

## 2. NATIONAL INCOME AND EXPENDITURE

### 2.1 Overall Trends

In 1999, Gross Domestic Product (GDP), in real terms, grew by 4.3 per cent compared with 4.7 per cent in 1998. Recovering from a low growth rate of 3.8 per cent in 1996, the annual average growth rate during 1997-99 reached 5.1 per cent. The economy sustained an annual growth rate of around 5 per cent during the last decade. Economic activities slowed down in the first half of the year, with a growth rate of 3 per cent, but picked up during the third quarter recording a growth rate of 4 per cent, responding strongly to growth in external demand. In the fourth quarter, GDP growth reached 6.9 per cent indicating further consolidation of progress towards a higher growth path. Manufacturing industry fared better during the latter part of the year with export oriented industries regaining their competitiveness with the gradual appreciation of the exchange rates of East Asian countries, along with their economic recovery.

Better co-ordination of overall economic policies in recent years has improved macroeconomic fundamentals and sustained a low inflationary growth momentum despite a volatile external environment and difficult domestic conditions. Prudent monetary management coupled with fiscal discipline helped to contain inflation to less than 5 per cent in 1999. The continuous decline in the rate of inflation since the fourth quarter of 1998 resulted in a gradual propagation of low inflation expectations, reducing pressures on interest rates and exchange rates. Declining interest rates, in association with low inflation, created a climate more conducive to investment and thus encouraged private sector investment. Low inflation has also helped to maintain real exchange rates at more realistic levels, thereby boosting the export sector.

Meanwhile, structural reforms adopted by the government in recent years have further augmented economic activities. These reforms included continuous privatisation, adoption of a goods and services tax, rationalisation of import tariffs and reduction of tax rates and financial sector reforms. Productivity growth and capacity expansion were evident in the recently privatised plantation and telecommunications sectors. Productivity growth emerging from the wider use of telecommunication and information technology has helped to enhance value added in the manufacturing and service sectors. Financial sector reforms have helped to attain greater efficiency and stability in domestic financial markets.

Increased investments led to output expansion in the transport, communication and utility sectors. In 'Investment Profile for 2000 – 2004', high priority has been given to

developing economic and social infrastructure. About one half of public investment was earmarked for the modernisation of telecommunications, ports, power and highways. Increased private sector participation in infrastructure development is also envisaged. Output in banking and other financial institutions also continued to grow during the year helped by ongoing financial sector reforms. The contribution of the tourist sector to growth was significant during the year.

The agriculture sector performed well in 1999 as the combined outcome of shifting cultivation to crops with higher comparative advantage, in parallel with trade liberalisation, better plantation management under privatisation, improved cultivation practices and more efficient distribution systems. The agriculture sector has continued to change from subsistence production to high value-added products based on improved technology and rational cultivation practices. This process will lead to the commercialisation of agriculture and to the development of agro-processing and agro-business activities. In order to promote these activities further, the Central Bank recently introduced the 'Govi Sahanaya' scheme under which farmers were encouraged to enter into forward contracts with buyers at a pre-determined price. This scheme is expected to reduce the volatility of farmer incomes and to promote agro-business and agro-processing enterprises.

A significant development in recent years has been the continuing output expansion in informal sector activities. Small and medium enterprises (SMEs) in the informal sector have expanded rapidly in the context of a liberalised economic framework, resulting in increased employment generation. The expansion was notable in small-scale enterprises in light engineering, catering services, manufacturing of bricks and tiles, automobile maintenance, air conditioning, computer hardware and software development, retail trade, personal services and landscaping.

In 1999, value added in real terms increased in Agriculture (4.5 per cent), Mining and quarrying (4.1 per cent), Manufacturing (4.4 per cent), Construction (4.8 per cent) and Services (4 per cent). The agriculture sector, which was responsible for 12 per cent of the increase in GNP in 1998, accounted for 25 per cent of the growth in 1999. The contributions of the Manufacturing, Construction, Mining and quarrying sectors were 20 per cent, 9 per cent and 2 per cent, respectively. The Wholesale and retail trade sector accounted for 6 per cent of the overall growth in 1999 when compared to 22 per cent in the previous year.

