increased taxes, and decreased government expenditures as proportion to the GDP at market prices. Obviously, higher taxes would reduce private sector's savings which is again reflected in the calculations. The public consumption shows a relative decline which largely accounts for the relative decline in overall consumption. The overall investment rate is assumed to remain more or less constant over the Plan period. It is important to note that these targets along with the physical targets

² Gross investment is obtained by adding changes in stocks (inventory) to Gross Fixed Capital Formation (GFCF) which represents investment in new physical assets including replacement in worn out plant and equipment.

discussed earlier provide the basic policy framework within which the government should formulate and implement policies to regulate and control the economic activities. The rest of the Plan usually provides specific suggestions and guidelines for the details of such policies and projects/programmes/schemes.

4. Planning Process In Kenya

Kenya's Planning Manual was prepared in the 1970's. It is a comprehensive document describing the administrative structure, job specification of different officers, plan formulation and implementation procedures, etc. The Manual is not updated so far, but the Blue Book on *District Focus For Rural Development* (1987) contains substantial revisions and modifications in the planning process of Kenya and they are all accepted and implemented by the government. The planning process as it exists now in Kenya could be conveniently outlined by considering the following five elements: a) sessional papers; b) five year development plan; c) annual plan; d) district plan; and e) planning by external agencies.

The government prepares detailed reports from time to time involving outside consultants on either specific issue or sectors. These are called Sessional Papers. They are ad hoc and occasional in nature. Usually when a problem becomes more persistent or an issue becomes very pressing, the government asks for a Sessional Paper on that issue or sector. In the past several such Sessional Papers are prepared on employment, education, health, housing, public sector investment, etc. These papers basically lay the economic and political framework to tackle the problem in the long term perspective. In short, they serve the same purpose as a perspective plan. In the case of the Sixth Plan in Kenya, Sessional Paper No.1 of 1986 on Economic Management for Renewed Growth provided comprehensive policy framework like a perspective plan upto the period 2000 A.D.

The formulation of the five year development plan begins during the fourth year of the implementation of the previous plan by a review of the situation organised by the Ministry of Planning and National Development (MPND). Discussions with the Ministry of Finance are held and a joint cabinet memorandum is prepared which is like an 'approach paper' to the next plan. It contains (i) chosen theme of the plan, (ii) key development priorities; and (iii) strategy for the plan. This is, then, communicated to different ministries who, in turn, start preparing proposals for programme of actions and submit them to the MPND which coordinate all these papers in the sense that it holds discussions and suggests modifications in their proposals. This takes about a year and a half. When the programme of action is finalised, it is taken to the Cabinet for final approval. It is also simultaneously sent to all Institutions, Ministries, Parastatals, etc., involved in the Plan implementation.

The annual plan, usually tied to the annual budget is a very important instrument in the planning process in Kenya. The Five Year Plan gets implemented through the Annual Plans. The budget is presented in the month of June. Three months before, the Finance Minister sets up a Budget Steering Committee which goes into the projections on revenue and expenditures including expected loans, grants from abroad, bilateral agreements, etc. It also reviews the past year's international and domestic economic environment and speculates about the future through the Economic Survey, generally brought out by May every year. While preparing the Survey, the committee also invites papers on special topics if required.

The most critical element of the Kenyan planning process where the Sixth Plan has introduced significant modifications is the district plan. Effective decentralisation of the planning process can be achieved only by strengthening this particular element. In Kenya, Province is not a planning unit. It is only an administrative unit. District is the next unit of planning and hence at the district level also the five year plan is prepared. Different departmental heads at the district levels are involved in the preparation of these plans. All these activities are closely coordinated and monitored by MPND. For every district, the draft plan is edited and approved by MPND only. These plans do not go to the Cabinet for approval. The plan has two components: a) National Component and b) District

Component. The Planning Manual does not draw any clear demarkation of activities into the national and district levels. Generally, they are decided and operated by mutual consent.

Lastly, external agencies have important role to play in the planning process in Kenya. There are again two broad categories here: a) Bilateral agreements on big projects like electricity system or transport network, etc. In such bilateral agreements, the country which funds the project in Kenya (like France or Germany) generally get their experts/consultants to plan for the activity and implement it with the available funds. b) Multilateral aid giving agencies like UNICEF, World Bank, ILO, UNDP, UNIDO, WHO, etc. These agencies also help the country with planning, monitoring and implementation. Different agencies usually have their own methods of working. However, by and large, they identify problem areas, look into the existing government programmes in these areas, identify projects/schemes/programmes which are agreed upon by the government and then they collaborate by providing required proportion of resources. Some of these agencies also provide specific help for specific issues/problems. The way these agencies are operating in Kenya, one may get a feeling that a part of the planning and priority fixing in the Kenyan Plan is not done in Kenya but at the headquarters of these agencies outside Kenya. It is perhaps for such reasons that it is explicitly mentioned in the Budget Rationalisation Programme to review the resources committed in the external agencies projects and programmes in Kenya.

Having outlined briefly the main elements of the planning process it would be interesting to examine the details of the decentralisation of planning implemented in Kenya. As we have already seen, the annual budget and the district plans are the critical elements here. Decentralisation in Kenya means shifting of the responsibility for planning and implementing rural development from the headquarters of the ministries to the district. It is based on the principle of a complementary relationship between the ministries with their sectoral approach to development and the district with their integrated approach to addressing local needs. Responsibility for the operational aspects of district-specific³ development projects has been delegated to the districts. The districts, however, do not have any powers to formulate their own policies. All policies are still formulated only at the central level. Responsibility for general policy and planning of multi-district and national programmes remains with the ministries. *The basic objective of such a decentralization of planning in Kenya is to broaden the base of rural development and encourage local initiative in order to improve problem identification, resource mobilisation, and project design and implementation.*

District Development Committee (DDC) headed by the District Commissioner (DC) in each district is an important instrument to decentralise planning effectively. It is responsible for rural development planning and coordination, project implementation, management of financial and other resources, overseeing local procurement of goods and services, management of personnel and provision of public information. The following are the distinct administrative levels in Kenya: a) Nation b) Province c) District d) Division e) Location f) Sub-location. Sub-location consists of a group of villages and settlements. At each level below district, there is a development committee whose membership includes local level leaders, local councillors, government officials (departmental chiefs and assistant chiefs) and representatives from parastatals, schools and non-governmental organisations (NGO). The chairman of such committees are senior government officials at respective levels. The DDC has members of the parliament from the district as members and elected members from the District Council along with representatives from NGOs and district departmental heads from the district bureaucracy. District Development Officer (DDO) is the secretary of DDC. This committee is responsible for preparing: (a) 5 year District Development Plan and (b) the annual Annex to that plan. It is responsible for planning and coordination of all district-specific projects sponsored by government, foreign donors, local authorities, Harambee efforts, parastatal organisations and NGOs.

³ Projects and local components of the larger programmes that are intended to serve a full or part of a district are considered district specific, e.g. a village water system, a rural access road, a rural health centre, etc. A provincial hospital or university, although located in one district, is intended to serve a much broader population and hence would not be considered district-specific.

It must also identify financing for proposed projects, ensure that the funds have been committed, and coordinate timely provision of the funds. Since funds are limited, the DDC has to set priorities for their use. Unlike the past Plans which tended to be the unconstrained lists of all projects wanted in the district-popularly called "shopping list approach" - the DDC must now assess the local development potential, needs and priorities.

The entire process of prioritising projects is an interesting aspect of the decentralisation of planning in Kenya. Since the district plan emanates from below, project identification takes place by considering a detailed area profile (resource map) and potentials, issues, problems and constraints in each of the sectors. Based on the broad evaluation guidelines and indicative limits on financial resources, priorities among different projects/programmes are derived within each sector. Priority ranking with location and all other relevant details of the projects are decided right from the sub-local level by the development committee at that level.⁴ Thus, these are supposed to reflect people's choices in the district. The administrative hierarchy is converted into its development linkage roles. However, it is important to note that the projects/programmes are finally prioritized at the District Level although they have to be screened at lower levels. Thus, the technical skills required at the district level are much higher. It is for this reason that DDC is aided by District Executive Committee which is served by District Planning Unit consisting of DDO, District Statistical Officers, Economists, Programme Officers, Physical Planners and assistants. District Information and Documentation Centre (DIDC) serves as an information arm for DPU. The District Executive Committee (DEC) consists of only technocrats from the government bureaucracy and headed again by the DC. In DEC, no political representation is allowed. DEC serves DDC in technical matters of prioritising projects after evaluating them. Since the chairman of DEC and DDC is the same, it is expected that the priorities set by DEC would not be substantially altered by DDC. A strong DC may achieve this, but not all can. Finally, it is interesting to note that while detailed exercises of prioritising projects by location and sectors are carried out, the national annual plan publication provides only broad financial allocation by sectors.⁵ This is done deliberately to avoid the expectations and speculations of political nature leading to unnecessary controversies.

In order to decentralise economic planning meaningfully, districts have to be fully involved in every stage of the government budgetary process. There are well defined procedures for this purpose which have to be complied with by the ministries and the district administration. The ministries prepare their budget estimates in Kenya in three phases (a) a Programme Review and Forward Budget for next 3 to 5 years is prepared during August and September every year; (b) Revised Estimates for the current financial year are prepared during October and November; and (c) Draft Annual Estimates for the next financial year are prepared during January and February. All these estimates are reviewed by the Treasury. Chart 1 summarises the steps and the timetable of the Kenyan budgetary process.

The crucial concept in this otherwise self-explanatory chart is the "district ceiling." These are provided to the district level officials by different ministries after carefully considering the District Development Plans and the Annexes of previous years. The term "District Ceilings" is used to denote several estimates e.g. (i) the amount of money which the district can allocate to specific projects; (ii) the sum of committed allocations for various specific ongoing or incomplete projects; (iii) allocated and unallocated funds; (iv) ceiling for the recurrent expenditure by budget head and item; etc. The ministries must also provide the districts with a statement of national and sectoral policies that guide ministry priority and budget expenditures. It should, moreover, incorporate district views based on the district development strategies and priorities as given in the district plans. Pre-existing project commitments should also be listed for the districts since they are included in the "district ceilings."

⁴ These committees are chaired by government officials. Generally, for the location and sub-location levels, university graduates are not available but for division, district and province levels, only graduates are taken.

⁵ Of late, the Five Year Plans, e.g. Sixth Plan, discuss only issues and problems of development with appropriate strategy and policy framework without going into the details of specific projects or financial allocations.

Chart 1 : Annual Budget Cycle

DISTRICTS

Identification
of Projects

Prepare Annual
Annex

Receive District
Forward Budget
Allocations/Prepare
Comments and
Recommendations

early February

Implementation Begins

MINISTRIES

Prepare District
Forward Budget Ceilings

early July

August 15th

Prepare Forward
Budget

September 30th

Receive Approved
Forward Budget/Prepare
District Disaggregations

early January

Prepare Draft
Annual Estimates

Draft Estimates to
Parliament

TREASURY

Treasury Review
and Approval of
Forward Budget

December 15th

February 28th

Treasury Review
of Draft Estimates

early June

The Kenyan planning process discussed so far indicates existence of two distinct flows: a) Top-down; b) Bottom-up. The top-down flows are in the form of district ceilings from different ministries/sectors which are financial. The bottom-up flows, on the contrary, are in the form of prioritised set of district-specific projects/programmes which are physical in nature. This entire process, however, leaves the sectoral allocations to be decided at the national level. To that extent, the Kenyan model provides the example of decentralised sectoral plans. The weak link in the whole process is the allocation of resources between the national component and the district component. One feels that decision about it remains somewhat arbitrary. The interdistrict allocations of the ceilings, however, are based on some objective criteria like population, development potentials, needs of the area, foreign agencies/donors' integrated programmes, etc.

5. Issues In Decentralisation of Planning

The process of decentralising planning in Kenya began during the Fifth Development Plan and progressed considerably during the Sixth Plan. Some experience of the decentralisation is already available which has also brought out some issues. These issues can be broadly classified into the following categories⁶: i) Statistical Development, ii) Qualified Personnel, iii) People's Participation, iv) Autonomy at lower levels and v) Political Interference.

i) *Statistical Development*: In any effort to decentralise decision making, the level of statistical development and sophistication plays very crucial role. Important relevant statistical data, if not available readily, regularly, and of reliable quality at the required level of disaggregation, the whole exercise of decentralising decision making at the district level or below can turn out to be counterproductive and inefficient. This problem was recognised early in Kenya and consequently, the District Information and Documentation Centre (DIDC) was proposed to be created as a component of the DEC. It is supposed to take care of the problem of creating the required data base for efficient decision making at the district level. In 18 out of 41 districts, the centre is already operational. The rest of the districts are also proposed to be covered gradually. Moreover, a massive projects on computerisation of infrastructural data on 12 items at locational and sub-locational level in each district is carried out currently. This information is proposed to be up-dated annually. The data are put on computers at MPND. It is, therefore, possible to incorporate additional data on annual basis as well as on additional variables if needed without any major costs.

ii) *Qualified Personnel*: The personnel quality is one of the main issues in successful implementation of decentralised decision making in most of the developing countries. As we have already seen, upto divisional level, the country must be capable of having well-qualified professionals who can formulate projects and evaluate them meaningfully relating them to the national and regional priorities and policies. A training programme on massive scale is needed for the purpose. Fortunately, UNICEF is providing substantial assistance on their ambitious project on Capacity Building at District Level wherein they identify the weaknesses and gaps in the currently available expertise at different regional levels, design appropriate curriculums and provide training to the selected personnel.

iii) *People's Participation*: The Kenyan model as discussed above appears very impressive in terms of people's participation in the planning process. However, there are some problems. The development committees at different levels like sub-location, location, division and district are made up of members, a large number of whom are appointed and not elected popularly. The people's input in the planning process is, therefore, limited to the perception and notions of a few persons not necessarily representing the desire/need of the people of the region. In fact, the prioritisation of the projects takes place only at DEC which is consisting of technocrats from the government bureaucracy. Thus, the plan at the district represents at best the government officials' views modified somewhat by a few selected persons from the region concerned. Meeting of people is not called at any level to

⁶ Kenyan model, decentralisation of planning does not pose any serious problems of ensuring internal consistency though in models of some other countries, it becomes a serious issue.

identify or prioritise project. The people's participation, however, is ensured in Kenya through what is known as Harambee movement. The spirit of this movement is self-help. Community projects where the community participation through required resources in terms of any one or more of labour, land, material or money comes forward are taken up by committing additional resources from either the government or foreign agencies under the Harambee Movement. In this way, people's participation is ensured in project identification and implementation but not necessarily in its formulation. For decentralised decision making, people's participation at the plan formulation stage is more crucial.

iv) *Autonomy*: Decentralisation becomes effective only if certain powers are devolved from the centre (Ministries) to the district and lower levels. These powers usually refer to the ones relating finance. In Kenya, since all policies are formulated only at the national level, the lower levels lack autonomy in this respect. The raising of financial resources is also confined to the centre and is not effectively devolved at the lower regional levels. Districts get their allotments in different sectors based on some criteria which are not necessarily perfect and fully objective. Since districts have to depend substantially on the centre for their resources, the practice of decentralized planning remains partial. In terms of the powers to approve projects and programmes, the DEC can give technical approval and authorise implementation of projects normally less than about K.Sh. 5.00 million. For any bigger projects, the technical approval (sanction) is given by the respective ministry headquarter at the centre. Moreover, in the case of such big projects, the centre also monitors the project. To this extent, then, even the district-specific component of the plan is not fully decentralised in Kenya.

v) *Political Interference*: This remains a very critical issue in any country's efforts to decentralise planning. Kenya is no exception. Eventhough Kenya has a single party democracy, the political interference remains a major problem. It invariably arises out of the uncertainties of political nature making the politicians feel insecure. In a multiparty democracy system, the uncertainties are of two types: (a) the party remaining in power and (b) the politician remaining in power/position. On account of a single party system, the first type of uncertainty along with several other complications arising out of sheer ideological clashes are avoided in Kenya, but the second type of uncertainty still remains. The politicians, ministers and permanent secretaries - are not all that permanent! They may be transferred from one position to another or from one portfolio to another. They therefore, try to push the projects/programmes benefitting them and their constituencies. Many a times, then it becomes difficult to rationalise the budget. Purely objective criteria for allocation of budgets are also not accepted largely for such reasons. It is, however, felt that the Minister's district might get a higher allocation once or twice but cannot continue to get favoured treatment over time. In other words, political interferences may distort planning but not considerably. Even the government bureaucracy holds the inside view of having as much specification as possible with the help of objective criteria and weights and then leaving the final decision to the politicians. This way, there are less chances of serious distortions.

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<i>Table 1</i>					
Growth Rates of Real Gross Domestic Product (GDP) at Constant 1982 Prices in Kenya					
<i>(in %)</i>					
Year	Agriculture	Manufacture	Government Services	Others	Total GDP
1972	7.6	7.3	12.8	3.6	6.8
1973	4.4	14.4	6.3	1.0	4.1
1974	-0.2	5.9	6.8	4.0	3.1
1975	4.6	4.0	8.5	-0.01	3.1
1976	3.7	14.0	5.1	2.0	4.2
1977	9.5	16.0	5.1	6.1	8.2
1978	8.9	12.5	6.4	8.4	7.9
1979	-0.3	7.6	7.1	7.7	5.0
1980	0.9	5.2	5.6	5.2	3.9
1981	6.1	3.6	5.3	6.9	6.0
1982	11.2	2.2	3.8	1.4	4.8
1983	1.6	4.5	4.2	1.5	2.3
1984	-3.9	4.3	2.9	2.7	0.8
1985	3.7	4.5	4.2	1.5	4.8
1986	4.9	5.8	6.3	5.4	5.5
1987	3.8	5.7	5.7	4.9	4.8

<i>Table 2</i>					
Investment and Savings in Kenya, 1965-87					
Per cent of GNP (current prices)	1965-69	1970-74	1975-79	1980-84	1985-87
Gross Investment*	19.7	25.4	24.5	25.3	23.5
Foreign Saving	3.2	7.5	7.0	7.0	5.2
Gross National Saving	16.5	17.9	17.5	18.3	18.3

* Calculated as percentage of total investment to total GNP.

<i>Table 3</i>						
Outstanding Public Debt in Kenya for Selected Years, 1964-87						
	1964	1972	1974	1978	1982	1987
Government Budget Overall Deficit* (K£ Mn)	-9.2	49.80	57.30	141.30	298.50	387.60
Debt:(K£ Mn)						
Domestic	17.99	88.54	129.13	283.57	454.20	716.93
Foreign	68.12	105.76	136.34	242.26	859.31	280.65
Total	86.11	194.30	265.47	525.83	1313.60	2997.58
Debt Service Charges:(K£ Mn)						
Domestic	3.24	9.47	9.40	29.45	77.21	206.38
Foreign	1.97	7.23	8.64	31.17	102.58	257.38
Total	5.21	16.70	18.04	60.62	184.79	463.76
GNP (K£ Mn)	348.87	731.28	1016.04	2049.81	3363.88	6363.21
Exports of Goods and Services** (K£ Mn)	119.70	200.11	357.20	593.10	877.6	1400.44
Ratio of Service Charges on External Debt to Exports of Goods and Services(%)**	1.65	3.61	2.42	5.25	11.69	18.38
External Debt Ratio to GNP(%)	19.50	14.50	13.40	12.40	25.50	35.80
* Calendar year totals, derived by averaging two financial years						
** Excludes factor incomes.						

<i>Table 4</i>				
Percentage Increases in Nairobi Consumer Prices, 1984/83-1987/86				
Income Group	1984/83	1985/84	1986/85	1987/86
Lower Income Index	10.3	13.0	4.0	5.7
Middle Income Index	8.9	11.1	7.7	8.3
Upper Income Index	8.0	8.0	5.3	7.8
Average Increases	9.1	10.7	5.7	7.1

Persons Engaged, 1984-87 (Thousands)						
	1984	1985	1986	1987	% Change 1984/1987	
					Total	Per Annum
Wage Employees						
Modern Sector						
- Private	577.9	599.8	620.7	638.1	10.4	3.36
- Public	541.5	574.6	599.8	624.6	15.3	4.87
Self-employed	32.4	33.1	35.4	38.1	17.6	5.55
Small-scale Enterprises	133.3	254.5	281.0	312.1	134.1	32.79
Total	1285.1	1462.0	1536.9	1612.9	25.5	7.87

Changes in Wage Employment, Prices and Real Earnings in Kenya, 1984-87 (Percentages)				
	1984	1985	1986	1987
Wage Employment	2.4	4.9	3.9	3.5
Average Earnings (Current Prices)	9.5	9.3	8.8	7.1
Consumer Price Index*	9.1	10.7	5.7	7.1
Real Earnings	0.4	-1.3	2.9	0.0

* Percentage increases are derived from a composite index of lower, middle and upper income indices calculated as an average of the indices. See [Table 4](#).

Progress of Harambee Movement in Kenya, 1965-84			
Item	Unit	1965-69	1980-84
1) Proportion of Harambee contributions on	in %	64	86
a) Social Development Projects	in %	36	14
b) Economic Development Projects			
2) Average Percapita Cash Contributions	K.Sh.	6.42	8.46
3) Number of Completed Projects	No.	6,711	14,028
4) Ratio of Project Completion to Project Starts	in %	35.6	80.4
5) Annual Harambee Capital Formation	K£ Mn	1.2	21.9

Table 8								
Sectoral Targets in the Sixth Plan (1989-93) Kenya								
(in %)								
Sectors	Annual Growth in				IFCO R	Percentage Share In		
	Real GDP		Employment	Lab. Prod.		Total Fixed Inv.	Real GDP	Employment
	1983-88	1988-93	1988-93	1988-93		1989-93	1988	1988
1	2	3	4	5	6	7	8	9
I. Monetary Economy	4.2	5.5	4.10	1.34	-	90.75	94.78	15.98
1)Agriculture	2.5	4.5	2.39	2.06	0.92	8.54	27.45	2.82
2)Forestry	6.9	8.0	4.75	3.10	0.42	0.17	0.86	0.27
3)Fishing	7.4	7.0	4.56	2.33	0.67	0.12	0.42	neg.
4)Mining & Quarry	8.0	8.0	6.62	1.29	5.35	0.88	0.27	0.07
5)Manufacturing	5.2	6.4	3.56	2.74	1.80	13.28	13.11	2.11
6)Building & Construction	1.1	4.5	3.22	1.24	4.25	6.05	2.89	0.72
7)Electricity & Water	6.0	7.0	5.83	1.11	6.90	5.19	1.77	0.25
8)Trade, Restaurants & Hotels	7.2	7.0	5.42	1.50	0.70	4.62	11.63	1.29
9)Transport, Storage & Communication	3.4	5.7	3.32	2.30	6.00	16.39	6.11	0.73
10)Finance & Insurance	4.8	5.4	3.86	1.48	0.77	1.97	7.19	0.73
11)Ownership of Dwellings	1.0	3.4	-	-	8.32	7.88	3.42	-
12)Other Services	7.6	8.2	6.60	1.50	6.00	8.19	2.73	2.73
13)Domestic Services	8.2	8.4	5.55	2.70	-	-	1.50	0.83
14)Government Services	5.0	5.0	2.94	2.00	3.36	17.46	15.43	3.44
II. Traditional Economy	4.0	3.6	4.27	(-)0.67	-	9.25	5.22	84.02
Rural Employment	-	-	3.8	NA	-	-	-	78.21
Urban Informal Employment	-	-	10.6	NA	-	-	-	5.32
Self-employment & Unpaid Family Workers	-	-	8.3	NA	-	-	-	0.49
III. Total Economy	4.2	5.4	4.2	1.2	3.64	100.00	100.00	100.00

<i>Table 9</i>			
Resources for the Sixth Plan (1989-93), Kenya			
(in % of GDP at M.P.)			
	Actual	Proposed	
	1987	1989	1993
1) GDP at Factor cost	86.21	86.21	86.21
2) Net Indirect Taxes	13.79	13.79	13.79
3) GDP at Market Prices	100.00	100.00	100.00
4) Imports	26.22	25.59	23.94
5) Exports	21.17	22.16	21.53
6) Foreign Saving	5.05	3.43	2.41
7) Domestic Saving	19.92	19.77	21.00
a) Private Sector	21.48	22.77	20.70
b) Government Sector	(-)1.56	(-)3.00	0.30
(i) Current Revenue	24.66	22.90	24.00
(ii) Current Expenditure	26.22	25.90	23.70
8) Total Gross Investment	24.97	23.20	23.41
a) Fixed Investment	20.18	19.68	19.88
b) Change in Stocks	4.79	3.52	3.53
9) Total Consumption	80.08	80.23	79.00
a) Public Consumption	19.39	17.78	16.83
b) Private Consumption	60.69	62.45	62.17

Chapter 6

Urban Development Through Corporatism - The Case of Toronto Harbourfront

I. Introduction

Removal of regional disparity in the levels of economic development along with achieving a high rate of economic growth are important objectives of planning and policy making in almost all nations with large geographical area. In the current global environment, it is hardly possible to sustain rapid progress without integrating the economy with the world economy. Being competitive in the world market becomes continuing concern over time. Technological sophistication, economies of scale & scope and, efficiency of man & machine hold the key. Since these are usually the features of the urban production system, it is not surprising that urban area development has started attracting the attention of policy makers in progressive economies. Although equitable regional distribution of the gains are crucial for large sized countries, it can no longer be left only to the central government. State or provincial governments on one hand and local self-governments like municipalities on the other hand need to be simultaneously pro-active. This is the essence of the approach of decentralized planning/policy efforts to tackle the regional problem. If the development initiatives are taken by the local communities themselves, people's participation and involvement all along the development projects not only in terms of moral support and backing, but also funding can be ensured. The possibility of political reality distorting people's participation in the decision making process at the local level is more in the educationally backward rural areas of the less developed countries than in the urban areas. Unfortunately, the discussion of decentralized planning or policy making has so much centred around rural areas that the urban dimension of the problem is virtually ignored. This gets reflected even in the constitutional, legal and institutional framework in most of the countries where formal coordination across various departments and among different levels of government hardly exists. Under such circumstances, local community's effective participation in decision making may go a long way in ensuring success of the development efforts. On the other hand, if the project is perceived to be an exclusive initiative of the senior level of government, irrespective of the quality of the effort, it may not succeed.

In most countries, constitutionally, urban development is considered a state or province subject, though Ministry of Urban Affairs may exist at central government level. Since they usually do not exercise any control over the plans and programmes of the other regular line departments, they by and large fail to coordinate urban development policy in different parts of the country. The result is lack of focus in national urban development policy if it exists! In Canada, the Ministry of State for Urban Affairs (MSUA) was created in the Federal Government in the 1970's. However, it could not serve any purpose and had to be wound up in the late 1970's. Artibise & Kieman (1988) find that in Canada, like most other countries, the efforts for urban economic development are without the conceptual and policy frameworks. Initiatives for urban economic development are not systematically taken either by the senior levels of (federal and provincial) governments or by the local (municipal) governments. The latter are constrained by limited financial resources and inadequate or non-existent legal powers. Moreover, they have non-interventionist philosophy making their activity in the field of economic development minimal and tentative. Hardly 0.33% of the total municipal spending in Canada are devoted to the economic development of the urban area. Of late, however, there is some evidence of a new, urban-based programmatic approach to regional development taking shape in Canada, which they have studied considering seven short cases including Toronto Harbourfront. [See Artibise & Kieman, 1988].

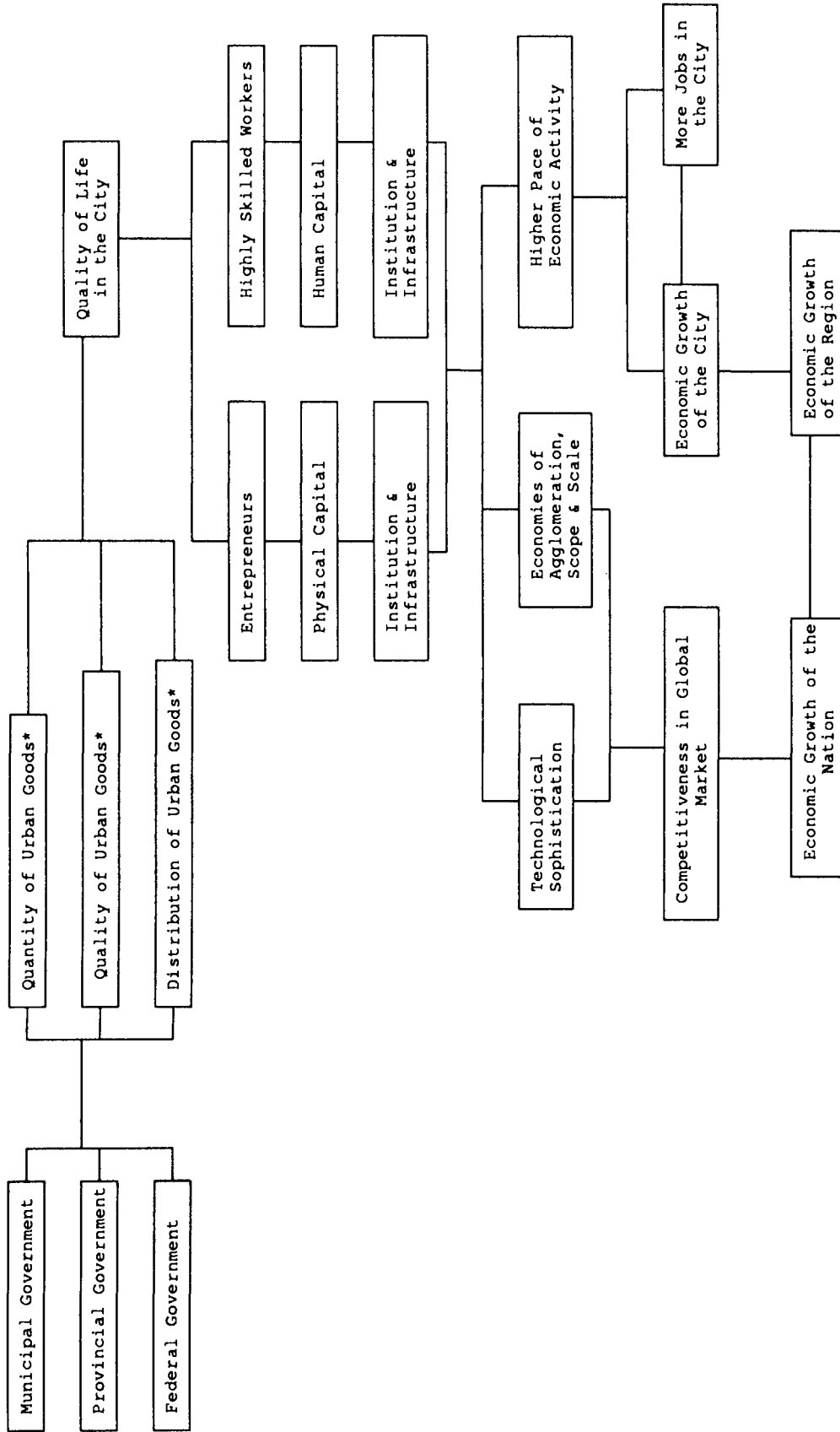
The phenomenon of urbanization in Canada has interesting history. During the Seventies, for the first time in Canada, rural areas recorded a faster rate of growth than the urban areas. The new era was labelled "post-urbanization" and "counter-urbanization". However, it did not last long. The 1986 Census proved that the urbanization in Canada preceded with the growth more centred in the metropolitan centres. The percentage of Canadian population living in major urban centres increased from 56 in 1976 to 61 in 1986. Moreover, unlike the period 1976-81 when the middle-sized urban centres grew at considerably higher rate (14.8%) than the large centres (5.9%), during 1981-86, the trend reversed with the large centres growing at 10% as compared to a meagre 3.6% for the middle-sized centres. Serious efforts for the urban revival and revitalization started taking place during the last seventies and early eighties in Canada. These efforts were the result of the growing conviction or belief in the critical role of cities and towns in the process of regional and national economic growth as comes out in the model as outlined in Chart 1 [Some of the basic ideas of the model are contained in Artibise & Kieman, 1988].

"Toronto is found to be the most livable city in North America" says Toronto Star (9th June 1990) based on a 20-factor livability index. The factors considered in the study included income, housing, homeless population, crimes, jobs, education, commuting facilities, transit fare, transit crimes, transit time, hospitals, stress, suicides, entertainment facilities and cost, cleanliness, environment, etc. Toronto is also the biggest metropolitan area in terms of population in Canada. The trend in Toronto's population is very similar to the Canada's large urban centres taken together. In order to gain further insights into the role of urban economic development initiatives, it is proposed to consider the experience of Toronto in further detail. Moreover, with a view to focussing on the policy initiatives to revitalize the inner-city, the case of Toronto Harbourfront Corporation is discussed in the present paper. In the next section, brief history of the Toronto Harbourfront is presented after reviewing the trends in the Toronto Inner City over the period 1951-86. The third section outlines the main features of the Toronto Harbourfront including its objectives, set-up, finance and activities. The fourth section is devoted to the discussion of the development during eighties including the most recent status of the Corporation (HC). The sixth and the final section examines major issues arising out of the Harbourfront experience.

II. Toronto Harbourfront Corporation - Background

The inner city of Toronto has been passing through a period of mild transition in recent years. Certain long-term historical trends have either slowed down or reversed. There are substantial differences between the inner city and the rest of the metropolitan area of Toronto. Table 1 presents a comparison between the two in respect of several features over the period 1951 to 1986. The inner city is inhabited more by young adults and senior citizens who are not married as compared to the outlying areas of Toronto. Moreover, there are fewer families with school-going children living in the inner city than the rest of the city. Percentage of people living alone is substantially high in the inner city than the outlying areas of Toronto. All these facts result in salient differences in the life-style between the two areas. The inner-city of Toronto also has a larger proportion of persons with high levels of education and of employees in managerial and professional occupations.

Chart 1 : The Model



* Also called "soft infrastructure" and would include health, safety, culture, education, recreation, entertainment, housing, transport, etc.

**Table 1
A Comparison of Inner City and Metropolitan Area of Toronto**

Item	Units	1951	1961	1971	1981	1986
1. Inner City Population	(In '000)	143.5	127.1	124.8	114.7	128.2
2. As Proportion of Total Metropolitan Area	(In %)	12.8	7.0	4.7	3.8	3.7
3. Proportion of Private Households with persons living alone :						
(a) Inner City	(In %)	9.8	22.5	34.7	51.4	48.9
(b) Remainder	(In %)	4.2	7.3	12.2	20.0	19.9
4. Proportion of Lone-Parent Families in All Families :						
(a) Inner City	(In %)	NA	NA	16.7	21.0	22.7
(b) Remainder	(In %)	NA	NA	8.9	11.5	12.4
5. Proportion of Immigrant Population						
(a) Inner City	(In %)	NA	40.3	41.0	40.9	39.1
(b) Remainder	(In %)	NA	32.7	33.6	37.9	36.3
6. Concentration of Ethnic Groups Other than British or French in Inner City Relative to Total Metropolitan Area	(Index*)	NA	122	111	102	102
7. Proportion of Population (15+) with University Education :						
(a) Inner City	(In %)	NA	NA	24.2	37.3	42.0
(b) Remainder	(In %)	NA	NA	13.2	20.4	23.3
8. Median Family Incomes in Constant 1985 Dollars :						
(a) Inner City	(In Can. \$)	NA	NA	22,689	NA	30,622
(b) Remainder	(In Can. \$)	NA	NA	32,624	NA	41,723
9. Proportion of Families in Selected Income Groups (at constant 1985 \$) :						
I. Less than \$ 20,000 :						
(a) Inner City	(In %)	NA	NA	43.3	NA	33.0
(b) Remainder	(In %)	NA	NA	19.9	NA	16.7
II. \$ 60,00 or More :						
(a) Inner City	(In %)	NA	NA	8.6	NA	22.0
(b) Remainder	(In %)	NA	NA	10.3	NA	22.7

Source : Statistics Canada : Inner City in Transition, Cat. # 98-123, December 1989.

* Index = (Proportion of ethnic groups in Inner City divided by Proportion of the Ethnic Group in Metropolitan Area) x 100.

NA = Not Available

Considering the historical trends over the period 1951 to 1986, we find that the declining trend in the population of the inner city of Toronto is reversed for the first time during 1981-86, though in percentage terms, the declining trend still continues. Similarly, the increasing trend of persons living alone is arrested during 1981-86 for the first time in both the inner and the outer city of Toronto. However, the increasing trend continues in the case of the lone-parent families. In terms of median income of family, the gap between the inner city and the outer city of Toronto is widening in absolute terms but declining in relative terms. The median family income of the inner city was only 69.5% of the one in outer city in 1970 whereas it was 73.4% in 1985. The income distribution has also changed over the same period in the same direction in both the inner and outer parts of Toronto. Proportion of families in lower income group declined and the one in the upper income group substantially increased over the period 1970-85. All these trends clearly indicate that the inner city of Toronto has been witnessing some powerful dynamic forces of economic and social development. Whether these forces are autonomous or induced can be judged only by looking into the history of the city.¹

Compared to other regions, the Toronto region attracted considerable growth of economic activity and hence population after the Second World War. The city started spreading outward converting farmlands into housing estates, schools, industrial parks. Shopping centres naturally followed providing further incentive to the population transfer. The central place started losing the business to the suburbs. This led to the declining importance of the inner city in both industry and trade and hence of the associated rail and water transportation. All these developments politically posed a threat to the traditional dominance of the city of Toronto in the metropolitan region. The city politicians, therefore, adopted a new plan for the city in 1969. It aimed at promoting more commercial and residential development in the central city. The residential development envisaged in the inner city was not for the poor but for the middle and upper-middle class contributing highly skilled manpower. Such a strategy resulted in proliferation of high-rise apartments into low-density neighbourhoods and threatened quality of life of the middle class neighbourhoods. The 1973 elections, therefore, witnessed a voter revolt and the pro-development city aldermen gave way to the reform-minded group.

The change of power in the city council meant substantial reorientation of policies in the light of changed objectives. The focus in the 1969 plan was on expanding employment in the Central Area with separating of residential areas whereas the new Council aimed at limiting growth in the Central Area and diversifying its land use. The new plan for the Central Area was adopted in 1978. The plan allowed some room for new commercial, institutional and residential activity by intensifying land-use in the Central Area, but a large part of the development was to be redirected to the regional sub-centres in order to protect the residential neighbourhoods surrounding the Central Area and the adjoining industrial areas from the commercial and institutional expansion. The 1978 plan, thus, had a bias against the redevelopment and intensification of the neighbourhoods surrounding the central area.

On the other hand, the economic structure of the Toronto region has been undergoing significant changes. The Central Area of Toronto emerged as a centre for high order information-based services which accounted for almost two-thirds of the labour force of the Toronto Metropolitan Area in 1981. There has been a massive relocation of the corporate headquarters to the central city area. By 1987, 39% of the top 500 Canadian companies and more than 50% of the largest financial institutions had their headquarters in this area.² The occupational structure in Toronto has also been rapidly shifting in favour of clerical, managerial, scientific, technical and service categories. These relatively affluent white-collar workers prefer a downtown residential location. Because of the 1978 plan, a large part

¹ The history of the City and HC is drawn from Desfor, et. al. (1988 and 1989) and Artibise & Kiernan (1988).

² In terms of non-American multinationals, Toronto is the fifth most important headquarters city in the world. [Toronto Star, September 9, 1986].

of the demand for such housing had to be met along the waterfront. The developers, therefore, saw a golden opportunity to build there for the high income housing market. However, most of the land along the central waterfront was controlled by federal government institutions like Toronto Harbour Commission (THC), national railways and Harbourfront Corporation. These institutions were subject to tremendous pressure from the market forces. On account of the mandate given to these institutions and hence their perceived organizational goals, some of these institutions had to yield to the market forces resulting in the residential and commercial developments along the central waterfront.³ High-rise residential towers and hotels created a conspicuous wall along the core of the central waterfront depriving the city of the view of the waterfront. The HC was created in October 1972 by the Federal Government of Canada in order to protect the waterfront from commercial exploitation.

During the federal election campaign in 1972, it was announced that the federal government would acquire 100 acres of prime central waterfront land on Lake Ontario and develop it as a park to provide recreation to all Torontonians. Initially at least such a concept proved popular with the Torontonians. Over the first 3 years, a lot of planning and consultative activity was undertaken with the Ministry of State for Urban Affairs (MSUA) taking the initiative. However, little actual development occurred. As Artibise and Kiernan (1988) argue, there were three basic reasons for this : "the impossibility of forging a consensus even within MSUA on how the lands ought to be developed; the sheer physical difficulty of actually acquiring and demolishing some of the obsolete industrial structures which stood on the site; and, most importantly, the virtual exclusion of the City of Toronto from the consultative process."

In 1975, MSUA set up an informal 'Harbourfront Council' whose nominees were representative officials from all the three levels of government and appointees of the Mayor and Metro Chairman of Toronto. In spite of this effort, intergovernmental issues reflecting the strained relations between politicians and planners did not allow any consensus to emerge on the objectives of the development. As a result of such a long patch of antipathy and inactivity, it was decided to transform the Harbourfront into a Crown Corporation to enable it to operate more effectively as a developer. Moreover, in 1978, the corporate board of HC appointed Howard Cohen as general manager. Mr. Cohen was the *de facto* chief planner for the city of Toronto prior to joining HC as a manager. Mr. Cohen was able to resolve some planning issues between the city of Toronto and HC and hence gave firmer direction for the latter's overall plan. The 1978 plan of the HC had three fundamental objectives : (a) to activate the inner city waterfront area by providing traffic generating cultural activities and other recreational facilities; (b) to activate the economy of the area through residential and commercial development; and (c) to generate sufficient development revenue for it to become self-financing within 7 years. Before we examine more recent experience, it would be interesting to review some important features of the HC.

III. Features of Harbourfront Corporation⁴

The Harbourfront Corporation (HC) is a Crown Corporation whose share capital is held by Her Majesty the Queen in Right of Canada (in short "Canada") as represented by the Minister of Public Works. The Corporation is exempt from the corporate income-tax. The site under the control of HC totals approximately 100 acres and occupies a central position on the Toronto waterfront. The HC is under a Management Agreement with Canada dated June 13, 1980 as amended and renewed from time to time but is expiring on March 31, 1991. As per this agreement, HC has a dual role and mandate:

- (a) To develop, manage and operate the Harbourfront site in accordance with a development framework approved by Canada' and

³ THC accumulated huge debt which led it to revise its development strategy in favour of commercial and residential development by mid-sixties.

⁴ Major source of material presented in this section is the series of the Annual Reports of HC.

- (b) To initiate, conduct or sponsor cultural, recreational, scientific and educational programmes which, in its view, are of advantage to the public.

HC was created politically to build a constituency of people on waterfront and hence there should be benefits on the real estate front. In terms of its role in economic development, the HC was expected to encourage private investment along with the public activities. It was envisaged that the private investments and activities would pay for the public activities. This was in line with the Rightist political swing of 1981. Thus, the HC is supposed to pursue 'public' objectives which necessitates a certain level of government control. On the other hand, however, it is expected to manage its activities so efficiently as to enable it to be self-financing which requires a lot of flexibility and freedom in its operating style. Such an internally contradicting mandate is an important feature of HC.

Another feature of HC is that the title to the lands of the Harbourfront site is held by Canada with the exception of park land and public infrastructure conveyed to municipal governments and certain lands transferred to the Corporation by Canada. Thus, the corporation can sell only air rights or give on lease the lands on the site on behalf of Canada. The net proceeds generated by the Corporation from the development of the Harbourfront site as well as capital contributions from Canada are credited to contributed capital to recognize Canada's contribution to the capital funding of HC. All the funds derived from the capitalized leasing, sale or resale of lands or development rights are available to the HC in fulfilling its mandate. These funds, when received from developers are placed on deposit with Canada in the Harbourfront Capital Account which is an interest bearing account of the Consolidated Revenue Fund. The HC can withdraw the principal only with the approval of Canada. Similarly, the interest can be distributed to HC on request. Annexure 1 below provides the consolidated financial statements of the Harbourfront Corporation for last few years.

It can be observed that about four-fifths of the current expenditure of HC is in the programming activities and only one-fifth is in real estate. Since HC is a huge production company with about 450 multi-cultural and special events communities involved, its range of programming activities is very wide and diverse. It is a highly labour intensive company. Annually around 4,000 different events, activities and performances take place in HC. Out of these, about 85% of the programmes are free for the public in the sense that there are no admission fees. Such programmes are underwritten by the HC. The box-office, therefore, does not contribute substantially to the revenues of HC though parking charges do (about 15% of expenditure)! Sponsorship for the shows from big private sector companies also earn about 13% of the total operating expenditure. The major source of revenue has all along been the real estate (rental of building, lease, etc.) which accounts for almost 40% of the expenditure.

Lands are all leased and not sold. The lease is for 60 years to 99 year period. There are, however, some retail deals also where the rent differs from case to case. Usually, the rent in such cases is consisting of two components: (a) the base rent and (b) 6 to 8% of gross sales. The base rent increases with time to provide effective hedge against inflation. Since land cannot be sold by HC, the ground-floor all along Harbourfront has to be public land. The real estate developer, therefore, has to retain the ground-floor. It is possible, however, to sell the building but not the land. Condominium⁵ laws with their loop-holes in Canada permit to sale outright the residence although on the leased land. The HC and developers have limited partnership in the proportion of 55% to 45%. The rentals are shared between the HC and the private developers as per their agreements.

The organization of the Harbourfront Corporation is summarized in Chart 2. There are in all six directors each looking after several divisions as indicated in the chart. These six directors report to the General Manager who is, in turn, answerable to the Board of Directors. The Board of Director is appointed by the Prime Minister's Office. Functionally, they report to the Minister of Public Works at Ottawa. There is no political representation on the Board. Similarly, the Province is not represented

⁵ Condominium is the getting together of individual leasers or buyers. It is a concept very similar to cooperatives.

on the Board. Conventionally 2 out of 18 Board members represent the local interest, one of whom is a nominee of the Mayor of the City of Toronto. In this connection, it is interesting to note that HC receives sponsorship support from funding agencies at all the three levels of government viz., federal, provincial and municipal.

IV. Development During the Eighties

The main thrust of the 1978 plan of the HC was to achieve financial self-sufficiency in due course. The fulfilment of other objectives of the Plan about the cultural activities and real estate development activities was involving enormous expenditure. Clearing the site of the industrial buildings and providing necessary infrastructure supporting the cultural activities and real estate development were very costly propositions. HC as an organization was, therefore, faced with the situation where it might have to depend on regular subsidies from the Government of Canada to cover both the capital and operating expenses. Under such circumstances, the HC staff feared that the required support from government might not come forth and hence decided to adopt the strategy of financial self-sufficiency. This strategy had to revolve around use of the basic asset of the Corporation viz., land. The real estate development at a fast pace was, therefore, considered the most optimal means to achieve the objectives. Considering the costs involved, the real estate development had to take the form of high-density residential schemes, luxurious housing projects and expensive commercial and retail space in order to generate the required level of revenue. To promote efficiency through competition among private developers and obtain the best bargain, system of 'proposal-call' was followed. Only the right to build on the public land was sold to the private developers. The pace of the development was dictated by the revenue need of the HC and the external environment.

In 1981-82, there was a world-wide recession and the real estate was down. It hit HC hard and nothing got started. In spite of these two bad years, the originally agreed time-period of 7 years from 1980-87 for attaining self-sufficiency in finance was not revised. Therefore, the period for the real development was confined to 1983-87 when the pace of development was too fast to escape the attention of public, the city politicians and the critics of the HC. As a result, since 1987, no significant real estate development could take place because the HC was facing moratoriums and development-freezes on account of several reviews and reassessments at various levels.⁶ The cultural programming activities, however, continued almost without any interruptions. A year-wise brief history of development and public programming at HC is presented in Annexure 2.

The issue of the autonomy of the Corporation is a critical one in this context. HC is accountable to the Federal Government and not to the City or Province. Jurisdictionally, the HC is not obliged to listen to the city and the Provincial governments.⁷ However, the normal approval procedures of the City became an effective tool of control for the City over the HC. Thus, HC was not autonomous from the local governments for practical purposes. The stories of disputes between the HC and the City officials were spreading and when they became well-known by 1987, the City councillors and their constituencies became more vociferous. The official plan and the zoning by-laws⁸ of the City of Toronto were binding on HC, though negotiation in this regard was possible. As a result of this, HC had to build 20 acres of park and public land to be turned over to the city. The infrastructure on this land also had to be built and improved by HC but the maintenance responsibility was with the city.

⁶ It is interesting to note that during this time, the Toronto down-town area experienced a massive real estate development generating considerable expansion of office-space approved by the City.

⁷ Toronto is governed by two-tiers of governments: area-wide government known as Metropolitan Toronto and six municipalities one of which is the City of Toronto. Planning functions are carried out at both levels of government.

⁸ Zoning by-laws provide zoning standards for lot size, unit size, set-backs, plot coverage, parking requirements, density, height, etc.

The actual point of control by the city comes at the time of issuing the building permit to the developers. As per the planning process, the Harbourfront area has five sub-areas, each having its sub-area plan showing the intent. The normal development review process in the city ends up with the agreement between the city, the HC and the builders/developers. As per the Provincial Planning Act, the city cannot frustrate the HC plan by not issuing the building permit. However, if the city refuses the permit, the HC has a right to appeal to the court or to the Ontario Municipal Board at the provincial level provided it conforms to the zoning by-laws of the city. Unfortunately, this process of appeal had to be undergone most of the time in the case of HC.

The main elements of the city's grievances against HC were [See, Artibise & Kiernan, 1988] : (a) The Corporation's initial commitment to the park space on waterfront was not being fulfilled by the plan proposed and executed by the HC. (b) The site was being severely overbuilt by HC to generate the required revenue out of the real estate development. (c) The waterfront view was being effectively denied to the Torontonians by the HC's Plan of building a row of high-rise structures creating almost a ceramic wall along the waterfront. (d) The nature of the real estate development taking place on the HC lands was basically resented by those who could not afford it. The commercial space was extremely expensive. The housing projects were also largely meant for the upper-middle class. The concept of affordable housing⁹ did not receive much attention. Some critics argued that such megaprojects are like vacuum cleaners sucking more from the economy than giving. They internalize all external economies of scale and scope and externalize all possible costs. The feeling among the Torontonians was that HC has benefitted the owner companies at the cost of the society and the residents of the city. Sheer size of the projects provides opportunity for political and economic leverage. When we considered all these together, the megaproject of HC, as argued by Artibise and Kiernan (1988), was becoming an antithesis of what it was originally intended to be. This led to a rapid fall of the HC in the eyes of the public.

