

Budget 2024

Background, Highlights and Policy Direction

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Presented at the Seminar on “*Navigating Economic Recovery: Sri Lanka’s Fiscal Policy, Investment Strategies and Future Prospects*”, organized by the Organization of Professional Association and held on 20 November 2023

Background

We all are well aware of the unprecedented multiple crises faced by Sri Lanka at present.

It has deep roots: **the country has long lived beyond its means** – borrowing too much and taxing too little – and produced below its potential.

It is also a result of several years of populist & and shortsighted policymaking, policy mis-steps & mismanagement, corruption vulnerabilities, political instability, and an overall lack of good governance.

Coupled with the impacts of external shocks such as the COVID-19 pandemic and the Russia – Ukraine conflict, **the country plunged into its worst-ever crisis in 2022.**

People's standards of living were devastated, with the heaviest blow to the poorest and most vulnerable and jeopardizing Sri Lanka's decades-long human capital gains with multiple challenges, including severe threats to nutrition, food security, healthcare, and education.

Widespread protests, mainly as a result of the above factors, were continuing with no clear path or hope for the future of the country.

Sri Lanka was on the brink of economic and social collapse.



Sri Lanka hospitals issue SOS as vital drugs, equipment run out
 Doctors warn deaths could exceed COVID and other disasters combined

MUNZA MUSHTAQ, Contributing writer
 April 12, 2022 14:15 JST

CRISIS: Drug Shortage List in Sri Lanka

🕒 April 9, 2022

The country continues to suffer severe shortfalls c from fuel to electricity. But health experts caution system could drive an escalation in deaths, if immr supplies.

DONATE

13th death reported in Sri Lanka fuel queues

IAN S / Jul 5, 2022, 15:47 IST

SHARE



Sri Lanka crisis forces 13-hour blackouts, hospitals stop surgery
 Power regulator urges government employees to work from home to save fuel and hospitals suspend routine surgeries as economic crisis deepens.

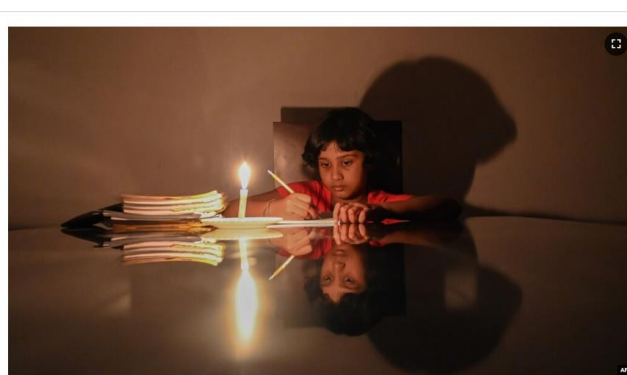


A woman works inside a shop attached to her house during a power cut in Colombo [Dinuka Liyanawatte/Reuters]

31 Mar 2022



Sri Lanka Imposes Power Cuts as Cash Crisis Deepens



A child studies at her home during a power cut in Biyagama, a suburb of the capital Colombo, Sri Lanka, Feb. 2, 2022.

SRI LANKA'S FOOD EMERGENCY

As Sri Lanka faces an unprecedented economic crisis, the soaring cost of living burns hole in Sri Lankans' pockets

NEWS18 creative



Lessons Learned.... (1)

- The socio-economic crisis in 2022 underlined many lessons that the country failed to grasp, despite the recurrence of such macroeconomic failures throughout its post-independence history.
- **This economic episode reiterated the,**
 - essentiality of data-driven policymaking
 - **devastating implications of ad hoc policy experiments**
 - crippling welfare impacts of myopic populist policies, and
 - **the cost of policy delays, disregarding evidence-based policy analysis, well-established economic fundamentals and expert opinions.**
- **The general public and businesses at large had to bear the cost of a one-time adjustment of delayed structural reforms.**

Press Release on Annual Report 2022 - CBSL

Lessons Learned.... (2)

The Supreme Court Judgment on SC FR No. 195/2022

- *“....Our attention was drawn to the issue as to whether the conduct of the respondents during the relevant period directly contributed to the economic crisis....”* (p 115).
- *“....On assumption of public office, it was their duty to ensure that the existing issues were addressed and resolved in the best interest of the country and take every possible measure to avoid an aggravation to the detriment of the people....”* (p 116).
- *“.... Prolonged inaction due to the arbitrary, irrational and/or manifestly unreasonable decisions and inadequate measures over the period under consideration had heavily contributed to disastrous consequences....”* (p 117).

“.... Public trust is an inherent responsibility bestowed on all officers who exercise powers which emanate from the sovereignty of the People....” (p 118).

