

# Sri Lanka Beyond 2011



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Sri Lanka has experienced one and half years of peace and security. During this time sections of the economy that were dormant have gradually begun to gather

momentum. Recognising the key elements that require urgent attention that would create the foundation for a solid future, the 2011 Budget presented by His Excellency Mahinda Rajapaksa, President of Sri Lanka provides a plethora of incentives that focus on energising the private sector as well as promoting import replacement industries where a knowledge based economy will be established in the future. Dr P B Jayasundera, Secretary to the Ministry of Finance and Planning, elaborated on the economic gains that the country would realise in the next decade where Sri Lanka will reach USD 4,000 per capita income, with low inflation, a growth rate of ten percent, a vibrant private sector and a self sufficient country, where agriculture will retain its prime place.

By Udeshi Amarasinghe | Photography by Menaka Aravinda and Mahesh Bandara

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**The Budget for 2011 has been made to keep the economy stable while allowing monetary policy to maintain low inflation and speed the development of the country. What are your thoughts on that?**

One of the greatest achievements in the last one and a half years other than restoring peace in this country was being able to control inflation successfully. As you may recall inflation was over 25 percent in 2009, however the conscious financial policies of the Government and the effort made by the Government to address a variety of structural factors obstructing the supply of goods and services, enabled the country to see a low inflation of around six percent. This is the biggest achievement which is essential for a strong economic growth. With the reduction in inflation, Sri Lanka has also been able to witness a decrease in the interest rates, which were in the 20 - 30 percent range. As far as the private sector borrowings are concerned, the applicable interest rates have come down below 16 percent during this period. Many sectors are now receiving credit at a rate of 10-12 percent and priority sectors are receiving credit at eight percent. Therefore, this achievement should be consolidated. The factors contributing to inflation should be addressed as a priority and the Government quite rightly focused on these aspects and has managed inflation well.

Sri Lanka's economy has expanded at an eight percent in 2010. From the beginning of the Presidential term in December 2005 Sri Lanka has experienced on an average growth of six percent. In certain years it rose to almost seven to

eight percent reflecting capacity in our economy. Due to the adverse impact of the global crisis particularly on our export and import sectors and also increase in oil prices, the Sri Lankan economy slowed down in 2009 to three and a half percent. This was also an average growth rate for the year but during the first half of 2009 the growth rate was below three percent. Therefore the economy suffered immensely in 2009 compared to the momentum that the President created in 2005. But, the economy bounced back in no time in the second half of 2009 and the momentum was sustained throughout 2010 and the economy is on an eight percent growth trend.

**This Is A Remarkable Achievement Because It Is The First Time Ever In The Last 40-50 Years In The Sri Lankan Economy That The Growth Rate Has Exceeded The Inflation Rate.**

The economy is growing over eight percent in real terms, while inflation is growing around six percent; this is a remarkable achievement because it is the first time ever in the last 40-50 years in the history of Sri Lankan economy that the growth rate has exceeded the inflation rate. Now, we need to maintain this achievement. The 2011 Budget has basically built on this achievement, to create the enabling environment to sustain this momentum. The 2011 Budget has been designed to accelerate the growth towards eight percent over the medium term and then accelerate further to ten percent while keeping inflation at around five to six percent, which will allow Sri Lanka to enjoy a period of economic expansion that will enable a qualitative improvement in the real economy.

**Sri Lanka is to reach USD 4,000 per capita income by 2016, what is the development approach envisaged to achieve this aim?**

From 2005 to 2009, the Sri Lankan economy doubled its per capita income from around USD 1,030 to over USD 2,000. In fact in 2010 Sri Lanka per capita income is expected to be around USD 2,400. This was achieved under very difficult conditions; the country was fighting against terrorism, the global situation was very bleak and the oil crisis affected all aspects of our economic life. On the other hand Sri Lanka did not have required infrastructure to speed up its development.

As a result during the period of 2005 to 2010, the Government attempted to address infrastructure bottlenecks that this country was confronted with. In my view the negligence of infrastructure development was as costly as the cost of

war, on the economy. Therefore, the President focused seriously on all aspects of infrastructure development by directing public investment towards development of ports, road network, irrigation facility, water supply schemes and power generation and distribution, at a national level as well as at a rural level because the Government believes that economic development will become meaningful to the citizens only if economic opportunities are created at a grassroots level. Connectivity through education, technology and transport, access to market places and critical infrastructure, which were all addressed during that period as connecting people and economic opportunities, are the central themes of Mahinda Chintana.

Prior to 2005, public investment was at a very low level. No country has generated private investment unless the Government provides the basic core investment. That is a fact. Everyone keeps talking about private investment and foreign direct investment, but the critical investment must come from the Government to facilitate private investments. What are the critical investments? One is the investment in law and order. Security is a must; every successful vibrant economy has invested heavily on security because security creates the enabling environment for investors to conduct their business. Second, is the heavy investment on roads, ports and other physical infrastructure from which the private sector generates business activities. Thus, these were the priorities of the Government.

### **No Country Has Generated Private Investment Unless The Government Provides The Basic Core Investment. That Is A Fact.**

The third aspect was to address the challenges in the real economy. The real economy must ultimately produce. Previously, agriculture, livestock and fishery sectors had been neglected. The situation was such that agriculture did not receive priority and farmers were not receiving remunerative prices, the input cost was very high, the motivation was very low to engage in agriculture and access to credit was extremely difficult, which is still a challenge that the country has to manage. Then access to market places remained restricted owing to various rigidities. The institutional arrangement that any country must have, to intervene to overcome problems associated with seasonal fluctuations of supply of goods and storage facilities were not satisfactory. Therefore the Government recognised the agriculture sector as a critical priority sector. As a result of all these, the Country managed to move from USD 1,000 to 2,000 during a five year

period. The lesson to be learnt is that if you really aspire to double the per capita income every 6 - 8 years, you need to get your act together. If one looks at the previous records, Sri Lanka has taken many years to double the per capita income and thus the people did not feel it. In fact, the feel good factor does not come unless growth is strong enough to double the income during a visible period of time. This happened during 2005 - 2010 because the Government was able to get all necessary building blocks together.

Based on that experience the Government is in a much stronger position to consider doubling the per capita income in the next six years. The war against terror is behind us, much expectation has been created and the investment climate is right. In fact, the expenditure on war that has now been saved is truly a real investment in this country. Then, we have an additional capacity; the biggest achievement from the war is not just ending the conflict, but also to regain the space of productive capacity in this country, which was not available for 25 years. The Northern and Eastern Provinces that have abundant resources for agriculture, livestock, fisheries and tourism are now economically active areas. All these valuable resources had been denied to the country due to LTTE Terrorism. Actually, without much investment, we should be able to reap benefits for three to four years from this new space that the Government has liberated. Although from 2013 onwards, we may need high investment of around 32 percent to generate higher growth. Even with little investment Sri Lanka can generate more growth because the existing capacity will get on to full production from now onwards. One will see the benefits of five districts in the North and three districts in the East coming into agricultural production in the current Maha season and it will be an added contribution to GDP of this country because this capacity could not be used due to terrorism. Similarly, livestock, fisheries and tourism are all expanding at a rapid rate in these areas, while allocating the full utilization of existing capacity in the rest of the country, particularly in tourism.

Sri Lanka can now comfortably speak of a solid infrastructure. No one is grumbling about the constraints in ports because everyone sees that there is a massive capacity expansion in ports to accommodate the demand of an expanded economy. Similarly, people appreciate that the road network has improved significantly. Everyday new routes are being constructed and added on to the network. Even those who are critical of the Government through a variety of political rhetoric have acknowledged that work is being done in the country.

