

8. FISCAL POLICY AND BUDGETARY OPERATIONS

8.1 Overview and Policy Strategy

The objective of the fiscal strategy is to move to a sustainable budget deficit reduction path within a medium-term fiscal consolidation framework to provide the basis for private sector led non-inflationary economic growth with external viability. The fiscal reform programme includes broadening the tax base, improving tax administration and compliance, rationalizing fiscal incentives, closing of tax loopholes, reforming public enterprises, simplifying the import tariff structure and reducing tariff protection. The 1996 Budget anticipated further progress in fiscal policy reforms and a reduction in the budget deficit to 6.6 per cent of GDP (7.8 before grants). The deficit was expected to be financed through non-bank sources. Significant progress was made on the fiscal policy front in 1996. The realised overall fiscal deficit of 7.8 per cent of GDP (8.9 per cent before grants) was lower than in 1995, but fell short of the 1996 budgetary expectation due to a sharp rise in defence expenditure, a steep increase in international wheat prices adding to the cost of the wheat flour subsidy, a shortfall in privatization proceeds and the adverse effects of the prolonged drought and the power cuts on government revenue. Resource constraints on the domestic front and delays in project implementation, particularly in the areas of energy, road, telecommunication and water supply, reduced the inflow of foreign resources for budgetary purposes. The appreciation of the rupee against the yen by 7 per cent also reduced the domestic currency value of yen proceeds. Hence 82 per cent of the deficit was financed through domestic borrowings, including 21 per cent through bank financing. Meanwhile, the 1997 Budget re-emphasized the need for urgent fiscal consolidation and has set a medium-term budget deficit target of 3.5 per cent of GDP (4.5 per cent of GDP before grants) for 1999, with a target of 6.1 per cent of GDP (7.3 per cent of GDP before grants) for 1997.

The tax policy reforms focussed upon improving revenue buoyancy by reducing distortions, broadening the tax base with lower tax rates applied according to the 'ability to pay' principle and minimizing tax reliefs and preferences. In 1996, the threshold for income taxes was raised, the rate bands widened and intermediate tax rates were lowered. Further, modifications were made in income taxation in the areas of employment credit, qualifying payments, computing assessable income, terminal benefits and surcharges on income tax to remove distortions and make the tax system more transparent.

Several tax measures were introduced to invigorate the capital market. These included extension of the tax holiday granted to Unit Trusts by two more years to provide for a wider participation in the capital market, removal of stamp duty on bonds and other debt securities of quoted public companies which are funded through the stock exchange and exemption of share brokers' fee and share transactions of investment companies and Unit Trusts from turnover tax in order to reduce the costs of transactions. Reforms were announced to harmonise various tax incentive schemes offered by the Department of Inland Revenue and the Board of Investment. Tax holidays, duty free import facilities and turnover tax exemptions on project specific imports were offered to companies in the manufacturing and service sectors. The defence levy, which was re-named as the National Security Levy, was reduced to 0.5 per cent from the initial level of 4.5 per cent for imports of capital goods to encourage the use of advanced technology.

Tariff and customs reforms were introduced to rectify the anomalies that arose when import tariffs were brought under a three rates band structure of 10, 20 and 35 per cent, ensuring uniformity for various sectors. Concessions were granted to raise productivity in agriculture and fisheries, to protect the environment and to promote the dissemination of knowledge. Import duties were reduced within the three rate band structure for goods such as agricultural tools and equipment, fishing nets, raw materials, intermediate goods and books and magazines. Excise taxes were rationalised by confining excise taxation to exciseables such as liquor, cigarettes, petrol, diesel and few luxury consumer goods. The excise tax on beer was reduced substantially to discourage the consumption of harmful alcohol and to promote investment in the industry which has an export potential.

Stamp duties were rationalised by introducing a value based sliding scale system as a revenue enhancing measure. Passport and visa fees were increased to cover administrative costs. A new tax named Save the Nation Contribution was imposed on personal emoluments over Rs.15,000 per month. A levy was imposed on Sri Lanka Telecom with a view to passing the turnover tax to the users of the facility.

On the expenditure side, an interim allowance was granted to government employees who had not received

wage increases during the salary revisions introduced in the previous year. Furthermore, a 10 per cent cut was imposed on both non-wage operational expenditures of the Government and low priority rupee funded capital projects. The Government issued long-term bonds to the two State Banks and the National Savings Bank as a temporary measure on account of the commitments made in the form of state directed credit in previous years outside the Budget, with the objective of regularising these liabilities and strengthening fiscal discipline, financial control and accountability.

In order to arrest the deterioration of the fiscal position in the wake of unexpected developments such as the increase in international wheat prices, escalation of defence expenditures and possible revenue shortfall due to the drought and the power cuts, the Government implemented several new revenue measures. Accordingly, the excise tax on cigarettes and hard liquor was raised and non-priority expenditures were pruned. A courageous decision to raise the administered price of wheat flour considerably was made during 1996, which raised the price of wheat flour by 42 per cent. While this corrective price adjustment in wheat flour has almost eliminated a major distortion, there should be a mechanism to ensure flexible free market pricing of wheat flour so that any possibility of a subsidy element re-emerging in the future is completely avoided.

In order to impose stricter fiscal discipline the Government did not raise the Rs.125,000 million limit on the outstanding level of Treasury bills, although there was a need for additional domestic financing.

8.2 Budget Out-turn

With the corrective measures introduced during the year, the overall fiscal deficit was contained at 8.9 per cent of GDP, thus falling short of expectations in the original Budget for 1996 by 1.1 per cent of GDP.

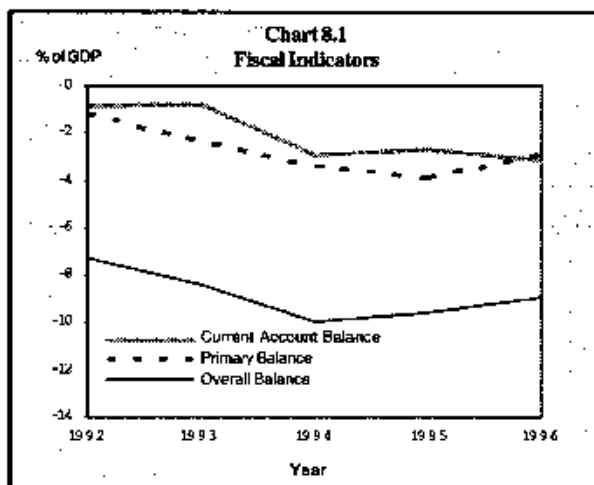
The total revenue collection declined from 20.4 per cent of GDP in 1995, to 19.0 per cent of GDP in 1996, owing to a relatively lower level of taxable imports, a decline in the average rate of import duty due to various tax relief measures and exemptions granted and a decrease in non-tax revenue collections.

The impact of the new measures, such as the upward revision of excise taxes, was partly offset by the marked decline in economic activities during the year. Despite the increases in defence expenditure, wheat flour subsidy, expenditure relating to refugees and the interest cost on domestic debt, the measures taken to curtail waste-

ful expenditure were effective in containing the recurrent expenditure at around 22.2 per cent of GDP, compared with 23.1 per cent in the previous year. The current account of the Budget was in deficit at 3.2 per cent of GDP.

Public investment, expected to be at 7.5 per cent of GDP in the 1996 Budget, dropped to 5.3 per cent of GDP, reflecting the underutilisation of foreign resources, mainly in the telecommunication and energy sectors. Net lending, which was expected to show an inflow of 0.6 per cent of GDP, turned out to be an outflow of 0.5 per cent of GDP due to slow progress in the privatisation programme. These indicate that the containment of the budget deficit was achieved partly by a reduction in public investment. This may not be a desirable feature considering the state of infrastructure development in the country. A low level of public investment will jeopardize the medium and long-term development efforts in the economy as the majority of these public investments were meant for the development and maintenance of the infrastructure of the economy.

Recent fiscal sector developments indicate that a heavy fiscal burden has emerged as a result of the rapidly rising interest cost on a high volume of public debt, public sector salaries and transfers to households in addition to rising defence expenditure. Although the overall budget deficit was 8.9 per cent of GDP in 1996, the primary deficit was only 2.9 per cent of GDP while the deficit excluding defence was 3.2 per cent of GDP. This indicates that there are structural weaknesses in the Budget which need to be corrected through a programme aimed at eliminating these structural weaknesses.



The use of foreign loans in financing the budget deficit decreased from 3.2 per cent of GDP in 1995 to 1.4 per cent of GDP in 1996, while the utilisation of domestic resources, on a net basis, increased from 5.1 per cent of

GDP in 1995 to 6.4 per cent of GDP in 1996. It is important to note that, though the Government expected a zero level of bank financing in the 1996 Budget, ultimately, borrowings from the banking sector amounted to Rs.12,344 million in 1996. As a ratio of GDP, bank financing increased from 1.1 per cent in 1995 to 1.6 per cent in 1996. The Central Bank financed part of the budget deficit through the revolving credit facility extended under provisional advances and an increased volume of Treasury bill holdings through open market operations. Government resource mobilisation from non-bank sources by issuing debt instruments was almost entirely limited to Rupee loans and Treasury bills. The funds collected through the Rupee Loan Programme amounted to Rs.46,716 million, out of which 81 per cent was from the Employees' Provident Fund and 12 per cent was from the National Savings Bank. With the net new issues of Treasury bills amounting to Rs.11,225 million by October 1996, the outstanding Treasury bill level reached its approved limit of Rs.125 billion. As the Treasury bill limit was not revised upward and there were no other government debt instruments available for mobilising short-term liquidity in the market, the Government resorted to borrowing from government institutions, statutory funds and other sources. Such borrowings amounted to Rs.10,363 million in 1996.

8.3 Revenue and Grants

The total revenue in 1996 at Rs.146,279 million registered a growth of 7 per cent in comparison to 24 per cent recorded in 1995. Tax revenue at Rs.130,202 million recorded an increase of 10 per cent. While the share of tax revenue in total revenue rose from 87 per cent in 1995 to 89 per cent in 1996. As a proportion of GDP, it declined from 17.8 per cent to 16.9 per cent over the same period. The reduction of revenue collection from turnover tax on imports and manufactured goods, excise tax on liquor and tax on excise (Special Provision Act) contributed to the slow growth in tax collection in 1996. Revenue collection from non-tax sources recorded a sharp decrease of 9 per cent in 1996 compared to the collection in 1995. This was owing to a substantial reduction in property income and dividends from the banking sector. Total foreign grants utilised for budgetary purposes were lower by 6 per cent in 1996.

Tax Revenue

Reflecting the tax relief granted to certain commodities during 1996, the share of taxes on goods and services, consisting of turnover taxes, defence levy and excise taxes, declined marginally to 59 per cent of total tax revenue from 60 per cent in 1995. The revenue from

these taxes recorded a slow growth of 9 per cent in comparison to a growth of 25 per cent observed in the previous year.

