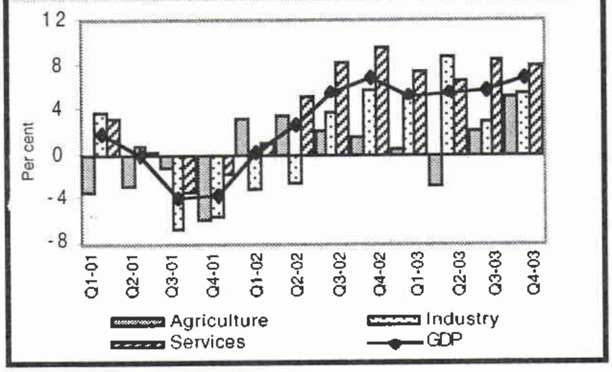
Chapter 2

NATIONAL INCOME AND EXPENDITURE

2.1 Overall Trends

In 2003, Gross Domestic Product (GDP) grew by 5.9 per cent, in real terms, continuing the recovery process that began from the second half of 2002. This growth was better than the growth of 5.5 per cent forecast for 2003 at the beginning of the year. The quarterly growth rates in 2003 were stable, in a range of 5.4 per cent to 6.9 per cent, the most stable quarterly growth rates during a year since the compilation of quarterly national accounts commenced in 1996. In comparison, the range in 2001 varied from –3.9 per cent to 1.8 per cent and in 2002, from 0.3 per cent to 7.0 per cent. Moreover, growth was recorded in all three major economic sectors throughout the year, with most sub sectors growing at a faster pace than in the previous year. These statistics reflected the stability and the predictability in economic activity that prevailed throughout 2003. They also emphasised the potential for longer-term sustainability of a broad based, stable economic growth trend in response to improved macro-economic fundamentals.

Chart 2.1
Quarterly Growth Rates



In 2002, the economy recovered from the recession experienced in 2001, and the growth was sufficient to regain the per capita income, in real terms, that had prevailed in 2000. By end 2003, per capita income had increased, in nominal terms, by nearly 10 per cent, which together with a GDP deflator of around 5 per cent reflected a real increase in per capita income of 4.6 per cent, signifying, on average, an improvement in living standards.

Two key factors supported the growth achieved in 2003. The first was the continuation of the ceasefire and the peace initiative which expanded economic activity by enabling comparatively free mobility of goods, services and labour throughout the entire country. The second was improved macroeconomic management, including prudent monetary management, greater fiscal discipline, and structural reforms, albeit with delays in some areas, that supported declining interest rates, a stable foreign exchange market, and falling inflation. This led to increases in both aggregate demand and supply through a rise in both consumer and investor confidence. In addition, favourable weather conditions, despite the severe floods experienced in May, also contributed to positive growth in agriculture and to an uninterrupted power supply throughout the year. The improving international economic environment also impacted positively on economic activity in 2003.

Meanwhile, in 2003, Gross National Product (GNP), defined as GDP adjusted for net factor income from abroad (NFIA), grew by 6.4 per cent in real terms, compared to a growth of 4.1 per cent in 2002. GNP growth in 2003 was higher than GDP growth by a greater margin than the historical pattern, due to the better performance of NFIA. NFIA, though remaining negative, improved by 26 per cent owing to receipts increasing at a higher rate than payments. Interest earnings improved in 2003 owing to the higher external reserves of the country compared with 2002, while improved reserves management also contributed to this increase.

The economic growth in 2003 was broad based. All three sectors, Agriculture, Industry, and Services, grew and contributed to overall economic growth. However, the Services sector dominated. Services activities grew by 7.7 per cent and contributed 70 per cent of growth. The resurgence of consumer confidence created demand for services such as trade; hotels, entertainment and related activities; communications; goods and passenger transport; financial and port services, all of which grew healthily. One exception was public administration and defence, following a policy decision to curtail expansion in the public sector unless considered essential as a part of the medium term fiscal consolidation strategy. The emergence of the Services sector as the fastest growing sector was not limited to Sri Lanka. In 2003, the Services sector provided the impetus for growth in most East Asian economies as well as in India. Meanwhile, the Industry sector, which grew by 1.0 per cent in the previous year, regained some of its growth momentum in 2003, with a growth of 5.5 per cent and a contribution of 25 per cent of the overall growth. This recovery in Industry also impacted positively on the Services sector, as the demand for related services increased. However, this growth was still

TABLE 2.1

Sectoral Composition and Increase in Gross Domestic Product at Constant (1996) Prices

Sector	Rate of Increase (%)		Contribution to Change in GDP (%)		Share of GDP (%)	
	2002(a)	2003(b)	2002(a)	2003(b)	2002(a)	2003(b)
1.Agriculture	2.5	1.5	12.7	5.0	19.8	19.0
1.1 Agriculture, forestry and fishing	2.5	1.5	12.7	5.0	19.8	19.0
Agriculture	1.9	3.0	7.5	7.7	15.1	14.7
Tea	5.1	-2.2	1.8	-0.5	1.4	1.3
Rubber	5.0	1.7	0.5	0.1	0.4	0.4
Coconut	-13.6	7.1	-5.3	1.5	1.3	1.3
Paddy	5.1	7.4	4.0	3.9	3.1	3.2
Other	2.9	1.8	6.6	2.7	8.9	8.6
Forestry	1.9	1.4	0.9	0.4	1.9	1.8
Fishing	6.3	-6.9	4.3	-3.2	2.7	2.4
2.Industry	1.0	5.5	6.6	24.9	26.6	26.5
2.1 Mining and quarrying	-1.1	3.6	-0.5	1.0	1.7	1.7
2.2. Manufacturing	2.1	4.4	8.8	12.4	16.6	16.4
Processing of tea, rubber and coconut kernel products	-0.9	2.2	-0.5	0.7	1.9	1.8
Factory industry	2.5	4.6	8.6	10.4	13.5	13.3
Small industry	2.1	6.1	0.7	1.3	1.2	1.2
2.3. Construction	-0.8	5.5	-1.5	6.4	6.9	6.9
2.4. Electricity, gas and water	-0.7	21.7	-0.3	5.1	1.4	1.6
Electricity	-1.5	25.3	-0.5	5.0	1.2	1.4
Water and gas	3.8	1.4	0.2	0.0	0.2	0.2
3.Services	6.1	7.7	80.7	70.1	53.6	54.5
3.1. Transport, storage and communication	7.6	10.2	23.8	22.1	12.8	13.3
Port services	2.4	10.8	0.5	1.4	0.8	0.8
Telecommunications	19.3	24.5	15.6	15.2	3.7	4.3
Transport	3.6	3.8	7.7	5.4	8.4	8.2
3.2. Wholesale and retail trade	5.6	7.3	29.5	26.3	21.3	21.6
Imports	8.4	11.2	19.1	17.8	9.4	9.9
Exports	2.0	3.5	1.3	1.5	2.5	2.4
Domestic	3.9	4.4	9.2	7.0	9.4	9.3
3.3. Banking, insurance and real estate	11.1	10.6	23.2	15.9	8.9	9.2
Banking	17.7	15.3	14.9	9.7	3.8	4.1
Insurance, real estate and other financial services	6.6	7.1	8.3	6.2	5.1	5.1
3.4. Ownership of dwellings	1.5	1.3	0.7	0.4	1.8	1.7
3.5. Public adminnistration and defence	0.0	0.6	0.0	0.5	4.8	4.5
3.6. Services (n.e.s.)	3.4	7.2	3.5	5.0	4.1	4.1
Hotels and restaurants	-1.1	22.0	-0.2	2.1	0.6	0.6
Other	4.1	4.8	3.7	2.9	3.5	3.5
4.Gross domestic product (1+2+3)	4.0	5.9	100.0	100.0	100.0	100.0

