Sri Lanka Development Context

Section II

"The Strength of this nation lies uniquely within. The policies we develop will take advantage of our competitive strengths and proactively plan the development path based on our culture, resources and regional dynamics. It is time to look ahead and convert strategies into action and make genuine progress towards sustainability for the benefit of the society, the environment and creation of wealth in Sri Lanka"
(Economic Policy Statement of the Government)

Overview of the Economy

Sri Lanka is a small open economy with a land area of 65, 610 sq km, with a population of 19.3 million in 2004. The country's per capita income exceeded US Dollars 1,000 in 2004 which is higher than that of most of its South Asian neighbors despite the country facing a 20 year civil conflict in the Northern and Eastern provinces. The pre Tsunami challenge for Sri Lanka was to place the economy on a pro-poor, pro-growth strategy within the Private-Public Partnership development framework as articulated in the new Government policy framework - 'Creating our Future - Building our Nation', announced in June 2004. The destructions caused by the Tsunamis have added new dimensions to the country's socio-economic challenges. Larger parts of the North and East coast as well as of the South and West coast, which are areas worst affected by the Tsunamis, represent a high level of poverty and unemployment and are now further confronted with the multifaceted challenge of rebuilding. As such the country in addition to being engaged in resolving the conflict in the North and East is now in the process of rehabilitating and reconstructing the areas affected by the Tsunamis. Consequently, Sri Lanka's post conflict and post Tsunami eras could be viewed as new opportunities capable of creating widespread equitable growth and development in the economy.

Sri Lanka has experienced a steady economic growth of around 5.5%, over the years. Despite having to face severe droughts and the rise in international oil prices, the country was able to achieve an economic growth rate of 5.4% in 2004. Sri Lanka was one of the first developing nations to understand the importance of investing in human resources and promoting gender equality. Sri Lanka's social indicators such as life expectancy, literacy rates are well above those in comparable developing countries and are on par with many developed countries. In terms of the Human Development Index (HDI) Sri Lanka ranked 96th with an index of 0.740 among 177 countries, in 2004. However, poverty still remains an issue affecting nearly one in four Sri Lankans.

The sectoral composition of the economy has changed from that of an agriculture based economy to one dominated by the services sector. The services sector has been the highest contributor to GDP of 56%, followed by the Industrial sector at 26% and the agricultural sector at 18% by the end of 2004. Liberalization, private sector participation, modernization and increased competition have contributed to the expansion of the services sector, with sectors such as transportation, communication, financial services, trade and tourism flourishing, reporting buoyant performance. Although its significance has declined in recent years, the agricultural sector is an important determinant of GDP, directly accounting for around one-fifth of national output and employing over one-third of the workforce. Indirectly, its importance is greater than what the figures indicate because of the link between agricultural, manufacturing and services sectors.

The manufacturing base is dominated by the apparel industry, the production of food and beverages, as well as chemical and rubber based goods are also important. Industrial production is dominated by the textile and apparel industry, which contributed to approximately 65% of industrial exports in 2004. The phasing out of the Multi Fiber Agreement is likely to pose some challenges despite the fact that this sector is already competing in a non quota market and caters to niche markets.

Sri Lanka's economy is predominantly a Small and Medium Enterprise (SME) economy where over 50% of our GDP is produced by the SME sector. The new Government having recognized the importance of this sector in achieving a balanced economic growth, equitable regional distribution and increasing employment and productivity levels, have adopted various policies for the development of SMEs in Sri Lanka. The launching of the SME Bank and the establishment of the SME Authority to function as the apex body for the development of the SME sector, are expected to be the catalyst for SME led growth.

The composition of exports has changed over the years from traditional exports to non-traditional industrial exports. In 1990, 36%, was agricultural based exports while industry accounted for 52%. In the first half of 2004, the composition of agricultural exports declined to 19% while the industrial exports accounted for 78%. The Government has implemented various policy measures to encourage greater non-traditional value addition to exports. Assistance to develop craft products for export markets, the apparel industry, and product improvement incentives for small exporters, product design, and financial assistance for technological improvements, are to name a few.

