

**MID YEAR
FISCAL POSITION REPORT
-2007-**

Ministry of Finance and Planning



**MID- YEAR
FISCAL POSITION REPORT**

2007

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Issued under Section 10 of the Fiscal Management (Responsibility)
Act No. 03 of 2003.

**Mahinda Rajapakshe
Minister of Finance and Planning**

Mid Year Fiscal Position Report
Issued by the Hon. Minister of Finance
Under the Section 10 of the Fiscal Management (Responsibility) Act No.03 of 2003

In terms of Section 10 of the Fiscal Management (Responsibility) Act No.03 of 2003 the Minister of Finance and Planning is requested to present the mid- year fiscal position report to the public by the last day of June in the year and thereafter laid before the parliament.

The purpose of this report is to provide updated information on the Government's fiscal performance against the fiscal strategy of the Government.

The report contains the performance of Government revenue, expenditure, cash flow operations and borrowings during the first four months in year 2007. The report also provides updated information, depending on the availability of information, relating to macro economic performance, price development, employment, foreign aid, Government debt, balance of payments, money and credit development.

Chapter 1

Fiscal Developments

Budget Deficit Managed

- Fiscal Developments during the first four months in 2007 indicated a 29 percent growth in Government Revenue with the tax revenue recording a growth of 30 percent. Despite an increase in the expenditures on account of salaries, pensions, national security and humanitarian activities in the newly liberated areas and as well as for maintaining public investment at a level to support growth rate of around 7 percent for the year, the growth of total expenditure was contained at around 8 percent during this period.
- Revenue generated during this period accounted for 28 percent of estimated revenue for the full year, around the same proportionate as in the corresponding period of 2006. The current expenditure accounted for 31 percent of the budgeted amounts in 2007, compared with 33 percent in the first four months in 2006.
- As a percentage of GDP, the revenue collected for the first four months was 5.3 percent compared to 4.7 percent in the corresponding period in 2006. The total expenditure GDP ratio was 7.6 percent compared to 8 percent in the same period of 2006. Reflecting the improved revenue performance and slower growth in recurrent expenditure, the deficit in the revenue account declined to 0.5 percent of GDP from 1.5 percent recorded in first four months in 2006.
- Another notable feature in fiscal developments was the net repayment of Rs. 27 billion to the banking sector during the first four months in 2007, compared to net borrowing of Rs.18.3 billion in the same period in 2006.
- These developments complemented the other actions being taken including the tightening of the monetary policy to contain inflationary pressures to promote sustainable higher growth.
- In a context where significant additional burden on treasury operations was imposed due to the sharp rise and unexpected volatility in interest rates, further fiscal consolidations through revenue augmentation helped to mitigate such pressures.

- Although the government debt operations raised Rs. 67.2 billion through market instruments during January-June 2007, which was only Rs. 2 billion higher than the first half of the previous year. When debt issuance to foreigners through the Treasury Bonds was excluded, the net borrowing from the domestic sources indicated a significant decline easing the pressure on rupee resources owing to budgetary operations.

Table I.1

Summary of the Budget (Jan – April) - Economic Classification

Rs.Mn.

	2006	2007
Revenue	130,977	170,374
Tax	118,086	153,945
Non-Tax	12,891	16,429
Expenditure	226,456	244,638
Current	174,709	185,675
Public Investment	54,987	63,775
Other	-3,239	-4,812
Revenue Account	-43,732	-15,302
Overall Deficit	-95,488	-74,264
Financing	95,488	74,264
Grant	7,325	10,878
Foreign Loans	11,406	25,826 *
Domestic Financing	76,749	37,560
Non Bank	58,367	64,873
Bank	18,382	-27,313
Revenue/ GDP(%)	4.7	5.3
Current Expenditure/GDP (%)	6.2	5.7
Public Investment/GDP (%)	2.0	2.0
Revenue Deficit/GDP (%)	1.5	0.5
Overall Budget Deficit/GDP (%)	3.4	2.3

Source: Department of Fiscal Policy

* Includes foreign investments on Treasury Bonds.

Government Revenue

Taxation Policy Changes Aimed at Higher Revenue

- With a view to sustain the higher revenue generation witnessed in last 3 years and to augment it further several policy measures were implemented to broaden the tax base, revision of the tax rates and to strengthen the tax administration while ensuring a conducive environment for investment.

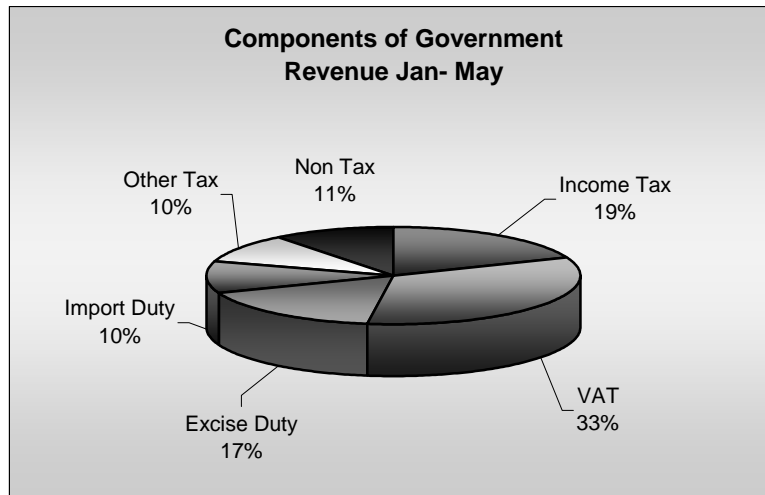
- Government revenue generated during January- May 2007 amounted to Rs. 218,034 million, a 27 percent growth over the same period of 2006. As a ratio of GDP it increased to 6.7 percent while the tax revenue increased to 6.0 percent from 5.2 percent. The revenue performance in the first five months was in line with the expectations for the full year, showing the possibility of meeting the budgetary target.

Table 1.2
Revenue Performance – (Jan- May)

	Rs. Mn.		
	2006	2007	Growth
Tax Revenue	153,460	195,084	27
Income Tax	24,768	41,143	66
VAT	59,879	72,573	21
Excise Tax	35,474	37,305	5
Stamp Duty	24	1,469	
Port & Airport Development Levy	7,503	9,850	31
Import duty	20,487	22,697	11
Other	5,325	10,047	88
Non Tax Revenue	18,917	22,950	21
Total Revenue	172,377	218,034	27

Source: Department of Fiscal Policy

Chart 1.1



Income Taxes Record a Steady Growth

- Total revenue from corporate profits tax, personal income tax, tax on interest income and Economic Service Charge (ESC) at Rs. 41,173 million recorded a significant increase of 66 percent in the first five months of 2007 compared to the corresponding period of the last year.
- Series of policy measures implemented to broaden the tax base, rate revisions & administrative improvements in the last 3 years coupled with the enhanced dedication by the tax administration contributed to this growth.
- With a view to augment the income tax revenue and reach around 3.5 percent of GDP in the medium term, several further measures were introduced in the 2007 Budget which came into force from 1st April 2007.

Income Tax Changes

Measures to broaden the tax base

- When the profits and income of the business of insurance is ascertained, the life insurance and the other insurance will be treated as separate business. Any loss from one business of insurance can be set off only against the profits from that business.
- Where for any tax year commencing on or after April 1st, 2007, the gross dividend distributed by any company is less than 25 percent of its distributable profits for the year,

the company will be required to pay additional tax amounting to 15 percent of the excess of one third of the distributable profits over the profits already distributed.

- The 15 percent rate will not be applied if the company is the holding company of any group of companies, if any subsidiary or any associated company of any group of companies.
- Changes in treating the bad debts of a bank or financial institute was limited to the lesser of the actual amount of the bad debt provision or 1 percent of the loan debtor balance at the end of the year.
- ESC non chargeability for 3 years following the commencement of business was limited only to manufacturing business.
- The threshold of relevant turnover at which chargeability arises in the case of ESC was reduced from Rs. 10 million to Rs. 7.5 million per quarter.