(a) Revised
(b) Provisional

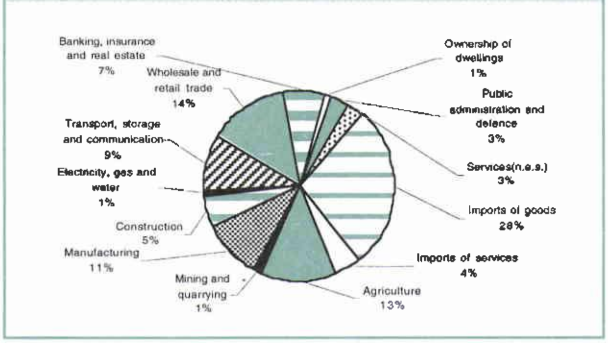
Source : Central Bank of Sri Lanka

below the average growth rate of the Industry sector prior to 2001. The Agriculture sector grew by 1.5 per cent. This sector, which contracted by 3.4 per cent in 2001 under adverse weather conditions, recorded a growth of 2.5 per cent in 2002. This growth in 2003 confirms full recovery of the Agriculture sector from the contraction in 2001. However, this also shows that growth in this sector has not achieved the dynamism of the other two sectors, and continues to lag behind due to inherent rigidities.

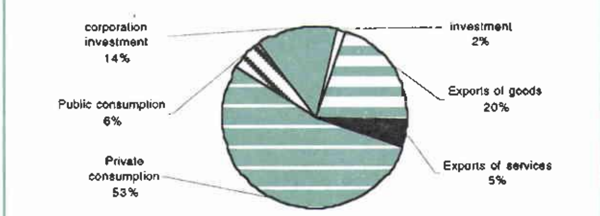
On the expenditure front, GDP at current market prices was estimated at Rs. 1,760 billion, in 2003, compared with Rs. 1,583 billion in 2002, recording an increase of 11.2 per cent in nominal terms. The increase in real economic activities was 5.9 per cent, while the increase in the general price level, as measured by the GDP deflator, was 5.0 per cent in 2003 in comparison to 8.4 per cent in 2002. The comparatively lower level of inflation was achieved through the increase in local production to meet the higher demand and improved macroeconomic stability. The declining trend in inflation was also reflected in all other price indices. Accordingly, GDP per capita for 2003 is estimated at Rs. 91,434, an increase of 9.8 per cent over the previous year's Rs. 83,267. This indicates an improvement in living standards, on average, as the growth in per capita income surpassed the increase in inflation. In US dollar terms, per capita GDP increased by 8.8 per cent, from US dollars 870 to 947. In comparison, in 2002, the per capita GDP in US dollar terms increased by 3.5 per cent, while it declined by 6.4 per cent in 2001. The high increase in 2003 was the combined outcome of comparatively higher economic growth and stability in the external value of the rupee against the US

Chart 2.2
The Economy in 2003 (at Current Prices)

Supply of Goods and Services (Rs. 2,506 billion)



Demand for Goods and Services (Rs. 2,506 billion)



dollar. The higher demand for services also reflects that with the rise in per capita income, on average, a relative share of consumer expenditure is shifting away from goods to satisfy basic needs such as food and clothing to consumer expenditure on services of their choice.

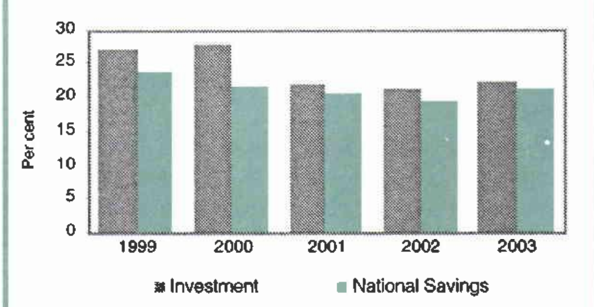
GDP at market prices, when estimated by the expenditure approach, reflects the total demand in the economy comprising both domestic and external demand. Domestic demand, (consumption plus investment demand) rose by 10.9 per cent at current market prices. In 2002, the corresponding increase was 13.1 per cent. However, with the decline in inflation, real domestic demand grew at a higher pace in 2003 than in 2002, indicating an increase in real purchasing power in the economy.

The recovery in 2002, from the first ever economic contraction in 2001, was driven by consumer confidence. The cessation of hostilities and the resultant peaceful environment that prevailed in the country paved the way for consumption driven growth. Of the overall growth in domestic demand of 6.6 per cent in 2002, nearly 80 per cent came from the increase in consumption expenditure. The investors' response was not as rapid and it was evident that investors were awaiting firmer signals on the success of the peace process during 2002, and the expected growth in investor confidence was seen by the second half of 2003.

The growth in consumer confidence that was seen in 2002 continued in 2003 as well, but at a somewhat slower pace. The total consumption expenditure, which includes private and government consumption expenditure, increased in current terms, by 9.6 per cent. This increase was solely due to the 10.7 per cent expansion in private consumption expenditure (PCE), which represents around 91 per cent of the total. Government consumption expenditure continued to decline, though marginally, due to commendable fiscal consolidation efforts. Total consumption expenditure in real terms grew by 6.1 per cent exceeding the real economic growth. The ceasefire throughout the country was the primary factor that enhanced the demand for goods and services. The increase in domestic production, declining inflation, and falling interest rates further encouraged consumer demand. Increases in domestic agricultural income owing to the higher production also raised the demand for consumer durables in 2003. The increase in imports of consumer goods by 12.5 per cent, in volume terms, in agricultural production that caters to the domestic market and in domestic market oriented industries also reflected higher consumer expenditure, in real terms, in 2003. In real terms, PCE grew by 7.3 per cent, against a population growth of 1.3 per cent, indicating an improvement in living standards. Consumption expenditure was responsible for 58 per cent of the 8.4 per cent growth in domestic demand in 2003.