Sri Lanka has shifted towards a lower tariff regime. In the 2005 Budget, tariff lines were further reduced in order to adopt a more liberal trade policy regime. Further, the country has entered into several preferential and regional trade agreements and as such is well integrated both regionally and internationally. Free Trade Agreements with neighbouring India and Pakistan have deepened the liberalize trade arrangements in the region.

In 2004, there was an increase in imports leading to a decline in the balance of trade by 49% from its value, in comparison to the same time last year. The higher import bill was mainly due to high international oil prices. Increases in inflows to the Services and Income Account from tourism, port related activities and inward remittances were able to offset only a part of the increase in trade deficit. The Government's key policy objectives relating to its balance of payments are to diversify export earnings, trade and services, improve inflows from overseas employment and promote foreign investment and build external reserves.

The declining tax to GDP ratio, lower levels of public investment and a relatively high level of debt to GDP ratio can be identified as the key problems in the fiscal sector in the recent years. A series of measures have been introduced to increase tax revenue, which include simplifying the tax system, expanding the tax base, rationalizing tax exemptions and improving tax administration. Sri Lanka is now committed to a large public investment program with a view to providing a wide range of infrastructure facilitates, developing human resources and undertaking governance and capacity building as well as post conflict rehabilitation work in the northern and eastern provinces. This was not the case in the past where, public investment in Sri Lanka declined from 8.3% in 1990 to 5% in 2004. Public investment is expected to increase to 8.0% of GDP in 2008 and various investment programmes have been planned towards achieving this target. (Annex 1)

Box 2 - Government Initiatives at Provincial Level

- **Gamata Thaakshanaya**

  This programme has been designed with the aim of supporting science and technology for national development. Provision of technology, basic infrastructure, market access and diversified production activities are considered essential in reducing rural poverty and regional disparities.

  For technology to be transferred to micro and SME entrepreneurs, computer linked "Vidatha" resource centers would be set-up in each of the 320 Divisional Secretariats in the country. In addition, at the village level science and technology societies would be formed to transfer technology to the villages and promote SMEs with the view to creating employment and reducing poverty.

- **Pubudamu Wellassa**

  Badulla and Monoragala districts are the poorest and most neglected districts in the island, where poverty remains high. School enrolment, access to drinking water, infrastructure and health facilities remain below national level. A 3 year accelerated development programme providing a wide range of infrastructure facilities would be implemented under this initiative.

- **Rajarata Navodaya**

  Villages in the Anuradhapura and Polonnaruwa districts and border villages of the conflict affected areas, which lack basic irrigation and infrastructure facilities would be developed under a 3 year programme.

- **Dayata Sevana**

  The Government's target is to construct 300,000 housing units to be developed for low and middle-income persons in the medium term. In this regard, priority would be given to low income housing requirements of shanty dwellers, the plantation community, the coastal fishing community and the rural sector.

- **Sector specific assistance programmes -**

  * Floriculture Sector Development
  * Dairy Industry Development
  * Incentives for Foundry Industries
  * Incentives for Prawn Farming
  * Assistance for Organic Product Exports
  * Development of the Cinnamon Export Industry
  * Incentives for cultivation and value addition of rubber
  * 'Osu Gammana'(promotion of growing medicinal plants) and the reforestation programme
  * Creation of model farms for fruit and vegetable
  * Assistance to develop craft products for export markets
  * Incentives for the revival of the construction industry
  * Incentives for advanced technology

Post Conflict Challenges

Two decades of conflict have hindered Sri Lanka's economic progress to a large extent, having adversely affected the socio economic conditions. Thousands have been killed or disabled due to the war. This has weakened the human capital base of the country and has also encouraged 'brain - drain'. Pre conflict Sri Lanka commanded the best human capital in Asia. The war has also prevented the economy from operating at its full capacity, hindered improvements in productivity, disrupted the efficiency of resource allocation, interfered with the free mobility of inputs and finished products, island wide thus making the economy vulnerable for numerous shocks. The resultant deterioration of market confidence and constrained investment expansion has particularly discouraged the much-needed foreign investment inflows. Moreover, a large extent of infrastructure such as roads, rail roads, telecommunications, electricity and housing have been destroyed, while agricultural and industrial resources have been heavily underutilized consequent to the war. The war has further aggravated the poverty situation and unemployment, especially in the Northern and the Eastern provinces and border villages to the conflict areas.