Finally, from January 1, 1991 the HC is reorganized as non-profit making new legal entity though the name is retained. The real concern was to continue the cultural and artistic programming in spite of its being costly. Recently, there is a drive for privatization all over the North America. The solution to the problem of HC was, therefore, thought to be to split the activities of HC into two : (a) cultural and recreational activities and (b) real estate development activities; and sell outright the assets of the latter to continue with the park and recreation. Thus, the real estate side of HC which was the major revenue generating activity is to be divested by selling it off. The buyer who would buy out all the leased interest and land, would also have the future development rights as per the city by-laws. Out of the 100 acres of land, about 50 acres are meant for parks and roads and 20 acres for private ownership for residence. The total value of the assets to be sold works out to approximately \$ 80 million. The sale will be completed in 3 to 5 years. An endowment would be created notionally right away and would be repaid in 3 to 5 years. Interest at the rate of 11% p.a. is assumed. On the basis of rational projection of cash flows, it is expected that the annual deficit of \$ 10.7 million would have to be financed out of the annual expenses of \$ 18.5 million on recreational programming and maintenance of park and roads. As a result of such a reorganization, 45 employees out of a total of 210 have already been laid off saving annually \$ 2.2 million in salaries and remuneration.

In order to overcome the mistrust from the city and the province, the new Board of Directors for the non-profit organization-HC would consist of 26 persons. 8 to 10 of these 26, would be from the existing Board prior to 1991. There would be a maximum of 6 representatives from different government levels. The balance of 10 to 12 members would be drawn from local people with roots in the communities like artists, businessmen, ethnic groups, etc. These are all political appointments

⁹ 'Affordable Housing' means housing which would have a market price or rent that would be affordable to households of low and moderate income which are defined as the ones within the lowest 60% of the income distribution for the housing region. Similarly, 'Affordable' means annual housing costs not exceeding 30% of gross annual household income. 'Housing Costs' are either gross rents or mortgage principal or interest amortized over 25 years, assuming a 25% down payment and taxes.

wherein half would be from the city and 25% each of the province and the Federal governments. All this restructuring and reorganization is expected to take 2 to 3 years.

V. Achievements of Harbourfront Corporation

Harbourfront has become one of the most popular attractions in Ontario. More than 3.5 million people out of whom about 80% live in the Toronto area visit the site every year. A person, on an average, visits the site 5 times a year. Thus the repeat clientele is also created. The park and recreational programmes at the Harbourfront have been largely successful in generating traffic in the downtown area and hence giving a boost to the economy of the inner city through consumption of goods and services. The most significant achievement of the HC is in terms of stimulating investment in the inner city area of Toronto. By the end of 1987, HC's investment in obtaining land and creating public infrastructural facilities was of the order of \$ 55 million and \$ 80 million respectively. This investment on the part of HC stimulated \$ 300 million investment on the site by the private sector in new housing, office and retail development by 1987. By now, the cumulative private investment on the site is nearing \$ 700 million mark. Considering the stimulant ratio of public investment to private investment of around 4 on other waterfronts in the world, the HC's performance on this count has been commendable. Thus, the HC proved very successful with both the city consumers and investors. It is only the popularity due to sheer performance that has enabled it to survive all along the period of political conflicts. In fact, HC received 3 times the "Excellence on Waterfront Award" so far, the last one being in September 1989 from the Waterfront Council in Washington DC.

It is worth noting at this stage that behind such a superlative performance of the HC were efficient management and hard work and commitment of the staff. The performance would have seriously suffered had there not been a strong marketing of the real estate development. After the world-wide slump of 1981-82, it was a difficult proposition to induce private developers. On the other hand, institutionally, they had a two-tier proposal call system which is appropriate when the real estate is hot. The two tier system was :

Stage I: Only broad proposals are invited from developers to short-list them on the basis of their background, past experience and ability to undertake the task.

Stage II: More detailed proposals mentioning the team, details of the plan, cost, etc. are invited from the shortlisted developers to make a final selection.

When the real estate was cold, the procedure was promptly changed because nobody came forward. Brokers were at once removed and research was sponsored by the HC. The socio-economic-demographic conditions of the downtown population were studied in 1982. This survey about the people, their income, consumption pattern, family size, labour force characteristics, etc. was used to derive plan and programmes which would work. The developers were taken into confidence by sharing the results of the survey and the research. Thus, HC's strategy was to look for private investors to produce the product with all specifications based on the research. In other words, the pre-sale functions were largely carried out by the HC which would reduce the cost and the risks of the private producers. Private developers were, then, hunted for undertaking the specific product. HC retained a fair degree of control because it also took up the monitoring function. In 1983, 539 units were sold only in 5 days - a sales performance worthy of praise considering the environment. Responsible for such a sharp turning around of the attitude of the developers was the management response in terms of marketing efforts and research undertaken by the HC rather than overall economic environment.

VI. Issues Arising from Harbourfront Experience

Major urban development projects like the HC take a long time to yield returns in terms of economic, social and cultural development of the city. It takes nothing less than 8 to 10 years. Once it creates

an impact, the physical conditions of living in the city rapidly changes. The soft infrastructure provided by such mega-projects starts attracting human capital in terms of highly skilled personnel to come, settle and give the boost to the business and the economy of the city. The experience of HC, however, raised several issues of critical importance in the success of such a strategy of urban and regional development [See, Artibise & Kiernan, 1988].

The Harbourfront Corporation was established in Toronto as an uncalled for intervention by the Federal government largely to serve political ends. The City was not even taken into confidence. The question of the city of Toronto proposing or demanding establishment of such a Corporation for its development simply did not arise. On the contrary, the announcement of HC was made in the context of wooing the voters by promising them park, open space and community activities which aroused very high and perhaps wrong expectations among the Torontonians. The issue of political overtones confusing the perception of the serious developmental effort is too important to be ignored. Had it not been allowed to raise wrong expectations from HC, the reaction of the city would have been less sharp and perhaps a lot of time wasted in the type of behind-the-scene guerilla wars between the city and the HC could have been saved and the bitterness averted.

Secondly, the issue regarding the full trust, understanding and cooperation among different levels of governments in such major developmental effort is critical for the ultimate success of the project. The senior levels of governments need not wait for the need of a major intervention to be felt by the city, but the city has to be taken into confidence. Ultimately, the local government is the government closest to the people and hence, they are directly answerable to the people in the city. The city politicians have to suffer if such projects fail to fulfill the expectations aroused. If, therefore, they are not taken into confidence, the project may have to face strong opposition from all sides including the media. This may lead to the loss of sympathy from the senior governments for such Corporations leading to further problems and crises for the management of the Corporations. It was felt by the HC management that proper representation of the city on its Board of Directors would have gone a long way to avoid the stalemate to resolve several issues between the city and the HC. The city with all its urban planning machinery should have been an active partner from the very beginning of the project.

Thirdly, the issue of a clear mandate with internal consistency is important for the long term performance of the project. When the strategy is to develop urban areas by creating public corporations, their institutional objectives, priorities and goals should be clearly defined. Moreover, there should not be internal contradictions among the objectives as far as possible. In the case of HC, the mandate given to it was internally contradicting. The goal of financial self-sufficiency was clearly not compatible with that of providing public parks, cultural amenities and activities and housing for all income ranges. This, created unnecessary tension and confusion for the management of HC which ultimately decided to interpret the mandate and the priorities as per their perception rather than the city's perception. The basic conflict and displeasure between the city and the HC arose out of such internally inconsistent mandate given to it.

Fourthly, the issue of privatization of such Corporation raises concerns about the ultimate aim and objective of creating such Corporations in first place. It is clear that "public control of land-base is absolutely indispensable to successful implementation of new urban mega-projects. By controlling the critical land resource, the Corporation can virtually dictate the timing, nature, quality and profitability of development". [Artibise & Kiernan, 1988]. To sell off these real estates to the private developers with the right for future developments on the site may amount to losing control over the critical land resource.

Finally, the issue of flexibility not only in day-to-day operations but in matters pertaining to long term planning and strategy formulation is also very significant for determining the performance of the project. The corporate structure of the intervention is perhaps best suited here as revealed by the experience of HC. Suitable management response to the changing environment can come forth most

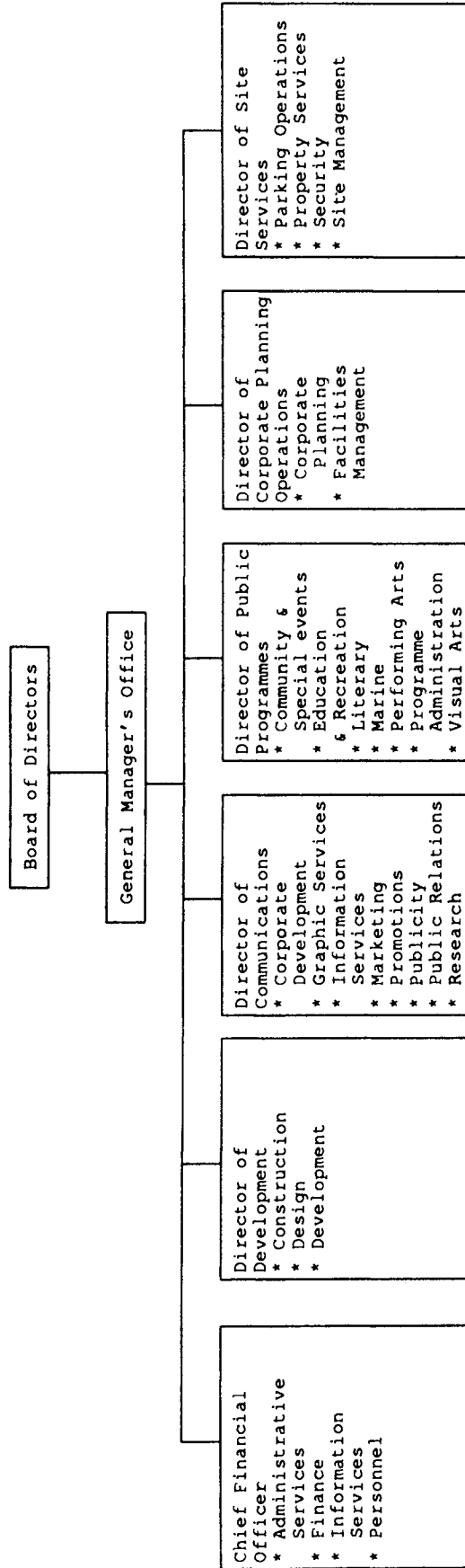
efficiently under the corporate structure. It also has the flexibility of incorporating representatives of different interest groups in their decision making process to ensure its ultimate success.

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Chart 2

Harbourfront Corporation Organization



Annexure I

Financial Statements of Harbourfront Corporation

Statement 1 : Consolidated Balance Sheet (\$ Million)				
	1990	1989	1988	1987
I. Assets				
A. Current Assets				
1. Cash and Term Deposits	5.010	1.880	2.794	2.534
2. Receivable from Canada	4.165	5.918	9.223	0.357
3. Receivable from Developers	0.929	4.999	9.797	12.254
4. Other Receivables and Assets	1.974	1.390	1.713	1.822
Sub-total	12.078	14.186	23.527	16.966
B. Non-Current Assets				
1. Receivable from Canada	---	1.839	0.732	6.973
2. Receivable from Developers	12.405	12.446	12.165	21.467
3. Prepaid Leases	0.290	0.435	0.580	---
4. Deferred Development Costs	5.082	4.448	4.141	6.229
5. Fixed Assets	1.197	1.608	1.266	1.044
Sub-Total	18.974	20.776	18.883	35.714
Grand Total	31.052	34.962	42.410	52.680
II. Liabilities & Shareholders' Equity				
C. Current Liabilities				
1. Accounts Payable & Accrued Liabilities	3.178	3.144	2.958	1.563
2. Deferred Revenues	2.653	0.886	0.772	1.488
Sub-total	5.830	4.030	3.730	3.051
D. Shareholders' Equity				
1. Share Capital	---	---	---	---
2. Contributed Capital (surplus)	31.935	32.494	34.441	41.605
3. Retained earnings	(-)6.7	(-)1.5	4.239	8.024
Sub-total	14	62	38.680	49.629
	25.221	30.932		
Grand total	31.052	34.962	42.410	52.680
Source : Harbourfront Corporation : Annual Reports				

Statement 2 : Consolidated Statement of Operations (\$ Million)				
	1990	1989	1988	1987
I. Public Programming and Facilities				
A. Revenues				
1. Event Admissions	2.106	2.005	1.689	1.348
2. Corporate Sponsorship	2.620	1.649	1.084	1.077
3. Government Grants	1.014	0.960	0.835	0.754
4. Parking & Other Income	4.602	3.726	3.218	2.662
5. Facility Rentals	0.769	0.830	0.870	0.650
Sub-total	11.111	9.170	7.696	6.490
B. Expenses				
1. Event Production	6.279	5.654	4.669	3.855
2. Event Administration	1.301	1.160	1.046	0.898
3. Marketing	2.798	2.647	2.337	1.527
4. Operation of Facilities	6.685	6.808	5.108	4.653
Sub-total	17.063	16.270	13.159	10.934
Net Income on Public Programming & Facilities	(-)5.952	(-)7.100	(-)5.463	(-)4.443
II. Commercial and Corporate Activities				
A. Revenues				
1. Commercial Income	2.631	2.295	2.520	2.172
2. Interest from Developers	1.094	1.290	0.868	1.272
3. Interest on HC Capital Account	0.439	0.918	0.643	0.534
Sub-total	4.164	4.503	4.031	3.978
B. Expenses				
1. Commercial Management	2.210	1.506	1.030	1.074
2. Corporate Administration	1.154	1.248	1.323	0.815
Sub-total	3.364	2.754	2.353	1.890
Net Income on Commercial and Corporate Activities	0.800	1.749	1.678	2.088
III. Net Income of HC	(-)5.152	(-)5.351	(-)3.785	2.355
Source : Same as Statement 1.				

Statement 3 : Consolidated Statement of Contributed Capital and Deficit (\$ Million)				
	1990	1989	1988	1987
I. Consolidated Capital				
1. Balance, beginning of year	32.494	34.441	41.605	45.270
2. Net Proceeds on Development Activities	(-)0.732	(-)0.062	0.376	0.450
3. Cost of Parklands and Public Infrastructure Conveyed to Municipal Governments	---	(-)0.206	(-)3.475	---
4. Period development and other public infrastructure costs	(-)3.476	(-)1.803	(-)4.065	(-)4.115
5. Capital Parliamentary appropriation from Canada	3.649	---	---	---
Balance at end of year	31.935	32.494	34.441	41.605
II. Deficit				
1. Retained earnings at beginning of the year	(-)1.562	3.789	8.024	10.379
2. Net Profit for the Year	(-)5.152	(-)5.351	(-)3.785	(-)2.355
Balance at end of year	(-)6.714	(-)1.562	4.239	8.024
Source : Same as Statement 1.				

Statement 4 : Consolidated Statement of Changes in Financial Position (\$ Million)				
	1990	1989	1988	1987
I. Operating				
1. Net Profit for the year	(-)5.152	(-)5.351	(-)3.785	(-)2.355
2. Depreciation	0.497	0.497	0.287	0.156
3. Profit on disposal of fixed assets	(-)0.001	(-)0.031	--	--
Sub-total (1 to 3)	(-)4.656	(-)4.885	(-)3.498	(-)2.199
4. Other receivables and assets	(-)0.584	0.324	0.109	(-)0.435
5. Prepaid leases	0.145	0.145	(-)0.580	--
6. Accounts payable and accrued liabilities	0.034	0.186	1.395	(-)0.644
7. Deferred Revenues	1.767	0.114	(-)0.716	(-)0.028
8. Interest receivable on HC Capital Account	0.751	(-)0.595	0.034	(-)0.012
Sub-total	(-)2.545	(-)4.712	(-)3.256	(-)3.318
II. Investing				
1. Investment in Fixed Assets	(-)0.316	(-)0.967	(-)1.353	(-)2.921
2. HC Capital Account :				
(a) Deposits	(-)4.412	(-)4.107	(-)11.059	(-)8.000
(b) Withdrawals	7.253	6.900	8.400	9.800
Sub-total	2.525	1.826	(-)4.012	(-)1.120
III. Financing				
1. Grant & Sponsorship of Fixed Assets	0.231	0.159	0.844	1.982
IV. Development				
1. Net Proceeds on Development Activities	(-)0.732	0.062	0.376	0.450
2. Cost of Parklands & Public Infrastructure to Municipal Governments	--	(-)0.206	(-)3.475	--
3. Period Development and other public infrastructure costs	(-)3.476	(-)1.803	(-)4.065	(-)4.115
4. Capital Parliamentary Appropriation from Canada	3.649	--	--	--
5. Deferred Development Costs				
6. Receivables from Developers	(-)0.634	(-)0.307	2.088	(-)3.818
Sub-total	4.111	4.067	11.759	11.642
	2.919	1.812	6.684	4.159
V. Change in the year	3.130	(-)0.914	0.260	1.703
VI. Cash & Term Deposit, beginning of the year	1.880	2.794	2.534	0.831
VII. Cash & Term Deposit, end of year	5.010	1.880	2.794	2.534
Source : Same as Statement 1.				

Annexure II

History and Development of the Site

1972 Events and Development

- 100 acres of Harbourfront property were assembled by the Crown for use as park land, through expropriation, direct acquisition, purchase of shares, etc.
- The Federal Government presented the property to the City of Toronto for redevelopment.

1972-76 Events and Development

- The land was administered by the Department of Public Works, followed by the Minister of State for Urban Affairs.
- No consensus on site utilization was achieved.
- A Harbourfront Committee was established by the Federal Government to advise on the future of the site. It recommended (with the support of the City and Metro) the transfer of decision-making authority to a local Toronto Corporation of community based people.
- Extensive public consultation on the future of Harbourfront.
- York Quay Park and Pond were completed for public use.

Public Programming

- First literary readings were held.
- First tours of site were held by school groups.
- 30 dealers participated in the Antique Market.
- Scotland at Harbourfront Scottish Festival.
- Philippine Cultural Festival.
- Crafts people demonstrating on site.

July 1976 Events and Development

- Harbourfront Corporation was established with local Board of Directors.

Public Programming

- The Art Gallery at Harbourfront was established.
- Creation of Programmes Division to fulfil public programming mandate.

1978 Events and Development

- New management was put in place by the Board.
- A development framework document was produced, defining Harbourfront as a mixed use waterfront development initiative. A seven-year plan towards operational self-sufficiency was proposed.
- Pier 4 Restaurant complex was developed by Whaler's group.

Public Programming

- Site attendance reached 700,000 as a result of programme initiatives.
- Brunch with bach series introduced.
- First summer day camps for children.
- First major Canada Day celebration.

1979-80 Events and Development

- First year of implementation of the development framework - improvements to York Quay Centre and Water's Edge Promenade.
- Proposal call for development on Spadina Quay and Terminal Warehouse.
- Private sector activities increased with new tenants on Queens Quay West, including an expanded Pier 4 facility.

Public Programming

- School by the Water, Harbourfront's urban studies and visual arts programme, was formally established with 850 schools visiting.
- First exhibition of crafts at Harbourfront.

June 1980 Events and Development

- Federal Government final approval of \$25.53 million to develop Harbourfront over a seven-year period from April 1980 to March 1987.
- Agreement reached with Olympia & York for renovations to the Terminal Warehouse, renamed Queen's Quay Terminal.

Public Programming

- Harbourfront Craft Fair established.
- Harbourfront Antique Market established as a permanent facility.
- The first international festival of Authors was held.

1981 Events and Development

- Second Phase of Water's Edge Promenada opened.
- Harbourfront negotiated and received final approval respecting the Harbourfront plan from the Ontario Municipal Board for City and Metro Bylaws.
- Negotiations with City of Toronto, Metro, Railways, etc., respecting modifications to City Zoning and the Official Plan for Harbourfront.
- Letters of intent completed with Rampart Enterprises and VKS Ltd. for the development of Spadina Quay for retail, condominiums, and office uses.
- Construction began on Queen's Quay Terminal.

Public Programming

- First Ice Canoe races were held.

1982 Events and Development

- Renovation of the north end of York Quay Centre.
- Harbourfront and the City of Toronto signed the master agreement that guides the location and development of parks, residential, commercial and retail uses and the development approval process.
- A two-year recession began. All private development was put on hold except for Queen's Quay Terminal.
- Announcement of four developers to build 500 units of non-profit housing on Bathurst Quay.

Public Programming

- Annual Winter Festival established
- First International Children's Festival is held.

1983 Events and Development

- Submission of Bathurst Quay sub-area plan to City for approval. Subsequent approval same year.
- City Council approved Spadina Quay sub-area plan.
- Federal Government announced \$ 23.8 million allocation to Harbourfront under the Special Capital Recovery Programme. Projects included a 1,200 car parking garage, the Spadina Pier, an artificial skating rink, the Peter Street Slip Bridge and improvements to Queens Quay West.
- Expression of interest document was issued for John/York Quays involving hotel, residential and commercial uses.
- Queen's Quay Terminal opened June 24, 1983.

Public Programming

- Official opening of Premiere Dance Theatre in Queen's Quay Terminal.

1984 Events and Development

- Parking garage opposite Queen's Quay Terminal Completed.

Public Programming

- Toronto International Festival, arts & cultural celebration.
- Worlds of Asia Festival
- Tall Ships.

- 1985** **Events and Development**
- York Quay centre renovation completed.
 - TTC announced its plan to serve the Harbourfront site with a light rail streetcar system.
 - 80% of site services are in place.
 - 41% of private investment is committed.
 - Metro Police Marine Unit Station opened.
 - City of Toronto Planning Department requested a six-month freeze on development. Negotiations between Harbourfront and City officials began.
 - Hotel Admiral opened by the Whalter's group.
- Public Programming*
- Creatove Sweden Festival.
 - Amsterdam via Toronto Festival.
- 1986** **Events and Development**
- City Council approved new parks and open space plan.
 - Opening of Spadina Gardens to the public by Toronto Mayor Eggleton and Parks and Recreation Commissioner Pirk.
 - Minister of Public Works announced a privatization study of Harbourfront.
 - Approval of 21 storey moderately priced rental housing project.
 - King's landing condominium completed by VKS Developments.
 - Harbour Point Condominiums completed by developers Huang and Danczkay.
- Public Programming*
- Opening of du MAURIER Theatre Centre.
 - First du Maurier Ltd. World Stage International Festival held.
 - Mennonite Bicentennial Festival.
- 1987** **Events and Development**
- Municipal moratorium and creation of the Harbourfront Review Committee by the City of Toronto.
 - Federal moratorium on development and announcement of a policy review on the role and mandate of Harbourfront.
 - City released six "pipeline" projects on condition of receiving 6.5 acres of parkland.
 - Minister of Public Works, with the support of the Toronto Ministers announced the end of the federal review of Harbourfront and confirmed the dual mandate of the company: the development of the site and the responsibility for public activities.
 - Harbourfront conveyed Bathurst and Spadina parks, for a total of 6.5 acres, meeting the condition for the release of the 'pipeline' projects.
 - After a federal endorsement and City Council Review, the Harbourfront 2000 plan was released to the public. The plan proposed to increase the quality and quantity of open space, offering 50 acres of publicly accessible open space (up from the previously agreed 40 acres), with 30 acres of dedicatable public parks (up from 20 acres).
 - The Federal government released the reports on the Management of Federal Lands in Toronto, prepared for the Bureau of Real Property Management at the Treasury Board.
 - King's landing complex completed by Rampart Developments.
 - Bathrust Quay non-profit housing completed.
 - Harbour Terrace condominium completed.
- Public Programming*
- Site attendance reached 3.5 million.
 - Opening of the Power Plant Contemporary Art at Harbourfront gallery.
 - Canoe Festival introduced.
 - Boulevard of Broken Dreams.
- 1988** **Events and Development**
- Interim Control Bylaw imposed by the City of Toronto freezing development until December 1988 and requesting a municipal report on the policies governing the development of Harbourfront.
 - A rental apartment complex (350-390 Queens Quay West) was completed with 500 inexpensive apartments opened.

- Harbour Channel Cooperative Housing (119 non-profit apartments) project started construction.
- Retail outlets opened on ground floor of King's landing complex, just east of Spadina.
- Harbourfront Antique Market moved to new location at Maple Leaf Quay, just west of Spadina.

Public Programming

- First du Maurier Ltd. Quay Works Festival.
- Quebec's Cirque du Soleil visited for two sold-out months.
- First Molson W.O.M.A.D. (World of Music, Art and Dance) Festival.

1989

Events and Development

- Interim Control Bylaw extended to November 1989, or until 40 acre parks agreement is negotiated with the city.
- The Royal Commission on the Future of Toronto's Waterfront initiated hearings into Harbourfront. The Corporation made an extensive presentation to the Commission, including the fully expanded Harbourfront 2000 development plan.
- Remodelling of old Antique Market site began, to allow for interim use of the remaining building.
- New shops opened in the Harbour Point complex.
- The Harbourfront portion of the Light Rail Transit (LRT) line was completed.
- Opening of the new tent in the square facility in the Urban Square at York Quay Centre.
- A creative Children's Play Area, part of Little Norway Park in Bathurst Quay, was completed, including a storytelling chair, a clam shell-designed pool, a children's maze, change rooms and washrooms.
- Harbourfront and the City of Toronto reached a negotiated settlement that would see the Interim Control Bylaw lifted and 41.3 acres of parks turned over to the City.
- The Provincial government announced an indefinite ministerial zoning on the Harbourfront lands, once again freezing all development.

Public Programming

- First TropiCanada - a Winter Heatwave outdoor recreational and indoor entertainment programme for three winter weekends.

1990

Events and Development

- The Federal government appointed a federal negotiator to resolve the Harbourfront impasse among all levels of government.

Public Programming

- Molson Canadian Festival Italiano and Hispanic Fiesta.
- First Molson Canadian Comedy Festival.
- First Pierhead Jump charter boat festival.
- Waterways -- Festival of marine culture introduced.

PART II - ECONOMIC POLICY REFORMS

Chapter 7

Economic Policy Reforms : The Mauritian Experience

I. Introduction

Mauritian experience of economic transition has been widely held as a noteworthy success story. During the eighties, Mauritian economy has achieved a remarkable degree of success in overcoming a wide range of economic problems that it faced during the latter half of seventies. In the process, Mauritius has joined the ranks of middle-income countries and the special significance of this achievement is brought out by a comparison of the development experience of Mauritius with that of other developing countries, especially the sub-Saharan African neighbours of Mauritius. With a per capita GNP of US \$ 2,600 in 1990, Mauritius has achieved the standards of living and the standards of nutrition, health care and general education that greatly exceed those observed in many developing countries.

Mauritius seems to have overcome the natural handicaps of being a small and relatively remote island economy to record impressive economic performance during the period 1983 to 1990. It would be interesting to examine the role of economic liberalisation and associated policy reforms in bringing about this remarkable economic turnaround in Mauritius. An attempt has been made in this case study to analyse Mauritian experience of economic development during the 80's in the context of formulation and implementation of economic policy reforms and also examine some of the issues relating to the formulation of macroeconomic strategy for the future.

II. The Background

Mauritius is a group of tropical islands of volcanic origin, with a land area of approximately 1,865 square kilometers, located in the Indian Ocean to the east of Madagascar. Following occupation by the Dutch in 1598, the French in 1715 and the British in 1810, the islands gained independence in 1968 and became a sovereign state within the British Commonwealth of Nations. Currently, the population of Mauritius is slightly over 1 million, around 3 per cent of which live on the outer island of Rodrigues. The population of Mauritius is a rich mosaic of the descendants of migrants from Asia, Africa and Europe, about 68 per cent of the population being of Indian origin, about 27 per cent of African or mixed descent, and the remaining 5 per cent being Sino-Mauritians and Franco-Mauritians. Within this ethnic, religious and cultural diversity, the government of Mauritius functions in a system of parliamentary democracy. With a life expectancy at birth of 68 years, an infant mortality rate of less than 20 per thousand, and a literacy rate well over 90 per cent, Mauritius has a standard of living of a middle-income developing country(Exhibit 1).

Sugar has traditionally been the life-blood of the Mauritian economy. Although sugarcane was first introduced by the Dutch in 1639, after various unsuccessful attempts to grow cotton, coffee, tobacco and spices, it was only in 1735 that sugarcane cultivation began in earnest and the first sugar mills came into existence. The volcanic soil of the island is highly suited to the cultivation of sugarcane and this crop is able to withstand the effects of frequently occurring cyclones. Moreover, Mauritian

sugar has always had a ready market and it has enjoyed preferential prices through the various agreements that have been negotiated at different times: the Imperial Preference regimes, the Commonwealth Sugar Agreement and the Sugar Protocol of the Lome Convention. Sugar has, therefore, played a unique role in the social and economic history of the island, contributing significantly to the generation of employment and incomes.

The early years preceding and following independence (1964-72) were characterised by indifferent economic performance and conservative financial management. During this period, the economy grew slowly at an annual average rate of about 1.8 per cent and sugarcane cultivation was the principal economic activity, accounting for over 25 per cent of gross domestic product (GDP). The manufacturing sector was relatively small and contributed about 7 per cent to GDP. It consisted of a number of small scale private industries producing almost exclusively for the domestic market. The principal industries that came up during this period were food, beverages, tobacco, footwear and the repair and assembly of machinery and transport equipment. Domestic savings and investment remained constant at about 16 per cent of GDP and exports and imports both grew at a real annual average rate of just about 3 per cent. The balance of payments yielded surpluses for most of the period and the overall fiscal deficit averaged around 5 per cent of GDP. At the same time, the labour force continued to expand at an annual rate of about 3.3 per cent, notwithstanding the fall in the annual growth rate of population from 3 per cent in the 1950s and early 1960s to around 1.5 per cent by the early 1970s largely in response to a vigorous family planning programme. As a result, although employment grew by about 3 per cent per annum between 1968 and 1972, the unemployment rate in Mauritius was estimated at about 16 per cent by 1972.

The boom in sugar prices in 1973 and 1974, coupled with favourable weather conditions, paved the way for a spurt in economic growth during the post-1972 period. Thus, Mauritian economy grew by more than 10 per cent per annum between 1972 and 1977. Gross domestic savings increased and provided the capital necessary to accelerate the development of the manufacturing and services sectors, along with an increase in employment. This period, during which the government followed an expansionary policy of increased public investment in response to rising unemployment, also witnessed rapid increases in costs, wages and prices throughout the economy. The subsequent reversal in the terms of trade caused by a sudden and sharp 23 per cent decline in sugar prices in 1976, coupled with the second oil price shock in 1979, led to a rapid deterioration in the balance of payments, which was further aggravated by the government's expansionary fiscal stance. The ensuing budget deficits were financed by an increasing recourse to non-concessionary foreign borrowing which caused the country's external debt to triple between 1976 and 1979 and the debt service ratio to increase from a very modest 1 per cent to about 10 per cent. This period was also marked by a significant deceleration in the growth of output and exports and a simultaneous acceleration in the rate of inflation.

Thus, by 1979, Mauritius was on the verge of plunging into serious economic crisis following significant deterioration in balance of payments, sharp increase in external debt, rapid erosion of foreign exchange reserves, high levels of unemployment, low levels of savings and investment, growing fiscal imbalances, rapid increase in inflation rate and significant decline in overall growth. Faced with such serious economic difficulties in 1979, the government decided to approach the IMF and the World Bank for necessary support to embark upon a stabilization and structural adjustment programme. Between 1980 and 1986, the government implemented five successive standby arrangements with the IMF and two structural adjustment programmes through World Bank assistance to correct the economic and financial imbalances in Mauritian economy. The conventional prescriptions, which were suggested by the IMF and the World Bank as a central part of the stabilization and structural adjustment programme, were :

- i. The adoption of appropriate exchange rate policies
- ii. Restrictive credit and monetary policies
- iii. Restrictions in the overall fiscal deficit
- iv. Maintenance of a liberal system of trade and payments

- v. Restrictions in consumer subsidies, and
- vi. Wage restraints.

The government decided to implement the above package of economic policy reforms incorporating every element without exception. The main focus of the first structural adjustment programme implemented during the period 1979-82 was on demand management. It commenced with a 30% devaluation of the Mauritian Rupee (MR) in October 1979. The subsequent period witnessed a significant revision of the tax structure, introduction of a new package of export incentives and introduction of policies to attract direct foreign investment as well as transfer of technology. The programme achieved a reasonable degree of success in (a) reducing the overall budget deficit, (b) improving the external current account balance, and (c) bringing down the domestic inflation rate. However, several unfavourable exogenous factors seriously affected the performance of Mauritian economy during 1979-1982. The more significant among these unfavourable external factors were (a) adverse weather conditions in 1979-80, (b) rising oil prices, (c) rising import prices, and (d) world-wide recession during 1980-82. The performance of Mauritian economy during the early stages of implementation of stabilisation and structural adjustment programmes has been extensively examined in a series of World Bank documents (May 1982 and April 1985) and IMF reports (September 1985 and October 1986).

On account of several unfavourable external factors that Mauritius faced during 1979-82, the first structural adjustment loan that Mauritius obtained from the World Bank proved to be inadequate. Hence the government had to approach the World Bank for a second structural adjustment loan in 1983. Moreover, the series of standby arrangements with the IMF lasted till August 1986. The period from 1983 onwards can be regarded as the second phase of implementation of stabilisation and structural adjustment programme in Mauritius. This phase of structural adjustment programme has turned out to be highly successful. The following indicators, quoted by the Prime Minister of Mauritius in his Budget Speech of 17th June 1991, clearly bring out the scale of success achieved by Mauritius during the post-1982 period:

- Gross Domestic Product has increased from MRs. 12 billion in 1982 to MRs.37 billion in 1990 and it is expected to reach MRs.41 billion in 1991.
- Income per head, in terms of US dollars, has increased from 1,100 in 1982 to 2,600 in 1991, and would reach around 2,800 by 1992.
- Rate of unemployment has fallen from 17 per cent in 1982-83 to 2.5 per cent by 1991.
- Female labour participation rate has increased from 26 per cent in 1982 to 44 per cent in 1990.
- Gross export earnings of the EPZ sector have increased tenfold from Rs.1.2 billion in 1982 to Rs.11.4 billion in 1990, while employment in that sector has increased from 23 thousand to 90 thousand.
- Gross export earnings of Tourism sector have increased eightfold from MRs. 0.45 billion to MRs.3.5 billion.
- Foreign exchange reserves have increased from MRs.0.28 billion in 1982 to MRs.9.1 billion in 1990 and would reach MRs.13.5 billion by 1992.
- Total government external debt outstanding as a ratio to GDP has fallen from 49 per cent in 1982 to 16 per cent in 1991.
- The overall budget deficit as a percentage of GDP has fallen from 13 per cent in 1982 to 2 per cent in 1991.

In what follows, we examine various aspects of economic policy reforms which may have contributed to the successful economic performance of Mauritius during the period 1983 to 1990.

III. Industrial Policy Reforms

Since 1970, promotion of export-oriented manufacturing has been the main thrust of industrial policy in Mauritius. The process of industrialisation in Mauritius has led to significant structural changes in the Mauritian economy over the last decade. During the period 1980 to 1990, the share of manufacturing in GDP increased from 15.2% to 24% at current prices and from 15.5% to 21.5% at 1982 prices (Exhibits 2 and 3). Similarly, the share of manufacturing in total employment increased from 18.4% in 1980 to 38.6% in 1990 (Exhibit 4).

For the purpose of formulating industrial policy, the manufacturing sector was divided into following four groups :

- (a) Sugar and sugar by-products;
- (b) Manufacturing for the domestic market with a Development Certificate (DC);
- (c) Manufacturing for the export markets with Export Enterprise Certificate (EEC); and
- (d) Standard manufacturing without DC/EEC incentives.
Within this group, the policy also focusses separately on the small scale enterprises including the informal sector units.

The growth of manufacturing sector during the post independence period can be broadly classified into the following four sub-periods:

- (a) 1965 to 1970 : Period of Slow take-off with particular reference to import substitution;
- (b) 1970 to 1976 : Period of rapid growth starting from a low base.
- (c) 1976 to 1982 : Period of marked slow down in growth.
- (d) 1982 to 1990 : Period of rapid growth based on export- led industrialisation.

Since early sixties, manufacturing activity in the organised sector was fostered by the award of a Development Certificate to enterprises which were considered beneficial to economic development of Mauritius. This policy was targetted essentially towards promotion of import substitution industries and it included attempts of the government to attract foreign capital and know-how for the development of such industries. The import substitution strategy was evolved largely in response to the inherent weaknesses of Mauritian economy in the early sixties and the corresponding need to halt outflow of foreign exchange and correct deficits in the balance of payments. As a result of this policy, several industries such as food processing, beverages, cosmetics, footwear, furniture, fertilizers, paints and chemicals, etc. came up to meet the domestic demand. However, this policy failed to create the required level of employment. Total employment in the manufacturing sector in late-sixties was only around 9000 and the unemployment rate was as high as 29%. As the government realised the significance of promoting manufactured exports and the role it could play in industrial growth, the emphasis in industrial policy started shifting from Development Certificate scheme to export promotion. Thus, in 1970, the Government introduced the Export Processing Zone Act which together with other administrative support measures aimed at providing a comprehensive package of incentives to stimulate export-oriented manufacturing industry. Simultaneously in 1974, the government decided through Development Incentives Act (1974), to award a Development Certificate only in exceptional circumstances, i.e., to industries of strategic importance.

The following incentives and facilities were offered to the export-oriented manufacturing sector under the Export Processing Zone Act :

- i) duty free imports of machinery, equipment, spare parts and raw materials;
- ii) exemption from income tax on dividends during the first 10 years of operation from start of production and free repatriation of dividends;
- iii) free-repatriation of capital (without appreciation) on obtention of APPROVED STATUS from the Bank of Mauritius;

- iv) easy access to electric power, loans, investment and export finance at preferential rates;
- v) liberal export credit and export insurance facilities;
- vi) liberal capital depreciation allowances and investment credit.
- vii) comparatively flexible labour legislation;
- viii) exemption from payment of half of the normal registration fee on land and buildings purchased for new enterprises;
- ix) issue of residence and work permits to major shareholders and the expatriate technical/professional personnel;
- x) easy accessibility to factories for lease/rent; and
- xi) guarantee against nationalisation.

During the period from 1970 to 1982, Mauritian government followed a mixed strategy aimed at stimulating both export-oriented enterprises as well as import substituting enterprises. While this strategy met with some initial success especially during the first half of seventies, it failed during the subsequent period. Thus, the unemployment rate which fell below 15% by mid-seventies, rose sharply to 22% by 1982. Buoyancy in the manufacturing sector experienced in mid-seventies declined significantly by 1982. Manufacturing activities in the DC sector slowed down after 1977. Capacity utilisation for DC companies was low (around 44%) which severely constrained their capacity for diversification. Moreover, import substitution strategy often encouraged the production of import substitute by capital intensive methods and hence failed to reduce the pressure of unemployment.

The basic weaknesses of import substitution strategy were three-fold: (a) It encouraged inefficiency among firms catering exclusively for the protected domestic market; (b) It diverted resources from the more efficient export-oriented firms; and (c) It led to price distortions in the economy. Thus, it was felt that, although the import substitution strategy had brought some tangible benefits to the economy, it had outlived its utility by late seventies. Consequently, the industrial policy reforms introduced in early eighties shifted the emphasis of Mauritian industrialisation strategy from import substitution to export-led growth. Significant changes were made in fiscal policy and trade policy to strengthen this strategic shift in favour of export-led growth.

The latter half of eighties also witnessed added emphasis on the development of small scale industries as a part of new industrialisation strategy. Under the Small Scale Industries Act, 1988, a small scale firm is defined as the one engaged in manufacturing and having production equipment not exceeding half-a-million Mauritian Rupees (c.i.f. value). The Central Statistical Office, Ministry of Economic Development and Planning applies the employment criterion and defines a small scale firm as any unit employing less than 10 persons. The small scale sector comprises a number of overlapping areas and receives assistance from several organizations such as the Development Bank of Mauritius, The Mauritius Commercial Bank, Employers' Federation, National Development Unit, The Chamber of Commerce and Industry, Mauritius Cooperative Central Bank, Small Industries Development Organization, Ministry of Industry and Industrial Technology and the Handicrafts Section of the Ministry of Education. However, the major problem with regard to such assistance has been that there is no coordination among various agencies providing assistance to the small scale sector. Moreover, there is an acute paucity of information on the small scale sector. According to rough estimates, the small scale manufacturing units collectively employed around 22,000 persons in 1988.

While availability of long term capital is not a constraint on the development of small scale industry, there are several other impediments which account for the failure of the small scale sector to take off. The major constraints faced by the small scale firms are as follows :

- 1) Cumbersome and time-consuming formalities including unusually long time lag between the date of application and the date of actual disbursement of loans (often around 9 to 12 months);
- 2) Insistence of the commercial banks on adequate security and actual operation of the unit for at least six months before the loans are sanctioned;
- 3) Poor management, production and quality control;

- 4) Lack of technical know-how in product costing and poor marketing outlets; and
- 5) Lack of information regarding the procurement of raw materials and machinery.

IV. Fiscal Policy Reforms

The main focus of fiscal policy reforms in Mauritius during the eighties has been the special emphasis laid on fiscal restraint as the key instrument of stabilisation. The overall budget deficit was as high as 12.4% of GDP in the fiscal year 1981-82, but it was brought down through sustained efforts to 1.8% by 1987-88 and it was estimated to be around 2.5% of GDP in 1990-91 (Exhibit 5). Such marked improvement in the country's fiscal position was achieved through the combined effort in the direction of reducing government expenditure from 31.4% of GDP in 1981-82 to 24.4% of GDP in 1990-91 and simultaneously raising total revenues as a proportion of GDP from 19% to 21.9% during the same period. The proportion of current expenditure financed by tax revenue, which was only around 67% in 1981-82, increased to more than 100% by 1990-91. Growth of current expenditure, which constitutes more than 80% of total expenditure, was kept under remarkable control during the eighties and as a result the ratio of current expenditure to GDP declined from 24.7% in 1981-82 to 20.1% in 1990-91. Such a decline in the ratio of current expenditure to GDP has been achieved through substantial reductions in budgetary subsidies on rice and wheat flour, reduction in the parastatal subsidies and restrictive wage policy. The wage bill of the government and total subsidies, which amounted to 17.3% of GDP in 1981-82, declined to 14% by 1987-88.

The government introduced major fiscal reforms during the period 1984 to 1986 to bring about rationalisation of overall tax in revenue collection through the introduction of new tax management techniques. In fiscal year 1984, the rate of corporate tax was significantly reduced from an average of 60% to a flat rate of 35%. Moreover in the following year, the entire corporate tax system was simplified by streamlining the various tax regimes for the main productive sectors of the economy. The entire tax system of providing tax exemptions under either complete or partial period of tax holidays coupled with differential rates of depreciation allowances and corporate tax rates was replaced by a uniform rate of 15% corporate tax throughout the life span of all EPZ companies and DC companies. Under the new tax regime, the standard rate of corporate tax, which had earlier been brought down to 35%, was applicable to non-DC, non-EPZ companies. However, to promote the development of capital market in Mauritius, provision has been made under the Finance Act of 1988 to charge concessional corporate tax rate of only 25% to those companies which elect to be quoted on the Port Louis Stock Exchange. Moreover, the dividends of companies listed on the stock exchange received by the individuals are exempted from tax to the extent of 35% of such income. To promote exports of locally manufactured goods by non-EPZ firms, a special provision was also made in the Finance Act of 1988 to allow a reduction of 2% in the corporate tax rate for every 10% of the turnover exported.

To pursue the policy of fiscal reform that aimed at growth with social justice, the government raised the minimum taxable income threshold in stages during 1984 to 1986, which led to total tax exemption of around thirty thousand tax-payers in lower income groups. Also, in the fiscal year 1985 the government reduced the maximum marginal rate of income tax from 70% to 35%. Moreover, to curb inflationary growth in consumption expenditure, Sales Tax was introduced in 1982 and several commodity tax rates were raised by 10% in 1984.

In the budget for 1991-92, several fiscal initiatives were taken to give a fillip to the development of electronic sector. A special scheme to award Pioneer Status Certificates was created for companies operating as supporting units to the electronic sector, i.e. for companies engaged in such activities as high precision machines of metal and plastic parts and assembly of high precision electronic equipment. Companies holding pioneering status certificates are granted complete exemption from customs duty, import levy and sales tax on equipment and material and they are also charged corporate tax at the reduced rate of 15%. The 1991 budget also introduced a system of progressive reduction of tax rate for non-EPZ manufacturing companies operating in the export market. The corporate tax rate

payable by a non-EPZ company is brought down to 25% for 10-30% export turnover ratio, 20% for 30-50% export turnover ratio and 15% if exports exceed half of the turnover. Thus, the process of fiscal reforms in Mauritius is still in progress and its main objectives continue to be the achievement of proper balance in public finance and a significant reduction in overall deficit to a level that could be financed without affecting medium term growth prospects or creating additional inflationary pressures.

V. Trade Policy Reforms

Efficient management of the external sector through appropriate trade policy reforms represents a crucial element of overall economic management in highly open and relatively small economy like Mauritius which is vulnerable to changes in international economic environment. To tide over the serious economic crisis faced by Mauritius, the Mauritian government entered into an agreement with the IMF in October 1979 to undertake an economic and financial stabilisation programme under a standby arrangement that would enable Mauritius to draw over a period of two years total financial assistance of SDR 73 million. As a part of this stabilisation programme package, the Mauritian Rupee was devalued on 23 October 1979 from MRe. 1 = SDR 0.13 to MRe. 1 = SDR 0.10. This exchange rate adjustment was made to restore the profitability and external competitiveness of Mauritian exports and simultaneously encourage the process of import substitution in the economy. This measure was also expected to depress the demand for imports through higher rupee prices of imports.

In September 1980, Mauritius entered into a new one-year stand-by arrangement with the IMF for a balance of payments assistance of SDR 35 million and in December 1981 it entered into another one year stand-by arrangement with the IMF for a further balance of payments assistance of SDR 30 million. Moreover, a Structural Adjustment Loan of US \$ 15 million was also contracted with the World Bank in June 1981 and this loan was fully disbursed by December 1981. Since Mauritius continued to face serious strains on its balance of payments during 1980-81 with overall BOP deficit rising sharply to exceed MRs. 950 million (Exhibit 6), another major exchange rate adjustment became inevitable. Thus, Mauritian Rupee was devalued again in September 1981 by 16.7% in terms of SDR (from MRe. 1 = SDR 0.10 to MRe. 1 = SDR 0.0833).

To attain greater flexibility in formulating the exchange rate policy, the government delinked the Mauritian Rupee from the SDR in 1983 and linked it to a trade-weighted basket of currencies. During the subsequent period, the Mauritian government followed a more realistic exchange rate policy that aimed at maintaining the international competitiveness of Mauritian exports through further depreciation of Mauritian rupee in terms of the nominal exchange rate. Thus, by 1985 the average annual exchange rate for US \$ and UK Pd. Sterling were MRs. 15.58 and MRs. 20.03 respectively (Exhibit 7). During the subsequent period from 1985 to 1990, Mauritian rupee continued to depreciate in nominal terms against British Pd. Stg., French Franc and Deutsche Mark. On the whole, the basic objective of the exchange rate policy of Mauritian government is to avoid appreciation in the real effective exchange rate of rupee.

By 1984, there were clear signals of economic revival in Mauritius. The overall growth rate went up from 0.4% in 1983 to 4.2% in 1984 and foreign investment went up sharply from MRs. 12 million in 1983 to MRs. 88 million in 1984. The rate of inflation, which was as high as 26.4% in 1980-81 and 13.4% in 1981-82 came down to 5.6% in 1983-84. In 1983-84, total exports increased by 25% while total imports increased by 16%. Encouraged by such positive signals of economic recovery, Mauritian government continued to pursue its economic adjustment programme with added enthusiasm and entered into its fifth stand-by arrangement with the IMF which commenced in January 1985 covering a period of 18 months involving overall balance of payments assistance of SDR 49 million. The government had already negotiated earlier (in 1983) the Second Structural Adjustment Loan of US \$ 40 million with the World Bank.

Besides the adoption of a realistic and flexible exchange rate policy, several other policy initiatives constituted important elements of the package of trade policy reforms introduced by the government in pursuit of the export-led growth strategy. These policy measures included elimination of quantitative restrictions on imports, rationalisation of tariff structure, substantial reduction of tariffs on several items of imports and various steps to encourage foreign private investment. As a part of the process of import liberalisation initiated in 1983, customs duties were significantly reduced for a large number of items and completely removed for items during the period 1983 to 1987. Moreover, the regime of import permits was completely abolished in July 1991. During the earlier period, industrial users had to obtain import permits for various items through an elaborate process of approvals involving Ministry of Foreign Trade and Ministry of Industry.

As a result of these policy reforms and also on account of sizeable assistance provided by the IMF and the World Bank during early eighties, the overall balance of payments position of Mauritius improved considerably by mid-eighties. The persistent and high deficits in balance of payments experienced during the period 1976 to 1982 disappeared and from 1984-85 onwards Mauritius has been enjoying an overall surplus in the balance of payments. The declining trend in foreign exchange reserves observed during 1976 to 1981 was arrested in 1982. In fact, during the post-1982 period, there has been a steady increase in the foreign exchange reserves of Mauritius from the highly vulnerable position of total reserves equivalent to only 2 weeks of imports in 1981 to more than 22 weeks of imports by 1990 (Exhibit 8).

The recovery and subsequent buoyancy in the balance of payments position has been partly also due to the rising trend in private foreign investment in Mauritius. During the latter half of eighties, there has been a significant inflow of foreign investment in Mauritian Export Processing Zone from various countries including Hong Kong, Taiwan, France, Germany, Switzerland, etc. and as a result aggregate foreign investment has increased sharply from MRs.73 million in 1986 to MRs. 299 million in 1989 and MRs.270 million in 1990 (Exhibit 9). Moreover, during the post-1982 period Mauritius has also enjoyed consistently favourable terms of trade with average export prices rising faster than average import prices (Exhibit 10). Improvement in the terms of trade indicates that the country is able to afford more imported goods for each rupee worth of goods exported and hence it implies rising real income leading to better standards of living. The improvement in the terms of trade was partly due to rising average price realisation for sugar exports, which still constitute around 30% of the country's total exports in 1989-90. The weighted average price of sugar exports increased by about 48% during the period 1986-87 to 1989-90 (Exhibit 11), while the average price index for exports increased by about 33% during the same period.