Revenue from the defence levy, which was imposed on all goods and services other than on exports, generated Rs.16,441 million and recorded a growth of 14 per cent in 1996, compared with 49 per cent in 1995. Revenue from this source accounted for 13 per cent of total tax revenue in 1996. Though there was a full year impact of the increase in, the defence levy (from 3.5 per cent to 4.5 per cent effected in June 1995) on the revenue collection in 1996, the slowing down of the growth in the import sector, the reduction of the defence levy from 4.5 per cent to 2.0 per cent in respect of imports of capital goods and the revision of the tax structure on cigarettes were mainly responsible for this deceleration.

Turnover taxes at Rs.37,631 million increased marginally by 3 per cent compared to an increase of 13 per cent in the previous year. Further, the share of revenue from turnover taxes in total tax income declined from 31 per cent in 1995 to 29 per cent in 1996. The slower growth in turnover taxes was owing to the decline in turnover tax collection on manufacturing activities by 10 per cent and on imports by 2 per cent. The reduction of growth in imports, together with turnover tax exemptions introduced during the year, caused the decline in turnover tax on imports. The reduction of the tax base on cigarettes due to the new tax revision introduced in the 1996 Budget, power shortages and labour unrest which hampered the level of output in the manufacturing sector and the exemption of petroleum products such as diesel and kerosene from turnover tax could be identified as the main causes for the reduction in turnover tax collections from the manufacturing sector in 1996. However, turnover taxes on non-manufacturing activities showed a significant increase of 37 per cent compared to an increase of 10 per cent observed in the previous year. The rapid expansion of service sector activities such as banking and financial services, telecommunication, ports, air travel and insurance contributed to the substantial increase in turnover tax collection. Meanwhile, the turnover tax rate bands of 6 per cent and 10 per cent were revised upward to 7 per cent and 11 per cent, respectively, in November 1996 in order to facilitate a smooth transformation to the GST system with a single moderate rate.

Revenue from excise taxes at Rs.22,067 million in 1996, recorded an increase of 14 per cent compared to a growth of 33 per cent registered in the previous year. The overall increase in revenue from this source was generated entirely by a significant growth in the excise tax on cigarettes, while the excise tax on liquor and commodities

TABLE 8.1
Summary of Government Fiscal Operations

Rs Million

Item	1992	1993	1994	1995	1996 Approved Estimates	1996 Provisional	1997 Approved Estimates
Total Revenue and Grants	94,061	106,364	118,295	145,286	157,207	154,779	180,044
Total Revenue	85,781	98,339	110,038	136,258	148,207	146,270	170,736
Tax Revenue	76,353	85,891	99,417	118,543	132,645	130,202	151,451
Non Tax Revenue	9,428	12,448	10,621	17,715	15,562	16,077	19,285
Grants	8,280	8,025	8,257	9,028	9,000	8,500	10,208
Expenditure and Lending minus Repayments	118,974	140,460	167,768	200,482	208,485	214,710	235,570
Current	89,639	102,288	127,084	154,159	169,781	170,629	177,930
Capital	24,949	33,662	30,391	41,722	40,203	40,034	47,879
Lending minus Repayment	2,386	4,510	10,293	4,601	-4,499	4,047	9,761
Current Account Surplus/Deficit(-)	-3,858	-3,943	-17,046	-17,901	-21,574	-24,351	-7,194
Budget Deficit (after grants)	-22,913	-34,096	-49,473	-55,196	-51,278	-59,932	-54,626
Financing	22,913	34,096	49,473	55,196	51,278	59,932	54,626
Foreign Borrowing	7,361	9,855	11,778	21,224	19,078	18,911	14,184
Domestic Borrowings	15,552	24,241	37,696	33,972	32,201	40,020	40,432
Market Borrowings	18,757	22,229	38,362	33,424	32,201	38,057	40,432
Non bank	21,079	28,308	37,205	26,359	32,201	26,313	40,432
Bank	-2,322	-6,079	1,157	7,065	-	12,344	-
Monetary Authority	-1,901	-13,857	1,764	7,662	-	9,873	-
Commercial Bank	-421	7,578	-607	-597	-	2,471	-
Other Borrowings	-3,205	2,012	-666	548	-	10,363	-
Memorandum Item: Budget Deficit (before grants)	-31,193	-42,121	-57,730	-64,224	-60,278	-69,432	-64,834

As a percentage of GDP

Total Revenue and Grants	22.1	21.3	20.4	21.8	20.3	20.1	20.3
Total Revenue	20.2	19.7	19.0	20.4	19.1	19.0	19.1
Tax Revenue	17.9	17.2	17.2	17.8	17.1	16.9	17.0
Non Tax Revenue	2.2	2.5	1.8	2.7	2.0	2.1	2.2
Grants	1.9	1.6	1.4	1.4	1.2	1.1	1.1
Expenditure and Lending minus Repayments	27.5	28.1	29.0	30.0	26.9	27.9	28.4
Current	21.1	20.5	21.9	23.1	21.9	22.2	19.9
Capital	5.9	6.7	5.2	6.2	5.6	5.2	5.4
Lending minus Repayments	0.5	0.9	1.8	0.7	-0.6	0.5	1.1
Current Account Surplus/Deficit(-)	-0.9	-0.8	-2.9	-2.7	-2.8	-3.2	-0.8
Budget Deficit (after grants)	-5.4	-6.8	-8.5	-8.3	-6.6	-7.8	-6.1
Financing	5.4	6.8	8.5	8.3	6.6	7.8	6.1
Foreign Borrowing	1.7	2.0	2.0	3.2	2.5	1.4	1.6
Domestic Borrowings	3.7	4.9	6.5	5.1	4.2	6.4	4.5
Market Borrowings	4.4	4.4	6.6	5.0	4.2	5.0	4.5
Non bank	5.0	5.7	6.4	3.9	4.2	3.4	4.5
Bank	-0.5	-1.2	0.2	1.1	-	1.6	-
Monetary Authority	-0.4	-2.7	0.3	1.1	-	1.3	-
Commercial Bank	-0.1	1.5	-0.1	-0.1	-	0.3	-
Other Borrowings	-0.8	0.4	-0.1	0.1	-	1.3	-
Memorandum Item: Budget Deficit (before grants)	-7.3	-8.4	-10.0	-9.6	-7.8	-9.9	-7.3

Source: Central Bank of Sri Lanka

listed under the Excise (Special Provision) Act recorded a reduction in revenue collection in 1996. The consolidation of the excise tax on tobacco leaf and cigarettes into a single unit tax based on internationally accepted lengths and weights of cigarettes and the upward revision of excise tax rates on cigarettes in July 1996, together with the increased volume of sales of cigarettes, were responsible for the marked increase in excise tax collection, at 46 per cent compared to 11 per cent recorded in the previous year. In contrast, revenue from excise tax on liquor, which amounted to Rs.5,839 million, showed a drop of 7 per cent

compared to the increase of 34 per cent in the previous year. Despite the upward revision in excise duty on hard liquor in July 1996, the drop in hard liquor production resulted in reduction of the revenue collection by 7 per cent. In addition, even the rapid increase in the production of beer, by 70 per cent in 1996, could not recoup the revenue losses due to the drastic reduction in excise tax on beer from Rs.33.60 per bulk litre to Rs.10.00 per bulk litre in November 1995. Following the simplification of the Excise (Special Provision) Act by continuing the tax only on commodities with high potential yield while elimi-

nating the tax on a large number of other commodities, revenue collection from this tax category dropped by 22 per cent to Rs.3,395 million. Meanwhile, the excise tax on petroleum products such as petrol and diesel, was rationalised by converting it from a fixed rate basis to an ad valorem basis with the upward revision of prices in November 1996.

In spite of an increase in the total value of imports by 14 per cent in 1996, revenue collection through import duties rose only by 4 per cent. This low growth was attributable to the downward revision of tariff rates for agricultural equipment, books, timber, fishing nets etc. and full or partial duty waivers granted for some imports, such as rice, sugar, potatoes, onions, dried chillies and motor spare parts, which resulted in a reduction of the share of dutiable imports in total imports from 44 per cent in 1995 to 42 per cent in 1996. Accordingly, the average import duty rate on total imports, which is derived by dividing the total import duty collected by total imports, declined from 10.0 per cent in 1995 to 9.2 per cent in 1996, while the average duty rate on dutiable imports dropped from 22.6 per cent in 1995 to 21.4 per cent in 1996. Meanwhile, import duty collections in relation to GDP declined from 3.6 per cent in 1995 to 3.3 per cent in 1996.

Revenue from income taxes at Rs.20,751 million in 1996 reflected a buoyant growth of 21 per cent over 1995. The share of income taxes to total tax income increased from 14 per cent in 1995 to 16 per cent in 1996, with a marginal increase from 2.6 per cent of GDP recorded in the previous two years to 2.7 per cent of GDP in 1996. Due to an increase in the tax threshold from Rs.60,000 per annum to Rs.100,000 per annum, widening of the tax slabs, lowering of intermediate tax rates and the removal of surcharges on income taxes, receipts from personal income taxes at Rs.7,315 million recorded a marginal decrease of Rs.43 million. Revenue from the new tax, Save the Nation Contribution, which was imposed on employees in the public and private sector at a rate of 2 per cent on those who earn monthly emoluments between Rs.15,000 and Rs.30,000 and at a rate of 3 per cent on those who earn monthly emoluments over Rs.30,000, amounted to Rs.125 million in 1996. Meanwhile, in spite of the discontinuation of surcharges imposed on corporate income tax, revenue collected from corporate income tax at Rs.13,311 million showed a remarkable growth of 36 per cent mainly due to improvements in tax administration, which was reflected in the collection of taxes on under disclosure of income amounting to Rs.1,476 million, improvement in service sector activities such as telecommunication, banking and insurance and the payment of arrears of income tax of about Rs.1,000 million by the Ports Authority during 1996.

Stamp duty at Rs.5,279 million in 1996, registered a marginal increase of 2 per cent compared to and increase of 18 per cent in the preceding year. In spite of the revision of stamp duties on receipts on the basis of a progressively sliding scale, the slow growth of imports and the exemption of bonds and debt securities from stamp duties have partly offset the expected higher revenue collections through the enhanced revenue measures.