The IMF – Extended Fund Facility (EFF)

The programme sets on 7 pillars

Revenue based fiscal consolidation	A stronger social safety net	Restoring debt sustainability	Restoring price stability/ rebuild external buffers	Safeguarding financial stability	Reducing corruption vulnerabilities	Growth enhancing reforms
<ul style="list-style-type: none"> - Progressive Tax policy and revenue administration reforms - Expenditure rationalization - Improve timeliness, accuracy, and coverage of fiscal data - Strengthening Governance and Financial Viability of SOEs - Strengthen core PFM with PFM act 	<ul style="list-style-type: none"> - Protect vulnerable through SSN Programme (Aswesuma/ Samurdhi) -Strengthening SSN institutional framework 	<p style="text-align: center;">- A debt resolution in consistent with IMF program parameters in a fair and equitable manner to the creditors</p> <ul style="list-style-type: none"> - Establishment of Public Debt Management Office - Publication of debt information quarterly 	<ul style="list-style-type: none"> - multi-pronged disinflation strategy - Greater Exchange Rate Flexibility - strengthen the institutional framework to monetary and external sector reforms -Administrative measures to support BOP 	<ul style="list-style-type: none"> - Healthy and adequately capitalized banking system - strengthening financial sector supervision - strengthening the resilience and governance of state-owned banks. 	<ul style="list-style-type: none"> - Conducting a Governance diagnosis and publication of the outcomes. - Enacting the Anti-Corruption Act - Improving fiscal transparency 	<ul style="list-style-type: none"> - Rationalizing para-tariffs - Implementation of a Single Window for trade - Comprehensive labor market reforms

Progress of key stabilization measures since April 2022

Restoring the supply of essential items and eliminating power cuts

Significant Tightening of Monetary Policy

Import restrictions/margin deposit requirements

Strengthening Social Safety Net (SSN)

Continuous Financial sector oversight

Energy & and electricity price revisions and SOE Reforms, including CPC & CEB

Substantial Fiscal Tightening

Credible and Transparent Policy Measures prevented further worsening of the crisis and Restored Socioeconomic Stability