Gross National Product (GNP), defined as the GDP adjusted for net factor income from abroad (NFIA), grew

by 3.8 per cent in 1999 compared with 4.6 per cent in 1998. This was mainly due to a reduction of US dollars 47.2 million in investment income receipts and an increase of US dollars 6.5 million in interest payment on foreign debt in 1999.

GDP at market prices is estimated to be around Rs. 1,111 billion. Accordingly, the GDP per capita is estimated at US dollars 829 in 1999. Gross Domestic Capital Formation (GDCF) is estimated to be Rs.302 billion, an increase of 18 per cent over 1998. Accordingly, the ratio of investments to GDP is estimated to have increased to 27.1 per cent in 1999 from 25.1 per cent in 1998.

Both private and public investment increased, supported by faster growth in infrastructure development and foreign direct investments. Public investment was mainly for the modernisation of telecommunications, ports, power and highways that enhanced the productivity in major economic sectors, while private investment was in housing construction, aviation, telecommunications and LP gas.

## 2.2 Sectoral Performance

The Agriculture sector grew by 4.5 per cent in 1999, the highest growth achieved since 1993. This was mainly due to the increased production in paddy, coconut, vegetables and fisheries. Overall, the improved performance of agricultural activities was well reflected in stable domestic food prices, mitigating the inflationary pressure in the economy. The combined paddy production in the 1998/99 Maha season and 1999 Yala season is estimated at 2,868 thousand metric tons, an increase of 6.6 per cent over the previous year. This is the highest production ever recorded. An increase in the average yield in the Maha season, as well as an increase in the extent harvested by 29 per cent in the Yala season, contributed towards the overall improvement. Output in the 'Other agriculture' sub-sector, largely consisting of vegetables, subsidiary food crops, minor export crops and animal husbandry, increased by 3.4 per cent in 1999, contributing almost one third of the growth in the agriculture sector. Vegetable production grew by 6.4 per cent, partly due to a shift to vegetable cultivation from potatoes and chillies, which have become less remunerative under the present trade policy regime. Output in the subsidiary food crops sub sector grew by 1.3 per cent supported by a bumper big onion crop and an increase in the production of red onions in the Yala season. Meanwhile, the performance of the animal husbandry sub-sector was mixed, with eggs and poultry production increasing, while milk production received a setback due to intermittent disruptions to milk collection by the major milk processing factories.

The plantation sector as a whole performed well in 1999. Continuing the upward trend recorded during last few years, tea production reached a new high level of 284 million kg surpassing the previous year's output by 1.3 per

cent. This was due mainly to improved management under private companies and better cultivation practices. Favourable weather conditions that prevailed throughout the year in tea growing areas also contributed to increase production. Rubber production, which dropped continually after 1996, improved marginally in 1999. Rubber prices showed a slight recovery during the last quarter of the year. Coconut production grew by 9 per cent, recording the highest production since 1986. Increased fertiliser application and the lagged effect of favourable weather conditions that prevailed in the previous year mainly contributed to this growth.

Fisheries production is estimated to have grown by 7.6 per cent, with both marine and inland fish production continuing to grow. The expansion in infrastructure for marine fisheries under the public investment programmes and the expansion in the fleet of mechanised boats through continuing investments by the private sector contributed to the growth in this sector.

Output in the Manufacturing sector grew by 4.4 per cent in 1999, compared with 6.3 per cent in 1998. The slower growth was largely due to a decline in foreign demand during the first half of the year as a result of the depressed world economic conditions. This had an adverse impact on several industries, mainly rubber and leather products, ceramic-ware and jewellery. Reflecting the recovery of industrial exports, the performance in most industrial categories was better during the second half of the year. The apparel industry recorded growth of 6.9 per cent compared to 4.5 per cent in 1998, largely due to greater diversification into non-quota items and expansion in the production of higher value-added items. Non-metallic mineral products also grew at a faster rate compared to the previous year due to substantial growth in the output of building materials and diamond processing, where the export demand has recovered.