Chart 8.2
Composition of Revenue

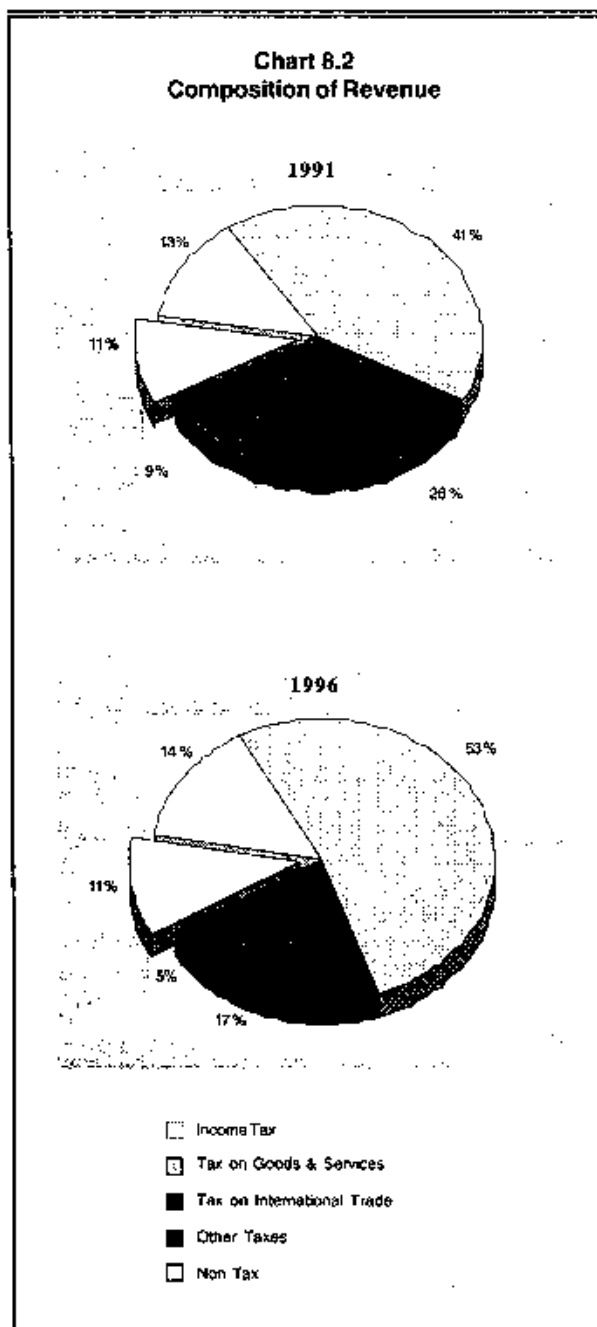


TABLE 8.2
Summary of Revenue by Component

Item	Rs Million						
	1992	1993	1994	1995	1996 Approved Estimates	1996 Provisional	1997 Approved Estimates
Tax Revenue	76,353	85,891	99,417	118,543	132,645	130,202	151,451
Income Taxes	10,967	12,543	15,277	17,161	17,299	20,751	21,345
Personal	4,067	5,235	5,621	7,358	4,787	7,315	7,825
Corporate	6,900	7,308	9,656	9,803	11,762	13,436	13,120
Save the Nation Contributions	-	-	-	-	750	5,125	400
Taxes on Property	3,597	3,493	4,386	5,162	5,839	6,276	6,788
Tax on Treasury bills held by Central Bank	1,991	1,073	471	1,050	-	1,684	350
Taxes on Domestic Goods and services	38,158	47,963	56,685	70,797	80,807	77,105	92,883
General sales and turnover tax	24,095	29,663	32,300	36,429	40,695	37,631	43,478
Manufacturing	8,262	9,231	9,171	9,908	9,699	8,874	12,023
Non Manufacturing	3,546	4,825	6,445	7,074	8,772	8,711	8,922
Imports	12,287	15,607	16,684	19,449	22,224	19,048	22,532
Excise Tax	10,232	11,655	14,632	19,436	21,775	22,567	28,936
Liquor	3,434	4,063	4,686	6,184	6,298	5,838	7,780
Tobacco	5,573	6,666	7,888	8,788	11,195	12,833	15,175
Other	1,225	726	2,058	3,730	4,350	3,895	5,981
Defence Levy	3,764	6,589	9,693	14,408	16,090	16,443	18,426
Licence fees	67	56	60	524	2,247	866	2,043
Taxes on International Trade	21,640	20,819	22,598	24,373	28,700	26,465	30,085
Imports	20,819	20,762	22,598	24,365	28,700	26,459	30,085
Exports	821	57	-	8	-	5	-
Non Tax Revenue	9,428	12,446	10,621	17,715	15,562	16,077	19,285
Property Income	6,262	8,154	7,360	12,858	10,082	10,059	12,046
of which: Central Bank Profits	1,150	1,000	1,200	1,200	1,200	1,700	1,500
Interest Income	3,596	4,390	4,560	6,946	6,006	6,222	6,496
Surplus of Trading Enterprises	1,179	-	-	-	-	-	-
Fees and charges	1,225	1,303	988	1,751	2,650	2,827	3,066
Other non-tax revenue	1,941	2,991	2,273	3,108	2,830	3,191	4,173
Total Revenue	85,781	98,339	110,038	136,258	148,207	146,279	170,736

As a percentage of GDP

Item	As a percentage of GDP						
	1992	1993	1994	1995	1996 Approved Estimates	1996 Provisional	1997 Approved Estimates
Tax Revenue	18.0	17.2	17.2	17.8	17.1	16.9	17.0
Income Taxes	2.6	2.5	2.6	2.6	2.2	2.7	2.4
Personal	1.0	1.0	1.0	1.1	0.6	1.0	0.9
Corporate	1.6	1.5	1.7	1.5	1.5	1.7	1.5
Save the Nation Contributions	-	-	-	-	0.1	0.0	-
Taxes on Property	0.8	0.7	0.8	0.6	0.6	0.7	0.8
Tax on Treasury bills held by Central Bank	0.5	0.2	0.1	0.2	0.0	0.2	0.0
Taxes on Domestic Goods and services	9.0	9.6	9.8	10.6	10.4	10.0	10.4
General sales and turnover tax	5.7	5.9	5.6	5.5	5.2	4.9	4.9
Manufacturing	1.9	1.8	1.6	1.5	1.3	1.2	1.3
Non Manufacturing	0.8	1.0	1.1	1.0	1.1	1.3	1.0
Imports	2.9	3.1	2.9	2.9	2.9	2.5	2.5
Excise Tax	2.4	2.3	2.5	2.9	2.8	2.9	3.2
Liquor	0.8	0.8	0.8	0.9	0.8	0.8	0.9
Tobacco	1.3	1.4	1.4	1.4	1.4	1.7	1.7
Other	0.3	0.1	0.4	0.6	0.6	0.4	0.7
Defence Levy	0.9	1.3	1.7	2.2	2.1	2.1	2.1
Licence fees	-	-	-	0.1	0.3	0.1	0.2
Taxes on International Trade	5.1	4.2	3.9	3.6	3.7	3.3	3.4
Imports	4.9	4.2	3.9	3.6	3.7	3.3	3.4
Exports	0.2	-	-	-	-	-	-
Non Tax Revenue	2.2	2.5	1.8	2.7	2.0	2.1	2.2
Property Income	1.5	1.6	1.3	2.0	1.3	1.3	1.4
of which: Central Bank Profits	0.3	0.2	0.2	0.2	0.2	0.2	0.2
Interest Income	0.8	0.9	0.8	1.0	0.8	0.7	0.7
Surplus of Trading Enterprises	0.3	-	-	-	-	-	-
Fees and charges	0.3	0.3	0.2	0.3	0.3	0.4	0.3
Other non-tax revenue	0.5	0.6	0.4	0.4	0.4	0.4	0.5
Total Revenue	20.2	19.7	19.0	20.4	19.1	18.0	19.1

Source: Central Bank of Sri Lanka

Non-Tax Revenue

Non-tax revenue recorded a decrease of 9 per cent in 1996, mainly reflected in a decline of property income from Rs.12,856 million in 1995 to Rs.10,059 million in 1996. The profits transferred by the Central Bank amounted to Rs.1,700 million in 1996. Postponement of interest payments by the National Development Bank (NDB) and the Development Finance Corporation of Ceylon (DFCC), the lower amount of dividends imposed under the Finance Act on public enterprises in 1996 and lower dividend payments by the two state banks were the major reasons for the reduction in property income. Meanwhile, revenue from fees and charges increased from Rs.1,751 million to Rs.2,827 million due to the upward revision of passport and visa fees and the full year impact of the 20 per cent increase in fees and charges on services rendered by government departments. The other non-tax income, which amounted to Rs.3,191 million, showed an increase of 3 per cent mainly due to a substantial increase in social security contributions.

Foreign Grants

Total foreign grants utilised for budgetary purposes in 1996 amounted to Rs.8,500 million, registering a decline of 6 per cent. Consequently, total foreign grants in relation to GDP, which have declined continuously in the recent past, further declined from 1.4 per cent in 1995 to 1.1 per cent in 1996. Receipts on account of project and programme grants amounted to Rs.6,140 million while commodity and food aid amounted to Rs.1,236 million. A sum of Rs.362 million was received under technical assistants, while the balance Rs.761 million was unclassified. As in previous years, Japan continued to be the major donor, providing Rs.2,880 million, followed by Norway, which provided Rs.2,424 million.

8.4 Expenditure

Total government expenditure and net lending at Rs.214,710 million recorded an increase of 7 per cent in 1996 compared to a 19 per cent increase in the previous year. However, total expenditure as a ratio of GDP declined sharply from 30.0 per cent in 1995 to 27.9 per cent in 1996. Current expenditure amounting to Rs.170,629 million accounted for 79 per cent of total expenditure in comparison to 77 per cent in the previous year. Public investments at Rs.48,370 million showed a decline of 8 per cent in 1996, while as a ratio of GDP it dropped from 8.0 per cent in 1995 to 6.3 per cent in 1996.

Current Expenditure

Current expenditure in 1996 at Rs.170,629 million recorded an increase of 11 per cent, which was substantially lower than the rate of growth of nominal GDP at 15 per cent in 1996. As a result, current expenditure as a ratio of GDP dropped from 23.1 per cent in 1995 to 22.2 per cent in 1996. Expenditure on defence, public sector salaries, pensions and interest payments on public debt remained at 77 per cent of total recurrent expenditure in 1996 as in the previous year. Despite the strict control on resource outlays of a current nature, Government was not able to contain current expenditure