Investment expenditure (Gross Domestic Capital Formation) at current market prices, which increased by 9.1 per cent in 2002, increased further by 16.3 per cent in 2003. In real terms, the investment expenditure rose by 17.0 per cent, whereas the corresponding growth in 2002 was 6.7 per cent. The higher growth in investment in real terms in 2003, compared to current terms, reflects the decline in the prices of investment goods in 2003 compared with 2002. The real growth compared to 2002 was reflected in many sectors and confirmed that the investment climate, which had lagged behind consumption earlier, had improved significantly by 2003. The Investment/GDP ratio had fallen from 28.0 per cent

Chart 2.3
Investment and Savings Ratio



in 2000 to 22.0 per cent in 2001. In 2002, though the economy grew by 4.0 per cent, the investment ratio declined further to 21.3 per cent, signifying the delay in investment decisions. Another factor that delayed new investment in 2002 was the excess capacity that existed in most economic sectors. This trend reversed in 2003 and the investment ratio rose to 22.3 per cent, confirming growing investor confidence. The turnaround in investment was mostly observed in the second half of the year as indicated by a sustained growth in private sector credit and a noticeable increase in the imports of investment goods during that period. However, the investment ratio is still below the level of 24 per cent initially projected for 2003 at the beginning of the year. The under-performance of capital formation was due to two major reasons. First, certain key economic sectors (e.g. export manufacturing and tourism) still performed at below existing capacity so that there was no immediate need for new investments in these sectors. Second, though the cessation of hostilities continued and a peaceful environment prevailed throughout the country, investors adopted a 'wait and see' policy to make investment decisions due to uncertainties that prevailed in both the peace process and the political environment. An investment level of 22.3 per cent is not sufficient to achieve the long-term envisaged growth of over 8 per cent that would be required for a sustainable improvement in living standards. In the long-run, the speedy implementation of power capacity expansion, labour market and land market reforms, further deregulation to reduce administrative bottlenecks, and further improvement in policy consistency are crucial to convert increasing investor confidence into real investment activity.

On the resource side, domestic savings, the sum of private and government savings, were estimated at Rs. 277 billion, an increase of 20.9 per cent, in nominal terms. In 2002, the corresponding increase was 3.3 per cent. As the increase in domestic savings exceeded that in GDP, the domestic savings/GDP ratio rose to 15.7 per cent in 2003 from 14.5 per cent in 2002. Both the private sector and the government sector contributed to the improvement. Private savings increased by 12.4 per cent, in nominal terms, while the private savings ratio, which was 18.8 per cent, improved to 19.0 per cent. Of the private savings, corporate sector savings increased due to better performance during the period. However, household sector savings declined due to higher consumer expenditure throughout the period. Government dis-savings, which improved marginally to 4.4 per cent of GDP in 2002 after rising drastically during the previous two years, improved to 3.3 per cent of GDP in 2003, due to continuation of prudent budgetary policies. The Fiscal Management (Responsibility) Act, that was passed in Parliament at end 2002 and stipulated a medium term fiscal strategy for reduction of the budget deficit to 5 per cent of GDP by 2006, impacted on the improvement in government dis-savings. The national savings ratio also increased from 19.5 per cent to 21.3 per cent. The gap between domestic savings and national savings widened in 2003, compared with 2002, due to the improvements in NFIA and increase in net private transfers from abroad by 10.8 per cent. The resource gap, the investment – national savings gap as a ratio of GDP, stood at 1.0 per cent. Despite this moderate gap, the low levels in investment and savings that remained below the projections made at the beginning of the year, despite improvements over 2002 levels, raise concerns, as they are inadequate to achieve the expected high growth in the future.

2.2 Sectoral Performance

Services Sector

The Services sector grew by 7.7 per cent contributing 70 per cent of overall growth. The recovery in economic activity that began from the second half of 2002 was driven by the growth of the Services sector. The Services sector had two advantages over the other two sectors. First, the demand for service activities such as trade, transport, tourism, financial services, port services and communication, increased at a higher rate, in the context of growing consumer confidence with the continuation of the ceasefire, than the demand for goods. Second, the economy was able to cater to this growing demand within existing capacity.

The faster growth of services sector and its continuously rising share in GDP in Sri Lanka are consistent with the usual development process of a country. The initial stages of economic development require a firm structural foundation to be laid by agriculture and industry. However, at the next stage, an efficient services sector is required to link production, distribution and consumption together, by lowering transaction costs and improving efficiency, while raising the quality of life of people, by enhancing their choices and increasing convenience. Hence, the dominance of the Services sector usually moves in tandem with a country evolving from low-income to high-income. In particular, as Sri Lanka has a low natural resource base, the magnitude and pace of future economic growth will rely heavily on the Services sector, as has been observed in the recent past.

Value added in the Transport, storage and communication sector increased by 10.2 per cent in 2003, compared to 7.6 per cent in 2002. This increase was largely due to the expansion in the telecommunication subsector by 24.5 per cent. The Fixed Access-Wireless Local Loop subscriber levels grew by 1.3 per cent, in comparison to a 3.8 per cent drop in 2002. The growth in the telecommunication sector was mainly driven by the upward trend in mobile phone usage that increased by 54 per cent. A growth of 21 per cent in Internet and e-mail users was recorded. The growth in the telecommunication sector was augmented by the growing demand from the Northern and the Eastern provinces for communication services, following the ceasefire.

The transport subsector, one of the largest service sectors in the economy, grew by 3.8 per cent as against 3.6 per cent in the previous year. This increase was the outcome of the combined performance of passenger and freight transport. Road haulage grew by 4.4 per cent reflecting the expansion in goods transport activities with the opening and greater use of roads to the North and the East following the ceasefire, the increase in domestic production and in international trade. During 2003, passenger kilometres operated by Sri Lanka Railways increased by 4.4 per cent as compared with 2.5 per cent in 2002. In comparison to the negative growth of 5.7 per cent in passenger kilometres flown by Sri Lankan Airlines during 2002, an increase of 12.1 per cent was recorded in 2003. In the public transport category, the growth performance in the private bus category improved, while that of Sri Lanka Transport Board contracted. The use of taxis, hired vans and three wheelers has also increased. These improvements in the transport sector were also reflected in the significant increase in imports and registration of motor vehicles during 2002 and 2003.

Port services recorded a growth of 10.8 per cent in 2003 as against 2.4 per cent in the previous year. The Port of Colombo including the South Asia Gateway Terminal (SAGT) handled a record volume of 1.96 million TEUs in 2003, up 10.8 per cent compared with the container throughput of 1.76 million TEUs in 2002. This was the highest container volume handled by the port and was a significant achievement when compared with stagnation in throughput levels during the last five years. Transshipment volumes, which usually account for two-thirds of throughput and experienced negative growth during the last five years except in 2002, recorded a growth of 12.2 per cent in 2003. The Colombo Port's success in 2003 was mainly driven by the Jaye Container Terminal (JCT). Of the total container throughput of 1.96 million TEUs, 68 per cent (or 1.33 million TEUs) was handled at JCT. JCT recorded a growth of 10.6 per cent in total container handling and 14.2 per cent in transshipment container handling. This high growth reflects steps taken by the SLPA to enhance productivity such as a voluntary retirement scheme introduced for surplus workers, 24-hour work arrangements and incentive payments. Also, marketing strategies followed by the SLPA were able to attract new shipping lines to provide services on a continuous basis to the Port of Colombo.

