

BUDGET 1989

The main thrust of the Finance Minister's Budget Speech on March 16 on behalf of the new government, was focussed on the implementation of President Premadasa's "Poverty Alleviation Programme". In a departure from tradition the entire Budget Speech was completed under 60 minutes. The usual review of the economy, which comes as a preamble to the proposals was tabled as a separate document, prepared by the Central Bank of Sri Lanka titled "Economic Survey 1988". The Minister referred to a "new vision" that has "awakened the whole country to tread a new path". He emphasised that it was his "sincere endeavour to reflect this new vision and to address the aspirations of the common people through this first Budget of this Government".

A theme of the Budget Speech was "the factors that contributed to an increasing impoverishment and malnutrition among our people. As a result, the productivity of the poor has steadily

declined with a colossal waste of our precious human resources. This waste cannot be measured merely in economic terms. The frustration and discontentment in the society that we see today have arisen from this deprivation of our people and militates against social stability and peace".

The Minister emphasised that "it is to redress this imbalance in our economy that His Excellency the President has emphasised that the main thrust of the country's development programme in the next two years would be on the alleviation of poverty and the creation of village based self-reliant organisations and small production units which would help to increase the productivity of the poor through creation of new employment opportunities This marriage between the big investors and the small producers will increase production, cut down on overheads, reduce inflation and generate sustainable employment and will also be the surest way to accelerate

the development of our remote and backward areas. This is the essential philosophy behind the Janasaviya Programme".

The Finance Minister maintained that the essential elements of the "new vision" of the President were the restoration of peace, enforcement of discipline and alleviation of poverty and it was his endeavour to reflect this new vision through this Budget. But two important factors that have to be considered, (as pointed out in the following note on the Budget by Dr.S.Tilekeratne) are the deterioration in the economic situation in 1988 and the economic and social problems that have spilled over from previous years. The success of the new lead programme will no doubt be closely related to how successfully the impact of these problems are overcome. The minus factors in Sri Lanka's economic performance of 1988 clearly outway the gains, according to the Central Bank's review. The adverse circumstances confronting the economic, social and political situation in the country had led to a serious deterioration in the budgetary position, an excessive growth in money supply, an escalation of consumer price levels, and unfavourable trends in the balance of payments, with external reserves continuing to fall heavily. Also, the significant bias in the economy towards services as against production, worsening of relative income distribution in favour of the highest income earners, a rise in external indebtedness, the growth of a considerable 'black' economy and a sharp rise in defence expenditure are all factors to be contended with.

In preparation of the Draft Estimates of Expenditure and Revenue priority has been given to provision for the Poverty Alleviation Programme. Total budgeted expenditure for 1989 reaches Rs. 108,103 mn, the highest on record and nearly 30 percent more than the previous highest expenditure of Rs.82,923 mn for 1988. Of the Budgetary Expenses of Rs.108 bn, about 55 percent is earmarked for Recurrent Expenditure and the balance for Capital Expenditure.

Of the total Budgeted Expenditure as much as 44 percent, amounting to Rs.47 bn, is allocated for the Ministry of Finance. Approximately 50 percent of this (Rs.23.6 bn) is allocated for the Public Debt, covering payments and repayments on loans. The other major allocation, close to 10 percent of total ex-