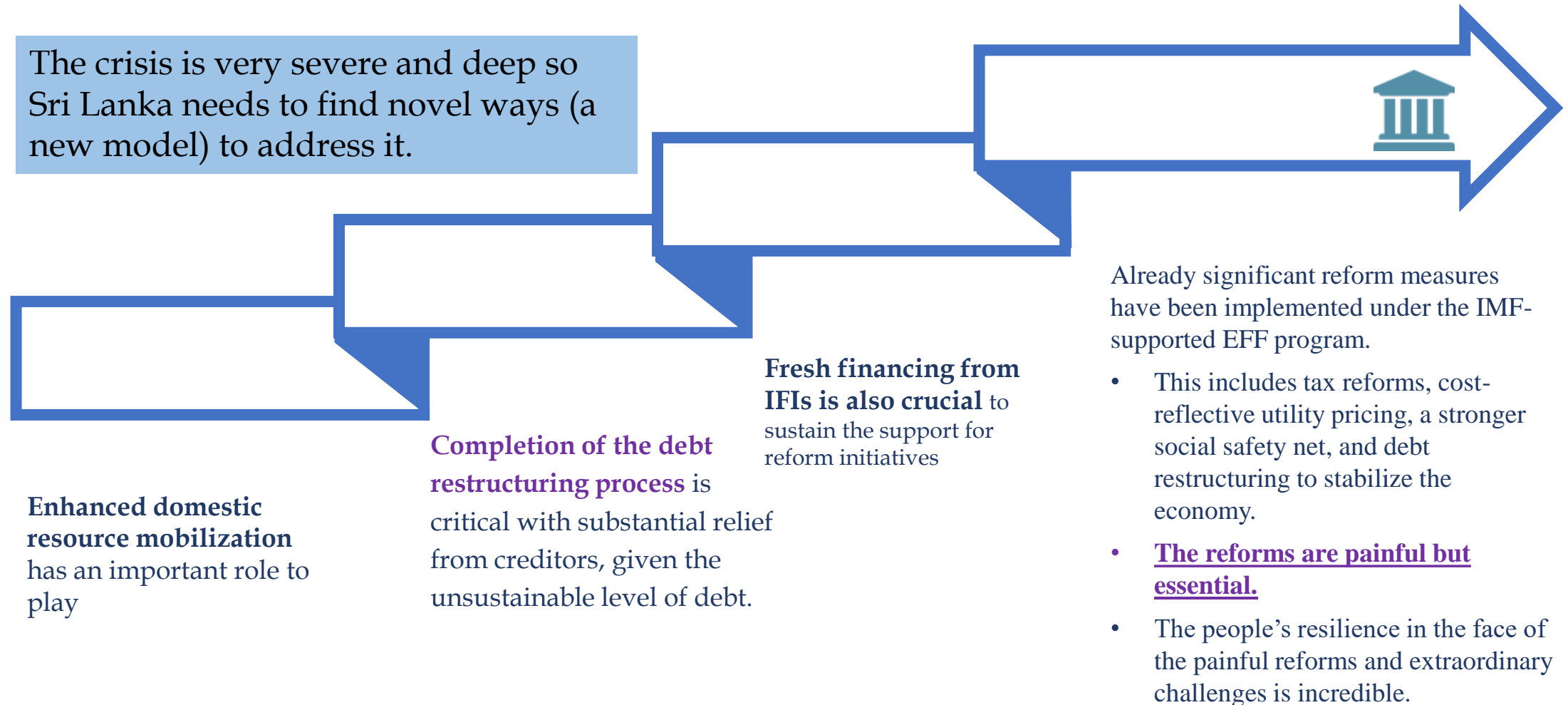
Forex and Rupee liquidity management

Stabilizing the exchange rate through market guidance

Announcement of the debt standstill and commencing debt restructuring

Negotiating an IMF-EFF Arrangement

Progress of key stabilization measures since April 2022



Tighter fiscal policy to improve revenue management



- *VAT rates* were increased to gradually to 15% from 8%
- A new *Social Security Contribution Levy* was introduced
- *VAT threshold and exemptions* were reduced
- *Corporate and personal income taxes* were changed
- Improvement in *tax administration*, including the *RAMIS*
- Establishment of a “*Parliamentary Committee on Ways and Means*”
- Implementing *National Tariffs Policy* to harmonize tariffs and para-tariffs
- *Strengthening fiscal discipline, institutions and fiscal governance*



- Expenditure control and rationalization measures, including strict Circular instructions
- Reducing the retirement age of government and semi-government employees
- No pay leave for 5 years for selected purposes
- Allowing selected personnel of the armed forces to retire early
- Proposed National Security 2030 programme
- A Presidential Commission to review all aspects of public service in line with current requirements and make recommendations including necessary reforms



- Establishing Parliamentary Budget Office
- Establishment of a National Debt Management Agency (NDMA) and improvement of debt management to ensure sustainability and reduce interest payments
- Introducing the Public Financial Management Act with binding fiscal rules
- Establishment of a National Operations Centre (NOC)
- Increasing digitalization in expenditure management (ITMIS)
- Establishing a new project appraisal scheme
- Strengthening Governance and Fighting Corruption

State Owned Enterprise Reforms

- Cost-reflective Pricing
- Introduction of Competition in Key Sectors
- Divestment of Non-strategic Assets
- Balance Sheet Restructuring
- Governance and Legislation

“...Many of these enterprises have garnered monopolistic positions in the market, hindering private investment. Price fixing, inefficient management, and poor entrepreneurship have weakened public finances, turning these institutions into national burdens that are dependent on the taxpayer”...

National Transformation Strategy

Monetary and financial sector policies

- **New Central Bank of Sri Lanka Act**
- The inflation reached single-digit levels supported mainly by monetary policy tightening and easing commodity prices.
- However, the base effect of inflation will be normalized in the medium term.
- The inflation is expected to stabilize around a mid-single-digit level in the medium term.
- The CBSL has eased the monetary policy stance since June 2023 moderating inflation, benign inflation expectations, and easing BOP pressures

- Additional Liquidity Injections to the Domestic Money Market through SRR Reduction
- The downward adjustment in market lending interest rates is expected to increase credit growth
- Monetary financing is expected to be low in the period ahead, supported by fiscal consolidation measures and the implementation of cost-reflective pricing by major SOBEs.

Debt restructuring.... Foreign Debt Restructuring is progressing

- **Following this budget, the next critical milestone would be the next steps in the process of external debt restructuring.**
 - Sri Lanka has asked its external creditors to accept significant losses on their holdings of Sri Lankan debt.
 - Creditors will be keeping a close eye on this budget to assess whether Sri Lanka is keeping to its commitments in establishing fiscal consolidation as the country's contribution towards achieving debt sustainability.
- **Sri Lanka has already provided all groups of creditors with indicative restructuring scenarios** that will enable the achievement of the debt reduction targets set by the IMF.
 - **That is, the reduction of Debt to GDP from 128% of GDP in 2022 to less than 95% of GDP in 2032**
 - **Reduction of Gross Financing Needs (GFN) from 34.6% of GDP in 2022 to less than 13% of GDP on average during 2027-2032, and**
 - **Restricting external debt service to GDP from 9.4% in 2022 to less than 4.5% in 2027-2032.**