Areas, which could not be utilised for production, particularly in agriculture, due to absence of irrigation facilities are now being gradually reached through massive irrigation programmes. Over 15 irrigation projects in this country are currently under construction. Existing major dams supporting over 30 major reservoirs are being rehabilitated to increase their capacity. The additional water capacity that is being created is sufficient to cultivate over 100,000 hectares of land due to this large water capacity that is being created. Moragahakanda water diversion is now a reality. The development schemes for Deduru Oya and various other irrigation projects are under satisfactory programmes.

We do not hear of prolonged power cuts in this country anymore. Industrialists do not complain about the cost of power because the availability of power is uniquely different in this country compared to all other countries in the region. While many people speak about promising economic opportunities in several other countries, they know these countries still experience power crisis and power in these places are not cheap either. Due to environmental considerations and various other factors, electricity is costly. Therefore in Sri Lanka, it is a major achievement for us in the sense that for the next 15-20 years, Sri Lanka will not see a constraint in the power sector even if we grow at eight to ten percent. Investors will have ample opportunities in all sectors. If electricity and ports are available and the connectivity is there and the telecommunication sector is expanding that means there will be ample opportunities in the real economy.

Traditionally, and still with historical legacy people speak of imports and exports confining to limited activities; you import and distribute food and consumer durables, or you produce tea or garments and consider the whole economy from such a limited perspective. However, when infrastructure is available from all fronts, the economic potentials and scope are quite different. Now Sri Lanka is set for a diversified high value added economy. All factors are conducive for Sri Lanka to exceed per capita income of USD 4,000 that the President has set as a key target for 2016. The 2011 budget has taken a medium to long term view to move the country in that direction.

There is an important factor that will support this growth in investment. In the 2011 Budget the Government has committed to a public investment of six to seven percent of GDP over the next 6 years. Total investment is expected to be five times of that figure. Currently private investment is around 25 to 27 percent and gradually it will move up. I am confident from the investment profile that we

are now managing that the country will see large investments coming from external sources as well as from our domestic enterprises that will take the Country's investment to around 28 - 30 percent in 2011. That will move per capita income rapidly towards the USD 4,000 target. Knowing that 2010 has already generated a per capita income near USD 2,400 with a low inflation and a higher growth than 2009, further expansion with similar trends in both inflation and growth in 2011 and posting the economy with per capita income around USD 2,800 is not a difficult mission to achieve. Therefore, the momentum now is in place to rapidly consolidate as an upper middle income economy.

**Do you think that the gap between high income earners and low income earners will widen during this process?**

**The Entire Thrust Of The Mahinda Chintana Is Focused On The Empowerment Of The Household And Village. The Village Is The Fundamental Neucleus In The Mahinda Chintana Development Strategy. Therefore, Unless The Household And Community Is Empowered, No Development Is Recognised As A Success In The Mahinda Chintana..**

No, this is another important aspect that the Government can proudly claim a success. We noticed even prior to 2005 that the Sri Lankan economy was growing around four to five percent. However, poverty remained stubbornly constant. Of course to make a decisive move on poverty reduction, economic growth needs to be strong. But in the last five years, we see a remarkable shift in all the statistical indicators. That is where many people still fail to understand the recent improved performance.

During the last five years, Sri Lanka has seen two household surveys; one is the 2006 household survey and the other is the 2009-2010 household survey. What do these household surveys indicate? Poverty has dropped from 15.2 to 7.6 percent between the two periods. Poverty has dropped by half. This poverty reduction is not confined only to urban areas. In fact, poverty reduction is remarkably stronger in the plantation and rural areas. The entire country has now witnessed much lower poverty incidence than any South Asian country. Why? There is a unique economic explanation; one is that economic growth is over six percent. The other is that the economic benefits have shifted in favour of low income earnings. Regardless of where people are engaged in small holder tea, rubber, paddy, corn or soya bean production or those who are engaged in vegetable and

fruit cultivation they all have seen high income during this period. If one looks at the daily wage rates in paddy, rubber or tea, their daily wage rates have increased considerably. The daily wage rates in the informal markets have also gone up. Thus their disposable income and capacity to spend have increased. Not only has household income improved but also the opportunity to earn a higher income for everyone in this country has expanded.

Most Sri Lankan households scattered around many districts, including the newly liberated North and East have access to electricity. This also means that 80 percent of the people in our country are connected to the world. They have access to telecommunication and roads. Over 40,000km of rural roads have been upgraded to solid conditions. These are no longer gravel roads. They are sustainable, improved concrete structures that have been constructed with the participation of the community. Thus, the community is empowered with the access that they have created. As a result children spend less time to travel to schools, the people take less time to travel to hospitals and transport their produce to markets. Therefore the transaction costs have dropped significantly to our people.

People can travel to many distant areas in half the time that they spent three to four years ago. These are real experiences. Colombo may still be congested, but even in Colombo many roads are continuously improving. Look at Parliament Road, look at the improvement in Colombo City and surrounding areas, look at the road network in the Gampaha, Kalutara and neighbouring districts. Forty percent of the country's road network is in an improved condition with very high quality construction activities taking place. There are economic benefits from all these. New houses are being built and new property development is taking place. New shops are being opened in response to growing purchasing power of the people. Development is taking place at the rural level. That is how the economy has moved with high growth and tangible reduction in poverty. That is the Goal of Mahinda Chintana. The President does not believe that economic development is enough. The entire thrust of the Mahinda Chintana is focused on the empowerment of the household and village. The village is the fundamental nucleus in the Mahinda Chintana development strategy. Therefore, unless the household and community is empowered, no development is recognised as a success of the Mahinda Chintana.

The last five year experience has proved that this strategy works on the ground.



In fact there is a wide acceptance of these strategies. The World Bank Managing Director who visited recently had a similar line of thinking. Even some of the opposition leaders in this country have begun to articulate Mahinda Chintana ideas to make development meaningful. It is now clear from global experience in recent times that policy makers have to move away from the conventional wisdom where some talk only about investment to generate growth, which in turn generates employment and thus reduces poverty. That was the conventional wisdom and therefore everyone concentrated only on investment, whereas President deviated from that. Investment is necessary, but he considered it is not sufficient and must be an inclusive and holistic process to make development meaningful to people and conducive to poverty reduction.

The target is to increase private investment from both foreign and domestic resources as well as public investment to a total of 32-35 percent of GDP. Where will this investment be targeted and what can be expected? What mechanisms have been put in place to attract large investments?

Investment is targeted in all areas. Each sector may respond at a different speed. Currently, the peace dividend is reflected everywhere in this country. But, the lead performance is taking place in the tourism sector. The Country has in 2010 surpassed 600,000 tourist arrivals. The hotel sector is one sector where investment will happen, but that will not happen overnight. The simple reason is that our hotel and tourism sectors are under utilised. We are still going through a period of fully utilising our existing capacity. Hotels are now seeing occupancy at over 80 percent on average, and over and above, room rates keep reaching true values.

There is a perception that hotel rates are rising slowly but hotels may have contractual obligations on the rate for a given period. However, the Government is pushing hard for the increase of room rates. In this Budget particularly, we have said that the minimum rate should be USD 125. Of course the Government will be flexible to allow contractual obligation to the owner, but everyone must start renewing their contracts and entering new agreements at high rates because the country now must attract high spending tourists. There is no point in drawing tourists who are not capable of spending even as much as the local tourists. That is the message we are giving to the hotel industry. This will improve their balance sheets and as a result they can raise investment. Therefore tourism is one area where investment will happen involving all small, medium and large

scale businesses. In fact very soon, you will see the world-class tourist investments taking place. Shangri-La global network is already here. The investment for a six-acre land at USD 75 million has already been paid. They are planning to increase the investment in land to USD 125 million. There will be an investment of around USD 400 million on the construction of integrated tourism facility, which is designed to complete over 30 months. This is a flagship FDI that one can talk proudly of. In the first half of 2011 few more flagship investments have been lined up for takeoff.