Meanwhile, increased defence expenditure due to the war has widened the fiscal deficit, thus reducing resources available for economic development and raising the burden of public debt. Defence expenditure as a percent of GDP, which was less than 3% during early 1980s increased to 4.5% by 2000 and declined to 3% of in 2004. The total Government debt, which was 77% of GDP in 1980 increased to 106% by 2004. Increased defence expenditure also exerted pressure on the domestic interest rates and the exchange rates. The production loss alone, due to the war has been estimated to be around 2% of GDP, per year.

However, since the ceasefire between the Government and the LTTE in February 2002, economic fundamentals have improved. Various projects are now being initiated with support from development partners of Sri Lanka in the rehabilitation and reconstruction efforts in the North and East. (Table 1)

Table 1: Development Initiatives in the Northern and Eastern Provinces

Donor	Project Name	Project Components
World Bank	North East Irrigation Agriculture Project (NEIAPI and II)	• Rehabilitation of small irrigation schemes • Community capacity building and reconstruction • Feasibility studies for major/medium term irrigation schemes • Project implementation support • Technical assistance • Village rehabilitation and development • Farmer organization capacity building and strengthening the agricultural support services
	North East Housing Reconstruction Project (NEIAP - ll)	• Housing assistance • Capacity building in housing repair and reconstruction • Programme management and monitoring
Asian Development Bank	Secondary Towns and Rural Community Based Water Supply and Sanitation Project	• New piped water system • Low cost latrine programme • Drainage improvement • Waste treatment plant for Batticaloa Hospital and Prison
	North East Costal Community Development Project	• Provision of micro credit to support sustainable livelihood activities • Resource management in Trincomalee Bay, Batticaloa Lagoon and Southern Ampara biodiversity Zone • Coastal resource planning in Trincomalee and Batticaloa districts • Fisheries development in Ampara, Batticaloa and Trincomalee
	Conflict Affected Area Rehabilitation Project	• Road rehabilitation • Water supply feasibility study • Power and electrification • Community development and income generation

Donor	Project Name	Project Components
ADB, OPEC,	NECORD	This project contributes towards the overall relief and rehabilitation of Programmes of the NE by improving the living conditions and well being of communities affected by the conflict sectors - education, health, agriculture, livestock, roads, water supply, fisheries, social welfare, institutional development, shelter, irrigation, vocational training. Up-front community development
Japan/JABIC Germany Netherlands	Small and Micro Industries Lender & Entrepreneurship Promotion Project II	Provision of small & micro finance to SMEs through banking system
	Poverty Alleviation and Micro Finance Project	Provision of small & micro credit to low income householders through the banking system
	Pro-poor Economic Advancement and Community Empowerment (PEACE) Project	Rehabilitation of irrigation facilities and income generating activities such as rehabilitation of tanks, training and awareness programmes, various livelihood support activities etc.
	Small-scale Infrastructure Rehabilitation and Upgrading Project (SIRUP)	• Development of education and health sectors • Road rehabilitation • Irrigation development • Water supply and sanitation
WFP	Project Relief and Recovery Operations	• Mother child nutrition • Food for education in selected primary schools • Food for work for the rehabilitation of village infrastructure
Austrada	Integrated Water Supply Scheme for Eastern Coastal Area	Provide safe drinking water to Ampara district
Austrade	Jaffna Water Conservation and Environmental Management Project	• Rehabilitation of 42 ponds and canals in Jaffna • Compost making • Rainwater harvesting
Sweden	Rehabilitation of bridges in the North East	Supply and construction of 89 bridges and 2 ferries in the North East
UNDP	Support to the Sri Lanka National Mine Action Project	Provide support to agencies involved in mine clearance such as survivor on mine fields
	Repatriation, Reintegration, and Reconstrcution Programme Rehabilitation	Protection, income generation, community infrastructure, local governance and capacity building

Impact of Tsunamis on the Economy and the Resultant Changes to the MDGs

The Tsunamis that devastated two thirds of the coastal belt of Sri Lanka on December 26th 2004, caused heavy damage to human life and property. Sri Lanka being the second worst affected country in the region, suffered extensive loss with more than 31,000 dead, over 15,000 injured, more than 5,000 reported missing and nearly a million people displaced. At least 100,000 people lost jobs. Even though the Tsunamis affected mostly the least developed areas in the country, the consequential asset loss is estimated to be around US$ 1,000 Million or 5 percent of the country's GDP, including loss to private property, transport infrastructure, fisheries harbours, hotels, schools, hospitals, water and electricity supplies and telecommunications.

