

BUDGET 1984 : THE GOVERNMENT'S STRATEGY BEHIND THE BUDGET — AN OFFICIAL VIEW

The Budget 1984 drew on previous experience and sought to consolidate past gains and to lay the foundation for sustained development in the future. It was set within the frame-work evolved in the Public Investment Programme (1983-87). The Budget Speech identified objectives, specified targets and outlined policies and measures for the period ahead.

The initial step in the whole process has been to try to evolve the optimal development strategy for Sri Lanka. In doing this it was recognised that each sovereign economic entity must base its strategy on the specific objective conditions that it has to contend with. The policy framework

that has been adopted is based on the premise that the liberalisation of the economy has been a major source of growth impulses and dynamism in the economy, during the past six years. It recognises that autarkic strategies are not practicable in Sri Lanka, given the country's resource endowment and domestic market size. This has been amply demonstrated by the failure of these policies to promote growth and employment during the past twenty years. Inward looking policies have the potential for improving the material well-being of the people on a sustained basis only in a context where a strong capital goods sector can be developed out of domestic savings. Small ex-colonial countries

like Sri Lanka do not have the capacity to generate sufficient savings, nor the resources or the market size to make a strong capital goods sector economically viable. In such a context sufficient foreign exchange must be earned to finance the capital and intermediate goods necessary for the structural transformation of the economy. In Sri Lanka's case the foreign exchange bottleneck is exacerbated by the country's reliance on imported fossil fuels for its energy requirements. In 1983 imports of petroleum products are estimated to have absorbed about 40 percent of total export earnings.

Given the limited options and narrowly circumscribed room for manoeuvre confronting countries like Sri Lanka, export-led economic diversification and an open economy arguably provide the best possible framework for economic policy. This was the justification for the far reaching economic reform introduced in 1977. These policies constituted a significant break from the inward looking and regulatory policies of the past. Trade and payments were liberalised. The exchange rate was unified and realistically realigned. Steps were taken to render the Public Sector more efficient and to revitalise the private sector. Incentives were offered to enhance investment, production and employment. An environment was created which fostered innovation, and entrepreneurship. These policies have served to double both investment as a percentage of GDP and real growth. In addition the rate of unemployment has been almost halved.

Closing up of the economy could well stifle many of the growth impulses that have emerged during the last six years. This would have a negative impact on incomes and employment as well. These are the ideological considerations that underpin the measures introduced in the Budget. These measures sought to reduce instability introduced into the system

Table 11
Recurrent Expenditure — Estimates 1983 and 1984

	Rs. Million	
	1983 Revised Estimates	1984 Budget Estimates
1. Personal emoluments	5,608	6,466
2. Pensions	1,848	2,108
3. Interest on Public Debt	6,912	7,995
Domestic	(5,442)	(6,261)
Foreign	(1,470)	(1,734)
4. Import Duty rebate	820	1,060
5. Transfers		4,002
Kerosene		387
Food stamps		1,510
Intergovernmental subsidy to NSB		500
Free Text books	4,335	60
Infant milk food		100
Price Support Scheme for tea		24
Milk Board		25
Fertilizer subsidy		1,000
Reimbursement of losses to Corporations		100
Other public institutions		296
6. Other	5,214	7,019
Add: (Estimated under expenditure)	1,496	—
Total	26,233	28,650