Rate Changes

- Several rate reductions with respect to ESC were introduced in sectors such as, export of gems/diamonds, jewellery, apparel, entrepot trade, industries engaged in production of value added products of tea, rubber, desiccated coconut, sheet rubber etc. and unit trusts.

Exemptions/ other Development Measures

- Unit trusts were granted to claim exemption of profits from the sale of shares to popularize the unit trust industry.
- The tax free threshold of partnerships was increased to Rs. 600,000 and for the divisible profits more than Rs. 600,000, the 10 percent rate was made applicable only on the amount in excess of Rs. 600,000/-
- Tax holidays were granted for newly constructed cinemas and existing cinemas. The qualifying payments on the cost of production of films that could be deducted from income taxes was increased from Rs. 10 million to Rs. 25 million , to boost the local film industry.

- Reduced Income tax rate of 33 1/3 percent for capital allowance in respect of ships acquired. Also income tax exemptions were granted on remuneration of any resident individual employed in a Sri Lankan ship, with a view to develop the Shipping Industry as a thrust industry in Sri Lanka.
- Income tax was exempted on profits of any individual engaged in construction work outside Sri Lanka for which payment is made in foreign currency and has been remitted to Sri Lanka through a bank to encourage locals providing such services outside Sri Lanka and encourage inward remittances through official channels.
- Increase of the depreciation allowance on machinery used in the construction industry from 12.5 percent to 25 percent.
- Withholding tax on interest accruing to individuals from banks and other financial institutions were made simpler and equitable.
- Concessions were granted on taxation for terminal benefits of retiring employees in the form of increased slabs of the taxable income particularly with regard to employees who retire after 20 years.
- Employees were exempted from income tax in respect of their benefits from participating in employee share option plans, to encourage employer/employee partnerships in the business development.

Administrative Changes

- Commissioner General of Inland Revenue (CGIR) was empowered to waive the penalty accrued for non payment of any amount of income tax for any tax year ending on or before 31st March 2005, if the defaulter pays the tax within a period of not more than 3 years in accordance with an installment plan agreed with CGIR, with a view to clear the taxes in default.

Moderate Growth in Value Added Tax (VAT) Revenue

- VAT revenue up to May 2007 amounted to Rs. 72,573 million, an increase of 21 percent over the corresponding period of last year. Slower growth in value of motor vehicle

imports, the services such as tourism performing at a level below potential, slower growth recorded in liquor and cigarettes sales contributed to the moderate growth in the VAT revenue collection.

Table 1.3
Performance of VAT – (Jan. – May)

(Rs.Mn.)

Tax Base	2006	2007	Growth
Domestic	32,355	36,286	12
Import	32,537	40,519	25
Gross revenue	64,892	76,805	18
Refunds	5,013	4,232	-16
Net Revenue	59,879	72,573	21
Refunds as % of Gross Revenue	7.7	5.5	

Source: Department of Fiscal Policy

Value Added Tax Changes

Broaden the tax base

- Input tax credit was restricted to either input tax allowable or 85 percent of the output tax declared for the taxable period, whichever is lower.
- The adjustment of input tax on Tax Debit Notes was restricted to such notes issued within 6 months for the date of the issue of original.
- The markup on CIF value on importation of goods was increased from 7 percent to 10 percent.
- The 50 percent of credit for input tax which was allowed on motor vehicles used for traveling was disallowed in full.
- Provisions were made to withhold 1/3 of the VAT payable to contractor or any other service providers, on supplies made to government agencies.
- Provisions were made to allow persons who are on the boarder of VAT threshold of Rs. 1.8 million to pay 5 percent non refundable VAT.

Rate Changes

- VAT rate reduced from 15 percent to 5 percent on the import and supply of high tech medical equipment.
- VAT rate reduced from 15 percent to 5 percent on the import and supply of green gram, chick peas and canned fish.
- VAT rate on supply of jewellery reduced from 20 to 5 percent.

Exemptions/ other Development Measures

- Supply of electricity, fuel oil and machinery & equipment imported by Ceylon Electricity Board and Private Power Suppliers who supply electricity to the grid were exempted in order to reduce the electricity tariff especially on industries to provide competitive inputs to promote manufacturing & value added products.
- VAT was exempted on supply of prawns to support local producers while import of cattle, buffalos etc and livestock breeding items were VAT exempted to enhance availability of such animals to improve livestock production. VAT exemptions were granted on importation of machinery for modernization of factories in the plantation sector, importation of material for processing and manufacturing of leather products to boost this sector.
- VAT exemption on production, distribution or exhibition of films to boost local film industry, while exemption on importing and chartering of vessels were exempted from VAT to promote shipping industry as a thrust industry to generate foreign exchange earnings, employment etc.

Slower Growth in Excise Duties

- Revenue from Excise taxes on liquor, cigarettes, petroleum products, motor vehicles and selected consumer durables increased marginally by 5 percent in the first five months in 2007 to Rs. 37,305 million.
- Despite the rate revisions in liquor and cigarettes, the slower growth in hard liquor production, drop in sales of cigarettes, reduced value growth in vehicle imports

contributed to the slower growth in excise duty collection. The hard liquor production increased by 9 percent in comparison to the 21 percent growth in the corresponding period in 2006. Cigarettes sales also declined by 2 percent.

Table 1.4
Excise Tax Performance – (Jan. - May)

(Rs. Mn.)

Item	2006	2007	Growth
Liquor	8,483	9,639	14
Cigarettes	12,621	12,134	-4
Petroleum & Motor vehicles	13,297	14,123	6
Other	1,073	1,409	31
Total	35,474	37,305	5

Source: Department of Fiscal Policy

Excise Duty Changes

Rate Changes

- Increases were made to excise duty on liquor excluding beer and selected brands of cigarettes.
- 5 percent excise duty was imposed on polythene and paints.

Broadening the Tax Base

- The HS Codes pertaining to the vehicles were revised to close the existing loopholes.
- The markup on CIF for charging excise tax at the point of import was increased from 5 to 10 percent with effect from November 2006.

Exemption/ other Development Measures

- Removal of excise tax on certain items related to printing & packaging industry.
- Excise duty imposed on production of paints was reduced granting exemptions for manufacturers with a turn over of less than 50 million, to support the small scale paint manufacturing.
- Granting a concessionary duty rate for public servants to import vehicles.

External Trade Based Taxes Record a Moderate Growth

- Import duty collection at Rs. 22,697 million in January- May 2007 registered a 11 percent growth over the corresponding period of 2006. This growth should be viewed in the background of the duty waivers granted on several commodities to curb the rising cost of living slower growth in the value of motor vehicle imports and the Free Trade Agreements causing most tariff lines being placed at lower rate of custom duty.
- The effort to minimize the under valuation issue was continued and several items such as tyres, confectionaries were placed on specific duties. Also the customs surveillance mechanisms contributed to improve the duty collection.
- The revenue forgone due to with the duty waivers granted on essential commodities stood at Rs. 4,085 million by end May 2007.

Import duty changes

Broadening the Tax Base

- In order to fulfill the requirement of International Organization of the World Customs Organization prevailing Harmonized System (HS) Codes were revised while changes were done on motor vehicle chapter to clear the ambiguities and thereby close loopholes which were in existence.

Rate changes

- Specific duties were imposed on the following items.
 - . Tyres- Rs. 80/ Kg
 - . Chocolate- Rs. 60/ Kg
 - . Other confectionaries- Rs. 40/ Kg
 - . Salt - Rs. 5 Kg.