TABLE 1 - ESTIMATES OF GOVERNMENT EXPENDITURE 1987 - 1989

MINISTRY	1987		1988		1989	
	EXPENDITURE (Rs. Mn.)	%	EXPENDITURE (Rs. Mn.)	%	EXPENDITURE (Rs. Mn.)	%
1 MINISTRY OF FINANCE	21,270.3	30.3	33,416.9	40.3	47,239.1	44.0
2 MINISTRY OF DEFENCE	11,519.9	16.4	9,372.7	11.3	8,917.8	8.3
3 MIN. OF PUBLIC ADMINISTRATION PROV. COUNCILS & HOME AFFAIRS	4,239.6	6.0	4,591.9	5.5	6,797.5	6.3
4 MINISTRY OF EDUCATION, CULTURAL AFFAIRS AND INFORMATION	4,558.0	6.5	4,929.3	5.9	6,359.5	5.9
5 MINISTRY OF LANDS, IRRIGATION AND MAHAWELE DEVELOPMENT	7,579.5	10.8	7,074.9	8.5	5,370.2	5.0
6 MINISTRY OF HEALTH AND WOMEN'S AFFAIRS	3,697.1	5.3	4,109.6	5.0	5,314.3	5.0
7 MINISTRY OF TRANSPORT & HIGHWAYS	3,413.1	4.9	3,261.2	3.9	5,285.4	4.9
8 MINISTRY OF POWER AND ENERGY	2,127.7	3.0	4,232.2	5.1	5,015.2	4.7
9 MINISTRY OF LABOUR AND SOCIAL WELFARE	83.4	0.1	106.6	0.1	2,928.2	2.7
10 MINISTRY OF AGRICULTURE, FOOD AND COOPERATIVES	1,465.2	2.1	1,559.8	1.9	2,716.5	2.5
11 MINISTRY OF POSTS AND TELECOMMUNICATIONS	1,755.4	2.5	1,678.5	2.0	2,338.5	2.2
12 MINISTRY OF HOUSING AND CONSTRUCTION	1,939.1	2.8	1,744.5	2.1	1,653.7	1.5
13 MINISTRY OF HIGHER EDUCATION, SCIENCE & TECHNOLOGY	1,005.5	1.4	1,076.1	1.3	1,539.7	1.4
14 MINISTRY OF POLICY PLANNING AND IMPLEMENTATION	1,251.8	1.8	1,374.6	1.7	1,301.6	1.2
15 MINISTRY OF PLANTATION INDUSTRIES	1,339.8	1.9	1,176.1	1.4	886.0	0.8
16 PRESIDENT, PRIME MINISTER, JUDGES ETC.	294.7	0.4	347.5	0.4	682.6	0.6
17 MINISTRY OF JUSTICE & PARLIAMENTARY AFFAIRS	699.3	1.0	1,018.5	1.2	662.2	0.6
18 MINISTRY OF FOREIGN AFFAIRS	455.3	0.6	481.3	0.6	537.4	0.5
19 MINISTRY OF FISHERIES AND AQUATIC RESOURCES	240.7	0.3	212.6	0.3	443.8	0.4
20 MINISTRY OF YOUTH AFFAIRS AND SPORTS	561.8	0.8	224.3	0.3	315.2	0.3
21 MINISTRY OF TRADE AND SHIPPING	149.2	0.2	374.2	0.5	287.3	0.3
22 MINISTRY OF TEXTILE AND RURAL INDUSTRIES DEVELOPMENT	105.3	0.2	130.1	0.2	250.9	0.2
23 MINISTRY OF INDUSTRIES	98.8	0.1	142.9	0.2	225.0	0.2
24 MINISTRY OF TOURISM	223.0	0.3	247.7	0.3	153.7	0.1
25 MINISTRY OF BUDDHA SASANA	10.2	0.0	11.9	0.0	26.2	0.0
TOTAL EXPENDITURE	70,083.5	100.0	82,895.8	100.0	107,250.5	100.0

penditure, is Rs.10,000 mn for the Poverty Alleviation and Nutrition Programme; and Rs.8,500 mn for Financial Assistance and Special Treasury Services and Expenses. In addition there is an allocation of Rs.4,600 mn for Rehabilitation and Reconstruction.

The next highest vote, of Rs.8.9 bn, is for the Ministry of Defence. The percentage of total expenditure for Defence has come down to 8.3 percent in 1989 as compared with 11.5 percent in 1988 and 16.8 percent in 1987. These two lead Ministries are followed by the Ministry of Public Administration, Provincial Councils and Home Affairs 6.3 percent; and Ministry of Education, Cultural Affairs and Information 5.9 percent. In fifth position is Lands, Irrigation and Mahaweli Development with 5.0 percent; though this Ministry was earlier in third position, taking up 8.7 percent of total expenditure in 1988 and 11 percent in 1987.