Another significant development during the latter half of eighties is the improvement in the external debt position of Mauritius. While the total external debt has steadily increased during the period 1985 to 1990, its pace of increase has slowed down considerably and as a result the ratio of external debt to GDP has declined from 58% in 1985 to 35% in 1990 (Exhibit 12). Moreover, the debt-service ratio has also declined from 24% to 6% over this period.

VI. Monetary Policy Reforms

Since 1976, monetary policy in Mauritius was formulated with the basic objective of checking the growth in aggregate domestic expenditure and arresting the drain in foreign exchange reserves. Monetary control was achieved by the imposition of ceilings on bank credit, the regulation of bank liquidity, constraints to the access on central bank credit and revisions in interest rates. A specially designed package of monetary measures was announced in October 1979 following the devaluation of Mauritian Rupee. The bank rate was raised from 9% to 10.5%, the interest rates were increased across the board by one and-a-half points, the entire interest rate structure was rationalised, the overall ceiling on bank credit to the private sector was reintroduced and the inter-bank money market was restored. It was also stipulated that the commercial banks should use the central bank's rediscount and advance facilities only as the last resort. In order to discourage any excessive growth in the lending

ability of banks, a two-tier structure of interest rates on borrowings from the central bank was effected. Under the two-tier structure, each bank has a prescribed borrowing limit within which it can borrow from the central bank at the bank rate and any borrowing in excess to this limit would carry a rate twice the bank rate.

During the subsequent period, the overall deficit in the balance of payments got converted to a surplus, which was growing rapidly with the passage of time. The growing surplus in the overall balance of payments of the country during 1986 to 1988 brought about an increase in liquidity in the economy. Around March 1987, excess liquidity with commercial banks had reached Rs.1,200 million. Moreover, there was also an across-the-board increase in wages and salaries, which would further enhance the excess liquidity with the banks. Two immediate and adverse consequences of the increase in banks' liquidity are: (a) an upsurge of imports leading to a deterioration in the trade balance, and (b) an increase in the rate of inflation. The mopping up of excess liquidity in the economy became a priority of the Bank of Mauritius. The following measures were, therefore, taken to mop up the excess liquidity with the individuals as well as with the commercial banks.

- (i) The Bank of Mauritius Bonds which were issued in 1987. These bonds were specifically designed to mop up surplus liquidity with individuals only. Two types of such bonds, both with maturities of up to 8 years, were issued one carrying an interest rate of 14 per cent with interest payable half-yearly and subject to income tax, and the other with the initial capital tripling in 8 years with total tax exemption, and through these bonds an amount of MRs.263 million was sterilized.
- (ii) The liquid assets ratio that commercial banks are required to maintain was raised in January 1988 from 20 per cent to 23 per cent with the cash ratio requirement remaining unchanged at 10 per cent thus bringing up their liquidity ratio requirement from 30 per cent to 33 per cent of each bank's total deposit liabilities.
- (iii) Liquid assets were redefined to exclude Government stocks with maturity periods exceeding 7 years.

Highly restrictive monetary policy followed during the period 1980 to 1987 succeeded in containing double-digit inflation and the rate of inflation fell sharply from 26.4% in 1980-81 and 13.4% in 1981-82 to 1.8% in 1986 and further to 0.5% in 1987 despite relatively high growth rates of money supply during mid-eighties (Exhibit 13). However, during the subsequent period, the rate of inflation has accelerated again and the consumer price index has increased at the rate of 12% to 13% per annum during 1989 as well as 1990. Bank of Mauritius has, therefore, continued to follow tight money policy also during the latter part of eighties. The bank rate was stepped up from 11% to 12% in October 1989 and corresponding changes were also made in the entire interest rate structure.

The high rate of monetary expansion during the latter half of eighties has been induced mainly by a continuous and rapid increase in the net foreign assets of the banking sector during this period. However, a monetary development during the same period has been that the bank credit to the private sector has increased at a significant rate while net credit to the Government has declined significantly following progressive reduction in current account deficit. Thus, the tight money policy and resulting credit squeeze has not resulted in crowding out of private sector investment.

One of the aims of monetary policy during post-1982 period has been to ensure that the real rate of interest is positive. If monetary policy has to support the development strategy based on an aggressive export-led industrialisation, it is necessary for the banking system to follow an interest rate policy that is conducive to maintaining a sound investment climate so as to sustain the pace of economic growth. Accordingly, the government has initiated the policy of liberalisation of interest rates to stimulate inter-bank competition with a view to bringing about the following changes :

- (a) Gradual rise in interest rates on savings and time deposits that would be instrumental in maintaining positive real rates of interest and thereby mopping up excess liquidity;

- (b) Moving the lending rates closer to the structure that would prevail under perfectly competitive conditions to ensure that resources are more efficiently allocated among different sectors of the economy. In pursuance of this policy, there was a partial decontrol of interest rates including abolition of minimum savings deposit rate and maximum lending rate.

However, the policy of interest rate liberalisation could prove to be ineffective if there is a high degree of monopolistic concentration in the banking sector. As at the end of June 1990, there were 13 commercial banks operating in Mauritius with 117 branches and aggregate deposits of MRs.20.2 billion of which demand deposits constituted 13.5%, savings deposits 37.1% and time deposits 49.4%. However, the two largest banks control over 75% of total bank deposits, while 9 small banks share 15% of deposits. With such high levels of deposit concentration, it is unlikely that any of the smaller banks would challenge the leaders. In fact, the available evidence suggests that the commercial banks are acting almost like a cartel while dealing with the public, especially in regard to the fixation of interest rates. According to the World Bank mission (1990) that reviewed the progress of economic liberalisation in Mauritius, while some progress has been achieved in pursuing the liberalisation of the financial sector, the following problems continue to exist : (a) lack of real competition within the financial sector; (b) absence of a market determined system for the allocation and pricing of credit resources; and (c) reliance on credit ceilings.

Despite such shortcomings, there has been a remarkable attempt on the part of Mauritian government to bring about a gradual shift in the monetary management of the economy from the regime of regulated interest rates and restructuring on credit structure to a more flexible market determined interest rate structure and increasing reliance on open market operations to control money supply.

VII. Export Processing Zone

The successful implementation of stabilisation and structural adjustment programme during early eighties created the economic environment in Mauritius in which most of the pre-conditions for sustained export-led growth strategy were fulfilled. The liberalisation of the exchange and trade regimes, improved resource mobilisation, effective control of public expenditures and restricted credit expansion contributed to laying a solid foundation for Mauritius to launch the new growth strategy and derive the maximum advantage of favourable developments in the global economic environment during the eighties. Moreover, throughout the structural adjustment period, Mauritius was able to derive the benefit of substantial foreign exchange earnings from sugar which were insulated against the adverse price behaviour in the world markets by virtue of the preferential price arrangements enjoyed by Mauritius with the EC under the Sugar Protocol of the Lome Convention. In fact, Mauritius enjoys the highest quota among the African, Caribbean and Pacific (ACP) countries currently fixed at 507 thousand metric tons, while the price that it has received from EC during most part of eighties on an average about three times the free world market price. Mauritius has made a very effective use of the resources generated from sugar exports to diversify into manufactured exports by explicitly and systematically focussing on the development of Export Processing Zone (EPZ).

Mauritian Export Processing Zone (MEPZ) was established in 1970. Following the examples of Hong Kong and Singapore, MEPZ is designed basically as a legal concept, unlike EPZs in other countries which have well defined geographical boundaries. Although MEPZ showed healthy growth during the first decade (1970-1980), its expansion accelerated significantly after the economic recovery in the post-1982 period. Thus, during the period 1982 to 1990, MEPZ has registered very impressive growth (Exhibit 15). The number of enterprises in EPZ sector has gone up from 115 to 568, employment from 23.5 to 88.3 thousand, value added has grown nine-fold and exports have grown from MRs. 1.2 billion to MRs. 11.5 billion. Currently, MEPZ has emerged as the single largest employer in the economy accounting for more than 20% of total employment and more than half of the employment in manufacturing sector. The share of EPZ exports in total exports has increased significantly from 31% in 1982 to around 64% by 1990. Similarly, the share of EPZ sector in the value added by the manufacturing sector has increased from less than 29% in 1982 to around 55% in 1990.

Rapid growth of the EPZ sector has failed to reduce the high degree of product-wise concentration in EPZ exports. Wearing apparel continues to dominate EPZ exports, and its share in total EPZ exports has in fact increased from 71% in 1982 to more than 79% in 1990 (Exhibit 16). Attempts to bring about diversification of EPZ exports has not produced the desired results so far. In fact, the only product group other than wearing apparel whose share in total EPZ exports has increased during the eighties is watches and clocks, with all other product groups indicating a marked decline in their relative share during this period. The high degree of product-wise concentration in MEPZ is also apparent from the fact that by 1990, the category of wearing apparel accounted for 61% of total firms and 84% of total employment in MEPZ (Exhibit 17). However, the degree of concentration measured in terms of size of EPZ firms seems to have declined during the period 1982 to 1990. Thus, the proportion of firms employing less than 50 workers has increased significantly and their share in total EPZ employment has also gone up during this period, while the proportion of firms employing more than 500 workers has declined and their share in total employment has also declined (Exhibit 18). It is also interesting to observe that the phenomenal growth of EPZ sector during the post-1983 period has brought about a significant decline in the incidence of sickness and closures of EPZ firms. The average proportion of closures of EPZ firms during 1978 to 1983 is found to be 9.5% per annum, while the average proportion for the subsequent period (1984 to 1988) has been much lower at 4.1% per annum (Exhibit 19). As against this, the average number of new EPZ firms being set up has increased sharply from 22 per annum during pre-1983 period to 106 per annum during the post-1983 period. Thus, entry of a large number of new firms in the EPZ sector during the post-1983 period has not seriously affected the viability of existing EPZ firms.

Backed by strong incentives and favourable economic environment, MEPZ enterprises have been able to take advantage of preferential access to European and American markets enjoyed by Mauritian products. Thus, about 75% of MEPZ exports go to EEC with France alone accounting for more than half of it, and another 20% go to USA (Exhibit 20).

VIII. SWOT Analysis of MEPZ

While analysing the past success and future prospects of MEPZ, it would be useful to examine its strengths and weaknesses and also evaluate the opportunities and threats facing MEPZ. The buoyancy of MEPZ during the eighties clearly indicates that Mauritius has successfully capitalized on global economic recovery during mid-eighties and has also exploited the available market opportunities through improved competitiveness of its exports resulting from an effective implementation of the structural adjustment programmes.

The strengths of MEPZ can be viewed in terms of the external factors as well as the internal factors. The main external factors which have proved to be major strengths for MEPZ are :

- i. Falling international oil prices;
- ii. Relative over-valuation of American and European currencies during mid-eighties coupled with rapid expansion of European and American markets;
- iii. Appreciation of Taiwanese dollar which reduced the competitive-ness of Taiwan firms and encouraged prospective Taiwanese investors to turn to Mauritius;
- iv. Political uncertainties in competitor countries especially Hong Kong, which pushed many successful firms to relocate their business out of Hong Kong. These firms found Mauritius to be a safe heaven for investment of their capital and relocation of manufacturing operations. In the process, the MEPZ not only gained in terms of inflow of foreign capital but also got the advantage of scarce know-how and international marketing network, which contributed to its rapid expansion.

The major internal factors which constitute the strengths of MEPZ are as follows :

- i. Mauritius offers a stable socio-political environment and the government which has a committed enthusiasm for private enterprise;

- ii. Mauritius offers a highly generous package of incentives for EPZ enterprises and it also accords a warm welcome to foreign investors with highly simplified administrative procedures for setting up enterprises in Mauritius. This creates a remarkably favourable business climate conducive to rapid growth of MEPZ;
- iii. In early-eighties, Mauritius offered an excellent combination of relatively cheap and reasonably skilled labour;
- iv. Economic planning and development of Mauritius during the sixties and seventies has ensured availability of physical infrastructure and institutional set up to facilitate industrial growth;
- v. Unlike EPZs in other countries which have relied over-whelmingly on foreign capital, MEPZ is financed substantially by local entrepreneurs and the foreign capital is used more as a stimulus rather than as an exclusive source of finance. The available information on the structure of capital ownership shows that share of accumulated capital invested by Mauritians has in fact risen from around 50% during mid-seventies to around 60% during mid-eighties. Thus, the local entrepreneurs have played a significant role in the growth of MEPZ.

The global as well as domestic economic environment has offered several opportunities to Mauritius which have effectively contributed to the growth of MEPZ during the eighties. Mauritius has benefitted significantly by effectively tapping the following opportunities:

- i. Mauritius is a signatory member of the LOME Convention between the EEC and the ACP states. Under the EEC-ACP agreement, goods manufactured from Mauritius enter the EEC market duty free as long as they satisfy the Rules of Origin (Annexure 1). LOME Convention has created vast opportunities for Mauritius and the Mauritian private sector has been fairly successful in taking full advantage of the preferential access that Mauritius has been enjoying with regard to the European Economic Community.
- ii. Mauritius enjoys an opportunity to charge preferential prices under the sugar protocol with the EEC since 1975 and currently Mauritius is the largest supplier of sugar to the EEC.
- iii. As a member of Preferential Trade Area (PTA) consisting of 19 Southern and East African countries, Mauritius derives significant benefits from Preferential Tariff Rates under the Treaty for PTA (Annexure 2).
- iv. Mauritius enjoys the benefit of a significant allocated quota on a number of textile items in both the USA and Canada. A wide range of Mauritian products also enter the USA free from quota (Annexure 3). Moreover, as a member of the Indian Ocean Island Commission, Mauritius also has easy access to a potential nearby market especially in Madagascar and Reunion.
- v. With the political climate set for reforms in South Africa, new opportunities are emerging in that region. South Africa with a population of more than 35 million and a per capita income in the range of US \$ 3000 provides vast opportunities both in the form of supply of critical raw materials and inputs to Mauritian manufacturing sector and also providing a large potential market for the goods manufactured by MEPZ.
- vi. Far reaching socioeconomic changes in Eastern Europe and USSR also represent significant opportunities for Mauritius. With the speeding up of the process of economic reforms in the erstwhile USSR and the consequent convertibility of Rouble, new opportunities have opened up for the Mauritian knitwear products. Similarly, the emergence of combined European market in 1992 would also provide fresh opportunities to Mauritius by making the access to EEC market more difficult for some of its competitor countries.
- vii. Mauritius has control over a large ocean area which represents vast untapped resources especially in the area of deep sea fishing.

While global economic environment offers many opportunities, it also poses certain threats. Among the major threats facing Mauritius, the following deserve special mention :

- i. Third World Countries with interest in the textile sector have been lobbying hard in recent years with the developed world to open fresh markets on equal terms to all textile exporters irrespective of their location or status. While not much progress has been made so far in this

- direction, the concerted efforts being continuously made by the non-ACP Third World countries poses a serious threat to Mauritian exports especially textiles. Similarly, Geneva talk for strengthening GATT instruments also poses a serious threat to the Mauritian textile sector.
- ii. USA has recently signed a pre-trade agreement with Canada. Moreover, there is also a distinct possibility of the setting up of an American free trade zone spanning the entire continent. If this possibility materialises in future, it would have serious implications for the future prospects of MEPZ.
 - iii. Successive oil shocks have led to rapid increases in freight charges. Thus, for instance, following the Gulf crisis, freight charges had increased by about 25% in 1990-91. Since Mauritius is located quite far from the main centres of international economic activities, increase in transport costs affects the prices of final products significantly and erodes the competitive age of MEPZ.
 - iv. The outcome of the last few UNCTAD meetings clearly shows the failure of the LDCs to secure a fairer deal for their manufactured exports. During the latter half of eighties, there has been a surge of protectionism and such pressures have resulted in the USA imposing quotas on a wide range of textile products produced by MEPZ which were earlier quota free. Thus, by 1988 29 categories of wearing apparel were brought under the quota system as against only 10 categories in 1984. The Multi Fibre Agreement (MFA) also continues to protect inefficient textile firms in the developing countries and this tendency poses a serious threat to countries like Mauritius.
 - v. Another serious threat to MEPZ emerges from the domestic environment. Even in those products where allocated quota is available, Mauritius has failed to make optimal utilisation of existing quotas. In fact, the average degree of quota utilisation by Mauritius has declined during the period 1985 to 1989.

Some of the weaknesses of Mauritian economy that would affect the prospects for continued expansion of MEPZ are as follows :

1. Mauritius continues to be vulnerable to external shocks.
2. MEPZ is highly dependent on the performance of the textile exports. There is a high degree of product concentration in MEPZ exports with wearing apparel accounting for more than four-fifths. Thus, the growth of MEPZ has not brought about the desired degree of diversification of Mauritian economy. It has only transformed Mauritius from a monocrop sugar dominated economy into a little more than a duo-product one. If due to some reasons Mauritian textile sector loses part of its competitiveness or preferential access to markets in EEC and USA, its repercussions on MEPZ and Mauritian economy in general could be quoted serious.
3. By the end of eighties Mauritius has started experiencing acute shortage of skilled labour as well as unskilled labour. Thus, a country which was proportionally facing the problem of surplus labour has transformed into a full employment economy facing shortages of labour. One of the consequences of such a situation has been a steadily mounting upward pressure on wage rates without there being any corresponding increase in productivity. Moreover, rapid expansion of manufacturing facility is extremely difficult under such condition.
4. Since 1989 Mauritius has been facing the problem of high rates of inflation. This has eroded part of the international competitiveness acquired by Mauritian products following depreciation of Mauritian Rupee in early 80's and mid-80's. Rising wages and rising prices of materials due to general inflation would ultimately create a situation in which Mauritian products would lose competitiveness especially in a situation where labour productivity is stagnant.

Thus, while Mauritian economy has several important strengths and is also benefitting from various opportunities provided by the global economic environment, it has also developed certain weaknesses and it is also facing some threats in recent years. The future scenario and macroeconomic strategy formulation in Mauritius will have to take cognizance of these factors.

Lome Convention

The first Lome Convention was signed in 1975. Currently the fourth Lome Convention is in force for the period March 1, 1990 to February 28, 2000. The cornerstone of this preferential trade agreement are the relatively free access of exports from ACP countries to the EEC market as well as the exemption of customs duty. Under Article 168 [1], the products which originate from 69 ACP countries (46 African countries, 15 Caribbean countries and 8 Pacific countries) enter the EEC free of customs duties or charges having equivalent effect. Article 169[1] further provides that no quantitative restrictions or measures having equivalent effect shall apply to imports of goods originating from ACP states. This convention bestows considerable advantages to Mauritius over non-ACP countries in that the latter's exports of textile and garments are liable to a 17% duty on entry into the EEC. Mauritius has successfully exploited this preferential treatment in the textile sector.

However, there are two specific provisions in the Lome Convention, designed to protect EEC domestic industries against external exemption, which constitute a major constraint to the exports of Mauritius. These are :

1. RULES OF ORIGIN clause - The objective of this clause is to ensure exports of ACP countries origin. This implies that (a) the products must be produced from inputs wholly produced in one or more ACP countries or (b) the goods are produced from imported inputs which have undergone sufficient transformation. Moreover, if the raw materials or intermediate products are from the EEC, and processed in an ACP country, the goods are deemed to have been wholly produced in the ACP state. However, the protocol of the convention is fairly bulky and complicated. The main obstacle relates to the definition of sufficient processing or transformation that would change the tariff heading of the products processed (Article 3[1] of Protocol I). In practice, many products may have undergone sufficient transformation for a change in tariff heading but are disqualified. To the extent that Mauritius is deficient in endogenous raw materials, the Rules of Origin pose serious difficulties particularly in the garments sector which would not satisfy the Rules of Origin if manufactured from imported fabrics from non-ACP/EEC sources. To overcome this constraint, Mauritius encouraged a process of vertical integration in the textile sectors through the introduction of such processes as spinning, weaving, dyeing, printing and finishing form to raise the value-added. With the success achieved in the textile sector, the magnitude of this constraint has considerably diminished. On the contrary, it is now in the interest of Mauritius to maintain the rigidity of the Rule of Origin for the textile sector. But the Rules of Origin constitute serious handicaps to efforts of industrial diversification. A case in point is the electronics sector where the Rules of Origin stipulate that all inputs have to be imported from the EEC or produced in the ACP countries. However, there exists the possibility of derogation.

2. SAFEGUARD CLAUSE : This clause seeks to ensure that EEC is protected against any large or sudden increase in ACP imports although in practice the EEC has never invoked this clause. But under LOME II, Mauritius had once voluntarily agreed to restrain exports of textile products to avert the possibility of the EEC resorting to safeguard clauses.

* Source : *Mauritius at Crossroads : The Industrial Challenges Ahead*, Ministry of Industry & Industrial Technology, Government of Mauritius, 1990.

Preferential Trade Area (PTA)

The Treaty for the establishment of Preferential Trade Area was signed in December 21, 1981 and entered into force on September 30, 1982. It sets out in 51 articles and 14 protocols, the legal and economic framework within which the member states of the Preferential Trade Area for Eastern and Southern African states (referred to as PTA) shall cooperate with the main objective of promoting the development of their economies through regional integration.

The PTA for Eastern and Southern African states covers an area of about 8.5 million sq. km. (27 per cent of the total of Africa) and currently consists of 19 countries. Forty-two per cent of the area is given as arable while 6 per cent is endowed with rivers and lakes but excludes the exclusive economic zones of island states which could be jointly exploited for irrigation, fisheries, hydropower and water transport development. Currently, less than 9 per cent of the arable land is under cultivation and only about 4 per cent of the available water is being utilised.

The human population of the PTA sub region is estimated at 175 million and increases on an average at 3 per cent per annum. The hydroelectric potential of the sub region is estimated at well over 700 billion kw per year. The countries of the sub region are rich in gold, diamonds, platinum, chrome and manganese. It has over 300 billion metric tons of phosphates, over 105 billion tons of iron ore deposits, over 60 billion tons of coal, over 170 cubic metres of natural gas, over 200 billion tons of petroleum and large quantities of uranium, nickel, copper and cobalt.

The ultimate objective of the PTA is to achieve sustained transformation of the nature of production of national economies, producing mainly unprocessed and semi-processed agricultural and mineral products, primarily for export to developed countries to high productivity and dynamic economies producing consumer and capital goods for national and sub-regional markets. The PTA is thus an instrument formulated for collective action in the generation of a process of self sustaining economic growth and development.

The treaty recognizes the fact that meaningful economic integration of the different PTA member states at different levels of economic development cannot be attained without restructuring their economies through cooperation in industrial development.

(a) According to the treaty, cooperation on industrial development will be to facilitate :

- (i) large scale capital and intermediate goods industries;
- (ii) food and agricultural industries; and
- (iii) consumer goods industries for the purpose of obtaining the economies of scale, reducing external dependence for the supply of industrial products and achieving greater complementarity of the economies of the member states.

(b) The methods of cooperation have been set out as :

- (i) the establishment of multinational enterprises;
- (ii) the establishment of joint industrial supporting institutions and infrastructural facilities;
- (iii) the encouragement of the rational and efficient use of existing as well as new industrial productive capacities, raw materials and other local resources through rationalisation and mutual sharing of resources where possible.

* Source : *Mauritius at Crossroads : The Industrial Challenges Ahead*, Ministry of Industry & Industrial Technology, Government of Mauritius, 1990.

- (iv) the promotion of the joint development of industrial research, skills and modern technology as well as the dissemination and exchange of related information; and
 - (v) ensuring that all the Member States gradually derive the greatest benefit and economic advantages from cooperation in industrial development.
- (c) Joint venture investments should be effected at state to state level, state to national (juridical and natural) level and national to national level. To facilitate joint ventures there is need for the PTA member states to agree on a common and preferential treatment of such ventures in relation to the movement of capital, benefits and incentives, remittances of profits and dividend, accessibility to credit, etc.

The provisions of the PTA treaty merely set out a legal economic framework within which the objectives of the PTA are to be achieved. These provisions have been concretized into programmes of action in the main economic sectors of trade, customs and monetary affairs; transport and communications; agriculture and industry. The PTA provides for eventual elimination of customs duties, modalities relating to rules of origin, clearing and payment arrangements, transport, communication, trade agriculture and industrial development, etc.

The Quota System

The US Government imposes quota restrictions on the import of given category of clothing once the imports of that product from a country into US attains 1% of US production in that category. The US would then call on that country to hold bilateral negotiations. Fortunately, quotas are specified in volume terms, not money terms. This therefore, still leaves a country the choice to go for higher-value products. Moreover, under the agreement, provision is made for a 6% annual growth rate for the following years within the agreement period. The exception to this rule is for the wool categories for which the annual growth rate is 1%.

During the recovery period, a number of businessmen from Hong Kong, in particular those who could no longer export to the USA owing to quota restrictions, looked for a safer production haven. Mauritius initially benefitted from both the inflow of foreign capital and technical know-how. One implication is that demand for wearing apparel is to some extent a function of demand of the parent company in Hong Kong. Mauritius may not benefit to the full since the prices and the US market, additional items have been brought under quotas. Some 29 categories of wearing apparel are now under quotas against 10 categories in 1984-85. Quota in garments for exports to the US market is allocated as follows :

- (i) 90% is allocated to companies on the basis of past performance
- (ii) the remaining 10% is reserved for new comers and distributed equally among those who have orders in hand.

Thus, an exporter who has satisfied the performance criterion the preceding year would be entitled his previous year's quota plus the overall growth. Exporters who fail to meet 50% of their quota lose their quota in the following year, while exporters performing between 51 to 90% of the quota allocations would be entitled a quota equivalent to their export performance.

Exporters can surrender their quota, and if the surrender is effected six months prior to the agreement year, the exporters are deemed to have performed their quota and so do not lose their quota in subsequent years. The unused quota becomes available for distribution to new comers. The Ministry of Trade and Shipping had also a generous provision for firms working on a CMT basis to large enterprises. Actually the quota may be shared between the satellite firm and the large establishment actually effecting the export in the ratio of 75:25 based on the performance for May 1985 to April 1986. The latter formula did not meet with much success since many of the satellite firms lacking finance, experience and managerial skill or the marketing network of Hong Kong based firms failed to secure orders. Many even resorted to selling their quotas. In such cases the Ministry of Trade and Shipping revoked the quota allocations.

* Source : *Mauritius at Crossroads : The Industrial Challenges Ahead*, Ministry of Industry & Industrial Technology, Government of Mauritius, 1990.

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<i>Exhibit 1</i> <i>Selected Socio-economic Indicators for Mauritian Economy, 1990</i>	
<i>Per Capita GNP (US \$)</i>	<i>2600</i>
<i>Population (000)</i>	<i>1036.8</i>
<i>Total Area (sq. km)</i>	<i>1865</i>
<i>Density (persons per sq. km)</i>	<i>556</i>
<i>Labour Participation rate (%)</i>	<i>41.5</i>
<i>Share of Agriculture in Employment (%)</i>	<i>16.8</i>
<i>Birth Rate (Per 1000)</i>	<i>20.8</i>
<i>Death Rate (Per 1000)</i>	<i>6.9</i>
<i>Infant Mortality Rate (Per 1000)</i>	<i>19.5</i>
<i>Life expectancy at birth (Years)</i>	<i>68</i>
<i>Literacy rate (%)</i>	<i>90</i>
<i>Number of Doctors (Per 10,000)</i>	<i>10</i>
<i>Number of beds in Government Hospitals (Per 1000)</i>	<i>2.8</i>
<i>Number of Registered Vehicles (per 100)</i>	<i>10</i>
<i>Number of Telephones (Per 100)</i>	<i>5</i>
<i>Average annual per capita electricity consumption (Kwh)</i>	<i>950</i>
<i>Length of Roads (Kms)</i>	<i>1801</i>
<i>Ratio of Exports to GDP (%)</i>	<i>48.2</i>
<i>Ratio of Imports to GDP (%)</i>	<i>63.7</i>
<i>Savings Rate (%)</i>	<i>22.2</i>
<i>Unemployment Rate (%)</i>	<i>2.5</i>
<i>Source : Ministry of Economic Development and Planning, Government of Mauritius.</i>	

Exhibit 2
Sectoral Composition of Gross Domestic Product and Related Aggregates

(MRs. Million at Current Factor Cost)

	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990
<i>Agriculture, Fishing and Mining</i>	929	1273	1547	1483	1755	2143	2532	2909	3094	3415	3855
<i>Manufacturing</i>	1127	1377	1560	1678	2183	2864	3830	4841	5627	6365	7450
<i>Electricity and Water</i>	209	188	260	245	296	397	462	490	517	577	540
<i>Construction</i>	561	588	625	655	690	775	880	1045	1370	1720	2185
<i>Tade, Restaurants and Hotels</i>	1050	1219	1290	1455	1640	1834	2300	2962	3785	4540	5390
<i>Transport, Storage and Communication</i>	837	997	1112	1230	1372	1510	1755	2075	2425	2915	3340
<i>Financing, Insurance and Real Estate</i>	1309	1517	1755	1890	2050	2190	2335	2482	2723	3150	3580
<i>Government Services</i>	952	1104	1275	1327	1379	1447	1560	2035	2680	2985	3360
<i>Other Services</i>	415	502	596	650	685	720	776	856	960	1172	1335
<i>Gross Domestic Product at factor cost</i>	7389	8765	10020	10613	12050	13880	16450	19695	23181	26839	31070
<i>Indirect Taxes (Net of subsidies)</i>	1308	1444	1705	2150	2310	2738	3250	3881	4622	5176	5875
<i>Gross Domestic Product at Market Prices</i>	8697	10209	11725	12763	14360	16618	19700	23576	27803	32015	36945
<i>Net factor income from rest of the world</i>	-178	-408	-498	-485	-626	-700	-729	-538	-593	-303	-170
<i>Gross National Product at factor cost</i>	7211	8357	9522	10128	11424	13180	15721	19157	22588	26536	30900

Source : Central Statistical Office, Government of Mauritius.

Exhibit 3									
Sectoral Composition of Gross Domestic Product and Related Aggregates									
<i>(MRs. Million at Constant 1982 prices)</i>									
	1982	1983	1984	1985	1986	1987	1988	1989	1990
<i>Agriculture, Fishing and Mining</i>	1547	1348	1358	1509	1670	1633	1544	1414	1564
<i>Manufacturing</i>	1560	1576	1768	2038	2450	2795	3030	3112	3330
<i>Electricity and Water</i>	260	243	267	315	343	360	372	415	425
<i>Construction</i>	625	633	646	698	768	834	978	1086	1206
<i>Trade, Restaurants and Hotels</i>	1290	1373	1455	1527	1677	2010	2247	2415	2549
<i>Transport, Storage and Communication</i>	1112	1151	1209	1260	1345	1465	1606	1727	1822
<i>Financing, Insurance and Real Estate</i>	1755	1812	1872	1935	1993	2070	2157	2270	2374
<i>Government Services</i>	1275	1300	1320	1330	1343	1383	1439	1491	1543
<i>Other Services</i>	596	627	646	652	675	710	753	802	834
<i>Gross Domestic Product at factor cost (MRs.'000)</i>	10020	10063	10541	11264	12264	13260	14006	14535	15458

Note : Figures for 1989 and 1990 are provisional.
Source : Central Statistical Office, Government of Mauritius.

Exhibit 4											
Employment in Large Establishments by Major Sectors											
<i>(Numbers in September in 000)</i>											
	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990
<i>Agriculture, Fishing and Mining</i>	58.10	57.10	56.90	56.00	53.70	52.90	52.20	50.20	50.00	48.00	47.00
<i>Manufacturing</i>	36.40	37.20	37.10	38.30	48.60	62.90	83.90	99.90	105.50	107.80	107.80
<i>Electricity and Water</i>	4.50	4.40	4.40	4.10	3.90	3.80	3.70	3.60	3.50	3.50	3.40
<i>Construction</i>	7.40	6.30	5.60	4.40	4.10	5.00	6.40	8.70	9.30	9.90	11.10
<i>Trade, Restaurants and Hotels</i>	9.20	9.00	9.00	8.90	8.90	9.20	10.10	11.90	13.20	14.50	17.40
<i>Transport, Storage and Communication</i>	8.10	8.20	7.90	8.00	8.50	8.70	9.10	10.00	11.30	12.00	13.30
<i>Government Services (incl Finance, Insurance and Real Estate)</i>	54.50	54.90	55.00	54.90	55.10	55.10	54.70	54.80	54.70	54.90	66.80
<i>Other Services</i>	19.40	19.20	19.40	19.20	17.80	17.80	18.20	20.60	21.50	22.50	12.70
Total	197.60	196.30	195.10	193.80	200.60	215.40	238.30	259.70	271.20	273.20	279.50

Source : 1. Bank of Mauritius, Annual Report 1990
2. Mauritius Chamber of Commerce and Industry, Annual Report 1990.

Exhibit 5										
Trends in Budget Deficit and Related Aggregates										
<i>(MRs. Million)</i>										
	1981-82	1982-83	1983-84	1984-85	1985-86	1986-87	1987-88	1988-89	1989-90	1990-91
Tax Revenue	1956	2437	2803	2993	3503	4317	5516	6656	7460	8689
Non-tax Revenue	268	366	267	403	395	624	625	557	609	543
Total Revenues	2224 (19.0)	2803 (22.0)	3070 (21.4)	3396 (20.4)	3898 (19.8)	4939 (20.9)	6141 (22.1)	7213 (22.4)	8068 (21.4)	9232 (21.9)
Current Expenditures	2891	3222	3393	3691	3938	4273	5298	6518	7739	8507
Capital Expenditure	444	360	349	585	567	935	1142	1110	1534	1734
Net Lending	341	402	237	110	266	216	204	603	85	60
Total Expenditures	3676 (31.4)	3984 (31.2)	3979 (27.7)	4386 (26.4)	4771 (24.2)	5424 (23.0)	6644 (23.9)	8231 (25.6)	9358 (24.8)	10301 (24.4)
Current Account Deficit/Surplus	-667	-419	-323	-295	-40	666	843	695	329	725
Overall Deficit/Surplus	-1452 (-12.4)	-1181 (-9.3)	-909 (-6.3)	-990 (-6.0)	-873 (-4.4)	-485 (-2.1)	-503 (-1.8)	-1018 (-3.2)	-1290 (-3.4)	-1069 (-2.5)
External Financing	866	-152	-88	887	119	336	816	-433	65	12
Domestic Financing	587	1333	997	103	754	149	-313	1451	1225	1057

Note : 1990-91 figures are Estimates.
Figures in Parantheses are per cent to GDP at market prices
Source : Annual Reports of the Bank of Mauritius.

Exhibit 6								
Balance of Payments Summary 1976-77 to 1989-90								
<i>(MRs. Million)</i>								
Year	Exports (FOB)	Imports (FOB)	Merchandise Balance	Services (net)	Transfers (net)	Current Account Balance	Capital Account Balance*	Overall Balance of Payments
1976-77	1947	2220	-273	-214	36	-451	44	-407
1977-78	2029	2523	-494	-223	89	-628	423	-205
1978-79	2202	2664	-462	-253	82	-633	128	-505
1979-80	2904	3533	-629	-300	116	-813	311	-502
1980-81	2877	4243	-1366	-250	192	-1424	471	-953
1981-82	3853	4255	-402	-447	232	-617	219	-398
1982-83	3844	4387	-543	-409	348	-604	339	-265
1983-84	4790	5080	-290	-452	320	-422	38	-384
1984-85	5766	6272	-506	-606	509	-603	1001	398
1985-86	7539	7529	10	-494	660	176	467	643
1986-87	10467	9651	816	81	678	1575	997	2572
1987-88	12377	14558	-2181	116	1099	-966	3694	2728
1988-89	14493	16137	-1644	337	1193	-114	2110	1996
1989-90 (Provisional)	15766	20019	-4253	1019	1259	-1975	5016	3041

**Including Errors & Omissions.*
Source : Annual Reports of Bank of Mauritius.

Exhibit 7				
Trends in Foreign Exchange Rates of Mauritian Rupee				
<i>(MRs. per unit of Foreign Currency)</i>				
<i>Year</i>	<i>U.S.A. (MRs./\$)</i>	<i>United Kingdom (MRs./Pd.Stg.)</i>	<i>France (MRs./Fr.)</i>	<i>Germany (MRs./DM)</i>
1983	11.91	17.86	1.56	4.64
1984	13.95	18.47	1.60	4.91
1985	15.58	20.03	1.74	5.33
1986	13.27	19.87	1.96	6.30
1987	13.01	21.20	2.15	7.26
1988	13.59	24.07	2.27	7.75
1989	15.36	24.83	2.44	8.31
1990	15.28	25.82	2.67	9.07

Source : Annual Reports of Bank of Mauritius.

Exhibit 8		
Trends in Foreign Exchange Reserves in Mauritius		
<i>Year</i>	<i>Forex Reserves at the end of June (MRs. Million)</i>	<i>Forex Reserves in terms of Weeks of Imports</i>
1975	598.5	15.60
1976	776.1	16.75
1977	369.5	6.51
1978	485.5	8.21
1979	224.9	3.22
1980	243.7	2.68
1981	205.8	2.14
1982	460.4	4.74
1983	457.0	4.59
1984	546.4	4.38
1985	852.0	5.46
1986	1307.9	7.39
1987	3193.1	12.73
1988	5547.3	16.52
1989	6995.8	17.99
1990	10268.9	22.23

Source : Annual Reports of Bank of Mauritius.

Exhibit 9					
Sources of Foreign Investments in Mauritian Export Processing Zone					
<i>(MRs. '000)</i>					
<i>Sources</i>	<i>1986</i>	<i>1987</i>	<i>1988</i>	<i>1989</i>	<i>1990</i>
<i>Australia</i>	--	6,505	1,000	--	4,500
<i>China</i>	--	--	20,469	6,018	13,354
<i>France</i>	4,359	7,572	13,252	31,937	57,948
<i>Germany</i>	3,464	500	1,785	49,663	3,761
<i>Holland</i>	--	--	--	2,200	--
<i>Hong Kong</i>	23,939	10,295	119,949	19,407	54,636
<i>India</i>	100	1,015	1,495	585	--
<i>Italy</i>	698	--	--	6,681	294
<i>Pakistan</i>	--	--	--	1,700	31
<i>Seychelles</i>	--	--	2,000	2,625	--
<i>Singapore</i>	--	400	1,000	5,300	--
<i>South Africa</i>	7,580	2,420	360	1,598	250
<i>Switzerland</i>	--	--	--	3,929	18,640
<i>Taiwan</i>	1,400	12,571	1,825	13,338	62,647
<i>United Kingdom</i>	3,141	6,466	12,387	28,698	7,218
<i>U.S.A.</i>	550	15,175	--	--	--
<i>Zimbabwe</i>	--	--	--	2,203	375
<i>Others</i>	28,174	126,284	68,362	122,667	46,541
TOTAL	73,405	189,203	235,864	298,549	270,195

Source : Mauritius Export Development and Investment Authority

Exhibit 10		
Export And Import Price Indices		
<i>(1982 = 100)</i>		
<i>Period</i>	<i>Price Indices</i>	
	<i>Export</i>	<i>Import</i>
<i>1982</i>	<i>100</i>	<i>100</i>
<i>1983</i>	<i>107</i>	<i>98</i>
<i>1984</i>	<i>119</i>	<i>110</i>
<i>1985</i>	<i>136</i>	<i>121</i>
<i>1986</i>	<i>144</i>	<i>98</i>
<i>1987</i>	<i>161</i>	<i>102</i>
<i>1988.</i>	<i>172</i>	<i>111</i>
<i>1989</i>	<i>191</i>	<i>132</i>

Source : Central Statistical Office, Government of Mauritius.

Exhibit 11				
Sugar Exports by Main Markets and Local Sales,				
Crop Year 1986-87 to 1989-90				
Destination/Item	1986-87	1987-88	1988-89	1989-90
E.E.C.				
<i>Quantity (000 M/tons)</i>	505.0	507.2	514.7	506.3
<i>Value (MRs. Mn.)</i>	3656.2	4055.8	4159.0	4515.2
<i>Average Price (MRs./Ton)</i>	7219	7988	8064	8900
U.S.A.				
<i>Quantity (000 M/tons)</i>	9.5	7.3	15.3	15.9
<i>Value (MRs. Mn.)</i>	54.1	41.8	99.7	115.0
<i>Average Price (MRs./Ton)</i>	5674	5913	6500	7243
World Market				
<i>Quantity (000 M/tons)</i>	147.8	144.0	69.5	10.2
<i>Value (MRs. Mn.)</i>	272.4	392.0	293.0	97.5
<i>Average Price (MRs./Ton)</i>	1840	2696	4204	6002
Total Exports				
<i>Quantity (000 M/tons)</i>	662.8	658.5	599.2	532.4
<i>Value (MRs. Mn.)</i>	3982.7	4489.6	4551.7	4727.7
<i>Average Price (MRs./Ton)</i>	5998	6800	7576	8862
Local Sales				
<i>Quantity (000 M/tons)</i>	44.8	32.4	34.7	36.0
<i>Value (MRs. Mn.)</i>	115.9	89.2	94.3	99.1
<i>Average Price (MRs./Ton)</i>	2580	2743	2714	2748
<i>Source : Digest of Industrial Statistics 1990, Central Statistical Office, government of Mauritius (June 1991).</i>				

Exhibit 12 <i>Trends in the External Debt of Mauritius</i>							
(US \$ Million)							
	1980	1985	1986	1987	1988	1989	1990
Public and Publicly Guaranteed Long Term Debt	295	397	466	581	652	631	699
Private Non-Guaranteed Long Term Debt	24	15	22	46	57	106	106
Total Long Term Debt (% Share of World Bank & IDA Assistance in Long Term Debt)	319 (17.33)	412 (33.15)	468 (35.85)	627 (33.85)	709 (29.47)	737 (26.37)	805 (24.21)
IMF Credit	102	165	162	152	103	63	22
Net Short Term Debt	47	51	38	34	49	32	32
Total External Debt	468	628	668	813	861	832	860
Total External Debt as Per cent of GDP	41.31	58.36	45.64	45.53	44.20	40.09	34.92
Total Debt Service as Per cent of Exports	9.07	24.28	16.23	10.84	14.33	10.86	6.13

Source : Trends in Developing Economies, 1990 and 1991, The World Bank.

Exhibit 13 <i>Trends in Money Supply and Related Indicators</i>									
(MRs. Million)									
	1982	1983	1984	1985	1986	1987	1988	1989	1990
Money (M_1)	1742	1806	1738	2041	2436	3304	3821	4514	5580
Quasi-Money	3185	3622	5022	6146	8085	10351	13748	15765	18990
Money and Quasi-Money (M_2)	4927	5428	6760	8187	10521	13655	17569	20279	24570
M_1 as % of GDPMP	14.9	14.2	12.1	12.3	12.4	14.0	13.7	14.0	14.8
M_2 as % of GDPMP	42.0	42.5	47.1	49.3	53.4	57.9	63.2	63.1	65.2
Velocity	2.4	2.4	2.1	2.0	1.9	1.7	1.6	1.6	1.5
Rate of Inflation (CPI)	11.5	5.6	7.4	6.7	1.8	0.5	9.2	12.6	13.5
Nominal Interest Rate (Saving Deposits)	9.0	9.0	8.5	8.5	8.5	8.0	8.0	10.0	12.0
Real Interest Rate (Saving Deposits)	-2.5	3.4	1.1	1.8	6.7	7.5	-1.2	-2.6	-1.5
Nominal Interest Rate (Time Deposits)	12.0	14.0	12.0	12.0	12.0	11.0	11.0	12.0	13.5
Real Interest Rate (Time Deposits)	0.5	8.4	4.6	5.3	10.2	10.5	1.8	-0.6	0.0
Nominal Growth of GDPMP	14.8	8.9	12.5	15.7	18.5	19.7	17.9	15.6	17.3
Nominal Growth of M_1	13.6	3.7	-3.8	17.4	19.4	35.6	15.6	18.1	23.6
Nominal Growth of M_2	23.4	10.2	24.5	21.1	28.5	29.8	28.7	15.4	21.2

Note: M_1 : Money supply -> currency held by the public plus demand deposits of the banking system.
 Quasi-Money : -> Savings and time deposits of the banking system.
 M_2 : Aggregate Monetary Resources -> M_1 + Quasi-Money.
 Sources : Annual Reports of Bank of Mauritius.

Exhibit 14								
Trends in Aggregate Employment, Unemployment and Labour Productivity								
	1983	1984	1985	1986	1987	1988	1989	1990
Population (000)	968.6	993.8	1003.8	993.8	1003.8	1016.6	1026.8	1036.8
Total Working Force (000)	279.3	302.3	336.2	366.5	389.6	418.0	425.6	440.7
Employment (in large establishments) (000)	193.8	200.6	215.4	238.3	259.7	271.2	273.2	279.5
Other Working Force (000)	85.5	101.7	120.8	128.2	129.9	146.8	152.4	161.2
Total Unemployment (000)	70.7	65.9	58.4	49.5	39.0	22.0	15.4	11.3
Total Labour Force (000)	350.0	368.2	394.6	416.0	428.6	440.0	441.0	452.0
Unemployment Rate(%)	20.2	17.9	14.8	11.9	9.1	5.0	3.5	2.5
Labour Productivity (at current prices) (MRs.000)	37998.6	39861.1	41284.9	44884.0	50551.9	55457.0	53322.4	71477.2
Labour Productivity at constant 1982 prices (MRs.000)	36029.3	34869.4	33503.9	33462.5	34034.9	33491.1	34151.8	35076.0

Note : Labour productivity is measured as the ratio of GDP at factor cost to total working force.
Source : Ministry of Economic Development and Planning, Mauritius.

Exhibit 15							
Growth of the Mauritian Export Processing Zone							
	1982	1985	1986	1987	1988	1989	1990
No. of Enterprise	115	290	408	531	591	563	568
Employment	23500	50047	70519	85685	89080	88650	88258
Value Added at Current Factor Cost (MRs. Mn.)	449	1333	1900	2585	3125	3450	4079
Total investment at Current Prices (MRs.Mn.)	38	340	560	655	870	900	750
Exports (MRs.Mn.)	1236	3283	4960	6567	8179	9057	11474
Imports (MRs.Mn.)	743	2530	3837	4800	5890	7502	7348
Share of EPZ Sector (%) :							
EPZ employment in total employment	12.0	14.5	18.8	20.9	21.3	20.8	20.5
EPZ employment in manufacturing employment	63.4	49.5	53.5	54.3	54.3	52.8	53.2
EPZ Value Added in GDP	4.5	9.6	11.6	13.1	13.5	12.8	13.1
EPZ Value Added in Manufacturing Value Added	28.8	46.5	49.6	53.4	55.5	54.2	54.6
EPZ investment in GDFCF	1.8	11.0	14.4	12.9	10.9	10.9	8.3
EPZ investment in manufacturing investment	12.1	45.9	52.3	44.9	46.4	42.2	35.0
EPZ exports in total exports	31.0	50.2	52.6	55.1	59.0	58.4	63.6
EPZ imports in total imports	14.7	31.2	42.0	36.8	33.7	37.1	30.7

Source : 1. *Digest of Industrial Statistics, 1990*, Central Statistical Office, Government of Mauritius.
2. *Mauritius at Crossroads*, Ministry of Industry and Industrial Technology, Government of Mauritius

Exhibit 16
Exports of Selected Commodities of EPZ Industries (1982-1990)

<i>Mrs. Mn.</i>									
<i>Product Group</i>	1982	1983	1984	1985	1986	1987	1988	1989	1990
<i>Fish and Fish Preparation</i>	47	68	99	115	97	100	173	190	142
<i>Textile Yarn, Fabrics, Made-up Articles</i>	89	66	78	86	101	138	180	361	444
<i>Articles of Apparel and clothing accessories</i>	877	921	1584	2539	4012	5407	6446	7038	9096
<i>Optical Goods, nes</i>	29	33	60	82	90	90	88	133	125
<i>Watches and clocks</i>	38	65	84	146	246	337	563	500	629
<i>Pearls, precious and semi-precious stones</i>	52	49	89	127	172	185	302	325	354
<i>Jewellery, gold-smühs' and silversmühs' wares</i>	27	31	48	58	82	65	69	80	155
<i>Toys, games and sporting goods</i>	30	34	50	44	57	78	85	90	124
<i>Others</i>	46	40	59	86	94	167	270	340	373
Total	1235	1307	2151	3283	4951	6567	8176	9057	11442

Source : Mauritius Export Development and Investment Authority

Exhibit 17
Percentage Distribution of EPZ Firms and Employment

<i>Product Group</i>	<i>Firms</i>		<i>Employment</i>	
	1983	1990	1983	1990
<i>Textiles</i>	5.5	5.4	5.4	4.8
<i>Wearing Apparel</i>	43.8	60.2	80.0	84.8
<i>Flowers</i>	10.3	7.5	0.6	0.6
<i>Leather Product/Footwear</i>	3.4	2.3	1.1	1.6
<i>Wood, Furniture and Paper</i>	2.7	2.8	1.9	0.6
<i>Optical Goods</i>	1.4	0.9	0.7	0.6
<i>Watches and Clocks</i>	4.1	1.0	1.5	1.0
<i>Jewellery</i>	6.2	3.3	2.7	1.5
<i>Toys and Carnival Articles</i>	4.1	1.4	2.1	1.1
<i>Other</i>	18.5	15.2	4.0	3.4
Total	100.0	100.0	100.0	100.0

Source : Ministry of Industry and Industrial Technology, Government of Mauritius.

Exhibit 18 Distribution of Mauritian EPZ Firms and Employment by Size						
Size of Employment	1982			1990		
	Firms		Employment	Firms		Employment
	No.	No.	%	No.	No.	%
<i>Less than 50</i>	47	871	3.7	299	6142	6.9
<i>51 - 100</i>	18	1179	5.0	77	5377	6.1
<i>101 - 300</i>	28	4051	17.3	105	19256	21.8
<i>301 - 500</i>	11	4270	18.2	37	11745	13.3
<i>501 - 1000</i>	9	5330	22.7	33	21127	24.0
<i>More than 1000</i>	5	7775	33.1	15	24611	27.9
	118	23476	100.0	566	88258	100.0

Source : Mauritian Export Development and Investment Authority.