The processing industries of tea, rubber and coconut kernel products grew by 3.8 per cent. The impetus to the growth in the processing industry came from an increase in output of desiccated coconuts by 43 per cent over the previous year. The small industry sub sector grew by 4.8 per cent with the expansion in assembly of computers and communication equipment, light engineering and rice milling.

The Construction sector recorded a growth rate of 4.8 per cent in 1999, compared to the growth of 7.1 per cent in 1998. The growth in this sector was mainly attributed to incentives given in the 1998 Budget encouraging private sector participation in housing construction and other infrastructure development projects in the country. Further, the state sector housing programme, implemented by the National Housing Development Authority (NHDA), showed significant progress especially in the Jana Udana and rural

**TABLE 2.1**  
**Sectoral Composition and Increase in Gross National Product at Constant (1996) Prices**

Sector	Rate of Increase		Contribution (%) to Change in GNP		Percentage Share of GNP	
	1998(a)	1999(a)	1998(a)	1999(a)	1998(a)	1999(a)
1. Agriculture, Forestry and Fishing	2.5	4.5	11.9	25.2	21.5	21.7
Agriculture	1.8	4.4	6.6	19.1	16.8	16.9
Tea	1.1	1.3	0.4	0.5	1.5	1.4
Rubber	-9.0	1.0	-1.0	0.1	0.5	0.4
Coconut	-3.2	9.1	-1.3	4.0	1.7	1.8
Paddy	18.3	6.6	11.9	5.9	3.4	3.5
Other	-1.5	3.4	-3.4	8.6	9.8	9.7
Forestry	1.2	1.3	0.5	0.7	2.0	1.9
Fishing	8.3	7.6	4.8	5.5	2.8	2.9
2. Mining and Quarrying	-5.4	4.1	-2.3	1.9	1.8	1.8
3. Manufacturing	6.3	4.4	22.9	19.7	17.1	17.2
Processing of Tea, Rubber & Coconut Kernel Products	-1.2	3.8	-0.6	2.1	2.2	2.2
Factory Industry	7.6	4.5	21.7	15.9	13.6	13.7
Small Industry	6.5	4.8	1.8	1.6	1.3	1.3
4. Construction	7.1	4.8	10.7	8.9	7.1	7.2
5. Electricity, Gas, Water and Sanitary Services	10.1	9.5	3.0	3.5	1.4	1.5
6. Transport, Storage and Communications	7.7	8.1	18.2	23.8	11.3	11.8
7. Wholesale and Retail Trade	4.5	1.0	21.7	5.7	22.5	21.9
Imports	8.2	-1.4	17.0	-3.6	10.0	9.5
Exports	0.1	6.1	0.1	3.8	2.4	2.5
Domestic	2.0	2.1	4.6	5.5	10.1	10.0
8. Banking, Insurance and Real Estate	6.4	4.6	10.2	9.1	7.6	7.7
9. Ownership of Dwellings	1.2	1.2	0.5	0.6	1.9	1.9
10. Public Administration and Defence	3.0	4.2	3.3	5.4	5.0	5.0
11. Services (n.e.s.)	3.7	9.8	3.2	10.1	4.0	4.2
12. G.D.P.	4.7	4.3	103.2	113.9	101.3	101.8
13. Net Factor Income from Abroad			-3.2	-13.9	-1.3	-1.8
14. G.N.P.	4.6	3.8	100.0	100.0	100.0	100.0

(a) Provisional

Source: Central Bank of Sri Lanka

housing programmes in 1999. Accordingly, loans granted for housing construction by credit institutions showed significant increases. Growth in the construction sector accelerated during the second half of the year as indicated by the significant rise in the sale of building construction materials such as cement, asbestos, steel, PVC and roofing materials.

The Mining and quarrying sector, which declined by 5.4 per cent in the previous year, grew by 4.1 per cent in 1999. Gem mining, which was badly affected by the East Asian crisis, has picked up since the second half of the year responding to the recovery in export demand from these countries. This recovery was partly offset by lower production of mineral sands, due to slow movement in exports to Japan. The quarrying sub-sector grew by 4.8 per

cent due to continuous expansion in construction activities, which have stimulated the demand for major quarrying products such as sand, metal stones, lime, and clay bricks and roofing tiles.