Debt restructuring.... Foreign Debt Restructuring is progressing

- **It is now up to external creditors to come to an agreement with Sri Lankan authorities on a debt treatment that helps achieve these targets.**
 - China Exim Bank has already come to an understanding with Sri Lanka regarding such a debt treatment.
 - The next step would be for the Official Creditor Committee (co-chaired by Japan, India, and France) to provide a similar understanding.
 - We are very closely working with all international partners and respective parties, and we are very hopeful that this will be materialised soon.
- **At that point, the IMF will be able to assess whether the debt treatments are sufficient to meet the targets and whether they meet the requirements of comparability of treatment.**
 - This would enable the IMF Executive Board to approve the first review and unlock the next tranche of financing.
 - The budget would need to be in line with agreed macroeconomic reform parameters to ensure both the IMF and external creditors are happy to proceed.
- **The continuity of the IMF programme and debt restructuring process is crucial to ensure global confidence in the Sri Lankan economy,** enabling the country to continue to engage in trade finance and regular financial market transactions.

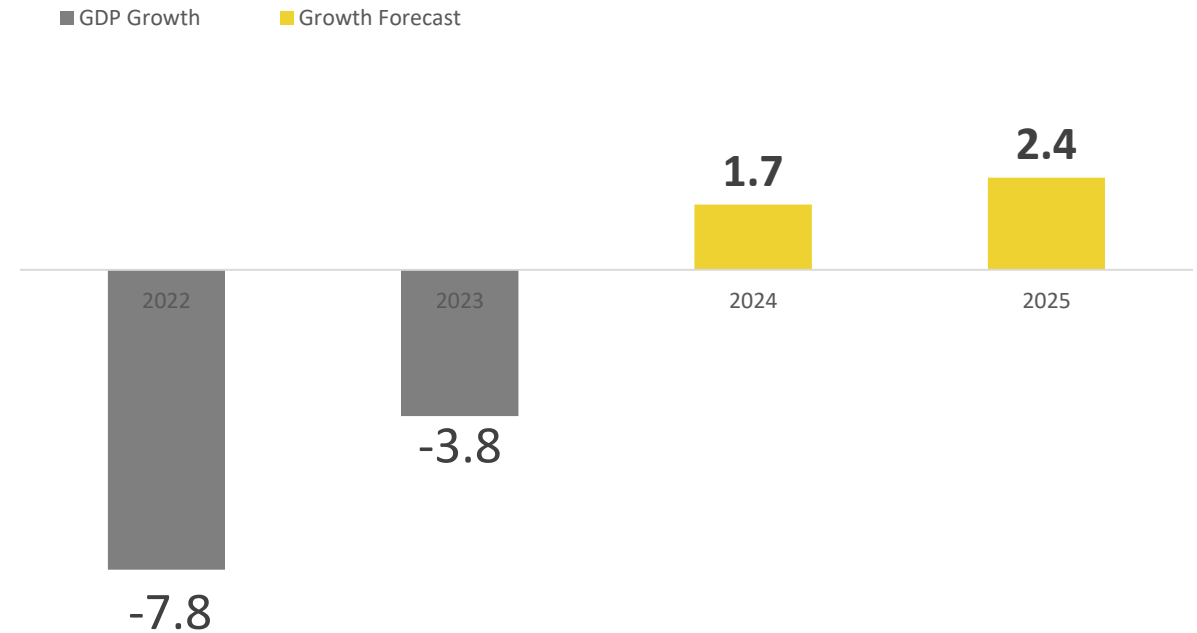
Progress of the IMF – Progress towards completing First Review

- The **Government successfully achieved most of the targets as scheduled**. Several targets were achieved with a slight delay.
- **Some targets include complex structural reforms** with lengthy legislative processes.
- The first review of the program was concluded in October 2023 and both parties reached a Staff Level Agreement (SLA) on 19 October 2023.
- **The SLA together with such assurances will provide access to the 2nd tranche of the program amounting to around USD 330 Mn.**
- **This would also unlock additional funding from other development partners** such as the World Bank and the Asian Development Bank
- **As important as the financing is the signal provided to the world that Sri Lanka's macroeconomic reforms remain on track.** This creates the confidence required to enable financial market transactions and FDI into the Sri Lankan economy.

Economy is gradually recovering....

- The economy is expected to move to positive territory from the last quarter of 2023.
- The efforts are required to solidify this growth.
- The volatile global economic environment remains a source of risk.