Administrative Measures

- Continuous improvements carried out in improving the custom surveillance mechanism

Exemptions / other Development Measures

- Duty waivers were granted on essential commodities to curtail rising cost of living.

Table 1.5
Import Duty Waivers Granted

Item	Applicable Duty	Waiver
Potatoes	Rs 20/kg	Rs 5/kg
Dried Fish	6per cent	Full
Sprats	6per cent	Full
Maldive Fish	6per cent	Full
Canned Fish	15 per cent	Full
B Onions	Rs 20/kg	Full
Red Onion	Rs 5/kg	Full
Sugar	Rs 10/kg	Rs 5/kg
Lentils	3 per cent	Full
Chilies	Rs 30/kg	Full
Cowpea	Rs 5/kg	Full
Chickpeas	15 per cent	Full
Green gram	Rs 5/kg	Full
Wheat Flour	15 per cent or Rs 12.50/kg	Rs 5/kg
Milk Powder	15 per cent	6 per cent

Source: Department of Trade, Tariff and Investment policy

- The existing duty exemptions granted to give an impetus to industries were further expanded to cover importation of machinery for modernization of factories of plantation sector, machinery used in poultry and film industries.
- Raw materials used for leather and livestock industries etc. were exempted to boost industries which has a high potential of adding high value to the overall production of the economy.
- Import of buses by the private sector to replace the existing buses was exempted to encourage the bus owners to increase their fleet as well as offer a better service to the commuters.

Other Taxes

- Revenue from Port and Airport Development Levy (PAL) generated Rs. 9,850 million during January- May 2005 compared to Rs. 7,508 million in the corresponding period in 2006, reflecting a 31 percent growth.
- Stamp Duty which came into effect from July 2006 generated Rs. 1,469 million within the first five months in 2007.
- Cess imposed on non essential imports yielded Rs. 5,180 million.
- The Regional Infrastructure Development Levy imposed on motor vehicles primarily to support the regional infrastructure development activities generated Rs. 593 million in the first five months in 2007.

Changes in other taxes

Rate changes

- PAL rate on items other than imports for exports was increased from 2.5 to 3 percent.
- Cess was imposed/ scaled up on identified non essential imports while Cess imposed on parts used for shoes has been removed.

Broadening the tax base

- A 10 percent markup on CIF was introduced for charging the Cess with effect from November, 2006.

Exemptions/ other Development Measures

- PAL rate was reduced to 2 percent on import of specified machinery used in apparel and textile industry.
- PAL was exempted on certain medical drugs used for terminal diseases.
- Removal of PAL on import of specified gems, diamonds and gold.
- Scaled up of Cess rates to support manufacture of straw and similar boards domestically and imposition of Cess on imported prawns, processed and unprocessed meat products, imported jewellery to support manufacturing/ producing of such items domestically.

Box 1.1

ACTIVITY REVIEW-FISCAL MEASURES -2007

Import Tariff

02.02.2007

- RPO 1/2007-Increase of the custom duty for petrol from Rs.5/- to Rs.20/- *gazette No 1482/28 of 01.02.2007*

15.05.2007

- RPO 2/2007-SAFTA Agreement & harmonized 2007 version (Commodity Coding System)& Trade & Tariff Cluster proposals –*Gazette No 1497/5 of 14.05.2007*

Excise Duty

01.01.2007

-Excise Notification No.892- *Gazette No 1477/25 of 29.12.2006*

29.01.2007

-Custom Ordinance-Approval of general rates of rebate- *Gazette No 1482/4 of 29.01.2007*

13.03.2007

-Excise Notification No.893, 894, 895, 896

- Increase of liquor rates-*Gazette No 1488/1 of 12.03.2007*

11.04.2007

-Excise (Special Provision) Act No.13 of 1989 (Section 3) Concessionary duties and taxes for vehicles imported by an officer- *Gazette No 1492/8 of 11.04.2007*

11.04.2007

-Excise (Special Provision) Act (Section 3C) - *Gazette No 1492/9 of 11.04.2007*

- Publish of motor vehicles exempted from excise duty

15 .05.2007

-Excise (Special Provision) (Amendment) Act No.13 of 1989- *Gazette No 1497/1 of 14.05.2007*

- Amendment of Chapter 87 to simplify the recovery of tax system

07.06.2007

-Excise (Special Provision) (Amendment) Act No.13 of 1989 order under Section 3 of the Act- *Gazette No 1500/21 of 06.06.2007*

- Revision of Cigarette rates

Cess

17.11.2006

- Sri Lanka Export Development Act No.40 of 1979 Section 14 (1) of the Act

- Removal of Cess on Imported parts of footwear and “B” onion- *Gazette No 1477/16 of 29.12.2006*

15.05.2007

- Sri Lanka Export Development Act No.40 of 1979 Section 14 of the Act

- Amendment of Chapter 87 to simplify the recovery of tax system-*Gazette No 1497/2 of 14.05.2007*

VAT

05.06.2007

-VAT (Amendment) Act No 06 of 2005 Section 2A of the Act *Gazette No 1500/20 of 06.06.2007*

- Reduction of VAT rate form 15% to 5% for Salmon ,Chickpeas & green gram

Other Tax Measures

14.05.2007

-Granting PAL exemption and concession for certain imported goods, under Section 2 of the Finance Act No.11of 2002- *Gazette No 1478/3 of 01.01.2007, Gazette No 1497/3 of 14.05.2007*

16.01.2007

-Finance Act No.11of 2006(Section 2(1)(b)(i)and(ii)) *Gazette No 1497/4 of 14.05.2007(Concession motor vehicles for tax payers)*

01.01.2007

-Granting Debit Tax exemption for Samurdhi Authority, under section 13 of Debit tax Act No.16 of 2002 - *Gazette No 1478/10 of 02.01.2007*

20.06.2007

-Economic Service Charge Act No. 13 of 2006 order under section 12 -*Gazette No 1502/10 of 20.06.2007*

01.01.2007

-Stamp Duty (Special Provision) Act No.12 of 2006

- Granting exemptions under Section 5
Gazette No 1478/7 of 01.01.2007

Other Measures

01.01.2007

-Turnover Tax Act No.69 of 1981

- Increased the Business Turnover tax Rate on liquor and Cigarettes for North and Eastern Provinces under Section 7- *Gazette No 1478/8 of 01.01.2007*

05.01.2007

-Increase of petrol prices by Rs.5/-

30.03.2007

-Increase of petrol prices by Rs.7/-

18.04.2007

-Increase of diesel prices by Rs.3/-, Kerosene by Rs.2/-, Furnace oil by Rs.3/-

27.04.2007

-Increase of petrol prices by Rs.1/-, Diesel by Rs.2/-

09.05.2007

-Increase of petrol prices by Rs.1/-, Diesel by Rs.2/-

16.05.2007

-Increase of Gas prices- Shell gas by Rs.38/-, Laugf gas by Rs.20/-

Non Tax Remained within the Estimates

- Non tax revenue at Rs. 22,950 million reflected an increase of 21 percent over first five months of the previous year. Profits and dividends from State Banks, Sri Lanka Telecom, Ports Authority, Telecommunication Regulatory Commission and fees & other charges boosted the non tax revenue during the period. Central Bank profit transfers amounted to Rs. 3,000 million.