Source: *General Treasury*

Table 111
Recurrent Expenditure (Ministry-wise) – 1983 and 1984

Ministry	1983		1984	
	Revised Estimates (Rs. Mn)	Percentage	Budget Estimates (Rs. Mn)	Percentage
1. The President, Prime Minister, Supreme Court Judges, etc.	181.9	0.7	142.4	0.5
2. Defence	1,184.6	4.6	1,416.5	4.9
3. Foreign Affairs	228.4	0.9	250.3	0.9
4. Plan Implementation	105.6	0.4	135.2	0.5
5. Lands and Land Development	330.5	1.3	337.2	1.2
6. Trade and Shipping	143.6	0.6	145.5	0.5
7. Education	2,360.9	9.1	2,567.8	9.0
8. Higher Education	280.8	1.1	335.3	1.2
9. Power and Energy	41.3	0.2	56.2	0.2
10. Labour	55.1	0.2	56.8	0.2
11. Public Administration	1,722.1	6.6	2,013.1	7.0
12. Rural Development	15.9	—	13.1	—
13. Local Govt. Housing & Construction	621.9	2.4	589.4	2.1
14. Industries and Scientific Affairs	46.8	0.2	54.6	0.2
15. Finance and Planning	12,265.2	47.1	13,123.0	45.8
16. Transport	857.6	3.3	1,090.3	3.8
17. Transport Boards	1.0	—	1.0	—
18. Private Omnibus Transport	0.9	—	0.9	—
19. Plantation Industry	2.4	—	12.8	—
20. Justice	212.8	0.8	239.9	0.8
21. Agricultural Development & Research	348.3	1.3	331.7	1.2
22. Fisheries	31.4	0.1	36.1	.1
23. Mahaveli Development	302.6	1.2	268.7	0.9
24. Youth Affairs & Employment	108.8	0.4	111.3	0.4
25. Rural Industrial Development	50.9	0.2	51.7	0.2
26. Posts & Telecommunications	589.6	2.3	747.1	2.6
27. Health	1,005.8	3.9	1,250.9	4.4
28. Colombo Hospitals & Family Health	280.0	1.1	316.6	1.1
29. Indigenous Medicine	31.4	0.1	38.9	0.1
30. State	217.4	0.8	251.6	0.9
31. Social Services	186.4	0.7	187.0	0.1
32. Cultural Affairs	29.6	0.1	30.8	0.1
33. Parliamentary Affairs & Sports	17.1	—	17.3	0.1
34. Food & Co-operatives	1,952.2	6.7	1,977.6	6.9
35. Textile Industries	29.6	0.1	31.2	0.1
36. Coconut Industry	1.6	—	1.5	—
37. Regional Development	5.8	—	6.1	—
38. Highways	173.6	0.7	180.0	0.6
39. Janatha Estate Development	0.8	—	0.8	—
40. State Plantations	0.4	—	0.4	—
41. Home Affairs	210.7	0.8	228.2	0.8
42. District Ministries	—	—	—	—
43. Rehabilitation	—	—	1.2	—
Total	26,233.2	100.0	28,650.0	100.0

Sources: *General Treasury, Central Bank of Ceylon.*

through the budget and to encourage exports and efficient import substitution. This would reduce price instability by increasing supplies and strengthen the balance of payments.

The budget has sought to set the course for the future on the basis of an honest appraisal of the country's resources. Notable progress has been made on the investment, output and employment fronts. These very successes, achieved in the context of an extremely hostile external environment have brought about certain imbalances in the economy. Global stagflation, weak commodity prices and increasing protectionism contributed in no small way to domestic price and external payments instability. The situation has been exacerbated by lack of discipline at the domestic level. The difficulties have been heightened by waste and non priority expenditures.

The mix of remedial fiscal, monetary and exchange rate policies have sought to balance the short-term need to bring about stabilisation and the long-term objective of increasing supplies and employment.

The fiscal measures incorporated in the Budget 1984 have sought to reduce the instability introduced into the system by the budgetary operations of the Government. At the outset of its period in office the Government was compelled to step up public sector infrastructural investment so as to enhance the productive and labour absorptive capacities of the economy. This was inevitable in an investment starved economy with extremely high unemployment. As a result public expenditure, particularly capital expenditure, has increased sharply. While this had beneficial effects in terms of higher employment and incomes, price instability was brought about because revenues were not buoyant enough to meet the increased expenditure. Increasing revenues was difficult at a time when