Sri Lanka
GDP Growth Forecsat



US-based RM Parks to start fuel supply in Sri Lanka soon; United faces delay



No more QR code

Watch on YouTube

No more QR code - Daily Mirror News

Asia&Pacific Saturday, October 28, 2023

Sri Lanka removes import restrictions on all items except vehicles

Source: Xinhua | 2023-10-10 00:05:00 | Editor: huaxia

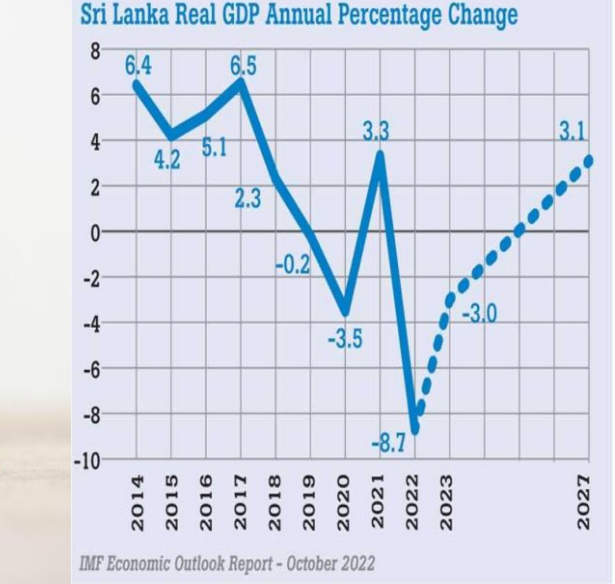
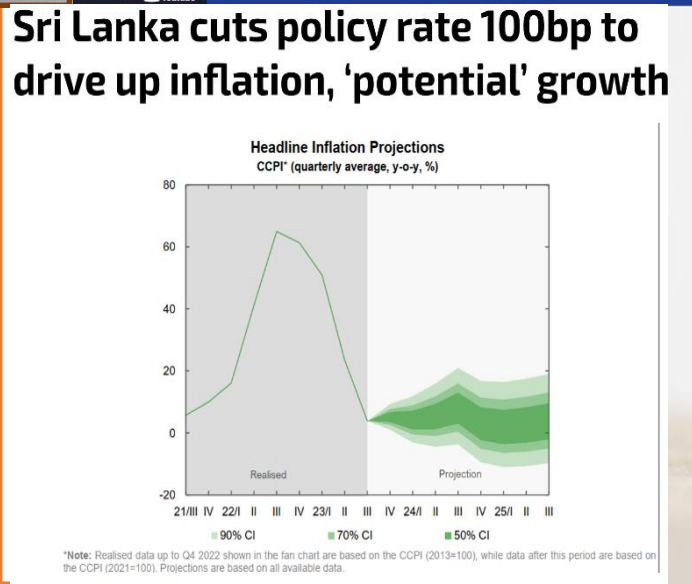
Asia&Pacific Saturday, October 28, 2023