The agricultural and services sectors are likely to decelerate mainly due to the anticipated underperformance in fisheries and tourism sectors, which have been badly affected by the Tsunamis. The relief is that, the fisheries and tourism sectors constitute only a small share of GDP, which is less than 3%. The Tsunami affected provinces, excluding the Western Province, account for 17.2% of GDP. Between 25%-33% of the population in the affected districts live below the poverty line. The Tsunami disaster has increased the vulnerability of a large proportion of the very people whose income was to be uplifted under the Governments poverty reduction programme. Economic growth in 2005 has been estimated to decelerate by about 0.5% - 1.0% from the original estimate of 6.0% due to the impact of the Tsunamis. The construction sector is expected to grow at more than 8% per annum as opposed to 5% before the Tsunamis due to the anticipated construction work related to reconstruction of the affected areas.As such, the external trade deficit is likely to widen in the short term mainly due to the anticipated increase in imports and the expected marginal drop in exports. However, this deficit will be more than offset by the expected inflows of foreign aid from international donors. The disaster would have a significant impact on the Government Budget, particularly on Government expenditure. However, this impact will be mitigated with the assistance extended by domestic and foreign donors. In fact, the exchange rate initially appreciated in view of the aid flow.

The Tsunami disaster would have a short term adverse impact on the MDGs, especially in the areas of poverty, education, child mortality, health and environment. The Government is adopting a multi-faceted approach in terms of rebuilding the affected areas and has already introduced a series of relief measures to restore the Tsunami affected areas on a fast track basis. It is therefore believed that the Tsunami disaster would not obstruct plans set out in achieving the MDGs. The Government's plan for rebuilding the nation addresses poverty alleviation, infrastructure development, rehabilitation of education and health sectors, social services, development of industrial and tourism sectors, gender dimension and environmental issues.

The initial institutional framework has already been set up for this purpose and the Government is firmly committed to ensure that essential rehabilitation and reconstruction work will be completed within a 2 - 3 year period. Tsunami inflicted areas would be developed on a sustainable basis with emphasis on infrastructure and services. Resource constraints would not hamper the proposed process since the required resources would be available through donor assistance already pledged for Tsunami related reconstruction and rehabilitation work. The effects of such development work will essentially have a positive impact on other areas as well, through employment generation, trade, and other services. Further, there is renewed trust for communal unity, which gives hope towards achieving permanent peace in the North and East.

Challenges and Risks over the Medium Term

As a small open economy, the challenge for Sri Lanka in the medium term is to achieve a sustainable high economic growth with greater equity whilst integrating in the process of globalization, achieving permanent peace, and rehabilitating and reconstructing the Tsunami affected areas. The costly and destructive civil conflict, macroeconomic imbalances mainly consequent to the high fiscal deficit, the slow progress in economic reforms and poor infrastructure are the factors responsible for limiting economic development in the past. Hence, achieving a sustainable high level of economic growth with equity and improving the resilience of the economy will largely depend on realizing permanent peace, prudent macro-economic management, undertaking necessary economic reforms, infrastructure development and human resource development.

The Medium Term Macro Economic Framework

The macro economic policy vision of the Government is to position Sri Lanka as a modern economy free from corruption and political interference, with equal opportunities for its citizens and to emerge as an environment-friendly development center. The medium term strategy of the Government is as follows:

- GDP growth is expected to increase to 7.5% in 2008. This growth is to be backed by a strong macro economic framework, which has a diversified domestic resource base, modern infrastructure and regionally balanced development. The use of untapped resources coupled with enhanced regional activities and infrastructure development will create employment opportunities, which in turn would address the issue of unemployment

- The Government will take appropriate measures in striking the right balance between foreign financing and domestic borrowing. This would assist in consolidating a low interest rate regime, which in turn would enable more resources to be channeled to the private sector, thus stimulating economic growth

- Monetary policy would be designed to prevent demand-fuelled inflation and would be formulated to promote a proper balance between investments and savings. Total investments and domestic savings is expected to grow by 25.8% and 36% respectively, over the medium term