Table IV
Capital Expenditure (Ministry-wise) – 1983 and 1984

Ministry	1983		1984	
	Revised Estimates (Rs. Mn)	Percentage	Budget Estimates (Rs. Mn)	Percentage
1. The President, Prime Minister				
Supreme Court, Judges etc.	134.5	0.5	64.7	0.3
2. Defence	836.9	3.3	912.9	4.2
3. Foreign Affairs	3.0	—	2.2	—
4. Plan Implementation	477.4	1.9	441.3	2.0
5. Land and Land Development	853.9	3.4	947.3	4.3
6. Trade and Shipping	269.6	1.1	219.2	1.0
7. Education	162.6	0.6	207.9	1.0
8. Higher Education	260.5	1.0	433.9	2.0
9. Power and Energy	808.8	3.2	747.4	3.4
10. Labour	10.9	—	23.4	0.1
11. Public Administration	0.5	—	2.0	—
12. Rural Development	5.0	—	5.0	—
13. Local Govt. Housing & Construction	2,490.9	9.8	2,056.9	9.4
14. Industries and Scientific Affairs	25.6	0.1	58.5	0.3
15. Finance & Planning	2,429.2	9.6	2,819.4	12.9
16. Transport	481.0	1.9	428.8	2.0
17. Transport Boards	156.2	1.8	—	—
18. Private Omnibus Transport	—	—	—	—
19. Plantation Industry	160.0	0.6	169.5	0.8
20. Justice	3.4	—	14.6	0.1
21. Agricultural Development & Research	724.3	2.9	860.0	3.9
22. Fisheries	182.1	0.7	199.3	0.9
23. Mahaweli Development	6,773.0	26.8	6,017.0	27.5
24. Youth Affairs & Employment	35.6	0.1	31.6	1.0
25. Rural Industrial Development	88.2	0.3	133.2	0.6
26. Posts & Telecommunications	574.5	2.3	512.1	2.3
27. Health	821.3	3.2	212.4	1.0
28. Colombo Hospitals & Family Health	6.2	—	18.4	0.1
29. Indigenous Medicine	3.0	—	14.3	0.1
30. State	12.3	—	60.8	0.3
31. Social Services	1.6	—	2.2	—
32. Cultural Affairs	36.0	0.1	19.5	0.1
33. Parliamentary Affairs & Sports	3.1	—	3.0	—
34. Food & Co-operatives	0.1	—	8.6	—
35. Textile Industries	24.8	0.1	55.6	0.3
36. Coconut Industry	166.7	0.7	229.7	1.1
37. Regional Development	13.5	0.1	13.8	0.1
38. Highways	225.7	0.9	221.0	1.0
39. Janatha Estates Development	344.8	1.4	389.0	1.8
40. State Plantations	86.0	0.3	95.5	0.4
41. Home Affairs	0.7	—	0.4	—
42. District Ministries	420.0	1.7	840.0	3.8
43. Rehabilitation	—	—	—	—
Total	20,413.5	80.7	19,492.4	89.2
Sinking Fund contributions and amortization payments	4,890.0	19.3	2,367.6	10.8
GRAND TOTAL	25,303.5	100.0	21,860.0	100.0

Sources: General Treasury, Central Bank of Ceylon.

(a) Includes a sum of Rs 10.6 million being unallocable to various ministries.

the export sector, which is still a major source of revenue, was afflicted by declining prices and when there was a perceived need to activate a private sector which had been stagnant for many years. Slowing down the momentum of the investment programme in mid-stream was also not feasible. Furthermore, the Government was anxious to implement its development programmes quickly so as to reduce the cost of energy in the economy and to combat the backlog of unemployment by increasing the opportunities for productive employment. The Budget 1984 introduced a mix of expenditure restraints and receipt increases which will serve to contain inflationary pressures emanating from the operations of the Government. Improved budgetary performance will also serve to reduce pressure on the balance of payments.

The Budget 1984 also reflects appreciation of the need to rely increasingly on domestic resources. The current levels of foreign financing (13.7 percent of GDP 1978–82) cannot be sustained without running into debt servicing problems. It is, therefore, noteworthy that the Government Current Account operations in 1984 are expected to yield savings that are contributing towards financing the development programme.

One may conclude that the formulation of the Budget 1984 was governed by the economic and social objectives of the Government for the next six years. These are to:—

- (i) maintain the highest viable rate of investment, savings and growth in the economy;
- (ii) increase employment opportunities;
- (iii) reduce the pressure on the balance of payments;
- (iv) maintain reasonable price stability;

- (v) enhance equality of income distribution and the quality of life of the people.

It was within this framework that the Budget 1984 was drawn up. The proposals it contained fall into two categories —

- (1) development oriented measures designed to increase supplies in the priority sectors, particularly exports and efficient import substitution —

- (i) production subsidies for Tea and Coconut were increased

- (ii) tax incentives for exports were rationalised and broadened —

- (a) Tax holidays where applicable have been extended to cover partnerships and individuals, in addition to Companies. In the case of garment exports, tax holidays will be granted hereafter only on profits derived from exports outside the garment quotas.

- (b) in the case of services the tax holiday is to be confined to ship repairing and ship breaking services, and production and export of computer software and computer related services.