Sri Lanka removes import restrictions on all items except vehicles

Source: Xinhua | 2023-10-10 00:05:00 | Editor: huaxia

Sri Lankan overseas workers remit US\$4.35 billion in 9 months 2023

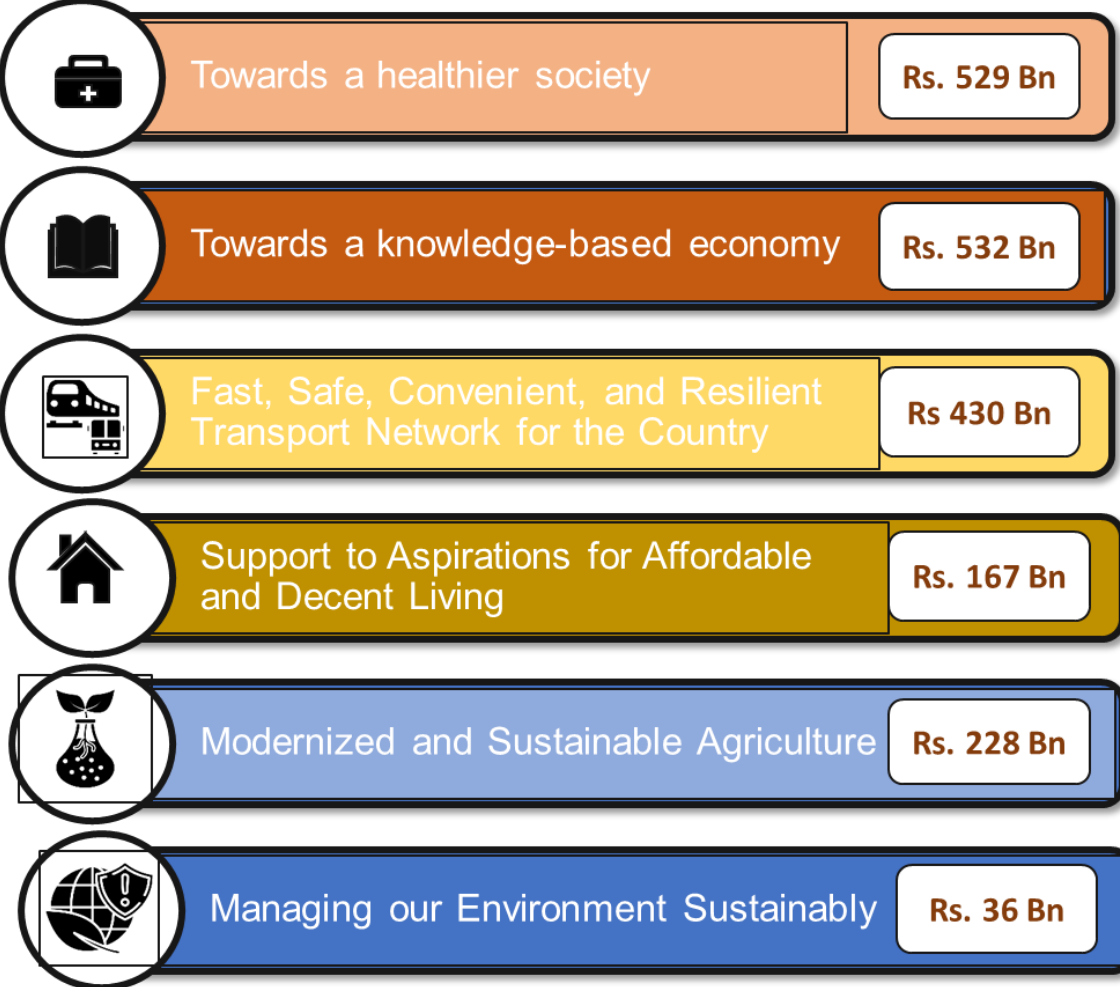
Oct 8, 2023 | 88 | 0



Sri Lanka: Strengthening Social Protection



Budget 2024 at a Glance



Budget 2024: Competing objectives and macroeconomic path....

- The budget required a **careful navigation of several competing objectives**.
 - First, it is necessary to ensure **continued adherence to the fiscal consolidation path to ensure macroeconomic stability**.
 - Secondly, it is equally important to **recognize the pain felt by citizens** and to provide some degree of relief, particularly to the most vulnerable groups.
 - Finally, it was also crucial to **take the first steps in shifting from stabilisation to economic growth**, and putting the economy on a fresh path of better quality growth.

- As is the case with most policy making efforts within significant economic constraints, **there are always policy trade-offs, there are always winners and losers, there are no perfect solutions**.
- **It is important to consider policy making, this budget included, from a holistic perspective.**
- **We should not forget the fact that we are managing a very dangerous crisis**. Therefore, practices or interventions that would usually be implemented under a “business as usual” scenario are not always feasible. There are many constraints including fiscal, social, and financial. Numerous policy aspects are inter-linked, and one intervention is likely to have unforeseen implications for other sectors.
- Therefore, policy selection must occur in a careful and pragmatic manner, considering all aspects in a holistic manner.

Budget 2024 - Key areas of importance....

- Whilst the initiatives taken over the last 18 months have helped broadly establish initial economic stability, there is a long way to go for this stability to be fully entrenched and for the economy to resume a path of recovery and growth.
- **Important measures in Budget 2024....**
 - Increasing revenue with improved tax administration and digitisation
 - Careful management of the government expenditure. **All proposed spending is matched by revenue measures that are already in place or have been announced prior to the budget.**
 - Ensuring fiscal discipline with legislative changes, including **Public Financial Management Act**
 - **Providing assistance to the people within the existing limits**
 - **Supporting activates to solidify the macroeconomic stability**
 - **Specific measures and structural reforms that go beyond the IMF programme to ensure a higher, green, and inclusive growth.**
 - A highly competitive economy in Sri Lanka with specific attention to digitalization, opening up of the economy, strong institutions, while protecting the poor and vulnerable.

**The journey is very tough,
but ESSENTIAL for the country....**

Moving towards economic growth....

