

**FINAL BUDGET POSITION REPORT
2003**

Issued under section 13 of the
Fiscal Management (Responsibility) Act No. 03 of 2003

Dr.Sarath Amunugama,MP
Minister of Finance



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**Issued by the
Hon. Minister of Finance
in terms of Section 13 of the
Fiscal Management (Responsibility) Act No.3 of 2003**

1. Introduction

In terms of Section 13 of the Fiscal Management (Responsibility) Act [FMRA], the Minister of Finance is required to present to the public and table in Parliament, the Final Budget Position Report in respect of each financial year.

The purpose of the report is to provide updated information on the fiscal position of the country, in order to evaluate the Government's fiscal performance as against its fiscal strategy. This report is issued in compliance with this requirement.

The Final Budget Position Report of 2003 contains a statement of estimated and actual Government expenditure, revenue, cash flows and borrowing for the year and gives the reasons for any shortfall in the estimated revenue or cash flow and any excess in the estimated expenditure or borrowing

2. Budget Estimates and Actual Outturn for 2003

The Budget estimates and actual outturn for expenditure, revenue and borrowing for 2003 is given in Table 1.

Table 1
Budget Estimate and Actual Outturn -2003

Item	Estimate		Actual	
	Rs. Bn	% GDP	Rs. Bn.	% GDP
Total Revenue	304	17.1	277	15.7
Tax Revenue	265	14.9	232	13.2
Income Tax	48	2.7	39	2.2
Value Added Tax	120	6.8	97	5.5
Excise Duty	49	2.8	51	2.9
Customs Duty	33	1.9	34	1.9
Other	13	0.7	10	0.7
Non Tax Revenue	39	2.2	45	2.5
Total Expenditure & Net Lending				
Total Expenditure & Net Lending	438	24.6	418	23.7
Current Expenditure	345	19.3	335	19.0
Salaries & Wages	91	5.1	92	5.2
Goods & Services	47	2.7	47	2.7
Subsidies & Transfers	77	4.3	71	4.0
Interest Payments	130	7.3	125	7.1
Capital Expenditure	82	4.6	75	4.3
Net Lending	12	0.7	8	0.4
Primary Deficit				
Primary Deficit	4	0.2	16	0.9
Budget Deficit				
Budget Deficit	134	7.5	141	8.0
Financing				
Financing	134	7.5	141	8.0
Net Foreign Borrowing	25	1.4	43	2.4
Net Domestic Borrowing	87	4.9	80	4.5
Asset Sales (Privatization)	14	0.8	10	0.6
Grants	9	0.5	8	0.5

a) Expenditure

As a result of expenditure rationalization measures implemented by the government, total expenditure and net lending amounted to Rs. 418 billion in 2003 against the estimate of Rs.438 billion. The containment of recurrent expenditure was due to the reduced cost of interest expenditure. Public investment was also below the estimates by Rs.8 billion due to expenditure cuts in capital expenditure and the shortfall in the utilization in the donor funds earmarked for capital projects.

Total expenditure in 2003 recorded a growth of 3.9 per cent over that of 2002.

(i) Recurrent Expenditure

Recurrent expenditure was restricted to Rs. 335 billion in 2003. This compares with an estimate of Rs.345 billion. Consequently, recurrent expenditure as a percentage of GDP declined from 20.9 per cent in 2002 to 19.0 per cent in 2003.

Interest Payments

Interest payments, the largest component in recurrent expenditure, was contained at Rs. 125 billion in 2003. Taking advantage of low interest rates prevailed the policy introduced to restructure government debt by replacing high cost debt with low cost debt was the main contributory factor for this position. The availability of donor funds through programme loans helped reduce pressure on domestic debt market. Accordingly, interest payments as a percentage of GDP declined from 7.4 per cent in 2002 to 7.1 per cent in 2003. Tight cash management measures implemented by the government also assisted keeping interest expenditure under control.

Salaries and Wages

The salaries and wages bill including defence wages was controlled at Rs.92 billion compared to Rs. 89 billion in 2002. Accordingly, salaries and wages bill as a share of GDP dropped from 5.6 per cent in 2002 to 5.2 per cent in 2003. The freeze of the recruitment of persons to the public service other than technical grades was largely responsible for the containment of expenditure on salaries and wages.