Exhibit 19 Number of Closures in the EPZ for the Period 1978-1990					
Period	No. of New EPZ firms starting operation	No. of EPZ Closures	Net Additions	Total No. of EPZ firms	Proportion of Closures (Per cent)
1978	12	15	-3	85	17.6
1979	16	7	9	94	7.4
1980	10	4	6	100	4.0
1981	18	10	8	107	9.3
1982	20	8	12	118	6.8
1983	57	17	40	146	11.6
1984	54	6	48	195	3.1
1985	101	6	95	290	2.1
1986	139	21	118	408	5.1
1987	141	20	121	531	3.8
1988	95	38	57	591	6.4

Source : Mauritius at Crossroads, Ministry of Industry and Industrial Technology, Mauritius.

Exhibit 20 Main EPZ Exports by Destination, 1988			
(Percentage Shares)			
	E.E.C	U.S.	Others
Garments	70.8	21.6	7.7
Textiles	54.0	37.5	8.5
Knitwear	86.5	6.6	6.9
Tuna	99.2	0.0	0.8
Yarn	84.4	0.0	15.6
Diamonds	68.7	4.7	26.6
Leather Goods	92.4	0.0	7.6
Spectacles and Goggles	17.1	63.0	19.9
Watches	86.8	0.0	13.2
Toys	97.8	0.0	2.2
Total	75.1	20.5	4.4

Source : World Bank Country Study on Mauritius.

Exhibit 21 Production Account of the EPZ Sector by Product Groups, 1989					
(MRs.Million)					
	Gross Output at Producers' Value	Intermediate Consumption	Value Added at Factor Cost	Compensation of Employees	Gross Operating Surplus
Food Products	246.2	195.8	50.4	26.8	23.6
Textile Yarn and Fabrics	924.4	603.2	321.2	119.2	202.0
Wearing Apparel	8156.0	591.2	2564.8	1415.4	1149.4
Leather Products	177.3	111.3	66.0	31.5	34.5
Wood and Furniture	33.7	13.7	20.0	10.4	9.6
Paper Products	24.6	14.0	10.6	4.8	5.8
Rubber and Plastic Products and Chemicals	96.2	68.7	27.5	5.9	21.6
Metal Products, Non-electrical Machinery and Electrical Machinery	37.7	23.2	14.5	5.0	9.5
Watches, clocks and optical goods	619.9	430.2	189.7	61.6	128.1
Jewellery	410.7	292.6	118.1	50.0	68.1
Other Products	161.1	93.9	67.2	34.4	32.8
Total	10887.8	7437.8	3450.0	1765.0	1685.0

Source : Digest of Industrial Statistics 1990, CSO, Government of Mauritius, June 1991.

Exhibit 22 Value Added, Employment and Productivity in EPZ Sector by Main Product Groups					
Item/Sector	1986	1987	1988	1989	1990
Value Added (MRs. Mn.)					
Textile Yarn & Fabrics	136.5	173.9	271.3	321.2	378.9
Wearing Apparel	1498.3	2058.5	2361.5	2564.8	3025.7
Watches, Clocks and Optical Goods	99.7	130.2	176.0	189.7	223.8
Jewellery and Related Articles	50.6	62.6	104.0	118.1	139.3
Other Products	114.8	159.8	212.2	256.2	302.3
Total	1899.9	2585.0	3125.0	3450.0	4070.0
Employment					
Textile Yarn & Fabrics	2631	3514	4171	4445	4360
Wearing Apparel	56879	70128	76667	74738	73263
Watches, Clocks and Optical Goods	1014	1258	1433	1502	1455
Jewellery and Related Articles	928	1029	1345	1623	1471
Other Products	3224	3621	3976	4674	4605
Total	64676	79550	87592	86982	85154
Productivity (MRs.000)					
Textile Yarn & Fabrics	51.9	49.5	65.0	72.3	86.9
Wearing Apparel	26.3	29.4	30.8	34.3	41.3
Watches, Clocks and Optical Goods	98.3	103.5	122.8	126.3	153.8
Jewellery and Related Articles	54.5	60.8	77.3	72.8	94.7
Other Products	35.6	44.1	53.4	54.8	65.6
Total	29.4	32.5	35.7	39.7	47.8

Note : 1. Employment indicates mid-year average.
2. Value added is at current factor cost.

Source : Digest of Industrial Statistics 1990, CSO, Government of Mauritius, June 1991.

Exhibit 23 Trends in Labour Productivity in Manufacturing and EPZ Sectors (1982 = 100)						
	Manufacturing Sector (including Sugar)			EPZ Sector		
	Production Index	Employment Index	Productivity Index	Production Index	Employment Index	Productivity Index
1982	100	100	100	100	100	100
1983	100	107	93	109	112	97
1984	113	134	84	145	165	88
1985	133	173	77	188	240	78
1986	153	216	71	254	319	80
1987	180	248	72	310	376	82
1988	197	256	77	347	385	90
1989	205	261	78	367	383	96
1990	220	264	83	400	375	107

Source : Digest of Industrial Statistics 1990, Central Statistical Office, Government of Mauritius, June 1991.

**Exhibit 24
Direction of Exports and Imports**

(MRs. Million)

	1986	1987	1988	1989	1990
Exports (F.O.B.)					
France	2121	2945	3025	2986	3981
Germany	660	907	1273	1391	1528
Italy	208	300	505	570	793
United Kingdom	3405	4076	4808	5384	6289
United States of America	1457	1699	1785	2076	2307
Other	1212	1570	2069	2642	2671
Total Exports	9063	11497	13465	15049	17569
E.E.C.	7010	9095	10622	11583	13997
Other Preferential Tariff Countries	1882	2271	2307	2835	2993
General Tariff Countries	171	131	536	631	579
Imports (c.i.f.)					
China	447	692	671	1000	810
France	1248	1699	2133	2746	3525
Germany	531	733	902	1462	1690
Hong Kong	626	822	942	971	932
India	281	492	643	759	1012
Japan	636	1279	1281	1843	1454
South Africa	910	1110	1482	1817	2110
Taiwan	414	685	765	1073	1123
United Kingdom	686	1058	1259	1284	1702
United States of America	163	227	2078	321	1102
Other	3148	4245	5091	6941	8559
Total Imports	9090	13042	17247	20217	24019
E.E.C.	3247	4281	5350	6923	8644
Other Preferential Tariff Countries	3010	4071	6991	6263	8253
General Tariff Countries	2833	4690	4906	7031	7122

Source : Central Statistical Office, Government of Mauritius

Chapter 8

Export Promotion Strategy and Trade Policy Reforms in Sri Lanka

I. Introduction

Major changes in global economic environment during the last two decades have induced many developing countries to re-examine their economic policies and bring about significant strategic shifts in their economic management. In most cases, there has been an attempt to move away from a relatively inward looking economic regime marked by various types of controls and dominance of state owned enterprises to an outward looking liberalised economy in which the private sector is expected to play a dominant role. Two successive oil shocks of the seventies have dealt a severe blow to the balance of payments position of many low income countries and the urgent need to tackle the resulting economic crisis seems to have hastened the process of economic liberalisation in several developing countries.

One of the main elements of this economic transition in developing countries has been a distinctive strategic shift from import substitution-based development strategy to export-led growth strategy. Among the developing Commonwealth countries which have attempted this kind of strategic shift in recent years, Sri Lanka can be regarded as an early starter. In Sri Lanka, the process of economic liberalisation and re-orientation of economic strategy commenced as early as in 1977. Hence, it would be interesting to examine Sri Lanka's experience with regard to export promotion and trade policy reforms to gain insights into some of the issues involved in the formulation and implementation of export-led growth strategy.

II. The Background

During the last five decades, Sri Lanka has completed a full circle with regard to its broad economic policy. In late 40's, Sri Lanka was a free market economy fully based on the principle of *laissez-faire*. After gaining Independence in 1948, Sri Lanka started moving towards a regime of controls which progressively tightened during the fifties and sixties and culminated in two decades of highly controlled and strictly regulated economic regime dominated by state enterprises (1958 to 1977). Significant economic deterioration experienced during this period led to a sharp turnaround in economic policy in 1977 which marked the beginning of Sri Lanka's journey back towards economic liberalisation and by the end of 1991 Sri Lanka had already travelled a long distance towards *laissez-faire* to emerge as a highly liberalised market oriented economy (Hettiarachchi, 1991). However, in this process Sri Lanka's relative economic position vis-a-vis other countries in South-East

Asia deteriorated considerably. In early 50's, Sri Lanka's per capita income was about half of Japan's, about the same as Malaysia's and significantly higher than that of Korea and Thailand. Now in early 90's, Sri Lanka's per capita income is less than 5% of Japan's, less than a fifth of Malaysia's and considerably below that of South Korea and Thailand (World Bank, 1992). Since Sri Lanka enjoyed a relatively high living standard in early 50's, several of its socio-demographic indicators such as life expectancy at birth, literacy rate, infant mortality rate, etc., were significantly higher than most developing countries at that time. While inadequate economic growth during the subsequent period has affected the development of the country's broad socio-economic profile, some of the socio-economic indicators of Sri Lanka are still significantly higher than those of many developing countries in early nineties and especially the health indicators are comparable to those of several middle income countries (see Exhibit 1).

During the initial years of the post-independence period, Sri Lanka's balance of payments was under severe pressure which led to a sharp decline in its foreign exchange reserves. Given the fixed exchange rate system which prevailed during that period, the government tried to achieve the required balance of payment adjustments by introducing the regime of controls. Accordingly the exchange controls and import restrictions were introduced in Sri Lanka for the first time in August 1957. However, the situation worsened during the subsequent period and by 1960, Sri Lanka faced the first severe foreign exchange crisis with the foreign exchange reserves falling sharply to the low level of Rs. 458 million indicating a sizeable loss of Rs. 521 million during 1958-60 (Hettiarachchi, 1991). Such a low level of external reserves was not considered good enough to support a sustained and large inflow of imports and, therefore, the government tightened import controls through various instruments such as import licensing, quota restrictions, significantly higher import duties, etc. Since all these measures failed to improve the BOP position, more controls and restrictions were clamped and by December 1964 the system of open general licence virtually ceased to operate and the entire range of private sector imports was brought under import licensing restrictions. Thus, by mid-sixties, the country's BOP was managed through the system of an implicit foreign exchange budget (Hettiarachchi, 1991). Finally when all these attempts failed to produce the desired results, the Sri Lankan rupee was devalued by 20% in November 1967 and a new scheme called, "The Foreign Exchange Entitlement Certificate Scheme" (FEEC) was introduced in May 1968. The FEEC scheme was in effect a dual exchange rate system under which one category of foreign exchange transactions were carried out at the official exchange rate while another category of transactions were carried out at a higher exchange rate which consisted of the official exchange rate plus the premium on FEEC. This measure was aimed at promoting and diversifying exports and simultaneously relaxing import controls, but it could not function effectively because the system of imports under OGL which was reintroduced in May 1968 was again abolished in August 1970 and all imports during the period from 1970 to 1977 continued to be governed by individual licensing and quota restrictions. The net impact of such strict regime of import controls and restrictions was felt in terms of severe shortages of essential consumer goods and the emergence of black markets for both foreign exchange as well as imported goods (Hettiarachchi, 1991). Moreover, it created an economic climate that discouraged foreign investment. Per capita income measured in real terms was virtually stagnant during 1970-77 and the rate of unemployment exceeded 20% of the working force.

In the Parliamentary elections held in July 1977, the ruling party, viz., the Sri Lankan Freedom Party (SLFP) suffered a stunning defeat with its strength in the Parliament reduced from 91 seats to only 8 seats and the United National Party (UNP) stormed into power by an unprecedented majority. In November 1977, the UNP came up with a new economic policy which aimed at transforming the Sri Lankan economy from an inward looking closed economy managed through administrative controls and regulations to a growing economy that was outward looking and market oriented.

On the political front, substantial changes in the governmental system were made by a new Constitution adopted in 1978, which introduced the Presidential system of government with the President becoming Head of the State and the Head of the Executive and the powers of the Prime Minister and Cabinet being drastically reduced. Mr. Jayewardene became the first President under the

1978 Constitution with Mr. Ranasinghe Premadasa as the Prime Minister. Subsequently, the life of the 1977 Parliament was extended through a Referendum held in 1982, to August 1989. Mr. Jayewardene's Presidency was also extended for a second term (EIU, 1992). While the economic policy reforms introduced during the 1977-82 were partially successful in accelerating economic growth and promoting employment generation and investment, the Sri Lankan economy continued to be characterised by bureaucratic intervention and a relatively high degree of State involvement in economic activity. Almost half of the industry remained in the public sector and in the plantation sector, two large state corporations accounted for nearly two-thirds of tea production, one-third of rubber production and one-tenth of coconut production (EIU, 1992). Moreover, returns on public sector investment were low and fiscal imbalances grew during this period. In December 1988, Mr. Premadasa (UNP) was elected as the President. Under his leadership, a new and more rigorous liberalisation programme was launched in 1989. Full liberalisation of the external sector, new thrust on export promotion and privatisation of state-owned enterprises were the main elements of the new liberalisation package.

The pace of liberalisation programme and economic policy reforms slowed down during mid-eighties. This was partly due to the outbreak of ethnic disturbances in the northern and eastern provinces in 1983 which continued unabated during the subsequent years and partly also because several favourable external factors enabled the government to postpone tough policy decisions during that period. During the first half of eighties, Sri Lanka had easy access to sizeable aid from donor countries, especially the aid consortium of western countries and the government was also able to tap concessional as well as commercial sources of external finance. In fact, continued inflow of significant volumes of foreign aid has played a crucial role in averting BOP crisis in Sri Lanka during the eighties. Moreover, there was a boom in tea prices in 1984 and there was also a significant inflow of remittances from Sri Lankan workers which eased the pressure on BOP (World Bank, 1992).

During the period 1983-1991, Sri Lanka completed the implementation of an eight-year programme supported by IMF's structural adjustment facility. The initial phase of this programme could not achieve the desired degree of success. However, the new government formed in April 1989 formulated a special programme for 1989-1992 with IDA and IMF support, which focussed on the need to restore economic stability in the short term and resuming the structural adjustment effort in the medium term (World Bank, 1992). The new government was fully committed to this package of structural reforms with a special sense of urgency, especially in view of the serious balance of payment crisis that loomed large on Sri Lankan economy in 1989. The sudden spurt in terrorist activities in the southern part by the Janata Vimukthi Peramuna (JVP) disrupted normal life and caused a tremendous setback in Sri Lanka in 1989. In fact during the second half of 1989, the economy reached a stage where its foreign exchange reserves were not enough to finance even one day's imports (Karunatilake, 1991). It was under such difficult conditions marked by unprecedented economic adversities and grave ethnic disturbances that the new government had to act decisively and launch another phase of liberalisation programme. The new phase of structural reforms achieved a reasonable degree of success during 1989-1992 and to sustain the economic revival, the IMF approved in September 1991 loans aggregating US \$ 455 million to be disbursed over a three-year period under the Enhanced Structural Adjustment Facility (ESAF) to support the government's structural reform programme during 1991-1994 period (FEER, 1992).

It would be interesting to examine the trends and pattern of Sri Lanka's economic growth during the post-1977 period. Exhibit 2 brings out the trends in Sri Lanka's GNP at current prices as well as at constant 1982 prices, while Exhibit 3 shows the pattern of sectoral growth rates during the post-1977 period. It is evident from Exhibit 3 that the growth rate of Sri Lanka's economy peaked to 7% per annum during the five year period following economic liberalisation in 1977 (1977-1982), but it dropped again to 3.9% during the subsequent five year period (1983-1988). However, it is interesting to observe that the growth rate of industrial sector showed significant acceleration to 6.3% during 1988-1988 from 3.7% observed during 1977-1982 (see Exhibit 3). In fact, the growth rate of industrial sector has improved further to 6.9% during post-1988 period and, as a result, the share of

manufacturing sector in GDP has increased from 14.5% in 1980 to over 18% by 1991 (see Exhibit 4). Thus, the process of economic liberalisation in Sri Lanka has helped the manufacturing sector to achieve significantly higher rates of growth during the last decade.

III. Trends in Balance of Payments

Like most LDCs, Sri Lanka experienced persistent deficits in the balance of payments. During the initial phase of economic liberalisation (1977 to 1980), Sri Lanka's balance of payments position deteriorated considerably. By 1980, the current account deficit increased sharply to 613 million SDRs (19.8% of GDP) from the initial low level of 121 million SDRs in 1978 (5.6% of GDP). This deterioration in the current account balance was mainly due to a significant surge in imports which was not accompanied by adequate growth of exports during the period 1978-1980. However, as shown in Exhibit 5, there was a significant improvement during the subsequent period and by 1984 the current account deficit declined to 249 million SDR (4.2% of GDP). The post-1988 period has again been marked by deterioration in BOP and this has imparted a sense of urgency to Sri Lanka's trade policy reforms and export promotion strategy. It is interesting to observe that the ratio of Sri Lanka's exports to imports was as high as 82% in 1978 which dropped to 52% by 1980 and again increased significantly to 70% in 1984 (see Exhibit 6). The deterioration in BOP experienced in recent years can be attributed to a decline in this ratio especially during 1988 and 1991.

To finance the persistent high levels of current account deficit, Sri Lanka has resorted to both short term as well as long term borrowings. Sri Lanka's external debt has increased from 3.4 billion SDRs in 1987 to 4.6 billion SDRs by 1991 (see Exhibit 7). However, since current account receipts have also increased rapidly from 1.6 billion SDRs in 1987 to 2.3 billion SDRs in 1991, the overall debt service ratio has actually declined from 23.2% in 1987 to 15.5% in 1991. Hence, the growing external debt of Sri Lanka is not likely to pose any serious problems in the medium term, but it could become a serious constraint in the long run if the growth of exports fails to accelerate during the 1990's.

IV. Trade Policy Reforms

The period of economic liberalisation in Sri Lanka which started from 1977 can be broadly divided into two sub-periods : the initial phase of partial liberalisation spread over the ten year period 1978-88, and the second phase of nearly full liberalisation which commenced from 1989. In both phases of liberalisation trade policy reforms constituted a major element of the package. During the first phase, a large number of trade-related controls were dismantled. Import quotas and restrictions were largely abolished (see SLEDB, 1985). Tariffs were lowered and rationalised. In November 1977, Sri Lankan rupee was devalued from Rs.9.1 to Rs.16.6 per US dollar (i.e., from SLR 1 = US \$ 0.11 to SLR 1 = US \$ 0.06), and the Foreign Exchange Entitlement Certificate Scheme (FEEC) and the Convertible Rupee Account System (CRA) were abolished. By this measure, the system of dual exchange rate prevailing prior to November 1977 was replaced by a unified exchange rate. The extent of depreciation was 46% from the previous official exchange rate and about 11% from the earlier certificate rate. Moreover, the exchange rate was tied to a basket of currencies and the country switched over to a floating exchange rate system that would allow the demand and supply conditions in the market to determine the exchange rate with only limited intervention by the central bank primarily aimed at eliminating erratic short-term fluctuations in exchange rate (Hettiarachchi, 1991).

Under the liberalised trade regime, the focus of trade policy was shifted from non-tariff instruments to tariff based instruments. Accordingly, a large proportion of the licensing and quota restrictions on imports was removed and the rest was liberalised to a significant extent. In October 1980, the first Presidential Tariff Commission was appointed to make recommendations regarding the simplification and rationalisation of import tariff structure. In 1985, following the recommendations of the Commission, the tariff structure was simplified and the maximum duty rate was brought down from over 300% to 100%. The maximum duty rate was further brought down to 60% in 1987. Thus, the

overall weighted average rate of duty, which used to be well above 125% during the sixties and over 100% during the seventies was already brought down to less than 60% by 1987.

The second phase of economic policy reforms initiated in 1989 saw further rationalisation of the tariff structure and also a further reduction of duty rates. In November 1990, the maximum rate of tariff was reduced from 60% to 50% and in November 1991 a four-band tariff structure was adopted, which effectively reduced the number of tariff bands from 19 in 1977 and 13 in 1990 to only 4 bands by 1991. The new tariff structure adopted in 1991 is given alongside.

Tariff Bands	Tariff Rates (Per cent)
Essential Commodities, Basic Raw Materials and Capital Goods	10
Intermediate Inputs and Semi-finished Products	20
Finished Products and Components for Assembly in Manufacturing Industries	35
Luxury Goods and Protective Tariff Items	50

In 1989, Sri Lanka adopted the harmonised system of tariff which has 5019 different tariff headings identified by a six-digit code as against 1011 tariff headings in the earlier BTN classification. The harmonised system takes into account the diversity and complexity of products resulting from rapid technological changes, and it also facilitates better coordination among different agencies and closer correlation between trade information system and production statistics.

In the second phase of trade policy reforms, a renewed emphasis was placed on the exchange rate as an important instrument for export promotion and efficient import substitution. The main objective of the exchange rate policy during the post-1989 period has been to ensure that the Sri Lankan currency does not appreciate in terms of real effective exchange rate vis-a-vis the currencies of Sri Lanka's major trading partners. In terms of the nominal exchange rate, the Sri Lankan rupee depreciated considerably vis-a-vis US \$ and other major currencies during the period 1978 to 1991. However, in terms of the real exchange rate, the Sri Lankan currency in effect appreciated against the US \$ during 1982-1988 and there were similar periods during mid-eighties when it appreciated against other major currencies, as indicated in Exhibit 8, which brings out the trends in the nominal exchange rates and real exchange rates of Sri Lankan rupee vis-a-vis selected currencies during the period 1978-1991.

V. Export Promotion Strategy

The basic rationale for an export-led growth strategy adopted by Sri Lanka is three-fold : Firstly, exports are a major component of Sri Lanka's GNP and hence a significant expansion of exports would lead to a sustained growth of GNP and general living standards in the country. Secondly, the size of domestic market in Sri Lanka being relatively smaller, tapping the export market is the only method by which the country can achieve economies of scale and thereby improve the overall efficiency of resource utilisation. Thirdly, rapid growth of exports is the only viable long term solution to the persistent deficit in Sri Lanka's BOP (SLEDB-NEDP, 1990). In formulating the strategy of export-led growth, policy-makers have emphasised the following aspects as the main ingredients of Sri Lanka's export promotion strategy :

- (1) *Institutional Infrastructure for Export Development* : The government established several specialised institutions to cater to the needs of export promotion such as the Sri Lanka Export Development Board (SLEDB), Sri Lanka Export Credit Insurance Corporation and Greater Colombo Economic Commission (GCEC). Sri Lanka Export Development Board was established in August 1979 as the apex organization of the Government of Sri Lanka for the formulation of policies and programmes with regard to exports. The main objective of SLEDB is to promote and develop various products and services for export promotion from Sri Lanka (for details, see Annexure 1). The GCEC was set up in 1978 to administer the

investment promotion zones/export processing zones. The main thrust of GCEC was to attract foreign investors who were prepared to accept a 100% export obligation. The GCEC enterprises were given various types of special tax concessions and other incentives (for details, see Annexure 2). The GCEC set up its first export promotion zone at Katunayake in 1978, the second zone at Biyagama in 1983 and the third zone was set up recently in 1990 at Koggala. The information on total number of enterprises, investment and employment in these export processing zones and other GCEC projects is given in Exhibit 9, while the information on gross and net exports of GCEC during the period 1982-1990 by individual product groups is given in Exhibit 10.

(2) *Export Incentives* : The government provide a wide range of fiscal and other incentives to promote exports during the post-1977 period. The following are the main elements of the export incentives offered during the liberalised regime:

- (a) Import duty concessions;
- (b) Tax incentives;
- (c) Special schemes for export promotion; and
- (d) Special incentives to attract foreign investments.

To ensure that Sri Lankan exporters have access to various inputs at international prices, the government offered various forms of import duty concessions to exporters. Under the Duty Rebate Scheme (DRS), import duties paid by exporters on raw materials, packing materials and consumables used in the production of non-traditional exports are fully reimbursable. The special feature of this scheme is that the exporters who are eligible for duty rebates are not required to make actual duty payments at the time of import, because the scheme allows the Customs to accept bank guarantee in lieu of such duty payments. This mechanism eliminates the problem of delays in the settlement of claims for duty rebates. Another scheme in operation is Manufacture In Bond Scheme (MIBS). Exporters are allowed duty-free imports of all inputs including packing and publicity material for 100% export-oriented production with the proviso that the inputs imported under MIBS should be stored in "bonded stores" approved by the Customs (SLEDB, 1990). Moreover, 100% export-oriented firms are also eligible for duty import of machinery used in the manufacturing process, while the firms exporting more than half of their output are eligible for a 50% exemption on duty. In addition to customs duty concessions, all manufactured exports have also been exempt from business turnover tax since 1968.

Another crucial element of the export incentive package has been the direct tax concessions given to exporters. Profit arising from all types of non-traditional exports are fully exempt from income-tax. This provision came into effect from April 1984 onwards. Similarly, the firms whose exports had a domestic value added content of 75% or more were eligible for a ten year "half-tax holiday" from April 1, 1985 and this provision was subsequently enlarged in 1988, whereby half-tax holidays were granted for a period of 5 years even to those companies who had a value-added content to 50% in their export turnover. In cases where an exporting company is eligible for a tax holiday, all dividends declared by the company during the period of tax holiday are exempt from income-tax in the hands of its shareholders, with an upper limit of Rs.12,000 per year in the case of individuals. Moreover, individuals investing in approved export companies are eligible for tax relief from their investments upto one-third of their assessable income or Rs.50,000, whichever is lower (SLEDB, 1990). It is evident that these measures would go a long way to channel private investible resources into export business.

In addition to the above fiscal incentives there are special schemes for providing assistance to exporters on various counts. Thus, for instance, there are financial assistance schemes which provide short-term pre-shipment credit as well as media term and long term credit to

exporters at concessional rates. The Export Development Board also operates a special scheme called "Export Development Investment Support Scheme (EDISS), under which specified payments are made to exporters of non-traditional items (excluding gems and garments exported under quota arrangement) at rates which represent a given percentage of the FOB value on their exports. It is significant to note that payments received under EDISS are exempt from income-tax. The rates of EDISS vary according to net foreign earnings percentage as indicated below :

In addition to the above rates, a special rate of 7% of the FOB value of exports is also paid to exporters of products where the value-added proportion exceeds 50% and where a special effort needs to be made for market development (SLEDB, 1990).

Category	Net Foreign Exchange Earnings Range (%)	EDISS Rate % on FOB Value)
A	20-30	3%
B	30-60	4%
C	More than 60	5%

While the export incentive mentioned above are available to domestic exporters, the government has also introduced several incentives which are designed specifically to attract foreign investors in export-oriented enterprises. Such incentive packages are covered under GCEC incentives, the details of which are given in Annexure 2.

- (3) *Export Development Planning* : The Sri Lanka Export Development Board prepares medium term and long term export development plans with the explicit objective of expanding and diversifying exports. The first National Export Development Plan (NEDP) prepared by SLEDB in 1983 covered the period 1983 to 1987 while the second NEDP prepared by SLEDB in 1990 would operate for the period 1990 to 1994. The NEDP contains a detailed sectoral planning exercise with explicit focus on the strategies and actions that need to be taken to overcome the constraints in the fulfillment of specified export targets for individual products and commodities. Moreover, in 1991, the government announced National Export Policy under which the priorities and specific policy measures for export promotion were clearly spelt out. The details of National Export Policy 1991 and related aspects are given in Annexure 3.

VI. Export Performance

It would be interesting to examine the impact of Sri Lanka's export promotion strategy and trade policy reforms on the performance of export sector during the post-1977 period. Exhibit 11 shows the trends in exports by major sectors measured in terms of both the domestic currency as well as SDRs during the period 1978-1991, while Exhibit 12 indicates the average annual growth rates of exports during this period.

It is evident from Exhibit 11 that Sri Lanka's exports valued in terms of nominal Sri Lankan Rupees (SLRs) have registered impressive growth during the post-1977 period. Traditional exports have increased by 140%, while non-traditional exports have registered a sixteen-fold increase and, as a result, total exports have increased more than five-fold during 1978-1991. However, the growth of exports valued in terms of SDRs has been much lower than the growth indicated by nominal SLRs primarily due to a significant depreciation of Sri Lankan currency during that period. In fact traditional exports measured in terms of SDRs, consisting of tea, rubber and coconut actually declined by 16%, while non-traditional exports registered a five-fold increase resulting in an increase of 120% in total exports during 1978-1991. Thus, liberalisation and trade policy reforms appear to have contributed to the rapid growth of non-traditional exports in Sri Lanka during the post 1977 period. In the process, the share of traditional exports has declined sharply from 72% in 1978 to 27% by 1991 and, correspondingly, the share of non-traditional exports has increased from 28% to 73%. In fact,

tea used to be the single largest export item in Sri Lanka's exports during the sixties and the seventies, but by 1991 textiles and garments emerged as the single largest item of export accounting for almost 40% of the country's total exports.

In the light of the background information on Sri Lanka's economy and liberalization process given in Section II above, we can divide the post-1977 period into three sub-periods : 1978 to 1982 (initial years of liberalised regime), 1982 to 1988 and the post-1988 period (second phase of liberalisation). It is evident from Exhibit 12 that there are significant differences and fluctuations in the average annual growth rates of export of different items during these sub-periods. Thus, for instance, among the three items of traditional exports, the growth rate of coconut exports (valued in SDRs) has increased significantly during 1988-1991, while the exports of rubber have declined sharply during this period. Similarly, there has been a significant acceleration in the growth rate of manufactured exports and garments during 1988-1991 in relation to 1982-1988, while the exports of marine products have declined in recent years. On the whole, the declining trend in traditional exports (valued in SDRs) taken together seems to have been arrested during 1988-1991, while growth rate of non-traditional exports has increased significantly from less than 6% during 1982-1988 to more than 16% during 1988-1991.

It would be interesting to examine the composition of imports in relation to the changing composition of exports especially during the recent years. Exhibit 13 shows the growth of Sri Lanka's imports by major categories during 1986-1991. During 1988-1991, imports of investment goods have increased sharply, while the imports of intermediate goods have shown a moderate increase. As a result, the share of investment goods in total imports has gone up from 17% in 1988 to 23.5% in 1991, while the share of intermediate goods has declined from 56.8% to 50.7% during this period. It may be noted that despite rapid growth of non-traditional exports in recent years, total earnings from non-traditional exports are still well below total expenditure on imports of intermediate and investment goods as of 1991.

Information on the direction of Sri Lanka's foreign trade is provided in Exhibit 14. It is evident that there is no perceptible change in the broad direction of Sri Lanka's exports during the period 1986-1991. Industrial countries account for more than three-fifths of Sri Lanka's exports, while Middle-East countries account for another one-sixth. However, there has been a significant change in the direction of imports. During 1986-91, the share of industrial countries in Sri Lanka's imports has declined from around 44% to 37%, while the share of Asian developing countries has increased from less than 34% to 49%.

It would be interesting to segregate the overall growth of foreign trade into two components of volume and price and examine the impact of price changes on the terms of trade. Exhibit 15 shows the movement of foreign trade indices during the period 1985-91, while Exhibit 16 provides the changes in unit values of traded goods during 1978-91. The behavior of terms of trade is brought out by the figures given in Exhibit 17. It can be seen from Exhibit 15 that the volume index of exports has actually declined during 1985-88, but it has been increasing at a significant rate thereafter and this increase is largely due to the rapid growth of export volume index for industrial products. While the overall volume index for imports also shows a similar pattern, the increase in the import volume index during 1988-1991 is significantly lower than the increase in export volume index. As against this, the overall price index for exports shows a lower increase (45.8%) during 1988-91 as compared to the overall price index for imports (58.2%) during the same period. Thus, there is a marked difference in the behaviour of volume and price indices for exports vis-a-vis imports during the recent years. Contrasting behaviour of export prices and import prices is also brought out by the comparative unit values of selected items of exports and imports shown in Exhibit 16.

It is evident that, in a situation where the import price index continues to grow at a relatively faster rate than the corresponding export price index, the terms of trade would progressively deteriorate with the passage of time. Exhibit 17 clearly shows that in the case of Sri Lankan economy, the import

price index has persistently grown at a rate that has been much higher than the rate of increase in export price index. Accordingly, Sri Lanka's terms of trade have registered a significant decline during the period 1970-1991. However, it is interesting to observe that the rate of decline in the terms of trade has been particularly sharp during the period 1977 to 1988, when the terms of trade (with 1970-71 as the base year) declined from 96 to 34. The rate of decline in terms of trade has reduced considerably thereafter. A major implication of the steadily deteriorating terms of trade is that it reduces the import capacity of the given volume of exports and thereby partially nullifies the positive impact of steady growth of exports on the country's BOP. In the case of Sri Lanka, the import capacity of exports declined by more than 40% during 1977-1988. However, during the subsequent period, there has been considerable improvement in the import capacity of Sri Lanka's exports, the index showing an increase from the level of 59 in 1988 to 67 by 1991.

VII. Future Outlook

According to the public investment plan for 1992-96, prepared by the Ministry of Policy Planning and Implementation, the overall growth rate of Sri Lankan economy is expected to be around 6% per annum during 1992-96 and the current account deficit as a ratio of GDP is likely to decline from 7.8% in 1991 to 5.3% in 1996. Fulfillment of both these targets requires sustained export growth of more than 7% in real terms with imports growing at a slower rate. According to the World Bank estimates, the annual external financing requirements of Sri Lanka over 1993-95 is expected to be around US \$ 1 billion (World Bank, 1992). Assuming that a large proportion of this would be met from foreign aid flows, Sri Lanka may be able to maintain gross official reserves at the current level of more than three months of imports. If these targets and expectations actually materialise, the Sri Lankan economy would certainly be poised for a significant economic revival during the nineties. However, the crucial factor that would determine the ultimate outcome in this regard is the degree of success that Sri Lanka is able to achieve in its export promotion efforts.

The Sri Lanka Export Development Board¹

1. The Purpose of the Board

The purpose of the Sri Lanka Export Development Board is to promote and develop products and services for export from Sri Lanka. The Board motivates exporters by providing incentives and removing disincentives. It is the apex organization of the Government of Sri Lanka for the formulation of policies and programmes with regard to exports. The production for exports is encouraged through a number of incentives and assistance schemes. The Board also provides services which are essential for the production for export.

2. The Export Development Act and the Export Development Board

The Export Development Board of Sri Lanka was established in August 1979 under the Sri Lanka Export Development Act, No. 40 of 1979. The Act and the subsequent setting up of the Board reflects the recognition of exports as a priority area in the economic development of the country.

3. The Export Development Council of Ministers

An Export Development Council of Ministers was set up under the Act with the President of the Republic of Sri Lanka as Chairman. The Council of Ministers comprises the Ministers in charge of Trade and Commerce; Ports and Shipping; Industries, Science and Technology; Agriculture Development and Research; Plantation Industries; Handlooms and Textile Industries, Fisheries, and Aquatic Resources, Finance; Foreign Affairs; Tourism and Rural Industrial Development; and Policy Planning and Implementation. The subject of Export Development falls within the purview of the Ministry of Trade and Commerce.

4. The Export Development Board

The Export Development Board is the executive arm of the Export Development Council of Ministers.

The Board is headed by a Chairman and comprises of 18 other members. They include the secretaries of the ministries in the Export Development Council of Ministers, six members who are experienced in the field of industry, business, commerce, finance or any other field relevant to exports appointed by the Minister of Trade and Commerce and a member representing the Greater Colombo Economic Commission appointed by the Minister in concurrence with the President.

5. The Board of Secretariat

The Chairman is the Chief Executive of the Organization. The Director-General and the Additional Director-General assist the Chairman in the overall management, control and administration of the Board. The Board Secretariat coordinates implementation of the policies and decisions of the Board and monitoring of its progress.

¹ Source: *EDB and Its Activities*, Sri Lanka Export Development Board, September 1992.

**Greater Colombo Economic Commission (GCEC)
Incentives for Export²**

Exporters registered with GCEC or who enter into agreements with the GCEC are eligible for various types of concessions and incentives as described below :

- I. Manufacturers and exporters of non-traditional products with at least 90% of the output exported or deemed to be exported under GCEC rules are eligible to the following incentives. A minimum investment in the project should be US \$ 250,000, all fixed assets procured from abroad and all working capital requirements should be funded from foreign sources. In the case of wholly owned foreign enterprises, the total project cost should be funded from foreign sources. Non-traditional goods manufactured and sold to other direct exporters also qualify for the incentives.
 - i. Tax holiday upto a maximum of 15 years reckoned from the first year of profits.
 - ii. Concessionary rate of income-tax varying between 2-5% if annual turnover after the expiry of the tax holiday for a period of 5 years.
 - iii. Exemption from income-tax on dividends paid to non-resident shareholders.
 - iv. Exemption from income-tax on dividends paid to resident shareholders out of exempt profits during the tax holiday period and one year thereafter.
 - v. Exemption from income-tax on royalties to non-residents during the tax holiday period and thereafter at 15% or at a lower rate stipulated in a Double Tax Relief Agreement.
 - vi. Exemption from income-tax on emoluments of foreign employees during the period of the tax holiday.
 - vii. Duty free imports of plant, machinery, equipment, raw material and other project related goods.
 - viii. Exemption from turnover tax and excise duty at the point of importation in respect of plant, machinery, equipment, raw materials and ancillary materials used in the manufacture of products for export.
 - ix. Duty free export of finished products.
 - x. Exemption from the Import and Export Control Act.
 - xi. Exemption from the Exchange Control Act and authorization to open Foreign Currency Banking Unit Accounts.
 - xii. Exemption from income-tax on capital gains arising from the transfer of shares of an enterprise.

- II. Export trading houses set up to undertake the business of exporting agricultural products, handloom textiles and non quota categories of textile apparel products and rural industrial products with a minimum investment of Rs. 7 mn. which is 100% locally owned, 100% foreign owned or a joint venture is eligible for the following incentives. It must also export not less than 90% of the product purchased by it from local sources. The products should be supplied by approved purchasing centres set up under the Janasaviya scheme registered growers and/or manufacturers.
 - i. Five year tax holiday reckoned from the first year of making profit.
 - ii. Five year half tax holiday or partial tax credit of 50% of the normal tax for a period of 5 years reckoned from the expiry of the tax holiday.
 - iii. Exemption from income-tax on dividends paid to non-resident shareholders.

² Source: Sri Lanka Export Development Board, *Incentives for the Sri Lankan Exporter*, October 1992.

- iv. Exemption from dividend tax on dividends paid to resident shareholders out of exempt profit during the tax holiday period and one year thereafter.
- v. Exemption from income-tax on royalties to non-residents during the tax holiday period and 15% or thereafter or a lower rate specified in a Double Tax Relief Agreement.
- vi. Exemption from income-tax on emoluments of foreign employees.
- vii. Duty free imports of plant, machinery, equipment, raw material and other project related goods.
- viii. Funding and credit facilities obtainable from local commercial banks and development banks.
- ix. Right to maintain a foreign currency banking account.
- x. Exemption from turnover tax and excise duty at the point of importation of plant, machinery equipment, raw material and ancillary materials.
- xi. Duty free export of finished products.
- xii. Exemption from the Import and Export Control Act.
- xiii. Exemption from income-tax on capital gains arising from the transfer of shares of the enterprises.

Annexure 3

National Export Policy³

National Export Policy was adopted by the Export Development Council of Ministers in March 1991. The highlights of the framework of this policy are as follows :

- a) The exchange rate will be maintained at a realistic level in order to ensure competitiveness of exports.
- b) Duty/tax free and unrestricted access to imported inputs will be ensured to all exporters.
- c) Export industries will be offered incentives comparable with those found in competing countries.
- d) Licensing and other bureaucratic controls will be reduced to a minimum. In particular, except for an identified "negative list", export licensing will, in fact, be completely dispensed with.
- e) Priority in the provision of public utilities and services will be given to all exporters.
- f) Access to finance at internationally competitive rates will be improved for all exporters.

In general, steps are being taken to ensure that the export sector is as competitive as other sectors of the economy, so that resources might flow into the sector on the basis of competitive advantage. Tariff policy has been a major instrument used to promote the competitiveness of Sri Lanka exports. The high protective duties have now been brought down to a five band tariff with a maximum tariff of 50% which makes Sri Lanka the most open economy in South Asia. The resulting increase in competition from abroad has induced local industries to be more efficient. However, they have complained of an inadequacy of support for adjustment, especially the high cost of long-term credit. As a part of the export drive the year 1992 has been declared the "Year of Exports" and the years 1992-2001 as the "Decade of Exports".

In view of the critical importance of the strategy of export led growth, a National Steering Committee has been set up with the intention of working out programmes and developing implementation strategies for the Export Decade, 1992-2001.

The Committee will consist of the Prime Minister, Minister of Trade and Commerce, Governor, Northern and Eastern Provinces, and the Chief Ministers of other provinces. The Committee is expected to carry out the following tasks :

1. The identification of sectors and sub-sectors of the economy which disclose high prospects for export development.
2. The determination of strategies for exploiting the potential of these sectors, sub-sectors, etc.
3. Overseeing of implementation by devising proper mechanism for coordination and execution of policy.
4. The identification of foreign markets, given the potential for export development in the Decade of Exports.
5. The determination of the various support needs of an export thrust, including incentives, tariff concessions for imported inputs, the development of the packaging sector, post harvest technology, R&D to assist in product development and innovation, etc.

As a part of export promotion activities undertaken in the Year of Exports - 1992, a World Trade Centre has been established in the heart of the city of Colombo. It will serve as a permanent display window and an information centre for the benefit of potential buyers of Sri Lanka export products.

³ Source : *Public Investment, 1992-1996*, Ministry of Policy Planning and Implementation, Government of Sri Lanka, October 1992.

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Exhibit 1

Selected Socio-economic Indicators for
Sri Lankan Economy, 1991⁴

	<u>1991</u>
<u>Total Population (Mn)</u>	17.2
Annual Growth Rate (%)	1.5
Density (per Sq.km.)	277
Urban Population (%)	21.5
 <u>Total Land Area (Sq.Km)</u>	 64453
 <u>National Income</u>	
Per Capita GNP (SLRs.)	19235
Per Capita GNP (US\$)	465
<u>Composition of GNP (%)</u>	
Agriculture	22.8
Industry	27.0
Services	50.2
 <u>Demographic Features</u>	
Birth Rate (per 1000)	20.0
Death Rate (per 1000)	5.8
Infant Mortality Rate (per 1000)	19.4
 <u>Life Expectancy at Birth</u>	
Total	72.5
Male	70.1
Female	74.8
 <u>Adult Literacy Rate (%)</u>	
Total	88.6
Male	93.4
Female	83.5
Female Labour participation Rate (%)	26.8
 <u>Government Expenditure by function (%)</u>	
Defence	3.8
Education	11.6
Health	6.7
 <u>Investment and Savings Rates</u>	
Investment Rate (% of GDP)	23.0
Domestic Savings Rate (% of GDP)	12.8

⁴ Sources:

1. *Sri Lanka Socio-Economic Data, 1992*, Statistical Department, Central Bank of Sri Lanka, Colombo, June 1992.
2. *Asia Year Book, 1992*, Far Eastern Economic Review

<u>Balance of Payments/GDP</u>	
Exports (%)	24.9
Imports (%)	37.4
Trade Balance (%)	-12.5
Current Account Deficit (%)	-7.8
<u>Government Finance/GDP at MP</u>	
Revenue (%)	20.4
Expenditure (%)	32.0
Current Account Surplus/Deficit (%)	-2.0
Budget Deficit (Before grants) (%)	-11.6
<u>Public Debt</u>	
Total Debt/GDP (MP) (%)	97.7
Domestic (%)	40.5
Foreign (%)	57.2
<u>Inflation Rate (1988-91)</u>	
Wholesale Prices (%)	13.4
Consumer Prices (%)	15.0
<u>Unemployment Rate (%)</u>	11.5
Length of Railways (Km)	1394
Length of Paved Highways (Km)	10582
<u>Health Care Indicators</u>	
Persons per hospital bed	340
Persons per Doctor	1164
<u>General Indicators (per 1000 population)</u>	
TV Sets	53
Radios	149
Telephones	15
Cars	10

Exhibit 2

Trends in Sri Lanka's GNP

(SLRs. Million)

S.No		At Current Prices					At Constant 1982 prices			
		1982	1988	1989	1990	1991	1988	1989	1990	1991
1.	Agriculture	24964	53600	58462	76504	91148	27984	27666	30011	30869
2.	Mining	2238	5567	5980	7098	7204	3392	3576	3901	3511
3.	Manufacturing	13601	31298	34941	43128	48361	19622	20488	22427	23979
4.	Construction	7959	14943	17332	21541	24376	8463	8514	8761	8963
5.	Electricity	1089	2492	2788	3652	4930	1499	1526	1681	1812
6.	Transport	10666	21988	23109	28655	34870	13619	13883	14410	15260
7.	Trade	19694	40578	46625	61812	71616	25164	25588	26497	28423
8.	Services	14468	33050	38901	48105	56553	19307	20488	21556	22572
9.	Gross Domestic Product	94679	203516	228138	290495	339058	119050	121729	129244	135389
10.	Net Factor Income from Abroad	-1959	-5266	-5739	-6685	-7316	-2836	-2855	-2818	-2964
11.	Gross National Product	92720	198250	222399	283810	331742	116214	118874	126426	132425

- Note:
1. Agriculture includes Forestry & Fishing
 2. Mining includes quarrying
 3. Electricity includes gas, water supply and sanitary services.
 4. Transport includes storage and communication
 5. Services include Banking, Insurance, Real Estate, ownership of dwellings, public administration, defence, and other services.

Source: Central Bank of Sri Lanka, Annual Report, 1991.

Exhibit 3

Growth Rates of GDP (at 1982 prices) By Sector of Origin

(Per cent per annum)

Period	Agriculture	Mining and Quarrying	Manufacturing	Construction	Services	GDP
1971-76	0.7	4.7	1.3	-1.4	4.7	2.7
1977-82	5.4	5.3	3.7	10.2	8.2	7.0
1983-88	1.9	7.2	6.3	1.0	4.5	3.9
1989-91	3.1	1.2	6.9	1.9	4.5	4.4

Source: Central Bank of Sri Lanka : Annual Report (various issues)

Exhibit 4

**Trends in Sectoral Distribution of GDP
(At 1982 Prices)**

(Per Cent)

Year	Agriculture	Mining & Quarrying	Manufacturing	Construction	Services	GDP
1970	31.2	0.5	17.6	10.2	40.5	100.0
1975	28.2	1.8	16.0	7.8	46.2	100.0
1980	26.7	2.4	14.5	9.8	46.5	100.0
1985	25.9	2.3	14.8	7.4	49.7	100.0
1991	23.3	2.6	18.1	6.8	49.2	100.0

Source: Same as Exhibit 3.

Exhibit 5
Trends in Sri Lanka's Balance of Payments : 1978-91

(SDR Millions)

	1978	1980	1984	1988	1990	1991
1. Trade Balance	-144	-758	-453	-568	-518	-725
1.1 Exports	675	818	1427	1098	1456	1491
1.2 Imports	819	1576	1880	1666	1974	2216
2. Services (Net)	6	40	-66	-114	-72	-78
2.1 Receipts	99	214	-329	306	391	465
2.2 Payments	93	174	395	420	463	543
3. Goods and Services (net)	-138	-718	-519	-682	-590	-803
4. Private Transfers	17	105	270	238	268	288
5. Current Account Balance	-121	-613	-249	-444	-322	-515
6. Official Transfers	46	106	198	154	130	143
7. Non-Monetary Capital	133	306	335	194	344	475
7.1 Direct Invest. (net)	1	35	36	32	31	74
7.2 Other Private (net)	7	150	193	-20	15	11
7.3 Government	125	121	237	182	298	390
8. Errors & Omissions	7	23	13	32	-19	47
9. Overall Balance	65	-178	297	-64	133	150
10. Monetary Movements	-65	178	-297	64	-133	-150
11. Exchange Rate (SLRs./SDR)	19.58	21.52	26.08	42.76	54.42	56.61
12. Current Account Deficit as Percentage of GDP	5.6	19.8	4.2	8.6	5.4	7.8

Source: Central Bank of Sri Lanka : *Annual Report and Review of the Economy* (Various issues)

Exhibit 6
Growth of Sri Lanka's Foreign Trade, 1978-1991

Year	Exports (Slrs. Mn.)	Imports (Slrs. Mn.)	Balance of Trade (Slrs. Mn.)	Ratio of Exports to GDP (%)	Ratio of Imports to GDP (%)	Ratio of Exports to Imports (%)
1978	13206	16049	-2843	31.2	37.9	82.3
1979	15282	22603	-7321	29.1	43.0	67.6
1980	17595	33942	-16347	26.4	50.9	51.8
1981	21043	36583	-15540	24.7	43.0	57.5
1982	21454	41946	-20492	22.7	44.3	51.1
1983	25096	45558	-20462	20.5	37.3	55.1
1984	37347	47541	-10194	24.2	30.8	78.6
1985	36207	54049	-17842	24.4	36.4	67.0
1986	34072	54559	-20487	20.8	33.3	62.4
1987	41133	60528	-19395	23.1	34.1	68.0
1988	46928	71030	-24102	23.1	34.9	66.1
1989	56175	80225	-24050	24.6	35.2	70.0
1990	79482	107729	-28247	27.4	37.1	73.8
1991	84379	126643	-42264	24.9	37.4	66.6

Source : 1. Central Bank of Sri Lanka.
2. Sri Lanka Customs.