- The budget needed to **provide the stepping stones for a shift from economic stabilisation to growth.**
- The economic growth is expected to recover in 2024 due to the improved macroeconomic environment.
- The **budget sets out the framework to support growth, led by non-debt creating inflows.**
- **Addressing the constraints to investment promotion are also articulated,** particularly in terms of access to land, raw materials, skills development, and so on.
- **Growth must also be inclusive.** That is why a lot of emphasis is placed on the integration of the rural economy and SMEs into broader value chains.
- **The budget also articulates the digital journey** that the country is expected to embark on, along with ensuring growth is driven by principles of sustainability and the green economy.

Financing of the Budget

- The revenue mobilization to finance the budget is derived largely from revenue measures that are already in place or that have been recently announced.
- Much has been said about the realism of revenue targets.
- The targets are ambitious, as they must be in order to reach the primary balance targets set in Sri Lanka's DSA.
- However, with the above measures, we expect the targets to also be realistic, with a lot of effort required from tax administration measures.

Tax Administration

- **Sri Lanka's tax administration structure is saddled with deep, long standing legacy issues. These constraints cannot be resolved overnight but we have to start somewhere.**
- Several ongoing tax admin measures are reflected in the budget such as risk based audits and expanding TIN coverage, among others. Several other measure are being implemented in parallel;

Digitalisation: Online filing of returns for corporate payers is now mandatory and the same is being applied for individual income tax payers. This will reduce interactions between tax payers and tax authorities and improve data analytics.

Information Sharing: Information sharing between the IRD and institutions such as the RMV, land registry, financial institutions, among others, helps identify conspicuous consumption. Measures are being taken to make such information sharing systematic and time bound. The legal framework to enable this has already been established.

Tax arrears: Enhanced efforts will be taken to collect the 20% of tax arrears that are not subject to legal dispute. Collection of such taxes will be monitored by strict targets and KPIs ensuring the ratio of uncollected taxes to revenue continues to decline.

On time filing: Documentation and filing processes will continue to be simplified to facilitate on time filing. On time filing ratios will be monitored to ensure they reach global best practice standards.

Legislative Measures

- **It is essential that legislation is put in place that helps lock in the reforms that are being implemented.** A rollback of these reforms would risk the country falling back into the dark days of 2022.
- The Ministry of Finance is in advanced stages of drafting the **Public Finance Management Bill**. The PFM legislation provides the legal framework to support the ongoing fiscal reforms.
- **This includes robust fiscal rules, enhanced disciplines on budgetary processes, developing the medium-term fiscal framework, improved transparency, and clear oversight on budget execution. The legislation is expected to be in place by early 2024.**
- In addition to the PFM law, there will be other legislation including the debt management law, procurement law, SOE law, PPP law, among others.
- **However, we are aware that legislation alone is not sufficient to drive meaningful change. Sri Lanka's experience with the FMRA legislation of 2003 is testament to that.**
- **Therefore, along with the legislation it is essential that all stakeholders, that is the Parliament, government officials, civil society, academia, the media, and the general public, all become stakeholders in this process to support the implementation of the PFM bill and other legislation to ensure that fiscal discipline in the country remains on track into the long term.**


Diverse views on the Budget 2024....

2024 Budget faces opposition scepticism over enforceability 

Budget 2024 likened to a 'fairy tale' amid unrealistic revenue targets 

Asian Markets
Sri Lanka's 2024 budget sets ambitious revenue, deficit targets 


Will Budget 2024 achieve a lower deficit despite higher expenditure? 

POLITICS
Budget 2024 is full of fairy tales
November 15, 2023 1:05 am • 0 comment 


Budget 2024: Paving the Way for the Nation's Future



News > World News > Sri Lanka's Economy Not Out Crisis Yet, Says President In Budget Speech
Sri Lanka's Economy Not Out Crisis Yet, Says President In Budget Speech 

Budget 2024: Revolutionary or a fairytale; depends on which side of the House one is in 

ECONOMY
Sri Lanka ruling party faction sceptical of president's 2024 budget


• Alleges blatant violation of the Fiscal Management Responsibility Act in Budget 2024, with Budget deficit exceeding 5% 


Sri Lanka Puts IMF Targets at Risk With 'Ambitious' Tax Goals

- Analysts say president's budget targets will be hard to meet
- Sri Lanka is already struggling to meet this year's tax goal



FITCH WIRE
Sri Lanka's Ambitious Budget Agenda Faces High Implementation Risks


Wed 15 Nov, 2023 - 4:49 AM ET

SRI LANKA CRISIS 
Sri Lanka's election-year budget straddles line between IMF and voters

Budget 2024 – Diverse views from Government and Opposition MPs' 

An illustration of the key developments of the severe economic crisis and way forward....