The other 5 main Ministries, where allocations exceeded Rs. 2 bn and were over 2 percent of total expenditure, were Health and Women's Affairs 5.0 percent; Transport and Highways 4.9 percent; Power and Energy 4.7 percent; Labour and Social Welfare 2.7 percent; Agriculture, Food and Co-operatives 2.5 percent; and Posts and Telecommunica-

cils and Home Affairs; Education, Cultural Affairs and Information; Health and Women's Affairs; and Labour and Social Services. The 2 Ministries of Finance; and Posts and Telecommunications have an almost equal share for both Capital and Recurrent Expenditure. (See Table 1 for details).

Of total Current Expenditure of nearly Rs.58 bn, almost half will be for salaries, wages, goods and services; while interest payments will take up about 30 percent. The balance will be mainly for transfer to public corporations and to households and for pensions.

Revenue from existing taxes and levies amounts to Rs. 52 bn and is expected to cover almost half the total expenditure. The main item in the Rs. 52 bn Government Estimates of Revenue is Rs. 38.6 bn from Taxes on Production and Expenditure as against Rs.32.8 bn expected in 1988. (See Table 2).

The balance Revenue or resource requirements of the Budget was around Rs. 44. bn and was expected to be filled through Foreign Aid 54 percent and Domestic Borrowings 46 percent.

The final budgetary out turn shows an Overall Deficit of Rs. 53 bn in 1989, as against Rs. 36 bn in 1988.

Recurrent Expenditure had increased 42 percent, from Rs.40.7 bn in 1988 to Rs.57.9 bn in 1989; while Capital Ex-

tions 2.2 percent. Together these 10 Ministries account for nearly 90 percent of total expenditure for 1989. Among these 10 Ministries Capital Expenditure was high among the 3 Ministries of Lands, Irrigation and Mahaweli Development; Power and Energy; and Transport and Highways. Recurrent Expenditure was high for the 5 Ministries of Defence, Public Administration, Provincial Coun-

TABLE 2 - ESTIMATES OF GOVERNMENT REVENUE 1988 AND 1989

Heads 1-12	Financial Year 1988 (Revised Estimates)	Financial Year 1989 (Original Estimates)
	Rs.	Rs.
Taxes on Production and Expenditure	32,838,810,000	38,579,740,000
Taxes on Corporate Income	3,120,000,000	3,175,000,000
Taxes from Non-Corporate Income	1,510,000,000	1,552,000,000
Receipts of Trading Enterprises	2,846,600,000	2,810,000,000
Rents, Interests, Profits and Dividends received	2,244,397,000	1,760,000,000
Sales and Security Charges	924,854,000	1,100,000,000
Social Security Contributions	177,500,000	350,000,000
Other Current Transfers	1,803,259,000	2,035,060,000
Sales of Capital Goods	50,000,000	20,000,000
Capital Transfers from Domestic Sector	1,296,580,000	67,000,000
Capital Transfers from Abroad	---	---
Repayment of Loans and Advances	463,000,000	551,200,000
Total Revenue	47,275,000,000	52,000,000,000

TABLE 3-THE FINAL BUDGETARY OUT-TURN

	1988 (Rs. Mn)	1989 (Rs. Mn)	Percentage Change
Recurrent Expenditure	-40,716	-57,891	+ 42.18
Revenue	+ 49,260	+ 52,000	+ 5.56
Current Account Surplus/Deficit	+ 8,544	- 5,891	- 68.94
Capital Expenditure	-44,620	-46,724	+ 4.72
Overall Budget Deficit	-36,176	-53,015	+ 46.55
Financing the Deficit			
Budget Revenue Proposals (Net)	1,910	7,020	+ 267.53
Foreign Aid-Loans	17,600	18,000	+ 2.27
Foreign Aid-Outright Grants	5,000	5,600	+ 12.00
Domestic Borrowings - (Non-Inflationary)	11,000	17,000	+ 54.55
Domestic Borrowings -Banking	2,576	3,339	+ 29.62

Source: *Budget Speeches November 1987 and March 1989*

penditure has increased by 5 percent, from Rs.44.6 bn in 1988 to Rs.46.7 bn in 1989.