Defence Expenditure

The continuation of the ceasefire and the ongoing peace process had a positive impact on defence expenditure. Spending on defence declined by 4 per cent in 2003 to Rs. 62 billion. Consequently, defence expenditure as a percentage of GDP declined from 4.1 per cent in 2002 to 3.5 per cent in 2003.

Subsidies and Transfers

Expenditure on subsidies and transfers declined by 4.7 per cent to Rs. 71 billion in 2003. The share of subsidies and transfers declined from 4.7 per cent of GDP in 2002 to 4.0 per cent of GDP in 2003. Payments on pensions and Samurdhi amounted to Rs. 31 billion and Rs. 9 billion respectively.

(ii) Public Investment

Public investment increased to 5.0 per cent of GDP in 2003 from its level of 4.6 per cent in 2002. However, in absolute terms public investment was nearly Rs. 8 billion lower than the budgeted expenditure due to curtailment of capital expenditure and shortfall in the utilization of donor funds. The realization of the public investment programme was 8 per cent below the expectation. More focus on this area is essential to place the country on a high growth path and also to generate productive employment.

b) Revenue

The total revenue collection for 2003 amounted to Rs. 277 billion, registering a 5.6 per cent increase over 2002. This was 91 per cent of the estimated revenue for the year. Of the total revenue, tax revenue amounted to Rs. 232 billion and non-tax revenue amounted to Rs. 45 billion. Revenue from taxes in 2003 increased by 4.4 per cent over the previous year. The tax revenue collected in 2003 was 87 per cent of the estimated revenue for the year. The under performance of Income Tax and Value Added Tax was the main reason for the non achievement of the tax revenue target. Non tax revenue recorded an increase of 12 per cent in 2003 over the previous year. Non tax revenue included transfers made from Central Bank (profits), "Strike, Riot, Civil Commotion and Terrorism Fund" and Customs fines. Revenue from non tax sources was above the annual target for 2003, achieving 115 per cent of the estimate for the year.

Total revenue as a percentage of GDP declined from 16.5 per cent in 2002 to 15.7 per cent in 2003. Tax revenue as a percentage of GDP declined from 14 per cent in 2002 to 13.2 per cent in 2003, whilst non-tax revenue as a percentage of GDP remained at 2.5 per cent.

Income Tax

Income tax collection totaled to Rs. 39 billion in 2003, an increase of 5.2 per cent over 2002. However, this was a realization of 81 per cent of the estimate for the year. Revenue from income tax as a percentage of GDP declined marginally from 2.4 per cent in 2002 to 2.2 per cent in 2003.

Corporate Tax

Corporate tax collection amounted to Rs. 15 billion in 2003. This was an increase of 9.6 per cent over 2002, but below the targeted level for 2003 by 24 per cent. The sluggish growth in corporate tax receipts was due to several reasons. The corporate tax rate was reduced from 35 per cent to 30 per cent from April 2003. A plethora of tax concessions, exemptions and holidays have also eroded the corporate tax base to a significant extent. As a consequence, large numbers of highly profitable companies are not liable to pay taxes. Tax relief allowances provided for capital investment projects have also reduced corporate tax collection. This has resulted in a drastic decline in the tax payments by the major public sector enterprises, such as Sri Lanka Telecom, Ceylon Petroleum Corporation, Ceylon Electricity Board and the Sri Lanka Ports Authority, on account of tax concessions for the investment projects undertaken by these institutions. In addition, the State Commercial Banks have also obtained tax relief against the write-off of bad debts.

Personal income tax receipts declined by 17 per cent and amounted to Rs.10 billion in 2003. Increasing the tax threshold and the upward revision introduced to tax slabs have had a negative impact on personal income tax collection.

Revenue from withholding tax rose sharply to Rs. 14 billion in 2003, an increase of 24 per cent over the previous year.

Several reasons contributed for the low performance on Income tax collections. There were delays in enacting amendments to the legislation relating to the taxation of the highly profitable Foreign Currency Banking Units of commercial banks, secondary market transactions and several other revenue enhancing measures in the Income Tax law. In addition, the tax amnesty which covered not only income taxes but taxes, duties levies and penalties under 26 laws and the extension of the deadline on two occasions in 2003 have had a negative effect on the tax collection.