**Establishing An Agricultural Base Will Also Be A Priority As Even The World Economy Has Recognised That Agriculture And Food Security Is A Priority Sector That Sri Lanka Will Benefit From The Changes In Global Development Patterns.**

Existing structures are being converted using advanced construction technology. For example the warehouses on the other side of the Beira Lake are now being converted into modern facilities to accommodate IT, BPO services, storage, bonding, trading, schools and higher learning institutions - all these things are yet another set of investments that private sector has entered into. Investments in IT and enabling services are targeting a billion dollar export activity that is being planned to achieve in this country over the next few years. Fortunately, these are also areas that no longer require heavy investments because technology has taken over heavy structures. Equally, high value added industrial activities such as the apparel products, blended and branded tea, rubber based products, gems and jewellery, spices and such. are climbing the value chain. This Budget has also recognised that any manufacturing activity over 65 percent value addition will be shifted towards a very low tax regime. Establishing an agricultural base will also be a priority as even the world economy has recognised that agriculture and food security is a priority sector that Sri Lanka will benefit from the changes in global development patterns.

There is thinking among some sections of the society that the country is shifting towards import substitution. This is not correct. The country has gained comparative advantage in many import replacement activities. When a country imports X amount of goods and services, it also reflects the potential the country has to manufacture it, if it can be done at a cost below other countries. Sri Lanka is one such country where agricultural exports and domestic value addition can be done and this Government has proved that this is possible for rice, maize, soya

bean and such. The Government is also promoting peanut, cashew, mango, strawberry and dragon fruit cultivation and other such activities where opportunities for investment have expanded. These investments may not be very big but for Sri Lankan agriculturalists, these are large investments. People who speak about traditional fruits are also speaking about new varieties of fruits and vegetables that are being exported in a big way in this country. These are not loudly spoken of.

In the fisheries sector, production was over 40,000 metric tonnes prior to the conflict in 1983. During the conflict, production decreased to around 15,000. Now it is getting back to 40,000 - 50,000 metric tonnes but this is just a recovery stage. Imagine the potential in the North and East, as well as for inland fisheries as well as deep sea fishing. This Budget made the fisheries sector a tax-free sector for a period of five years so that everyone could feel the freedom of operating in a tax free environment. Livestock again is another industry that is prevalent in many districts of this country. Until recently, even Colombo had the livestock industry. Investments are taking place in this sector and remarkable opportunities are available for medium size investment to take place while flagship blue chips can also invest in these areas.

**Sri Lanka Is One Such Country Where Agricultural Exports And Domestic Value Addition Can Be Done And This Government Has Proved That This Is Possible.**

Energy will be the largest import replacement industry in the country in time to come. Renewable energy has gathered considerable momentum due to climatic changes and many other concerns. Sri Lanka has been importing three billion dollars of oil. This year rain has saved us a large amount of funds, no one realises that the value of water may be worth more than three billion dollars because all the reservoirs are full, all the irrigation schemes are active and as a result huge savings have taken place in power generation and agriculture production. The conservation of water itself is a good import substitution from my point of view. Apart from hydro power there is a shift towards renewable energy, wind and solar power. I have seen quite a number of new upmarket hotels (that consist of environmentally friendly structures with renewable energy use). Room rates are in the range of USD 500-700 a night. They have gone into solar and windmill and the mix of the two as a major power generation activity. Some are even generating excess and contributing to the national grid.

2011 will be Sri Lanka's first year of coal power use. Therefore in the next ten years, I am quite optimistic that apart from shifting from fuel to coal-based power generation Sri Lanka also will expand hydro and renewable energy sources, which will create enormous opportunities in this country for new investments in the power sector. Of course investments in the construction industry, is a priority of the Government. During the next three years the country will see an expanded phase of construction of roads, water and irrigation schemes. Similarly private investment in the construction of hotels, property development, shopping complexes and new houses are projected to intensify. The Government plans to envisage the share of construction industry in the GDP to exceed ten percent and expand at an average rate of around ten percent.

Looking at the real economy, if one looks at the number of export and import items in Sri Lanka, it is a clear indication of where one can target investment. Take pharmaceuticals as an example. It is a USD 400 million-dollar market of which 90 percent is imported. Therefore in this Budget the pharmaceutical industry has been given incentives, not only to bring the drug prices down, but also for investors to think of moving into pharmaceutical manufacturing activities domestically.

President Mahinda Rajapaksa is very keen that Sri Lanka's future is designed on knowledge-based activities. The emphasis in economic development is very much linked to knowledge. Sri Lanka is no longer a labour abundant country. Our unemployment rates are around five percent and labour force has many options including overseas jobs. People are educated and healthy. Skill levels are improving very rapidly and as a result, from childhood to the retirement age, activities based on knowledge are likely to expand in this country. I will not be surprised to see investments in international legal firms, accounting and financial services, architectural, medical and engineering services taking place in the country over the coming decades. We have the knowledge, infrastructure and also the enabling environment to provide such services globally.

Then other areas where investment will be made is in technology, advertising, marketing related activities and value addition. Our tea industry is no longer talking only about growing, processing and exporting tea in bulk. They are also expanding value added tea production, packaging, branding and marketing. Producing and packaging are associated activities supporting expanded economy, particularly when it becomes value added service economy. Therefore, in my view

one should not go by lists. Investment will happen where a profitable activity can take place and that environment is now in place as an emerging economy.

### **Substantial changes have been made in the tax structure, what was the thinking behind this?**

Sri Lanka is fast becoming a middle-income country. While individual income status is improving the country is consolidating as an emerging economy. This means the people need systems that are very simple to manage. The Government has a responsibility and has to spend on education, healthcare, security, public facilities and conserve the environment. Public needs to be maintained through public expenditure. People are willing to pay for these facilities. The willingness to pay must be explored by creating a system that people can live with, people can comply with. The administrator must be able to efficiently implement tax system. That is the vision of the President, to go for a simple broad base the tax system which is equitable.

Sri Lanka has numerous taxes at the national level, provincial level and then also at the local authority level. Therefore there are many Sri Lankan household and private sector establishments, largely small timers and SMEs who cannot acquire services of tax experts and advisors. They have to spend time and money. The associated transaction costs from taxation are high. It also creates difficulties for tax administrators. Though everybody blames tax administrators they too manage a very complex system and are basically enforcing a legal framework. Therefore, the aim was to remove unnecessary taxes and simplify the tax structure. That was the thinking behind this. The Presidential Taxation Commission was appointed to address the issues pertaining to the tax structure. The President himself engaged in a wide range of consultations with various individuals and professionals. We as technocrats did our part by looking at various options to move in this direction while maintaining revenue neutrality which is equally important in a country where we have to bring down the fiscal imbalances. Of course when making tax reforms the Government needs to be absolutely bold because it involves a transition and takes time to give best outcomes of these actions. Those who are liable to PAYE tax no longer have to pay taxes if their income is below 50,000 rupees. Even if it is above 50,000 rupees per month, it is a much simpler rate. No one will pay over 24 percent compared to almost 37 percent now. Furthermore tax is deducted at the source and as such there would be no need to file returns if you do not have other sources of income.

**The President Took A Very Bold Decision By Simplifying The Tax System. Though There Maybe A Reduction In Tax Revenue We Believe That The Expansion In The Economy Broadening The Taxation Base As Well As With 'Revenue Positive Reforms' And Easy Tax Administration Will Maintain The Required Revenue In 2011.**

The taxation structure in the telecommunication sector was simplified recognizing its pivotal role in development. Previously there were about seven taxes, which have been consolidated with one simplified tax; a straightforward telecommunication levy. Similarly, the various indirect taxes the country has gone through at national level have now been brought down to VAT and NBT. The NBT has harmonised with the provincial turnover tax, so that the provincial and national Government will share the revenue. With regard to imported branded products which are not manufactured here are subject to Port Levy and NBT only. Combined tax rate is around seven percent. Mobile phones, wrist watches, perfumes, cameras, very sophisticated electronic equipment that are required for people for modern lifestyles and tourism and the promotion of international shopping facilities are being basically put under simple taxes. With regard to essential commodities, there is the special commodity levy which is the only tax that will be applicable at the point of customs.