Exhibit 7
Sri Lanka's External Debt and Debt Service, 1986-1991

		(SDR Million)					
Item	1986	1987	1988	1989	1990	1991	
1. Medium & Long-Term Debt	3227	3228	3531	3642	3828	4249	
1.1 Government	2551	2615	2848	2976	3190	3601	
1.2 Public Corporations	266	232	189	160	141	135	
1.3 Private Sector	176	216	240	231	209	233	
1.4 IMF Drawings	234	165	254	275	288	280	
2. Short Term Debt	151	203	179	297	294	349	
3. Total External Debt	3378	3431	3710	3939	4122	4598	
4. Debt Service Payments	356.8	383.3	402.8	374.7	328.5	353.5	
4.1 Amortization	213.5	253.5	258.8	217.3	182	197.7	
(i) To IMF	58.6	69.3	64.1	46	31.8	63.6	
(ii) To Others	154.9	184.2	194.7	171.3	150.2	134.1	
4.2 Interest Payments	143.3	129.8	144	157.4	146.6	155.8	
(i) To IMF	21.3	18.3	18.5	22.7	20.6	14.7	
(ii) To Others	122.0	111.5	125.5	134.7	126	141.1	
5. Earnings from Merchandise Exports and Services	1352.6	1384.4	1404	1522.4	1847.3	1955.7	
6. Receipts from Merchandise Exports, Services & Private Transfers	1622.4	1654.7	1670.6	1801.6	2143.7	2275.5	
7. Debt Service Ratios							
7.1 As a Percentage of (5) Above							
(i) Overall Ratio	26.4	27.7	28.7	24.6	17.8	18.1	
(ii) Excluding IMF Transactions	20.5	21.4	22.8	20.1	14.9	14.1	
7.2 As a Percentage of (6) Above							
(i) Overall Ratio	22.0	23.2	24.1	20.8	15.3	15.5	
(ii) Excluding IMF Transactions	17.1	17.9	19.2	17	12.9	12.1	

Source : Central Bank of Sri Lanka, Annual Report, 1990 & 1991.

Exhibit 8
Trends in Nominal Exchange Rates and Real Exchange Rates of Sri Lankan Rupee
(SLRs. per Unit of Foreign Currency)

Year	US Dollar		UK Pound		German Mark		Japanese Yen		French Franc	
	NER	RER	NER	RER	NER	RER	NER	RER	NER	RER
1978	15.51	25.34	31.67	43.57	8.55	14.98	0.08	0.15	3.75	5.87
1979	15.45	25.91	34.57	48.09	9.00	15.07	0.06	0.11	3.86	5.51
1980	18.00	25.74	42.70	50.62	9.21	12.39	0.08	0.13	3.98	4.25
1981	20.55	27.42	39.10	43.44	9.01	11.17	0.09	0.13	3.58	3.65
1982	21.32	27.51	34.61	39.26	8.98	11.18	0.09	0.12	3.17	3.41
1983	25.00	26.12	35.89	34.32	9.11	9.21	0.11	0.12	2.97	2.78
1984	26.28	22.40	30.51	24.58	8.35	6.91	0.10	0.09	2.73	2.22
1985	27.21	27.21	36.02	36.02	9.48	9.48	0.12	0.12	3.11	3.11
1986	28.05	28.08	41.30	44.41	13.11	13.18	0.17	0.16	4.08	4.09
1987	29.53	26.76	48.85	48.10	16.66	14.40	0.21	0.16	4.97	4.40
1988	31.88	25.51	56.80	49.61	18.14	13.48	0.25	0.16	5.35	4.24
1989	36.31	27.96	59.30	49.94	19.49	13.93	0.26	0.17	5.74	4.39
1990	40.07	26.15	71.75	52.34	24.87	14.89	0.28	0.15	7.39	4.57
1991	41.37	24.78	72.84	51.44	23.09	12.74	0.31	0.15	7.25	4.06

Note : 1985 is used as the base year for the computation of Real Exchange Rate.

Source: 1. Central Bank of Sri Lanka; 2. Export Development Board, Government of Sri Lanka.

Exhibit 9

Investment and Employment in GCEC Projects, 1992

Location	No. of Enterprises	Foreign Inv. (March '92) (Mn. SLRs.)	Local Inv. (March '92) (Mn. SLRs.)	Total Inv. (March '92) (Mn.SLRs.)	Employment
Katunayake Export Processing Zone	77	3564	644	4208	51885
Biyagama Export Processing Zone	33	3109	315	3424	19626
Koggala Export Processing Zone	7	26	0	26	2297
Total of 3 EPZs	117	6699	959	7658	73808
Other Projects	62	5427	9528	14955	25190
Total	179	12126	10487	22613	98998
	(118)	(7832)	(8887)	(16719)	(61429)

Note : Figures in parentheses relate to the year 1989.

Source : Greater Colombo Economic Commission, Government of Sri Lanka.

Exhibit 10

GCEC Exports Classified by Product Group for the Period 1982-1990

Sl. No.	Product Group	Gross Value of Exports (SLRs.Mn)	Net Value of Exports (SLRs. Mn.)	(3) as % of (2)
	(1)	(2)	(3)	(4)
1.	Wearing Apparel	42952.6	10100.4	23.52
2.	Jewellery and Lapidary	3174.2	324.8	10.23
3.	Textiles	3056.4	629.9	20.61
4.	Fabricated Metal	2177.7	593.0	27.23
5.	PVC Products	1790.5	626.0	34.96
6.	Beverages and Tobacco	1753.0	339.8	19.38
7.	Rubber Products	1423.2	887.7	62.37
8.	Footwear	1376.0	357.0	25.94
9.	Leather Garments	1259.3	207.4	16.47
10.	Electronics and Electrical Tools	762.7	116.6	15.29
11.	Non-metallic Minerals	699.5	492.5	70.41
12.	Cosmetic Products	430.5	122.0	28.34
13.	Horticulture	225.1	125.9	55.93
14.	Fishing Gear & Accessories	103.5	18.3	18.16
15.	Food Processing	96.9	80.0	82.56
16.	Wood Products	30.7	18.0	58.63
17.	Coir Products	25.2	14.7	58.33
18.	Transport Equipment	15.6	1.2	7.69
19.	Others	1133.8	354.5	31.27
20.	Total	62486.4	15410.2	24.66

Source: N.L. Sirisena, 1991.

Exhibit 11

Trends in Exports by Major Sectors

Sector	1978	1982	1984	1986	1988	1990	1991
Value of Exports in Million SLRs.							
Tea	6401	6342	15764	9253	12299	19823	17865
Rubber	2021	2323	3301	2622	3706	3062	2663
Coconut	1120	1496	2118	2389	1538	2650	2454
Total Traditional Exports	9542 (72.3)	10161 (47.4)	21183 (56.7)	14264 (41.9)	17543 (37.4)	25535 (32.1)	22982 (27.2)
Other Agricultural Exports	813	1495	1358	1500	2561	3350	3581
Marine Products	235	434	601	624	830	912	900
Gems and Jewellery	531	704	654	1852	3810	6746	5496
Textiles and Garments	482	3502	7535	9629	14260	25556	32515
Manufactures	497	1036	1131	2169	3580	8718	10964
Petroleum Products	944	3280	3288	2358	2265	4105	3412
Others (including Re-exports)	162	842	1597	1676	2079	4560	4529
Total Non-traditional Exports	3664 (27.7)	11293 (52.6)	16164 (43.3)	19808 (58.1)	29385 (62.6)	53947 (67.9)	61397 (72.8)
Total Exports	13206 (100.0)	21454 (100.0)	37347 (100.0)	34072 (100.0)	46928 (100.0)	79482 (100.0)	84379 (100.0)
Value of Exports in Million SDRs.							
Tea	327.0	276.0	604.1	284.1	287.7	364.3	316.0
Rubber	104.0	101.1	126.5	80.5	86.7	56.6	47.0
Coconut	57.0	65.1	81.2	73.3	36.0	51.1	46.0
Total Traditional Exports	488.0 (72.3)	442.2 (47.4)	811.7 (56.7)	437.9 (41.9)	410.3 (37.4)	472.0 (32.3)	409.0 (27.4)
Other Agricultural Exports	42.0	65.1	52.0	46.1	59.9	58.2	60.0
Marine Products	12.0	18.9	23.0	19.2	19.4	16.4	15.5
Gems and Jewellery	27.0	30.6	25.1	56.9	89.1	124.0	94.4
Textiles and Garments	25.0	152.4	288.7	295.6	333.5	462.4	588.0
Manufactures	25.0	45.0	43.3	66.6	83.7	140.9	188.3
Petroleum Products	48.0	142.7	126.0	72.4	53.0	73.0	58.0
Others (including Re-exports)	8.0	36.7	61.2	51.4	48.6	113.6	77.8
Total Non-traditional Exports	187.0 (27.7)	491.4 (52.6)	619.4 (43.3)	608.1 (58.1)	687.3 (62.6)	988.5 (67.7)	1082.0 (72.6)
Total Exports	675.0 (100.0)	933.6 (100.0)	1431.1 (100.0)	1046.0 (100.0)	1097.6 (100.0)	1460.5 (100.0)	1491.0 (100.0)

Source : 1. Central Bank of Sri Lanka
2. Sri Lanka Customs

Exhibit 12

Growth Rates of Exports by Major Sectors

(percent per annum)

Sector	Growth Rate of Exports in SLRs.				Growth Rate of Exports in SDRs.			
	1978-82	1982-88	1988-91	1978-91	1978-82	1982-88	1988-91	1978-91
Tea	-0.23	11.67	13.25	8.22	-4.15	0.69	3.18	-0.26
Rubber	3.54	8.10	-10.43	2.14	-0.70	-2.53	-18.46	-5.93
Coconut	7.50	0.46	16.85	6.22	3.38	-9.40	8.51	-1.64
Total Traditional Exports	1.58	9.53	9.42	7.00	-2.43	-1.24	-0.11	-1.35
Other Agricultural Exports	16.45	9.39	11.82	12.08	11.58	-1.38	0.06	2.78
Marine Products	16.58	11.41	2.74	10.88	12.03	0.44	-7.21	1.99
Gems and Jewellery	7.30	32.50	12.99	19.69	3.18	19.50	1.94	10.11
Textile and Garments	64.18	26.37	31.62	38.26	57.13	13.94	20.81	27.50
Manufactures	20.16	22.96	45.22	26.87	15.83	10.90	31.03	16.80
Petroleum Products	36.53	-5.98	14.63	10.39	31.31	-15.22	3.05	1.47
Others (including Re-exports)	50.99	16.26	29.63	29.20	46.35	4.79	16.98	19.12
Total Non-traditional Exports	32.50	17.28	27.84	24.21	27.32	5.75	16.33	14.46
Total Exports	12.90	13.93	21.60	15.33	8.45	2.73	10.75	6.29

Source : Exhibit 11.

Exhibit 13

Imports by Major Categories

(SLRs.Mn.)

Sl. No.	Category	1986	1987	1988	1989	1990	1991
I	Consumer Goods	12256 (22.5)	13814 (22.8)	17438 (24.5)	20962 (26.1)	28420 (26.4)	32357 (25.6)
II	Intermediate Goods	28618 (52.5)	34619 (57.2)	40325 (56.8)	45255 (56.4)	55757 (51.8)	64265 (50.7)
III	Investment Goods	10556 (19.3)	11334 (18.7)	12081 (17.0)	12018 (15.0)	23412 (21.7)	29792 (23.5)
IV	Unclassified Imports	3129 (5.7)	761 (1.3)	1186 (1.7)	1990 (2.5)	139 (0.1)	229 (0.2)
V	Total Imports	54559 (100.0)	60528 (100.0)	71030 (100.0)	80225 (100.0)	107728 (100.0)	126643 (100.0)

Note : Figures in parentheses indicate percentage of respective totals.
Source : 1. Central Bank of Sri Lanka.
2. Sri Lanka Customs.

Exhibit 14

Direction of Sri Lanka's Foreign Trade

Sl. No.	Group of Countries	Exports				Imports			
		1986	1988	1990	1991	1986	1988	1990	1991
I	Industrial Countries	20500 (60.2)	27460 (58.5)	46998 (59.1)	53665 (63.6)	23846 (43.7)	31318 (44.1)	41972 (39.0)	46541 (36.8)
I.1	USA	8908	11684	19732	23128	3291	4857	8322	7221
I.2	UK	1956	2574	4613	5222	2882	4025	5847	6881
I.3	France	461	905	1750	2657	704	1640	1699	1441
I.4	Germany	2335	3317	5075	6157	2405	3265	3361	4215
I.5	Japan	1879	2702	4102	4204	8934	9705	13035	14828
I.6	Others	4961	6278	11726	12297	5630	7826	9708	11955
II	Middle East	6005 (17.6)	8427 (18.0)	13383 (16.9)	13539 (16.0)	5355 (9.8)	7346 (10.3)	12135 (11.3)	11175 (8.8)
III	Asian Developing Countries	3733 (11.0)	6759 (14.4)	7652 (9.6)	8921 (10.6)	18363 (33.7)	26321 (37.1)	43004 (39.9)	62084 (49.0)
IV	Other Countries	3834 (11.2)	4282 (9.1)	11449 (14.4)	8254 (9.8)	6995 (12.8)	6045 (8.5)	10617 (9.8)	6843 (5.4)
V	Total	34072 (100.0)	46928 (100.0)	79482 (100.0)	84379 (100.0)	54559 (100.0)	71030 (100.0)	107728 (100.0)	126643 (100.0)

Note : Figures in parentheses indicate percentage of respective totals.

Source : 1. Central Bank of Sri Lanka

2. Sri Lanka Customs

Exhibit 15

Movement of Foreign Trade Indices, 1985-1991

(Base Year 1985 = 100)

S.No.	Category	1986	1987	1988	1989	1990	1991
I	Volume						
I.1	Exports	105.2	103.8	101.4	103.0	120.0	125.0
I.1.1	Agricultural Exports	103.7	99.6	96.6	94.9	101.6	97.0
I.1.2	Industrial Products	115.7	116.1	116.6	116.6	141.6	157.3
I.1.3	Mineral Products	120.8	128.6	211.3	249.5	232.3	157.0
I.2	Imports	100.8	101.0	95.6	90.0	95.2	107.7
I.2.1	Consumer Goods	103.0	104.1	100.3	95.6	106.1	118.3
I.2.2	Intermediate Goods	124.1	133.7	133.4	119.2	123.7	146.5
I.2.3	Investment Goods	81.6	82.2	71.4	64.7	73.6	85.1
II	Price						
II.1	Exports	89.5	109.4	127.8	150.7	183.0	186.4
II.1.1	Agricultural Exports	79.6	92.2	109.7	122.3	150.0	144.3
II.1.2	Industrial Products	96.0	120.6	136.1	170.8	205.1	225.7
II.1.3	Mineral Products	113.3	162.5	143.1	124.9	179.3	188.8
II.2	Imports	100.2	110.9	137.5	164.8	209.4	217.5
II.2.1	Consumer Goods	113.7	126.8	166.1	209.5	251.8	261.5
II.2.2	Intermediate Goods	77.3	87.4	100.8	128.4	165.4	161.7
II.2.3	Investment Goods	127.9	138.0	177.2	193.6	252.2	277.9
III	Value						
III.1	Exports	94.1	113.6	129.6	155.2	219.5	233.0
III.1.1	Agricultural Exports	82.6	91.9	106.0	116.0	152.4	140.0
III.1.2	Industrial Products	111.1	139.9	158.6	199.2	290.4	354.9
III.1.3	Mineral Products	136.8	208.9	302.5	311.6	416.5	296.5
III.2	Imports	100.9	112.0	131.4	148.4	199.3	234.3
III.2.1	Consumer Goods	117.1	132.0	166.7	200.4	267.2	309.3
III.2.2	Intermediate Goods	96.0	116.8	134.4	153.0	204.6	237.0
III.2.3	Investment Goods	104.4	113.4	126.6	125.2	185.8	236.4

Source : Central Bank of Sri Lanka

Exhibit 16

Changes in Unit Values of Traded Goods

(SDR Per Unit)

	1978	1988	1989	1990	1991
Export Unit Values (FOB)					
Tea (Kg.)	1.70	1.31	1.45	1.69	1.49
Rubber (Kg.)	0.75	0.87	0.78	0.65	0.61
Coconuts (nut)	0.08	0.09	0.07	0.07	0.09
Import Unit Values (CIF)					
Rice (Mt)	188	200	236	186	211
Sugar (Mt)	180	215	294	315	253
Wheat (Kg)	85	114	148	121	87
Crude Oil (Barrel)	10.2	11.3	13.7	17.3	14.2

- Sources: 1. Central Bank of Sri Lanka : Annual Reports and Review of the Economy (Various issues).
2. Sri Lanka Customs.

Exhibit 17

Trends in Terms of Trade and Import Capacity of Exports, 1970-1991.

Year	Export Price Index	Import Price Index	Terms of Trade	Index of Import Capacity of Exports
1970	100	100	100	100
1971	100	106	94	90
1972	100	112	89	84
1973	117	150	78	78
1974	182	262	69	64
1975	171	306	56	63
1976	200	275	73	85
1977	324	337	96	98
1978	588	625	94	105
1979	641	950	67	80
1980	741	1356	55	64
1981	759	1762	43	58
1982	700	1931	36	54
1983	970	2344	41	53
1984	1218	2594	47	71
1985	1041	2877	36	61
1986	932	2883	32	59
1987	1139	3191	36	64
1988	1330	3956	34	59
1989	1569	4741	33	59
1990	1905	6024	32	65
1991	1940	6257	31	67

- Source: 1. Central Bank of Sri Lanka.
2. Sri Lanka Export Development Board.

PART III : MONETARY MANAGEMENT

Chapter 9

Issues in Monetary Management in Tanzania¹

1. Introduction

On April 27, 1964, Tanganyika and Zanzibar combined to form one country which was named as 'The United Republic of Tanzania' on October 29, 1964. It shares its border with Kenya, Uganda, Rwanda-Burundi, Zaire, Zambia, Malawi and Mozambique. Its total geographical area covers 945.1 thousand square kilometers of which about 51% is agricultural land and 6% is covered by water. Low areas on the periphery receives about 50 inches of rainfall per annum which is adequate for good yields of perennial and annual crops. The central part of Tanzania is largely arid bush, having a mean rainfall of less than 30 inches. Only one-tenth of the land is cultivated and a slightly larger area is grazed. Tanzania's population is estimated to be 23.9 million in 1987 of which urban population is 29%. The annual average compound growth of total population during 1978-88 is estimated at about 2.8%. The density of population is about 26 persons per square km. About two-fifth of the population is economically actively engaged in Tanzania. The per capita GDP at factor cost at current prices is estimated to be T.Shillings 12,076 in 1988. At constant 1976 prices, it works out at T.Sh.1201 which is lower than in 1976. Personal income distribution in Tanzania is highly skewed with top 5% of households accounting for 33.5% of private income and top 20% households accounting for about 63% of private income. Poverty is widespread. About 60% of population lives below poverty level in rural areas and about 10% in the urban areas. Tables 1 and 2 provide information on the basic structural characteristics of the Tanzanian economy.

2. Main Objectives of Economic Policies

In 1967, six years after independence, the Tanzanian government adopted the Arusha Declaration introducing sweeping changes to embark on a new era of economic management based on socialist approach. Although substantial progress was made in the sphere of social equity, Tanzania experienced economic crisis conditions during the late 1970's and early 1980's. The crisis was caused by a series of external factors like successive droughts, oil price hikes, collapse of East African Community and the war with Uganda. To overcome this crisis, the government launched Economic Survival Plans in 1980 and 1981. However, only with introduction of a Structural Adjustment Programme (SAP) in 1982, a comprehensive approach to resolve the crises was initiated. This programme sought to provide an overall framework of measures with the objective to (i) restore financial and economic stability, (ii) stimulate agricultural development, (iii) improve efficiency, (iv) protect the provision of basic social services and (v) protect real income of the most vulnerable groups in the society. Although SAP had some positive impact, it was on the whole not successful in stimulating any major recovery in the Tanzanian economy. In mid-1986, therefore, the government introduced a new Economic Recovery Programme (ERP) covering a 3 year

¹We are grateful to Mr. Sunil N. Dalal, who co-authored this case, for giving permission to include it in the present volume.

period 1986-87 to 1988-89) to overcome some of the deficiencies of the policies in SAP.

Table 1													
Selected Important Ratios for Tanzanian Economy, 1976-88													
(In percentage)													
Ratios	Years												
	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988
1	2	3	4	5	6	7	8	9	10	11	12	13	14
1. Share in GDP at 1976 Prices													
a. Primary Sector	41.8	42.1	40.5	39.7	40.2	40.8	41.1	43.3	43.6	45.0	46.2	46.5	46.6
b. Secondary Sector	19.0	18.5	18.0	18.5	17.9	16.7	16.4	14.2	14.6	13.6	13.3	13.3	13.4
c. Tertiary Sector	39.2	39.4	41.5	41.8	41.8	42.5	42.5	42.5	41.8	41.4	40.5	40.2	40.0
2. GCF/GDP at 1976 at prices	25.8	29.7	28.0	29.9	26.1	27.3	28.0	20.2	26.8	31.4	29.6	28.3	26.3
3. GFCF/GDP at 1976 prices	23.8	26.3	25.7	28.0	24.0	24.9	25.8	17.7	24.9	29.7	28.0	26.7	24.8
4. Gross Savings/GDP at current prices	25.0	29.0	15.6	19.2	13.6	17.5	16.7	11.0	9.8	10.5	14.9	18.3	14.4
5. Tax/GDP at current prices	16.5	17.4	16.4	15.9	16.5	17.1	16.8	17.2	16.6	14.0	15.6	16.1	17.4
6. Per Capita GDP													
a) At Current Prices (in T.Shs.)	1362	1561	1681	1847	2072	2354	2729	3151	3811	5221	6715	8811	12076
b) At 1976 prices (in T.Shs.)	1362	1320	1303	1306	1295	1249	1217	1152	1154	1172	1181	1186	1201

Source: Bureau of Statistics, The President's Office, Planning Commission, Dar-es-Salaam.

The specific objectives of the ERP were to increase the output of food and export crops, to rehabilitate the physical infrastructure and raise capacity utilization through allocation of foreign exchange resources and restore internal and external balance by pursuit of prudent fiscal, monetary and trade policies. At the end of the ERP, considerable achievement was recorded in the performance of the real sector of the economy. Real GDP increased by 3.6% in 1986, 3.9% in 1987, 4.1% in 1988 and about 4.5% in 1989 as against an average growth of 1% during 1980-85. The revival in the real GDP growth meant that per capita output which had been declining steadily has now become positive. The main source of GDP growth has so far been agriculture with the contributing factors being favourable weather conditions, improved availability of inputs and the impact of attractive incentives to producers. The external sector, however, remains a problem area of economic management. The balance of payments position remains depressed in spite of increased exports particularly of non-traditional goods and increased external support improving the foreign exchange situation. At the end of ERP, exports are still only one third of import bill. The recovery in the agricultural production could not be translated into increase in exports due to structural bottlenecks including transport, processing and marketing.

The main objective of the monetary policy under the ERP was to control monetary expansion and reduce inflation. Credit to the government had to be contained during ERP. However, credit for the

<i>Table 2</i>	
External Account and Fiscal Position of Tanzania Averages for 1985-87	
(In percent)	
1. Export/Imports Ratio	32.8
2. Current Account Balance/GDP Ratio	-7.0
3. Capital Account Balance/Imports Ratio	1.5
4. Imports Support & Exceptional Finance/Import Ratio	5.8
5. Overall Balance/Import Ratio	-33.1
6. External Debt/Export Ratio	902.4
7. External Debt/GDP Ratio	76.4
8. Debt Service/Export Ratio	15.3
9. Government Expenditure/GDP Ratio	30.0
10. Government Revenue/GDP Ratio	16.5
11. External Finance/GDP Ratio	8.0
12. Domestic Non-Bank Borrowing/GDP Ratio	1.1
13. Bank Borrowing/GDP Ratio	0.9
14. Expenditure Float*/GDP Ratio	3.5
15. Tax/GDP Ratio	16.4
Source: Bureau of Statistics and BOT	
* Expenditure Float is defined as the amount of government cheques issued during a given year but unrepresented or uncleared through the BOT during that year.	

marketing of agricultural produce could not be contained within targets. The growth of this component of the total credit has been startling. Credit to the agricultural marketing institutions increased from T.Shs. 7.0 billion in June 1986 to T.Shs. 21.4 billion in June 1988 and T.Shs. 33.2 billion in June 1989. This has been partly due to exceptionally good crops (cotton and grains) and partly due to transportation, processing and marketing bottlenecks coupled with management deficiencies. Table-3 presents the targeted and actual annual growth rates in the total credit, money supply and prices during the ERP period.

The successor programme to ERP is the Economic and Social Action Programme (ESAP) covering the period 1989-90 to 1991-92. It stresses the consolidation of the gains so far achieved, intensification of

efforts in areas where positive results have begun to emerge, mitigating adverse effects of some measures affecting the human social dimension and taking further steps to ensure a sustained economic recovery. Its stated objectives include restoring internal and external balances and reducing the domestic inflation from 28% in 1988-89 to less than 10% in 1991-92.

The central objectives of the monetary policy during the next 3 years will be to sustain the growth of real GDP, to reduce inflation and to strengthen balance of payments position. These objectives are sought to be achieved through continued restraint on bank credit to government, and reforms of agricultural marketing and the financial sector.

It is proposed to revamp the financial sector with a view to improving the management of monetary policy and enhancing domestic savings. It is also proposed to maintain the positive interest rates attained during the ERP period and to improve efficiency and diversification of services in the financial system through institutional reforms.

3. Existing Financial Structure

The financial institutions in Tanzania form a very compact and highly differentiated structure as a result of the various nationalization and consolidation after the Arusha Declaration (1967) in the field of banking and credit. The main formal financial institutions existing in the Tanzanian financial system are:

- i) The Bank of Tanzania (BOT), the central bank which provides liquidity to banking institutions and the economy. It has legislative regulatory and supervisory powers over the formal financial sector in Tanzania. Chart 1 provides synoptic view of the main functions of BOT.

Chart 1: Functions of the Bank of Tanzania			
1.	Banking	Currency Issue Banker to Government Banker to Banks Banker to DFI's	
2.	Domestic Monetary Management (In terms of Finance and Credit Plan)	Govt.	Financing Budget Deficit Managing Govt. Debt Adviser to Govt.
		Banks & DFI's & SFI's	Short Term Loans - Advances, Bill Rediscounting - Interest Rate Policy - Control of Volume, Allocation & Terms & Conditions of Credit to their clients

3.	External Monetary Management	<ul style="list-style-type: none"> - Management of Foreign Exchange Reserves - Policy & Administration of Exchange & Import Controls - Export Promotion - Transactions with IMF - Exchange Rate of the T.Shilling 	
4.	Development	<ul style="list-style-type: none"> -Banks & DFI's & - SFI's 	<ul style="list-style-type: none"> - Medium & Long Term Loans - Contribution to share capital - Guarantee facilities - Supervision - Calling for Information - Provision of Training facilities

- ii) Three banks, viz. the National Bank of Commerce (NBC), the Co-operative and Rural Development Bank (CRDB) and the People's Bank of Zanzibar (PBZ) which provide commercial banking services. They also act as channels for government funds.
- iii) Two development finance institutions, viz. Tanzania Investment Bank (TIB) and Tanganyika Development Finance Company Ltd (TDFC) which provide long term development finance.
- iv) A savings bank viz., Post Office Savings Bank (POSB); a housing bank viz. Tanzania Housing Bank (THB); and the insurance/pensions funds, viz. National Insurance Corporation (NIC) and National Provident Fund (NPF).
- v) Two small financial institutions in the private sector, viz. Diamond Jubilee Investment Trust (DJIT) which accepts deposits and makes loans to small businesses and individuals mainly of the Ismaili Community; and the Karadha Company (KC) which is a hire/purchase company.
- vi) 381 savings and credit societies mainly in the urban areas and 201 multi-purpose cooperatives mainly in the rural areas which are involved in financial intermediation.

Chart 2 presents a synoptic view of the financial institutions in Tanzania.

It is important to note that, in Tanzania there is neither capital market nor a formal money market. Determination of effective interest rates and cash management of enterprises are, therefore, rendered very difficult. For the issue of bonds and treasury bills by the government, no secondary market exists. As a result, BOT ends up holding a very large proportion of these. At the end of March 1989 treasury bills outstanding amounted to T.Sh. 454 billion, and longer term government bonds totalled T.Sh.50 billion of which about T.Sh.33 billion were held by the BOT. NIC, NPF and POSB purchase a set amount of the bond issue and keep them to maturity. The absence of the bond and equity market has led companies and parastatals² to severe short term debt problems.

Chart 2 : Financial Institutions in Tanzania			
Institution	Form of Saving Mobilization	Type of Credit	Sector Receiving Credit
Bank of Tanzania	Currency Issue	Short, Medium and Long Term	Government, Commercial Banks and D.F.I's

² Parastatals are the organizations in the public sector wherein the government has the major share of ownership.

National Bank of Commerce & People Bank of Zanzibar	Acceptance of Demand, Savings & Time Deposits	Short, Medium and Long Term	Productive & Distributive Sectors of Government Economy
Tanzania Co-op. and Rural Development Bank	Acceptance of Demand, Savings & Time Deposits	Short Term Savings & Time Deposits	Co-op.Unions and Primary Societies; Small Businesses and Individuals
Tanzania Housing Bank	Savings and Time Deposits	Medium and Long Term	Building Construction & closely allied industries
Post Office Savings Bank	Savings and Time Deposits	Medium and Long Term	Government
Tanzania Investment Bank	None	Medium & Long Term Credit & Equity Investment	Commercial Agriculture and all types of industry
Tanganyika Development Fin.Co.Ltd.	None	Medium & Long Term Credit	Industry
National Insurance Corporation	Premium Income	Short, Medium and Long Term	Government
National Provident Fund	Provident Fund Contribution	Short, Medium & Long Term	Government
Karadha Company	None	Hire Purchase	Transport Finance
Diamond Jubilee Investment Trust	Acceptance of Demand, Savings & Time Deposits	Short, Medium and Long Term	Small Businesses and Individuals Community

On the other hand, Tanzania has an active informal financial market with foreign exchange dealings, funds transfer, debt and venture capital financing for businessmen. Table-4 presents brief monetary survey for Tanzania for the period 1987-89 which provides insights into the importance of the informal financial market in Tanzania. The ratio of currency to money supply works out at 35.35% for M2 and 51.43% for M1 in June 1989. The informal market has gained such prominence perhaps on account of inefficiencies and lack of adequate accessibility to the formal banking system. Interest rates in the formal system are not perhaps the main cause. Table-5 presents the interest rate structure in the formal banking system in Tanzania. As compared to a 31% p.a. maximum loan rates in the formal sector, interest rates in the informal market are estimated to be around 60% p.a. which cannot be considered very excessive particularly because the former do not include the high cost of transactions caused by inefficiencies. Even the informal market is very limited in its reach in Tanzania. Thus, smaller Tanzanian entrepreneurs face the major constraint of finance because neither formal nor informal financial systems cater to their needs.

<i>Table 4</i>				
Monetary Survey for Tanzania, June, 1987 to June 1990				
Millions of T.Shs.				
Items	June 1987	June 1988	June 1989	June 1990*
(1)	(2)	(3)	(4)	(5)
1. Net foreign assets of Banking System	-17,570.8	-13,120.8	-20,497.6	-23,008.7
2. Net claims on government	33,907.3	51,960.1	47,083.7	54,052.8
3. Lending to other domestic sectors	33,193.3	51,138.1	86,081.9	110,883.6
4. Other items	-466.0	-23,120.5	-20,269.4	-16,783.9
5. Total Money Supply (M2)	49,063.8	66,756.9	92,398.6	125,143.8
6. Currency in circulation outside banks	17,472.6	23,685.1	32,660.1	45,117.3
7. Demand Deposits	15,997.8	23,301.2	30,837.9	38,809.8
8. Money Supply(M1)	33,470.4	46,986.3	63,498.0	83,927.1
9. Savings Deposits	5,806.3	8,039.0	11,515.5	13,758.5
10. Time Deposits	9,787.1	11,731.6	17,385.1	27,458.2
Currency/M1 Ratio (in %)	52.20	50.41	51.43	53.76
Currency/M2 Ratio (in %)	35.61	35.47	35.35	36.05
*Provisional				
Source: <u>Bank of Tanzania: Economic and Operations Report for the year ended 30th June, 1989 and Quarterly Bulletins.</u>				

Table 5										
Interest Rate Structure										
Type of Deposits	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989
A. Deposit Rates										
1. Savings	5.00	6.00	7.50	7.50	7.50	10.00	10.00	21.50	21.50	26.00
2. Short-term (31-91 days)	3.15-3.50	3.15-3.50	3.15-3.50	3.50	3.50	5.00	5.00	14.50	14.50	16.00
3. Fixed (3-60 months)	4.00-7.00	4.00-8.50	4.00-10.25	4.00-11.00	4.00-11.00	6.00-14.00	6.00-14.00	15.50-27.00	15.50-27.00	17.00-29.00
B. Lending Rates										
1. Short-term	7.50-12.00	7.50-12.50	8.00-12.50	9.50	9.50	11.00-16.00	11.00-16.00	18.00-29.00	18.00-29.00	20.00-31.00
2. Medium & Long term	5.00-11.00	4.00-12.00	5.00-13.50	9.00-13.50	9.00-13.50	11.00-16.00	11.00-16.00	19.00-29.00	19.00-29.00	21.00-31.00
3. Housing Mortgages	5.00-11.00	4.00-11.00	5.00-13.50	13.50	13.50	8.00-16.00	8.00-16.00	7.00-29.00	9.00-29.00	9.00-29.00
C. Government Securities										
1. Direct Advances	4.77	4.77	4.77	4.00	4.00	5.00	5.00	11.25	11.25	14.50
2. Treasury Bills	4.27	4.27	4.27	4.95	4.95	5.33-6.00	5.33-6.00	11.25-12.00	11.25-12.00	14.50-15.50
3. Treasury Notes	5.00	5.00	5.00	5.00	5.00	10.00	10.00	18.75	18.75	23.00
4. Stocks	6.00-7.50	6.75-7.50	7.00-7.50	7.25-7.75	7.50-8.50	7.50-8.50	12.00-16.00	21.50-27.50	21.50-27.50	24.00-29.00
5. Tax Reserve Certificates	4.00	4.00	4.00	4.00	4.00	6.00	9.50	13.00	13.50	16.50
Source: Bank of Tanzania										

4. Instruments of Monetary Control

As a central bank, BOT has wide powers to control bank credit and currency. These powers have been conferred on BOT by the BOT Act 1965 and the amendments of the Act in 1971 and 1978. In the original statute, BOT was given the powers to use the cash ratio in the case of banks³ and direct control instruments for banks and Specified Financial Institutions (SFI's).⁴ The amendments of the Act, however, gave additional power to use Liquid Asset Ratio (LAR) besides placing certain responsibilities on the BOT in matters relating to financial planning. The BOT has also been given various powers regarding inspection of banks and SFI's. The following excerpts from the BOT publication entitled 'Bank of Tanzania: Its Role and Functions', (1979; pp.45-46) provide details on the provisions contained in the amended Act on different instruments of control of banking and credit in Tanzania.

³ A "bank" is defined as any undertaking carrying on banking business in Tanzania. Banking business in turn is defined as the business of receiving money on current account subject to withdrawal by cheque.

⁴ SFI's: 'Specified Financial Institutions' which according to the definition are credit institutions other than a bank.

The Cash Ratio: The Bank has been empowered by the Act: (i) to ask all banks to keep certain minimum cash balances on deposits with it as reserves against their deposit and all other liabilities in Tanzania except the paid-up capital, reserves, credit balance in the profit and loss account, advances taken from the Bank and any other liabilities as the Bank may exclude by giving a notice in the Gazette; (ii) to prescribe different ratios against different kinds of liabilities; and (iii) to prescribe methods of computing the reserves. However the total of all the balances kept as reserves must not exceed 20 percent of these liabilities, the ratios and methods must be the same for all banks and, whenever any ratio is increased, it can be effective only 30 days after the notice of increase is given to the banks. If any bank fails to maintain the balances as required, the Bank can levy a penalty charge on it. The maximum rate for such a charge is 1/10 of 1% per day of the amount by which the actual balance is less than the balance required.

The Liquid Assets Ratio: All banks are required by the Act to maintain liquid assets equal in value to at least 20% of their deposit and other liabilities. These liquid assets are defined as cash on hand (i.e. with the bank itself), balances with the Bank, unencumbered securities issued or guaranteed by the Government - i.e. those securities which have not been pledged as a security against a loan and any other assets which are specified as liquid assets by the Bank giving a notice in the Gazette.

Direct Control Instruments: (i) Deposit interest rates: The Bank can prescribe the maximum interest rates to be paid on various types of deposits by banks and SFI's or the minimum rates that they must pay. In specifying these rates the Bank can choose whether to apply them to both banks or SFI's or only the banks, or only the SFI's or only to a group of SFI's. Whichever group is chosen the orders apply to all institutions in that group.

(ii) Control and allocation of bank credit: The Bank has been given powers to control the total volume of credit given by banks, its allocation amongst different sectors and the terms and conditions on which it is given.

(iii) Control and allocation of credit from SFI's: In respect of credit given by SFI's the Bank has been given powers similar to those for controlling bank credit.

Financial Planning: The Bank is required to collect all information necessary for the preparation of the annual Finance and Credit Plan, the Foreign Exchange Plan and other monetary plans and to participate in their preparation, implementation and monitoring. It has to submit at least one report every three months to the Minister on the implementation of these plans and/or general developments in the economy. Furthermore, if the Bank finds that in actual practice there are significant deviations from the targets set in the plans, it must recommend to the Government such measures to remedy the situation as it (the Bank) considers desirable.

Power to call for information: The Bank can call from banks and SFI's such information as is necessary for the proper discharge of its functions and responsibilities. The information can be published either whole or in part, but in doing so care must be taken that no information on the financial affairs of any individual customer of the banks or SFI's is published without his written consent.

Power to inspect banks and SFI's: The Bank can ask a bank or an SFI to produce for inspection by persons in its service, books, minutes, accounts, cash, securities, documents, vouchers and other things in the possession of the institution relating to its business. A copy of the Bank's report on the inspection has to be sent to the institution concerned. If in the Bank's opinion the report shows that the business of the institution is conducted in a manner detrimental either to the institution's own interest or the public

interest, the Bank may either ask the institution to take such remedial measures as the Bank directs or appoint, with the Minister's approval, a competent person to advise the institution on the remedial measures to be taken by it and the institution has to comply with the advice.

Penalties for non-compliance: Any bank or SFI which does not carry out any of the instructions given by the Bank under the various powers described above; and every officer of that bank or SFI is liable to a default fine.

5. Recent Experience in Monetary Management

Under the present monetary framework, the targets of the monetary policy are aggregate supply of money and credit. As we have stated earlier (Table 3) both the targets are totally frustrated in practice during 1987-89. The deviations resulting in constant upward revisions in credit growth are not only due to economic environment but also because of the conflicting objectives of the BOT which include maintenance of monetary stability and the promotion of rural and industrial development. Almost all financial institutions in Tanzania hardly perform any important financial intermediation function because they essentially act as fiscal agents of the government. As a result, the only real instrument of monetary policy in Tanzania is the refinancing facility provided by the BOT. Since this facility is available to banks, particularly NBC, at concessional rate, it has been used as a permanent source of funds and a potential source of profits for banks. The rate charged by BOT is lower than the savings and time deposits rates. However, it is felt that banks' failure to mobilize private deposits is a more crucial factor determining their borrowing from the BOT rather than the interest rate differential. The BOT funding of the banks' activities shot up from T.Sh. 7.4 billion or 15% of total banks' liabilities in June 1987 to T.Sh. 59 billion or 42% of liabilities in June 1989. Thus, BOT seems to be exercising hardly any control over the growth of money supply when it concedes almost automatically to the bank's requests for financing. Fueling inflationary forces is an inevitable consequence.

The other instruments of monetary policy like the reserve requirements are not effectively used for controlling the bank credit and hence the money supply. This instrument is rendered ineffective by the practice of the BOT to extend automatic overdraft facilities to the banks defaulting in maintenance of the Cash-Reserve Ratio (CRR). The interest rate policy has also not been used for restraining the growth of credit since it is considered essentially a means to subsidize parastatals and cooperatives. Moreover, cost of credit is not a consideration for the parastatals and cooperatives since government stands guarantee for them under all circumstances. The bank's lending are right now the directed lending with the direct intervention of government without any regard to credit worthiness in terms of credit appraisal, past performance and profitability of the venture. The banks do not behave as profit maximizing business entities. Rather they have been viewing their role as channelling official resources towards priority activities and expect government to stand guarantee for their lending. The official budget of the government does not include such borrowings. However, the net effect of all this is that the annual Finance and Credit Plan and other monetary plans prepared by the BOT lose their operational significance.

6. Problems in Monetary Management

Recent experience of monetary management in Tanzania reveals several problems which are discussed in the following paragraphs:

i) **Instability of the Money Multiplier:** In an economy where the informal financial sector is growing, the money multiplier tends to decline over time. This is because currency is the predominant

medium of transactions there. The liabilities of the non-institutional financial sector do not possess the attributes of money. Therefore, the credit operations in the informal financial sector do not create corresponding flow of deposits. Tanzania has a growing informal financial sector, as a result of which the money multiplier shows a declining trend with instability. (See Table 6). This renders the control of money supply through the monetary base difficult.

<i>Table 6</i>							
Money Multiplier in Tanzania, 1976-1989							
(Millions of T.Shs.)							
Year	Currency in circulation	Banks' Deposits	Other Deposits with BOT	High Powered Money (H)		Money Multiplier	
				Excl. OD	Incl. OD	Excl.OD	Incl.OD
1	2	3	4	5	6	7	8
1) 1976	2214.9	14.7	19.9	2229.6	2249.5	3.12	3.09
2) 1977	2565.0	38.3	19.7	2603.3	2623.0	3.21	3.18
3) 1978	3143.5	12.4	22.4	3155.9	3178.3	2.98	2.96
4) 1979	4278.2	109.9	169.7	4388.1	4557.8	3.15	3.03
5) 1980	5522.9	39.3	25.1	5562.2	5587.3	3.15	3.14
6) 1981	6950.0	186.8	42.5	7136.8	7179.3	2.90	2.88
7) 1982	8381.9	244.8	37.4	8626.7	8664.1	2.87	2.85
8) 1983	8717.3	176.4	37.4	8893.7	8931.1	3.28	3.26
9) 1984	11341.2	230.1	--	11571.3	11571.3	2.61	2.61
10) 1985	13556.6	473.4	7046.5	14030.0	21076.5	2.78	1.85
11) 1986	19451.6	269.5	8139.4	19721.1	27860.5	2.55	1.81
12) 1987	26328.5	1554.4	13468.4	27882.9	41351.3	2.38	1.61
13) 1988	33817.0	2360.1	16017.9	36177.1	52195.0	2.48	1.72
14) 1989 (June)	34980.3	1995.0	16282.0	36975.3	53257.3	2.50	1.73
1) Other Deposits with BOT include deposits of commercial banks corresponding to pipeline remittances abroad and sundry deposits such as BOT staff deposits. 2) Money Multiplier = M_2/H Source: Bank of Tanzania: Economic Bulletin for the Quarter Ended 31st March, 1989 and Economic and Operations Report, 1989.							

ii) **Instability of Demand for Money:** Over the last two decades, demand for money in Tanzania measured in terms of income velocity of narrow money (i.e. GDP/M1) has been found to be unstable. (See Table 7). However, income velocity of broad money (i.e. GDP/M2) has a clear U-shaped curve over the years 1976 to 1988 with the minimum reached in 1982. Its value can, therefore, be predicted statistically by fitting a quadratic time trend. For monetary management, however, more relevant is its interest elasticity the magnitude of which, along with the stability of the demand for money function, can determine the effectiveness of the interest rate policy for achieving monetary targets. The estimate of the interest elasticity of demand for money is not readily available for Tanzania though it is speculated that it is not likely to be very high.

iii) **Structure of Interest Rates:** BOT prescribes annually a detailed structure of deposit and lending rates for all financial institutions in Tanzania. The primary considerations in determination of the interest rate structure have been to channelize subsidies to the parastatals. As a result, real interest rates were negative for quite some time. Of late, when they have been raised significantly so as to turn positive, the response in terms of deposit mobilization and resource reallocation has been negligible. This is largely due to the underdeveloped condition of the financial sector and the system of directed credit in Tanzania. These problems are further aggravated by the fact that the spread of interest rates available to the financial institutions is not adequate in terms of meeting their administrative costs, risks and a margin for profits. The present structure of interest rates does not allow higher rates for higher risk loans, e.g. interest rates for mortgages of T.Sh.5,00,000 or less are 9% p.a. and for small enterprises and agriculture range from 20 to 23% p.a. as against the ranges of loan rates from 20 to 31%, deposit rates from 16% to 29% and government stock rates from 14.5% to 29% p.a.

Income Velocity of Circulation in Tanzania, 1976-1988					
Years	Money Supply in Million T.Shs. in December		GDP at Market prices (M.T.Shs.)	Income Velocity	
	Narrowly defined (M1)	Broadly defined (M2)		GDP/M1	GDP/M2
1) 1976	5331.8	6946.8	24419	4.5799	3.5151
2) 1977	6382.8	8346.7	28868	4.5228	3.4586
3) 1978	6826.9	9396.3	32169	4.7121	3.4236
4) 1979	10435.4	13806.6	36285	3.4771	2.6281
5) 1980	13345.9	17519.9	42118	3.1559	2.4040
6) 1981	15401.2	20694.7	49102	3.1882	2.3727
7) 1982	18323.2	24728.6	58226	3.1777	2.3546
8) 1983	20564.3	29127.4	70509	3.4287	2.4207
9) 1984	20537.1	30218.1	88892	4.3284	2.9417
10)1985	25270.2	38971.0	120621	4.7733	3.0951
11)1986	35809.5	50353.4	159648	4.4583	3.1706
12)1987	47130.6	66442.9	219036	4.6474	3.2966
13)1988	65400.9	89809.1	311478	4.7626	3.4682

Source: Bureau of Statistics and Bank of Tanzania.

iv) **Regulatory and Supervisory Framework:** This framework is provided by the 1960 Banking Ordinance as amended from time to time. However, in Tanzania, the system of relatively informal bank supervision has come into existence since banks are state-owned and are considered to be the fiscal arm of the government. The responsibility and authority of the BOT to intervene in the matters pertaining to

the financial institutions in Tanzania is not well defined because the banking legislation and subsequent Act establishing banks are inconsistent and outdated. The regulatory framework for bank operations is weak, e.g. there are no capital asset ratio requirements and the broadly defined liquidity ratios are hardly enforced.⁵ Loan classification rules, interest accrual rules, lending concentration limits, etc. are far from satisfactory, e.g. NBC's official financial statements show a 61% return on equity in 1988, although it is technically insolvent! This is explained largely in terms of inadequate provisioning and the accrual of interest on non-performing loans in the statements. Similarly, the audit procedures are weak and rules for reporting are not enforced. Securities taken against the loans are not properly documented and the government guarantees are hardly ever collected. On-site inspection of bank branches are rarely carried out perhaps because of understaffing of the Supervision Department of the BOT. All these features of the regulatory and supervisory framework in Tanzania impose serious limitations on the efficacy of the monetary policy in the country.

v) **Financial Insolvency:** The banks face the problems of insolvency due to illiquidity arising out of high arrears with poor prospects of recovery. If all provisions are properly accounted for and prudent capital adequacy ratios are maintained by the banks, their recapitalization needs are estimated to be about T.Sh.62 billion in total which is 22% of GDP, 75% of government expenditures and 109% of government revenues. Some new cash injections into the system have to be considered inevitable which imposes serious constraints on the tight money policy. Among the bank clients, the parastatals, marketing boards and cooperative unions are faced with serious problems of insolvency. The private sector firms are by and large able to withstand the adverse economic environmental changes due to their better management and commercial principles. As against 55% of the loans to the agricultural parastatals and cooperative unions, only 7% of loans to the private sector need provisioning.

vi) **Institutional Weaknesses:** Banking system in Tanzania suffers from institutional mismanagement and inefficiencies. Very simple type of transactions like cheque cashing, transfer of funds, etc. involve very time consuming procedures with the result that, private individuals and companies are forced to minimize their business with banks. Facilities and procedures compel the rural borrowers to come personally all the way to Dar-es-Salaam to finalize arrangements! Staff training is inadequate and technical facilities are deficient. Personnel and salary policies and procedures demotivate the existing staff and create difficulties in hiring new staff. The pool of qualified labour is very limited in Tanzania and is often lured away into the private sector jobs. The salary structure of the bank employees and civil servants vis-a-vis the private sector jobs is a major issue and has much wider implications.

vii) **Lack of Competition:** NBC dominates Tanzania's financial system. Its current accounts are 13 times, deposits/saving accounts are 12 times and loans and overdrafts are 14 times as large as its nearest competitor, CRDB. Term lending is offered by TIB, TDFL and CRDB (for agriculture). THB is the only supplier of mortgages in the formal market in Tanzania. Stock market does not exist and equity finance is not readily available. The informal market is increasing in importance but its reach is limited. Thus, lack of effective competition has made the system weak and inefficient. It also reduces the effectiveness and efficiency of the monetary policy. Right now, the barriers to competition in Tanzanian financial system are: (a) rigidity of interest rate structure, (b) system of directed credit allocation, (c) ownership structure, (d) size of financial institutions, (e) inadequate salary and incentive structure for the staff as well as management, and (f) poor financial conditions of the banks.

⁵ Banks are required to maintain minimum deposits with BOT, not exceeding 20% of liabilities, and to keep liquid assets not less than 20% of liabilities.

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Chapter 10

Issues in Monetary Management in Countries with Common Currency: The Case of East Caribbean Central Bank

1. Introduction

Recent developments world over have revealed unprecedented dissatisfaction with the existing economic and political order. More of autonomy, democratic values, openness and less of centralization, controls and restrictions are generally preferred. On the other hand, trends of unification and integration of different economies have become stronger in some parts giving rise to sizeable regional blocks. Some communities are, however, caught in the dilemma and confusion over several questions, e.g. what are the costs of autonomy? Whether economic integration implies loss of autonomy and sovereignty? What are the political, economic and socio-cultural implications of economic integration of different economies? In order to have clues to such profound questions, it is desirable to examine the available experience in different spheres. In the field of monetary management, the East Caribbean Countries represent a unique case of monetary integration achieved over years through establishment of specific institutions like a common central bank with common currency. In the present paper, the case of The Eastern Caribbean Central Bank (ECCB) is discussed with emphasis on its role in the macroeconomic management of the economies of the Organisation of Eastern Caribbean States (OECS).

