

## SAVINGS, INVESTMENTS AND THE BUDGET

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Low level of savings has been a major constraint to economic growth in Sri Lanka as in the case of many other developing countries. National savings as a ratio of Gross Domestic Product (GDP) in Sri Lanka was only about 14 per cent during the period 1978-86. Unless national savings are supplemented by foreign savings in the form of foreign loans and grants, the domestic investment will also remain at a low level and will restrain growth. Therefore, a consensus effort has been made in the successive Budgets in the past decade to push up domestic investment by means of absorbing foreign savings through the current account deficit of the balance of payments. Thus, the domestic savings gap has been filled by foreign resources and the gross domestic investment as a ratio of GDP was maintained around 24 per cent as against a savings rate of 14 per cent during 1978-86.

Continuing the recent trend, the Budget for 1988 indicates a further increase in savings arising from government fiscal operations. Government savings (or dis-savings) are equivalent to the Current Account surplus (or deficit) of the Budget. The Current Account surplus (or deficit) can be defined as the difference between the total government revenue and recurrent expenditure adjusted for under expenditure. The current account surplus for 1988 is estimated at Rs8.5 billion as shown in the following budgetary outturn; this is equivalent to about 3.8 per cent of GDP. These savings are sufficient to finance about one fifth of the capital expenditure in 1988. The balance sum of capital expenditure is expected to be provided through foreign aid and domestic borrowings.

It is important to note here that government savings have increased

considerably since 1983. This was largely an outcome of the demand management policies adopted during this period. The Public Investment Programme envisages that government savings will remain around Rs. 7 billion per year during 1989-91.

The investment outlays presented in the Budget are closely tied up with the development projects identified in the Public Investment Programme, 1987-91. This Programme envisages that the total public investment during the period 1987-91 will be about Rs.154,156 billion. Of this amount, about Rs.151,376 million will be provided through budgetary provisions. The capital expenditure is allocated to various projects in the sectors of agriculture, industries, human settlements and economic and social infrastructure. The present Budget has allocated financial resources to these projects for the fiscal year 1988.

Within the broad framework of macroeconomic strategy, the recent budgetary policies are based on the Medium Term Policy Framework introduced in last year's Budget Speech. This Framework was initially meant for the period 1987-89. The recent Budget Speech has drawn up a Framework on the same lines for 1988-90.

### GOVERNMENT SAVINGS (CURRENT ACCOUNT SURPLUS) 1978-88

	(RS'MILLION)	PERCENTAGE OF GDP
1978	- 551	-1.3
1981	+ 200	+0.3
1980	-2421	-3.6
1981	-1493	-1.8
1982	-1422	-1.4
1983	+ 128	+0.1
1984	+5889	+3.8
1985	+4854	+3.0
1986	+7042	+3.9
1987	+5954	+3.0
1988	+4544	+3.8

Sources: Central Bank of Sri Lanka, Annual Review 1986 Budget Speech, 1988

The basic objective of this Framework is to stabilise the economy mainly by means of reducing the deficits in the Budget and the balance of payments. For this purpose targets have been set for government revenue, expenditure and current account deficit of the balance of payments. It is expected that these policies help to enhance domestic savings and investment and thereby contribute to economic growth.

Under the Policy Framework announced in the recent Budget, the government savings are to be maintained at a reasonable level in the next three years by curtailing current expenditure. This will be achieved mainly by adopting measures such as cutting waste, reducing overstaffing, avoiding unnecessary activities and elimi-

### BUDGETARY OUTTURN FOR 1988 (RS.MILLION)

Recurrent Expenditure	-41,760	
Less: Savings 2.5%	+ 1,044	-40,716
Revenue		+49,260
Current Account Surplus		+ 8,544
Capital Expenditure		-44,620
Net Lending on Advance Accounts		- 100
Overall Budget Deficit		-36,176
Financing of Budget Deficit		+36,176
1. Foreign Outright Grants		5,000
2. Foreign Project & Commodity Loans		17,600
3. Domestic non-bank Borrowing		11,000
4. Domestic Bank Borrowing		2,576

Source: Budget Speech, 1988.

nating unproductive subsidies. As part of this broad programme, a major reform in the Public Service is also to be implemented shortly in order to improve its efficiency and productivity. A reduction in the government capital expenditure to more manageable level is also expected for the next three years. The large public investment programme launched in the recent past to improve the infrastructure will taper off in the future years. However, a considerable amount of resources will have to be provided for defence and rehabilitation purposes in the near future on account of the civil disturbances in the Northern and Eastern provinces. The constraints the ability to restrict the government expenditure to a certain extent.

It is anticipated that the present budgetary policies will help to avoid pre-emption of domestic savings available to the private sector. It has been observed in many countries that growing budget deficits arising from huge government expenditure lead to absorb a large proportion of bank lendings to the public sector and thus, pre-empts resources from the private sector. Also, government borrowings from the banking sector is inflationary. These repercussions are found to be unfavourable to savings and investment activities in the private sector. In view of these considerations, it is planned to reduce the budget deficit gradually under the Medium Term Policy Framework. Accordingly, the budget deficit (excluding grants) is expected to be reduced from 12 per cent of GDP in 1987 to about 9 per cent by 1990. When grants are taken into account the budget deficit is to be reduced from 9.5 per cent in 1987 to 7 per cent in 1990.

This improved budgetary performance is expected to be achieved mainly by means of government expenditure controls. In terms of the Policy Framework, the government expenditure is targetted to fall from 33 per cent of GDP in 1987 to 29 per cent by 1990. However, the govern-

ment revenue is expected to be around 20 per cent of GDP throughout this period.

In the background of these policy measures, it is envisaged in the Budget Speech that the private sector will take an active lead in the economic growth process by mobilizing more savings and effecting higher investments. The role of the private sector in these activities will be facilitated by a carefully planned privatization programme and improvements in money and capital markets.

These measures are expected to ease the pressures on the budget in the promotion of domestic investment. The level of domestic investment is projected to rise from Rs.45 billion in 1987 to Rs.68 billion in 1991 in terms of the latest Public Investment Programme. An increasing proportion of this total investment is to be borne by the private sector during this projected period. The present share of the private sector in domestic investment is about 38 per cent and the balance 62 per cent is financed by the public sector. It is envisaged that the private sector would bear about one half of the domestic investment by 1991 thus reducing the burden on the public sector. Domestic investment will be about 21 per cent of GDP in 1991 as against a savings rate of 18 per cent. The resulting domestic savings-investment gap to be financed by foreign resources will decline from the present level of 8 per cent of GDP to a mere 3 per cent in 1991. The rate of economic growth is expected to recover from about 3 per cent in 1987 to about 5 per annum in 1988-91.

The theme of these macroeconomic targets is to sustain a higher growth momentum while maintaining stability. This is to be achieved through an increased mobilization of domestic savings and a carefully designed expansion of the private sector in investment activities. A firm commitment to achieve these objectives is reflected in the present Budget.