The President took a very bold decision by simplifying the tax system. Though there may be a reduction in tax revenue we believe that the expansion in the economy, broadening the taxation base as well as with 'revenue positive reforms' and easy tax administration will maintain required revenue in 2011. People will have more money to spend and save, and funds are likely to move to the stock market, bank deposits and a whole range of activities.

**Import substitution will be given priority with the aim of expanding exports and replacing imports. A CESS will be imposed on the exportation of raw materials. Value addition is the key and substantial relief has been given to industries that are exporting finished goods and value added products. Will this stimulate the export industry or stifle them? How do you see smaller enterprises doing well in this context?**

This is the global pattern. Many developing countries including Sri Lanka were essentially primary commodity export economies about 20-30 years ago. Sri Lanka grew tea and exported it in raw form, Sri Lanka developed rubber and

other plantation crops, but not as industries. It was the same with cinnamon. Over time, with globalisation providing unique access to advance technology, the Country has begun value added industrialization using these raw materials. Some countries which have absolutely no plantations or availability of raw material have begun advanced technology based industries on our plantations and raw materials.

There is no justification for Sri Lankan tea to be sent to other destination for value addition and brand elsewhere, unless Sri Lankan tea preserve its identity and price. Sri Lankan tea growers must think of tea as an industry; industry involves cultivation, processing, manufacturing, research, value addition and marketing. with different types of products, brands, markets including high-end markets. To be very proud, quite a number of Sri Lankan entrepreneurs have realised this, and over the last several years, slowly, but steadily, moved in this direction. As a result we can proudly speak of good names like Dilmah, Mlesna, Heladiva, Akbar Brothers and many others who are taking Ceylon Tea to the world. These companies are growing at a rapid rate, and as a result their prices are very high and they have been able to make profits. The country can make tea industry a USD 3 - 4 billion activity only if plantations maintain its growth with continuous planting practices and value adding here with local brands without allowing imports. Similarly rubber producers are making huge value added rubber products in this country. Surgical gloves, tyres and such other products can be manufactured here as we produce natural rubber. This is another industry that can surpass the USD 1 billion export turnover soon.

Therefore, any value addition process needs incentives. The first action is to discourage the export in raw forms. Today, tea, rubber, coconut and several other plantation crops are exported in raw form. Therefore, the Government decided to impose CESS on export of raw materials while freeing value added forms of exports from CESS and export taxes. All value added forms of exports are tax free, but the raw form is taxed. Unprocessed tea, rubber, coconut, cinnamon and such are subjected to CESS. Then sand and other minerals are also exported from our country, which can be processed within Sri Lanka. Therefore, all raw form of exports are subjected to taxes. That required funds can be channeled to these sectors for expansion.

The second aspect is that the value added form should be rewarded. That is why the proposed new tax structure is designed to give the lowest tax rate of ten

percent to the value added form of exports. Any item such as apparel, tea, rubber, cinnamon, gems and such. that has a domestic value addition over 65 percent will enjoy lower taxes. Third, the value addition requires access to modern technology processes at lowest cost. Therefore, all machinery and equipment that need to be imported are permitted without any tax. In the 2011 Budget we worked very hard to identify each item that needed to be clarified on such basis. The proposed tax system itself provides the depreciation allowance to make the capital cost cheaper.

The Budget speech has made references to cover all the aspects. Large areas of land are to be brought under cultivation including areas in Monaragala, Mullativu and Vavuniya for rubber. The biggest problem for the development of the agriculture sector in this country was the non-availability of long-term funds. Agriculture means long-term. You cannot enter plantations unless you are willing to wait for five to seven years to see fruits. Therefore, long-term lending is required.

This Budget has, in addition to providing some funds to support plantation activities, has also made the banking system to create investment fund accounts to promote long term lending. Each bank is required to open an investment fund account this year from which they have to lend long term, at low rate of interests and they must develop project financing capabilities as well. Banks must promote long term lending to agriculture, plantation, construction, value addition and brand promotion, factory modernization, fisheries, livestock and many such risk taking activities.

While the farmers are taking the full risk, the bank should also try to share part of it in this decade of development as banks can easily share peace dividend that they enjoy. That is the direction the country needs to go and the Government expects every single bank whether they are foreign or domestic to move in this direction using their tax savings. The banking and financial institutions will benefit from the reduction in VAT from 20 to 12 percent and corporate tax from 37 to 28 percent. These savings will go into the investment fund accounts for a period of three years so banks can build a good long funding capacity. However, we do not expect anyone to rush as everybody must plan well. The private sector needs to develop new proposals, while the Ministry of Finance will develop guidelines and get the entire Government machinery, research institutions and extension services. to help entrepreneurs to develop proposals that will qualify for



loans.

Let us be very clear, the President's Budget is not meant only for 2011, it is a journey starting from 2011 for the next six years. The 2011 Budget essentially sets the direction and momentum. The process should be a sustainable one which requires the people to build on these proposals. That is why even in the Government development strategy, value addition has been recognised as a key component.

**Significant changes have been made in the Telecommunication tax system and call rates have been revised. How will this benefit the consumer?**

Telecommunication is one of the private sector driven infrastructure industries that has to play a vital role in the next five years. In our deliberation with the industry stakeholders we found, the industry itself is preparing for a two billion dollar investment in infrastructure to deepen the telecommunication facilities in our economy responding to energized sophisticated IT, knowledge based activities and a wide range of service industries relating to export and import trade. The Government has ensured that all companies have access to technology. Therefore duties and taxes have been reduced on the importation of such items and the tax system itself has been designed to be conducive to expand this industry.

**Let Us Be Very Clear, The President's Budget Is Not Meant Only For 2011, It Is A Journey Starting From 2011 For The Next Six Years. The 2011 Budget Essentially Sets The Direction And Momentum.**

Therefore with a simpler tax system, access to cheaper capital, provision of machinery and equipment, an expanding economy of well over eight percent, the demand for telecommunication services coming from many sophisticated industries and services, the telecommunication industry is positioned to be a lead industry. There will be further investment in the broadband infrastructure facility because the country needs to provide high intensity telecommunication facilities in the region.

**Tax changes have been made in the Banking sector as well, such as abolishing of the debit tax, reduction of VAT on financial services. How will the public benefit?**

These activities benefit the public in many ways. The biggest hassle that people have to face is the hidden transaction costs associated with the operation of a multiplicity of taxes on financial transactions. When people buy a product or a service it is not only the price they have to worry about, but also the process they have to follow and tax liabilities associated with such a process. When withdrawals are liable to debit tax people tend to discourage the use of banks and increase their informal cash holding activities. As a result, banking and formal financial activities do not develop. There are many implications from these kinds of activities for the development of long term financial industry. That is why the debit tax was removed.

Then, having two to three different tax rates on different financial products create problems. VAT on leasing is different from VAT on some other financial services. Leased vehicles, machinery. will be used in investment and production activity. Some of the SME sector activities are burdened by heavy taxes. In order to promote investment and reduce cost of transaction we need to remove barriers for such activities. It is like, when the war is over, people want to remove road barriers, because people need to enjoy the benefit of peace. Similarly, when the economy is ready to take off, certain barriers have to be removed and debit tax and different rate of VAT and such were such barriers affecting growth.

**In the banking sector we see that lending facilities are restricted. When new businesses go for loans, there are many procedures involved. Do you see the banking sector relaxing these procedures?**

To be very frank the banking sector has quite a lot to do. Though banks have gone on a technological drive over the last few years through online banking and other such facilities, the average customers that I meet at various industry meetings express three concerns. First is the cost of finance that is interest rates and maturity structure related issues. Second, they speak about the attitudes of the banks particularly at operational ends. The CRIB and various other tools, which were designed to assist banks to conduct professional risk assessment, are used to refuse credit. Third is the procedure that they have to follow at banks. Despite online banking facilities being available, a customer still needs to complete the same applications, which consist of many pages designed to suit a different era. Today in a world where everything has been simplified I am amazed why only Sri Lankan banks are not inspired by such methods particularly when their profits are absolutely sound and human resource base is quite strong.