In the next section, we briefly outline the history of ECCB. The third section discusses the basic objectives and functioning of the Bank. The fourth section highlights some important provisions in the ECCB Agreement reached in 1983 which have implications on ECCB's control of the financial aspects of the economy. The fifth section is then devoted to the discussion of the important features of the financial institutional structure existing in the region which have some bearing on the effectiveness of the ECCB's control and conduct of monetary policy. The issues in monetary policy are discussed in the sixth section highlighting some features of the economies in the region. In the seventh and the final section, some alternatives before the region are discussed for meeting the challenge arising out of EC 1992 which is likely to result in a severe shock to the economies of the region.

2. Historical Perspective

ECCB is the apex body of the region's monetary system. It was established only recently on October 1, 1983 which marked a new phase in the development of the area's monetary system. Prior to any formal institutional set up existed in the area, i.e. before 1950, the foreign commercial banks issued their own notes which served as medium of exchange and store of value along with coins issued by the British government. In 1950, the need was felt to set up the British Caribbean Currency Board (BCCB) to facilitate the issue of currency of the colonial power to the commercial banks in the area. The BCCB was set up in Trinidad to cover the area of 10 member states viz. Trinidad & Tobago, Guyana, Barbados, Antigua & Barbuda, Dominica, Grenada, Montserrat, St.Kitts & Nevis, St.Lucia and St.Vincent & Grenadines. In 1965, the BCCB had to be dissolved because Trinidad & Tobago and Guyana withdrew to establish their own central banks. The move on their part was primarily guided by the desire to have

financial and fiscal autonomy. In 1965, therefore, East Caribbean Currency Authority (ECCA) was established in Barbados to serve the remaining members of the former BCCB. In 1974, Barbados also withdrew in order to have its own central bank. The headquarters of ECCA were shifted to St. Kitts in 1975. In 1976, the East Caribbean Currency Agreement was amended to provide choice in terms of the exchange rate regime to be followed. The choice was exercised and as a result, the EC dollar was delinked with the British pound and was linked to the U.S. dollar.

Since 1950, the BCCB operations were carried out on the principle of 100% back up of the currency put in circulation by the foreign reserves. These reserves had to be invested in the British government securities and treasury bills. The commercial banks in the BCCB area were required to deposit the British pounds to get equivalent British Caribbean Currency. The ECCA Agreement in 1965, on the other hand, revised such a stringent requirement of 100% backing to only 70% backing in terms of the foreign reserves. There was also a provision for reducing this ratio to 60% if required. This was the major move towards autonomy because it gave the much needed power to the ECCA to finance the deficits of the member governments by investing in their securities and treasury bills rather than investing solely in the British government securities. This shift, therefore, implied a major change in the role of the monetary system to cater to the needs of the area as reflected in their governments' budget allocations. The ECCA, however, was not meant to provide advice to governments. It also lacked any authority to exercise influence on factors affecting the stability of the EC dollar. The ECCA had no powers to supervise the banking system or impose any reserve requirements. In short, it had no role to play in the credit policies in the area of its operation.

With the passage of time, as the Wind of Independence blew and pressure for greater autonomy increased, the role of ECCA steadily increased. The monetary authority started playing more pro-active role by acting as intermediary for receiving overseas aid funds on behalf of member governments and for dealing with the IMF and the World Bank as the fiscal agent for its members. It was becoming more and more clear that in order to facilitate economic growth with stability, sound and efficient management of the monetary sector is imperative. The financial structure of the area had also undergone substantial changes since 1973 when only 5.1% of the area's deposits were held by indigenous banks. By October 1983, around 35% of the area's deposits were held by indigenous banks who did not enjoy the advantage of having a head office to look after their liquidity problems under crisis. These local institutions had to be provided with the lender of the last resort. It was, moreover, clearly recognised that money and credit have to be consciously managed through policies which direct them to the desired ends. Since the participating government authorities decided in favour of the discretionary control of monetary system, creation of a Central Bank was the natural outcome. With a view to creating and maintaining a sound monetary, credit and banking system within the territories of the member countries, in 1983, an agreement was, therefore, reached to convert the existing ECCA into a common central bank - ECCB.

3. Objectives and Organisation of ECCB

Like all other central banks, ECCB also has well defined objectives to be achieved. Depending on the time of reference, the list of objectives would be modified or more sharply focussed as required, but within the frame clearly spelt out in Section 4 of the ECCB Agreement of 1983. The section 4 is reproduced as under:

"The purposes of the Bank are:-

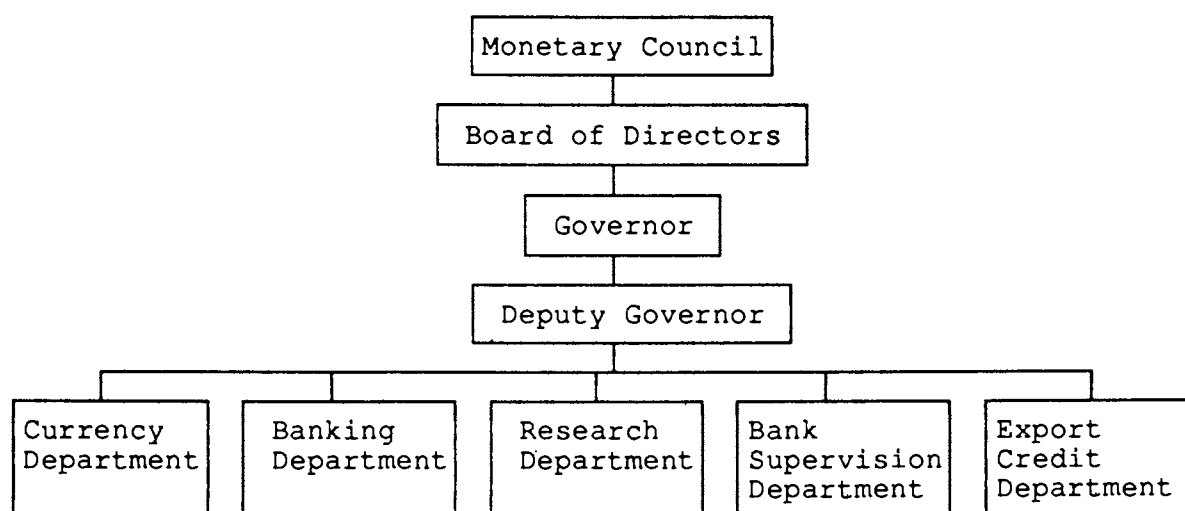
- (1) to regulate the availability of money and credit;

- (2) to promote and maintain monetary stability;
- (3) to promote credit and exchange conditions and a sound financial structure conducive to the balanced growth and development of the economies of the territories of the Participating Governments;
- (4) to actively promote through means consistent with its other objectives of the economic development of the territories of the Participating Governments." (P.2)

In short, the basic objectives of the ECCB are to maintain stability in the external and internal value of EC dollar; to ensure availability of credit at reasonable cost to the priority sectors; and monitor the domestic as well as foreign saving flows. Since ECCB is a central bank to 8 different countries including Anguilla, it has to work in close collaboration with governments of each country to fulfill its objectives regarding allocation of credit and saving flows. In this context, the organization of ECCB plays important role.

Chart 1 outlines the organisation of ECCB. The Monetary Council is the highest decision making authority and hence consists of one Minister (usually looking after Ministry of Finance or Economic Development) appointed by each participating government. The Minister may appoint an alternate to participate in his absence. This council meets at least twice a year and provides directives and guidelines for the monetary and credit policy to be pursued by ECCB. The powers of the Bank are vested in the Board of Directors which consists of 10 Directors including the Governor and the Deputy Governor. The other 8 Directors are appointed by the participating governments - one from each country. Generally, the Permanent Secretary of Finance or Fiscal Advisor is appointed as the Director by the participating governments to ensure proper linkages and coordination between the monetary policy and their individual fiscal policies. The Board of Directors is responsible for the policy and general administration of the Bank. The Governor who is the chief executive of the Bank looks after the day-to-day management and operations of ECCB with the assistance of the Deputy Governor. The Governor and Deputy Governor are appointed for a term of 5 years by the Monetary Council and are eligible for reappointment. The Governor provides direct link between the Monetary Council and the Board of Directors. The Governor is the ex-officio chairman of the Board of Directors and has a casting vote in case of a tie. The Governor and Deputy Governor do not have the right to vote in the Board's meetings. The Board would meet as often as the business of the Bank requires but not less than once every three months. The term of the Directors is 3 years but they are eligible for reappointment. The quorum requirement for both the Monetary Council and Board of Directors is the presence of 5 appointed members from among the participating governments.

Chart 1: Organization Chart



It is important to note that every member has only one vote and the decisions are taken by simple majority except a few cases where unanimous decisions are required. Thus, participating governments get equal weight in the decision making irrespective of their size, problems or levels of development. Such a democratic organisational set up has worked effectively now for over 8 years without any significant problems encountered so far. The environment in the meetings is generally very friendly. No serious conflicts arise in the meetings though differences of opinions do exist. However, the decisions are generally arrived at by consensus through persuading arguments and discussions.

For carrying out various activities, the ECCB has 5 major departments like most other central banks. These are: (1) Currency Department whose responsibility includes, among other, to make accurate forecasts of territorial demands of coins and currency; (2) Banking Department which performs the banking function, accounting function and the investment function; (3) Research Department which is the economic intelligence unit of the Bank in charge of the dissemination of information and analysis to all quarters; (4) Bank Supervision Department whose main function is to safeguard the interest of depositors, borrowers and customers who obtain financial services from the Bank; and (5) Export Credit Guarantee Department whose main function is to encourage, facilitate and promote the export trade of the Eastern Caribbean Region.

4. The ECCB Agreement

The 1983 Agreement among the participating governments has several important provisions which define the nature and scope of ECCB's activities and its relationship with the financial institutions in the region and with the participating governments and hence their fiscal policies. The following are some of the important provisions in the Agreement.

The external value of the Eastern Caribbean Dollar can be decided by the Monetary Council on recommendation of the Board of Directors only when both the recommendation and the decision are adopted unanimously by all their members. Probably it is this provision which explains constant nominal exchange rate of the EC dollar with U.S. dollar over the period 1976 till today. This provision makes the alternatives of free float of the EC dollar or pegging of it with a basket of currencies a non-workable solution. Unanimity rule is a very strong condition for making changes in the status quo. If the external value of the EC dollar does not change with respect to the U.S. dollar, it has significant implications on the internal balance of the economy through the balance of payments and internal value of the currency. There is however, a provision that the Monetary Council would arrange for reasonable compensation to a participating government adversely affected by the change in the external value of the EC dollar. The compensation arrangement to cover losses due to changes in external value of the EC dollar provides for conducting an impact study, establishing a special compensatory financing fund, mobilizing resources from outside the Bank, etc.

Another set of important provisions in the Agreement is about the external reserves. As per the provision, the Bank should maintain External Reserves of at least 60% of the value of the currency and coins in circulation. This percentage can be changed by the Bank only by unanimous agreement of all of the members of the Monetary Council. Moreover, the Bank would be the depository of the external

assets of the participating governments, boards, agencies and other statutory bodies of these governments. The Bank can also designate agents and correspondents to hold these assets. The Bank would deal in gold coins, bullion or other precious metals and foreign exchange. It can buy, sell or deal in all these at rates fixed by it from time to time.

Provisions with regard to the relations of the Bank with financial institutions are as usual concerning the control of the latter by the former and providing basic services and facilities in return. In this context, 'financial institution' is defined as any person⁶ doing banking business. All offices and branches of financial institution in the territories of the participating governments are treated as one financial institution. Provisions pertaining to the control and regulation of financial institutions include the ones on rates of discounts and rediscounts; differential rates and ceilings for various classes of transactions or maturities; reserve and marginal reserve requirements; different reserve ratios for different classes of deposit and other liabilities; supervision through accounts and other information; etc. A worth-noting provision in this regard is that the ECCB can grant a financial institution advances against treasury bills and securities issued or guaranteed by any of the participating governments or its agencies subject to some maximum of all such bills and securities accumulated with ECCB. This calls for strict fiscal discipline on the part of the participating governments as well as the financial institutions dealing with them. The Bank may also require the financial institutions to hold securities issued by the participating governments up to 10% of the institution's deposits and similar liabilities. This is primarily required because well developed capital market does not exist. The Bank can also prescribe from time to time the method of computation as well as minimum and maximum rates of interest payable in respect of deposits and other similar liabilities. However, these decisions can be taken by the Monetary Council only by two-thirds majority of all its members on the recommendation of the Board of Directors with minimum two-thirds of the majority of all its appointed members. This makes such changes less frequent. The information provided by all financial institutions can be shared with the concerned participating government at the latter's request on the condition that it would be treated as secret.

The relation of ECCB with the participating government is defined by a set of provisions most of which are routine ones, e.g. the Bank would be the banker, fiscal agent and advisor to the participating governments on monetary and financial matters and would be the depository of funds of those governments. However, the participating governments are expected to maintain working balances with other financial institutions and generally use their services. But when the governments are facing temporary problems, the Bank can make temporary advances to them for meeting their seasonal needs subject to the limit of 5% of their average annual recurrent revenue during the given financial year. The average is taken over the three preceding financial years. Moreover, holding of treasury bills of any one government at any one point of time by ECCB should not exceed 10% of the estimated recurrent revenue of that government as determined by the Bank for the current year. Similarly, the other constraint imposed by the Agreement on the participating governments borrowings from ECCB is that the ECCB can purchase or sell publicly issued securities payable in EC dollars and maturing in 15 years or less, provided that all such securities at any one point of time do not exceed 15% of currency issued by the Bank. The only exception to this are the bonds of any corporation established under the authority of the participating government/s for the express purpose of financing development within their territories. In such cases the amount of bonds should not exceed 2.5% of the average annual recurrent revenue of the government. The Bank is also expected to monitor the operations of the licensed offshore

⁶ "Person includes any corporation, either aggregate or sole, and any undertaking, club, society, association or other body of one or more persons" (p.2 of the 1983 Agreement).

financial institutions. It is also explicitly stated in the Agreement of 1983 that "in carrying out its functions the Bank shall be guided solely by technical criteria and considerations and shall not discriminate in any aspect of its operations on political or other non-economic grounds." (p.21).

5. Financial Structure

The financial system in the OECS region is not well developed. The range of financial institutions is limited to commercial banks and a few non-commercial institutions. The banking sector is still dominated by foreign banks having branches and subsidiaries in the OECS region. The indigenous banks are still struggling to acquire a larger market share. The indigenous banks are those which have at least 51% of local ownership. These banks vary considerably in terms of the government involvement in their ownership from negligible to cent percent. The foreign banks in the OECS region are again mainly confined to four major banks which operate in more than one territories. These branches which are not locally incorporated in the region represent a tiny proportion of the total business of their respective parent banks. They have the basic advantage of falling back on their headquarters for any short term liquidity-crunch. Since they have the advantage of early entry into the market in the colonial days, they still enjoy greater confidence and a psyche of better service from the public. The market share in terms of assets is approximately in the proportion of 65:35 between the foreign banks and the indigenous banks.

The financial performance of the foreign banks in OECS has been significantly better than the local banks in terms of profitability which is generally measured as return (after tax) on assets employed. In the North America, a return on assets in excess of 1.0% is regarded as an excellent performance. Although all the commercial banks taken together in OECS region as well as in every individual country have the ratio well in excess of 1.0%, in 1983 when the separate data were available, Liburd and Ferracho (1985) have found that the ratio is only 0.90% for the local banks against 1.49% for the foreign banks in the OECS region. The explanation for this according to Liburd and Ferracho (1985) is in terms of the net interest margin and non-interest income of the banks. The composition of their assets and liabilities differed considerably. The public sector loans at concessional rates accounted for 36% of the total loans in the local banks as against only 12% in the foreign banks. In absolute terms too, the local banks' credit to the public sector was 89% more than the foreign banks. On the other hand, the loan-asset ratio in the two types of banks was very similar. The composition of deposits in the two types of banks was also unfavourable to the local banks. They had 43% of time deposits, 12% of demand deposits and 21% of savings deposits as against the foreign banks where these proportions out of total liability were 25% (TD), 14% (DD) and 36% (SD). Similarly the share of private sector deposits in total deposits was 64% in the local banks as against 95% in the foreign banks. The deposit structure has obvious implications on the cost of funds. Moreover, as already mentioned, local banks have to offer a higher interest rate for deposits to maintain their market share. If the local banks want to increase their profitability, they have to increase the margin further. How far this is possible is a difficult question particularly now when ECCB sets the minimum and maximum interest rates on deposits and loans. The interest rates are set by the commercial banks to achieve a target rate of return on capital. They, therefore, set overall level of the deposit rates so as to allow the deposits to grow at the desired rate. The lending rates are then set to achieve the target rate of return based on the projection of assets and liabilities.

The other actors in the financial system in the OECS include development banks which exist almost in all countries. These banks mainly cater to the medium and long term financial needs of the business sector. They also pay special attention to the financing problems of small enterprises. Other development oriented activities like home building and education are also financed by these development banks.

Together with the National Commercial Banks established in most countries with substantial government involvement and which cater to the short term financial needs of the priority sectors, the development banks represent the government effort to develop financial institutions to encourage savings and channelize them in priority or vital sectors in each country.

Other financial institutions include mortgage and finance houses which are locally incorporated (with a couple of exceptions) and hence operate within their home territories; life insurance companies which are predominantly foreign; and the national insurance schemes. These institutions together mobilize a significant portion of financial savings in OECS region. In order to recycle liquidity with profit in the banking system, in 1986 an Inter-Bank Market was introduced. This institution enlarged the options of the commercial banks and reduced their dependence on ECCB. Similarly, in January 1988, Treasury Bill Market is introduced to widen the range of options available to the commercial banks for management of their liquidity. Thus, in the OECS region, although the money market exists, there is a serious gap in terms of institution trading in equities and other long term securities.

The informal credit market in the OECS countries is practically non-existent except in the form of credit unions which are a force to reckon with in Dominica. They are not directly or even indirectly controlled by ECCB. These credit unions are becoming stronger and stronger controlling larger amount of assets than commercial banks. These unions enjoy a high degree of confidence of the people. They are primarily meant to serve the credit needs of the informal sector where the policy does not reach. These credit unions are not banks but their mobilization of savings is significant. They provide much more and better service to their clients who have to be their members. For instance, they provide built-in life insurance, accident insurance, etc. to the depositors or members. Similarly, as a share holder, one participates in their profits through dividends. For the borrowers, the procedures to secure a loan are less complicated and less time-consuming than those in commercial banks. The credit unions require even less collateral. Moreover, their net-work is very extensive and are deeply community based. They are genuinely village and people's institutions. In spite of all these advantages, there is no nominal interest rate differential between credit unions and banks. When imputed value of all these advantages are considered, deposits and loans with credit unions become more attractive in real terms. Currently, the ECCB is negotiating with these unions to incorporate them into its net so that their activities can be monitored and supervised. ECCB is aware that totally different set of norms and criteria would be required for the purpose.

6. ECCB and Monetary Control

Monetary policy is an important instrument for aggregate demand management in any country. In the monetary union crystalized in ECCB, the eastern caribbean countries agree to share the same monetary policy for all member countries. In order to monitor liquidity in the economy by controlling and regulating the cost and availability of credit to various sectors, the policy instruments available to any central bank are bank rate, open market operations, reserve requirements, ceilings on bank credit, etc. on quantitative side and moral suation on qualitative side. The provisions in the Agreement of 1983 as discussed earlier give all these powers to the ECCB. The prevalent financial structure in the OECS region, however, imposes certain constraints on ECCB which reduce the effectiveness of the traditional instruments of monetary control. As we have already discussed in the previous section, the financial structure of the ECCB area is underdeveloped. Capital market is not developed and money market assets are limited in quantum and diversity. Any organised market for conducting open market operations by ECCB does not exist for all practical purposes. Thus, the environmental constraint makes the open market operations ineffective instruments for ECCB. They are otherwise the most popular tool used

effectively by central banks in the developed countries.

Again, the financial structure in the OECS area wherein foreign banks dominate the banking system, imposes a limitation on bank rate to be an effective regulatory tool of policy. The major foreign banks in the area are only small branches in the international network of their parent banks. Traditionally, these branches were dependent on their respective head-quarters for liquidity crunch. Their reliance on ECCB as the lender of the last resort is minimal. The bank rate policy of ECCB functioned more as a penalty rate encouraging banks to bring in funds from abroad rather than borrow from it. However, with the creation of inter-bank market in the area, the bank-rate policy is likely to assume more importance. But so long as there are no controls on the inflows of banking funds, the bank-rate policy is less likely to be effective because large holding of net foreign assets from which the credit needs can be met are possible with banks under the present system. The bank rate policy has, therefore, little or no influence on the structure of interest rates.

The reserve requirements are generally considered to be very strong instrument of monetary control. The effects of changes in this measure are likely to be dramatic on small country open economies of the islands because it cuts the profitability of the banks. Frequent changes in the reserve requirements are, therefore, not desirable for stability of the banking business in the economy. Such considerations have dictated the choice of ECCB of not changing the reserve requirements of only 6% of the deposit liabilities ever since they were introduced in 1984.⁷

Thus, the traditional instruments of monetary control are not effectively available to ECCB. As a central bank for the countries in the OECS region, ECCB exercises control on the monetary resources or broadly defined money supply in the economy without the help of these three most commonly used instruments.

The basic framework is provided by the money-multiplier theory at the root of which lies the identity that money supply (M) is the product of money multiplier (m) and high powered money (H); i.e.

$$M = m.H \qquad \dots (1)$$

Liburd and Temprow (1986) have tried to argue that money multiplier (m) was relatively stable for the ECCB member countries over the period 1975-85 as a whole. However, their data show wide annual fluctuations in money multiplier. Table 1 presents the time-series data on M,m,H and its components for the ECCB member countries for the period 1980 to 1990. From the table, it can be seen that not only that m changes considerably from year to year but it shows cyclical behaviour. Such a cyclical behaviour of m in the face of almost continuously declining trend in the proportion of currency and coins (cash) in circulation in the money supply (M1) implies that other elements in the money multiplier are also not stable in the ECCB area. However, the monetary management by ECCB is based on the assumption of stable m which implies exclusive focus on the monetary base for monetary control in the region.

⁷ Even in 1984, the policy was intended only to ensure uniformity in the minimum level of reserves in the ECCB area. Prior to this policy also, several banks held balances with the Central Bank in excess of the requirement. Prior to 1984, respective governments held the statutory reserves of commercial banks. The rates varied from country to country and the resources were used for financing budget deficits.

Year	Money supply		Monetary base (H)	Assets with ECCB		Money multiplier with M2	Proportion of cash in M1 (in %)
	M1	M2		NFA	DC		
1	2	3	4	5	6	7	8
1980	259	909	255	209	46	3.56	36.48
1981	287	1056	236	184	52	4.47	36.78
1982	294	1165	205	132	73	5.68	36.80
1983	315	1321	209	135	74	6.32	35.76
1984	362	1489	364	208	156	4.09	34.47
1985	378	1664	428	270	158	3.89	36.31
1986	513	2004	550	382	168	3.64	32.14
1987	602	2280	589	415	174	3.87	30.61
1988	804	2719	582	412	170	4.67	26.68
1989	946	3114	641	473	168	4.86	26.01
1990	939	3353	651	466	185	5.15	24.56

Note: (1) Figures for all years except 1990 are for period ended December; For 1990 the figures are for period ended September.
(2) Columns (2) to (6) are in EC\$ millions.
(3) From 1984, Statutory Required Reserves were introduced.
Source: ECCB Quarterly Reports.

Monetary base or the high powered money consists of the Net Foreign Assets (NFA) with ECCB which accounts for 60 to 70 percents of H (See Table 1) and Domestic Credit (DC) to the government sector and commercial banks. i.e.

$$H = NFA + DC \quad \dots (2)$$

NFA changes according to the overall balance of payments position. In other words, it is affected by ECCB's foreign exchange trading which essentially reflects changing conditions in the exports and imports markets as well as net flows of capital between the ECCB region and the rest of the world. In the presence of the fixed exchange rate regime in the ECCB region, control over NFA or an independent deliberate monetary policy to regulate it, is not possible. A direct relationship between the NFA and M is at the root of the fixed exchange rate regime.

The main focus of ECCB for monetary control, therefore, is the component of Domestic Credit (DC) in the monetary base. Since there are statutory limits imposed on the ECCB's credit to governments of the participating countries in the Agreement of 1983, ECCB can exercise sufficient control over this component unlike many other central banks of LDCs. It is precisely this component of DC which is manipulated through political pressures ultimately frustrating all serious efforts at monetary control in

other LDCs. The ECCB is an exception in this regard thanks to the strict provisions in the Agreement. The link between the fiscal policy and monetary policy is critically dependent on the ability and willingness of the central bank to monetize the budgetary deficits by extending credit to the government. In ECCB this aspect is very well regulated.

The monetary management of the system is done by deciding annual limits for domestic credit expansion. ECCB considers the existing level of NFA as well as the demand liabilities. It has an obligation to maintain a reserve of NFA of at least 60% of the currency liabilities with it. ECCB also generates some tentative forecasts of the magnitude of NFA during the year which represents more of judgement and informed guesses rather than any sophisticated forecasts based on a model. Considering the expected growth of incomes in the regional economy and the expected inflation rate in the economy which is adopted from the expectations about the U.S. inflation, the growth of nominal money supply is estimated. Based on the assumption of the stability of the money multiplier, the targetted growth of high powered money is obtained. Then, using equation (2) above, the target for domestic credit expansion in the region as a whole is derived as the residual. Once such a global target for DC is derived, it is decomposed and allocated to different member governments according to the share of a government in the total recurrent revenues in the region. The governments can use these quotas to finance their budget deficits as and when required but they cannot exceed them. ECCB may advise the governments on the composition of treasury bills and long-term securities. If any government wants to exceed its quota, it can do so only after modifying the provisions in the ECCB Agreement which requires unanimity of all participating government on the issue. So far, however, such a need has never arisen. Actually, the monetary arrangement through ECCB has been able to impose such fiscal discipline on the participating governments that "the global amount allocated in any one year has never been taken up in full, though on occasions individual governments utilized the full amount of their respective limits." (Liburd, 1990).

One of the reasons for such a disciplined performance by the participating governments is that they could borrow from the commercial banks. However, the impact on the economy would be very different in such a case as compared to the situation when the central bank extends credit to the government. In the latter case, there is a direct expansion in the monetary base resulting in a multiple increase in money supply. In the former case, there are greater chances of the phenomenon of crowding out of private sector credit occurring rather than the money supply increasing. This is because the money supply would be affected only when the government borrowing is financed out of excess reserves with the banking system if they exist. In such a case the money multiplier increases and the money supply is increased. Experience of the past decade (Table 1) suggests existence of such a phenomenon. Moreover, competition among commercial banks in the region is also limited and imperfect as discussed earlier. Some flexibility in interest rate structure exists but it is insufficient to eliminate excess reserves from the system. As a result, the effect of government borrowing from commercial banks is likely to be in terms of both crowding out as well as increased liquidity in the system. The existence of foreign banks only aggravate the situation. The excess reserves with the foreign banks are likely to be relatively less. When the governments borrow heavy amounts from the foreign banks, they may depend on their head quarters to lend the sum increasing the liquidity in the process. This can happen if the interest rates prevalent here are favourable as compared to abroad. However, as we have already seen, the government is borrowing largely from the local banks in this region with only small amount borrowed from the foreign banks. Secondly, the foreign banks in this region are not known to be very heavily and frequently dependent on their head quarters. The interest rates prevalent here are also by and large in line with those prevalent in USA. All these together reduces the significance of the government borrowing from the foreign banks in the ECCB region.

It is important to note that how the governments' borrowing is financed has direct implications on the balance of payments of the region. If it is financed by the ECCB credit, it is likely to lead to a reduction in NFA because it would increase the supply of liquidity relative to its demand in the system depressing the nominal interest rates. With fixed exchange rate regime (at least vis-a-vis U.S.A.) and lack of effective exchange controls, increased supply of liquidity and hence lower interest rates would give rise to increased net outflow of capital, domestic prices remaining the same. If exchange controls were effective, increased supply of liquidity would trigger off inflation in the domestic economy again depressing the real interest rates but, this time, affecting adversely the current account of the balance of payments through decreased competitiveness of the system. On the other hand, if the government borrowing is financed by commercial banks, normally the supply of liquidity remains more or less unchanged in the system. Increased demand for credit may, therefore, lead to increased interest rates giving rise to the phenomenon of crowding out. In the absence of effective exchange controls, increased interest rates prices remaining the same may lead to increased net inflow of capital thereby affecting the balance of payments. If exchange controls exist, change in the composition of output implied by the crowding out, may pull costs of domestic output downward making returns on investment and exports more attractive. This is likely to affect both the current and capital accounts of balance of payments favourably. A judicious mix of the two ways of financing the government borrowing and some basic fiscal discipline implicit in the monetary arrangements in the ECCB area are the critical elements in the monetary management by ECCB. The major problems in its way are the relative instability of money multiplier and the existence of excess reserves in the banking system in the region.

The interest rate policy of ECCB is expected to take care of these two problems. The minimum interest rate on the savings deposit was raised to 4% by ECCB in January 1985. With the objective of promoting financial intermediation by encouraging savings of small deposit holders. This was a major change because prior to 1985, the interest rates on savings deposits were as low as 2.5% or less. As the IMF study by Grant-Suttie and Vaez-Zadeh (1982) found, the time deposit rates were changed whenever there were deviations from the targetted liquidity with banks. In order to maintain the desired (target) rate of return, the lending rates were then adjusted. Fixing minimum interest rate on saving deposits at 4% is expected to affect this process and rationalize the interest rate structure. The interest rates as well as movements therein varied from country to country within the ECCB region as can be seen from Table 2. Even within a country, the effective interest rates vary between the foreign banks and local banks as already discussed. The interest rate structure in different OECS countries showsthat the nominal spread between the saving deposit rate and the prime lending rate ranges between 6 to 8 percentage points, but as Liburd and Ferracho (1985) have argued, the effective spread has been much wider. It depends on the structure of the deposit base and the discounting procedure used for lending operation. Moral Suation is actively pursued by ECCB to encourage the banks to reduce lending rates particularly when their liquidity position is not tight. All these point to the existing imperfections in the competition among commercial banks in the area. However, interest sensitivity of bank deposits in the area also cannot be ignored. The proportion of cash in money supply has been falling since 1985 implying increased proportion of bank deposits in the money supply. If the money supply is interest elastic in the region, the volatility of the money multiplier can be controlled with proper interest rate policy. It is for this reason that ECCB monitors both the interest rate and the monetary base as targets for achieving the desired money supply.

The monetary control in the ECCB member countries requires monitoring the most important element of NFA. It is already argued that NFA is largely governed by conditions in the export and import markets and flows of capital to and from abroad. While the capital flows are determined to some extent by the interest rates and expectations of exchange rate fluctuations, the export-import markets are largely

determined by the degree of competitiveness of the economy which is measured by the real effective exchange rate (REER). The latter is determined by the domestic inflation rate in relation to the inflation abroad besides the nominal exchange rate. In order to maintain exchange rate stability, the EC dollar has been pegged to the U.S. dollar since July 1976 at the rate of \$1 U.S. = EC \$2.70. This arrangement makes EC\$ move in the same way as the U.S.\$ in the international market. Since different member countries have different trading partners and since their trade composition and pattern are significantly different, they are affected differently by the movement of US \$ against major currencies in the world market. Such effects include the ones on the competitiveness of the economies, their foreign exchange earnings through exports and imports, and the cost of living as reflected in the consumer price inflation index. The countries like Dominica and Grenada are more directly hit by the fluctuations of the U.S. dollar because of the pre-dominance of their trade with non-U.S.\$ linked countries.

Table 2: Interest Rates in Commercial Banks in ECCB Member Countries, 1984-90 (in %)								
End of Year	Deposit Rates		Lending Rates		Deposit Rates		Lending Rates	
	Savings	Time	Prime	Others	Savings	Time	Prime	Others
1	2	3	4	5	6	7	8	9
	Country: Anguilla				Country: Antigua & Barbuda			
1984	3.5-4.0	7.5-8.0	10.0-11.5	10.0-16.0	2.5-6.0	7.0-13.0	12.5-13.0	12.5-18.0
1985	3.5-4.0	6.0-7.0	9.0-12.0	9.0-16.0	3.5-6.0	4.8-08.5	9.0-13.0	9.0-24.0
1986	3.5-4.0	5.0-6.3	10.0-12.0	10.0-16.0	3.5-5.0	4.0-08.3	11.0-13.0	11.0-23.2
1987	4.0	4.5-6.3	10.0-12.0	10.0-18.1	3.5-5.0	4.0-07.5	10.0-12.0	10.0-23.2
1988	4.0	4.0-6.3	10.0-12.0	10.0-20.0	4.0-5.0	4.0-07.5	10.0-11.5	10.0-23.2
1989	4.0	4.0-6.3	10.0-12.0	10.0-18.1	4.0-5.5	4.0-10.0	10.0-12.0	10.0-23.2
1990	4.0-7.8	4.0-9.0	10.0-12.0	10.0-18.1	4.0-7.5	4.0-10.0	10.5-12.0	10.5-23.2
	Country: Dominica				Country: Grenada			
1984	2.5-3.0	5.5-6.0	9.0-10.0	9.0-14.0	4.0	4.0-8.0	9.0-10.5	9.0-12.5
1985	4.0	5.5-6.0	9.0-10.5	9.0-15.0	4.0-5.0	4.0-8.0	10.5-11.5	10.5-15.0
1986	4.0	4.0-6.0	9.0-10.5	9.0-19.7	4.0-5.0	4.0-7.5	10.5-11.5	10.5-14.0
1987	4.0	3.5-6.0	9.0-10.5	9.0-19.7	4.0-5.0	4.0-6.5	10.5-11.5	10.5-14.0
1988	4.0	3.5-6.0	9.0-10.5	9.0-18.2	4.0-5.0	4.0-6.0	10.5	10.5-15.0
1989	4.0-5.0	3.5-6.0	9.0-10.5	9.0-18.2	4.0-5.0	4.0-7.0	10.5	10.5-15.0
1990	4.0-6.5	3.5-8.0	9.0-10.5	9.0-18.2	4.0-5.0	4.0-8.0	10.5	10.5-15.0
	Country: Montserrat				Country: St. Kitts & Nevis			
1984	2.5-6.3	3.5-5.5	8.5	8.5-14.0	2.5-5.0	5.5-7.0	8.0-10.0	8.0-17.5
1985	4.0	4.0-5.5	9.5-10.0	9.5-18.0	4.0-5.0	5.0-8.0	8.0-12.0	8.0-17.3
1986	4.0-5.0	4.0-5.5	9.5-10.0	9.5-18.0	4.0-5.0	4.0-7.0	8.0-12.0	8.0-18.2
1987	4.0	4.0-6.0	9.5-10.0	9.5-18.0	4.0-5.0	4.0-6.5	9.5-12.5	9.5-18.2
1988	4.0	4.0-6.0	9.5-15.0	9.5-18.0	4.0-6.5	4.0-8.0	9.0-12.0	9.0-23.3
1989	4.0-6.0	4.0-7.5	9.5-12.0	9.5-18.0	4.0-6.5	4.5-9.0	9.0-12.0	9.0-23.3
1990	4.0-5.3	4.0-7.0	9.5-11.0	9.5-17.3	4.0-6.5	4.5-9.0	9.0-12.0	9.0-23.3

	Country: St.Lucia				Country: St.Vincent & Grenadines			
1984	3.0-6.3	7.5-10.0	13.0-14.0	13.0-22.0	2.5-5.0	4.5-7.5	9.0-12.0	9.0-14.5
1985	4.0-8.5	3.3-10.0	12.0-14.0	12.5-19.5	3.0-5.0	4.5-7.5	11.0-12.5	11.0-15.5
1986	4.0-6.0	2.8-10.0	10.5-14.0	10.5-22.9	4.0-6.0	4.3-7.5	12.0	12.0-15.5
1987	4.0-5.3	4.0-6.0	9.0-11.0	9.0-23.9	4.0-5.0	4.5-6.5	11.0-12.5	11.0-15.5
1988	4.0-5.3	4.0-6.5	9.0-10.0	9.0-23.1	4.0-5.0	3.8-6.3	11.0-12.0	11.0-15.5
1989	4.0-5.3	4.0-6.5	9.0-10.0	9.0-23.0	4.0-5.0	3.8-5.8	11.0-12.5	11.0-15.5
1990	4.0-6.0	4.0-7.0	9.0-10.5	9.0-21.3	4.0-5.0	3.8-5.5	11.0-12.5	11.0-15.5

Source: ECCB: Commercial Banking Statistics (Monthly Publication).

It is found that the consumer price inflation is highly associated with the prices of food articles in the Caribbean region (See Caribbean Community Secretariate, 1988, p. 169). For the small open economies of OECS region heavily reliant on imports of food and other necessities, domestic inflation is largely imported. However, it determines their competitiveness through the real effective exchange rates. Table 3 provides information on the rates of growth of real GDP and inflation for the member countries for the five years 1985-89. It can be seen from the table that the ECCB member countries have experienced a very high growth and relatively low inflation rates in recent years. However, the performance has been considerably different across the countries. Considering the fact that all these countries have the same currency and monetary policy, differences in the inflation rates although of small magnitude, may appear to be surprising. However, when we consider that (i) interest rates prevalent in these economics are different (Table 2); (ii) the growth of real GDP differs substantially during the given years (Table 3) and (iii) that composition of exports and imports are different giving rise to different trade weighted nominal exchange rates, it is possible to reconcile differing inflation rates among the ECCB member countries. In order to appreciate the magnitude of the effect of fluctuations of US \$ on effective exchange rates for the ECCB member countries, Table 4 provides information on REER for these countries over the period 1977-87. It can be seen from the table that the differences in the movements of REER are confined only to the rates of change rather than direction of change among the member countries. However, the differences in REER existing over a given period of time are very crucial for the individual economies and their relative as well as absolute performances over the period.

Countries	Annual Rate of Growth in Real GDP					Annual Rate of Inflation (CPI)				
	1985	1986	1987	1988	1989	1985	1986	1987	1988	1989
1	2	3	4	5	6	7	8	9	10	11
1. Anguilla	8.2	11.1	12.3	9.3	9.0	N.A.	2.3	2.6	4.5	4.9
2. Antigua & Barbuda	7.8	8.4	8.8	7.6	6.2	-2.0	0.5	3.6	3.4	5.3
3. Dominica	1.7	6.8	6.8	7.9	-1.6	3.5	3.0	2.9	5.2	4.2
4. Grenada	4.9	5.5	6.0	5.3	5.6	1.8	-0.8	0.6	6.5	3.7

5. Montserrat	4.6	5.8	10.8	12.4	N.A.	3.2	0.2	2.7	3.6	1.8
6. St.Kitts & Nevis	5.6	6.3	7.5	6.7	5.1	1.8	-0.8	2.6	0.2	6.6
7. St.Lucia	6.0	5.8	2.1	6.8	4.0	1.0	4.5	5.1	1.6	3.8
8. St.Vincent & Grenadines	5.9	7.2	6.4	8.6	5.9	1.3	0.5	3.4	2.1	3.5
Source: ECCB Annual Reports.										

The World Bank study (1989) has tried to provide an explanation for the variations in REER by identifying the major causes as: (i) the resource gap as defined in terms of excess of real aggregate expenditure over real output (aggregate supply) which is measured as excess of imports over exports of goods and non-factor services as a proportion of real GDP; (ii) the relative price of bananas with four out of the eight member countries having preferential market for their bananas in U.K. such that they get a much higher price for their bananas than the Central American producers which exert both the expenditure and substitution effects on domestic price levels; and (iii) changes in REER between the U.S.\$ and other major currencies affecting domestic prices in the ECCB member countries through their impact on prices of the traded goods. The study found that on an average one percentage point (i) increase in the resource gap causes a real appreciation of EC \$ by 0.4%; (ii) appreciation of U.S.\$ vis-a-vis other major currencies results in real appreciation of EC \$ by 0.7%; and (iii) increase in the real price of banana causes the real appreciation of EC\$ in Dominica, St.Lucia and Grenada by about 0.4% to 0.5%. These results assume no changes in other factors. They clearly point to the three fundamental issues in the exchange rate management in the ECCB area. These issues are so vital that the future of ECCB as a monetary arrangement depends on them.

Year	St.Kitts & Nevis	Antigua & Barbuda	Dominica	Grenada	St.Lucia	St.Vincent & Grenadines
1	2	3	4	5	6	7
1977	98.95	90.15	114.86	118.33	98.61	99.91
1978	100.62	95.39	121.56	114.31	101.48	105.19
1979	103.01	97.51	114.89	106.67	105.10	103.13
1980	100.00	100.00	100.00	100.00	100.00	100.00
1981	89.43	92.76	87.75	83.69	86.38	88.22
1982	82.40	82.96	81.98	75.80	80.62	80.29
1983	79.68	78.04	77.89	70.62	78.53	75.26

1984	76.82	73.32	75.49	66.23	76.83	72.61
1985	74.77	68.24	73.60	64.31	75.48	70.79
1986	82.85	72.78	79.54	71.19	82.15	77.83
1987	90.34	74.52	83.49	78.94	84.46	83.25

Note: The real exchange rate is measured using a weighted average of the wholesale price index in 6 major countries.
Source: World Bank (1989).

7. Future Challenges For ECCB

Liburd and Bain (1989) have shown that domestic saving rate in the OECS region is not affected by the real interest rate but is negatively influenced by the magnitude of foreign saving rate. The latter is, however, directly determined by the resource gap which is found to influence the REER. The resource gap could be financed either by foreign aid or by foreign private investments. Table 5 provides some estimates of the domestic and foreign savings over the period 1981-88 and Table 6 provides information on the summary of balance of payments for the five years 1985-89 for the ECCB member countries. From these tables, it is very clear that the OECS countries are heavily relying on foreign savings to sustain their growth. As long as they get preferential treatments for their exports, such trends may not pose serious threats, but if such preferential access to the markets of their major exports stops, heavy reliance on foreign investment would start becoming a burden to the economy raising problems of debt servicing and repatriation of factor incomes. The long term solution is, therefore, to encourage domestic savings and reduce reliance on foreign savings. Since this is well recognised by the governments in the area, the variations in the level and rates of REER across the countries are not desirable.

Country	Rates	1981	1982	1983	1984	1985	1986	1987	1988
1	2	3	4	5	6	7	8	9	10
1. Antigua	s_d	11.8	10.5	18.1	15.4	10.2	11.0	13.0	N.A.
	s	53.2	49.7	25.5	31.6	28.0	36.0	42.0	N.A.
	s_f	41.4	39.2	7.4	16.2	17.8	25.0	29.0	N.A.
2. Dominica	s_d	-4.0	9.4	16.5	19.7	5.0	15.0	13.0	N.A.
	s	37.3	33.6	32.3	44.9	28.0	22.0	23.0	N.A.
	s_f	41.3	24.2	15.8	25.2	23.0	7.0	10.0	N.A.
3. Grenada	s_d	13.0	17.2	14.2	14.4	1.0	2.0	8.0	10.0
	s	47.0	62.8	52.2	39.4	31.0	33.0	35.0	36.0
	s_f	34.0	45.6	38.0	25.0	30.0	31.0	27.0	26.0
4. Montserrat	s_d	-27.1	-25.1	-19.8	-11.5	-17.0	-10.0	-8.0	-1.0
	s	52.7	45.2	33.5	21.9	27.0	34.0	39.0	47.0
	s_f	79.8	70.3	53.3	33.4	44.0	44.0	47.0	48.0

5. St.Kitts	s_d	28.0	22.4	-0.4	19.4	8.0	7.0	-1.0	-7.0
	s	38.3	40.0	36.6	29.4	32.0	28.0	29.0	31.0
	s_f	10.3	17.6	37.0	10.0	24.0	21.0	30.0	38.0
6. St.Lucia	s_d	-2.3	14.4	23.3	16.2	18.0	29.0	24.0	N.A.
	s	55.0	46.5	35.2	35.7	35.0	38.0	44.0	N.A.
	s_f	57.3	32.1	11.9	19.5	17.0	11.0	20.0	N.A.
7. St.Vincent	s_d	0.8	14.4	27.3	32.3	22.0	18.0	7.0	13.0
	s	39.0	36.3	36.1	38.9	28.0	20.0	33.0	31.0
	s_f	38.2	21.9	8.8	6.6	6.0	2.0	26.0	18.0
<p>Note: s_d is Gross Domestic Saving as % of GDP; s is Gross Domestic Investment as % of GDP; and s_f is Foreign Savings as % of GDP.</p> <p>Source: Statistical Department, OECS Secretariat and ECCB Estimates.</p>									

Closely connected with the above is the threat of EC 1992 developments which are likely to give a severe external shock to the OECS countries - particularly those dependent on banana exports. Currently under the Lome Agreement Protocol between the EEC and ACP states, bananas are sold in the protected UK market at a much higher price than the world price. The estimated implicit subsidy received by the OECS banana exporting countries through the protected UK market was of the order of US \$ 149 million or 6% of GDP between 1980 and 1986 (World Bank, 1989, p.29). In 1986 alone, the subsidy came to about 37% of the value of banana exports. If the proposed single integrated market in Europe results in elimination or significant reduction of this subsidy, its effects on REER can be estimated by the results of the World Bank study (1989) reported in the previous section. Only by itself, a fall in the real price of banana to such an extent would lead to a substantial real depreciation of EC\$. If we add to it the effects on resource gap of such a fall in banana price, the REER would depreciate still further. With fixed nominal exchange rates, such huge depreciation in real terms could be achieved only with strong deflation on prices, output and employment in the domestic economy. Unemployment would rise, real wages would decline, output and incomes would fall dramatically. If, however, the prices of the non-traded goods were downward rigid, such a drastic depreciation in real terms could be achieved by devaluing EC \$ with respect to the U.S.\$. Such a situation would be further aggravated by expectations for depreciation leading to capital flight from OECS countries. At this stage, it is important to note that devaluation requires unanimity among ECCB member governments and that only 4 out of the 8 member countries would be severely hit by the banana price crash. The devaluation to such an extent may not, therefore, be agreed upon.

Year/Items	Antigua	Dominica	Grenada	Montserrat	St.Kitts	St. Lucia	St. Vincent
1	2	3	4	5	6	7	8
1985: GDP	464.8	223.3	246.2	86.0	171.8	388.8	250.2
Resource Gap	98.1	62.3	93.3	27.6	43.6	79.6	14.5
Current A/c	-67.0	-9.2	11.2	1.0	-10.8	-25.4	23.9

Capital A/c	78.5	11.7	15.5	5.9	15.4	40.0	2.0
1986: GDP	537.2	253.3	279.2	97.9	213.2	426.6	282.0
Resource Gap	375.6	20.7	95.9	29.6	46.9	43.7	32.6
Current A/c	-342.9	11.3	-1.1	-0.6	-18.3	4.5	16.0
Capital A/c	370.0	4.0	6.9	8.2	26.7	26.3	15.1
1987: GDP	614.2	281.8	320.5	113.5	239.8	453.2	318.0
Resource Gap	212.1	38.1	114.8	38.5	59.6	60.9	70.1
Current A/c	-189.9	4.8	-66.7	-6.1	-28.1	-14.2	-41.7
Capital A/c	183.2	19.5	77.1	9.5	29.9	29.4	26.6
1988: GDP	722.7	324.3	350.2	146.3*	278.3	504.4	358.5
Resource Gap	215.1	64.2	107.2	41.7	87.1	34.1	37.4
Current A/c	-189.0	-20.3	-54.5	-5.3	-52.3	-3.9	-7.4
Capital A/c	196.0	18.2	39.6	6.1	52.1	9.7	12.6
1989: GDP	773.1	339.5	376.4	N.A.	302.3	545.5	393.2
Resource Gap	254.4	142.1	135.8	38.6	85.8	161.0	76.3
Current A/c	-220.9	-87.4	-86.5	21.4	-50.5	-128.5	-30.0
Capital A/c	221.0	89.4	82.9	-20.7	67.6	143.6	32.7
* at current market prices							
Note: (i) GDP is at current factor cost.							
(ii) Resource Gap is measured as excess of imports over exports of goods and non-factor services.							
(iii) Figures for 1989 are Provisional estimates.							
Source: ECCB Annual Reports.							

The deflationary pressure on the banana exporting countries would lead the whole region into a severe balance of payment crisis because reduction in income and prices in those countries would lead to excess supply of liquidity resulting in lower interest rates inducing capital flights and severe pressure on the foreign exchange reserves not only of the affected countries but also of all ECCB member countries. Since these will be deficits, they are hard to handle. In the past favourable external shocks through banana boom was experienced. It was easy to handle because surpluses can be invested off-shore but deficits cannot be met likewise so easily.

The hard options before the ECCB member countries are to search some solutions within, e.g. try to diversify the economic base of their economies; develop sound alternative exports or foreign exchange earning activities like tourism; promote greater freedom of movement of capital and labour across member countries; increase flexibility in resource use by reducing restrictions on land-use, introducing flexibility in money wages, company laws, etc. In other words it calls for a greater integration and liberalization of the economies of member countries. It puts further constraints on the political and economic choices of the member countries.

The other option is to reconsider the pegging of EC\$ with the US\$. Instead, it could be pegged to a basket of currencies or a freely floating exchange rate system. In both these latter alternatives, continuous political and administrative attention is needed. Moreover, the level of sophistication, skills and competence required to manage such a system effectively is not readily available in the region. The current fixed exchange rate system on the other hand is simple to administer. The current system has served the member countries reasonably well so far. It has withstood external shocks as well. However, the imminent shock is different in its magnitude and differential impacts on member economies. It will really test the soundness of the monetary integration model of the ECCB.

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PART IV : TOURISM DEVELOPMENT

Chapter 11

Tourism Development in St.Kitts and Nevis: Problems and Prospects

I. The Background

St.Kitts and Nevis is small twin island country in the northeastern Caribbean Sea. The two islands of St.Kitts and Nevis are separated by a 2 mile wide channel referred to as "The narrows". Their total geographical area is 104 sq.miles - 68 sq.miles for St.Kitts and 36 sq.miles for Nevis. The population of the country is about 43 thousands - 35 thousands for St.Kitts and 8 thousands for Nevis. Topographywise both the islands are mountainous and volcanic consisting of central mountain mass rising from the sea. The highest point on St.Kitts is at 3,792 ft. and on Nevis is at 3,232 ft. above the sea level. The mountains are almost fully covered with greeneries. Both the islands have excellent beaches. Climate is tropical with temperature generally remaining between 20 and 30 degrees Celsius (See Table 1). Average annual rainfall is about 55 inches in St.Kitts and 48 inches in Nevis. Water supply is abundant throughout the year on both the islands. Although there are no known commercially viable mineral deposits, the nature has been very bountiful to the islands of St.Kitts and Nevis in terms of scenic beauty of gentle rolling landscapes, tropical rain forests, majestic mountain ranges and climate. The islands are, however, subject to devastating hurricane which strikes the islands once in a while. The last it struck was in September 1989 causing enormous loss of crop, fish and property.