- The Government's industrialization strategy is towards high value-added domestic-based production. As such domestic industries would be encouraged to diversify and improve productivity levels. Liberalization commitments and trade agreements would be encouraged to ensure competitiveness, interest rate management, labour market reforms, maintaining a stable exchange rate and policies for the development of the SME sector are measures taken in support thereof

- As the part of the Government's investment strategy, Public-Private Partnerships would be encouraged to promote large scale infrastructure projects. The Government aims to move away from its reliance on debt finance and instead focus on targeting private equity funds and increased foreign direct investments (FDIs) to the country. For the country to achieve growth, enhance competitiveness and further development, attracting FDIs is important as it affects the rate of growth through research and development and its impact on human capital and infrastructure development

- The Government's aim is to attract FDIs into strategic sectors, activities or regions, for industrial policy considerations. As such, it is necessary to maintain a stable macro and fiscal policy environment. The Government having recognized this has taken several measures for fiscal consolidation, human resource development including development of the education sector, enhancing IT skills and has also adopted various policy measures including strengthening governance, towards creating a macro economic environment which is conducive for foreign investment

- As a measure towards promoting foreign investment, the Board of Investment (BOI) is being restructured to make it more pro-active and focused towards investor needs and to be the "one - stop - shop" for investors. Its functions are being strengthened to ensure speedy clearance of investment approvals and related clearances

- The Government hopes to attract FDIs into export industries and industries engaged in high local value addition, generating employment, use advanced technological methods and undertake high research and development. In addition to the manufacturing sector, FDIs are sought after, for developing the tourism sector and funding of infrastructure development projects across the island. Enhancement of investment activities funded by foreign capital inflows will necessitate higher investment related imports. Although this would widen the current account deficit of the Balance of Payments, these imports would positively contribute to higher economic growth in the future

- The Government's trade and tariff policy would be aimed at providing a stable and predictable medium term framework and would be geared to facilitate a fair trading environment for the import and export sectors, in order to enhance a competitive environment. Sri Lanka is committed to strengthen its standards of health, environment and labour safety to comply with best international practices

- The Government has recognized the importance of a governance structure that is transparent, accountable and built on an equitable legal and institutional framework to achieve economic growth. As such, institutions responsible for law reform are being strengthened with capacity building and outlived legislations are being repealed or amended

Table 2 : Growth with Development

OUTPUT	2004	2005	2006	2007	2008
GDP at Market prices (Rs. Bn)	2,029	2,343	2,658	3,000	3,371
Real GDP Growth (%)	5.4	5.3	6.0	6.5	7.0
Inflation/GDP Deflator (%)	9.2	9.7	7.0	6.0	5.0
INVESTMENT & SAVINGS (% GDP)					
Total Investments	25.0	30.0	32.2	32.8	33.9
Private Investments	19.8	21.9	22.7	24.2	25.9
Public Investments	5.2	8.1	9.5	8.6	8.0
Domestic Savings	15.9	17.0	20.8	22.2	24.8
Private Savings	19.8	18.6	20.3	19.8	21.2
Public Savings	-3.9	-1.6	0.5	2.4	3.6
National Savings	21.6	23.1	26.1	27.6	30.1
TRADE (US$ Mn)					
Trade Gap	-2,243	-3,370	-3,353	-3,478	-3,406
Exports	5,757	6,354	6,860	7,343	7,978
Imports	8,000	9,725	10,213	10,821	11,384
Services	419	352	484	521	593
Receipts	1,527	1,572	1,794	1,952	2,131
Payments	1,108	1,220	1,310	1,431	1,538
BALANCE OF PAYMENTS (US$ Mn)					
Current Account	-648	-1,572	-1,505	-1,408	-1,133
Current Account Deficit (% GDP)	-3.3	-6.8	-6.0	-5.1	-3.7
Overall Balance	-205	101	176	200	250
External Reserves (Months of imports)	2.8	2.7	2.9	3.1	3.2
Debt Servicing (% GDP)	11.5	7.4	11.1	10.0	9.7
GOVERNMENT FINANCE (% GDP)					
Revenue	15.4	16.9	17.8	18.8	19.5
Expenditure	23.5	26.5	26.8	25.1	24.0
Revenue (Deficit/Surplus)	-3.9	-1.6	0.5	2.4	3.6
Overall Budget Deficit	-8.2	-9.6	-9.0	-6.3	-4.4
Domestic Financing	5.8	3.6	2.9	2.0	1.6
Government Debt	106.2	103.9	102.1	98.1	93.5
MONEY SUPPLY (YoY % Growth)					
Broad Money (M2)	19.6	15.0	14.0	13.0	12.5
Narrow Money (M1)	16.6	13.0	12.0	11.0	10.5