## **To Be Very Frank The Banking Sector Has Quite A Lot To Do... Banks Have Gone On A Technological Drive Over The Last Few Years Through Online Banking And Other Such Facilities...**

Of course banks must make profits and system, stability must be maintained at all times. They must comply with regulatory standards. Our Central Bank has been able to maintain a solid banking and financial system in the country, less vulnerable to external shocks and as a result we have not been subjected to downside risks that the world went through. All these achievements are very good, but at the same time, looking at only the non-performing loans will not work. All other issues must be addressed. The President had the vision to provide a road map for banks to move on to long-term lending, but banks also need to think of a simplified way of doing banking. Why is it that people go for financing despite the high cost? Because of the simple procedures and less rigid security cover. Why do people still go for informal banking despite the risks? Because of the cumbersome bureaucracy within the banking institutions. I hope our banking and financial institutions will address these issues as the economic outlook has improved considerably and banks have a good reasonably sound tax system in the country.

The President has proposed to appoint a Banking and Financial Commission because we know that reducing taxes or long term lending alone is not enough. This country needs another ten-year journey - a journey that will adequately compensate what the country lost over 26 years of terror and banks are the critical institutional set up to drive this process. To drive development, credit, equity, various banking and financial products, insurance, leasing, merchant banking, investment banking and project financing, are all a wide range of products that must come from the banking and financial system. Therefore, the President in this Budget has also proposed to appoint a Banking and Financial Commission, which may take some time just like the taxation commission to have public hearings, discussions with bankers, share international experience and propose required changes beyond the regulatory and conventional aspects. Development depends on the banking and financial institutions. We need to ask whether our development banks have done enough, or are they shifting towards commercial banking, how far our banks are capable of taking risks, how far our banks can restructure during bad times as well as in good times and how every customer in the bank can obtain support. The attitudes of the employees in

branch networks of the banks are important. They need to think whether it is enough just popularising a wide range of deposits through children, elderly, school leavers, university students and government servants. I hope the commission will address some of these issues and the bankers themselves will find solutions to these issues soon.

**We Need To Improve Our Agricultural Infrastructure To Contain Vulnerabilities On The Supply Side. Now Infrastructure Such As Roads And Various Other Facilities As Well As Irrigation Facilities Are Being Constructed. But We Need To Increase Our Production.**

**When will we see lending interest rates falling to single digits?**

That depends on several factors. To reach solid single digit interest rates, the Government must manage single digit inflation. That is our responsibility. But that is a complex responsibility. From one hand the monetary authority has to conduct the monetary policy in such a way that liquidity management will not fuel inflation. That is a difficult process in time to come because we are also expecting heavy capital inflows, which means additional process on liquidity. Too much liquidity cannot be permitted from the inflation point of view. Similarly too little liquidity cost growth.

Therefore, it is a delicate balancing process. From the Government point of view the President has announced the Government Budget deficits will systematically reduce over time. In his Budget speech, which was delivered on November 22, 2010 as well as in his wind up at the committee stage of the Ministry of Finance, the President very clearly spelt out the medium term direction which involves a qualitative improvement in the Budget. The information that the Government will disclose on the Budget is the direction that the Budget will go. The quality of the Budget making process has changed. At the end, the Government and the private sector share the available savings in the country. Thus the budget will be designed in such a way it will not add undue pressure on the allocation of savings on the financial system. This is from the demand side of the equation. But, more fundamentally, in a country like ours, inflation is not just a financial outcome. It is also affected by real economy and structural issues. Our efficiency or inefficiency in production and distribution of goods matters, our banking system and intermediary costs matter. Supply bottlenecks and seasonal disturbances affect the real economy and create inflation. Look at the recent floods, not only in Sri

Lanka but also India - they are talking about high onion prices as a national issue, it is a temporary crisis. India has banned exports. Now if we impose a ban, someone will say that we are going against international trade practices. India had to impose a ban, because it is such a delicate problem as one flood ruined the key commodity that the country needs. Fortunately the flood in Sri Lanka is conducive for a good Maha cultivation. But imagine the price impact on food and vegetables if rain was too much, then what actions would we take?

Therefore, we need to improve our agricultural infrastructure to contain vulnerabilities on the supply side. Infrastructure such as roads and various other facilities as well as irrigation facilities are being constructed. But we need to increase our production. Fortunately we are now self sufficient in rice. We have to increase our rice production not just for 12 months but in excess of a 14 month requirement. We need to increase our production beyond our consumption requirement and we need to maintain certain stocks in other essential commodities as well. Globally dairy products are becoming increasingly expensive; therefore Sri Lanka needs to move on to dairy production activities. Similarly, with poultry, we saw what happened to chicken prices because of bird flu and various other problems that many poultry producing countries went through during the last five to six years. Therefore, those factors also need to be managed in order to bring down inflation on a sustainable basis. As such in this Budget, though people do not speak about it loudly, the Government talks of a backyard economy. One million home economy; two activities which are designed to reduce the frequency of people going to the market for certain basic food items. This strategy will also encourage certain households to generate a surplus in their own home economy so that they can sell at the market. If you go to the village pola (fair), what vendors sell is the surplus produce from their home gardens. These activities have immense potential in our economy.

Therefore these activities will help inflation to come down. If everybody rallies round His Excellency the President and work hard to improve infrastructure, the rural economy, improvement of one million backyard - home economy concept, distribution network and storage facilities, the supply side will certainly produce results. The determination of Central Bank to maintain 5-6 percent interest rate can be realized. All the demand and supply side considerations will address and that in the determination of the Government. I do not see any reason why interest rates should be say more than two to three percent higher than the inflation rate.

**In Sri Lanka there is a gap between the tax department and the people. How can we address this?**

**2011 Is A Beginning Of A Peace Decade That Support A Development And A Prosperous Decade. That Decade Will Make The Emerging Wonder Of Asia A Reality.**

There is a gap. That is partly because the tax system is very complex. From the point of view of the department, to justify what they have done, the department was managing unmanageable taxes. Each tax has its own interpretation. If you go to two officers, they will give two different interpretations. Then, certain people started making money out of it, corruption crept into it, various tax consultants came and complicated the system. That is part of the problem as to why people and the Tax Department work differently.

The second thing is, sadly and regrettably, we do not trust people. Nothing happens on trust. Good and bad people are equally treated. As a result you do not know how to reward a good tax payer. These things must stop. But, we cannot blame the officials alone because what they are saying is that they manage complex tax laws. Therefore, one step is to have a simplified tax system. That is what the 2011 Budget has introduced.

Then, rather than blaming Government on corruption and irregularities, the people must stop corruption. To speak very loudly, they should not give money to any public servant. If they have problems they must report them to the respective heads of departments or secretaries. They also use various names in this country.

The private sector should stop lobbying if you want to have a good government. If they have a problem, they have to bring it to our notice, and then we will address them. We must address them not for individual interests but in the interest of the entire society. We have initiated that process at Customs. Some people tell me that if they bring these things to the notice of the government then the cost is more. But we have to meet that cost if we want to clean the country.

This must happen now and if a public servant asks for a bribe, disclose it. Rather than saying that the public service is corrupt, I am taking the position that the public service is not corrupt.

It is my duty to say on behalf of all public servants that the public service is not

corrupt. We may have made judgmental errors, we may continue to do that. That is our judgment; that is not corruption. If it is a deliberate action to act in an individual's interest, then it is corruption.