The Wholesale and retail trade sector, the largest sector in terms of value added, grew by 7.3 per cent. The growth was largely due to the improved performance of the import trade subsector, which grew by 11.2 per cent. This subsector, which suffered a severe setback in 2001, recovered in 2002 owing to the increase in domestic demand. This trend continued in 2003 with the continuation of consumer confidence that prevailed throughout the year and revival in investor confidence by the second half of 2003. The import of investment goods increased in 2003 by 28.7 per cent, in volume terms, while that of consumer goods increased by 12.5 per cent. The volume of intermediate goods imports also grew by 4.1 per cent, mainly driven by raw material imports for industries catering to the domestic market. The decline in the international prices of investment goods, by 11.7 per cent on average, also stimulated the importation of investment goods. Of consumer goods imports, imports of basic food items, such as rice, wheat grain and sugar, declined in the light of the increases in domestic production of rice and sugar, and substitution effects. Imports of other consumer goods, such as motor vehicles and household goods, grew by 25.3 per cent. The domestic trade subsector, defined as the trading of domestically produced and traded goods, grew by 4.4 per cent. This growth was stimulated by the increase in consumer confidence, higher domestic production and low level of inflation. The export trade subsector, which suffered a setback of 8.0 per cent in 2001 and then grew by 2.0 per cent in 2002, grew by 3.5 per cent in 2003. Exports of agricultural products grew by 5.5 per cent, led by the recovery in coconut products exports by 24 per cent. Industrial products exports grew by 3.1 per cent. Among industrial exports, the textiles and garments sector, which accounts for around 67 per cent of this category, grew modestly by 2.5 per cent. Meanwhile, all other industrial exports, which accounted for 30 per cent of industrial exports excluding petroleum, performed better, and grew by 5.3 per cent. Both exports and imports performed better than the projections for 2003 made at the beginning of the year.

The Banking, insurance and the real estate sector recorded the highest growth of 10.6 per cent. The growth in the banking sector by 15.3 per cent was mainly responsible. Interest income in the banking sector, which still covers over 80 per cent of the total income of that sector, remained constant at the previous year's level. However, interest expenses dropped by 16 per cent, under declining interest rates, enhancing the net interest earnings of the banking sector. This further reflects the downward rigidity in lending rates in the banking sector in Sri Lanka, clearly implying that the pass-through to investors, in particular, and the economy in general, of the advantages of lower interest rates, is slow. Meanwhile, non interest income in the banking sector, in current terms, increased by 27 per cent. Increased profits from activities in the foreign exchange market and increased commissions and brokerage income from fee-based activities were the main reasons for this increase. The licensed specialised banking sector gained mainly from securities sales in the context of the buoyancy in the stock market throughout most of the year. The insurance, real estate and other financial services sector also grew healthily by 7.1 per cent, reflecting the continuing demand for such services, which recorded a 6.6 per cent growth in 2002 as well.

The Services (n.e.s.) category, which includes all other unclassified services such as private education, health, hotels and restaurants, advertising, private security, janitorial services, personal services and all other business services, grew by 7.2 per cent. This was mainly due to enhanced activities in the hotels and restaurants services, as well as other subsectors, such as advertising and motor and electrical repairs, albeit to a lesser degree. Hotels and restaurants services expanded significantly with the increase in tourist arrivals mainly from Western Europe and Asia. In 2003, tourist arrivals increased by 27.3 per

Box 6

The Rising Importance of the Services Sector: A Natural Outcome of the Development Process

Introduction

The faster growth and rising share of the Services sector in the GDP of a country, in tandem with the increase in per capita income, has been observed in the development process of developed as well as developing countries. Moreover, in countries like Sri Lanka, with a limited natural resource base, the rising dominance of the Services sector in economic activity is also a natural outcome of the need for creating more income-earning opportunities against the rising population and dwindling land areas for agriculture. Today, the Services sector in Sri Lanka generates more than half the GDP and provides employment for three million people, 43 per cent of the total employed. In comparison, the Industry and Agriculture sectors contribute 27 per cent and 19 per cent, respectively, to the GDP, and together supply another 4 million jobs in the country.

Historical Progress

At Independence, at that early stage of her development process, Sri Lanka was heavily dependent on agriculture in terms of output and employment. The Agriculture sector consisted mainly of three export commodities, tea, rubber and coconut, and the production of paddy. The latter provided a livelihood for a significant proportion of the population in the country who lived in rural areas. The Agriculture sector contributed nearly one half of the GDP and employed more than 40 per cent of the labour force in the country. The share of the Industry sector was less than 20 per cent of GDP and it was mainly confined to the processing of the major agricultural crops and to a few medium sized industrial plants producing basic needs such as cement, textiles and soap and small scale traditional industries such as handicrafts and ropes, nets and brick making that catered to rural economic needs. Even at that stage, Services sector activities were responsible for nearly two fifths of the GDP and largely comprised banking and insurance and trade and transportation, activities that had developed in parallel with the expansion of the export-led plantation agriculture in the country.

After Independence, as the country developed from a low-income economy, the economic structure underwent transformation to meet the emerging needs of a developing economy with a low natural resource base. The share of the Agriculture sector in terms of both output and employment declined, while those of Industry and Services rose, the latter growing at a faster pace. In 2003, the Industry sector was responsible for over one fourth of the GDP and 22 per cent of total employment, while more than half of GDP and 43 per cent of employment were generated by the Services sector. While both exports and imports increased in volume terms, their composition changed to meet the needs of the diversified economy. The relative shares of industrial products in exports and intermediate and investment goods in imports rose over time to displace primary agricultural commodities as the main component of exports and consumer goods as the main component of imports. Meanwhile, per capita income increased from US dollars 120 in 1950 to US dollars 947 in 2003, growing by 4 per cent per year, on average.

TABLE 1
Structure of the Economy in Sri Lanka

Period	Agriculture (%)	Industry (%)	Services (%)
1951 - 1960	42	17	40
1961 - 1970	35	18	47
1971 - 1980	29	27	44
1981 - 1990	27	27	46
1991 - 2000	23	27	50
2001 - 2003	20	26	54

Source: Central Bank of Sri Lanka

In the early period after Independence, development of the Agriculture sector had been given very high priority. At a later period, Services sector activities such as trade, transport, telecommunication and postal services and banking and other financial services had been dominated by state monopolies, causing a reduction in efficiency and thereby the sectoral growth rates. The Services sector had further been affected by exchange controls, nationalisation of private businesses, high taxes and complex tariff structures. With rationing and control systems, consumer choices had been supplanted by community choices effected through planners' preferences. These restrictions on Services sector growth not only reduced overall growth and income generation, but also weakened the linkages between consumers and producers in the production sectors of Agriculture and Industry.

