Sri Lankan government imposes new taxes to fund war

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In a desperate attempt to raise money for its renewed war, the Sri Lankan government rammed five finance bills through parliament on September 6 increasing taxes on a range of goods and services. With the 2008 budget due in early November, these bills are a stopgap measure to raise around 10 billion rupees ($US88 million)and plug a hole in the government's finances.

The new imposts include: an increase in the tax on cellular phones from 2.5 to 10 percent; a rise in the levy on larger motor vehicles from 2.5 to 5 percent; the excise duty on imported goods will increase from 10 to 15 percent; and the production tax on domestically manufactured goods will rise from 10 to 15 percent. Between them, the excise duty and production levy cover most goods, further fuelling already sharp price rises.

Speaking in the parliamentary debate, deputy finance minister Ranjith Siyambalapitiya justified the bills by declaring: "The imposition of such taxes is necessary in view of other obligations of the government including ensuring national security and providing subsidies to the people." The money is not for "providing subsidies"—the government has in fact been slashing subsidies—but to prosecute its communal war against the Liberation Tigers of Tamil Eelam (LTTE).

Defence spending escalated sharply following a series of military offensives in July 2006 to seize LTTE territory in the East of the island—in open breach of the 2002 ceasefire. President Mahinda Rajapakse, who also presides over the defence and finance ministries, boosted defence expenditure in 2007 by 45 percent to 139 billion rupees compared to 2006. Since the budget was announced, military spending has continued to rise.

Having proclaimed "victory" in the East, the Rajapakse government is preparing to launch a new offensive against the LTTE's northern strongholds. The president and his brother, Defence Secretary Gotabhaya Rajapakse, have made clear that military operations will not be halted by the expense or by public hostility over the rising cost of living. Over the past year, the military has made heavy use of air strikes, artillery and multi-barrel rocket launchers, all of which are expensive to maintain and operate.

The tax bills provoked a farcical debate in parliament, with the United National Party (UNP) and the Janatha Vimukthi Peramuna (JVP) heatedly denouncing the government for imposing new burdens on voters. Opposition leader Ranil Wickremesinghe objected to the use of electronic voting and demanded a show of hands. A UNP MP tried to grab documents from the speaker, provoking scuffles in the chamber. Opposition MPs raised their mobile phones and declared they were "against taxes". Amid the uproar, the bills were passed 106 to 81 with the pro-LTTE Tamil National Alliance (TNA) joining the UNP and JVP to vote against.

This political pantomime was designed to obscure the fact that neither the UNP nor the JVP raised any principled opposition to the bills. Their show of concern for the masses is only because they are well aware that the war and its economic burdens are deeply unpopular. The UNP and the JVP, however, support the new offensives against the LTTE and did not oppose the reactionary purposes to which the money will be put.

In the case of the JVP, its opposition is particularly two-faced—the logic of its demand for the war to be intensified is for more taxes, not less. Its motto—"Motherland First, other things later"—means that working people must sacrifice for the war. The JVP continues to support the government on key votes. At the same time, it tries to posture as a defender of workers and the rural poor. Not surprisingly, in the midst of the parliamentary ruckus, the JVP MPs maintained a complete silence on the war.

As for the UNP, it quietly dropped its claim that the vote had been “illegal”. The UNP’s differences with the Rajapakse government are purely tactical. Its stance reflects the concerns of sections of business that the war is affecting the economy and could end in military disaster. But the UNP, which launched the war against the LTTE in 1983, does not oppose the renewed military offensives.

The government is obviously in financial difficulty. In June, a meeting of provincial council chief ministers complained that funds from the central government had been slashed by 60 percent. The business web site, *Money Report*, revealed in early August that the government had cut 65 billion rupees, or 25 percent, from its budget for public investment for this year.

Another controversy has erupted over plans to raise $500 million on the international money markets. A team of major banks—Barclays Capital, the Hong Kong and Shanghai Bank (HSBC) and JP Stanley Morgan—has been engaged to launch the bond issue. The government has been evasive as to the purpose of the loan. Initially, it declared the money was for development and infrastructure projects, but failed to specifically identify them.

Last weekend’s *Sunday Times* questioned the government’s claims that the loan was for “infrastructure” and pointed to its real purpose. “The worst scenario would be its use for military expenditure that is not economically productive. To the extent that it is for military hardware imports, even the immediate benefit to the balance of payments by the inflow of funds would be quickly offset by the outflow of funds for imports. To the extent that it is used for domestic expenditure in the war, it would be inflationary.”

Despite the various disguises, the loan will, in one way or another, be used to fund the war. The government is prepared to pay commercial interest rates, rather than seeking development loans from the IMF or other sources, because it does not want to be constrained in how the money is spent. While the size of the loan may not appear large, it will add significantly to foreign debt, which as of June stood at 1,014 billion rupees ($US8.95 billion). The bond offering has been delayed by the international financial turmoil triggered by the crisis over sub-prime mortgage loans in the US.

Prices are already increasing sharply. In the same week that it raised taxes, the government allowed Shell Gas to increase the price of gas by 20 percent—the third rise this year. Last month, the government agreed with the company to allow prices to change in line with international fluctuations. On September 11, consumer affairs minister Bandula Gunawardene announced that the government had okayed a price increase for powdered milk of between 28 to 39 percent—again, the third rise for the year.

The annualised inflation rate for August was 17.3 percent, slightly down from the July figure of 17.6 percent, but nowhere near the single digit rate promised by the Central Bank. The value of the Sri Lankan rupee has continued to decline against the US dollar even as the dollar has slid against other international currencies. The rate has risen from 106 rupees to a US dollar in January to 113 rupees in September.

In a bid to curb inflation, the Central Bank has kept the benchmark interest rate at a five-year high of 10.5 percent. Bank interest rates have soared to over 17.5 percent. The tightening of credit, however, has not restrained prices and has only led to a slowing of economic growth. *Bloomberg News Survey* reported on September 12 that the second quarter growth rate was 6.1 percent—similar to the first quarter GDP increase, which was a two-year low.

Defending his announced price increases, consumer affairs minister Gunawardene bluntly explained the economic logic of the government’s policies: “The defence bill is 140 billion rupees. We need to import bullets and shells. If we could shoot at [LTTE leader] Prabakharan with a catapult we would not have to spend foreign exchange.” Asked by reporters about the government’s previous promises to control prices, he declared dismissively that these were just “political slogans”.

New taxes and price rises are clearly the means by which the government intends to place the burden of its war onto the backs of working people.