Revenue from existing sources (as given in the Govt. Estimates) shows a 5.6 percent increase in 1989. The Current Account Revenue less Current Expenditure Advance Accounts shows a drop of 69 percent, from plus Rs.8.5 bn in 1988 to minus Rs.5.9 bn in 1989. Meanwhile, the overall Budget Deficit in 1989 is 46.6 percent more than in 1988.

In financing of the Budget Deficit, the comparative position for these two years shows that the largest increase of 54.6 percent is in Domestic Borrowings from non-inflationary sources; while Domestic Borrowings from banking sources shows a 29.6 percent increase.

In the final budgetary position of these two years Foreign Aid-Loans shows a 2.3 percent increase; and Foreign Aid-Grants a 12 percent increase (See Table 3).

A summary of Government Fiscal Operations for 1979-1988, as given in the Central Bank Review of the Economy, 1987 (Table 88) shows the following position upto 1988. (See Table 4).

The Government's budgetary performance and fiscal operations in 1988 are very relevant to how expenditure and revenue expectations can be realised in 1989. The following brief review by the Central Bank shows where the major shortfalls occurred and also clearly indicates the trends in fiscal operations.

GOVERNMENT FINANCE IN 1988

Fiscal Trends

The revised 1988 estimates of government revenue and expenditure reveal a current account deficit of Rs.4,819 million and an overall deficit (before grants) of Rs.34,553 million in 1988. In the previous year, the current account of the budget was in surplus to the extent of Rs.2,585 million, although the overall budget was in deficit of Rs.21,749 million.

The deterioration in the fiscal position during 1988 was the outcome of several factors. First, government revenue showed only a marginal increase due to the unsettled conditions which resulted in a lower collection from a number of revenue sources. Second, there were increased commitments on account of several items of current expenditure such as salaries and wages, the Food Stamps Scheme and drought relief programs. Third, advance account operations. Fourth, large numbers of supplementary capital expenditure programs were permitted for on-going development activities. As a result of these developments, government revenue/GDP ratio declined from 21.4 percent in 1987 to 19 percent in 1988, while total expenditure and lending rose from 32.5 percent to 34.1 percent, leading to an increase of the budget deficit from 11 percent of GDP to 15 percent.

Revenue

According to revised estimates, government revenue in 1988 totalled Rs. 43,338 million. This was an increase of 3 percent over the previous year's revenue of Rs.42,145 million. Total revenue of the government consisted of Rs. 37,266 million of tax revenue (86 percent) and Rs.6,072 million of non tax revenue (14 percent). While tax revenue reflected an increase of 6 percent, non tax revenue registered a decline of 14 percent over the amounts received in the previous year.

Despite the unsettled conditions in the country, revenue collection from turnover taxes rose by 16 percent mainly due to higher prices and revisions in excise duties on tobacco, the revenue collection from this source showed a decline of 19 percent due to the shortfall in the volume of sales resulting from both labour disputes and unsettled conditions

TABLE 4. SUMMARY OF BUDGETARY POSITION 1979-1989

(Rs. million)

Year	Revenue	Expenditure	Budget Deficit	Financing the Deficit			
				Bank Borrowing	Non Bank Borrowing	Foreign Loans	Foreign Grants
1979	12,730	21,521	8,791	680	3,902	2,847	1,390
1980	14,068	30,343	16,274	7,126	2,485	4,116	2,620
1981	16,228	31,094	14,866	3,917	2,779	5,487	2,721
1982	17,809	37,900	20,091	4,006	7,606	5,418	3,376
1983	25,210	46,815	21,606	1,204	10,146	7,478	3,473
1984	37,731	53,592	15,861	2,644	6,589	7,958	3,293
1985	39,010	64,685	25,676	7,451	8,520	8,898	3,307
1986	41,644	69,715	28,071	2,299	9,178	12,081	3,753
1987 Approved Estimates	44,115	70,300	26,185	3,470	7,500	11,120	4,095
1988 Approved Estimates	49,260	85,436	36,176	2,576	11,000	17,600	5,000
1989 Budget Estimates	52,000	105,015	53,015	3,339	17,000	18,000	5,600

in the country. However, revenue collection from excise duties on liquor at Rs. 1,800 million reflected an increase of 9 percent mainly due to the upward revision in duty rates.