More recently, as the economy developed and diversified, there was a need for a fast growing, more dynamic Services sector that could provide modern, efficient and convenient links between production and consumption. These shortcomings were identified and

Box 6 (Contd.)

private sector participation in Services activities was encouraged through reforms that liberalised trade, transport, communications and financial services. Even in those sectors that were reserved for the state, e.g., monopolies in telecommunication, transport and postal services, a competitive environment towards improving efficiency of the services provided was created by permitting private sector participation. These reforms aimed at expanding the Services sector to meet emerging needs and also at encouraging activities in Services subsectors such as international transport, telecommunications and financial services, where Sri Lanka has a comparative/competitive advantage over other countries in the region and stood to gain from her close proximity to India, as the Indian economy expanded and moved to a higher growth path.

Regional Comparison

Sri Lanka's experience is comparable with that of other countries in the region. In Korea, during a period of 17 years from 1985 to 2002, the Services sector share increased from 47 per cent to 55 per cent of GDP, whereas the Agriculture sector share decreased from 13 per cent to 4 per cent. India, with a more diversified resource base and a larger domestic market, also recorded the same trend. The experience of Thailand and Malaysia that have more natural resources was somewhat different; the Industry and Services sector shares both grew to replace Agriculture. In Singapore, which has a low natural resource base, the Services sector has accounted for two thirds of GDP during the last 20 years.

Conclusions

The faster growth of the services sector and its continuously rising share in Sri Lanka's economy are in line with the normal trend that has been observed in the development process of a country. At the initial phases of economic development, Agriculture and Industry, including construction, provide a firm structural foundation to an economy. However, at later stages, the sustainability of these sectors as creators of wealth will depend crucially on the existence of an efficient Services sector. This is because the Services sector links the three basic activities of an economy - production, distribution and consumption, while it also raises the quality of life of people by enhancing their choice set, lowering transaction costs and increasing convenience. Hence, when a country evolves from low – income to high – income, a normal trend has been the increasing share of its Services sector in the economy. This sector is particularly important for Sri Lanka, as its natural resource base is relatively low. An efficient production system requires the delivery of inputs to production units, satisfying three requirements – timeliness, quantity and quality. At the other end of the production line, consumption too requires that the final products be delivered to the consumer, satisfying the same three requirements - timeliness, quantity and quality. It is the Services sector which fulfils these requirements and facilitates production, distribution, and consumption to perform efficiently. Hence, the growth of the Services sector should be viewed as a salutary development, and not as a growing structural weakness in the economy.

TABLE 2

Regional Comparison of Economic Structure

Country /Period	Agriculture (%)	Industry (%)	Services (%)
Singapore			
1985	1.0	34.5	68.8
1995	0.2	33.3	65.3
2001	0.1	32.0	67.7
2002	0.1	33.6	66.6
Korea			
1985	12.6	41.0	46.5
1995	6.2	43.2	50.6
2001	4.3	42.0	53.7
2002	4.0	40.9	55.1
India			
1985	33.0	28.2	38.8
1995	28.4	27.9	43.7
2001	25.0	25.9	49.2
2002	22.7	26.6	50.7
Thailand			
1985	15.8	31.8	52.3
1995	11.0	39.3	49.7
2001	10.4	40.7	48.9
2002	9.0	42.5	48.5
Sri Lanka			
1985	24.4	26.8	48.8
1995	18.7	28.1	53.1
2001	20.1	26.8	53.1
2002	20.1	26.3	53.6
Malaysia			
1985	n.a.	n.a.	n.a.
1995	12.9	41.4	47.9
2001	8.5	49.1	47.3
2002	9.1	48.3	46.4

Source: Key Economic Indicators 2003 - ADB cent to 500,642. Arrivals from Western Europe increased by 27.4 per cent, while arrivals from the Asian region rose by 24.0 per cent. Following the United Kingdom with 93,278 arrivals, India continued its position as the second major tourist generating market with 90,603 arrivals. The hotels were able to increase their profitability from higher occupancy by foreign tourists. During the year, foreign guest nights rose by 32.9 per cent from the marginal drop recorded in 2002, while local guest nights of all graded hotels recorded an increase of 7.5 per cent. Consequently, hotels and restaurants services grew by 22.0 per cent, in real terms, in 2003. The advertising subsector recorded a healthy growth of 13.6 per cent in 2003, with the rising consumer demand and ensuing competition from suppliers in many sectors. Repairs of motor vehicles, motorcycles and personal and household goods rose by 11.7 per cent following the rapid increase in the importation of those items in the recent past.

Industry Sector

The Industry sector, which comprises Manufacturing, Construction, Mining and quarrying, and Electricity, gas and water, grew by 5.5 per cent in 2003 and contributed 25 per cent of overall growth. This sector contracted in 2001 by 2.1 per cent and grew by 1.0 per cent in 2002. In this context, the performance of the Industry sector in 2003 displays a complete recovery from the setback in 2001. All sub-categories contributed to the recovery.

The Manufacturing sector, the largest subsector in Industry, grew by 4.4 per cent in 2003. The growth in factory industry and small industry was mainly responsible for this growth. The factory industry subsector, which covers the production of large and medium-scale industries, grew by 4.6 per cent in 2003. This subsector contracted by 3.9 per cent in 2001 and recovered partly in 2002 by 2.5 per cent due to the favourable performance of domestic market oriented industries. In 2003, domestic oriented industries continued to grow in response to sustained consumer confidence. The food, beverages and tobacco category grew by 6.3 per cent, with the production of processed foods growing by 7.3 per cent and liquor by 12.0 per cent. The decline in the tobacco industry was 3.5 per cent. High rates of taxes on tobacco threatened the industry, together with illegally imported cigarettes that were available in the market. Domestic market oriented industries such as wood and wood products, plastic and PVC products, cement, basic metal products, and fabricated metal products also performed well during the period mainly due to the increased demand from construction activities. The export market oriented industries, which contracted severely in 2001, and recovered marginally in 2002, grew at a modest rate of 2.6 per cent. The combined growth of 2002 and 2003 was not sufficient to offset the contraction experienced in 2001. This raises concerns, as export-oriented industries account for 60 per cent of factory industry and are important in terms of value addition, employment generation, and foreign exchange earnings.

The textiles, apparel and leather products subsector, the largest industrial subsector in factory industry, grew by 2.7 per cent in 2003. The competitiveness of Sri Lankan products that was maintained with aggressive cost cutting and an improved real effective exchange rate helped this growth. However, the recovery of the garment industry was slower than expected due to the slower recovery of major importing countries such as USA and Japan, continuing deflationary pressures in some international markets and intense competition from low cost manufacturing countries, such as China and those in East Europe. Of the export-oriented industries, rubber products recorded the highest growth of 22 per cent. The demand for rubber based products such as rubber gloves and industrial tyres increased, despite severe competition from China, as a result of close relations with global retailers, continuous improvement in quality and advanced marketing strategies. Under the Indo Lanka Free Trade Agreement, domestic tyre manufacturers explored the Indian market in 2003, for the first time.