Box 1.2

Finance & Revenue related Legislation (2006 Nov-2007 June)

Statute	Objective
Banking (Amendment) Act No. 46 of 2006	Since the banking Act did not permit the transfer of assets and /or liabilities of one Specialized bank to another, appropriate amendments were made to the Banking Act to provide for the transfer of assets and liabilities of certain failed banks to a state bank.
Finance (Amendment) Act No. 48 of 2006	An Act to amend the rates of the Port and Airport Development Levy providing exemptions and imposition of concessionary rates on items which are regarded as important to the interest of the national economy.
Value Added Tax (Amendment) Act No.49 of 2006	An Act to increase the markup on CIF for charging VAT at the point of customs with a view to minimizing the government revenue loss due to undervaluation of goods being imported.
Excise (Special Provision) Amendment Act 50 of 2006	An Act to increase the markup on CIF for charging Excise Duty at the point of customs with a view to minimizing the government revenue loss due to undervaluation of goods being imported.
Regional Infrastructure development Levy Act no.51 of 2006	An Act to provide for the imposition of a levy applicable for the motor vehicles, which are liable for payment of Excise duty under the Excise (Special Provisions) Act.
Value Added Tax (Amendment) Act no 14 of 2007	An Act to introduce exemptions, reduction of rate to 5%, introduction of VAT withholding provisions changes to input tax credit for certain items by amending the VAT Act No 14 of 2002
Inland Revenue Act No. 10 of 2007	An Act to provide legal provisions for the proposals in relation to the Income tax in the budget speech 2007 such as treatment of life and general insurance business separately, exemption for income from sale of shares of unit trust, provision of tax free threshold of Rs.600,000 for partnerships by amending the Income Tax Act no 10 of 2006.
Economic Service Charge Act No.15 of 2007	An Act to amend the threshold of ESC, 3 years tax concession for manufacturing institutions from ESC, reduction of ESC rate for certain businesses.
Finance Act No.13 of 2007	An Act to amend the Finance Act No.11 of 2006 (Imposition of Motor Vehicle Concessionary levy) Finance Act No.5 of 2005 (Construction Industry Guarantee Fund Levy), Finance Act No.11 of 2002.
Debit Tax (Amendment) Act No 12 of 2007	An Act to include saving accounts maintained by finance companies, current accounts maintained by specialized banks in order to create a level playing field. Also to exempt "Treasury Bond Investment External Rupee Account" from Debit Tax.

Policy Thrust to Rationalize Public Expenditure

- New rural development initiatives continued to be targeted to the poorest divisional secretariats in the country and the conflict affected areas, especially the newly liberated areas in the Eastern Province through programs such as “*Jathika Saviya – Gama Neguma*”, “*Maga Neguma*” and other pro – poor , pro – growth initiatives.
- Cadre management and new recruitment guidelines were put in to place within the budgetary allocation while striking a balance to enable the smooth functioning of the public sector service mechanism.
- New circular instructions were issued with regard to the public servants housing loans revising the interest rates of such loans ensuring the interest cost of these loans for the lower salary earners in the public sector remains unchanged.
- With the removal of the fuel subsidy, a subsidy package is being worked out to cushion the burden on vulnerable segments such as Samurdhi beneficiaries, fisherman and three wheeler owners. Although Ceylon Petroleum Corporation has revised the prices periodically, domestic petroleum products are being sold at a price less than the cost price. The package that has been worked out on petroleum products would ensure to minimize the present burden on Ceylon Petroleum Corporation while creating a safety net for the poorer segment of the society.
- Government borrowing program was managed through the use of least cost borrowing instruments through selection of an appropriate mix between domestic and foreign debt. The decisions to allow foreigners to invest in Treasury bonds have paid dividends and by end May US \$ 460 million had been invested there by easing the preserve on domestic market borrowing.
- To arrest the deficiencies in the present fund transfer system between the Treasury and line ministries and vice versa action has been taken to move towards a treasury single account. This will enable the utilization of all unused cash balances in Government bank accounts on overnight basis resulting in a considerable savings on the interest payable by the Government. With this operation the unused cash balances in the system could be used to reduce the Treasury overdraft balances on a daily basis.

Government Expenditure

- The overall public expenditure for the first five months of 2007 stood at Rs. 318,023 million which constituted of Rs. 247,623 million of recurrent expenditure and Rs.70,400 million of capital expenditure. Notable feature of the government expenditure during this period was despite the additional pressure exerted on the budget through increase recurrent expenditures in the areas of salaries, pensions, interest payments and security related expenditure, the commitment to accelerate development programmes in areas such as road development, water and sanitation, health, education and provincial development activities continued through local funds and foreign aid disbursements.

Table 1.6
Performance of Government Expenditure- (Jan. – May)

(Rs. Mn.)

	2006	2007(prov.)
Current expenditure	222,614	247,623
Salaries and wages	65,998	85,496
Interest	62,036	71,300
Samurdhi	3,844	3,850
Fertilizer subsidy	6,374	6,600
Pension	22,752	27,131
Other expenditure	61,610	53,246
Capital expenditure	60,157	70,399
Large infrastructure	23,402	30,800
Provincial Councils	3,129	4,365
Small infrastructure and other	33,626	35,234

Source: Dept. of National Budget

Salaries and Pension

- Expenditure on salaries to public servants increased to Rs. 85,496 million, 30 percent increase over the corresponding period of the previous year. The cost of living allowance and new recruitments and filling up of vacancies to provide a better public service

delivery system contributed to the salary increase. Further, the recruitments necessitated to strengthen the national security and protecting the newly liberated areas, also enhanced the salary bill.

- Total pension payments increased by 19 percent to Rs. 27,131 million mainly reflecting the pension increases and cost of living allowance payment announced in the budget and full impact of around 18,000 retirees enrolled as pensioners last year at enhanced scales.

Upward Pressure on Debt Servicing

- Interest payment on foreign and domestic debt amounted to Rs. 71,300 million registering a 15 percent increase mainly due to increase in domestic interest rates on government securities in response to the upward adjustment in policy rates by the Central Bank of Sri Lanka coupled with the tendency in investing in short term maturity debt instruments. The depreciation in the exchange rate also partly contributed to the high interest cost. Re- profiling the public debt portfolio, a better debt management mechanism and alternative financial arrangement has become a paramount requirement in the control of rising interest rates.

Table 1.7
Behavior of Yield Rates - 2007

Year	Treasury Bills			Treasury Bonds			
	91 days	182 days	364 days	2 year	3 year	4 year	5 year
2006 May	10.09	10.36	10.38	-	10.9	10.92	10.95
2007 Jan	12.84	12.96	13.05	-	12.35	-	12.36
2007 Feb	13.61	13.81	14.16	13.35	13.1	13.81	13.35
2007 Mar	14.34	14.43	14.41	14.07	14.1	14.13	13.68
2007 Apr	15.34	15.15	14.49	-	14.2	-	13.67
2007 May	16.59	16.34	16.21	-	14.24	-	13.67
Change	6.5	5.98	5.83	-	3.34	-	2.72

Source: Department of Treasury Operations

Welfare Payments and Social Safety Net on Vulnerable Groups Continued

- Strengthening the rural economy through pro-poor growth initiatives continued in 2007 to support the vulnerable groups through a social safety net while enhancing the income generating activities of such groups.

- Samurdhi assistance amounted to Rs. 3,850 million while other welfare programmes such as providing nutritional food package, free text book, season tickets, bursaries, assistance to disable soldiers continued with an enhance cost.

Table 1.8
Welfare payment and subsidies- (Jan.-May)

(Rs. Mn.)

Item	2006	2007
Children		
Infant Milk Food Subsidy	30	32
Poshana Malla	30	33
Triposha Programme	102	115
Free Text Books & Uniforms	495	575
School Season Tickets	150	190
Dharma School Text Books & Uniforms	30	34
School Nutritional Foods	350	389
Agriculture		
Interest Subsidy for Agricultural Loans etc	30	35
Fertilizer Subsidy	6,374	6,600
Welfare Payments		
Samurdhi Relief	3,844	3,850
Assistance to Disabled Soldiers	2,031	3,400
WFP food Assistance	500	520
Flood and Drought Relief	75	57

Source: Dept. of National Budget

- “*Jathika Saviya -Gama Neguma*” program , a community based integrated rural development initiative to empower the poor was further strengthened in 2007. The cost of the program was Rs. 1,890 million as at May, 2007.