Chart 8.3
Composition of Expenditure

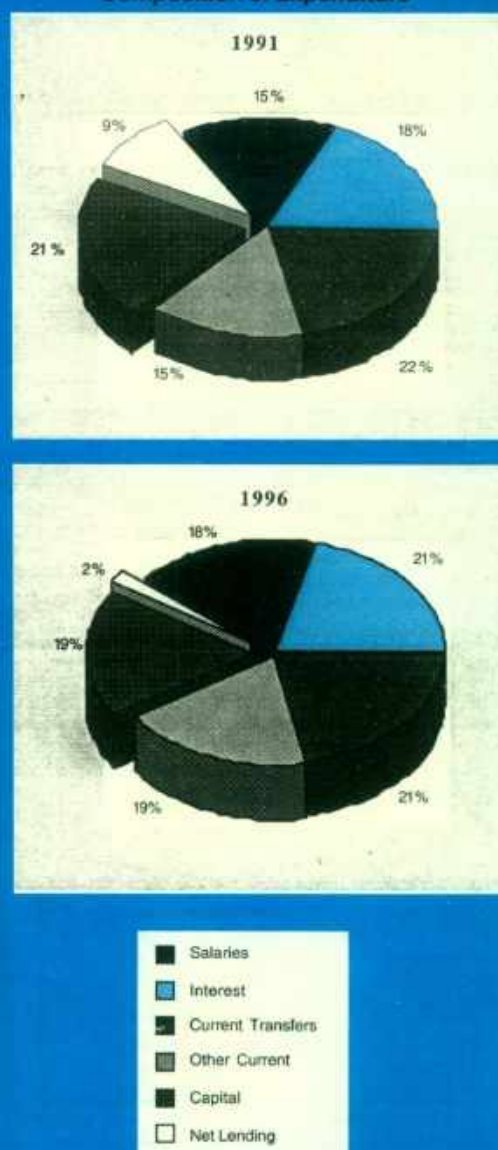


TABLE 8.3
Economic Classification of Expenditure and Lending minus Repayment

Item	Rs. Million						
	1992	1993	1994	1995	1996 Approved Estimates	1996 Provisional	1997 Approved Estimates
Current Expenditure	88,639	102,288	127,084	154,159	188,781	170,629	177,930
Expenditure on Goods and Services	39,692	44,895	54,700	75,447	82,519	76,660	83,086
Salaries and wages	20,793	26,332	29,309	34,909	39,978	36,332	44,603
Other Goods and Services	18,898	18,563	25,391	40,538	42,541	40,328	38,483
Interest Payments	25,940	30,203	38,031	38,225	44,057	46,021	49,800
Foreign	4,739	5,102	5,511	6,162	7,351	6,739	8,338
Domestic	21,201	25,101	32,520	32,063	36,706	39,282	41,462
Current Transfers and Subsidies	24,007	27,190	34,180	40,487	48,105	46,813	44,044
To public Corporations	1,428	1,571	2,634	7,841	6,308	8,233	2,239
To public Institutions	1,649	2,031	1,976	2,182	2,739	2,284	3,931
To Other levels of Government	1,111	896	1,307	1,157	1,512	1,592	1,464
To households and other sectors	19,819	22,692	28,263	29,307	37,545	34,706	36,410
Food stamps, food subsidy etc.	4,466	4,580	4,654	1,799	1,082	606	385
Jana Saviya/Samurdhi	3,096	3,685	5,369	5,130	11,794	8,591	8,692
Pensions	8,099	10,516	13,271	14,549	16,825	15,465	18,075
Fertilizer Subsidy	-	-	630	1,345	1,500	1,500	1,500
Other	4,158	3,911	4,339	6,484	6,345	8,644	6,658
Provision for Under expenditure	-	-	-	-	-4,900	-872	1,000
Capital Expenditure	24,948	33,662	30,391	41,722	43,203	40,634	47,879
Acquisition of Real Assets	12,604	19,719	16,747	22,589	27,313	24,576	28,726
Capital transfers	12,345	13,943	13,644	19,134	18,290	16,058	19,153
To public Corporations	4,610	4,311	4,246	7,614	5,123	6,017	6,371
To public Institutions	6,663	8,551	8,433	10,446	12,119	8,603	11,532
To Other levels of Government	1,028	1,036	914	1,057	1,000	1,042	1,200
Other	44	45	51	17	49	39	50
Provision for Under expenditure	-	-	-	-	-2,400	-1,243	-
Lending minus Repayment	2,386	4,510	10,293	4,601	-4,499	4,047	9,761
Advance accounts	-150	410	2,462	-1,580	500	630	500
On lending	6,246	6,265	10,064	11,087	15,313	8,336	12,665
Restructuring Cost	1,750	1,465	3,739	3,191	4,792	2,993	6,492
Privatisation proceeds	-2,850	-1,200	-2,996	-3,001	-21,000	-4,728	-5,000
Loan Repayments	-2,810	-2,430	-2,976	-5,097	-4,104	-3,182	-4,896
Total Expenditure and Net Lending	116,974	140,460	167,758	200,482	208,485	214,710	235,570

As a percentage of GDP

Item	As a percentage of GDP						
	1992	1993	1994	1995	1996 Approved Estimates	1996 Provisional	1997 Approved Estimates
Current Expenditure	21.1	20.5	21.9	23.1	21.9	22.2	19.9
Expenditure on Goods and Services	9.3	9.0	9.4	11.3	10.6	10.3	9.3
Salaries and wages	4.9	5.3	5.1	5.2	5.2	5.0	5.0
Other Goods and Services	4.4	3.7	4.4	6.1	5.5	5.2	4.3
Interest Payments	6.1	6.0	6.6	5.7	5.7	6.0	5.6
Foreign	1.1	1.0	1.0	0.9	0.9	0.9	0.9
Domestic	5.0	5.0	5.6	4.8	4.7	5.1	4.6
Current Transfers and Subsidies	5.6	5.4	5.9	6.1	6.2	6.1	4.9
To public Corporations	0.3	0.3	0.5	1.2	0.8	1.1	0.3
To public Institutions	0.4	0.4	0.3	0.3	0.4	0.3	0.4
To Other levels of Government	0.3	0.2	0.2	0.2	0.2	0.2	0.2
To households and other sectors	4.7	4.5	4.9	4.4	4.8	4.6	4.1
Food stamps, food subsidy etc.	1.1	0.9	0.8	0.3	0.1	0.1	0.0
Jana Saviya	0.7	0.7	0.9	0.8	1.5	1.1	1.1
Pensions	1.9	2.1	2.3	2.2	2.2	2.0	2.0
Fertilizer Subsidy	0.0	0.0	0.1	0.2	0.2	0.2	0.2
Other	-	-	0.7	1.0	0.8	1.1	0.7
Provision for Under expenditure	-	-	-	-	-0.6	-0.1	-
Capital Expenditure	5.8	6.7	5.2	6.2	5.6	5.7	5.4
Acquisition of Real Assets	3.0	3.9	2.9	3.4	3.5	3.2	3.2
Capital transfers	2.9	2.8	2.4	2.9	2.4	2.2	2.1
To public Corporations	1.1	0.9	0.7	1.1	0.7	0.8	0.7
To public Institutions	1.6	1.7	1.5	1.6	1.6	1.2	1.3
To Other levels of Government	0.2	0.2	0.2	0.2	0.1	0.1	0.1
Other	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Provision for Under expenditure	-	-	-	-	-	-0.2	0.0
Lending minus Repayment	0.6	0.9	1.8	0.7	-0.6	0.5	1.1
of which Advance accounts	-	0.1	0.4	-0.2	0.1	0.1	0.1
Total Expenditure and Net Lending	27.5	26.1	29.0	30.0	26.9	27.9	26.4

Source: Central Bank of Sri Lanka

at 21.9 per cent as targetted in the Budget, mainly due to the enhanced expenditure on defence.

Following the revision of salaries for teachers in 1995, salaries of all government employees who had not received any wage increases in 1995 were revised upward according to the recommendations made by the Salaries' Review Commission. An interim allowance of Rs. 100 per month during the first six months and Rs. 250 per month from July onwards was paid until the new salary revision was effected. In addition, an extra allowance was paid in 1996 to defence personnel who worked in operational areas. As a result, the total cost of personal emoluments increased by 10 per cent, from Rs. 34,909 million in 1995 to Rs. 38,332 million in 1996. The total wage bill included Rs. 13,337 million for defence services, which recorded a 10 per cent increase in 1996. Expenditure on salaries and wages accounted for 22 per cent of current expenditure, while as a share of the total government revenue it was 26 per cent. The total wage bill as a ratio of GDP declined to 5.0 per cent compared to 5.2 per cent in 1995.

Interest payments on public debt at Rs. 46,021 million recorded a substantial increase of 20 per cent compared to the marginal increase in 1995, while as a percentage of GDP, it increased to 6.0 per cent from 5.7 per cent in the previous year. The interest cost of domestic debt at Rs. 39,282 million showed an increase of 23 per cent over the previous year. Interest paid on Rupee Securities at Rs. 20,311 million recorded an increase of 12 per cent, while the average interest rate on Rupee Loans was about 13.8 per cent. The increase in the Rupee Loan stock, net of bond issues, by Rs. 24,174 million and the issue of Rupee Loans at a higher rate of interest ranging from 13-15 per cent per annum during the first half of 1996 pushed up the total interest cost on Rupee Loans in 1996. Meanwhile, the interest cost on Treasury bills showed a marked increase of 29 per cent to Rs. 18,053 million due to the new issues of Treasury bills which amounted to Rs. 11,225 million during first ten months in 1996, high interest rates prevailing during 1995 and until February 1996, and the high proportion of 3-month Treasury bills issued during 1996. Interest rates on Treasury bills with one year maturity ranged from 12.20 to 19.43 per cent per annum in 1994, 13.68 to 20.45 per cent per annum in 1995, and 14.40 to 19.05 per cent per annum in 1996. The limit on borrowings through Treasury bills prevented a further increase in interest costs on Treasury bills in 1996 as the outstanding stock reached the approved Treasury bills limit of Rs. 125 billion. The average interest cost of Treasury bills was 15.86 per cent per annum compared to 14.10 per cent in the previous year. The interest cost of foreign debt increased by 9 per cent to Rs. 6,739 million in 1996, while the original

budgetary estimate was Rs. 7,351 million. Government's ability to borrow low cost concessional loans with longer grace periods and the appreciation of the rupee against the Japanese yen by 7 per cent during 1996, (about 30 per cent of total outstanding foreign debt liability was denominated in yen) could be identified as major factors contributing to the lower interest cost of foreign debt in 1996. Displaying the concessionary nature of the outstanding foreign debt, the average rate of interest on foreign debt stock remained around 1.9 per cent in 1996 compared to 1.8 per cent in 1995.

The total amount of transfer payments, comprising transfers to households, public corporations and institutions and local government, at Rs. 46,813 million, recorded an increase of 16 per cent compared to 18 per cent recorded in the previous year. Despite the reduction in current transfers to the plantation sector as a result of the privatisation of 13 plantation companies in 1995 and 1996, transfers to public corporations increased by 5 per cent to Rs. 8,232 million mainly due to increased operational losses at the Railway and Postal departments and the large expenditure on the wheat flour subsidy in 1996. In spite of several upward revisions in wheat flour prices from Rs. 11.95 per kg. to Rs. 16.95 per kg. during 1996, total current transfers to the Co-operative Wholesale Establishment (CWE) on account of losses incurred on wheat flour sales was estimated to be about Rs. 5,515 million, compared to Rs. 6,200 million in the previous year. A sharp rise in wheat grain prices in the international market by 19 per cent from US dollars 186 per metric ton in 1995 to US dollars 221 per metric ton in 1996 (average C&F price), 8 per cent exchange rate depreciation of the rupee against the US dollar and an increase in the operational cost of wheat flour distribution resulted in an average loss of Rs. 6.97 per kg. in 1996, even with the revised prices, compared to Rs. 9.02 per kg. in 1995. Wheat flour consumption in 1996 remained high at 692,164 metric tons compared to 683,683 metric tons in 1995. The sharp increase in the price of rice due to the shortage in supply resulting from the fall in paddy production by 27 per cent and the high prices of imported rice contributed to the high level of wheat flour consumption in 1996. The combined effect of these factors, i.e., the high import price of wheat grain, depreciation of the rupee and the high level of wheat flour consumption, offset the effect of domestic price adjustments made in wheat flour, requiring a substantial subsidy on wheat flour sales in 1996. Meanwhile, transfers to public institutions increased marginally from Rs. 2,182 million in 1995 to Rs. 2,284 million in 1996. However, total current transfers to corporations and institutions declined from 1.5 per cent of GDP in 1995 to 1.4 per cent of GDP in 1996.