The islands were discovered for the Europeans by Christopher Columbus in November 1493. After a century long struggle between the French and the British, ultimately they became British colony in 1783. In 1967, St.Kitts and Nevis became a "State in Association" with Britain. Only in September 1983, the country gained full independence. It is a member of the British Commonwealth, the Caribbean Community (CARICOM), the Caribbean Development Bank (CDB), the Organisation of Eastern Caribbean States (OECS) and the Eastern Caribbean Central Bank (ECCB). It has a parliamentary democracy with a stable government. It may be noted here that the political climate in the country is one of the most stable in the western hemisphere. It extends cooperation to other member countries of CARICOM in areas such as economic policy, trade, industrial policy, nutrition and foreign relations. It also shares a common currency, regulation of civil aviation and common institutional arrangements for the judiciary.

Traditionally, the economy of St.Kitts and Nevis was plantation-based, dominated by a single crop of sugarcane accounting for 75% of the total arable land (18,618 ha.) and contributing about 50% of the value added by the agricultural sector. The other half is contributed by vegetables, fruits, other crops like cotton, copra, coconut, corn, coffee, etc., livestock and fishing. Forestry is surprisingly negligible. Although the contribution of agriculture in terms of gross domestic product (GDP) has been declining from about 17% in 1981 to 9% in 1989 (See Table 2), the sector has a significant role to play in the economy. It satisfies almost 40% of the domestic food requirements besides generating the largest amount of employment in the economy. Its direct forward linkages are with the sugar industry in the domestic manufacturing sector which accounts for nearly 35% of domestic exports (See Table 2). The declining importance of sugar industry is partly due to problems of management and labour shortages within the industry and partly due to the government's efforts to take economy away from heavy reliance on sugar. It can be seen from Table 2 that food is a major item of import, the other one being machinery. To reduce the import bill, diversification of agriculture to produce vegetables and fruits where the islands have relative advantage is the obvious alternative before the government which is pursuing it rigorously.

The per capita GDP at current prices in St.Kitts and Nevis is estimated at EC \$6800 in 1989. Since EC dollar is pegged to the U.S. dollar, the exchange rate between them is fixed and stable at U.S.\$ 1 = EC \$ 2.70. Thus, the country is classified as belonging to the upper middle income countries category as per the World Bank classification. The growth in the real GDP in the country during the last decade has been remarkable except for the year 1983 when it experienced negative growth in real GDP. Its average annual compound rate of growth during the period 1981-89 works out to be as high as 5.6%. It is, thus, a fast growing economy with manufacturing, construction, trade and 'other activities' (including hotels and transport) expanding more rapidly than other sectors like agriculture, government services, etc. (See Table 2).

In terms of other development indicators also, the islands economy is fairly well developed as can be seen from Table 3. The literacy rate among adults is about 90%. Access of the population to safe drinking water and electricity is 100%. Population per doctor is 2800 and population per hospital bed is only 100. The islands, moreover, have very good road net-work with about 300 k.m. length of roads in the two islands together. Out of these, nearly 127 k.m. length of roads are paved, 96 k.m. are unpaved and 83 k.m. are track roads. The main highway on St.Kitts runs around the perimeter of the island and covers about 53 k.m. length which also represents an attraction in itself. The unemployment rate fluctuates between 10 to 20% as per a rough estimate. There is considerable seasonal variation in it particularly because there are two peak seasons - harvest season and tourist season. The main problem of the economy, however, appears to be the negative growth of population. It is not on account of the natural growth of population but due to migration. There are no institutions of higher learning in St.Kitts and Nevis. The students have to therefore go to other countries either in the Caribbean or north America for higher studies. Many a times, they tend to settle there. Moreover, the local population generally has very close family connections in U.S.A., Canada or U.K. The earning opportunities attract them out of St.Kitts and Nevis though they usually retain land and property here so that they could return here for their retirement. However, temporarily, this causes severe stress on the skilled labour market and has the perverting effect on the cost structure in the country.

The government has perceived tourism as an important source of growth in the country's economy. It not only generates direct income and employment in the hotel sector but also has considerable linkages with other sectors in the economy. In other words, the government considers tourism development as an essential driving force. In the next section, we consider the prospects and potential of tourism in St.Kitts and Nevis. In the third section, then we discuss the role of tourism in the economy. The fourth section is devoted to the review of the government's efforts to develop tourism in the two islands. Finally, in the fifth section, we discuss a few issues emerging out of the tourism development efforts in St.Kitts and Nevis.

II. Growth of Tourism In St.Kitts & Nevis

Tourists arrivals to St.Kitts and Nevis have increased remarkably during the last decade. Between 1981 and 1990, the number of stay-over visitors has increased by 113% or at an annual compound rate of 8.8%. The cruise ship passengers have increased by 213% or by annual compound rate of 13.5% over the same period. The total visitors to the islands have, thus, more than doubled in the last 9 years (See Table 4). It is also very clear from the statistics on the tourists inflow in these islands that more than half of the total tourists who come here are from the North America. U.S.A. has the highest share followed by Canada in the visitor traffic here. The situation was not the same at the beginning of the decade. CARICOM countries and United Kingdom contributed a greater share of the passenger traffic to these islands upto 1984-85 when there was a quantum jump in the visitor traffic from Canada to these islands. This was largely due to the aggressive marketing efforts both by the government's tourist department and the island's largest hotel, Jack Tar which started operating chartered flights from Canada and later from U.S.A.

The high growth of tourism in these islands was achieved by constant effort to improve tourists' facilities in the islands. There was for example a significant increase in the airline seats, telephone subscription and number of licensed vehicles in the two islands as can be seen from Table 5. The aircraft arrivals almost doubled and the telephone subscription increased by more than four-fold during the last decade. We have already seen that in terms of basic infrastructure like roads, electricity and water, the islands are very well equipped. Even the accommodation facilities for the tourists have also expanded considerably during the last decade. In 1980, the total number of rooms in hotels and guest houses were hardly 500 in both the islands together. In 1991, there are approximately 1400 rooms in the two islands - St.Kitts having about 880 rooms and Nevis about 520 rooms. Currently, there are 25 hotels - 16 in St.Kitts with 786 rooms/units and 9 in Nevis with 450 rooms/units. There are about 31 guest houses/appartments/cottages in the two islands.

In order to assess the potential for future growth of tourism in St.Kitts and Nevis, it is important to note some of the recent developments taking place in the two islands in this context. Only in February 1990, the Southeast Peninsular highway was inaugurated. This road, built with a concessional loan from U.S.A. is only 10 k.m. long but allows access for the first time to some of country's best beaches and provides for one of the most scenic drives in the Caribbean. This Peninsula is one of the few remaining undeveloped and now easily accessible areas in the Eastern Caribbean. The eight beachfront properties now made available for development in this narrow stretch of land are hardly 25 minutes or less from the Golden Rock International Airport in St.Kitts with an 8,000 ft. runway capable of easily accommodating large jet aircrafts. The Peninsula is ready for development with all necessary infrastructure for hotel constructions including underground electric and telephone lines. Several international developers and hotels companies are moving quickly to take advantage of the emerging opportunities by coming up with proposals for big and luxurious hotels and resorts. On Nevis also, four seasons and Dumez construction company have completed a 196 room hotel resort with 18 hole golf course at Pinney's Beach on the west coast and have proved to be a grand success. Moreover, there are several additional sites in the area available for sale and development.

That the opportunities exist for hotel construction and development of sites on the islands is clear from the above discussion. Whether these opportunities would be converted into successful business propositions or not could be assessed if we look at the hotel occupancy rates of some selected hotels in St.Kitts. Table-6 presents this information for 1988. As can be seen from the table, the country's largest development viz. Jack Tar Village with 263 rooms has been doing extremely well with the occupancy rates in both the tourists' season (winter) and off-season. Apart from Jack Tar, the average capacity of hotels was only 27 rooms in 1988. Table-7 presents the percentage distribution of total stayover tourists arrivals in St.Kitts and Nevis by months for the last five years. It can be seen that November to March represent months with relatively higher tourist traffic in the two islands with December contributing the highest tourist arrivals. In the light of such a nature of the traffic flows the small hotels suffer from seasonality and low occupancy rates. Moreover, they are not geared to the requirements of large volume international vacation travel. A minimum scale of operation of a hotel which matches hotel beds with seats on wide-bodied charter aircraft like the Jack Tar can only generate volume traffic year round. It is for this reason that bigger hotels with clear clientele identified and ability to market and own tour operators have better chances of success. What is likely to occur in future in St.Kitts and Nevis is that bigger and luxurious hotels would come up on the abovementioned sites. This is further supported by the fact that as per 1990 data, almost 94% of the visitors come here for holiday and pleasure whereas 5% come for business purposes. The remaining 1% are visiting for health or educational purposes. Similarly, in 1990, about 53% of the tourists stayed in a hotel, about 8% stayed in guesthouses, appartments, villa, etc. and about 38% stayed with friends, relatives or own homes. The 1990 data on occupational break-up of visitors also reveal that, out of the total visitors, 4.5% are holding administrative or managerial position, 38.9% are professionals, 18.4% are office workers whereas 9.3% are blue collar workers, 3.6% are in other occupations, 13% are students, 5.3% are housewives and only 3.7% are retired or disabled persons. In terms of the age composition of the visitors, the age-group 30-49 accounts for about 44% of the total visitors to these twin islands.

Table-8 presents the average length of stay in days of the stayover tourists in St.Kitts and Nevis over the years 1981-90. It can be seen from the table that the length of stay of the tourists has considerably increased from only 5.4 days in 1981 to 8.6 days in 1990. This increase alongwith the phenomenal increase in the number of tourists to these islands implies that there has been a tremendous increase in the tourists' time spent on the islands over the last decade. Tourism activities in these islands are indeed booming. The increased average length of stay, moreover, is largely on account of the increase in the average length of stay of tourists in hotels and guest houses as revealed by the Table-8. Thus, demand for hotel accommodation is on increase in St.Kitts and Nevis and if the present trends continue, hotel industry in these islands would be perhaps the fastest growing industry. This is all the more so because the fundamental characteristics of the islands as the natural attraction to tourists viz., clean, green, accessible, sunny, unpolluted beaches and affordable - are not going to change in near future.

III. Role of Tourism in the Economy

The National Development Plan of St.Kitts and Nevis 1986-90 devotes considerable attention to tourism as a sector and observes, "Tourism has been playing an increasingly important role in the development process as indicated by this sector's performance during the last few years. There is full evidence that this sector has considerable potential for further development of the economy. This potential will be fully exploited, given the government's policy of diversification of the economy from its traditional base of sugar. The sector's contributions to Gross Domestic Product (GDP), employment and foreign exchange earnings have increased significantly." (p.121). Thus, the role of tourism in a small island economy like St.Kitts and Nevis is not confined only to its direct contribution to the income, employment and foreign exchange earnings but also includes more important indirect contributions by generating demand in the economy for variety of commodities and services and thereby helping revitalization and diversification of the economic base. Some of the clear beneficiary sectors out of expansion of tourism activities are: Hotels & Restaurants, Construction, Electricity & Water, Wholesale & Retail Trade, Communications and Banks & Insurance. Similarly, fishing and manufacturing other than sugar might also receive some benefits out of increased extent of tourism. Table 9 represents the GDP at 1977 constant prices for all these sectors for selected years. It can be seen from the table that all these sectors and sub-sectors have experienced improvements in their shares in real GDP over the period 1977 to 1988, with the most remarkable growth in the sectors of Hotels & Restaurants and Communications. All these sectors together accounted for nearly 44% of the total real GDP of the country in 1977 and about 60% in 1988. The real driving force behind this large segment of the economy is tourism which is fully recognised by the government of St.Kitts and Nevis.

In terms of employment, it is estimated that 1,572 persons are directly employed in 1989 in tourism related activities like hotels, restaurants, guesthouses, local transport and water-sport¹. With expansion of tourism, there would be significant increase in the demand for workers in most of the above-mentioned sectors/sub-sectors of the economy. Such employment generation is basically the result of the interlinkages obtaining within the economy with the tourism sector. The World Bank study (Nov. 1989), however, draws attention particularly to the likely shortages of labour during heavy construction periods. The islands have already started experiencing serious shortages of labour in the peak agricultural seasons due to more lucrative construction activity expansion. According to the World Bank, the hotel room availability in St.Kitts and Nevis is projected to increase to 2051 in 1994 and to 3303 in 1999. Similarly, direct employment in tourism related activities is also projected to increase from 1572 in 1989 to 4102 in 1994 to 6274 in 1999. Such a rapid growth of employment in a particular sub-sector would have significant effects on the wage-structure in the economy, unless specific measures to train workforce in the relevant occupation are taken along with liberalising immigration policies. Table 10 presents prevalent weekly average wage-rates (in US \$) assuming 45

¹ Second round employment effects in agriculture and manufacturing and employment in construction activities related to tourism are excluded.

hours per week for the year 1987 in St.Kitts and Nevis in selected occupations. As can be seen from the table, the construction workers already have relatively very high wage rates and if steps are not taken to ensure their adequate supply, their wages would further rise. This may become a constraint for the growth of the sector in the country.

The contribution of tourism to the country's foreign exchange earnings is mainly seen in terms of the tourists' expenditure in the country. Table-11 presents estimates of average daily expenditure by visitor categories and total visitor expenditures for the years 1981 to 1990. It can be observed that total visitor expenditure has increased by about 350% over the 9 years 1981 to 1990 implying a staggering 18% rate of growth compounded per annum. In terms of the potential as revealed by the growth in the recent past, tourism has been the single most important foreign exchange earning activity for St.Kitts and Nevis. In fact, since 1987, travel receipts have been higher than the earnings out of all merchandise exports put together in St.Kitts and Nevis. It accounts for almost 45% of the foreign exchange earnings on current account of the balance of payments in the country.

Tourism also contributes directly to the government revenues. In St.Kitts and Nevis, the government has created several avenues to tax the tourist almost directly. The indirect taxes on his consumption items are of course extra. The direct avenues are: hotel room tax, departure tax, travel tax and foreign currency tax. Table 12 presents the actual receipts from these sources and the total actual receipt on recurrent account of the government of St.Kitts and Nevis for the years 1980 to 1989. The proportion of revenue from these four sources to the total revenue on recurrent account has increased from 3% in 1980 to 4.5% in 1989. The tax revenue from these four sources grew at an average compound rate of 10.6% p.a. during the period 1980-89. Compared to the growth of tourist traffic and the tourist expenditure in St.Kitts and Nevis over the same period, the growth in the (direct) tax revenue from tourists appears to be on the lower side. This is particularly so because except the foreign currency tax which was removed in 1983 and reintroduced in 1986 at a lower rate, the rest of the taxes have been revised upwards, e.g. travel tax was 5% and was revised to 7.5% from 1985. Similarly, hotel room tax was 5% and was revised to 7% from 1983. One of the explanations could be the increasing amount of tax evasion by the hotel owners.²

The basic contribution of tourism is to increase the number of people on the islands. When we consider the average length of stay and the volume of visitors, we find that in 1990, the visitor population was equivalent to about 5% of the resident population in terms of total days spent on the islands. This obviously raises the demand for the private goods and services on the islands but it also raises the demand for the public goods and services on the island. To this extent, increased tourist flow could be a burden to the government and it is, therefore, justified in collecting some contribution from the tourists in the form of taxes. A share of 4.5% in the form of direct tax collection from visitors when they are contributing only about 5% equivalent of the resident population appears very reasonable and fair though their actual contribution would be much higher when we add the indirect taxes they have to pay. One can argue, therefore, that the government in St.Kitts and Nevis is discriminating against the visitors and subsidising local population by charging the foreigners more. This argument ignores, however, the ability to pay of the locals and foreigners.

The discussion of the role of tourism would remain incomplete without considering its interlinkages with precise sub-sectors in the economies of St.Kitts and Nevis. Data constraints do not allow precise quantitative estimates but it is possible to list out the sub-sectors and their products through which major interlinkages exist with tourism in the economy. The following is an attempted tabular classification of some major linkages with tourism in St.Kitts and Nevis.

² It is interesting to note here that the Statistical Division in the Ministry of Development has given up collecting statistics on room occupancy in hotels because in their opinion, the hotel owners were deliberately understating the figures for the fear of tax! On the other hand the plan document sets an explicit target for increasing the hotel room occupancy rate from 40% in 1986 to 55% by 1990!

Sub-sector	Product consumed by Tourism Sector
Small Farmers	Vegetables and fruits
Fishery	Fish
Poultry	Eggs and chicken
Dairy	Milk and ice-cream
Food processing	Beef, sausages, broilers, margarine
Beverages	Beer and liquor
Furniture	Wooden furniture, plastic furniture
Repair	Automobile repair and furniture repairs
Garments	Uniforms to hotel employees
Handicraft	Numerous handicraft products and souvenirs
Photography	Pictures and services
Masonry	Concrete blocks and tiles
Electricity and Water	Electricity and water
Communications	Telephones, telex, fax, postal services
Transport	Car-rentals, taxis, sea-port and airport services
Trade	Wholesale and retail trade services
Entertainment	Groups for music and dances

This list is by no means an exhaustive one. It only attempts to list the major areas of linkages of the tourism sector in a small and relatively less diversified economy of St.Kitts and Nevis. Investment in tourism leads to increased activity in all these sectors. In St.Kitts and Nevis, hotel sector is dominated by foreign investment. Somehow, the local investment is less in this vital sector. In the newly developing Frigate Bay area, the land is owned by the locals and the foreigners in equal proportion. In the rest of the residential area, the proportion is 75% : 25% between locals and foreigners. Many locals tend to migrate out to U.S.A. or Canada during their working life. However, they retain their property here so that they can return and settle here during retirement. As a result, several furnished houses are available for rents and are actually rented to visitors even for short periods.

IV. Government's Efforts To Develop Tourism

The government of St.Kitts and Nevis is committed to developing tourism on both the islands as an integral part of its strategy to diversify the economic base of the country and take it away from heavy reliance on sugar. Since it is small country, the labour and tourism departments are put under a common Ministry of Labour and Tourism. Expenditures of the Department of Tourism over last 5 years as given in Table 13 clearly show a rapidly rising trend. In 1986, the actual expenditure of the department was only EC \$ 1.01 million. In 5 years time in 1991, the budget estimate has been more than double at EC \$ 2.07 million. It implies an annual compound rate of growth of 15.4%. Thus, the commitment of the government towards developing tourism gets clear reflection in the fast increasing

budget allocation to the department. Table 13, moreover, reveals that there is also a marked shift in the government's strategy within this sector towards marketing of tourism and away from reliance on contracts. In 1986, the contracts were the most important single item in the budget with 36% share. Marketing expenses were only 33% of the total budget of the department. Salaries and membership to tourism organisations were respectively 9% and 3% of the budget in 1986. In 1991, however, there has been a significant structural shift with marketing emerging as the most important expenditure item having a share of 43%. Contracts on the other hand, have diminished in their importance considerably having only 27% of the share in the department's budget in 1991. Salaries and membership to tourism organizations have also declined in their importance in the budget of 1991 to 8% and 2% respectively. The marked structural shifts in the government expenditure in a short span of 5 years reveals not only the government's firm commitment to develop tourism but also its aggressive efforts to achieve rapid results in the desired direction.

The approach of the government to the tourism sector has shifted in recent years from considering it as a service sector to treating it as a modern industry in the world market. It has therefore, started viewing its role as a manager of the tourism product development on the islands. As a result, it has started paying attention to several important activities and matters connected with tourism apart from the accommodation. For instance, tourism sector of the country can compete in the international market only when modern facilities with international standard in some of the areas like shopping, car-rentals, taxis, guides in appropriate places of interest, restaurants, roads, electricity, telephones, sea-ports, airports, etc. The taxi drivers and guides as well as hotel and restaurant staff have to be trained. Natural attraction sites have to be managed and maintained properly. The beaches have to be cleaned and kept tidy. All this requires tremendous efforts which the government is determined to put in. For instance, a tourism shopping complex with 26 duty-free shops and a modern restaurant is almost completed and is likely to open soon.

Since the government's strategy emphasises marketing of the islands as the tourists' attraction, it has also opened its offices in the countries from where it gets maximum tourists' traffic. Thus, the tourism department has its branch in New York (Since 1981), Toronto (Since Sept.1985), London (Since Oct. 1989) and Chicago (Since April 1991). Opening up of offices in foreign countries, on the one hand is costly but on the other, is an aggressive marketing venture which having identified the target population tries to sell the product directly to meet the set goals. In order to help this process further by basing important decisions on facts rather than hunches, there is already an effort to collect, compile and tabulate relevant statistics on tourists segments. Table-14 provides the so collected data on stay-over visitors in the year 1990 classified by countries and occupation. Such data would enormously help identifying appropriate market segment in different countries so that relevant tourism product can be more meaningfully and effectively marketed. It is also worthnoting that these statistics are compiled by the statistical division in the Ministry of Development which passed on the data to the tourism department for its use in planning its marketing action. All these government efforts on various fronts are as per the 1986-90 National Development Plan objectives, targets and policies for tourism sector. Some of the targets set in the Plan have not been fully met but the shortfalls have been minor rather major.

In terms of the policies to promote tourism development, apart from the provision and improvement of the infrastructural facilities like roads, electricity, water supply, telephones, airports and seaport services, the government is fast expanding the capacity to train hotel staff and improve the skills of the existing ones. It also encourages expansion of the existing accommodation establishments. But more importantly, it has assembled a comprehensive package of incentives to promote hotel investment on the islands - particularly the large ones. Briefly the operating investment incentives for hotel construction can be summarized as follows:

1. Tax holidays of upto ten years for all hotels. The holiday exempts hotels from: (a) Corporate taxes, (b) income tax, (c) dividend tax (tax free dividends can be distributed for upto 2 years after the tax holiday expires), and (d) taxes on import of capital and operating items for first

installation. For larger hotels (i.e. with more than 100 rooms and in some cases 200 rooms), the period for tax holiday could be extended to 15 years.

2. Loss carry forward that can be used to reduce taxable profits for upto five years after expiration of the tax holiday.
3. Accelerated depreciation of assets for tax purposes.
4. Duty-free import of materials and equipment necessary for the establishment and operation of a hotel.
5. Repatriation of profits, dividends and imported capital.
6. No personal income tax.
7. Hotels of 250 or more rooms may apply for a casino license.

On the basis of the past trends and likely developments in the economy of St.Kitts and Nevis, the World Bank study (Nov. 1989) on the Long-Term Economic Prospects of the OECS countries has made projections of the growth of tourism in the country. Table-15 summarises the projections. Accordingly, by 1999, the direct employment in tourism industry is likely to increase four-fold, the tourists' expenditure is likely to tripple in real terms, and stayover visitors are likely to be two and a half times the ones in 1989. These figures are no doubt very encouraging for the growth of tourism sector in St.Kitts and Nevis. However, several issues arise in these context. We discuss them in the next section.

V. Issues In Tourism Development In St.Kitts & Nevis

From the foregoing discussion it becomes clear that the government of St.Kitts and Nevis considers tourism development as their main strategy to achieve numerous goals simultaneously and treats it with utmost priority. The main goals that it seeks to achieve thereby are: diversification of the economy from heavy reliance on sugar, reduce vulnerability of the economic performance of the country to natural calamities, achieve respectable growth of the economy with stability, improve balance on current account of the balance of payments and generate productive sustainable employment opportunities in the economy. These objectives on the one hand, and the various government efforts to promote tourism as outlined in the previous section on the other hand give rise to several issues. Some of them are listed below:

1. *Competition among Caribbean Islands:* It should be noted that the economic problems faced by the economy of St.Kitts and Nevis are in no way specific to it only. They are applicable more or less with equal force to several other islands economies within the Caribbean region. Similarly like St.Kitts and Nevis, other island countries in the Caribbean also possess unique attraction for tourists all over the world. If every country within Caribbean region starts focussing heavily on tourism development, the total effect on the World tourists' traffic to the Caribbean region would be worth examining. Assuming that the latter is relatively inelastic to the cummulative effort of the region, countries within the Caribbean region might end up competing with each other which might go against the powerful undercurrents for unification in the region. If the Caribbean island economies end up competing within themselves, some countries would gain at the expense of others. If, however, the tourists' demand of Caribbean destinations are relatively more elastic to the cummulative efforts, the region as a whole would gain and the question of competition among Caribbean countries becomes less relevant. For St.Kitts and Nevis, however, it can be argued that even when the world tourists' demand for Caribbean destinations is less elastic to the cumulative efforts. It is likely to be highly elastic to the efforts of their individual government. This is because currently, their share in the total world tourists traffic to the Caribbean region is very small. For instance, stayover visitor arrivals to

St.Kitts and Nevis in 1986 represented hardly 0.7% of approximately 10 million such visitor arrivals in the whole Caribbean region. Similarly, the share of cruise passenger was hardly 1%. The importance of being unimportant is that proportionately even substantial increases in the share of traffic to the islands would not induce any severe competitive reaction from others.

2. *Linkages Within Domestic Economy:* As it appears from earlier discussion, the linkages of tourism with other activities in the St.Kitts and Nevis economy are not strong. This is largely because it is predominantly an agro-based economy in terms of its goods production structure. The economy is far from having a modern and sophisticated manufacturing and service sector. It, therefore, tends to rely heavily on imports even for its domestic consumption - leave aside the tourists. In order to encourage hotel industry on the other hand, the government has liberalised imports to the sector. Since the government of St.Kitts and Nevis like other Caribbean countries believe in operating through moral suasion rather than direct controls and regulations, the issue is how much boost the other activities in the economy would get as a result of tourism development. In other words, would the government succeed in its diversification goal to be achieved with the tool of tourism development? Or is tourism development itself considered diversification of the economic base? These are pertinent questions because, as the statistics reveal, about 34% of the gross income in the hotel sector and about 41% in the restaurant sector is spent on food and beverages, the 80% of which is imported in St.Kitts and Nevis. Similarly, other material constitutes about 23% in hotel sector's and 30% in the restaurant sector's gross income. More than 90% of this other material is again imported in the economy. The gross value added in the hotel sector is about 43% and in restaurant sector is about 29% of the gross incomes in the respective sectors. Since gross value added includes interest, rent, and profits besides depreciation and wages, again a large proportion of this value added would represent an outflow owing to the fact that foreign investment dominates the hotel sector in St.Kitts and Nevis. It may, however, be argued that unless domestic market is developed, the production of other commodities would never take off in the economy. Thus, if hotels have created the domestic market for goods and services, perhaps at a later stage domestic industries might get encouraged and the imported goods could be substituted by domestically produced goods in future. This would, however, take long time because in tourism industry, quality matters most. It would require a very sophisticated technology and equally skilled manpower which is the greatest bottleneck in St.Kitts and Nevis. In any case, the issue of linkages of tourism has temporal dimensions and is truly dynamic in nature.

3. *Large vs Small Hotels:* A related issue to the question of linkages is that of scale of operation. As observed earlier, the government in St.Kitts and Nevis has been encouraging large scale hotels more than the small scale hotels. The large scale hotels have better chances of success because they follow their own marketing strategy and push the image of the island for their own benefits. At a sufficiently higher scale of operation, charter flights of tourists with pre-arrangements also become profitable for the hotel management. Their occupancy rate is also, therefore, far better than the small hotels. However, it is known that larger hotels with their main headquarters abroad deal largely in the foreign currency at the origin rather than destinations. Almost all their materials are also imported. The government also allows duty-free imports of almost everything to them. Their internal linkages with the domestic economy of St.Kitts and Nevis are therefore, negligible and is limited to the tourists' purchases of local items or their visits to local sites. On the other hand, small hotels have much higher linkages with the domestic economy but they are hardly viable. Their room occupancy rates are low and highly fluctuating with seasons. Moreover, they on their own cannot attract larger traffic volume to the country. They depend on the Ministry's efforts to increase the tourists' flow.

4. *Cost-Benefits of Incentives to Hotels:* The preceding two issues point to the basic justification for the various incentives given by the government to the hotel industry. As outlined in the preceding section, government has given major concessions to hotels in terms of tax holiday of 10 years to 15 years and duty-free imports of material and equipment for establishing hotels. For large hotels, even the food and beverages can be imported without duty. The rate of import duty is 45% in St.Kitts and Nevis. Even consumption tax of 15% and stamp duty of 2% can be exempted in special cases.

It is estimated that almost 85 to 90% of the building materials for hotels in St.Kitts and Nevis are imported. Although labour is largely local, its cost share in the total construction value is hardly 30%. On the other hand, the departure tax, the hotel room tax and the foreign exchange spent by the visitors in the country on domestically produced goods represent the flow of benefits besides generating employment in the hotel and its construction. It is, therefore, an empirical issue to determine whether the cost of the incentive package offered by the government to the hotel sector is more than the benefits it generates to the society.

5. *Shortage of Labour*: It is already pointed out earlier that St.Kitts and Nevis have acute shortage of skilled and trained manpower required for modern sectors of the economy. It is also important to note that labour shortage is a more general problem not only confined to the category of skilled workers. Even the construction and farm labour are also in short supply during peak season. In the past, labour had to be imported from Guyana and Puerto Rico. The problem of unemployment is, therefore more structural in nature. With a programme for rapid growth of hotel establishments, there would be further pressure on the labour market particularly in the construction sector and hotel service sector. If these labourers are imported to meet the requirement, again the goal of productive employment generation on sustained basis in the economy would be frustrated. If the local labour has to be employed, their wages would soar up substantially distorting the wage structure in the economy. More capital intensive methods of production would, therefore, be employed reducing the employment generation. It would imply further reliance on imports and less linkage benefits to the domestic economy. Apart from this, a sharp increase in wages in 2 of the fastest growing sectors of the economy may disrupt labour market functioning in the other sectors of the economy leading to overall cost-push effect. The domestic economy may, therefore, tend to lose its competitive edge. If such effects are to be averted, adequate supply of labour should immediately be ensured. Liberal migration policy may lead to socio-cultural politico problems in future.

6. *Openness of the Economy*: Heavy reliance on only one crop like sugarcane and one product like sugar is, of course, very dangerous to the economy. Diversification of the economy through development of a sector like tourism, however, does not reduce the reliance of the economy on external environment. It, in fact, increases the openness of the economy. Although it helps in building resilience in the economy to the natural calamities, it widens the avenues for the world business cycles to destabilise the domestic economy. The volume of tourist traffic depends critically on the performance of the foreign economies on the income and employment front. These 'foreign countries' moreover are the industrialized rich nations of North America and Europe which among them have close trading links. The business cycles in these countries, therefore, tend to synchronise. Since the origin of the volume of visitor traffic to the island is heavily concentrated in a few closely related and co-moving economies, the visitor arrivals usually tend to show wide annual fluctuations (See [Table 4](#)). If diversification in the country of origin of the visitor arrivals is not achieved along with the rapid expansion of tourism sector, the economy of St.Kitts and Nevis may get seriously affected and to a certain extent destabilized by the business cycles in the countries that matter for the tourists.

7. *Limits To Growth*: With the current strategy for the development of tourism sector, the growth of GNP of the country would certainly increase but whether the growth of GDP would increase or not is a matter of speculation. Perhaps in the short-run it might increase because of new expansion in the hotel industry, construction, local trade, etc. But once all the sites are developed, hotels are built and construction activity stops, the economy might again start showing a sign of stagnation. This is because there is a physical limit to which tourism in small islands like St.Kitts and Nevis can develop. The size also puts the constraint on the capacity to hold and accommodate the traffic. No sooner does this potential get fully exhausted than the growth gets tapered off unless by then the domestic linkages of tourism sector get strengthened and start operating. With limited population and little or no growth in it, this appears too optimistic. For long term self-sustaining growth, other alternatives will have to be actively searched. The only other option is to think actively about increasing domestic linkages of tourism sector as rapidly as possible. Among other things, this would require an immediate critical look at some of the policies currently being followed and introduction of some new policy measures.

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Table 1 : Climate for St.Kitts & Nevis										
		1981	1982	1983	1984	1985	1986	1987	1988	1989
Annual Average	Celsius	27.3	25.6	27.1	26.4	26.5	26.6	27.0	26.9	26.7
	Fahrenheit	81.1	78.1	80.8	79.5	79.7	79.9	80.6	80.4	80.1
Annual Maximum	Celsius	31.6	30.7	31.1	30.1	32.1	32.1	31.0	30.7	29.1
	Fahrenheit	88.9	87.3	88.0	86.2	89.8	89.8	87.8	87.3	84.4
Annual Minimum	Celsius	21.7	19.8	23.6	21.0	18.8	18.0	21.3	20.7	23.4
	Fahrenheit	71.1	67.6	74.5	69.8	65.8	64.4	69.8	69.3	74.1
Average Rainfall (mm.)		1428.0	906.0	1319.0	959.0	855.3	1095.2	1822.7	1206.5	1336.0
Average Rainfall (ins.)		56.2	35.7	51.9	37.8	33.7	43.1	71.8	47.5	52.6
Average Humidity (%)		76.0	76.0	76.0	76.0	77.0	76.0	79.0	76.0	73.7
Average Wind Speed (knots)		10.6	11.4	11.0	13.3	13.2	12.7	11.3	12.0	12.0
Source: Statistical Division, Planning Unit, Ministry of Development, St.Kitts & Nevis.										

Table 2 : Economic Aggregates and Other Indicators for St.Kitts & Nevis										
Indicators	1981	1982	1983	1984	1985	1986	1987	1988	1989	
GDP at factor cost in current prices (EC\$M)	121.44	138.74	136.39	159.32	171.76	214.38	239.78	278.56	302.27	
GDP in 1977 prices (EC\$M)	84.38	89.7	88.72	96.72	102.11	108.43	116.43	124.62	130.97	
Annual growth of real GDP	--	6.30	(-1.09)	9.02	5.57	6.19	7.38	7.03	5.10	
Per capita GDP at current prices (EC\$)	2,711	3,055	2,980	3,324	3,580	4,863	5,474	6,277	6,808	
Per capita GDP at 1977 prices (EC\$)	1,846	2,002	2,021	2,159	2,321	2,498	2,670	2,808	2,950	
Agriculture (% of GDP)	16.7	15.71	12.96	12.4	11.48	10.75	10.82	9.99	9.16	
Manufacture (% of GDP)	14.72	13.45	12.86	14.2	12.77	15.31	14.75	15.89	15.67	
Construction (% of GDP)	8.93	9.8	10.96	8.05	8.76	7.78	8.89	10.32	11.85	
Producer of Govt. services (% of GDP)	21.94	20.58	21.93	22.65	21.73	19.23	18.62	17.78	18.03	
Wholesale & retail trade (% of GDP)	11.60	11.91	13.39	12.99	13.94	13.04	13.76	12.69	12.63	
Other activities (% of GDP)	28.88	27.89	28.87	29.11	30.18	32.64	33.01	32.11	32.66	
Value of domestic exports (EC\$M)	60.5	46.5	47.1	52.6	48.9	67.9	71.6	76.6	68.9	
Sugar (% of domestic export)	65.8	35.3	66.1	58.0	52.0	40.0	32.3	34.1	35.0	
Value of re-exports (EC\$M)	5.02	4.31	2.67	1.80	6.10	4.30	3.90	5.00	8.9	
Value of imports (EC\$M)	128.8	119.8	133.7	140.1	138.6	169.8	214.6	255.7	275.1	
Food (% of imports)	19.5	20.6	18.3	19.8	21.3	18.0	15.5	15.5	14.2	
Machinery (% of imports)	20.5	18.9	19.2	19.8	20.1	23.2	29.6	32.1	34.0	
Average consumer price index 1st Jan. 1978 = 100	152.3	161.3	165.0	169.5	173.3	174.0	175.6	176.0	189.4	
Population (mid-year) estimates	45,707	44,795	43,889	44,800	44,000	43,700	43,410	44,380	44,400	
Source: Same as Table 1.										

Table 3 : Demographic Indicators of Development St.Kitts & Nevis									
	1981	1982	1983	1984	1985	1986	1987	1988	
Crude birth rate (per 000)	25.6	29.0	24.4	24.1	23.3	23.0	21.8	21.3	
Crude death rate (per 000)	11.3	10.1	11.2	10.7	10.0	10.5	10.6	10.5	
Rate of natural increase	15.5	17.8	13.7	14.1	13.3	12.5	11.2	10.8	
Infant mortality rate (per 000)	45.7	42.8	41.2	27.8	30.2	39.7	22.2	24.4	
Neonatal death rate	29.0	26.0	20.1	18.8	20.3	28.8	16.9	14.8	
General fertility rate	21.6	14.3	11.7	10.8	10.3	10.9	10.2	9.0	
Total fertility rate	3.3	3.0	3.0	3.0	2.9	3.0	2.9	2.9	
Gross reproduction rate	1.59	1.42	1.44	1.47	1.43	1.48	1.43	1.39	
Expectation of life at birth (years)	Male	--	64.10	66.12	64.94	65.99	65.45	65.33	65.87
	Female	--	68.46	69.81	68.53	69.67	69.9	70.77	70.98

Source: Same as in Table 1

Table 4 : Tourists in St.Kitts & Nevis: Growth and Origin										
Passenger Arrivals & Departures	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990
Arrivals (000's)	54.2	51.9	52.4	59.1	68.0	80.6	92.3	99.1	105.2	110.5
Departures (000's)	54.7	52.4	53.5	59.2	68.0	78.9	92.9	100.1	106.5	117.7
Visitor Arrivals										
Stopover visitors	35,476	34,575	34,269	39,866	47,547	56,805	66,450	69,608	72,125	75,689
Yacht/cruise ship passengers	10,850	11,146	22,835	34,062	31,522	26,963	31,438	53,645	36,559	33,941
Total visitor arrivals	46,326	45,721	57,104	73,928	79,069	83,768	97,888	123,253	108,684	109,630
% change over previous year	20.22	-1.31	24.90	29.46	6.95	5.94	16.86	25.91	-11.82	0.87
Yacht & cruise ship calls (no.)	15	12	22	40	73	63	136	197	198	158
Stopover visitors by country/region										
% of total visitor arrivals										
United States of America	34.8	31.4	28.8	36.5	23.2	34.5	41.7	42.3	38.7	38.8
United Kingdom	7.2	7.8	8.3	7.7	7.1	6.2	6.3	6.9	6.9	7.3
Canada	5.8	7.1	6.0	6.3	16.3	18.9	15.9	12.3	16.3	15.7
Caricom	15.5	16.3	16.8	15.6	13.6	11.7	11.3	10.6	11.7	13.0
Others	36.7	37.4	40.1	33.9	29.8	28.7	24.8	27.9	26.4	25.2

Source: Same as Table 1

Table 5 : Licensed Vehicles, Aircraft Arrivals and Telephone Subscription in St.Kitts & Nevis									
Type of Vehicle	Number of Vehicles Licensed								
	1981	1982	1983	1984	1985	1986	1987	1988	1989
Private Cars	2032	2174	2319	2392	2475	2649	2796	2815	
Public Service Vehicles	320	405	388	381	375	359	416	415	
Commercial Vehicles	1193	1204	1325	1405	1544	1494	1541	1673	
Total	3545	3783	4032	4178	4394	4502	4853	4903	
Aircraft Arrivals By Port									
Airport									
Golden Rock (St.Kitts)	8.0	7.6	8.7	10.5	9.2	10.2	12.1	11.9	13.0
Newcastle (Nevis)	3.7	4.3	4.6	5.2	5.0	5.1	6.0	6.2	7.2
Telephone Subscribers									
No.of Subscribers (000)	1.8	1.9	1.9	1.9	2.5	3.0	4.2	7.0	8.1
Source: Same as Table 1.									

Table 6(a) : Hotel Occupancy Rates: Selected Hotels in St.Kitts (1988)								
Hotel	# of rooms	Rates ¹ (US\$)				Estimated occupancy		On-site Amenities
		Summer		Winter		Summer	Winter	
		Single	Double	Single	Double			
Banana Bay	20	\$140 ²	\$180 ²	\$180 ²	\$250 ²	47%	82%	a,c,d,h
Fairview Inn	30	\$50-60	\$60-70	\$78-88	\$88-98	50%	80%	b,d,e
Fort Thomas	64	\$50-55	\$60-65	\$78-80	\$80-95	47%	82%	b,c,d,e,g
Frigate Bay	64		\$50-150		\$95-310	50%	85%	b,c,d,e
Golden Lemon	11	\$145-185 ²	\$225-575 ²	\$185-225 ²	\$275-715 ²	52%	97%	a,b,c,d,g
Jack Tar Village	263	\$180 ³	\$140 ^{3,4}	\$190 ³	\$150 ^{3,4}	80%	100%	a,b,c,d,e,f,g,h
Ocean Terrace	54	\$58-176	\$75-176	\$70-270	\$85-270	50%	80%	b,c,d,e,g,h

Amenities Code: a = Beach; b = Swimming Pool; c = Tennis; d = Restaurant; e = Conference Facilities; f = Casino Gambling; g = Shopping; h = Water Sports
1: European Plan; 2: Modified American Plan; 3: All inclusive; 4: Per person

Table 6(b): Number of Rooms in Accommodation Establishments and Average Annual Occupancy Rates, 1984-88.		
Year	Available Rooms	Average % Occupancy
1984	548	n.a.
1985	531	29.6
1986	603	32.0
1987	712	49.9
1988	791	48.4

Source: World Bank: *Long-Term Economic Prospects of the OECS Countries*, Nov. 1989; p.60.

Table 7 : St.Kitts and Nevis Stayover Tourist Arrivals by Month 1986-90 (Percent of annual total)					
Month	1986	1987	1988	1989	1990
January	8.1	9.6	9.3	9.1	8.3
February	8.6	9.3	9.4	9.5	8.9
March	9.1	9.8	9.4	10.0	8.0
April	7.4	10.2	7.7	8.3	8.5
May	6.5	7.4	6.8	7.3	7.9
June	6.7	6.8	6.8	7.0	8.2
July	9.1	8.4	10.1	10.8	9.7
August	9.9	6.9	7.8	8.6	8.2
September	6.0	5.3	6.1	4.9	5.5
October	6.2	6.5	7.2	6.1	6.3
November	8.3	7.4	7.3	7.0	8.1
December	13.7	12.2	12.0	11.4	12.4
TOTAL	100	100	100	100	100
Source: The same as Table 1.					

Table 8 : Average length of stay (in days)										
	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990
Average length of stay (in days)	5.4	6.3	6.3	6.3	6.9	6.9	6.9	6.9	8.7	8.6
Hotel	5.4	6.6	6.5	6.5	7.0	7.0	7.0	7.0		
Private houses and others	12.2	12.4	12.5	12.5	12.5	12.5	12.5	12.5	NA	NA
Business	4.8	4.9	5.0	5.0	5.0	5.0	5.0	5.0	NA	NA
Source: Ministry of Finance, St.Kitts.										

Table 9 : Gross Domestic Product by Economic Activity, At Factor Cost in Constant Prices St.Kitts & Nevis						
	In EC \$ Million			Percentage Contribution		
	1977	1981	1986	1977	1981	1986
Agriculture - Fishing	0.93	1.46	1.96	1.94	1.73	1.81
Manufacturing - Other	3.94	5.32	7.45	5.69	6.30	6.88
Electricity & Water	0.61	0.94	1.27	0.88	1.11	1.17
Construction	6.59	7.99	10.3	9.52	9.47	9.51
Wholesale & Retail Trade	7.01	9.20	14.50	10.13	110.90	13.39
Hotels & Restaurants	1.42	2.91	6.22	• 2.05	3.45	5.74
Transport	3.81	4.85	6.35	5.51	5.75	5.86
Road Transport	2.90	3.57	4.36	4.19	4.23	4.03
Sea Transport	0.41	0.52	0.90	0.59	0.62	0.83
Air Transport	0.50	0.76	1.09	0.72	0.90	1.01
Communications	2.05	4.44	7.39	2.96	5.26	6.83
Banks & Insurance	3.79	4.19	6.42	5.48	4.97	5.93
TOTAL (G.D.P. at F.C.)	69.20	84.38	108.27	100.00	100.00	100.00

Source: Statistics Division, Planning Unit, Ministry of Development, St.Kitts & Nevis.

Table 10 :Weekly Average Wage Rates (in US \$) Assuming 45 Hours Per Week for the year 1987 In St.Kitts & Nevis	
Housekeeping	
Maid	\$37.00
Houseman	\$37.50
Supervisor	\$45.00
Restaurant and Bar	
Bartender	\$43.00
Waiter	\$41.00
Captain	\$46.00
Supervisor	\$58.00
Kitchen	
Dishwasher	\$36.00
Cook	\$59.00
Kitchen Helper	\$38.00
Chef	\$154.00
Gardener	\$47.00
Receptionist	\$58.00
Construction	
Mason	\$114.00
Carpenter	\$114.00
Painter	\$108.00
Laborer	\$79.00
Foreman	\$202.00
Fringe Benefits	
Annual Paid Vacation	14 days
Paid Holidays	13 days
Source: St.Kitts and Nevis Investment Promotion Agency.	

Table 11 : Estimates of Average Daily Expenditure by Visitor (in millions of U.S.Dollars)										
	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990
Cruise-ship	15.5	16.0	17.0	17.50	20.00	21.20	22.47	23.82	NA	NA
Excursionist				33.00	33.00	34.98	37.08	39.30	NA	NA
Hotel	71.4	75.0	80.5	84.50	84.50	89.57	94.94	100.64	NA	NA
Private homes and others	14.3	15.0	16.5	17.50	17.50	18.55	19.66	20.84	NA	NA
Business	76.2	80.0	84.0	88.20	90.00	95.40	101.12	107.19	NA	NA
Total Visitor Expenditure	9.85	10.8	11.60	15.20	20.06	26.47	33.54	37.63	39.70	43.66
Definitions: Excursionists are those who stay for less than a day. Stayover passengers are the ones who spend more than a day in the islands.										
Source: ECCB.										

Table 12: Inland Revenue from Tourism Related Heads; St.Kitts and Nevis Budget 1986-1991					
[EC\$ in 000]					
Year	Actual Inland Revenue from				
	Hotel room tax	Deaprture tax	Travel tax	Foreign currency tax	Total recurrent account
1980	147	167	---	1366	55752
1981	423	232	192	1726	55363
1982	422	213	277	1844	51098
1983	365	204	310	1900	47956
1984	688	204	272	---	50554
1985	834	458	406	---	49118
1986	1327	695	472	246	62295
1987	1652	762	524	583	73020
1988	1770	786	607	834	80550
1989	1859	826	573	940	93017
1990*	2200	1200	700	900	96969
1991**	2200	1350	700	900	103598

* Revised estimates
** Budget estimates
Source: Ministry of Finance: Annual Budget Estimates for St.Kitts and Nevis.

Table 13: Expenditures of Department of Tourism over the Last Five Years (in EC \$)						
Details of Expenditure	Actual 1986	Actual 1987	Actual 1988	Actual 1989	Revised 1990	Estimates 1991
Salaries and Wages	90,155	89,059	97,120	135,043	115,000	166,960
Transport Allowances	5,850	3,390	5,610	6,543	6,000	9,000
Contingencies	299	180	180	280	450	450
Telephones, Telegrams and Official Postage	33,009	22,771	24,763	34,366	35,000	35,000
Office Expenses	135,140	186,000	238,467	245,225	356,000	356,000
Marketing	335,120	434,986	647,984	850,753	710,000	900,000
Contracts	364,561	405,947	419,541	436,428	554,210	560,000
Organisations	32,576	26,799	34,895	41,000	43,000	45,000
Item not repeated in 1988	17,149					

Source: Budget Documents.

Table 14: Tourists By Country of Residence and Occupational Group in St.Kitts & Nevis (January to December 1990)										
Country of Residence	Occupational Group									
	Admin Manag erial	Profession al Technical	Office workers	Blue collar workers	Other occup ations	Students & children	House wives	Retired or disabled	Not stated	Total
Total Visitors	3,251	28,204	13,352	6,747	2,587	9,429	3,848	2,692	2,414	72,524
United States	1,269	12,635	5,429	1,956	724	2,652	1,587	1,700	665	28,617
Canada	625	4,859	2,681	1,075	240	1,022	523	415	270	11,710
Europe	425	3,138	1,067	487	152	705	397	202	293	6,866
United Kingdom	331	2,268	885	358	136	552	365	171	165	5,231
France	39	463	38	74	5	64	13	9	82	787
West Germany	26	161	101	23	5	28	8	12	14	378
Holland	9	34	4	3	3	6	3	2	8	72
Rest of Europe	20	212	39	29	3	55	8	8	24	398
Italy	3	15	8	5	0	4	0	0	1	36
Denmark	0	7	0	0	0	0	0	0	0	7
Norway	1	12	1	1	0	7	0	2	3	27
Sweden	3	44	6	8	0	4	1	1	2	69
Switzerland	7	99	16	13	1	20	4	4	11	175
Luxemburg	0	0	0	0	0	0	0	0	0	0
Austria	3	23	8	0	1	12	1	0	1	49
Belgium	2	7	0	0	1	7	0	1	5	23
Greece	0	1	0	1	0	0	0	0	0	2
Portugal	0	1	0	0	0	0	1	0	0	2
Republic of Ireland	0	0	0	0	0	0	0	0	0	0
Spain	1	3	0	1	0	1	1	0	1	8
Other Europe	0	0	0	0	0	0	0	0	0	0
Caribbean	890	6,974	4,034	3,158	1,451	4,909	1,280	365	1,109	24,170
Commonwealth Caribbean	543	4,510	2,308	1,682	793	1,906	572	171	349	12,834
Caricom	415	3,648	1,750	1,072	452	1,111	327	90	194	9,0594
OECS Countries	189	2,005	1,174	665	331	829	181	61	138	5,573
Antigua	99	926	578	301	143	497	78	25	77	2,724
Dominica	22	277	140	84	66	74	22	8	16	709
Grenada	14	100	101	33	10	23	12	2	3	298
Montserrat	18	335	188	107	64	146	35	17	24	934
St.Lucia	27	183	123	32	19	55	22	2	4	467
St.Vincent	9	184	44	108	29	34	12	7	14	441
Other Caricom	226	1,643	576	407	121	282	146	29	56	3,486
Belize	0	2	1	2	0	0	0	0	0	5
Barbados	117	596	290	71	30	101	40	11	16	1,272
Guyana	12	142	38	71	15	44	29	0	9	360
Jamaica	23	311	94	24	19	43	12	2	4	532
Trinidad & Tobago	74	592	153	239	57	94	65	16	27	1,317

Source: Statistics Division, Planning Unit, Ministry of Development, St.Kitts & Nevis.