Intensified economic issues due to Easter Sunday Attack, Outbreak of COVID-19 Pandemic and external shocks....

Sovereign Rating downgrades and loss of access to international capital markets → → → → →

NEXT STEPS

Fiscal support in spite of unavailability of fiscal space

Use of Official Reserves to pay-off debt

Very low level of usable reserves

Change in the Presidency of the country

Reaching Staff Level Agreement & Completion of Prior Actions under EFF

Completion of the debt restructuring process, strengthening macroeconomic stability and implementing growth promoting structural policy reforms to remove obstacles to growth, open up the economy and facilitate domestic and foreign private investment to strengthen the growth process to improve living standards of the people.

Extraordinary monetary policy support

Shortage of forex even for essential imports

Soaring Cost of Living

Other changes in the Administration

Obtaining Financial Assurances from Bilateral Creditors

High Monetary financing of budget deficit

Liquidity issues in banks

Shortages of Fuel / LP Gas

Prolong Power Outages

Urgent need for redefining policy priorities to address the turmoil

Initiating debt restructuring process

Incentivity for changing dynamics

Use of Official Reserves to facilitate essential imports

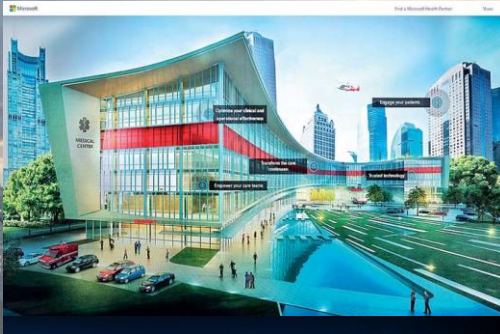
Shortages of other items

Mass Protests "Aragalaya"

Securing IMF EFF Program for Sri Lanka

Continue to implement IMF-EFF Program

Officially sought the IMF assistance



Concluding remarks

- **The country has collectively undertaken great sacrifices** over the last year to enable the economy to stabilize and set the stage for recovery.
- Despite the gradual improvements observed in the economy, **there is no room for complacency.**
- The **next reform steps are crucial** to economic stability and recovery.
- **Budget 2024 ensures Sri Lanka's IMF programme fiscal targets (revenue/primary balance) remain on track**
- **Budget 2024 also contains a number of reforms** to ensure Sri Lanka emerges as a fast growing, equitable, green and sustainable economy.

The implementation of the budget proposals, with the support of stakeholders, is the key.

Private sector has a critical role to play in this endeavor.

Concluding remarks.... (2)

Reducing corruption vulnerabilities and improving governance are important....

- Following key areas are highlighted in this regard;
 - It is important that the **corruption be eliminated** and all stakeholders must work together to **reset Sri Lanka's governance culture**.
 - **Economic management must be underpinned by evidence based policy making** and the willingness to respond to changing economic circumstances, without being rigidly fixed to personal dogmas and political ideologies.
 - Last week, we saw positive developments in terms of enhanced accountability in terms of economic governance.
 - This is expected to ensure that **present and future policy makers do not make the same mistakes.**

Concluding remarks.... (3)

- Budget 2024 strikes a difficult balance between;
 - a. consolidating stabilization
 - b. providing relief within feasible limits, and
 - c. setting the stage for sustainable and inclusive economic growth.
- **Everyone must work together** to implement the next stage of reforms effectively
- **There is no margin for error to deviate from the envisaged reform path** by reverting to unsustainable policies and practices of the past.
- There is a strong need for a new Social Contract deviating from the past.
- The discussions, reviews and deliberations should be directed in that direction.

Shortsighted, populist and politically motivated moves to derail the progress so far achieved will certainly lead to serious detrimental consequences, which would even be worse than the difficulties experienced in 2022.

Concluding remarks.... (4) Important thing to remember....

Taking firm actions without any further delay is crucial to lessen the impact of adverse developments on the economy and the people, and any failure to do so will be very costly...

- Given the serious issues in the Sri Lankan economy, firm and coordinated efforts, led by an appropriate fiscal response, is essential.
- When it comes to preparing for a coordinated effort, it is important to remember Shakespeare's advice:

“Better three hours too soon, than a minute too late”^{1/}

**THE CLOCK
IS
TICKING... ***

^{1/}William Shakespeare, *The Merry Wives of Windsor*. Act II. Scene II.

**used for saying that someone must do something quickly because there will soon be no more time*

40

Above is a slide of a presentation that I made to the Monetary Board of the Central Bank in **July 2021**.

Again, I see the importance of addressing the prevailing issues in the economy urgently with a holistic view and strong coordination & commitment by all stakeholders without being late.

Thank you.