BOX 3 - Government's New Policy Initiatives

- **National Council for Economic Development (NCED)**

  The NCED is built on the concept of bringing together stakeholders from the private and state sectors to jointly develop national economic policies and action plans. 22 cluster committees have been created directly engaging over 300 private and public sector domain expertise and citizen volunteer members who facilitate in the policy formulation and execution process of the Government. Clusters vary from Exports to Employment Creation, Financial Sector Reforms, Education, Taxation, Legal, Trade and Tariff and Millennium Development Goals.

- **Strategic Enterprise Management Agency (SEMA)**

  SEMA has been created to strengthen the management of 14 strategic state enterprises and to improve their performance. It is managed by a team of professionals with domain knowledge and expertise to assist business development of these state enterprises. Their mandate is to ensure that these enterprises would adopt best management practices and corporate strategies, and also undertake management reforms to ensure optimum productivity and focus on initiatives to become efficient partners in the national economy.

- **Administrative Reforms Committee (ARC)**

  ARC was established to oversee institutional reforms in the public sector in order to make the Government's administrative machinery efficient, citizen friendly and modern. Major areas of reform would be the rationalization of the activities of Government agencies, to ensure that they are focused on functions relevant to current needs, with special emphasis on transparency and use of modern technology.

- **National Procurement Agency (NPA)**

  NPA has been established to strengthen and streamline the Government procurement system. It is mandated to prevent delays and inefficiencies through the formulation of simplified and harmonized procurement policies, guidelines and standards. In addition NPA will also engage in capacity building and monitoring to ensure accountability and transparency in procurement practices.

- **National Council for Administration (NCA)**

  NCA was created to revive the recommendations of the Salaries Commission - 2000, which called for the establishment of a permanent commission on administration with statutory powers. Some of the responsibilities of the council include, monitoring of salary structures and making relevant recommendations to the Government, developing a national wage policy, cadre management in the public sector, identifying institutional shortcomings and taking measures to remove such constraints.

- **Inland Revenue Modernization Project**

  Measures are underway to modernize the Inland Revenue Department through the introduction of a modern administrative structure supported by technology and human resource development.

- **Automation of the Company Registrar's Office**

  The objective is to transform the Company Registrar's Office into a more effective and efficient unit in order to provide quality and timely services to its clients and to perform its monitoring and regulatory functions more expeditiously, towards facilitating and promoting enterprise development in the country. This measure will enable the public to perform registration on, searching, etc. of companies online which minimizes human intervention and thereby corruption.

Medium Term Fiscal Framework

The country's current macro economic policies are geared to achieving a high economic growth which is sustainable, with macro economic stability as well as greater regional and income equality. As such, the medium term macro fiscal policy framework of the Government is designed to achieve the following three key objectives;

- Transform the prevailing revenue deficit in the national budget to a surplus and generate Government savings of over 2% of GDP by 2007

- Augment public investment over 7% of GDP by 2006, in order to accelerate the national infrastructure development programme, rapidly expand provincial and rural infrastructure facilities, rehabilitate and reconstruct infrastructure in the North and East and upgrade and modernize human resource development facilities

- Reduce domestic borrowings to 2% of GDP in order to enhance available resources for the development of SME led private sector capital formation and income generation activities

Through the improvement of productivity in all industrial sectors, including the public sector, Sri Lanka is seeking to attract investment, promote economic growth, and increase the national income. It will be essential for Sri Lanka to raise productivity in all sectors of the economy by removing barriers impeding the productive use of its resources. The future of the country's economy will heavily depend on the continuous improvements to its capabilities to attract foreign