Output in the Transport, storage and communication sector, which increased by 7.7 per cent in the previous year, grew by 8.1 per cent in 1999, maintaining the growth momentum registered in recent years. The impetus to growth in this sub sector came mainly from telecommunications, which alone grew by 39.2 per cent and contributed 26 per cent of sectoral growth. While transport and port services registered a slower growth, the strong growth performance of the telecommunications sector in 1999 was sufficient to offset the decline in the other two sub-sectors and to maintain the growth momentum.

**TABLE 2.2**  
**Composition of the Other Agriculture Sub Sector**

Sector	Value Added (1996) Constant Prices (Rs.Mn.)		
	1997(a)	1998(a)	1999(a)
Vegetables	31,676	33,126	35,234
Subsidiary Food Crops(b)	18,501	15,577	15,871
Minor Export Crops (c)	7,874	7,825	7,666
Sugar cane	1,203	1,202	1,281
Tobacco	1,553	1,569	1,484
Animal Husbandry (d)	6,293	6,560	6,597
Other	8,763	8,837	9,192

Source :Central Bank of Sri Lanka

(a) Provisional

(b) Subsidiary food crops mainly include potatoes, chillies, red onions, big onions, green gram, cowpea and kurakkan

(c) Minor export crops mainly include coffee, pepper, cinnamon, cloves, cashew nuts and betel leaves.

(d) Animal Husbandry comprises milk, eggs, poultry and other meats.

The number of subscribers under Sri Lanka Telecom (SLT) and private operators registered significant increases in 1999. SLT was able to provide around 133,700 new telephone lines in 1999. The number of subscribers for cellular phones increased by 47 per cent while that for wireless local loop telephones grew by 35 per cent. Accordingly, telephone density (the number of fixed phones per 100 persons) increased by 26 per cent from 2.79 in 1998 to 3.52 in 1999. These improvements were possible with substantial capital investments and new development projects handled by SLT and private sector operators. In addition, the quality of services in the industry improved with the application of new technology and increased competitiveness among service providers. The number of applicants on the waiting list for SLT telephone facilities indicates that this industry has potential to grow further in the coming years. Meanwhile, current expansion projects in the telecommunications sector jointly handled by the Japan Bank for International Cooperation and SLT, aim to provide universal telecommunication facilities, emphasizing the rural sector of the country. Postal services also improved during the year, with the expansion of the post office network and service quality.

Port services grew marginally, by 1 per cent, indicating a decelerating trend in 1999. The volume of cargo handled grew by 1 per cent, while handling of trans-shipments decreased by 3 per cent. The total revenue of all ports, which grew by 24 per cent in the previous year, remained unchanged in 1999. Competition from neighbouring ports and shrinkage of regional trading activities have threatened the growth of port activities. Currently, the Sri Lanka Ports Authority is implementing several projects to enhance productivity and expand port facilities to meet this challenge. The North Pier development project (Phase II) in the Colombo Port, construction of a new jetty in the Port of Galle, construction of a new pier in Trincomalee harbour and the Queen Elizabeth Quay (QEY) project, which began in 1998 with private sector participation, are notable among them.

The transport sub sector, which includes road, rail and air services, grew by 2.9 per cent in 1999. The expansion in road transport services is largely in response to expansion in the Agriculture, Manufacturing and Construction sectors leading to an increase in the demand for goods transportation. Growth in air transportation was due to increased tourist arrivals in 1999. The number of passenger kilometers flown by SriLankan Airlines increased to 5,145 million in 1999 from 4,155 million in 1998.

The Banking, insurance and real estate sector grew by 4.6 per cent as compared to 6.4 per cent in 1998. The deceleration in the growth in value-added in the banking sector is attributed to a slowing down in wholesale and retail trade, in particular, and slowing down in the economy, in general. Activities in the insurance and leasing sub sectors expanded considerably in 1999.