Transfer payments on account of the operational losses of the Railway and Postal departments stood at Rs.1,232 million, a 21 per cent increase over the losses incurred in the previous year. Despite the increase in railway fares by 15 per cent in March 1996, the total revenue collection of Sri Lanka Railways dropped marginally from Rs.947 million in 1995 to Rs.938 million in 1996, while the recurrent expenditure rose by 5 per cent to Rs.1,826 million. Meanwhile, the revenue collection of the Postal department remained at Rs.1,326 million, almost equal to the level recorded in 1995 while current expenditure increased by 7 per cent to Rs.1,670 million. As a result, the operational losses of the Postal department rose by 48 per cent to Rs.344 million, while the losses of the Railway department at Rs.888 million increased by 13 per cent, resulting in total operational losses of Rs.1,232 million in 1996.

Transfers to households, consisting of pensions and other welfare payments, amounted to Rs.34,706 million showing a 18 per cent increase in 1996. Pension payments increased by 6 per cent to Rs.15,465 million and amounted to 2 per cent of GDP in 1996. This increase was a combined result of the addition of about 8,000 new retirees and the payment of the overdue cost of living allowance in 1996. Meanwhile, initial steps were taken to consolidate multiple welfare programmes such as food stamps, kerosene stamps, Janasaviya and Samurdhi into a single welfare programme, which would be operated under the Samurdhi programme. Total direct subsidies to households under schemes such as Samurdhi, Janasaviya, food stamps, kerosene stamps, infant milk food, school season tickets, free school books, free school uniforms and Thripasha care increased by 21 per cent to Rs.12,735 million in 1996. Although the mid-day meal programme was terminated from the beginning of 1996, the increase in the total number of recipients under the Samurdhi programme from 1,213,535 in 1995 to 1,458,888 in 1996 together with the increase in the number of Samurdhi animators to 23,648 and Samurdhi supervisors to 1,337 contributed to the substantial increase in welfare expenditure in 1996. The escalation of the war in the Northern and Eastern provinces increased the number of displaced families, enhancing the expenditure on refugee related relief programmes from Rs.2,325 million in 1995 to Rs.3,275 million in 1996. Meanwhile, the cost of the fertilizer subsidy scheme amounted to Rs.1,500 million, compared to Rs.1,345 million in 1995 due to the increased usage of fertiliser in 1996. As a result, transfers to households as a ratio of GDP showed a marginal increase from 4.4 per cent in 1995 to 4.5 per cent in 1996. Current expenditure incurred in processing various goods and services required for operational purposes decreased

marginally to Rs.40,334 million in 1996 from Rs.40,538 million in the previous year. This decline was a combined outcome of a marginal reduction in defence outlays and expenditure on civil administration in 1996. Due to the stringent measures taken to contain current expenditure on other goods and services on non-defence activities, such expenditure declined marginally, to Rs.9,485 million, in 1996 from Rs.9,495 million in 1995.

In terms of the functional classification, current expenditure on social services comprising education, health, welfare and community services at Rs.59,294 million, accounting for 35 per cent of the total current expenditure. Current expenditure on education and health accounted for 43 per cent of total expenditure on social services, while welfare payments accounted for 55 per cent. Total expenditure on social services however dropped from 8.6 per cent of GDP in 1995 to 7.7 per cent in 1996.

Current outlays provided for the operation and maintenance of economic services increased by 9 per cent to Rs.8,807 million in 1996. Economic services such as transport and communication and trade and commerce, largely accounted for this increase in 1996.

Current expenditure on general public services at Rs.53,168 million showed an increase of 11 per cent and accounted for 31 per cent of the total current expenditure in 1996. This was a combined result of a 4 per cent increase in expenditure on defence and public order and safety to Rs.42,961 million and an increase in expenditure on civil administration by 56 per cent to Rs.10,207 million, mainly due to enhanced expenditure for Divisional Secretariats and Provincial Councils.

Public Investment

Public investment consisting of capital expenditure and on lending to public enterprises, recorded a drop of 8 per cent to Rs.48,370 million, and as a ratio of GDP, declined from 8.0 per cent in 1995 to 6.3 per cent in 1996. Capital expenditure, which consisted of acquisition of real assets by government ministries and departments and capital transfers to public corporations, institutions and other levels of government, recorded a decline of 4 per cent from Rs.41,722 million in 1995 to Rs.40,034 million in 1996, while on-lending to public enterprises dropped from Rs.11,087 million in 1995 to Rs.8,336 million in 1996. Acquisition of real assets that enhanced the capital stock of government ministries and departments under the Public Investment Programme (PIP) increased by 9 per cent to Rs.24,576 million.

TABLE 8.4
Functional Classification of Expenditure

Item	1992	1993	1994	1995	1996 Approved Estimates	Rs. Million	
						1996 Provisional	1997 Approved Estimates
Current Expenditure							
General Public Services	24,453	27,564	30,444	47,888	48,400	59,189	54,955
Civil Administration	7,099	7,405	4,637	6,562	16,202	10,207	13,431
Defence	12,876	15,413	19,415	35,186	25,180	37,370	33,528
Public Order and Safety	4,478	4,746	6,392	6,140	7,018	6,591	7,997
Social Services	32,700	37,476	47,655	57,648	63,194	59,294	58,740
Education	10,533	11,225	14,836	15,784	13,231	16,016	13,407
Health	4,518	5,711	7,666	8,818	10,566	9,260	12,054
Welfare	17,378	20,255	24,560	32,106	38,550	32,824	31,824
Housing	-	-	-	-	-	-	-
Community Services	271	265	593	941	847	1,191	1,455
Economic Services	3,834	4,328	6,195	8,078	8,169	8,807	8,532
Agriculture & Irrigation	1,396	1,483	2,506	3,826	3,448	3,894	4,175
Fisheries	68	107	99	105	178	148	193
Manufacturing and Mining	349	403	351	252	702	262	650
Energy and Water Supply	133	93	518	960	810	590	728
Transport & Communication	1,208	1,346	2,024	2,014	1,974	2,423	1,822
Trade & Commerce	232	203	72	172	267	691	241
Other	446	693	625	719	771	580	718
Other	28,652	32,920	42,769	49,546	54,918	50,231	55,783
of which: Interest	25,940	30,203	38,031	38,687	44,057	48,021	49,800
Provision for Under Expenditure	-	-	-	-	-4,900	-872	-
Total Current Expenditure	69,639	102,285	127,084	154,159	169,781	170,829	177,930
Capital Expenditure and Lending							
General Public Services	1,970	4,086	2,390	5,776	4,335	2,827	3,810
Civil Administration	1,256	3,463	1,753	3,962	3,226	1,662	3,810
Public Order and Safety	714	622	637	1,814	1,109	1,226	-
Social Services	6,136	6,075	7,677	9,854	12,363	11,198	13,676
Education	2,008	2,845	2,877	3,124	4,418	4,364	4,552
Health	2,023	1,353	1,519	2,134	3,661	2,768	3,985
Welfare	1,191	1,084	1,681	1,690	1,145	1,068	852
Housing	767	804	802	1,810	1,256	1,606	1,526
Community Services	148	189	758	1,297	1,882	1,359	2,786
Economic Services	20,444	29,500	29,304	36,106	43,170	34,519	41,808
Agriculture & Irrigation	5,890	5,682	5,179	6,060	6,525	5,491	6,233
on Mahaweli Project	2,670	2,810	2,598	3,090	2,133	1,940	1,655
Fisheries	175	124	368	361	542	311	525
Manufacturing and Mining	184	1,471	22	250	1,019	379	1,256
Energy and Water Supply	5,527	4,728	5,518	5,003	6,914	6,035	7,949
Transport & Communication	4,363	10,165	14,522	18,898	19,696	14,896	18,468
Trade & Commerce	365	364	182	20	353	105	321
Other	3,840	7,066	3,513	5,524	8,121	7,360	7,056
Other	1,072	1,081	1,084	1,074	1,049	1,062	1,250
Provision for Under Expenditure	-	-	-	-	-2,400	-1,243	-
Total Capital Expenditure and Lending	29,622	40,841	40,455	52,810	58,515	48,369	60,544

Source: Central Bank of Sri Lanka

Meanwhile, capital transfers to public corporations and institutions, which amounted to Rs.15,620, million reflected a 14 per cent reduction largely due to the decline in capital transfers to the Mahaweli Authority and the Road Development Authority in 1996. In addition, the higher level of capital transfers for the settlement of arrears amounting to Rs.2,395 million to the Shipping Corporation attributed to enlarge the capital transfers in 1995. Government institutions which were directly involved in infrastructure development, such as the Road Development Authority (Rs.4,404 million), Urban Development Authority (Rs.776 million), Southern Development Project (Rs.334 million), National Water Supply and Drainage Board (Rs.3,313 million) and Land Reclamation and De-

velopment Board (Rs.2,414 million), were given priority in capital transfers.

Capital expenditure incurred by public corporations and institutions from funds mobilised by way of government on-lending amounted to Rs.8,335 million which was only 54 per cent of the budgetary provision in 1996. This reduction was the combined outcome of large capital savings of Rs.2,355 million by the Ports Authority in the Ports Development Projects and the underutilisation of capital by Sri Lanka Telecom (Rs.947 million), Ceylon Electricity Board (Rs.1,837 million) and other enterprises totalling to Rs.4,254 million. Although the budgetary provisions for the Port Development Authority for the construction of

Jayah Container Terminal Stage III and IV was Rs.5,100 million, the two projects were completed at a cost of Rs.2,745 million, which saved Rs.2,355 million in the capital budget. This saving was largely attributed to bulk purchases of machinery and equipment for both projects at competitive prices from the international market. Meanwhile, the delays in administrative procedures and the environmental concerns, which affected the development activities of the Ceylon Electricity Board, Sri Lanka Telecom and other institutions, were responsible for the underutilisation of resources in 1996.