Table 3 : Medium Term Macro Fiscal Framework 2004-2008

(As a % of GDP)	2004	2005	2006	2007	2008
	Revised	Budget	Medium Term Budget		
Revenue	15.6	17.2	18.0	18.9	19.5
Taxation	14.1	15.5	16.3	17.1	17.7
Income and Profits	2.2	2.4	2.6	2.9	3.1
Goods and Services	9.4	10.1	10.6	11.1	11.5
Non Tax Revenue	1.5	1.7	1.7	1.8	1.9
Profit and Dividend of State Owned Enterprises	0.3	0.3	0.4	0.5	0.6
Expenditure	24.2	24.8	24.7	24.6	23.9
Current Expenditure	19.3	18.5	17.6	16.7	15.9
HR Development	2.7	2.8	2.9	3.0	3.0
Interest on Public Debt	6.0	5.7	5.4	4.9	4.5
Public Investments	5.0	6.4	7.0	7.8	7.9
Large Scale Infrastructure	2.4	2.5	3.1	3.1	3.3
Provincial/Rural Infrastructure	2.6	3.8	4.0	4.7	4.6
Government Savings	-3.7	-1.3	0.4	2.2	3.6
Budget Deficit	-8.6	-7.6	-6.7	-5.7	-4.4
Overseas Development Assistance	1.7	2.6	3.1	2.9	2.7
Domestic Financing	6.8	4.6	3.5	2.7	1.6
Non-Bank Institutional Savings	5.3	4.6	3.5	2.7	1.6
Bank Financing	1.5	0.0	0.0	0.0	0.0
Other	0.1	0.3	0.1	0.1	0.1

Source-Spotlight on Budget 2005, Ministry of Finance investment and promotion of Public-Private Partnerships. A sound macro economic environment with diverse incentives to attract foreign investment should be in place in establishing its position as an export - oriented economy. In addition, the improvement of the country's economic infrastructure and the implementation of institutional capacity building programmes are also essential. Such strong Government supported initiatives are likely to pave the way for Sri Lanka to achieve sound economic growth to reach and exceed its Millennium Development Goals.

The Way Forward

Around 30%- 40% of the total population in Sri Lanka is considered poor and 90% of them live in rural areas. The Government is aiming at an annual economic growth rate of 7%-8% over the medium term. The Government's way forward to achieve such growth is by adopting pro-poor, pro-growth strategies.

The potentials from globalization in terms of growing connectivity and productive capacity are immense. For globalization to be effective for people, it is necessary to develop a system of global governance that is supportive of and conducive to national development strategies. Economic and social objectives should focus on the needs and aspirations of the ordinary people who are the center of development policy. It is in this regard that the Government has adopted measures to enhance infrastructure development, improve social infrastructure, rejuvenate the agricultural, livestock and fisheries sectors, create a dynamic and export-oriented industrial sector, encourage human resource development, and implement livelihood support programmes for the poor.

The principal objective of the Government's growth strategy is poverty reduction. For growth to be pro- poor, it must stimulate productivity, and create employment. In this regard, infrastructure development lagging in areas of agriculture, industry and tourism is the main focus of Government strategy. In addition, targeted programmes would also be initiated for the benefit of the vulnerable groups in the society such as the elderly and the disabled.

As most of the rural poor are engaged in the agricultural sector, research and development in agriculture would be encouraged. In addition, farmer education programmes on water conservation and timely cultivation methods, the use of new high-yielding varieties of crops, and adoption of indigenous technology would also be introduced.

The Government having recognized the importance of knowledge and skills development and in keeping with its commitment to achieve the MDGs, a National Action Plan for Children (NPC) for 2004-2008 with a budget of Rs. 2.2 billion was initiated. The objectives of this programme include increasing enrolment rates, increasing access to safe drinking water for the child population, protecting disadvantaged children and combating child labour. Further, technical and vocational schools, modern classroom teaching methods and resources such as IT infrastructure and computer laboratories would be set up. English Language and Information Communication Technology would be introduced as new subjects into the curricula. A programme to reduce the present 50-1 pupil-teacher ratio and measures to increase the quality of teacher training would also be introduced. In addition, 397 schools in rural areas would be developed under the "Navodaya" school development programme. The above policies together with a sound macro-economic environment, a strong financial services sector, productivity improvement programmes and sustained economic reforms would ensure equitable economic growth with low incidence of poverty, in the medium term.