### **Is Sri Lanka moving towards import-substitution and protectionist policies?**

No, it is not. Import substitution means in theoretical terms, banning of imports. There is not a single ban of imports in this country unless such imports are harmful on security, health or environmental considerations. This country is probably the most liberal economy compared to several other countries in Asia. Anyone can import as long as they fulfill health, security and environmental considerations. We do not have trade restrictions. In the 2011 Budget the Government proposes to introduce anti dumping legislation, because there are many substandard products available in the market. Though they may appear to be cheap, they are not cheap from a long-term perspective, because people are consuming poor quality products, in the name of cheap imports. It is the responsibility of the Government to prevent such imports taking place, not by restricting but by setting standards that need to be met when importing products to Sri Lanka. No country can export anything of poor quality to the advanced economies. You can see the difference of cars for example exported to advanced countries vs to cars coming to our country. That is because we do not strictly impose these standards.

Sri Lanka has also adopted certain policies. Whatever Sri Lanka can competitively grow here such as, rice, there will be duty on imports during harvesting periods. Other than the duty, rice is not a banned item. Anyone can import rice and sell subject to standard duty. Similarly, we should not permit import of tea because we are a major tea exporting country. Some people are of the view that if the Country permits the import of tea, it can create value addition. That is a model applicable maybe for countries which do not grow tea. Twenty percent of the world's best tea is grown here, and Sri Lanka has an identity of its own. We do not need to import tea for mixing and export. What Sri Lankan entrepreneurs or investors need to do is see how Sri Lankan tea can be converted to a value added product without mixing with foreign grown tea. These are not protective measures, these are essential to exploit our full competitive advantage to the best interest of Sri Lanka, because only then Sri Lanka can create a value added economy and move away from the primary commodity exporting and importing

status.

I had a meeting with the beauty care industry prior to the Budget. All the top names were here because we wanted to know whether introducing high CESS, taxes and quality standards for the importation of international products would harm the beauty care industry. A large section of this industry asked us not to reduce such taxes and duties because skin care products that are being developed by Nature's Secret, Janet, Link Natural and several other local producers in Sri Lanka are now of very high quality. They use world-class natural herbal raw material that is grown in Sri Lanka. There is immense potential for this industry in Sri Lanka.

### **What Sri Lankan Entrepreneurs Or Investors Need To Do Is See How Sri Lankan Tea Can Be Converted To A Value Added Product.**

Therefore I do not think we are going for import substitution, what would you say if we discover gas? Are we shifting to an import substitution strategy? No, because gas is available here. Similarly mineral and several other products. In this Budget the government allowed people to import raw gems from Madagascar and various other places because, a) Government wants to preserve our environment and, b) minerals should be protected as it is an asset and the value will continue to increase. Until Sri Lanka develops its own technology the Government has permitted people to import raw gems, like raw textiles and do value additions here and export. That kind of trade pattern is taking place in the country. The tea and apparel are two good examples.

We had extensive consultations with the IT and computer software industry. They say that they can develop the required software needs. All what they required was the facilities which the Government has now made available. The industry is becoming a world class software supplier, maybe not to the scale that many other countries do but we do not need that scale. Therefore one should not think in a narrow theoretical sense that these are import substitution strategies. We see designer shirts and other garments manufactured in Sri Lanka are purchased in New York and brought here. Some Sri Lankans who shop in New York do not like to buy them because the garment is made in Sri Lanka. I cannot understand why a Sri Lankan can't be proud of buying a Sri Lankan designer product in New York instead of buying a product made by another country. Our manufacturers are of that scale now. That is why the Government advised the apparel industry not to



be panic over the GSP Plus withdrawal, because the industry was not operating at the lower end of the market. The GSP Plus was a bonus for the economy, but even if it is not there, our products are well received in those markets. As I mentioned in both my previous interviews last year, the apparel industry has proved that it can survive. SMEs have different problems, which the Government addressed in this Budget.

**If we move on to the tourism sector, the target is to attract 2.5 million tourists by 2015. Currently the progress in the tourism industry in terms of development of infrastructure, facilities and services is slow. What has been put in place to expand this sector?**

With the tourism sector, again, we must be ready to accept a transitional phase. Hon. Minister Basil Rajapaksa, was quite realistic in his approach to expand tourism. His idea was that the industry should not excessively be excited about putting up hotels all over the country, because first the industry must allow existing hotels to get the full benefit by pricing their products right. Tourism is a product; it is not just a hotel. Industry needs to get the Sri Lankan product right. Thus, he allowed the industry to slowly move in that direction, providing good products, improving the Colombo city environment, tourist attractions, ensuring security and let each visiting tourist becomes a promoter of Sri Lanka. Let each tourist say how wonderful Sri Lanka is and ensure that they will come back next time with another person. Imagine the expansion if all the 600,000 tourists, return with another tourist this year. That is better than us spending millions and millions of dollars in few cities on promotion at this stage.

Web marketing is done and each hotel can do their own marketing of their products. New products need to be developed and the country must look into more environmental friendly, wide ranging diversified products like wildlife, nature activities, mountain climbing etc. Then Sri Lanka has history, art, music and events that need to be organised. Industry and the Government must look at an event calendar to make all-round diversified activities that the tourists can spend during their holidays. Tourism is mainly about attracting people.

The President is speaking of a sports economy. Imagine the impact of Sri Lanka's sports economy expanded beyond cricket and targeting 100,000 tourists coming for sports events. Therefore these types of preparations are necessary when industry speaks of 2.5 million tourists. It must also be a sustainable tourism. For

example, tourism activities associated with the Kandy Perahera, maintain certain values even when the environment was not conducive for tourism during the past 26 years. Despite the war and natural disasters, cricket took place in various designated destinations and Sri Lankan team kept their flag flying globally. Now Sri Lanka should be one such location for such activities, not only for cricket but other sports events too.

The President is speaking beyond cricket. All domestic and international sports are to be developed within Sri Lanka. So that Sri Lanka will be speaking of not only economic and traditional activities, but also about the sports economy. Maybe it is very costly for Sri Lanka to bid for international events. It is necessary to show our willingness and capacity creation ability for such global events, through expressing of interest to participate in such ambitious initiatives.

**The aim is to increase market capitalisation from two trillion rupees to three trillion rupees, which needs to be done by encouraging the listing of new companies and debt instruments. How will this be achieved?**

This will be achieved in several ways. First the improvement in security as well as economic environment is very critical to attract investment into the stock market. Second, low interest rates and low inflation rate regime will bring equity as an attractive investment. In this background the Government has taken a number of measures to promote unit trust and the insurance industry to promote market development. With expected investment picking up from 2011, many companies will enter the stock market for capital formation.

The Government itself is looking at companies such as SriLankan Catering, Litro gas and such. for listing options. I am also told by two or three large private sector investors that they will bring their businesses into the stock market. It is encouraging that medium sized companies too are placing their confidence in the market. The listing of Laugfs, and several other local power companies have given the lead. The medium sized companies are no longer relying on bank borrowings, but on the Stock Market. Because they feel that the capital market is a good vehicle for both market promotions and capital formation. This will continue because of the improved economic climate, low interest rates and improved taxation arrangement. After all no capital gain tax in Sri Lanka.

Above all, what is important for everyone to realize is that during 2010, the daily

market turnover has been sufficiently large; approximately two billion rupees. This is a significant change considering the market turnover of around 200 million rupees until recently. Of the blue chip companies, at least well established companies have a good asset base. Companies that are in plantations have benefited from commodity price boom. Companies which are in tourism have benefited from the surge in tourism and earning potentials. Similarly, the companies in export and business activities are also recovering. As most of our companies are highly diversified the market will pick up rapidly.

**During the next decade our aim is to increase our productivity from five percent to six percent. How will this be achieved?**

Productivity is very crucial. With stability coming into the country, the critical variable that explains economic growth is productivity. Until recently, most of our export and import substitution industries were supported by the depreciating exchange rate, approximately 10 - 12 percent per annum throughout a long period of time. That is the environment within which we managed this economy. But now, the country is stabilised and inflation is stable. In fact the exchange rate has been appreciated by about three percent during 2010. This is more or less the general tendency in an emerging economy. In that context, the country needs to move on to productivity improvement more regularly.