In terms of functional classification, though public investment in economic services in 1996 recorded a 4 per cent drop to Rs.34,519 million, it accounted for 71 per cent of total public investment compared to 68 per cent in the previous year. The transport and communication sector accounted for Rs.14,898 million or 43 per cent of total expenditure on account of economic services, out of which the Road Development Authority (Rs.4,404 million), Ports Authority (Rs.2,776 million) and Sri Lanka Telecom (Rs.2,406 million) accounted for Rs.9,586 million or 64 per cent of the total cost on transport and communication. The capital expenditure of the Mahaweli Authority of Sri Lanka accounted for 35 per cent of capital expenditure on agriculture and irrigation services, and 7 per cent of total capital expenditure on economic services. Meanwhile, public investment in the energy and water supply sector amounted to Rs.6,035 million showing a 21 per cent increase in 1996. This sector accounted for 17 per cent of the total capital expenditure on economic services. Investment in the National Water Supply and Drainage Board at Rs.3,313 million and on lending of Rs.2,721 million to the Ceylon Electricity Board (CEB) accounted for almost the entirety of the capital expenditure on energy and water supply services.

Public investment on social services, consisting of education, health, welfare, housing and community services, increased by 14 per cent to Rs.11,185 million and accounted for 23 per cent of total public investments in 1996. Investment in education at Rs.4,384 million and health at Rs.2,768 million showed increases of 40 per cent and 30 per cent, respectively. These increases were largely due to the increased expenditure on construction of hostels for university students in the education sector and on patient care services such as acquisition of equipment and improvement of capital assets in the health sector. Meanwhile, the expenditure on special welfare services declined by 37 per cent mainly due to the consolidation and targeting of existing welfare programmes in 1996. Capital investment in general public services at Rs.2,827 million recorded a marked decline of 51 per cent in 1996, mainly due to the strict measures taken to curtail non-

priority capital expenditure in the area of civil administration. As a result, the total capital investment in general administration declined from 0.9 per cent of GDP in 1995 to 0.4 per cent in 1996.

8.5 Provincial Councils

The main objective of establishing the Provincial Council (PC) system under the 13th Amendment to the Constitution; Provincial Councils Act No. 42 of 1987 was to decentralise the decision making process by the delegation of administrative powers to these Councils. As the powers given to the PCs are not sufficient to raise adequate revenue to meet their operational expenses, the Central Government allocates funds for certain devolved activities at the PC level. These funds are provided as block grants, while devolved activities of a capital nature are financed through criteria based grants by the Central Government.

The revenue collected by PCs at provincial level by way of taxes on production and consumption, stamp duty,

TABLE 8.5
Budget Out-turn for Provincial Councils

Item	1995	Rs Million
1 Total Revenue	4,440.3	4,864.4
1.1 Tax on Production and Expenditure	3,180.8	3,416.3
Turnover Taxes	2,335.2	2,463.6
Licence Fees	839.6	946.2
Other Taxes	5.8	10.5
1.2 Profits and Dividends	68.2	67.3
1.3 Sales and Charges	317.0	355.4
1.4 Stamp Duty	867.1	1,096.0
1.5 Other	7.2	9.8
2. Total Expenditure	20,852.6	22,128.1
2.1 Current Expenditure	19,795.3	20,941.3
Functional Basis	19,795.3	20,941.3
Provincial Administration	2,066.9	1,841.9
Economic Services	755.1	833.8
Social Services	16,973.3	18,195.6
Economic Basis	19,795.3	20,941.3
Personal Emoluments	16,030.6	16,262.8
Other	3,764.6	4,678.7
2.2 Capital Expenditure	1,057.3	1,186.8
Acquisition of Capital Goods	593.7	766.6
Capital Transfers	66.4	82.0
Other	397.2	337.3
3 Financing	15,288.0	15,572.7
3.1 Block Grants	14,065.9	15,030.6
3.2 Criteria Based Grants	897.1	500.0
3.3 Matching Grants	325.0	242.1

(a) Provisional

Sources: Ministry of Co-operative, Provincial Councils & Indigenous Medicine
Central Bank of Sri Lanka

property income, sales and charges and sales of capital goods increased by 10 per cent to Rs.4,884 million in 1996 compared to Rs.4,440 million in the previous year. Revenue collection from taxes on production and consumption, which includes turnover taxes on wholesale and retail businesses, licence fees and other taxes, amounted to Rs.3,416 million, accounting for 70 per cent of the total (devolved) revenue collection and showed an increase of 7 per cent over the previous year. Turnover tax on wholesale and retail businesses amounted to Rs.2,464 million, recording a 6 per cent increase in 1996. A turnover tax rate of 1 per cent had been imposed on most wholesale and retail businesses, while certain businesses such as the selling of timber and furniture were liable to pay turnover tax at a rate of 5 per cent. Revenue collection through licence fees showed a 13 per cent increase to Rs.946 million, compared to Rs.840 million in the previous year. The issue of motor vehicle licences and licences for liquor shops was the main source of revenue in this category.

The collection of stamp duty at Rs.1,036 million showed an increase of 19 per cent in 1996. Meanwhile, sales and charges which mainly includes courts' fines and fees and charges under the Motor Traffic Act, amounted to Rs.355 million, recording an increase of 12 per cent in 1996.

On the basis of revenue performance by PCs, total revenue collection by the Western Provincial Council stood at Rs.3,232 million, accounting for 66 per cent of total revenue collection by PCs, followed by the Central, North Western and Southern Provincial Councils, each accounting for around 8 per cent of total revenue in 1996. In fact, the revenue of these 4 councils represented about 90 per cent of the total revenue collection in 1996.

Total current expenditure of PCs amounted to Rs.20,941 million, registering an increase of 6 per cent in 1996. Personal emoluments totalled Rs.16,263 million, representing 78 per cent of total recurrent expenditure in 1996. The total emoluments paid on a functional basis showed that education (Rs.11,634 million), health (Rs.2,850 million) and divisional administration (Rs.548 million) accounted for 92 per cent of total personal emoluments in 1996. Meanwhile, total expenditure on education (Rs.11,948 million), health (Rs.3,562 million), local government (Rs.1,614 million), social services (Rs.639 million) and divisional administration (Rs.662 million), represented 88 per cent of total recurrent expenditure in 1996. In terms of the functional classification of expenditure, social services at Rs.18,166 million accounted for 87 per cent of the total recurrent expenditure followed by economic services at Rs.834 million and provincial administration at Rs.1,942

million, representing 4 per cent and 9 per cent of total recurrent expenditure, respectively, in 1996. In comparison, the shares of these sectors in 1995 were 86 per cent, 4 per cent and 10 per cent, respectively.

In contrast to the pattern of revenue distribution among PCs, the distribution of recurrent expenditure was more uniform. Although the current expenditure of the Western Provincial Council at Rs.4,994 million, accounted for 24 per cent of the total recurrent expenditure, the shares of all other PCs ranged between 7-14 per cent in 1996.

Capital expenditure at Rs.1,187 million in 1996 showed an increase of 12 per cent over the Rs.1,057 million recorded in 1995. Of total capital expenditure, outlays on equipment, construction and land improvement at Rs.757 million accounted for 64 per cent in 1996, indicating an increase of 27 per cent compared to Rs.594 million in the previous year. In addition, PCs have taken over work related to capital expenditure from the respective line ministries and the necessary funds were provided under the Medium Term Investment Programme (MTIP).

The operations of PCs generated a loss of Rs.16,057 million in 1996 compared to a loss of Rs.15,355 million in the previous year. The overall deficit was Rs.17,244 million in 1996, compared to Rs.16,412 million in 1995. The Central Government provided block grants totalling Rs.15,831 million in 1996 to finance these operational losses compared to Rs.14,066 million provided in the previous year. Meanwhile, criteria based grants amounting to Rs.800 million were also provided by the Central Government in 1996 for capital expenses. This figure was higher in 1995 at Rs.897 million. The balance financial requirement for capital expenditure was provided by the Central Government as a matching grant.

8.6 Public Enterprise Reforms

The Public Enterprises Reform Commission (PERC) was established under the Public Enterprises Reform Commission of Sri Lanka Act, No. 1 of 1996. The main functions of the Commission are to advise and assist the Government on the reform of public enterprises with a view to fostering and accelerating economic development, upgrading production and services with access to international markets, acquisition of new technology and expertise, developing and broad basing the capital market and mobilizing long term private savings, motivating the private sector and augmenting government revenue so as to enable it to better address its social agenda.

TABLE 8.6
Realisation of Privatisation Proceeds in 1996(a)

Name of the Enterprise	Sale of Majority Share Holding			Public Share Issue		Total Amount Realised Rs. Million
	% Divested	Local Rs. Million	Foreign Rs. Million	% Divested	Amount Realised Rs. Million	
Plantation Companies						
Watawala Plantations Limited(b)	51	295.40	-	-	-	295.40
Horana Plantations Limited(b)	51	88.80	-	-	-	88.80
Maskeliya Plantations Limited	51	219.30	-	-	-	219.30
Madulsima Plantations Limited	51	102.00	-	-	-	102.00
Agarapathana Plantations Limited	51	267.87	-	-	-	267.87
Hapugastenna Plantations Limited	51	242.25	-	-	-	242.25
Balangoda Plantations Limited	51	420.75	-	-	-	420.75
Uda Pussellawa Plantations Limited	51	316.14	-	-	-	316.14
Other Enterprises						
Orient Lanka Limited	60	-	1,000.00	-	-	1,000.00
Tea Smallholder Factories Limited	-	-	-	39	54.60	54.60
Rajarata Agro Fertilizer Co. Limited	90	60.05	-	-	-	60.05
Lanka Lubricants Limited	-	-	-	39	547.24	547.24
Ceylon Steel Corporation	90	-	849.45	-	-	849.45
Total		2,010.56	1,849.45		611.84	4,471.85

(a) The government accounts show net receipts from divestiture proceeds after paying commission to Colombo Stock Exchange, other service charges etc.

Source: Public Enterprise Reform Commission

(b) Balance payment received in 1996 where an advance payment was received in 1995 as follows:

Watawala Plantations Limited	Rs. 10.6 million
Horana Plantations Limited	Rs. 15.2 Million

During 1996, the Public Enterprises Reform Programme generated Rs.4,661 million on privatisation proceeds. The divestiture of 60 per cent shares of Orient Lanka Limited and the divestiture of 90 per cent shares of Ceylon Steel Corporation Limited raised Rs.1,000 million and Rs.849 million, respectively. Privatization proceeds for these two enterprises were wholly from foreign sources.

In the area of plantation industry, six plantation companies namely, Maskeliya Plantations Limited, Madulsima Plantations Limited, Agarapathana Plantations Limited, Hapugastenna Plantations Limited, Balangoda Plantations Limited and Uda Pussellawa Plantations Limited were privatized in 1996, where 51 per cent of the majority shareholdings were divested raising Rs.1,568 million of revenue for the Government. In 1996, Rs.382 million was received from the divestiture of 51 per cent of majority shareholdings of Watawala Plantations Limited and Horana Plantations Limited in addition to the advance payment of Rs.26 million received in the previous year. A part of the sale proceeds of 51 per cent of the majority shareholdings and 20 per cent issues to the public each of Agalawatta Plantations Limited and Kelani Valley Plantations Limited spilled over to 1996 and amounted to Rs.123 million. In total, the privatization proceeds from the 10 plantation companies mentioned above amounted to Rs.2,111 million, accounting for 45 per cent of the privatization proceeds in 1996.