Small industries grew by 6.1 per cent, compared with the growth of 2.1 per cent in 2002. The paddy milling industry, the most widespread small industry in the country, performed well in 2003 due to the bumper paddy harvest. The bakery industry also grew amidst the growing demand for prepared foods. Small industries such as timber mills, rock and metal products, and tiles, bricks, cement blocks and related products benefited from the growth in the construction industry.

The Electricity, water and gas sector grew by 21.7 per cent in 2003, in contrast to the 0.7 per cent decrease in the previous year. Electricity generation during the first half of the year increased by 17.4 per cent on the low base in the corresponding period of last year where power cuts were imposed till mid May 2002. In the second half of the year, generation rose by 6.9 per cent, resulting in an annual increase of 11.7 per cent. The demand for electricity grew by 12.9 per cent during the year, mainly due to high growth in the industrial and commercial sectors. Hydropower generation by the CEB and private power producers increased by 22.9 per cent, while thermal power generation increased by 4.5 per cent. During the year a 163 MW combined cycle thermal power plant constructed by AES (Pvt.) Ltd and the 70 MW Kukule Ganga hydropower plant were commissioned in February and September, respectively. Consequently, installed capacity expanded by 10 per cent and the value addition in the electricity subsector increased by 25.3 per cent due to higher generation of low cost hydropower, particularly in the second quarter, and lower usage of high cost hired thermal power from the second quarter onwards. During the year, 56.5 per cent of the total electricity was generated thermally, in comparison to 60.4 per cent in 2002. Meanwhile, water distribution increased by 1.4 per cent compared with 3.8 per cent in the previous year.

The Construction sector grew by 5.5 per cent in 2003. This sector had faced difficulties in 2001 with the economic recession and even though the overall economy recovered in 2002, with a moderate growth, this sector contracted by 0.8 per cent due to the low level of investment that prevailed and weak implementation of large-scale government projects. The growth in 2003 came from both public investment and private sector small and medium scale activities such as construction of apartment complexes and condominiums, supermarkets and retail trade outlets, fuel pumping stations, and individual housing projects. Large-scale road construction projects in both the Southern and Northern parts of the country contributed to the growth performance of the construction sector. The growth in the construction sector was also consistent with the high production, imports and sales of cement and other construction materials.

Agriculture Sector

The Agriculture sector, which expanded by 2.5 per cent in the previous year, grew by 1.5 per cent in 2003 under structural rigidities and mixed weather conditions. The relative importance of the Agriculture sector continued to decline from 19.8 per cent in 2002 to 19.0 per cent in 2003. In 2003, the production of most major crops such as vegetables, paddy, coconut, rubber and minor export crops improved, while tea, subsidiary food crops and tobacco production were unsatisfactory. The flood situation in some parts of the country in mid 2003 adversely affected the output of most agricultural products.

In plantation agriculture, tea production dipped slightly with an output of 303.2 million kg. This was a decline of 2.2 per cent. There had been seven consecutive record tea harvests till 2002, when output was an all time high amounting to 310 million kg. The main contributory factor towards the decline in 2003 was the output drop of 6.2 per cent from the high-grown sector due to dry weather conditions at the end of the year. Production in the low grown areas was affected by the mid-year rains and subsequent floods and earthslips that resulted in a marginal decline in low grown teas. The prices, which were adversely affected by the Iraqi war in the first half of the year, became attractive in the latter half. Overall, tea prices declined marginally by 0.3 per cent, on average, in 2003. Exports of tea in 2003 amounted to 298.3 million kg, which is an all time record and an increase of 6.5 million kg over 2002.

Despite a notable price hike of 51 per cent, rubber production in 2003 increased only marginally by 1.7 per cent. However production was on an increasing trend till September 2003. The recovery in international prices is attributed to production cutbacks by major rubber producers in East Asia and higher demand on the back of improved world economic growth. Domestic consumption, which absorbs about 60 per cent of total production, has been growing at a faster pace with the expansion of rubber manufacturing industries.

Coconut production, which had declined continuously since the first quarter of 2001, recorded a 7.1 per cent growth in 2003. Coconut output amounted to 2,562 million nuts, against the 2,392 million nuts in 2002 due to the lagged effect of the favourable weather that prevailed during 2002. It is expected that this growth will continue in the near term. The increase in output was reflected in the decrease in annual average producer prices by 11.6 per cent. Further, the decline in prices was 26 per cent in the second half of the year.

In domestic agriculture, paddy production in 2003 was 3.067 million metric tons, an increase of 7.2 per cent over the previous year. The paddy output in both Maha and Yala seasons were all time records. During 2002/2003 Maha, paddy output was 1.895 million metric tons, an increase of 6.8 per cent over the previous Maha season. Yala output increased by 7.9 per cent recording a harvest of 1.172 million metric tons. The value addition for the year recorded an increase of 7.4 per cent. The ongoing peace process has enabled paddy cultivation in areas in the North and the East, which had earlier been abandoned due to the civil conflict. Also, favourable weather conditions facilitated a high level of output. The area cultivated increased by 15.2 per cent, while that in the North and the East rose by 17.8 per cent. However the yield per hectare declined due to the cultivation of marginal lands. Decline in paddy prices by 8.6 per cent and the drop in imports of rice in volume terms by 64 per cent clearly reflect the high production volumes during the cultivation year.

TABLE 2.2

Composition of the Other Agriculture Subsector

Sector	Value Added (1996) Constant Prices (Rs.mn.)		
	2001	2002(a)	2003(b)
Total	76,205	78,397	79,797
Vegetables	35,166	34,155	35,761
Subsidiary food crops(c)	15,312	17,126	16,216
Minor export crops (d)	6,297	7,116	7,443
Sugarcane	1,048	1,058	1,217
Tobacco	1,297	1,487	1,435
Animal husbandry(e)	7,377	7,303	7,431
Other	9,708	10,152	10,294

(a) Revised

(b) Provisional

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

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

(e) Animal husbandry comprises milk, eggs, poultry and other meats.

Source: Central Bank of Sri Lanka

Value added in the other agriculture subsector, which consists of vegetables, subsidiary food crops, minor export crops, animal husbandry, sugarcane, tobacco and fruits, increased by 1.8 per cent in 2003. In this category, vegetable production increased by 4.0 per cent. Almost all varieties of low country vegetable production increased, while the production levels of most up country vegetables declined. The subsidiary food crops category recorded a decline of 4.3 per cent. This decline was a consequence of the combined effect of 1.2 per cent growth in the Maha season and 10.5 per cent decline in the Yala season. The decline in the production of potatoes was mainly responsible for the decline in the production of subsidiary food crops.