Despite a substantial increase in the value of imports, revenue from import duties at Rs.12,000 million registered only an increase of 9 percent. This was mainly due to the downward revisions in duties on selected items such as motor vehicles, liquor, tobacco and wheat flour and the exemption of essential consumer items such as rice from import duties.

Revenue collection from export duty on rubber continued to improve due to favourable price developments. However, revenue from export duty on tea declined by 29 percent owing to a reduction in export duty on tea. Owing to a decline in the value of coconut exports, revenue collection from export duty on coconut declined to Rs.65 million in 1988 from Rs. 148 million in 1987.

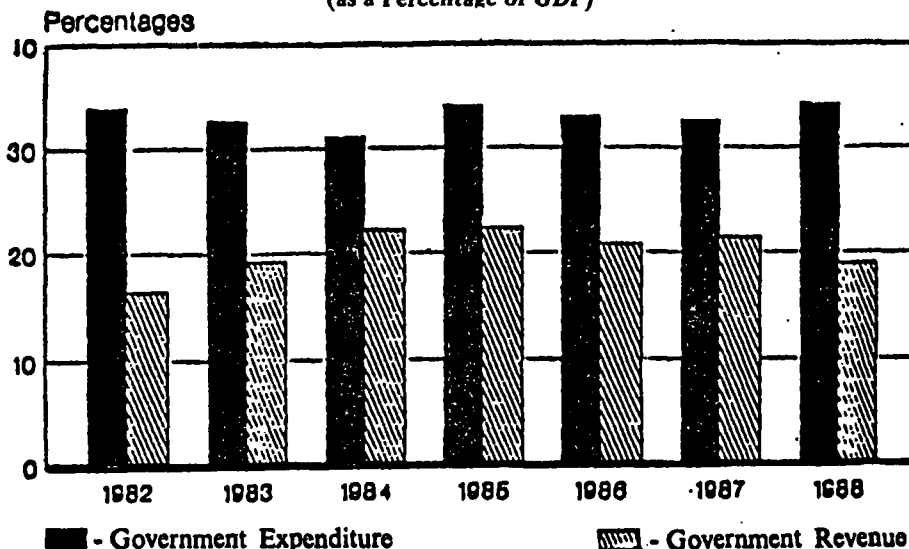
Meanwhile, estimated revenue from income taxes at Rs.4,825 million recorded a marginal decline of 2 percent, largely due to a reduction in personal income taxes. Taxes on property transactions at Rs.1,693 million showed a growth of 8 percent mainly due to increased stamp duties on Letters of Credit. Central Bank profits, interest income and surplus of the Department of Telecommunications continued to be the largest sources of non-tax revenue of the government.

Expenditure

According to the latest available data, total expenditure in 1988 amounted to Rs.77,891 million. This represented a 22 percent increase over the expenditure in the previous year. The expenditure in 1988 consisted of Rs.48,157 of current expenditure and Rs.29,734 million of capital expenditure and net lending.

Current expenditure at Rs.48,157 million accounted for three-fifths of total expenditure in 1988. Total salaries and wages at Rs.10,671 million was an increase of 33 percent over the salaries and wages bill of the previous year. The substantial increase in salaries and wages was entirely due to the salary revisions effected in 1988. The expenditure on other goods and services at Rs.11,779 million was an increase of 13 percent,

GOVERNMENT REVENUE AND EXPENDITURE (as a Percentage of GDP)



and this was largely due to enhanced expenditure on defence and security related activities.

Interest payments on government debt in 1988 amounted to Rs.12,412 million. This was an increase of 22 percent over the previous year's payments of Rs. 10,157 million. Interest payments on domestic debt rose by 24 percent owing to both a rise in outstanding liabilities, as well as an upward movement in interest rates, particularly on Treasury bills. Meanwhile, interest payments on foreign debt rose by 16 percent owing to servicing of an enhanced quantum of outstanding debt, reinforced by exchange rate variations.