Value Added Tax

Revenue from Value Added Tax (VAT) amounted to Rs. 97 billion achieving 81 per cent of the estimated target for 2003. The two main factors that stifled the achievement of the VAT target for 2003 was the payment of higher refunds for input credits to tea, leasing, construction and hotel industries due to the two-tiered rate structure that was in operation in 2003 and the postponement of the extension of VAT to the retail and wholesale trade sectors. In addition, the delay in enacting the amendments to the VAT Act which contained several revenue augmenting measures such as restricting input tax entitlement and imposition of VAT on supply of financial services etc too contributed to the low performance under VAT collection.

Debits Tax

Revenue from debits tax amounted to Rs. 4 billion in 2003, realizing 88 per cent of the estimated target for the year.

Excise Duty

Revenue from excise duty amounted to Rs. 51 billion in 2003 and realized 103 per cent of the estimated target for the year. Excise tax collection on liquor, cigarettes and petroleum products amounted to Rs. 11 billion, Rs. 20 billion and Rs. 13 billion respectively in 2003. Revenue from excise taxes on motor vehicles amounted to Rs. 7 billion in 2003. The share of excise taxes to GDP however, declined from 3.3 per cent in 2002 to 2.9 per cent in 2003.

Taxes on External Trade

Revenue from import duties increased by 21 per cent to Rs. 34 billion in 2003, achieving 102 per cent of the estimated target for the year. Increase in tariffs, reduction of the number of items with duty exemptions and the growth in trade contributed for this increase. Revenue from the Ports and Airports Development Levy (PAL) amounted to Rs. 5 billion in 2003, an increase of

57 per cent. However, the collection was only 90 per cent of the estimated target. The revenue share of import duties and PAL to GDP rose from 2.0 per cent in 2002 to 2.3 per cent in 2003.

Non Tax Revenue

The main components of revenue from non tax sources in 2003 were profit transfers from the Central Bank of Sri Lanka (Rs. 10 billion), fees and charges (Rs. 9 billion), interest payments on on-lending activities (Rs. 8 billion) and profits and dividends (Rs. 5 billion). Against a background of reduced revenue from tax sources the government had to depend heavily on non tax sources such as profits from Central Bank , transfers from “Strike, Riot, Civil Commotion and Terrorism Fund” and Customs fines which will not be available in the future. Total non-tax revenue at Rs.45 billion accounted for 16 per cent of the total revenue compared to 15 per cent in the previous year. As a percentage to GDP non-tax revenue in 2003 remained at 2.5 per cent as in 2002.

(c) Cash Flow operations of the Government

Cash inflows of the Government during 2003 including grants amounted to Rs. 310 billion as against the original estimate of Rs. 338 billion. The deviation of Rs. 28 billion from the original estimate was mainly due to the shortfall in tax revenue

Cash outflows on account of operating activities amounted to Rs 331 billion as against the original estimate of Rs. 334 billion generating a net cash deficit of Rs. 21 billion as against an estimated surplus of Rs 4 billion originally from operating activities.

Cash outflows on investment activities amounted to Rs. 113 billion as against an estimated of Rs. 119 billion. Although the supplementary estimates on capital expenditure accounted for Rs 19 billion enhancing the estimated outflows on investment to Rs 139 billion the actual outflow fell below by Rs 25 billion.

A summary of the cash flow estimates and actual performance is given below.

Summary of Government Cash Flow Operations in 2003

Rs billion

Item	Original Estimate	Supplemen-tary Estimates	Total Estimate	Actual Cash Flow	Devia-Tion
Total Cash Inflows	338	0.6	339	310	(29)
Total Cash Outflows from Operating Activities	(334)	(2)	(336)	(331)	5
Net Cash Flow from Operating Activities	4		3	(21)	(24)
Cash Flow from Investing Activities	(119)	(19)	(139)	(113)	25
Net Cash Surplus/ Deficit	(115)		(136)	(134)	2
Opening Cash Balance	(5)		(5)	(5)	
Gross Borrowings	311	54	365	358	(7)
Debt Repayments	196	33	229	219	10
Net Borrowings	115		136	139	3
Temporary Employed Balance and other Adjustments *				2	2
Ending Balance	(5)		(5)	(3)	2
Approved Borrowings	316	54	370	358	(12)