Production in the minor export crops category increased by 4.6 per cent. Export volumes of coffee, nutmeg and mace, cardamoms and betel leaves grew. Export earnings, however, dropped by 22.5 per cent relative to the 52 per cent growth recorded in 2002. Tobacco production declined by 3.5 per cent mainly owing to the setback in the tobacco industry mentioned earlier. The animal husbandry subsector recorded a growth of 1.8 per cent during the year. Poultry meat production grew by 3.6 per cent during 2003 in comparison to the growth of 4.7 per cent in 2002. Meanwhile, value added in milk production increased by 1.2 per cent, amidst the adverse effects of high input costs, particularly the price of cattle feed.

According to primary data sources, fish production during the year declined by 5.5 per cent. This decline was the combined outcome of the decline in output in the marine sector by 6.8 per cent and an increase in output of inland fisheries by 7.6 per cent, leading to a decline in value addition by 6.9 per cent for that sector. The drop in marine fish production is attributed to the depletion in the fleet of multiday boats as well as the loss of fishing days due to bad weather experienced in the Southern and Northwestern coastal areas during the months of May and June in 2003. Fishing in the Northern territorial waters was also apparently affected by poaching. The drop in output was reflected in the increase in fish prices by 7.4 per cent, on average. While domestic agricultural production in the North and the East has responded positively to the ceasefire, such positive developments are yet to be realised in the fisheries sector even after 2 years. One reason cited is the limited refrigeration and other infrastructure facilities for the transport of fish from these areas.

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 expenditure of the private and public sectors of the economy. In 2003, GDE or total domestic demand was estimated at Rs. 1,876 billion, at current market prices, reflecting an increase of 10.9 per cent over 2002. In comparison, domestic demand increased by 13.1 per cent in 2002 in nominal terms. In 2002, the real increase in domestic demand was 6.6 per cent whereas in 2003 the corresponding increase was 8.4 per cent. The higher increase in 2003 reflects higher consumer and investor confidence in a conducive macroeconomic environment, as well as the lower inflation that prevailed in 2003. Of the total expenditure, consumption expenditure accounted for 78 per cent, the same level that prevailed in 2002. GDP at market prices, the sum of GDE and net imports, was estimated at Rs. 1,760 billion, an increase of 11.2 per cent.

Consumption expenditure at current market prices was estimated at Rs. 1,483 billion, an increase of 9.6 per cent over the previous year. This reflects an increase of 3.2 per cent in the average price level and of real consumption by 6.1 per cent. Of the total consumption, PCE rose by 10.7 per cent while government consumption, which declined by 3.6 per cent in 2002, continued to decline in 2003. Consequently, the share of PCE increased to 91 per cent of total consumption expenditure from 90 per cent in the previous year. In recent years, it was observed that government consumption has been gradually shrinking with diminishing public sector economic activity in line with the policy of private sector led economic growth. In

TABLE 2.3
Aggregate Demand

Rs. million

Item	Current Market Prices			Constant (1996) Prices		
	2001	2002(a)	2003(b)	2001	2002(a)	2003(b)
A. Domestic demand						
Consumption	1,185,482	1,353,428	1,483,164	826,552	880,489	934,555
(% change)	14.2	14.2	9.6	0.2	6.5	6.1
Gross domestic capital formation	309,684	337,782	392,940	214,731	229,094	267,945
(% change)	-12.2	9.1	16.3	-17.5	6.7	17.0
Total domestic demand	**1,495,166**	**1,691,210**	**1,876,104**	**1,041,283**	**1,109,583**	**1,202,500**
(% change)	**7.5**	**13.1**	**10.9**	**-4.0**	**6.6**	**8.4**
B. External demand						
Exports of goods and non-factor services	525,398	570,995	629,696	352,064	374,223	392,148
(% change)	7.1	8.7	10.3	-5.3	6.3	4.8
Imports of goods and non-factor services (c)	613,167	679,550	745,520	461,917	515,448	569,121
(% change)	-1.7	10.8	9.7	-9.5	11.6	10.4
Net external demand	**-87,768**	**-108,555**	**-115,824**	**-109,853**	**-141,225**	**-176,973**
C. Total demand	**1,407,398**	**1,582,655**	**1,760,280**	**931,430**	**968,358**	**1,025,527**
(% change)	**11.9**	**12.5**	**11.2**	**-1.5**	**4.0**	**5.9**

(a) Revised
(b) Provisional
(c) The repayment of loans, taken for the purchase of aircraft, of US$ 292.8 million, from the receipts of insurance payments, against the destruction of those aircraft, included in the BOP service account as a balancing item was not considered as a non-factor service for the year 2001.

Source : Central Bank of Sri Lanka

PCE, the expenditure on locally produced goods increased by 9.2 per cent, while the expenditure on imported goods and non-factor services increased by 14.1 per cent due to the significant rise in domestic demand.

Of the PCE, the highest expenditure was for food and non-alcoholic beverages, as in previous years. However, the relative importance of this category declined from 37 per cent in 2002 to 34 per cent in 2003. The declining importance of this category was observed since these data series began in 1996. With the improvement in living standards and quality of life, the relative share of expenditure on basic needs such as food has diversified to other sectors. In 2003, the expenditure on food and non-alcoholic beverages grew by 1.7 per cent, the lowest growth in all categories. The decline in prices of essential commodities in 2003, such as rice, sugar, coconut, coconut oil and some subsidiary food crops, led to this slow growth. The expenditure share on clothing declined marginally and remained at below 6 per cent. The highest growth of 48 per cent was recorded for transportation. The increase was reflected in the increase in imports and new registrations of motor vehicles, in 2003. Also, the higher consumption of fuel for transportation, despite the increase in prices, also contributed to the higher expenditure on transportation. The expenditure on communications also increased in 2003, by 33 per cent. This was supported by the increased availability and use of telecommunication facilities island-wide. However, the share of communication still remains at 2.2 per cent of total PCE. In addition, the expenditure on housing and utilities, health, and miscellaneous goods and services also increased at significant rates. Almost all these categories indicated an increase in consumption, in real terms. The purpose-wise classification of PCE (Appendix Table 7) revealed that the economic growth in 2003 was mostly based on services activities. The statistics revealed that the demand for goods increased at a relatively slower pace compared with that for services, enabling services activities to grow at a faster rate. These observations support other available evidence that Sri Lanka is moving away from a low-income situation to one where, with the rise in per capita income, the relative share of consumer expenditure on goods to meet basic needs is declining in favour of services of the consumers' choice.

Gross Domestic Capital Formation, or investment expenditure, at current market prices was estimated at Rs.393 billion, an increase of 16.3 per cent over the previous year. In the previous year, the corresponding increase was 9.1 per cent. In real terms, capital formation increased by 17.0 per cent in 2003 while the corresponding growth in the previous year was 6.7 per cent. In the years 2001 and 2002, investment expenditure was lower than in 2000. This level was exceeded in 2003. The continuation of the ceasefire and the peace process, steady expansion of economic activity and economic growth, donor support for the government's economic programme, lower interest rates, and improved macroeconomic management were the major reasons that led to the increase in investment.