Table 15: Summary of Projections for Tourism Sector in St.Kitts & Nevis.			
Item	1989	1994	1999
1. Employment			
a) In Accommodation	881	2461	3632
b) In other Tourism Enterprises	691	1641	2642
c) Total Direct Employment	1572	4102	6274
2. Traffic			
a) Available Rooms	864	2051	3302
b) Available Bed-nights	630.7	1497.2	2410.5
c) Rented Bed-nights	315.4	718.7	1108.8
d) Arrivals (in '000)	48.5	102.7	158.4
e) Tourists staying in Private Homes (in '000)	32.38	44.0	52.8
f) Total Tourists (in '000)	80.8	146.7	211.2
3. Receipts from (in EC\$ million)			
a) From Stayover Tourists	97.39	191.05	306.58
b) From Excursionists	0.28	0.35	0.44
c) From Cruise Passengers	3.54	4.42	5.53
d) Total Receipts	101.21	195.82	312.55
Source: World Bank (1989): <i>Long Term Economic Prospects of the OECS Countries</i> , Annex VI.			

Chapter 12

Role of Tourism Sector in Mauritian Economy

1. Background Information on the Economy

Mauritius is a small island economy situated in the Indian Ocean to the east of Madagascar in the Southern hemisphere. The country has several small islands spread around the main island. The main island which is about 61 km long and 47 km wide, has the land area of 1865 square kilometers with a population of 1.1 million. Compared to many such small island economies, Mauritius is very densely populated country. These islands are the result of volcanic eruptions. Several extinct and dormant craters are located on these islands. The soil on the main island is very fertile. Just over half the land is cultivable. It has 160 kms of coastline almost entirely surrounded by coral reefs. The landscape is a beautiful mixture of plains of central plateau and impressive mountains which not only add to the scenic beauty but also create ideal conditions for forests and agriculture. The central plateau is dotted with rivers, streams and waterfalls. The island, however, is not rich in terms of natural resources like minerals but has plenty of water, fertile soil and excellent climate throughout the year. Temperature during the year ranges between 13°C to 31°C. The country is subject to cyclones between late December and March. They sometimes cause severe damage. In terms of location, Mauritius has a disadvantageous position since it does not lie on the main sea routes. The distance of Mauritius from major markets is an adverse factor raising the transport cost not only of goods but also of passengers as compared to its competitors.

The population of Mauritius is made up of various ethnic groups. There is hardly any native population. About 68% of the population is of Indian origin. Only the traders and entrepreneurial class have links alive with their roots in India. The rest of the population of Indian origin have no formal or informal links with India. About 27% of the population has African and creole or mixed descent, while the remaining 5% of the population are Franco-Mauritians and Sino-Mauritians. There are all the major religions of the world here: Hinduism, Islam, Buddhism and Christianity. They all live in complete harmony. The official language is English but French is more commonly spoken with creole (a broken French) as the link language. Hindi is also very popular language here. All the cultures are encouraged to flourish. Such ethnic cultural diversity contributes to the country's lively and competitive environment. The government is organised in the system of parliamentary democracy and in early 1992, it is becoming a Republic on the lines of the Indian model. The country is enjoying sound democratic values and a stable government.

Mauritius has a per capita GNP of about U.S. \$2,600 in 1990. It is, thus, a middle income developing country. In terms of economic and social development it is far ahead of most of its neighbouring countries. In 1990, its adult literacy rate is well over 90%, life expectancy at birth is 65 years for males and 73 years for females, the infant mortality rate is as low as 19.9 per thousand births, crude birth rate is 21 and crude death rate is 6.6 per thousand, and the basic needs of the population are extensively covered. Education is not compulsory but free from primary to university levels. According to the recent epidemiological situation, there is no malaria risk in the country. The doctor-population ratio is about 1:1200. Medical care is free in government hospitals. The island of Mauritius has the best road network for this part of the world. It has a road density of about 1 km. per Square km. and 92% of these roads are paved. There is a rapid direct access from the airport to the major conurbations. 1790 kms of tarred roads criss-crossing the island and a motor-way linking the north (Pamplemousses) to the south (Nonville France) provide easy access to all the nooks and

corners of Mauritius. In terms of the private car ownership, Mauritius ranks high with one car per 13 persons. Communication facilities like telephone lines, post-office network, telex and fax are well developed on the island. There are 107 post-offices with one mobile post-office spread all over the island. Similarly, there is one telephone line per 15 persons.

There are about 17 small islands besides the main island in the country. All of them except Rodrigues are uninhabited. They are too small in area and are considered reserved land. Rodrigues is situated about 560 km east of Mauritius. It has a total area of 108 sq km, however because of the hilly nature of the land, the actual surface area is much greater. It has a population of 37,590, 95% of which is of Roman Catholic faith. It is well connected by air and other communication network with Mauritius main island.

2. Trends in the Mauritian Economy

Mauritius became an independent nation on March 12, 1968 without any bloodshed. The whole economy of Mauritius has been dominated by a single crop of sugar. It still occupies more than 85% of the cultivable area and accounts for about one third of the export earnings. There has been a significant expansion of other sectors particularly manufacturing and tourism since early 1970s. However, sugar continues to dominate and dictate the economic trends and fortunes of the country. In 1973-74, there was a sugar boom and as a consequence the economy was also booming. In 1976, however, there was a sharp decline in sugar prices which started a period of serious difficulty for Mauritius. Situation worsened in 1979 when the second oil-shock was experienced world over. This led to a considerable deterioration in the country's terms of trade and hence balance of payments. During 1976-79, the country's external debt more than tripled with significant adverse movements in the debt-service ratio. This was the critical period in the economic history of Mauritius.

In 1979, the government had to resort to the IMF loan and the World Bank assistance based on the standard structural adjustment programme package. During the period between the first two oil shocks, the country had suffered seriously in terms of the inflation rate (CPI) which rose from 3.6% p.a. during 1965-73 to 15.3% during 1973-80. Gross national savings were also adversely affected. They declined in absolute terms by 12.5% p.a. during 1973-80; and as proportion to GDP from 24.7% in 1973 to 10.6% in 1980. The first SAP was marked by unfavourable exogenous factors like adverse weather conditions in 1980 and 1983 and a worldwide recession during 1980-82 resulting in continued deterioration in the country's external terms of trade. As a result of all this, the inflation rate continued to be around 11% p.a. during 1980-84. Exports also registered an absolute decline in U.S. dollar terms from \$574 million in 1980 to \$505 million in 1984. However, imports also declined from \$690 million in 1980 to \$542 million in 1984. The external current account balance, therefore, marginally improved.

The second phase of SAP beginning from the early 1980s emphasised economic growth based on export oriented manufacturing and tourism with some selective import substitution in food, energy and a few manufactured products. Government's policies also became more liberalised and open. The economy witnessed the period of rapid expansion-cum-recovery during 1983-88. Real GDP increased by 6.8% p.a.; and since population grew only at 1% p.a., the real GDP per capita increased at the phenomenal rate of 5.7% p.a. during 1983-88. Such a rapid rate of growth was largely achieved by the export processing zone (EPZ) industries which grew at the rate of 28% p.a. in real terms during 1983-88. Similarly, the tourists arrivals also increased by 14% p.a. Even the sugar industry recovered and expanded with a bumper crop of sugar in 1986. Rate of inflation also fell to around 4% p.a. over the period. Gross fixed investments in the economy increased in real terms by 15% p.a. and the gross national savings as a proportion to the GDP again rose to 26% in 1988. The rate of unemployment also fell sharply from 11% in 1980 to 4% in 1988 thanks to the strategy of promoting labour intensive EPZ industries which absorbed not only the unemployed but also the new entrants in the labour market. This has led to significant structural changes in the Mauritian economy. The share of sugar

sector in GDP (at factor cost) sharply declined from 20% in 1979 to 13% in 1988; while the share of total manufacturing excluding sugar milling, has risen from 11% in 1979 to 22% in 1988.

During the period after 1988, the growth of output was more or less maintained but consequent continued decline in the unemployment rate which stands at less than 2% in 1991 has exerted tremendous pressure on the labour market. Coupled with spurt in the private consumption on account of wage revisions, the spell of high growth and employment accompanied by easy money and fiscal policies has driven the economy back to a double digit inflation. During 1990, the inflation was 13%, but it is expected to come down only to 7.5% during 1991. The saving rate has declined to 22% in 1990, but is expected to be 23.1% in 1991. Shortage of labour in general and skilled labour in particular has become a major constraint. The relative wage developments in the public and private sectors have emerged as the major destabilising and disequilibrating factors.

The future growth prospects of the Mauritian economy continue to hinge on exports of sugar and garments unless export base is diversified and expanded further. In this regard, the role of tourism sector in Mauritius is of crucial importance because of its foreign exchange earning capacity as well as its linkages with the domestic economy. If the Mauritian economy has to develop resilience to exogenous shocks like weather conditions, fluctuations in the world markets and prices, protectionistic tendencies of the industrial countries, etc., it must aim at accumulating a large stock of foreign exchange reserves besides servicing and, if required, prepaying some of the more expensive loans. In order to achieve this, strategy consisting of selective import substitution in energy, tourism development with environmental protection and diversification of industrial base has to be followed. Since tourism industry has important linkages to the domestic economy, its development in Mauritius is critical for the future course of the economy.

3. Features of Tourism Industry

Main parameters of the tourism industry are the tourist arrival, their pattern according to season and country of residence; length of their stay; the rooms and bed occupancy rates; employment generated in the industry; expenditures by tourists, etc.

Tourist Arrivals: A tourist is defined as a non-resident staying in the island for more than 24 hours but less than a year. Tourists constitute about 70% of the total arrivals in Mauritius. The remaining 30% of the arrivals are accounted for by the Mauritians settled abroad, Mauritian residents and passengers in transit. Table 1 provides information on number of total arrivals, tourists arrival by sea and air and tourists nights spent for the period 1981-90. It can be readily observed from the table that air is the most important mode of transport for tourists. Sea as a mode of transport for tourists is not at all significant. It can also be calculated from the table that tourists arrivals increased at the average compound rate of 10.2% p.a. against 10.6% p.a. growth of total arrivals. The proportion of tourists in total arrivals, therefore, declined marginally from 72% in 1981 to 70% in 1990. The increase in the non-tourists traffic on the island is worth-noting. It is largely on account of rapidly growing arrivals of Mauritians residents which may be consequent upon the high growth of the economy. On the other hand, the tourist nights spent on the island increased at the average compound rate of 11.1% p.a. implying an increase in the average length of stay of tourists over the period 1981-90.

Length of Stay: Table 2 provides information on the average length of stay of tourists in Mauritius by their country of residence over the period 1981-90. It can be seen from the table that average length of stay of all tourists has increased marginally over the period 1981-90. In terms of the country profile of the tourists, the average length of stay of tourists from all countries except U.K., Zambia and Singapore has either remained more or less the same or increased over the period 1981-90. Average length of stay of the tourists from the short houl like Seychelles, Kenya and Zimbabwe is increasing. Most of the long-houl tourists except from Japan and Singapore are staying for longer period on the island. The short-houl tourists from Malagasy Republic, Reunion, Republic of South Africa, Zambia, etc., are staying for shorter period.

Tourists by Country: Table 3 provides information on arrivals of tourists by their country of residence over the period 1981-90. It gives us the idea about the share of different countries and their behavior over the last decade. It can be readily seen that the Reunion Island, Republic of South Africa and France are the major sources contributing about 60% of the total tourists to Mauritius. Over the period 1981-90, the share of Republic of South Africa is steadily declining but that of Reunion is increasing. The shares of France, Germany, Italy and U.S.A. on the other hand hardly reveal any trend. However, the shares of U.K., Switzerland, Seychelles, Japan and Singapore show increasing trend. It is worth-noting that even in 1990, Mauritius depends heavily on the European (42%) and African (46%) markets for its tourists. In this context, declining share of Australia causes concern.

Seasonality: Table 4 provides information on the seasonal index of tourist arrivals in Mauritius by months over the decade 1981-90. From the table, it can be seen that seasonality is not a very serious problem in Mauritius. The seasonality index has not crossed 140 and not fallen below 62 for any month during the last decade. The months of high traffic have been December and August which coincide with the holidays in Europe and Africa; whereas it is June when the tourist traffic is at the minimum in Mauritius. Given the year round excellent climatic conditions on the island where one can swim and tan throughout the year since the temperature of the sea water remains around 25°C, it is natural that the extent of seasonality of tourist traffic is low. Even the occasionally occurring cyclones are not very dangerous and can be an enjoyable experience if advice given on precautions are seriously taken. It is worth-noting that whatever extent of seasonality exists in tourist arrival is also on decline during the recent years as revealed by the measure of range reported in the table.

Hotels, Rooms and Beds: Table 5 provides information on the total number of hotels, rooms and bed places available in Mauritius. They include only the hotels and not the boarding houses. There are about 22 boarding houses with about 350 rooms. The growth of number of rooms and bed places over the period 1981-90 is continuous but after 1985 has been considerably higher than before. However, the growth in hotel rooms and bed places did not keep pace with the growth in hotel rooms and bed places did not keep pace with the growth of tourist arrivals and tourist nights (see Table 1). The abnormal growth of hotel rooms and bed-places during 1990 is worth-noting. There are about 61 restaurants spread over the whole island serving European, Creole, Chinese and Indian dishes.

Occupancy Rates: Table 6 provides information on the room and bed occupancy rates in the large hotels and all hotels for the years 1988-90. A large hotel is defined as the one with 60 or more rooms. In Mauritius, large hotels account for 23% of total hotels, 53% of rooms and 52% of bed-places in hotels. It can be readily seen that large hotels cater almost exclusively to the tourists only while the smaller hotels also cater to non-tourists. Moreover, it is clearly brought out that large hotels are much more efficient in terms of their occupancy rates for both rooms and beds than the smaller hotels. The underutilization of the capacity created in the smaller hotels is thus a more serious problem than in the larger hotels. Another worth-noting fact is the declining occupancy rates for rooms as well as bed-places in large and smaller hotels over recent years.³ With the rate of growth of tourists and tourist nights being much in excess of the rate of growth of hotel rooms and beds except in 1990, declining occupancy rates of rooms and beds in hotels imply that tourists have preferred private bungalows and boarding houses to hotels in 1988 and 1989. Table 7 supports this contention. It provides information on the type of accommodation the tourists used for selected years. It can be seen from the table that the proportion of tourists using commercial accommodation has been declining from 92.1% in 1984 to 88.7% in 1988. The decline is sharper in the proportion of tourists using hotels - from 81.6% in 1984 to 71.4% in 1988. On the other hand, proportions of tourists using private bungalows, boarding houses or non-commercial accommodation is increasing.

Employment Generation: Tourism as an industry generates direct as well as indirect employment in the economy. Table 8 provides some information on the number of people employed directly in large

³ This trend continues even during 1991 from the evidence available on the first three quarters of 1991.

establishments in restaurants, hotels and travel and tourism agencies. A large establishment is the one employing 10 or more persons. Thus, for instance, direct employment generated even in the private taxis is not included in these figures. The hotels account for about 60% of the direct employment whereas travel and tourism agencies account for about 26% to 28% of the direct employment generated in the tourism industry in Mauritius over the period 1986-90. Employment in tourism industry has been growing significantly at 15.7% p.a. compound rate of growth during 1986-91. Thus, tourism has been a very important sector in generating employment in Mauritius. It seems to have contributed substantially to the present full (or over!) employment situation in the country.

Expenditure & Receipts: Tourism is important for any small country because it contributes to the foreign exchange earnings. Table 9 provides information on the gross receipts from the tourists in Mauritius for the period 1981-91. These figures are collected from the Bank of Mauritius and hence are likely to capture only direct foreign exchange receipts from tourists. This may underestimate the expenditures since the method ignores indirect conversion of foreign currency into Mauritian Rupees by the tourists for certain types of their expenditures. The table, however, reveals interesting pattern. The total receipts from the tourists in Mauritius is growing at the phenomenal rate of 24.3% p.a. over 1981-91. Average receipt per tourist, however, is growing at a slower rate of 13.3% p.a. because the number of tourists is also growing rapidly over the same period. Average receipt per tourist per day has been growing in nominal terms at a rate of 12.6% p.a. over 1981-91 which is remarkable considering the overall inflation rate during the decade of 8.1% p.a. Thus, tourists' expenditure per day spent in Mauritius in real terms has also increased at the rate of 4.5% p.a.

Tourists expenditure by types of expenditure provides useful information on the possible linkages of tourism to the rest of the economy. Table 10 gives result of the surveys of outgoing tourists on their expenditures on different items for selected years. From the table, it is clear that accommodation is predominantly important item of tourists' expenditure followed by meals and beverages, shopping and travel in the order of importance. Although in absolute terms the tourists' expenditure on accommodation increased substantially, it declined sharply in relative terms over the period 1984 to 1988. Such a declining trend in the face of considerable expansion of hotel rooms and bed-places in recent years is bound to cause concern. The other items like shopping, travel and meals and beverages have experienced improvement in relative terms in the tourists budgets. All these items have close links with the domestic economy and hence such increasing trend may be considered good for the economy.

Table 11 presents expenditures of tourists by country of residence for the survey years. If we consider only the total expenditure by tourists, in 1984 the Republic of South Africa was contributing maximum followed by France and Reunion Island. After 1986, however, France has become the most important contributor followed by Republic of South Africa, Reunion Island and Germany. The table also presents figures of average expenditure per tourist and average expenditure per tourist night spent in Mauritius during the same period. It can be seen that tourists from countries at shorter distance like Malagasy Republic, Reunion Island and South Africa are spending lower amount than the tourists from countries at longer distance. The importance of the long haul market is thus obvious. It may, however, be noted that tourist expenditure per night spent in Mauritius which indicates the willingness and ability of tourists to spend is higher among tourists from South Africa as compared to the ones from France and U.K. What may be more surprising is that tourists from France spend less than average per night in Mauritius. However, when we consider the fact that Mauritius was a French colony for a long time; that French is still a major language - almost a second language for Mauritians; and that there are significant French interests in Mauritius, it is possible that several French tourists may be preferring private bungalows and private houses to hotels for their stay in Mauritius.

4. Impact of Tourism on the Economy

The importance of tourism industry is derived not only from its foreign exchange earning capacity but also from its income and employment generating aspects. The latter depends more on the structure

and nature of the domestic economy. In Mauritius, the World Bank had sponsored a study under the United Nations Development Programme in November 1980 with an explicit objective of providing the government of Mauritius with a comprehensive assessment of the contribution tourism is making to the Mauritian economy in terms of income generated, net foreign exchange earnings, contributions to government revenue and employment. (See Archer & Wanhill, 1981.) We summarise here the principal findings of this survey-based year long study because it provided the basis for the government policy changes for the tourism industry during the Eighties. The most pertinent findings of the study were:

- i) The number of tourists increased at an annual rate of 15% between 1970 and 1980 with the principal tourism markets being Reunion, South Africa and France.
- ii) In 1980, tourism contributed 6.15% of GNP at factor cost, though its direct contribution was only 1.87%.
- iii) In 1980, tourism generated wages, salaries and income from self-employment to the extent of 3.8% of GDP at factor cost.
- iv) In 1980, Money accruing to the government from the direct and secondary effects of tourism was about 1.1% of GDP at factor cost.
- v) In 1980, tourism occasioned about 7% of total imports but over a third of these benefitted Mauritian households.
- vi) Tourism income multiplier⁴ was 0.96.
- vii) The multiplier for imports was 0.91 and hence net effect of tourism on Balance Payments was only 0.09 of the total tourists expenditure in Mauritius in 1980.
- viii) In 1980, on average, every Rs.100,000 spent by tourists maintained about 5 jobs and every 100 tourists maintained a total of about 15 jobs.
- ix) For every direct job, tourists' spending maintained an additional 2.76 secondary jobs elsewhere in the economy.
- x) The 1980 survey results show that tourists on the package tour spend more per capita than other tourists on accommodation, gratuities, transport, casinos, sporting activities and local handicrafts than other tourists. In 1980, the proportion of the package tourist was about one-third. In terms of income multipliers of the package tourists and the other tourists, two types of tourists have the same effects statistically.
- xi) As Table 12 shows, the impact measured in terms of tourist income multiplier is higher in Mauritius than many other island economies.
- xii) Tourists' expenditure per capita can be increased by developing the European market still further.
- xiii) It is also clear that greatest impact on income, employment, etc. is made by tourists with highest spending. Thus, tourists from European countries make much more impact on Mauritian economy than tourists from Reunion Island and Malagasy Island.

Based on the methodology discussed in Annexure 1 below, we have estimated tourism multipliers for the Mauritian economy in the year 1988. Our major findings are:

- 1) In 1988, tourism contributed 11% of GNP at factor cost though its direct contribution was only 3%.
- 2) In 1988, the money accruing to the government on account of the tourism activity in the economy was about 2.2% of GDP at factor cost.
- 3) In 1988, tourism occasioned about 6% of total imports but about 38% of these benefitted the Mauritian households.
- 4) In 1988, the estimated tourism multipliers for Mauritian economy are summarised below:

⁴ Tourists' expenditure becomes revenue to hotels, restaurants, night clubs, casinos, tour companies, taxi operators, sports firms, shops and street vendors. This money is then respent and gets recirculated in various ways in successive rounds. It forms a declining series and hence has finite total. This process of income generation is aimed to be summarised by the measure of tourism multipliers.

Aggregate	Multiplier*
GDP at factor cost	1.05
Import Duty & Sales Tax	0.130
Net other Indirect Taxes	0.085
Imports	0.503
Net Balance of Payments(Current A/c)	0.497
* Multipliers represent ratio of change in the aggregate due to tourism to the total tourist expenditure.	

When we compare our results with those of the study by Archer and Wanhill (1981), it becomes clear that over the period 1980-88, the import intensity of tourism (direct as well as total) has considerably declined and that the economy has been more integrated with stronger interindustry linkages. As a result, the net impact of tourism on the country's Balance Payment has become much more favourable than before.

It is important to recognise that tourism industry does not have only positive effects on the economy. It also has negative effects in terms of putting severe strain on the island's infrastructure. The existing road, telephone and electricity networks are sometimes being overutilised. As per a survey of the departing tourists in 1988, infrastructure was considered to be the biggest problem. Mauritian citizens have started linking tourists with the island's environmental degradation though no serious research has been undertaken to evaluate the environmental effects of tourism on the island. However, the following observations are made about the environmental effects of tourism expansion (See, Ministry of Tourism, 1988):

- a) Unregulated sewage and garbage disposal is a major cause of environmental degradation.
- b) Tourist related activities like yachting adversely affect the mangroves, reefs and seagrasses.
- c) Destruction of coral reef leads to beach erosion which is one of the greatest threats to beach hotel tourism.
- d) Extraction of sand from beaches for use in the construction of concrete buildings including hotels causes beach erosion.
- e) Uncontrolled development has spoilt many beautiful places.
- f) Coastlines, particularly beaches are among the least stable and most physically changeable of earth's landform systems and hence highly vulnerable environment.
- g) It takes a considerably long time to restore an ecosystem once it is damaged.
- h) Tourism may substantially contribute to damaging the environment if tourists are overcrowding the island.

In this context, the concept of 'tourist carrying capacity' of the island which relates to the quality of the tourism related resources, becomes relevant. 1982 World Tourism Conference had stated with consensus of all member states that "satisfaction of tourism requirements must not be prejudicial to the social and economic interests of the population in tourist areas, to the environment, or above all, to the natural resources, which are the fundamental attraction of tourism." Excess flow of tourists can damage seriously the environment which would prove less and less attractive to the tourists in future. Thus, the concept of 'tourists carrying capacity' is connected to the optimal tourists' flow in the temporal context.

5. Government Policies Related to Tourism

Development of the tourism industry was an important element of the structural adjustment programme started in 1979. Through tourism development, the government primarily aimed to increase foreign exchange earnings and generate additional employment. The government took several measures to strengthen the promotion of Mauritius as a destination for tourists, improve air access to the country from abroad, diversify tourists markets and encourage hotel development to expand existing room capacity. As a result of these measures, the tourism industry in Mauritius grew very rapidly. It became the third most important industry on the island. Over the decade 1979-88, tourists arrival increased at a rate of 14% p.a. Such a fast pace of development has necessitated that the country takes a pause for reassessment because its physical and social capacities are limited and also because tourism industry is highly volatile adding further to the instability and risk of the small island economy which is already overexposed to the factors beyond its control. The government, therefore, decided to bring out a White Paper on Tourism in 1988 which clearly sounds a note of caution in this regard. To quote from the White Paper the "government has decided to:

- maintain the present position of the tourism industry in the economy without it becoming the main one.
- aim at a carrying capacity of about 325,000 tourists by 1992.
- stop granting new sites for the construction of resort hotels immediately."

It is thought that a comprehensive policy for tourism and related services should guarantee a reduction of social disparity and greater advantages for all social strata. The policy should be devised keeping in view the temporariness of the tourists population so that greater consideration should be given to the comforts and advantages of the local population than of the tourists. The salient features of the current policy of the government in various sub-sectors can be summarised as follows:

A) Tourists: (i) Encourage selective tourism aiming at the upmarket; (ii) Mass-tourism is discouraged; (iii) Chartered flights are not allowed; (iv) In order to maintain ecological balance, the annual tourists; flow will not be allowed to exceed a third of the total population of the island. Currently this ceiling is not effective but in near future it is likely to be if the past trends continue.

B) Tourism Product: (i) Maintain Mauritius as essentially a resort destination; (ii) Take measures to encourage the 'culture industry' because the tourists of the 1990's are likely to be interested in the cultural and linguistic diversity of the island. Besides specific projects for this, Museums, parks, inland tours, etc. have to be encouraged; (iii) Cultural component has to be emphasised in the promotional activities; (iv) Develop outer islands like Rodrigues to attract and accommodate enthusiasts; (v) Provide caravanning and camping sites to cater for the local population.

C) Air Access: (i) Promote additional route network in the region on selective basis; (ii) Take necessary measures to maximise air transport capacities through the national carrier; (iii) Try to get landing rights in Japan; (iv) Establish a direct air link with Australia where there is a large colony of Mauritians who would like to return to Mauritius once in a year. Recently 32 flights in a year by Air Mauritius have been started; (v) Similar direct air link by the national carrier is sought to be established with Middle East and Malaysia.

D) Marketing: (i) Diversify the existing market sources and tap new markets; (ii) Make efforts to increase the share of long-haul tourists, raise their length of stay and increase their per capita expenditure; (iii) Publish a quarterly tourism newsletter for local and overseas distribution; (iv) Produce good promotional film and attractive promotional material on Mauritius; (v) Organise international events in Mauritius on a regular basis; (vi) Establish well-defined system whereby the public and the private sectors participate jointly in promotional campaigns; (vii) Organise annual workshops involving all professionals of the industry and the government's agents overseas; (viii) It is under consideration to earmark 5% of total tourism earnings for promotional activities.

E) **Infrastructure:** (i) Encourage the construction of golf courses of international standard; (ii) Provide enough budget to implement the infrastructure plans in the main tourists zones; (iii) Signpost all roads leading to tourists sites; (iv) Encourage construction of marinas and regulate yachting; (v) Set up additional duty-free shops throughout the island; (vi) Equip all taxis with taxi-meters; (vii) Provide basic infrastructure on Rodrigues and Agalega islands to encourage tourists flow.

F) **Hotel Industry:** (i) New Hotel Development certificates are not to be issued as far as possible for next 5 years; (ii) Take necessary steps to complete the already planned hotel projects; (iii) No further extension to promoters failing to respect time limit allowed to them for starting construction; (iv) Give priority to the Mauritian entrepreneurs over foreign nationals in reallocation of hotel sites; (v) Set up a Tourism Co-ordination, Evaluation and Monitoring Unit at the Ministry of Housing, Lands and Environment; (vi) Review and revise the standard list of equipments and materials qualifying for duty concession so as to encourage maximum use of locally available materials and items. Since September 1991, Ministry of Finance and Ministry of Tourism jointly approve such a list; (vii) On obtaining an HDC, the hotel enjoys benefits like concessions in sales tax, tax holiday or exemption from income tax for 10 years, import duty concessions on selected items, etc.; (viii) 10% Government tax surcharge on all hotel bills; (ix) Maximum size of the hotel is restricted to 200 rooms; (x) Hotels on the coast will not be high - rise i.e. groundfloor + one floor; (xi) Plot coverage ratio can be at the most 40%; (xii) Training of the hotel staff has to be strengthened so as to achieve high standards in hotel service. Vocational training centres to be encouraged for upgrading skills of existing labour in the industry. In this connection, Government Hotel and Catering Training School established in 1973 has been given special attention.

G) **Environment:** (i) Hotels with 60 or more rooms should have a water treatment plant (which is very costly) so that the water should be recycled but should not be driven at sea. Hotels with less than 60 rooms should have a septic tank depending on the recommendation of Ministries of Health, Sanitation and Environment; (ii) Review the refuse collection system nationwide; (iii) Restore and protect coastal stretches and create a marina; (iv) Quality control is imposed on all tourist resorts in the country; (v) Ban on removal of corals and shells from the sea; (vi) Encourage use of rocksand for construction purposes; (vii) Control the use of transistor radios on beaches; (viii) Restrict movement of speed boats and waterskiers along the shores; (ix) Take appropriate measures to preserve the social and cultural values of people and discourage the commercialization of religious rites and ceremonies; (x) Undertake a programme to eliminate stray dogs and cats throughout the island; (xi) All development projects must comply and attune to environmental and cultural protection in terms of their architectural design, landscaping, etc.; (xii) Take measures to protect the wild flora and fauna of the islands; (xiii) Environmental Protection Department has been set up to prevent, reduce and control pollution from any source.

H) **Handicraft:** (i) Take measures to raise substantially the local handicraft production; (ii) Restructure the National Handicraft Centre by giving it more autonomy; (iii) Provide adequate training to trainers and set up ten training centres accordingly; (iv) Undertake an intensive promotion of handicraft in local and international markets through participation in exhibitions and advertising campaigns.

6. Issues in Tourism Development

In spite of the government's declared intentions of targeting and promoting only select clientele in the up-scale tourist market, the growth of all categories of tourists in Mauritius in recent years has been phenomenal. The government does not want the tourism to become the most dominant industry in Mauritius because of its very volatile nature. Moreover, it would only increase the economy's dependence on exogenous factors like recession in the source countries. The main issues emerging in the development of tourism industry in Mauritius may, therefore, be considered as follows.

Targetting only the upper-end of the tourist market has the benefits of less crowding, more earnings of foreign exchange, greater favourable impacts on the economy's income, lower degree of interference

with local population and all related benefits on ecological and environmental fronts. It, however, has several problems, too. It requires significantly higher quantity and quality of the promotional activity with much larger budget allocation. Serious campaign of diversification of tourists market has to be launched. In terms of the long-haul market, the island's biggest contributor, viz. France, has majority of the tourists spending less than the average. Other markets like Japan, Far-East and Middle-East have to be seriously explored and developed. In this connection, it is interesting to note that, as per 1985 survey, only 15% of the tourists are persuaded by travel agents, tour operators or media advertisements to come to Mauritius. About 50% of the tourists come here on the recommendation of friends. Given this finding, the level and quality of service provided to tourists in Mauritius assumes added significance. In this connection, it may be noted that, in 1988, only two-fifths of the existing hotels, accounting for two-thirds of the rooms, are of acceptable quality. [World Bank, 1989]. Upgradation of the existing hotels is, therefore, urgently required which would again demand considerable resources.

In order to attract upper-end tourist market, the country must offer a wide range of tourist products and easy and convenient access to them. Hotels in Mauritius are dispersed in isolated locations by intentional policy of having pockets of development throughout the island rather than concentrated development approach. The transport network including road, car-rentals and taxis play a very important role. Not all taxis on the island have meters even today. Car-rentals are limited and expensive. Roads have been improved of late. Other tourist related infrastructure like golf courses, yacht chartering, deep-sea fishing, sea-diving, recreational park, cinemas, museums, shopping centres have to be developed with certain minimum quality level assured. This would further require investment of resources. Since most of such facilities are largely used by tourists of certain categories, their regular flow has to be of a magnitude which would make provision of these facilities viable on sustained basis. Whether such a magnitude of the flow of tourists is consistent with the overall annual ceiling of 1/3rd of population prescribed by the government on tourist flow has to be carefully investigated.

Selective clientele strategy can prove to be viable only if expenditure per tourist increases substantially. Given the shopping facilities on the island, the average expenditure of tourists on purchase of souvenirs and local handicrafts remains very low. The idea of providing specialised duty-free shops in hotels may not work because the long-haul tourists invariably come via airports with very attractive duty-free shopping on their way to and fro the island. In any case, it involves increased import intensity and it may or may not be considered desirable for the domestic economy. If the duty-free shopping has to cater to only short-haul tourists who are known to be spending considerably lower amount than average, it is not likely to be a viable proposition.

In order to meet standard of services in hotels to cater to the up-scale tourists, the Mauritius Government Hotel and Catering Training School has to train 800 persons per year. However, the school was not able to perform its task even to the extent of 25% of its target. This was on account of a high turnover of its teachers due to low salaries in the school, and lack of necessary equipment. The government has recently revised the teachers salaries substantially and has renovated its facilities with provision of additional equipments. Private sector institutions have also come up to bridge the gap. Even the University of Mauritius has started a two-year diploma course in hotel management since 1987. In the light of the current state of employment in the country where the unemployment rate has fallen below 2%, all such training efforts imply serious problem of labour shortage. In such an environment, the hotel industry would flourish only at the expense of some other industries. The government here like many other places does not encourage import of labour. All this puts tremendous pressure on the labour market. Wages are, therefore, rising and so the prices. High inflation would cause loss of overall competitiveness of the economy which would be very dangerous for stability of the country in the long run when preferential access to export markets particularly of sugar and garments stops or declines. Thus, the policy of tourism based on selective clientele may lead to high cost economy reducing the competitiveness of its products and thereby contradicting its basic objective. Such trends, moreover, may also lead to distortions in the resource allocation because

of the government's intervention of market forces by direct or indirect subsidisation of sectors like tourism industry. There is hardly any serious effort to appraise such a policy of subsidisation from the long run point of view.

Methodology for Estimating Tourism Multipliers

We have followed the same methodology as is followed in Archer and Wanhill (1981). We, however, reproduce it below because there are some variations dictated by the non-availability of disaggregated data in our case. Basically, it represents an application of Input-Output Tables. National Accounts Statistics of Mauritius, 1990 presents an I-O Transaction Table for the year 1987. It is a 15 x 15 sector classification with the primary factors consisting of imports, import duty, employee compensation, operating surplus and net indirect taxes. The final demand included household consumption, government consumption, domestic fixed capital formation, change in stock and exports of goods and services. The system can be represented in the matrix form as:

$$X = AX + F \quad \text{And } P = BX \quad (1)$$

Where

$X = n \times 1$ vector of gross output

$F = n \times 1$ vector of total final demand

$P = K \times 1$ vector of primary factors

$A = n \times n$ matrix of input coefficients

$B = K \times n$ matrix of factor input coefficients.

$$\Delta X = (I - A)^{-1} \Delta F \quad (2)$$

$$\text{and } \Delta P = B \Delta X \quad (3)$$

Tourists expenditures by sectors are recorded in ΔF . From (2), we obtain corresponding changes in X . The resultant ΔX vector is then diagonalized to form an $n \times n$ matrix, say ΔX . Then,

$$\Delta P = B \cdot \Delta X \quad (4)$$

Where ΔP is a $K \times n$ matrix in which each row contains the effects of the tourist expenditure on the given primary factor in each of the sectors. The multipliers are then obtained by dividing these elements and their total by the total tourist expenditure. Such multipliers estimate only the direct and indirect effects of the expenditures. They ignore the induced effects on account of increased consumption expenditures by households out of the increased income they receive on account of the direct and indirect effects of the tourists expenditures. In order to estimate the (total) income multipliers of the tourists expenditures, matrix A is augmented with an additional column and a row. The column is the final consumption expenditures by households and the row consists of gross value added at factor costs. Let augmented matrix be A^* . Following the same formula as in (2), we obtain,

$$\Delta X^* = (I - A^*)^{-1} \cdot \Delta F^* \quad (5)$$

After diagonalizing ΔX^* we obtain $A^* \Delta X^*$ whose $(n+1)^{\text{th}}$ row contains the total effect of tourists expenditures on the personal income generated in each sector of the economy. Similarly, the impact on imports and government revenue (i.e. taxes) are obtained by the matrix $B^* \Delta X^*$. Multipliers are obtained by dividing the elements in the respective rows and their totals by the total tourists expenditures.

Apart from the assumptions of the standard Input-Output model, the estimation of the (total) tourists multipliers are based on the assumption of constant Average Propensity to Consume for household sector with unit income elasticity of demand for every commodity. It also assumes autonomous exports, investment and government expenditures. However, it assumes constant Marginal Propensity to Import with unit income elasticity of demand for all imported commodities for final consumption and constant import coefficients for imports of all goods and services used as intermediate products. Finally, it is assumed that all tourists expenditure in 1988 in Mauritius is on final goods and services produced in the year 1988.

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Table 1
Tourist arrivals by mode of transport, total arrivals and tourist nights spent during period 1981-1990

Year	Total Arrivals	Tourists arriving during period			Tourist nights spent during period	% change during period	
		Sea	Air	Total		Tourist Arrivals	Tourist nights
1981	168,973	590	121,030	121,620	1,361,200	+ 5.7	+ 4.6
1982	155,669	680	117,680	118,360	1,392,510	- 2.7	+ 2.3
1983	177,665	960	122,860	123,820	1,405,870	+ 4.6	+ 1.0
1984	195,461	1,230	138,440	139,670	1,541,590	+ 12.8	+ 9.7
1985	212,860	920	147,940	148,860	1,735,960	+ 6.6	+ 12.6
1986	235,640	950	164,360	165,310	1,878,370	+ 11.1	+ 8.2
1987	293,160	1,530	206,040	207,570	2,371,970	+ 25.6	+ 26.3
1988	343,940	1,770	237,530	239,300	3,002,820	+ 15.3	+ 26.6
1989	379,080	840	261,950	262,790	3,196,780	+ 9.8	+ 6.5
1990	418,200	1,200	290,350	291,550	3,500,000	+ 10.9	+ 9.5
1991	--	--	--	305,000*	3,660,000*		

* Forecast based on first nine months of 1991.

Source: Central Statistical Office.

Table 2
Average length of stay of tourist by country of residence, 1981-1990

Country of residence	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990*
Belgium	20.4	12.7	13.5	12.4	14.3	14.7	17.0	15.4	16.7	16.0
France	11.9	12.9	12.6	12.6	12.7	11.7	12.0	13.4	13.4	13.0
Germany Fed.Republic	16.3	16.7	16.1	14.8	16.4	15.8	15.2	15.5	15.2	15.0
Italy	10.3	11.3	11.8	11.8	11.2	11.0	10.9	11.5	11.8	12.0
Switzerland	13.5	20.5	14.3	13.6	14.7	16.1	15.0	14.9	15.7	16.0
United Kingdom	21.7	20.8	21.8	21.3	17.4	16.9	17.3	17.2	18.9	19.0
Malagasy Rep.	6.1	7.7	6.6	7.4	7.8	8.6	8.1	10.0	7.9	8.0
Reunion	8.4	9.7	8.1	8.2	9.5	8.4	8.2	9.4	8.7	9.0
Seychelles	7.3	8.2	14.9	25.4	14.6	12.4	16.7	13.4	12.0	12.0
Kenya	7.4	13.0	12.7	10.1	10.1	11.9	8.9	10.2	15.9	16.0
South Africa Rep.of	9.3	9.3	9.1	9.1	9.4	10.0	10.2	11.2	10.1	10.0
Zambia	8.7	14.5	23.5	13.3	20.1	11.3	14.9	8.0	10.8	11.0
Zimbabwe	9.6	12.6	11.5	11.7	15.0	15.3	14.7	12.1	12.6	12.0
Australia	13.1	10.5	18.8	13.3	11.2	12.4	12.7	14.5	16.5	16.0
India	15.4	14.6	22.0	13.1	17.2	20.2	15.4	20.0	18.1	18.0
Japan	8.0	3.8	16.8	4.9	7.8	6.1	5.7	7.1	5.4	6.0
Singapore	7.1	10.3	46.0	3.9	8.6	7.8	9.8	12.6	6.6	7.0
U.S.A.	12.7	18.6	11.4	13.6	14.8	8.1	13.0	15.7	14.6	15.0
Other countries	15.7	14.1	14.6	14.8	12.7	14.1	12.7	17.3	15.3	10.6
All countries	11.2	11.8	11.4	11.0	11.7	11.4	11.4	12.5	12.2	12.0

*Provisional

Country of residence	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990*
Belgium	0.6	0.5	0.5	0.6	0.6	0.7	0.7	0.7	0.6	0.7
France	17.9	19.0	17.8	18.2	18.5	19.6	21.3	21.0	20.4	18.2
Germany Fed.Republic	6.2	5.9	5.6	5.7	6.0	5.5	6.6	6.3	6.9	6.8
Italy	4.9	4.8	4.5	4.4	4.6	5.5	5.9	6.2	5.5	4.9
Switzerland	1.2	1.3	2.1	3.9	4.3	4.5	4.0	3.8	4.1	3.7
United Kingdom	5.2	4.9	4.7	4.1	4.8	5.1	5.7	5.8	6.3	7.5
Malagasy Rep.	5.7	6.0	6.5	5.6	4.5	3.7	3.5	2.8	2.5	2.2
Reunion	22.7	25.5	24.4	23.2	23.9	24.7	23.1	23.8	24.9	25.1
Seychelles	0.5	0.5	0.4	0.2	0.5	0.5	0.5	0.8	1.3	1.2
Kenya	0.8	0.6	0.6	0.5	0.5	0.5	0.5	0.5	0.4	0.5
South Africa Rep.of	20.5	19.1	21.9	22.6	18.4	16.1	14.9	15.0	14.0	14.4
Zambia	1.1	0.9	0.6	0.5	0.3	0.2	0.4	1.1	0.7	0.5
Zimbabwe	1.0	0.8	1.4	1.3	1.3	1.7	1.2	1.2	1.1	1.3
Australia	3.0	2.3	1.3	1.1	1.7	1.5	1.5	1.0	1.0	1.0
India	1.9	1.5	1.4	1.8	2.0	1.4	1.4	1.8	1.8	2.8
Japan	0.2	0.2	0.1	0.2	0.4	1.1	0.9	0.9	1.1	1.1
Singapore	0.1	0.1	0.0	0.1	0.7	0.8	0.5	0.6	0.8	0.7
U.S.A.	0.9	0.8	0.8	0.8	1.0	1.1	0.9	0.6	0.7	0.8
Other countries	5.6	5.3	5.4	5.2	6.0	5.8	6.5	6.1	5.9	6.6
All countries	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: Same as Table 1.

Table 4 Tourist arrivals, seasonal index 1981-1990										
Month of arrival	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990
January	110	121	127	122	115	119	109	116	120	115
February	92	86	89	93	86	84	81	82	77	80
March	91	87	95	96	95	101	78	90	89	81
April	103	102	83	95	93	86	105	87	89	105
May	89	97	93	95	92	95	86	99	92	96
June	62	59	62	65	68	63	83	67	67	74
July	87	93	95	90	79	91	91	96	96	91
August	128	129	126	117	140	131	121	125	125	129
September	106	104	98	94	93	88	106	92	95	95
October	97	99	97	97	95	92	109	117	116	111
November	105	99	101	107	112	119	106	105	103	100
December	132	123	135	128	133	132	125	12	132	122
Range	70	64	73	63	72	69	47	58	65	55

Monthly Tourist Arrival
 Note: Seasonal Index = ----- x 100
 Monthly Average for the year
 Source: Basic Data from Central Statistical Office, Mauritius.

Table 5 Hotels, rooms and Bed places, 1981-1990					
Year	No. of Hotels*	No. of Rooms	% Change	No. of bed Places	% Change
1981	51	2,201	--	4,484	--
1982	51	2,204	0.1	4,530	1.0
1983	55	2,300	4.4	4,900	8.2
1984	54	2,488	8.2	5,102	4.1
1985	55	2,630	5.7	5,387	5.6
1986	56	2,888	9.8	5,955	10.5
1987	60	3,108	7.6	6,418	7.8
1988	64	3,399	9.4	7,005	9.1
1989	67	3,605	6.1	7,374	5.3
1990	75	4,603	27.7	9,572	29.8
1991 (Sept.)	80	4,777	--	9,925	--

Note: *Exclude hotels converted into boarding houses but include newly constructed hotels.
 Source: Ministry of Youth, Sports and Tourism.

Table 6						
Occupancy Rates in Hotels in Mauritius(in %)						
	Large Hotels			All Hotels		
	1988	1989	1990	1988	1989	1990
I. Room Occupancy Rates						
(a) Total	82.9	77.8	76.7	66.1	62.8	61.8
(b) Tourists	82.8	77.6	76.4	65.3	61.9	61.2
II. Bed Occupancy Rates						
(a) Total	74.1	69.6	68.4	58.2	55.3	54.3
(b) Tourists	74.0	69.4	68.1	57.4	54.6	53.6
Source: Ministry of Youth, Sports and Tourism.						

Table 7			
Percentage distribution of tourists interviewed by type of accommodation used, 1984-1988			
Type of Accommodation	1984	1986	1988
Commercial	92.1	90.6	88.7
1. Hotel	81.6	76.4	71.4
2. Private Bungalow	6.2	6.9	10.8
3. Boarding House/ Guest House	3.3	5.2	5.1
4. Private House	0.6	1.6	1.3
5. Other Commercial residence	0.4	0.5	0.1
Non-commercial	7.9	9.4	11.3
6. With friends/Relatives	7.3	8.7	9.9
7. Other Non Commercial Residence and Not stated	0.6	0.7	1.4
TOTAL	100.0	100.0	100.0
Source: Survey of Outgoing Tourists, conducted by Mauritius Government Tourist Office.			

Table 8 Employment* in the tourist industry, 1986-1990**						
Industrial Group	1986	1987	1988	1989	1990	1991
Restaurant	672	725	867	1,010	900	900
Hotel	3,079	3,670	4,116	4,600	5,995	6,850
Travel & Tourism	1,329	1,732	1,991	2,065	2,775	2,800
Total	5,080	6,127	6,974	7,684	9,670	10,550

* Large establishments only (i.e. employing 10 or more persons)
 ** During September of each year.
 Source: Central Statistical Office, Mauritius.

Table 9 Gross Receipts from tourism, 1981-1990			
Year	Total (Rs. Million)	Average in Rs. per	
		Tourist	Tourist Night
1981	433.0	3,560	318.10
1982	450.3	3,804	323.37
1983	503.0	4,062	357.79
1984	632.9	4,531	410.55
1985	844.5	5,673	486.47
1986	1,190.1	7,199	633.58
1987	1,786.0	8,604	752.92
1988	2,373.6	9,919	790.46
1989	2,795.7	10,639	874.54
1990	3,500.0*	12,005	1,000.00
1991	3,800.0*	12,459	1,038.25

* Provisional
 Source: Bank of Mauritius.

Table 10 Expenditure of tourists by type of expenditure, 1984-1988						
Type of Expenditure	Expenditure (000' Rs.)					
	1984	%	1986	%	1988	%
Accommodation	383,032	(59)	631,980	(52)	1,078,765	(45)
Meals and beverages	94,382	(15)	216,060	(18)	464,243	(19)
Gratuities	4,245	(1)	16,531	(1)	30,871	(1)
Transport	48,906	(8)	94,227	(8)	263,231	(11)
Casinos	14,862	(2)	37,029	(3)	50,971	(2)
Sporting activities	7,343	(1)	18,680	(2)	50,253	(2)
Shopping (including local, handicraft and souvenir)	75,945	(12)	178,700	(15)	377,378	(16)
Other	16,577	(3)	25,293	(2)	72,365	(3)
Total	645,292	(100)	1,218,500	(100)	2,388,077	(100)

* The figures in this table are different from those in Table 9. These are obtained from the Survey of Outgoing Tourists conducted by MGTO, while the former are the results from compilation of the Balance of Payments by the Bank of Mauritius.

Table 11 Expenditure of tourists by country of residence, 1984-1988									
Country of Residence	1984			1986			1988		
	Total (in Rs'000)	Average per		Total (in Rs'000)	Average per		Total (in Rs'000)	Average per	
		Tourist (in Rs)	Tourist night (in Rs)		Tourist (in Rs)	Tourist night (in Rs)		Tourist (in Rs)	Tourist night (in Rs)
France	109,202	4,289	353	240,509	7,430	636	526,863	10,487	783
Germany, Federal Republic	53,470	6,777	459	118,989	13,047	828	260,143	17,194	1,109
Italy	51,117	8,285	699	99,363	10,907	992	216,934	14,501	1,266
Switzerland	45,975	8,451	620	96,041	12,996	807	158,716	17,480	1,170
United Kingdom	53,396	9,270	436	88,468	10,408	616	218,274	15,840	919
Malagasy Republic	9,474	1,217	164	15,191	2,458	287	19,945	2,946	295
Reunion Island	74,857	2,318	283	168,138	4,120	490	277,021	4,866	518
South Africa, Rep.of	157,258	4,983	547	177,155	6,640	666	345,473	9,634	859
Singapore	N.A.	N.A.	N.A.	10,274	7,554	970	12,159	9,074	720

Source: Same as Table 10.

Table 12 Tourist Income Multipliers in Small Island Economies	
Country	Tourism Income multiplier
1. Dominica	1.20
2. Mauritius (a) in 1988 (b) in 1980	1.05 0.96
3. Bermuda	1.03
4. Hong Kong	1.02
5. Hawaii	0.90 - 1.30
6. Antigua	0.88
7. Bahamas	0.78
8. Fiji	0.69
9. Cayman Islands	0.65
10. British Virgin Islands	0.58

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