*The private sector has to be more aggressive in productivity improvement progress. Productivity cannot be achieved in conventional ways and it needs to be innovation centric.*

Productivity can be achieved in two ways. First is that the labour force productivity which needs to be improved by knowledge based activities and skills development. The 2011 Budget has placed a significant emphasis on the need for the private sector and public sector to get together and partner on skills development activities. The SME restructuring package of the Government itself recognises the need to improve workforce to be skilled to make their contribution towards reviewing SMEs. Second, productivity improvement needs continuous research and technology improvement. The Government has given a double deduction of research and development expenditure to entrepreneurs. The 2011 Budget has suggested that all the government research organisations and private sector organisations get together and engage in research and development activities. In the agricultural sector, intensive researches towards promoting right

seeds, planting material, production technology, water and fertilizer conservation and new business practices are vital to move towards making surplus production in food items.

Sri Lankan economy and its industries and enterprises which suffered for 26 years must have access to modern machinery equipment from abroad. Therefore, the entire customs tariffs and duties have been restructured to facilitate our industries to buy those machinery equipment at competitive prices. Importation of such machinery equipment including those required for the health, education, pharmaceutical industry. allows the economy to be benefited from the latest technological advancement. All these will contribute towards productivity. The creation of the separate Ministry dedicated to productivity with the National Productivity drive together with the National productivity Council will enable the country to use a coordinated approach. Emphasis has also been placed with the Secretariat for Senior Ministers who can guide the line ministries and private sector on research, technology and productivity activities with their vast experience in Government.

Productivity needs well-coordinated machinery and all the ministries need to work towards productivity improvement. In this context, the systems and procedures adopted in many government agencies are not conducive to improve productivity in our country. Therefore, those systems and procedures are being looked at seriously. The pioneering work done by Motor Traffic Department, selected hospitals, District Secretariats and such. show the way forward. Apart from simpler taxes, the modernisation of Customs and Inland Revenue will also contribute immensely towards productivity improvement and reduce transaction cost. If everything goes well, Customs will move towards a technology based documentation processing system from this month. This will help our trade economy to improve its international competencies.

The private sector has to be more aggressive in productivity improvement progress. Productivity cannot be achieved in conventional ways and it needs to be innovation centric. Our labour force is educated, they must be motivated, equipped with technology and be managed with expertise. HR managers are all a part of it. Of course, I hope the private sector will be able to have a motivated executive and the middle level managerial categories from 2011, thanks to the President's bold initiative of introducing a lower and simpler PAYE tax system in this country.

**With Sri Lanka poised to become an Aviation Hub significant encouragement has been given to SriLankan Airlines and Mihin Lanka, can you elaborate on this?**

Any economy emerging as an aviation, port or knowledge hub, needs a critical mass provided within the country. Open sky policy is good, only if you are looking at free access. Who provides is irrelevant. However, if a country wants to create a hub, the core activity must come within. SriLankan Airlines and Mihin Lanka have been targeted as critical service providers. The airport authority itself needs to be a service and infrastructure provider for two international airports; Katunayaka and Mattala and also the domestic airports.

All airlines coming to Sri Lanka, who are either stopping over for fueling or transit or flying direct as a destination, need various services like fuelling, ground handling, catering, maintenance and repairs and new skills. All these are part of this aviation hub concept. As a result the whole industry is being restructured.

In this context, why SriLankan Airlines and Mihin Lanka were given special concessions was because their airline activity is offshore and you need good skills to manage such services. Also, in order to maintain their viability, they need to be given a period of consolidation. The package we have given to SriLankan and Mihin Lanka is not different to the package the Government gave to Emirates when they took over in 1998. From 1998 to 2008, they enjoyed tax holidays, free importation facilities and such. The Government considers that SriLankan and Mihin can reach very specific markets in the region. Mihin will be targeting selected destinations in the Indian, East Asian and the Middle East markets. Mihin is also expected to be the feeder airline for SriLankan. SriLankan will target Europe, Far East, various destinations in South Asia and network Sri Lanka to a global hub. Sri Lankan needs to be positioned well as our country is better located to connect to the Asia Pacific, Middle East and Europe.

**I Request The Tourism Industry And The Country To Recognise The Contribution Of The SriLankan Airlines During Trying Times In The Country.**

In this context the planned strategies include the expansion in the airline over the next three years to about 30 modern aircraft fleet structure. The new Board of Directors, the Aviation Ministry, the line agencies, the private sector and Finance

Ministry are expected to work towards this goal. I request the tourism industry and the country to recognise the contribution of the SriLankan Airlines during trying times in the country. It was only SriLankan who brought tourists to the country. Even now, 70 percent of the tourists are coming through SriLankan Airlines and that market share must be maintained at all times.

It is true, open sky is welcome, but it should not be at the cost of the national carrier. Air balance needs to be established in a competitive environment. The message to SriLankan Airlines is that they must be equally competitive. They cannot charge high prices, they must become the promoter of Sri Lanka for travel. SriLankan Airlines also like other private sector businesses must try to use local talents and local products in their planes, they must show and offer local products that are being manufactured today. I do not see any reason why they cannot use local biscuits, chocolates, magazines, flowers and fruits, thereby giving a national identity to the Airline. I hope in the coming year, SriLankan Airlines will change their business plan to maximize value chain in this industry and Sri Lankan economy.

**Certain products such as the surgical gauze, pharmaceutical products, text books etc are to be supplied by SMEs, is the capacity there to fulfil domestic demand? If not how will it be generated?**

The capacity has to be developed. It is a chicken and egg situation. If you look at the Government Budget, each Ministry provides a variety of free goods and services to the people. There has not been a focused planning exercise to use that as a demand tool to improve production. For example, the Health Ministry provides the triposha programme at a cost of 1.5 billion rupees to improve nutritional standards of lactating mothers. This needs soya, maize and milk powder all can be developed in local economy. Then, we have a USD 300 million pharmaceutical market of which sixty percent is imported and distributed by the Government itself to provide medicine free of charge to all our hospitals in the country. I am sure a fraction can be manufactured and the local capacity can be built. Based on that, you can move towards a USD 300 million pharmaceutical industry locally.

The Government spends about 400 billion rupees to purchase surgical gauze which is a household and SME industry. All what the Government has to do is to set the standards required and allow SMEs to manufacture the country's

requirement.

Look at the Ministry of Education, it buys all the furniture for schools all over the island, provides free text books and free uniforms to all the 4 million school children. All three can be made locally. Then, we have a huge fertiliser subsidy which costs about USD 300 million per annum. Part of it can be exploited locally by moving to organic fertiliser as well as various other varieties. Therefore, I am of the view that a massive domestic economy can be built based on the Government's free services provided both the government agencies and boards, private sector, all commit to quality local production using technology and best business practices. This is why His Excellency the President in his Budget speech for 2011 placed in special emphasis on these activities and I hope all concerned government agencies will work towards achieving this objective. Private sector equally can work in that direction.

Supply of linen to the hotel industry, can be a solid market for our textile industry. Gift manufacturing can be a beneficiary activity from tourism provided that proper business links are established. That is how Japan, Korea and all other emerging economies established internal economic integration. At the initial stage they gave this kind of guaranteed markets for local suppliers to build their production base. Quite a large number of activities are being identified and further planning and coordination is necessary to make such a programme to deliver results. We hope the Ministry of Economic Development and other ministries will get together and coordinate these activities to replace most of the unwanted and wasteful imports. Hon. Basil Rajapaksa, Minister of Economic Development is fully committed to these initiatives.