The recovery in investment expenditure was led by the private sector. Even though the overall investment ratio dropped from 22.0 per cent to 21.3 per cent in 2002, the private investment ratio (private sector investment/GDP) continued to grow in 2002 from 16.2 per cent to 16.7 per cent. This ratio improved further to 17.0 per cent in 2003. Private sector investment was mainly concentrated in power generation, telecommunications, transportation, and retail trading. On a sectoral basis, investment in transport equipment recorded the highest increase of 38 per cent. Investment in buildings and other construction increased by 14 per cent, while that on plant and machinery increased by 10 per cent. As most of these investments occurred in the second half of the year, the impact will be reflected in production in 2004 as well.

TABLE 2.4

Total Resources and Their Uses at Constant (1996) Prices

Item	Value (Rs. mn.)			Percentage Share			Percentage Growth	
	2001	2002(a)	2003(b)	2001	2002(a)	2003(b)	2002(a)	2003(b)
1. Total resources	1,393,347	1,483,806	1,594,648	100	100	100	6.5	7.5
GDP at market prices	931,430	968,358	1,025,527	67	65	64	4.0	5.9
Imports of goods and non-factor services (c)	461,917	515,448	569,121	33	35	36	11.6	10.4
2 Utilisation	1,393,347	1,483,806	1,594,648	100	100	100	6.5	7.5
Consumption	826,552	880,489	934,555	59	59	59	6.5	6.1
Gross domestic fixed capital formation	214,702	226,037	266,428	15	15	17	5.3	17.9
Private sector and public corporations	185,490	204,490	234,980	13	14	15	10.2	14.9
Government	29,212	21,547	31,448	2	1	2	-26.2	46.0
Changes in stocks	29	3,057	1,517	0	0	0	10,441.4	-50.4
Exports of goods and non-factor services	352,064	374,223	392,148	25	25	25	6.3	4.8

Source : Central Bank of Sri Lanka

(a) Revised
(b) Provisional
(c) The repayment of loans, taken for the purchase of aircraft, of US$ 292.8 million, from the receipts of insurance payments, against the destruction of these aircraft, included in the BOP service account as a balancing item was not considered as a non-factor service for the year 2001.

Government investment was estimated at Rs. 40.7 billion, an increase of 28 per cent over the level of 2002. In 2002, government investment declined by 25 per cent. The increase in public investment in 2003 was coupled with the curtailment of government current expenditure. Government investment mainly focused on road development, including the Colombo – Matara highway project, regional development, and rehabilitation work in the Northern and the Eastern provinces. Regional development was centered on small-scale power projects, water supply and road construction.

2.4 Availability and Utilisation of Resources

The total availability of resources in a country consists of GDP (domestic resources) and imports of goods and non-factor services (foreign resources). This was estimated at Rs. 2,506 billion, at current market prices, an increase of 10.8 per cent over the previous year. This increase was generated by an increase of Rs. 178 billion (11.2 per cent) in domestic resources and an increase of Rs. 66 billion (9.7 per cent) in foreign resources. In real terms, the availability of resources grew by 7.5 per cent. This includes real growth of domestic resources by 5.9 per cent and of imports of goods and non-factor services by 10.4 per cent. The corresponding growth rates in 2002 were 4.0 per cent and 11.6 per cent, respectively.

With regard to utilisation of resources, consumption grew by 6.1 per cent, in real terms. In the previous year, the corresponding growth was 6.5 per cent. Resource utilisation for fixed capital formation grew at 17.9 per cent, and the exports of goods and non-factor services by 4.8 per cent. In 2002, the growth rates were 5.3 per cent and 6.3 per cent, respectively. Of the total resources available 58.6 per cent was absorbed by consumption, lower than in 2002. This was offset by the share of capital formation increasing from 15.2 per cent in 2002 to 16.7 per cent in 2003. The share of exports of goods and non-factor services remained around 25 per cent. The growth in consumption, in real terms of 6.5 per cent and 6.1 per cent, in 2002 and 2003, respectively, further emphasise the consumer confidence that prevailed during these two years. The growth of 17.9 per cent in fixed capital formation in real terms compared to 5.3 per cent in 2002 also confirms the growth in investor confidence in 2003.

2.5 Domestic Savings and National Savings

Domestic savings, which include both private and government savings, were estimated at Rs 277 billion, an increase of 20.9 per cent over the previous year, thereby signifying a considerable improvement in relation to the growth in GDP. In 2002, the corresponding increase was 3.3 per cent. Both the private and government sectors contributed to the increase.

TABLE 2.5

Investment and Savings at Current Market Prices

Item	Value (Rs. mn.)			Percentage Change	
	2001	2002(a)	2003(b)	2002(a)	2003(b)
1. Gross domestic product at market prices	1,407,398	1,582,655	1,760,280	12.5	11.2
2. Private investment	228,165	264,770	299,247	16.0	13.0
3. Government and public corporation investment	81,519	73,013	93,693	-10.4	28.3
4. Total investment (2+3)	309,684	337,782	392,940	5.6	41.3
5. Private savings	290,982	298,229	335,292	2.5	12.4
6. Government savings	-69,066	-69,002	-58,176	0.1	15.7
7. Domestic savings (5+6)	221,916	229,227	277,116	3.3	20.9
8. Net factor income from abroad	-23,830	-25,159	-18,821	-5.6	25.2
9. Net private transfers from abroad	87,902	104,938	116,307	19.4	10.8
10. National savings (7+8+9)	285,988	309,007	374,601	8.0	21.2
11. Investment ratio (4 as a % of 1)	22.0	21.3	22.3		
12. Domestic savings ratio (7 as a % of 1)	15.8	14.5	15.7		
13. National savings ratio (10 as a % of 1)	20.3	19.5	21.3		

(a) Revised
(b) Provisional

Source : Central Bank of Sri Lanka

Private savings grew by 12.4 per cent. This growth came largely from corporate sector savings in the context of higher profitability and better performance. Household sector savings grew at a lower pace as the consumer confidence that prevailed in 2003 led to higher spending and lower savings. Meanwhile, government dis-savings improved by 15.7 per cent. Consequently, the domestic savings ratio (domestic savings/ GDP), which was 14.5 per cent in 2002, improved to 15.7 per cent in 2003.

National savings, the sum of domestic savings, net foreign private transfers and NFIA, also increased by 21.2 per cent over the previous year to Rs. 375 billion. The national savings ratio (national savings/GDP) rose by nearly one percentage point to 21.3 per cent. NFIA although negative, improved, and helped to maintain a higher growth of national savings compared with the growth of domestic savings. Net private transfers, which consist mainly of workers' remittances, grew by 10.8 per cent in 2003, at a rate lower than the growth registered in the past few years. One reason was the stable external value of the rupee against the US dollar in 2003 that curtailed the growth of workers' remittances in rupee terms. Meanwhile, the growth in departures for employment abroad also decelerated in 2003 compared to previous years. Net foreign private transfers, which accounted for 34 per cent of national savings in 2002, contributed 31 per cent in 2003.