Table 1.9
Summary of Gamma Neguma Jathika Saviya- as at May, 2007

District	PS/Urban	GN Division	No. of Projects	Allocation Rs. Mn.
Colombo	8	144	135	32.10
Gampaha	13	266	234	118.40
Kalutara	14	242	238	60.20
Galle	19	268	262	125.00
Matara	15	216	210	108.60
Hambantota	11	144	128	101.50
Kandy	19	279	294	146.10
Matale	11	146	146	74.00
Nuwara Eliya	6	144	142	84.80
Anuradhapura	19	256	252	128.00
Polonnaruwa	7	114	108	50.60
Kegalle	11	223	217	96.70
Ratnapura	16	268	265	131.50
Puttalam	12	207	198	96.30
Kurunegala	18	347	341	170.50
Ampara	16	189	143	71.40
Trincomalee	11	103	100	51.10
Batticaloa	3	50	17	70.00
Badulla	17	216	216	112.40
Moneragala	11	124	124	60.90
Total	257	3,946	3,800	1,890.10

Source: Ministry of Nation Building

- The cost as the “*Maga Neguma*” programe designed to improve the rural infrastructure was Rs. 700 million by end May 2007 uplifting around 200 Km. of rural roads.

Enhanced Assistance for Agriculture

- The fertilizer subsidy targeted the small holder agriculture to assist low income families was continued at a cost of Rs. 6,600 million by end May 2007.
- The advances provided for the purchase of paddy through Government Agents through the revolving fund established amounted to Rs. 1,600 million by end May, 2007. Through the recoveries of the advances granted earlier created an environment of smooth functioning of the revolving fund established for the paddy purchases. This has resulted to mitigate the burden on the government budget.
- Other operations channeled to agriculture by way of interest subsidy for agriculture credit, restructuring credit for paddy mills and provision of agricultural seeds stood at Rs. 35 million as at May 2007.
- Maintaining a high tariff on import of wheat flour and grain was continued to re-orient consumption towards rice.
- The profit on processed agriculture products was exempted from income tax and this was expanded to cover diary products such as curd, yogurt etc.

Resettlement of displaced community in the newly liberated areas and other development activities gathered momentum

- Resettlement of internally displaced persons (IDPs) in Eastern Province has been carried out during this period. Resettlement of IDPs in Eruvil, Poraithivu Parru, Pattipola and Vawnathivu and Vakarai in Batticaloa District has been completed. In areas such as Verugal and Eachchcail Pattu in Trincomalee District, the resettlement is in progress. So far around 130,000 families have been resettled in these areas.
- Providing of basic needs such as electricity, building of roads, bridges etc and revamping the government administration mechanism is underway. The cost incurred in the resettlement, development activities and humanitarian work was around Rs 288 million.

Increase Spending on Development Programs

Human Resource Development

- Total expenditure on health, skills development and education stood at Rs.48 billion up to May 2007 compared to Rs 42 billion in the corresponding period in 2006.
- The medical supplies cost was Rs. 1,572 million by end April.
- To address the human resource shortage, recruitments in the health sector continued in 2007. 1,146 nurses, 732 medical officers, 712 midwives, and 311 other technical grades were absorbed to the system.

Roads

- The investment on road sector was around Rs. 12 billion up to May 2007. This includes Rs 2, 881million on express ways development, Rs.4, 954 million on highways development, Rs 542 million on construction of bridges and flyovers and Rs. 911 million on Tsunami effected roads.
- Several major road projects such as Ambalangoda – Elpitiya Road (21 kilometer) Gampola – Nuwara Eliya road (54 Km) and three roads affected by the floods in Galle and Rathnapura districts were completed during the period.

Water Supply

- Water and sanitation project cost for the first five months in 2007 amounted to Rs. 6,500 million.
- Large scale water supply schemes in several townships were undertaken in 2007. The water treatment plant with a capacity of 126 million gallons per day was commissioned in Ampara while 50 Km pipeline in Ninthavur, 180 Km long distributing pipe lying in Galle were completed in this period. Work on 7 million gallons per day water treatment plant in Peradeniya has been started and work on 6 reservoirs under this programme has been completed.
- Rs. 337 million has been spent on Tsunami affected areas water supply schemes during the first quarter to supply water to resettlement sites as well as for the expansion and improvement in distribution and transmission system in the area of Pottuvil, Kalutara, Matara, Tangalle Hambantota, Kirinde, Ambalnatota, and Thirikovil etc.

- Rs. 450 million has been spent for rural water supply during the first quarter for the construction of water supply schemes in 240 Grama Niladari Divisions in Gampaha, Ratnapura, Anuradhapura, Matale & Badulla districts.
- Also water supply schemes in 282 Grama Niladari Divisions have been commissioned in Matale, Kandy, Nuwara Eliya and Kurunegala Districts benefiting about 70,000 families.

Government Treasury Operations

Cash Operations

- The net cash out flow from operating activities, by the end of May 2007 amounted to Rs. 11.6 billion, as there has been a marginal shortfall in the cash inflow in the form of revenue. The Government's cash operations, after investment activities, during the first five months (Jan – May) in 2007 indicated a net cash deficit of Rs. 54.3 billion, compared with Rs. 45.7 billion during the corresponding period in 2006. Cash outflow from investment activities increased by Rs. 2.3 billion over the original cash flow estimates. The repayment on debt was in par with the estimates, and gross borrowings were raised to meet the cash deficit of Rs. 66 billion.
- The overall closing balance which corresponds to working overdraft balance with the banks increased from Rs.31.6 billion at the beginning of the year to Rs. 33.4 billion at the end of May 2007.

Table 1.10
Statement on Government Cash Flow Operations – (Jan. May)

(Rs. Mn.)

Item	Actual 2006	Original estimate 2007	Actual cash flow 2007
Total cash inflows from revenue	175,729	229,016	218,180
Total cash outflow from operating activities	(211,454)	(232,714)	(229,802)
Net cash flow from operating activities	(35,725)	(3,698)	(11,622)
Cash flow from investment activities	(45,682)	(51,968)	(54,298)
Net cash surplus (deficit)	(81,407)	(55,666)	(65,920)
Opening cash balance	(10,989)	(31,622)	(31,622)
Gross borrowing	170,953	170,435	173,650
Debt repayment	(98,665)	(87,449)	(87,431)
Net borrowing	72,288	82,986	86,219
Adjustment Account Balance (TEB, RFA, deposits. etc.)	1,675	23,793	22,094
Closing balance	(21,783)	(28,095)	(33,417)

Source: Department of Treasury Operations

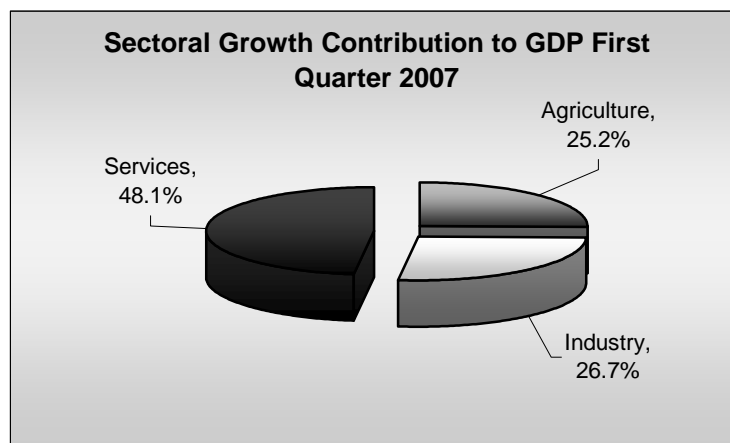
Chapter 2

The Economy

Growth Momentum Continues

- The Sri Lankan economy continued to display strong growth momentum with the GDP registering 6.1 per cent growth in first quarter in 2007, despite a reduction in the output of some major agricultural products. Industry and service sectors grew by over 7.0 per cent in the first quarter. In the agricultural sector output of livestock, highland crop productions, fruit and vegetable production improved while decreases were recorded in paddy and minor export crops due to unfavorable weather in the fourth quarter in 2006 and the first quarter in 2007. The agriculture sub sector maintained the same levels as in the first quarter in 2006.