The Wholesale and retail trade sector, the third largest sector, which 22 per cent of GNP, grew at 1 per cent in 1999 when compared to 4.5 per cent in 1998. The slow growth was mainly due to reduced imports. The volume of import trade was estimated to have fallen by 1.4 per cent in 1999. The export sub sector picked up during the second half of 1999 and grew by 6.1 per cent in 1999. The significant deceleration in trade negatively affected the profitability of the commercial banking and road haulage sub sectors, lowering the overall economic growth. The volume of exports in all three major categories of exports, i.e., agricultural, industrial and mineral, expanded. Gem exports, the dominant category in mineral exports, grew by 22.9 per cent, mainly due to increased demand from East Asian countries and Japan.

Value added in the import trade decreased by 1.4 per cent in 1999, compared with a growth of 8.2 per cent in the corresponding period in 1998. While imports of consumer goods and intermediate goods declined by 0.3 per cent, and 0.5 per cent respectively, imports of investment goods recorded an increase of 6 per cent in 1999. The latter includes the value of three aircraft worth US dollars 298 million imported under the re-fleeting programme of SriLankan Airlines. Excluding aircraft, import expenditure on investment goods declined by 14.2 per cent.

The expansion in activities in the primary and secondary sectors of the economy contributed positively to domestic trade in 1999. In particular, significant increases in domestic trade pertaining to food commodities were evident during the year in line with increased agricultural output. This, coupled with better wholesale distribution facilities and market awareness programmes contributed considerably to contain the price increases in food items during the year. Domestic trade grew by 2.1 per cent.

The 'Other' services sector, which captures service activities not classified under major services, grew by 9.8 per cent in 1999 when compared to 3.7 per cent in 1998.

Increased private participation and greater diversification of economic activities were mainly responsible for the growth in this sector. Among the large number of sub categories in this sector, hotel services, computer software and data related services, advertising, and entertainment have been identified as the high growth sub-sectors.

Hotel related services registered a 16.4 per cent growth in real terms in 1999. This was due to the 15 per cent growth of tourist arrivals in 1999 coupled with a growing trend in domestic tourism. Household based catering services and fast food outlets also have expanded rapidly with changing consumer habits in recent years. Health services, especially in the private sector, indicated significant improvements during the year. This development was witnessed in the increased number of private hospitals and health clinics with both local and foreign private sector participation. The education sub sector is another area where private sector participation is growing rapidly. This sector as a whole has grown at a rate of 4.6 per cent. The organised private sector has recorded a major improvement with a real growth rate as high as 23.5 per cent. Over the last few years a large number of educational institutions have emerged with courses of study to meet increasing demand. Most of these are professional courses rather than academic. The most frequently criticised deficiency of the state education system is the mismatch of its output with the demand in the economy. Recent developments in the private sector educational services have filled this gap to some extent. That some students opt to follow professional courses at private expense rather than select university education at state expense is indicative of this trend. Another development observed in the services sector is the formalisation of some services with private sector participation. Private security and janitorial services are examples. These sectors grew at a rate of 10 per cent. Repair services of all types, ranging from household appliances to vehicles, are another expanding sector.

## 2.3 Expenditure

The aggregate demand generated by domestic economic activity is measured by Gross Domestic Expenditure (GDE), which is the sum of consumption and investment (Gross Domestic Capital Formation) expenditure of the private and public sectors of the economy. GDE was estimated at Rs.1,192 billion, reflecting an increase of 10.4 per cent over 1998.

Consumption expenditure is estimated at Rs.890 billion, an increase of 8 per cent over the Rs.823 billion registered in the previous year. Private consumption expenditure, which represents almost 90 per cent of overall GDE, recorded a growth of 9.1 per cent from Rs.724 billion in 1998 to Rs.790 billion in 1999. In 1998, the corresponding growth rate was 11.8 per cent. The deceleration was mainly due to slower growth in prices in 1999. Private consumption expenditure on imported goods and non-factor services registered an increase of 10 per cent, against a 15 per cent increase in 1998. Of the imported items, expenditure on food and consumer durable goods increased by around 10 per cent over the previous year, while expenditure on imported non factor services grew marginally. In the domestically produced goods category, expenditure on rice, coconut products, other food crops and fish improved considerably, mainly due to increased domestic production of these items. Expenditure on industrial goods recorded a growth of 8 per cent over the previous year, with the consumption of processed foods, clothing and plastic goods displaying a noteworthy increase.