- (c) companies eligible for a tax holiday will also qualify for "approved undertaking" status,

- (d) a new scheme is being formulated to encourage gem exporters to export through legitimate channels.

- (iii) Five Year Tax Holidays will be granted to import substitution industries engaged in:—

- (a) the production and processing of sugar,

- (b) the production and processing of milk and milk products,

- (c) livestock activities,

- (d) fisheries activities,

- (e) certain agro-based industries which will be specified,

- (f) tax exemption of interest from non resident foreign currency accounts will be increased from 3 to 6 years.

- (iv) In order to give more meaning to decentralisation and to strengthen the District Council system each DDC has been granted a block vote equivalent to the total sum a district was receiving under the decentralised budget. The total allocation for district budgets was, therefore, increased from Rs. 420 M. to Rs. 840 M.

- (2) Revenue measures designed to enhance the surplus in the current account of the Budget:—

	Rs. (Million)
Income Tax	200
Rehabilitation levy	200
Rehabilitation surcharge	400
Turnover Tax	400
Tobacco Tax	100
Excise duties	90
Customs duties	30
Postal rates	130
Telecommunication charges	90
Passport fees	40
Government fees and rents	30
	1,710

Widespread tax evasion is to be reduced through the introduction of administrative reforms designed to improve the working of the Inland Revenue Department. In addition,

relief has been provided to lower income groups by increasing the threshold and moderating the tax slabs. This helps to offset the "bracket creep" that has taken place due to inflation.

The final estimates of expenditure and revenue are as follows:—
Rs. Million

(i) Recurrent Expenditure	- 28,650
Less Provision for under-expenditure +	573 -28,077
(ii) Revenue	+30,770
(iii) Current Account Surplus	+2,693
(iv) Capital Expenditure net of Public Debt Amortisation	- 19,492
Less Provision for under-expenditure +	2,924 -16,568
Add Public Debt Amortization	- 2,368 -18,936
(v) Net lending on Advance A/cs	-300
(vi) Overall deficit	-16,543

The deficit is to be financed as follows

(a) Foreign outright grants	Rs.4,150 mln.
(b) Project/commodity and other	Rs.8,162 mln.
(c) Domestic Rupee Loans	Rs.3,550 mln.
(d) Banking System	Rs.681 mln.

It is noteworthy that Revenue is expected to increase from 19.9 percent of GDP in 1983 to 22.1 percent in 1984. Recurrent expenditure which amounted to 20.4 percent of GDP in 1983 is expected to be 20.2 percent in 1984. The decision not to undertake any new projects during the current year has meant that capital expenditure has decreased from 12.6 percent of GDP in 1983 to 11.9 percent in 1984. It is creditable that expenditure is expected to be lower than in 1983 when there was significant under-expenditure due to the vote on account and the July disturbances. This combination of increased revenue and restrained expenditure is expected to bring about significant improvement in budgetary performance. The current account is expected to move

from a deficit of 0.5 percent of GDP to a surplus of 1.9 percent of GDP. In addition the overall deficit is expected to fall from 17.8 percent of GDP in 1983 to 11.9 percent in 1984. Another notable feature is the anticipated reduction in total domestic borrowing from 7.6 percent of GDP in 1983 to 3.0 percent in 1984. This means that the budget will pre-empt a smaller share of domestic resources, thus reducing the "crowding out" of the private sector. In addition bank borrowing is expected to be only 0.5 percent of GDP. This will mean that inflationary pressures stemming from the budget will be contained. The budgetary estimates for 1984 are conservative and do not take into account the windfall increase in tea earnings as a result of India's decision to limit her exports. The Budget 1984 has set out to curb price instability and improve balance of payments viability. It has gone some way towards placing the economy on a path of sustained growth and development in the medium and long-term.

Economic management in the modern world is a continuous process. It cannot be a once and for all effort at the time the Budget is presented each year. In our interdependent world constant fine tuning is necessary and continuous adjustment is far less painful than sudden spurts of policy change designed to make up a backlog of adjustment. Fiscal policies must be supplemented by monetary, tariff and exchange rate policies that maintain the competitiveness of the economy and create an environment that is conducive to non-inflationary growth and development. Given the exposure to uncertain external forces that the country experiences, it is also important to ensure that cyclical improvements in the external account do not detract attention from the need to effect structural transformation of the economy. Increased export earnings must be used to build up the productive capacity of the economy rather than on consumption.