Chart 2.1



- The manufacturing sector indicated a 5.4 percent growth for this quarter compared to 4.1 percent in the first quarter of 2006. The textile and garment industry sustained its resilience in the context of highly competitive global trading environment and grew by 5 percent against 0.9 percent recorded for the same period in 2006. The construction industry recorded an impressive growth of 9.5 percent continuing its strong growth momentum.
- The service economy recorded a buoyant 7.1 per cent growth in the first quarter in 2007. Value added in export trade increased by 7.7 percent while domestic trade industry rose by 6.4 percent. Displaying the sustained dynamism of the telecommunication sector the number of fixed and mobile telephones by 52.4 and 61 percent respectively during this period. Reflecting the expansion in the banking and insurance activities, the financial

sector grew by 6.5 percent. Volume of port activities expanded considerably with a 26.2 percent increase in cargo handling and 33.8 percent increase in transshipment cargo. With the increased recognition of effective public service delivery, the Government services grew by 7.6 percent compared to 6.7 percent in the first quarter in 2006.

Table 2.1
Gross Domestic Product – Sectoral Composition (2002) Constant Prices
(Rs. Mn.)

	2006 1 st Q	2007 1 st Q
Agriculture, Forestry and Fishing	73,915	73,900
Agriculture, Livestock and Forestry	69,096	67,747
Tea	6,729	5,534
Rubber	744	822
Coconut	7,103	7,161
Minor export crops	1,858	1,774
Paddy	18,760	17,303
Highland crops	9,735	10,174
Fruits	416	438
Vegetables	13,301	13,534
Livestock	3,872	4,107
Other Agriculture	3,643	3,779
Firewood & Forestry	2,934	3,121
Fishing	4,819	6,153
Industry	144,519	154,637
Mining and Quarrying	9,429	10,763
Manufacturing	93,644	98,685
Processing Industries	3,675	3,555
Factory industry	83,700	88,553
Small industries	6,269	6,577
Electricity, gas and water	10,686	11,492
Electricity	9,260	9,760
Gas	882	1,148
Water	544	584
Construction	30,760	33,697
Services	306,150	327,792
Wholesale and retail trade	127,875	134,403
Import trade	42,635	43,442
Export trade	22,168	23,883
Domestic trade	63,072	67,078
Hotels and restaurants	1,933	1,830
Transport and communication	63,746	71,077
Transport	54,917	60,731
Cargo handling-Ports and Civil aviation	3,095	3,561
Post and telecommunication	5,736	6,784
Banking , insurance and real estate etc.	45,334	49,231
Ownership of dwellings	17,867	18,065
Government services	37,291	40,141
Private Services	12,103	13,046
Gross Domestic Product	524,583	556,329

Source: Department of Census & Statistics

Downward Trend in Unemployment

- With sustained high economic growth over the preceding 3 years, country's unemployment rate declined further to 6.8 percent in the first quarter in 2007 compared to 7.2 percent in the first quarter of last year. The numbers employed in industry and service sectors had increased by around 39,000 during the first quarter in 2007.

Table 2.2
Unemployment Rate

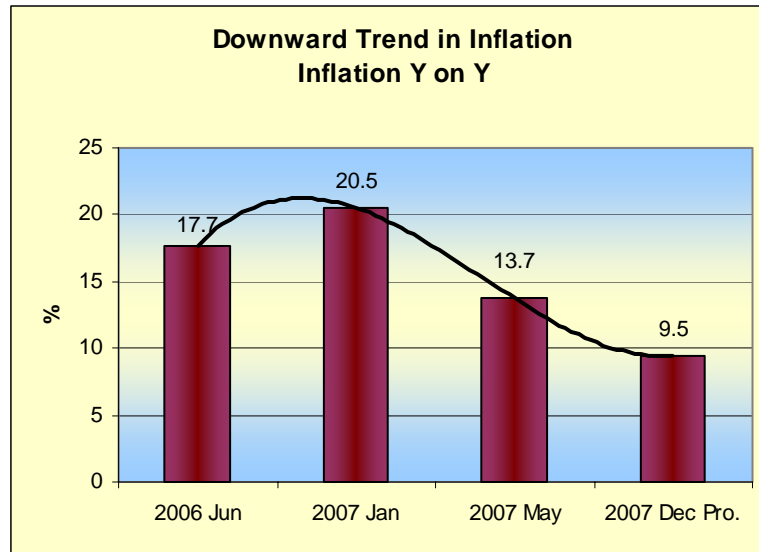
Period	Rate
2002	8.8
2003	8.1
2004	8.1
2005	7.2
2006 Q1	7.2
2007 Q1	6.8

Source: Department of Census and Statistic

Inflation on a Declining Path

- Owing to both fiscal and monetary measures taken to arrest the price pressures as well as reflecting the inflation pattern in Sri Lanka as expected inflation rate started to decline after the first few months of this year.
- The duty waivers granted on essential commodities together with strict targeting of monetary policy and strengthened fiscal consolidation helped to curb the rate of increase in prices in the recent months. The policy interest rates were further raised by 50 basis points in February 2007, by the Central Bank of Sri Lanka while becoming more aggressive in the conduct of open market operations to mop up excess liquidity. Market interest rates reached a new hike causing roll over debt to rise from an average of 11.7 per cent to 16.64 per cent during the first half in 2007 compared to the first half in 2006.

Chart 2.2



- The point to point inflation by end May declined to 13.7 percent from the peak of 20.5 percent in January 2007. The current projections for the year indicate the possibility of inflation will decline to 9-10 percent by end 2007.

Table 2.3

Inflation Trend Point to point

Month	CCPI		SLCPI	
	2006	2007	2006	2007
January	8.0	20.5	3.2	17.8
February	7.1	19.2	3.5	18.1
March	6.4	19.5	4.0	18.6
April	9.2	16.3	5.3	16.3
May	13.2	13.7	8.4	
June	17.7		10.7	
July	14.7		9.9	
August	15.3		10.9	
September	15.4		11.5	
October	17.2		12.6	
November	19.8		16.4	
December	19.3		17.9	

Source: Central Bank of Sri Lanka

External Sector Development

Buoyant Export Growth

- Exports grew by 11.5 percent during the first 4 months in 2007 compared with 8.4 percent growth during 2006 indicating a somewhat faster rate than expected at the beginning of the year. The total exports earning in the first four months in 2007 amounted to US\$ 2,252 million.
- The favorable external demand and opening up of new world markets contributed to the buoyancy of exports. Agriculture exports grew by 11 percent where tea exports grew by 5 percent with the diversification of agricultural products to more value added products, minor agricultural exports increased by 16.1 percent during the period. The value of textile and garments recorded a healthy growth of over 10 percent while overall industrial exports grew by 11 percent.

Decline in imports

- Imports, after growing by 15.7 percent in 2006 slowed down to 7.4 percent during the first 4 months in 2007, while maintaining the growth momentum of development oriented goods. Import of investment goods increased by 11 percent during the first four months in 2007. Total imports amounted to US \$ 3, 303 million during the first four months compared to US \$ 3,071 million in the same period in 2006.
- The cost of petroleum imports continued to be a heavy burden on the balance of payment. Petroleum products imports absorb 27 percent of the export earnings costing US \$ 623 million in the first four months in 2007. The forecasts showing continuation of high crude oil prices in the balance period in 2007, the total oil bill is likely to be in the region of US \$ 2, 200 million by end of this year, a level slightly lower than the inflow of worker remittances.