Total transfer payments in 1988 at Rs. 14,515 million was an increase of 33 percent. The substantial increase in

transfer payments was due to the additional outlays on pensions, the food stamp scheme and drought relief and enhanced current transfers to public enterprises.

Capital expenditure and lending at Rs. 29,734 million was 22 percent higher than the amount utilised in the previous year. Despite a substantial under-utilization of rehabilitation expenditure, capital expenditure and lending during 1988 showed considerable growth owing to additional supplementary expenditure provided under various development programs such as Air Port development, Telecommunications and Electricity. The Mahaweli Development Scheme, Development of Air Port and Aviation services, Water Supply and Drainage Scheme, Road Development, Power and Energy and Land Development and Telecommunications continued to be the major capital expenditure programs of the government.

Financing of the Budget Deficit

The revised estimates for 1988 reveal a budget deficit (after grants) of Rs. 28,478 million, as against a deficit of Rs.17,072 million in the previous year. In financing the deficit, a sum of Rs. 7,319 million was obtained from foreign sources, while Rs.21,159 million was utilized from domestic sources.

The net foreign borrowings of Rs. 7,319 million, which reflected an increase of 28 percent over the preceding year, financed 26 percent of the budget deficit. The original budget estimates for 1988 anticipated the utilization of Rs.12,520 million of foreign financing.

Summary of Government Fiscal Operations (Economic Classification)

Item	Rs. Million	
	1987	1988 Estimates
1. Total Revenue & Grants	46,822	49,413
2. Total Revenue	42,145	43,338
2.1 Tax Revenue	35,119	37,266
2.2 Non Tax Revenue	7,026	6,072
3. Grants	4,677	6,075
4. Expenditure & Lending Minus Repayment	63,894	77,891
4.1 Current	39,560	48,157
4.2 Capital	22,816	23,123
4.3 Lending - Repayment	1,518	6,611
5. Current Account Surplus/Deficit (-)	2,518	-4,819
6. Budget Deficit (Before Grants)	-21,749	-34,553
7. Budget Deficit (After Grants)	-17,072	-28,478
8. Financing	17,072	28,478
8.1 Foreign Borrowing	5,716	7,319
8.2 Domestic Borrowing	11,356	21,159
8.2.1 Non-Market	1,415	0
8.2.2 Market	9,941	21,159
8.2.2.1 Non-Bank	6,400	10,163
8.2.2.2 Bank	3,541	10,996

Sources: General Treasury, Central Bank of Sri Lanka

Accordingly, the actual utilization of foreign financing in 1988 was lower by 42 percent. This was largely due to a substantial under expenditure on account of rehabilitation expenditure in 1988.

The financing from domestic sources consisted of Rs.10,163 million from non-bank sources and Rs.10,996 million from banking sources. Despite an increased quantum of repayments during this year, net resource mobilization from non-bank sources through rupee securities remained at Rs.6,163 million, slightly lower than that in the previous year. Through the popularization of Treasury bills, a further sum of Rs.2,601 million was mobilized from non-bank sources in 1988.

Resources available from foreign and domestic non-bank sources financed a total sum of Rs.17,482 million, out of an overall deficit of Rs.28,478 million. In financing this resource gap, a sum of Rs.11,249 million was obtained from banking sources through the issue of Treasury bills, while a further sum of Rs.926 million was obtained from the Central Bank under provisional advances. However, due to a cash build up of Rs.1,179 million, the net bank financing of the budget deficit was restricted to Rs.10,996 million. The latter none-the-less represented a three-fold increase over the amount borrowed from the banking system in the previous year.

Government Debt

The outstanding government debt as at the end of 1988 was Rs.223,503 million. This was an increase of 15 percent over the debt outstanding amounting to Rs.191,634 million at the end of the previous year. Domestic debt rose by 25 percent to Rs.98,594 million, while foreign debt increased by 11 percent to Rs.124,909 million.