- Other Adjustments are on account of Reimbursable Foreign Aid Advances, Imprest balances and other deposit balances.

d) Borrowings

The Parliament approved Rs 316 billion as total gross borrowings (in terms of book value) in Budget 2003. Due to the supplementary estimates as shown above and the

repayment of high cost debt of Rs 33 billion the gross borrowing limit was enhanced to Rs.370 billion.

Gross domestic borrowings amounted to Rs. 272 billion while domestic repayments were at Rs 192 billion, of which repayments to the banking sector accounted for Rs 21 billion . Therefore, the net domestic borrowing amounted to Rs 80 billion.

Gross foreign borrowings accounted for Rs. 87 billion, which included foreign commercial borrowing of Rs 10 billion and private sector development loans of Rs 10 billion. The repayments on account of foreign loans amounted to Rs 34 billion. Therefore, the net foreign borrowings excluding private sector development loans amounted to Rs.43 billion.

The financing of the budget deficit comprised Rs 80 billion and Rs 43 billion from domestic and foreign sources respectively while grants and proceeds from privatization accounted for Rs 8 billion and Rs. 10 billion respectively.

On the basis of the foregoing operations of the Government the budget deficit as a percentage of GDP was at 8 per cent as against the original estimate of 7.5 per cent. However, the deficit in 2003 recorded an improvement as compared to the 8.9 per cent deficit of the previous year. The deviation of the deficit as against the original estimate of 2003 was mainly due to the shortfall in tax revenue but it had been arrested to some extent through expenditure cuts both in recurrent and capital.

e) Government Debt

The total outstanding debt as at end 2003 was Rs. 1,864 billion out of which 55 per cent was domestic debt. The total debt stock increased by 12 per cent bringing the end year debt to GDP ratio to 105.9 per cent from its level of 105.4 per cent in the previous year. Increase in the domestic debt in 2003 was 7.5 per cent or by Rs. 72 billion compared to

16 per cent increase in 2002. The deceleration in the increase of domestic debt was due to the availability of budgetary financing through foreign programme loans and commercial loans to the extent of Rs. 23 billion and Rs. 10 billion respectively. The foreign debt stock in rupee terms increased by 17 per cent in 2003 where 56 per cent or Rs. 68 billion of this increase was on account of the exchange rate variations. The increase in the foreign debt stock due to exchange rate variation was due to the higher depreciation of the rupee against the Japanese yen and SDR (13 per cent and 10 per cent respectively) as 75 per cent of the foreign debt stock consists of yen and SDR denominated loans.

Total debt service payments in 2003 amounted to Rs. 345 billion which constituted of Rs. 125 billion of interest payments and Rs. 220 billion of amortization payments, reflecting an increase of 21 per cent over 2002. As a percentage of GDP the debt service payments rose to 19.6 in 2003 from 17.9 per cent in 2002. The major contributory factor for the increase in the debt service payments was the increased amortization payments on account of early retirement of high cost debt.

Outstanding Government Debt (as at end year)

	2002		2003	
	Rs. Bn.	% of GDP	Rs. Bn.	% of GDP
Total Domestic Debt	948	59.8	1,020	57.9
Short Term	259	16.4	250	14.2
Medium & Long Term	689	43.5	770	43.7
Total Foreign Debt	722	45.6	844	47.9
Project Loans	640	40.4	770	43.7
Non Project Loans	82	5.2	74	4.2
Total Outstanding Debt	1,670	105.4	1,864	105.9

Government Debt Service Payments

	2002		2003	
	Rs. Bn.	% of GDP	Rs. Bn.	% of GDP
Amortisation Payments	168	10.6	220	12.5
Domestic	131	8.3	185	10.5
Foreign	37	2.3	34	1.9
Interest Payments	117	7.4	125	7.1
Domestic	106	6.7	114	6.5
Foreign	11	0.7	12	0.7
Total Debt Service Payments	285	17.9	345	19.6