Sri Lankan budget: increased defence spending and further IMF restructuring

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The sixth budget of the People's Alliance (PA) government in Sri Lanka was presented to the parliament on February 14, increasing the country's defence expenditure, continuing IMF restructuring and providing further concessions to big business, particularly foreign investors. The budget was due last November but was postponed because of the snap presidential election held in December.

President Chandrika Kumaratunga, who holds the post of finance minister, chose to present the budget to parliament herself this time. Her appearance, which breaks from the tradition of the president being represented by a minister or deputy minister, was a calculated move. Kumaratunga, who is under pressure to abolish the country's executive presidency, claimed her attendance in parliament was a move to the "further democratisation of the institution of the executive presidency and then to go on to its abolition".

With a general election due in August, media commentators have widely interpreted it as an "election budget". In fact the largest items of government expenditure are on the military and the repayment of the huge public debt. The burden falls heavily on the working class. Government officers had expected a salary increase to make up for a drastic decline in their real wages but they were told simply that a commission would be appointed to look into the matter.

While the budget announced no new price or tax increases, the government had already increased diesel, kerosene and gas prices sharply by 23, 48 and 9 percent respectively only a week before. Higher fuel prices have resulted in higher transport costs. Fares for state-owned bus services have gone up by 15 to 25 percent and private bus owners are demanding permission for a 15 percent hike on top of a 15 percent increase last month. Higher kerosene prices directly affect the rural and urban poor and plantation workers whose main source of energy and lighting is kerosene oil.

The government increased defence expenditure by $US70 million to a total of $718 million (52.4 billion rupees)—higher than the combined spending on education and health of just $470 million. Even this figure is an underestimate as over the past few years the defence budget has been supplemented throughout the year with additional allocations to meet the escalating cost of the ongoing war against the separatist Liberation Tigers of Tamil Eelam (LTTE).

The higher military spending takes place as Kumaratunga is preparing for negotiations with the LTTE mediated by Norway on ending the war. The Treasury Secretary claimed in cautious comments to the *Daily Mirror* on February 18 that the "hefty defence spending" was "to keep the (military) presence to create pressure to take the peace process forward". No doubt the government is wanting to strengthen its hand in any talks with the LTTE, but it is also preparing for a renewal of the war as well as to deal with the social unrest over deteriorating living standards. The "focus in the defence budget this year is to strengthen the police," he said.

Sections of big business are pushing for an end to the 17-year war, as it has become a huge drain on the economy. Military expenditure now consumes nearly 25 percent of government revenue and has undermined efforts to reduce the budget deficit as demanded by the IMF. The PA government promised in its first budget in 1995 to reduce the deficit to 6 percent by 1999. Despite substantial cutbacks to education, health and government services, military spending has soared and the deficit stood at 8 percent for last year.

The largest single slice of government expenditure—about $1,318 million—was allocated for the repayments of debts. Even though the budget speech did not provide a breakdown, on past trends more than one third of that sum will go on interest and repayments on foreign borrowings. The government is hoping to collect $411 million through the sale of state ventures and use the money to partly pay off government debts.

Privatisation is just part of a broad agenda of economic restructuring being implemented by the government at the behest of the International Monetary Fund. “The government will also go ahead with its divestiture program in respect of hotels, Bogala Graphite (a graphite mining venture) and agricultural and livestock farms,” Kumaratunga announced. She promised that “restrictions in respect of foreign investments in Sri Lanka particularly in the financial sector will also be further relaxed...”

The government has decided to allow 90 percent foreign participation in the insurance sector and the budget announced the complete sale of one insurance corporation. Restrictions on foreign brokerage firms will also be removed. In the banking sector, government will end 49 percent limit on foreign equity and allow 60 percent equity ownership.

The budget also calls for the restructuring of state banks, Ceylon Electricity Board, and the Ports Authority. At present these are wholly state-owned enterprises in which employees have continuously opposed moves to privatisation. Electricity Board workers struck for three days in 1996 blacking out the country. State bank employees have been involved in continuous agitation against privatisation.

The Kumaratunga government is under pressure from the IMF to implement the “reform” measures in “banking sector, civil service and the labor market” in order to fulfill conditions for a $500 million loan. IMF country representative in Sri Lanka, Nadeem ul Haque, has made clear that “the quantum of assistance would depend on the degree of reforms. The program must be sustainable and I know the government is keen to progress with the second generation of reforms.”

Business groups such as the National Chamber of Commerce of Sri Lanka and the Exporters Association have welcomed the budget. The Ceylon Chamber of Commerce said it was pleased the president “stressed the need to boldly offer a political solution to the North east conflict through consensus building with all concerned parties and groups” and added that most of the budget proposals were positive.

Sections of business have, however, expressed concerns about the lowering of tariffs. The budget announced that the maximum tariff rate would be reduced from 30 percent to 25 percent. Fears that Sri Lankan companies will be unable to compete with cheap imports have been compounded by the implementation of the Indo-Lanka Free Trade Agreement signed last year.

In her speech, Kumaratunga boasted that her government had saved Sri Lanka from the impact of the Asian economic crisis. But two days earlier the Central Bank issued a press release painting a gloomy picture for the 1999. “Export earnings declined by 4 percent in 1999, attributed to a decline in world commodity prices resulting from depressed global demand,” it stated. “The overall export price index declined by 10 percent reflecting lower prices of garments, tea, rubber and rubber based products.” As a result the trade deficit for 1999 increased to $1,294 million up from $1,092 million in 1998.

The IMF and the World Bank have approved the government's policy of “gradual devaluation” of the rupee, which has already been devalued 46 percent since 1995. Already the treasury officials have expressed their concern about the rising oil prices in the world market upsetting their economic targets. Kumaratunga's “vision for the 21st century” will not bring the “prosperity” she suggests but will only widen the gulf between rich and poor and lead to a further erosion of the living standards as prices soar and jobs are destroyed.