Trade deficit

- Reflecting these developments, the cumulative trade deficit by April reached US \$ 1,050 million against the US \$ 1,056 million in the corresponding period in 2006.

Services and Transfer Flows

- Service account continued to record surpluses due to earnings from port activities, coupled with new emerging services such as IT exports and communication services such as Business Processing Outsourcing. These developments helped to mitigate the declined tourist earnings.
- Reflecting the increase in average earnings by migrant workers and increased transfers from the workers, through enhanced bank mobilization of private remittances amounted to US\$ 864 million in the first four months in 2007, a 17.4 percent increase compared to the same period in 2006.

Overall Balance and Official Reserves

- The Balance of Payment (BOP) had generated a surplus of US\$ 250 million by end of May 2007 compared to US \$ 158 million at the end May 2006.
- Gross official reserves have increased to US\$ 2.8 billion at end May 2007 from US \$ 2.5 billion at end 2006, while total reserves reached US \$ 4 billion by end April 2007. The official and total reserves of the country were sufficient to cover 3 months and 4.7 months of country's imports respectively.

Table 2.4**Performance of External Trade - (Jan-April)**

US\$ Mn.

	2006	2007
Exports	2,021	2,253
Agriculture	384	430
Tea	267	282
Other	116	148
Industrial	1,574	1,756
Food, Beverages and Tobacco	130	144
Textiles and Garments	899	996
Rubber products	115	133
Diamond and Jewellery	98	105
Other	332	378
Mineral	51	47
Unclassified	11	20
Imports	3,077	3,304
Consumer goods	560	652
Food & Drink	273	336
Other Consumer Goods	288	315
Motor Cars & Cycles	90	107
Intermediate goods	1,790	1,828
Petroleum	639	632
Fertilizer	69	33
Chemicals	77	94
Textiles & Clothing	438	489
Diamonds	71	79
Other Intermediate Goods	496	500
Investment goods	697	774
Machinery & Equipment	354	356
Transport Equipment	113	124
Building Materials	175	215
Other Investment Goods	55	80
Unclassified	31	50
Trade Balance	(1,056)	(1,051)

Source: Central Bank of Sri Lanka

Financial Sector Developments

- Financial markets responded to the tightening of monetary policy through a significant upward movement of interest rates. This altered the demand structure of government debt instruments, with market participants, preferring more short- term instruments.
- The Central Bank of Sri Lanka maintained the reserve money within the targeted levels reflecting a growth of 17.3 per cent in the first quarter of 2007. The expansion in reserve money was entirely due to increase in Net Foreign Assets (NFA) of the Central Bank while Net Domestic Assets (NDA) has declined indicating a decline in T-bill holding.
- The broad money growth has decelerated by April 2007 recording 16.8 per cent growth in April 2007. Both the expansion in NFA and NDA has contributed to the monetary expansion during the first four months. Net foreign assets of the banking system increased and contributed around 32 per cent of the monetary expansion during the period. However this has been entirely due to the increase in NFA of the Central Bank.
- Net credit to government during the first four months in 2007 has declined by Rs.27 billion, outperforming the target levels. The improvement was mainly reflected from the decline in Treasury bill holding of the Central bank.
- Credit to the private sector continued its high growth trend thus far in 2007 in line with expanding economic activities, credit promotion schemes offered by banks

Chapter 3

Foreign Assistance

Foreign Aid Commitments

- The total aid commitment made by the donors to Sri Lanka by signing necessary loan/grant agreements during the period of January to end of May 2007 amounted to US\$ 874 million (Table 3.1). This comprised of US\$ 803 million in project loans and US\$ 71 million in grants.

Table 3.1
Aid Commitments (Jan. - May, 2007)

Donor	US\$ Mn.
Japan	362.8
Asian Development Bank	300.0
China	66.1
World Bank	32.5
IFAD	22.9
Spain	17.0
Germany	17.2
Export Credit	12.7
Other	43.1
Total	874.3

Source: Department of External Resources

Chart 3.1
Donor Share of Aid Commitments from January to May 2007

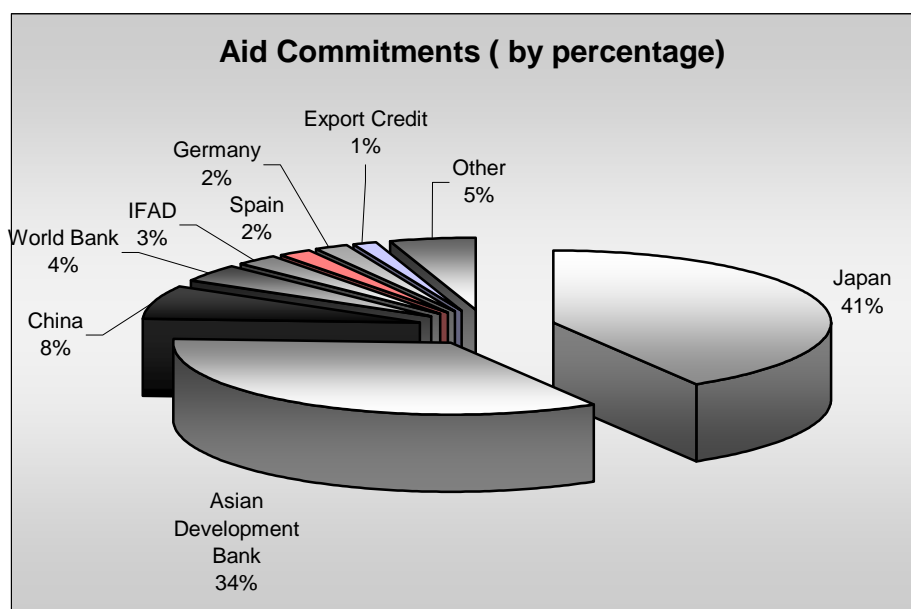


Table 3.2
Loan / Grant Agreements Signed - 01.01.2007 to 31.05.2007 (By Sector)

			US\$ Mn.	
Sector	Country	Project Name	Loan	Grant
Roads and Bridges	Japan	Greater Colombo Transport Development Project.	186.6	
	Japan	Detail Design & Construction of Mannar Bridge & Improvement of Causeway		15.7
Rural Development	Japan	Pro-Poor Rural Development Project	34.8	
Water supply	Japan	Water Sector Development Project	112.7	
	Austria	Greater Colombo Sewerage Rehabilitation System II	12.7	
	Spain	Design Supply & Setting up of two water treatment plants at Galle & Negombo	17.0	
Agriculture	Japan	Japanese 2KR Food Production Grant - 2006		2.8
	FAO	Hybrid Rice Development & Use for Food Security		0.3
	IFAD	Smallholder Plantation Entrepreneurship Dev. Programme	22.9	
	Germany	Food Security of Conflict Transformation		3.7
Housing & Rehabilitation	France	Construction Sector Support Project [for Post Tsunami reconstruction]	13.6	
	Germany	Northern Rehabilitation Project		1.3
	World Bank	Puttalam Housing Project	32.5	
	Germany	Resource Network for Conflict Studies		3.6
Railway	China	Supply of 100 Nos . Railway Passenger Carriages.	27.2	
	China	Supply of 15 Nos. Diesel Multiple Units	38.9	
Power & Energy	USA	Oil and Gas Regulatory Project		0.5
Ports & Shipping	ADB	Colombo Port Expansion Project	300.0	
	Netherlands	Supply of two Multipurpose River sea Vessels 7400 DWT under the ORET Programme		11.7
Health, Education & Social Welfare	UNICEF	UNICEF Country program 2007		11.8
	Germany	Education for Social Cohesion [ESC]		3.3
Other	Japan	Japan's Non-Project Grant Aid		10.2
	UNDP	Institutional Strengthening - Phase V		0.1
	Germany	Microfinance System Development		5.3
	Sweden	Quality Infrastructure Development Project		1.1
	Norway	Delimitation of the Outer Edge of the Continental Margin of Sri Lanka	4.0	
Sub Total			802.9	71.4
Grand Total		Loan+ Grant	874.3	