The public share issues of 39 per cent each of the shares of Lanka Lubricants Limited and Tea Smallholder

Factories Limited were carried out in 1996 and the divestiture proceeds amounted to Rs.612 million, in addition to Rs.318 million collected in 1994 when the divestiture process began for these two enterprises, with the divestiture of a 51 per cent majority shareholding.

The divestiture of 90 per cent of the shares of Rajarata Agro Fertiliser Company Limited raised Rs.60 million. In 1996, Rs.18 million was received as divestiture proceeds from Lanka Plywood Products Limited, Ruhunu Agro Fertiliser Company Limited and Wayamba Agro Fertiliser Company Limited, whose divestiture proceeds have been received in installments from 1993, 1994 and 1995 onwards, respectively.

The transfers of ownership of shares of privatized public enterprises to the employees of such enterprises were also carried out during 1996. The ownership of 1.1 per cent of the shares of Capital Development and Investment Company Limited, 3 per cent of shares of Orient Lanka Limited and 10 per cent of shares each of Shell Gas Lanka Limited, Tea Smallholder Factories Limited, Lanka Ceramic Company Limited and Puttalam Cement Company Limited was gifted to the employees of those companies.

In the area of privatization policy, the Government addressed a key problem that arose due to unsound strategies adopted in privatization of certain public enterprises in the past. To address this problem the Government introduced the Rehabilitation of Public Enterprises Act, No. 29 of 1996 to provide for the rehabilitation of privatized

TABLE 8.7
Failed Privatised Public Enterprises

Status	Colombo Commercial Fertilizer Limited	Kantalai Sugar Industries Limited	Hingurana Sugar Industries Limited	Kahalagaha Graphite Lanka Limited	Lanka Loha Hardware Limited	Mattegama Textiles Mills Limited
Percentage of Shares Sold	90	90	90	90	90	90
Percentage of Shares Gifted to Employees	10	-	10	10	10	10
Month of Stoppage of Operations	Dec.-1994	Jul.-1994	Nov.-1996	Nov.-1994	May-1996	Jun.-1996
Number of Employees Affected	330	500 (could be employed)	1,290	700	300	1,002
Non-Payment of Wages, EPF, ETF etc.	From Dec.-94 in full	From Jul.-94 in full	Rs.47.1 million	From Dec.-94 in full	From Dec.-94 in full	Rs. 10.5 million

Source: General Treasury

public enterprises. The Act permits the Government to take appropriate steps to rehabilitate privatized public companies when the business undertakings of such companies have failed resulting in non-employment, retrenchment, non-payment of wages and statutory dues of workers of such companies and when it is necessary and expedient, in the interest of the national economy, and for the purpose of securing recognition of, and respect for, the rights of the workers of such companies, and upgrading the production of such companies to meet the just requirement of the general welfare of a democratic society.

At the time of enactment of the Rehabilitation of Public Enterprises Act, six failed privatized public enterprises were in need of rehabilitation as defined in the said Act. These enterprises were Colombo Commercial Fertilizers Limited, Kantalai Sugar Industries Limited, Hingurana Sugar Industries Limited, Kahalagaha Graphite Lanka Limited, Lanka Loha Hardware Company Limited and Mattegama Textile Mills Limited. In the process of privatization 90 per cent of the shares of each of these six public enterprises were divested. All these companies were not engaged in commercial operations by June 1996.

Recoveries from past on-lending by the Government amounted to Rs.3,473 million, of which Rs.1,578 million was paid by the Ceylon Electricity Board. Annual interest payments on government bonds held by the two state banks in respect of their restructuring programme amounted to Rs.2,891 million. In 1996, People's Bank, Bank of Ceylon and National Savings Bank were issued with government bonds to the value of Rs.10,056 million, Rs.9,336 million and Rs.4,480 million, respectively.

8.7 Financing the Budget Deficit

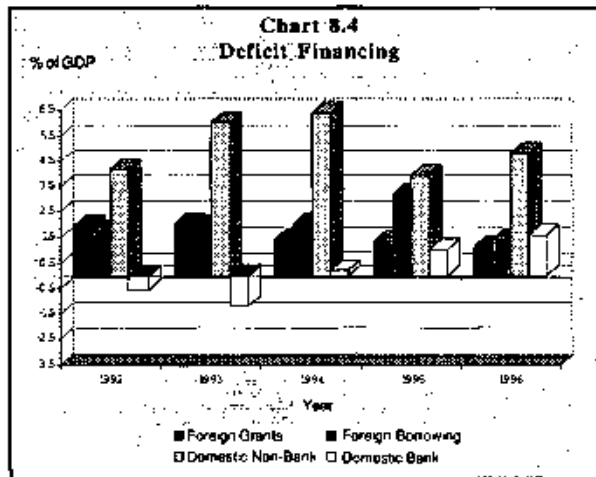
The budget deficit (after grants) in 1996 amounted to Rs.59,932 million. Gross foreign borrowings available for

financing the deficit decreased by 28 per cent to Rs.21,402 million. Net foreign borrowings amounted to Rs.10,911 million, indicating a larger decline due to an increase in foreign loan repayments in 1996. Gross disbursements on foreign borrowing were 24 per cent below the amount budgeted for 1996. The major reasons observed for this underutilisation of foreign resources were delays in project implementation, particularly in the areas of energy, road development, telecommunication and water supply and resource constraints on the domestic front for projects implemented on a reimbursable foreign aid basis. The appreciation of the domestic currency especially against the Japanese yen (7 per cent appreciation of the rupee against the Japanese yen in 1996) which accounted for 35 per cent of disbursements of gross foreign borrowing also reduced the domestic currency value of yen proceeds in 1996. Net foreign borrowings as a ratio of GDP declined from 3.2 per cent in 1995 to 1.4 per cent in 1996. Meanwhile, the share of net foreign borrowings to the total deficit (after grants) declined from 38 per cent in 1995 to 18 per cent in 1996.

Reflecting a large resource gap in government fiscal operations in 1996, the net borrowing requirement from domestic sources at Rs.49,020 million recorded a 44 per cent increase over the level of Rs.33,972 million recorded in the previous year. The net domestic financing as a proportion of GDP was 6.4 per cent, while as a share of the deficit (after grants), it stood at 82 per cent in 1996. Total net borrowings from domestic sources comprised bank borrowings of Rs.12,344 million and non-bank borrowings of Rs.36,676 million which included arrears payable to domestic sources amounting to Rs.2,715 million.

Gross borrowings for deficit financing from non-bank domestic sources through the issue of Rupee Loans, Treasury bills and other borrowings amounted to Rs.56,710 million in 1996, compared to Rs.54,976 million in the previous year. Gross borrowings through the Rupee Loan

Programme amounted to Rs.46,717 million, compared to Rs.46,715 million in the previous year. With repayments of Rs.22,567 million, net borrowings through the Rupee Loan Programme showed an increase of 19 per cent to Rs.24,174 million compared to Rs.20,386 million in 1995. The Employees' Provident Fund (EPF) continued to be the major subscriber to the Rupee Loan Programme as in the previous years with subscriptions totalling Rs.37,689 million, compared to Rs.31,420 million in 1995. Meanwhile, the National Savings Bank (NSB) continued its downward trend in investing in Rupee Loans for the second consecutive year. Total subscriptions by the NSB were Rs.5,790 million, compared to Rs.14,429 in 1995 and Rs.19,595 million in 1994. Resources raised through Rupee Securities from other non-bank sources amounted to Rs.3,237 million, compared to Rs.1,029 million in the previous year. The main reason for the reduction in gross borrowing through the Rupee Loan Programme was the borrowing of funds from non-captive sources through administrative arrangements in 1996.



Resource mobilisation through the new issues of Treasury bills amounted to Rs.10,741 million. The ownership of Treasury bills changed due to open market operations which resulted in an increase in Central Bank holdings of Treasury bills to Rs.17,100 million at the end of 1996, compared to Rs.12,525 million at the end of the previous year. When adjustments for secondary market operations are made, Treasury bill holdings by the banking sector as a ratio of total outstanding Treasury bills amounted to 31 per cent. Meanwhile, borrowing through Treasury bills reached the approved limit of Rs.125,000 million in October 1996. The Treasury bill borrowing limit was not revised upward and the Government faced considerable difficulty in mobilising resources from the market due to the non-availability of market oriented debt instruments. As a result, borrowings through administrative arrangements with government financial and non-financial institutions amounted to Rs.7,648 million. The rates of inter-

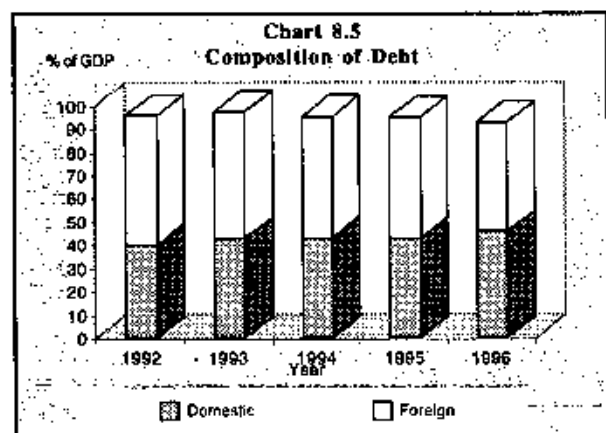
est on these borrowings were generally equivalent to the yield on Treasury bills prevailing at the time of borrowing.

The large resource gap that emerged in 1996 compelled the Government to borrow from the banking system to finance the budget deficit. The total borrowing from the financial sector amounted to Rs.12,344 million, compared to Rs.7,065 million in 1995. Of this, borrowings from the monetary authority stood at Rs.9,873 million, while borrowings from commercial banks amounted to Rs.2,471 million. The increased borrowings from the Central Bank, through the use of provisional advances (Rs.3,995 million), the net position of government deposits and cash items in the process of collection (Rs.1,303 million) and increased Central Bank Treasury bill holdings (Rs.4,575 million), resulted in a total net borrowing of Rs.9,873 million in 1996, contributing to an expansion in high powered money.

Net credit to government from commercial banks, excluding the issue of long-term bonds of Rs.19,393 million, increased by Rs.2,472 million in 1996. This was a net result of an increase in government borrowings from the commercial banks by Rs.5,890 million and a build up of government deposit balances by Rs.3,418 million. Thus, the total net government borrowings from the banking sector amounted to Rs.12,344 million in 1996. Gross government borrowings from the banking system at the end of 1996, on which interest was paid, amounted to Rs.39,707 million. However, the Government also had deposit balances with the banking system amounting to Rs.16,413 million, of which Rs.14,379 million was held in current accounts which earned no interest. This emphasises the urgent need of improving the Government's cash management in order to reduce the high interest burden on government budgetary operations.