Gross Domestic Capital Formation, is estimated have increased by 17.9 per cent to Rs.301 billion. Private sector investment, which comprised 88 per cent of total investment, grew at a faster rate of 20.2 per cent, while the increase in government investment was 5.6 per cent. Private sector investment was concentrated in the key sectors of industry, housing construction, transport and communications, while public investment focussed on

TABLE 2.3  
Total Resources and Their Uses at Constant (1996) Prices

Item	Percentage Share			Percentage Growth	
	1997(a)	1998(a)	1999(a)	1998	1999
1. Total Resources	100	100	100	6.8	5.2
GDP at Market Prices	69	67	67	4.7	4.3
Imports of Goods & Non-Factor Services	31	33	33	11.5	7.0
2. Utilisation	100	100	100	6.8	5.2
Consumption	59	59	58	7	5.3
Gross Domestic Fixed Capital Formation	16	17	18	15.3	6.4
Government	2	2	2	11.5	2.8
Private Sector & Public Corporations	14	15	16	15.9	7.8
Change in Stocks	0	0	0	-30.5	-45.9
Exports of Goods & Non-Factor Services	25	24	24	1.0	4.0

(a) Provisional.

Source: Central Bank of Sri Lanka

development and maintenance of economic infrastructure, such as roads, irrigation and water supply.

## 2.4 Availability and Utilisation of Resources

The total resources available to the economy, consisting of Gross Domestic Product and imports of goods and non-factor services (foreign resources), increased to Rs.1,583 billion in 1999 from Rs.1,448 billion in 1998. This increase of Rs.135 billion was generated by a Rs.93 billion increase in GDP at current market prices and a Rs. 42 billion increase in foreign resources. Of the total resources, 56 per cent was spent on consumption and 19 per cent on capital formation, while 25 per cent was used as exports of goods and non factor services.

The availability of resources valued at constant (1996) prices rose by 5.2 per cent in 1999 compared with an increase of 6.8 per cent in 1998. In 1999, consumption expenditure grew by 5.3 per cent, while Gross Domestic Fixed Capital Formation (GDFCF) increased by 6.4 per cent to Rs.237 billion.

## 2.5 Domestic and National Savings

Domestic savings are estimated as a residual, the difference between investment and external resources (defined as the net imports of goods and non-factor services). Domestic savings in 1999 were estimated at Rs.220 billion, 19.8 per cent of GDP, compared to 19.1 per cent in 1998. Increased corporate and household savings and a reduction in

government dis-savings contributed to higher domestic savings in 1999.

National savings, the sum of domestic savings, net foreign transfers and net factor income, rose to Rs.265 billion (23.9 per cent of GDP). Net private transfers, which consists mainly of workers' remittances from the Middle East, accounted for around one fourth of national savings in 1999.

**TABLE 2.4**  
**National Savings at Current Market Prices**

Category	Rs. Mn			
	1996(a)	1997(a)	1998(a)	1999(a)
1. Gross Domestic Product at Market Prices	768,128	890,272	1,017,986	1,110,653
2. Domestic Savings	117,691	154,237	194,735	220,423
3. Net Factor Income from Abroad	-11,258	-9,409	-11,556	-17,813
4. Net Private Transfers from Abroad	39,242	46,472	54,785	62,438
5. National Savings	145,674	191,301	237,965	265,048
6. Domestic Savings Ratio (2 as a % of 1)	15.3	17.3	19.1	19.8
7. National Savings Ratio (5 as a % of 1)	19.0	21.5	23.4	23.9

(a) Provisional

Source: Central Bank of Sri Lanka