Source: Department of External Resources

- The Government of Japan committed US\$ 338 million for infrastructure projects in the areas of roads, water and rural development. The Greater Colombo Urban Transport Development project is the largest project included in the Japanese aid package with an allocation of US\$ 187 million. For the development of water sector, the Government of Japan committed US\$ 113 million. It includes the implementation of Greater Kandy water Supply project, Second Phase of the towns north of Colombo Water Supply Project, Greater Colombo Water Rehabilitation Project and Kandy City Wastewater Disposal project.
- In addition, Japan has committed US\$ 35 million for the pro-poor rural development project to mitigate regional inequalities by enhancing accessibility through rehabilitating and upgrading of national and provincial roads in economically backward areas. Under the Japanese grant assistance programme, US\$ 15.9 million has been provided for the construction of a New Bridge connecting the Mannar Island to the Mainland and improvement of its Causeway.
- The Asian Development Bank has provided US\$ 300 million for the Colombo Port Expansion project. The activities financed under the project includes construction of breakwater, the dredging of approach channels and harbor basin, relocation of the submarine oil pipeline, construction of ancillary facilities as well as the provision of navigational aids. The construction of the first container terminal and procurement of associated handling equipment will be done through the private sector financing. The Government will select the concessionaire for at least the first two terminal components through open competitive bidding. The objective of the project is to promote the country's economic growth by improving the competitiveness of Sri Lanka in international trade through expansion of the Colombo Port using public-private partnership to maintain its status as a regional transshipment hub port.
- The funds committed from the Government of China will be utilized for the procurement of 15 Diesel Multiple Units and 100 Passenger Carriages for the railway sector development. Diesel Multiple units will facilitate significantly improving Colombo sub-urban train service. The new 100 carriages will be utilized mainly to strengthen long destination and intercity services.

- The World Bank provided US\$ 33 million to implement the infrastructure and housing development project in Puttalam district to provide basic infrastructure facilities for 20,600 internally displaced families and other families in the area.

Committed Undisbursed Balance (CUB)

- At the end of May 2007 the total Committed Un-disbursed Balance (CUB) available for the Government's development programmes (including post Tsunami reconstruction activities) amounted to US\$ 4.7 billion. The utilization of these commitments involves 3 to 5 year time frame depending on the duration of the project implementation. Generally, a utilization of one-fifth to one-fourth of the committed funds each year is considered satisfactory. Table 3.3 indicates the sectoral classification of the committed un-disbursed balance.

Table 3.3

Committed Un-disbursed Balance - (by sector) as of 31st May 2007

Sector	US\$ Mn.	% of Total
Agriculture, Irrigation, Forestry, Land & Environment	267.1	5.7
Roads, Bridges, Ports & Aviation	1,342.2	28.0
Financial Management	139.5	3.0
Health, Social Welfare, Education & Vocational Training	297.8	6.0
Power & Energy	590.3	12.0
Tourism, Media & Cultural Affairs	39.1	0.8
Fisheries	42.4	0.9
Housing and Urban Development	79.3	1.8
Trade, Industrial Development & Information Technology	96.9	1.9
Plantation	39.2	0.8
Private Sector Development	112.0	2.3
Rehabilitation	181.2	4.0
Rural Development	125.1	3.0
Tsunami Rehabilitation	916.6	19.0
Water Supply and Sanitation	424.7	9.0
Other	70.2	1.6
Total	4,763.6	100

Source: Department of External Resources

Foreign Aid Disbursements

- The total foreign aid disbursement by end of May 2007 amounted to US \$ 331 million on account of project loans and grants. Of the total disbursement, project loans accounted for

US \$ 219 million and grants accounted for US \$ 112 million. Table 3.4 shows the disbursement of funds by each donor during the review period in 2007.

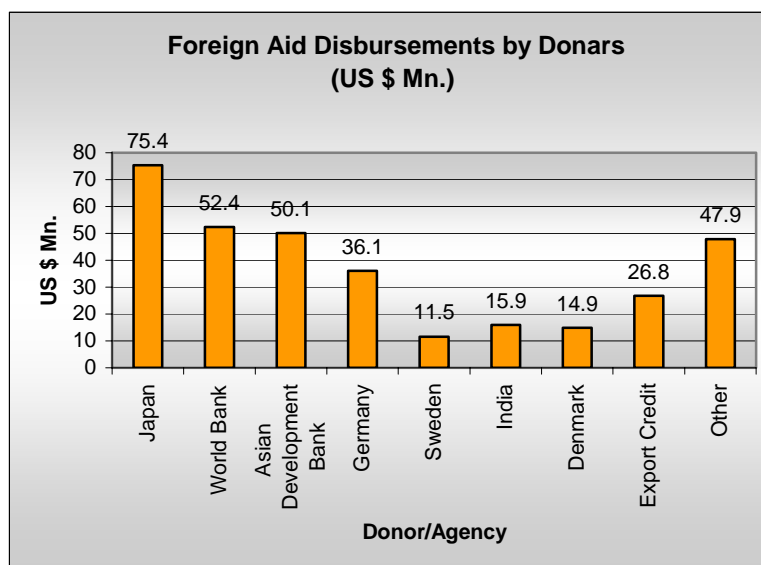
Table 3.4
Foreign Aid Disbursement (January to 31st May 2007)

Donor	US\$ Mn.
Japan	75.4
World Bank	52.4
Asian Development Bank	50.1
Germany	36.1
Sweden	11.5
India	15.9
Denmark	14.9
Export Credit	26.8
Other	47.9
Total	331.0

Source: Department of External Resources

- The Government of Japan maintained its leading position among development partners with the total disbursement of US\$ 75.4 million as of 31st May 2007 which accounted for about 23 percent of the total disbursement. During this period, both the World Bank and ADB had recorded over US\$ 100 million disbursements under their commitments. A substantial amount of disbursements, amounting to US\$ 36.1 million were also made as development assistance from Germany.

Chart 3.2
Foreign Aid Disbursements by Donors



External Debt

- Total stock of external debt of the government as at end May 2007 stood at US\$ 10.7 billion. This was an increase of US\$ 100 million compared to the debt stock stood at end 2006.
- The total debt service payment up to 31st May 2007 amounted to US\$ 383 million. Of this US\$ 311 million was for principal repayments and the balance US\$ 72 million was for the interest and other charges. The debt service payments made during this period accounted for 44.5 per cent of the estimated debt service of US\$ 860 million for 2007.

Sri Lanka Development Forum

- The Sri Lanka Development Forum 2007 was held on 29 - 30 January, 2007 in Galle, Sri Lanka, under the chairmanship of His Excellency Mahinda Rajapaksa, The President of Sri Lanka with participation of over fifty countries and international donor agencies. The Forum provided an opportunity to engage in a wider consultation process with all the donor community on “Mahinda Chintana: Vision for a New Sri Lanka – A Ten Year Horizon Development Framework for 2006 – 2016”, Assessment of Post Tsunami Recovery and Reconstruction Challenges and Emerging Issues, “*Gama Neguma*” and the Development of Lagging Regions and Partnership in Development and Peace. The Government presentations also focused on issues related to security, law and order, conflict, terrorism and peace, human rights, humanitarian and resettlement challenges, reconstruction of conflict affected areas, the continuing role of civil society and donor assistance. The Forum also reviewed the progress made in the utilization of development assistance in 2006 and some of the implementation challenges.