8.8 Government Debt

The outstanding government debt at the end of 1996 stood at Rs.708,859 million and amounted to 92 per cent of GDP. This includes Rs.23,873 million of 10 year bonds issued in 1996 to the two state banks and the National Savings Bank to settle overdue loans which had been granted under government guarantee and Rs.24,088 million of 30 year bonds issued in 1993 to the two state banks. Total government debt, excluding the bonds issued during the year, increased by 8 per cent in 1996 compared with 15 per cent in 1995. Domestic debt at Rs.349,007 million accounted for 49 per cent of total debt, while the balance 51 per cent was on account of foreign debt amounting to Rs.359,852 million.



Domestic Debt

Domestic debt, exclusive of long-term bonds, amounted to Rs.325,134 million and registered an increase of 14 per cent in 1996 compared to a 15 per cent increase in the previous year. Short-term debt (maturity of one year or less) at Rs.142,689 million accounted for 41 per

TABLE 8.8
Outstanding Central Government Debt (a)

	1992	1993	1994	1995	1996
	Rs. Million				
Total Domestic Debt (b)	170,020	213,685	249,118	285,759	349,007
Short Term	97,924	101,845	108,725	127,471	142,689
Medium and Long term	72,096	111,840	140,393	158,288	206,318
By Debt Instruments	170,020	213,685	249,118	285,759	349,007
Rupee Securities	69,160	105,707	137,554	157,928	205,975
Treasury Bills	67,096	67,196	98,896	113,771	124,996
Other	13,744	10,782	12,669	14,060	18,036
By Institutions	170,020	213,684	249,119	285,759	349,007
Banks	58,111	90,134	100,043	113,356	155,895
Central Bank	34,932	16,480	21,345	28,684	37,475
Commercial Banks	23,179	73,654	78,698	84,671	119,022
Sinking Fund	359	239	137	100	100
Non-Bank Sector	111,550	123,311	148,939	172,304	192,212
National Savings Bank	30,782	37,767	46,407	48,406	56,852
Employees' Provident Fund	54,563	65,645	79,745	95,000	110,481
Other	26,205	19,899	22,786	28,898	34,329
Total Foreign Debt	235,539	270,224	301,812	348,286	359,856
Project Loans	185,003	218,355	246,075	286,848	302,470
Non-Project Loans	50,536	51,869	55,737	59,438	57,386
By Institutions	235,539	270,224	301,812	348,286	359,856
Concessional Loans	225,132	260,557	292,463	335,656	346,856
Commercial Loans	10,407	9,667	9,350	10,630	10,956
External Supplier's Credit	1,094	1,065	950	1,020	954
Total Outstanding Govt. Debt	405,559	483,909	550,930	632,045	708,863
Total Outstanding Govt. Debt Net of Sinking Fund	405,199	483,589	550,793	631,945	708,758

Source: Central Bank of Sri Lanka

(a) Values at end year.

(b) Inclusive of Rs. 24,088 Million and Rs.23,873 Million of Long Term Bonds issued in 1993 and 1995 respectively.

cent of total domestic debt at the end of 1996 compared to 45 per cent at the end of 1995. Reflecting a low level of borrowing through short-term debt instruments, due to the limit on the issue of Treasury bills, short term borrowings increased by only 12 per cent compared to 17 per cent in the previous year. As the authorised limit on the outstanding level of Treasury bills at Rs.125 billion was not revised upward and the borrowings through Treasury bills reached that limit in October 1996, total borrowings through the issue of new Treasury bills was limited to Rs.11,225 million in 1996, in comparison to Rs.14,875 million in 1995. The outstanding liability on account of Treasury bills at Rs.124,996 million accounted for 88 per cent of the total short-term debt. Meanwhile, the outstanding liability on account of the Central Bank's provisional advances, which accounted for the balance 12 per cent of short-term debt, rose by 29 per cent to Rs.17,693 million at the end of 1996.

The outstanding liability on medium and long-term debt, which included long-term restructuring bonds of Rs.24,088 million issued in 1993 and Rs.23,873 million issued in 1996, totalled Rs.206,318 million and accounted for 59 per cent of the total domestic debt at end 1996. Rupee Securities represented almost the entirety of the medium and long-term domestic debt stock of the Government.

The outstanding liability on Rupee Securities, including two long-term restructuring bonds of Rs.47,961 million, stood at Rs.205,975 million at end 1996. Total Rupee Securities issued for financing the deficit amounted to Rs.46,716 million, while total repayments were Rs.22,543 million, resulting in a net increase of Rs.24,173 million (excluding long-term bonds). Rupee loans floated during 1996 carried a maturity period of two to six years with interest rates ranging from 13.5 to 15.0 per cent per annum. The main intention of issuing two year Rupee Securities at a higher interest rate of 15 per cent per annum was to provide an attractive debt instrument alternative to Treasury bills to attract funds from non-captive sources. The Employees' Provident Fund (EPF) and the National Savings Bank (NSB) continued to be the two main subscribers to the Rupee Loan Programme, accounting for 75 per cent of the total outstanding Rupee Securities as at end 1996. Due to the two issues of long-term restructuring bonds, the two state banks accounted for 22 per cent of total outstanding Rupee Securities, while Rupee Securities exclusive of long-term bonds were almost entirely held by non-bank sources.

The Government issued long-term bonds with a maturity period of ten years to the value of Rs.23,873 million to the two state banks (Rs.10,056.3 million to People's

Bank and Rs.9,336.3 million to Bank of Ceylon) and NSB (Rs.4,479.9 million) at an interest rate of 14 per cent per annum in 1996. The purpose of issuing these bonds was to enable these institutions to recapitalise their liabilities by settling overdue loans granted under government guarantees for various projects.

Foreign Debt

The total outstanding liability on foreign debt at Rs.359,852 million at the end of 1996, recorded an increase of Rs.13,566 million or 4 per cent over the level recorded at the end of the previous year. The increase in the foreign debt was the net result of gross foreign borrowing of Rs.24,435 million, a repayment of Rs.8,939 million and a reduction in liability of Rs.1,929 million arising from exchange rate variations.

TABLE 8.9
Effect of Exchange Rate Variation on Foreign Loans

Item	Rs. Million				
	1992	1993	1994	1995	1996 (a)
Gross receipts	15,316	16,839	19,384	24,359	24,435
Repayments	7,955	6,984	7,606	8,477	8,939
Net receipts	7,361	9,855	11,778	15,882	15,495
Change in liability due to					
Exchange rate Variations	13,599	24,831	19,810	28,592	1,929
Liability as at end of period	235,538	270,224	301,812	346,288	359,852

(a) Data is based on value date recording system. Source: Central Bank of Sri Lanka

(b) Provisional

The outstanding liability on account of concessional loans at Rs.348,898 million increased by Rs.13,242 million or 4 per cent over the previous year. This increase resulted from gross receipts of Rs.23,370 million, repayment of Rs.7,665 million and a reduction in liability of Rs.2,463 million on account of exchange rate movements. The share of the concessional debt to total foreign debt stood at 97 per cent as in the previous year. Bilateral loans at Rs.188,498 million accounted for 54 per cent of total concessional loans, while multi-lateral loans at Rs.160,400 million accounted for the balance 46 per cent. The outstanding liability on account of commercial loans increased marginally from Rs.10,630 million to Rs.10,954 million at the end of 1996.

Liabilities on account of project and programme loans at Rs.302,470 million at the end of 1996 showing an increase of Rs.15,622 million. This was a net result of gross receipts of Rs.23,237 million, repayment of Rs.5,986 million and a reduction in liability of Rs.1,629 million result-

ing from exchange rate variations. The outstanding liability on commodity loans declined by Rs.2,477 million to Rs.55,238 million at the end of 1996 from Rs.57,715 million in 1995, mainly due to the net repayments of Rs.2,104 million and the reduction of total liability by Rs.373 million on account of exchange rate variations. Approximately 98 per cent of the project and programme loans were obtained from multilateral and bilateral sources, while all commodity loans were from bilateral sources.

Government Debt Service Payments

The debt service payments of the Government at Rs.79,261 million, consisting of Rs.46,021 million of interest payments and Rs.33,240 million of amortization payments, registered an increase of Rs.4,489 million over the previous year. However, debt service payments as a ratio of GDP recorded a reduction from 11.2 per cent in 1995 to 10.3 per cent in 1996. This was the net outcome of a reduction in amortization payments by Rs.3,306 million and an increase in interest payments by Rs.7,795 million.

Despite the increase in amortization payments on account of foreign loans by Rs.2,014 million, the reduction in amortization payments on account of domestic loans by Rs.5,320 million due to a lower volume of Rupee Securities maturing, contributed to the overall reduction by Rs.3,306 million. Total debt repayments on both domestic and foreign debt accounted for 42 per cent of total debt service payments in 1996, compared to 49 per cent in the previous year.

The interest payments on domestic debt increased by 23 per cent to Rs.39,282 million in 1996. This was the

TABLE 8.10
Government Debt Service Payments

Item	Rs. Million				
	1992	1993	1994	1995	1996 (a)
Debt Service Payments	52,018	57,493	60,702	74,772	79,261
Amortization Payments	28,078	27,290	22,671	36,546	33,240
Domestic	18,123	20,327	15,065	28,069	22,749
Foreign	7,955	6,963	7,606	8,477	10,491
Interest Payments	25,940	30,203	38,031	38,226	46,021
Domestic	21,201	25,101	32,520	32,064	39,282
Short Term	11,923	13,351	18,712	13,947	18,942
Medium & Long-Term	9,278	11,750	13,808	18,117	20,340
Foreign	4,739	5,102	5,511	6,162	6,739
Interest/Current Expenditure (%)	28.94	29.53	29.93	24.80	26.47
Debt Service/GDP(%)	12.23	11.50	10.48	11.20	10.31

(a) Provisional

Source: Central Bank of Sri Lanka

combined effect of the enhanced volume of outstanding debt stock and significantly high interest cost on Treasury bills issued in 1995. Reflecting the benefits of the appreciation of the rupee against the Japanese yen and the concessionary nature of new foreign borrowings, the interest payments on foreign debt increased by only Rs.577 million in 1996.

In terms of economic classification, total interest payments accounted for 27 per cent of current expenditure and 31 per cent of government revenue, indicating the continuation of the burden of interest payments on government budgetary operations. The ratios of total interest payments to total revenue during the last two years were 26 per cent and 28 per cent, respectively.

Reflecting the enhanced volume and the high interest rates on Treasury bills prevailed during 1995, together with the high volume of Treasury bills issued in the three month category, interest payments on short-term debt at Rs.18,942 million increased by 36 per cent compared to the 25 per cent decline in 1995. Interest payments on medium and long-term debt amounting to Rs.20,340 million, rose by 12 per cent in 1996 compared to a 31 per cent increase in the previous year. The heavy dependency on Rupee Securities for financing the fiscal deficit at a higher interest rate has contributed to the high interest cost on medium and long-term debt in recent years. The high interest rates that prevailed in the Treasury bill market directly pushed up the interest rate structure on medium and long-term Rupee Securities as higher interest rates were necessary to absorb resources especially from non-captive sources.