**This Is Why His Excellency The President In His Budget Speech For 2011 Placed In Special Emphasis On These Activities And I Hope All Concerned Government Agencies Will Work Towards Achieving This Objective. Private Sector Equally Can Work In That Direction.**

Why should the country import soya bean when our farmers can grow it? Why can't we tell them the soya bean requirement so they can plan? The triposha requirement alone is a good model for the country to think about, how Sri Lanka can meet the nutritional food requirement of lactating mothers in the country. We can even supply to other developing countries through WHO and such other sources, because our health standards and our achievements are very impressive.

We can target a bigger market and we ourselves have 1.1 million expectant mothers each year. Those mothers need nutritional food. I do not see a capacity constraint, it is only lack of proper planning by each ministry to work closely with the private sector. The private sector we are talking here are our small farmers, our small industries and our small service providers. They must be guided and the Government has a huge network to support them. Industrial Development Board with its countrywide network can provide technological assistance. The seed certification services of the Agricultural Department can provide the extension services to make quality seeds, best cultivation practices, apply post and pre harvest technology. The message is that if all line ministries, secretaries, heads of departments and agencies work together and coordinate, rather than working in a compartmentalised environment, then Sri Lanka can maximize its national output significantly and improve the living standards of the people. Also we all must work with our district administration and Government Agents who have a superb operational network to reach our farmers and small producers. I do not see that capacity problem is an issue for SME development.

### **How do we get ministries to come out of the individualistic approach and work in a coordinated manner?**

The restructured cabinet in my view is very subject specific. First time in our system it is also supported by a team of senior ministers who can lead the coordination work to break silo operations. The structure has been worked out on the basis of national priorities. This kind of national attention at a cabinet level is required. The senior ministerial model is like Singapore, which was recognised to give a more macro approach to policy development and coordination. For example, think of the national issue of food security which cannot be achieved by one single department or a ministry. It requires the involvement of a wide range of ministries. Therefore, the Ministry of Economic Development, in terms of the mandate assigned to it, requires to work with other ministries plus the senior ministers, who have been entrusted by his Excellency the President, to coordinate several ministries to achieve such national goals. I feel overtime this compartmentalised approach will disappear and everybody will get onto a team work. It will not happen overnight. People are used to various power blocks and they like to work in those areas, but if one can coordinate these segments, it can make a huge difference. This Budget attempted to bring the devolution meaningful by making the Provincial Council and the Government to work



together. Earlier we had taxation at two levels. Now, taxes are collected by one agency at one level and share the revenue in a meaningful and equitable manner, so the provincial devolved administration will be able to provide those services without creating difficulties to the community. This is just the beginning; these new changes that have come up will be institutionalized overtime. Everybody expects miracles, but miracles cannot happen unless changes take place over time on a sustainable manner. All the successful countries today that people quote are all 30 year matured stories. We have, President Mahinda Rajapaksa's Mahinda Chintana new approach, which is only a five year story so far. The Country has achieved a lot. A decisive change will happen when he completes the 10th year. People are beginning to appreciate this, even the top class private sector people who did not believe that this Government can make a difference are now beginning to see the difference. They see a meaning to domestic value addition to domestic branded products being recognised, there is a meaning to private sector being recognised. Certain resourceful private sector investors have told me during discussions that if an enabling environment is created, resources and money retained abroad by many of them is sufficient to change this economy. That's the message that they are giving.

This is because confidence is building slowly. The confidence is what matters while we are trying to promote foreign direct investment. Last several years, what has been our foreign direct investment? 600 million dollars per year. How much money do you think has gone out of this country? How much money has our private sector retained elsewhere? No one has computed. How much money do you think people are taking to educate their children abroad? All the top high net worth people, where do they do their medical testing, are they doing their testing in local health facilities? Calculate this money. If you compute, I can basically estimate that the money we take out from this country for tourism, while we promote tourism is greater. Our people are travelling elsewhere, so the money is spent on tourism, money is spent by our people on education, money is spent by our people on health, shopping, and various other things. Plus, the money retained by our own investors when they are exporting and importing, their money transactions cannot be controlled. If you create an enabling environment and reverse a fraction of this process they themselves come and tell me, we have money here to bring the required investment. One thing we must be happy is every investor who came from 1977, take Prima, take the famous Tao investment, then take all the foreign investors who came for the garment industry, our export

processing zones, they have not taken a large amount of money out of the zones. They continue to use their retained profits as investments and therefore retained investment is very high.

**We Have, President Mahinda Rajapaksa's Mahinda Chintana New Approach, Which Is Only A Five Year Story So Far. Country Has Achieved A Lot. A Decisive Change Will Happen When He Completes The 10th Year. People Are Beginning To Appreciate This, Even The Top Class Private Sector People Who Did Not Believe This Government Can Make A Difference Are Now Beginning To See The Difference.**

I am very confident that the enabling environment we have created is more than sufficient for our private sector to now embrace a government free of politics, because politics is not required for the private sector. What private sector needs is the right business environment and the right business environment has been created, right stability has been created, we have assurance of the Defence Secretary. The credible assurance has given does not stop just at terrorism, but also law and order will be preserved because the Government considers that for the investor the biggest risk they cannot manage is the security risk. Nothing else. They have expertise on profit and business. There is plenty of investment opportunities in this country and that is what we should target. We definitely need about three percent of FDI coming in, but please remember, that we should not underestimate the potential of our domestic investors. Their funds are sufficient for productive investment.

Capital expenditure in education and health sector is 54 billion rupees. However, there are still short comings in both these sectors especially in rural areas. What is being done to further develop this sector and ensure that facilities are available for all?

Here is one area where I tend to disagree with some of the critics. Capital provision in the budget for education and health is 50 billion rupees. That is purely for the development of school buildings, hospitals and related infrastructure. But there is another 150 billion rupees for the education and health sector to pay salaries to teachers, doctors, nurses and other employees. Though these outlays are classified as recurrent, they are essentially investment in education each year because you need to pay the teachers to educate children and doctors and nurses to provide health services. Education is not actually

buildings and furniture. Health is not just hospitals and operating theatres. It is the availability of quality services that matters. Sri Lanka has 1,100 consultants in a wide range of specialization. 12,000 highly qualified, world class doctors, nursing and pharmaceutical services. Their standards are very well recognized. So the recent expenditure for them is essentially to provide a long term products. This Government has allocated 200 billion rupees for three services in 2011. If you go to distant places there is a dispensary and there is a school in each of these places. Of course, there are gaps. But this Government has changed that. The Government has proposed to develop 1,000 colleges right across the country. They will be like satellite schools linked with five to ten primary schools so that everyone will have access to a recognised college. Similarly hospital needs of rural areas are being addressed. This Government has an uncompromising commitment to take education and health to rural areas to provide access to health and education to each and every person in the society.

The President himself is committed to position Sri Lanka as a lead nation achieving Millennium Development Goals. While many countries are struggling to finance programmes towards achieving Millennium Development Goals, Sri Lanka is already ahead of many other nations free of poverty. Only in the area of nutrition our country performance is slightly below the Millennium Development Goal targets. That is why this Budget has given special attention to address nutritional needs of the population.

There will be a reformulation of strategies and institutional mechanisms to improve the investment climate of the country. BOI will be reformulated and institutional mechanisms will be changed. The BOI has to be the investment promotion agency in the country. Anyone who goes there must be able to come back with a very credible response. There is no harm rejecting investment proposals upfront if it is not acceptable. But an investor does not like a 'wait and see' attitude.

**The President Himself Is Committed To Position Sri Lanka As A Lead Nation Achieving Millennium Development Goals. While Many Countries Are Struggling To Finance Programmes Towards Achieving Millennium Development Goals, Sri Lanka Is Already Ahead Of Many Other Nations Free Of Poverty.**

Above all, the BOI officials must be two hundred percent dynamic. Institutional

dynamism should come from the Chairman, the Board of Directors, the executives and the officials. Recognising these changes to be made to the BOI, 2011 Budget has outlined the way forward for BOI. It has twelve well-established zones right around the country. Each zone has lived upto certain expectations. But now the country has to ensure that those zones will live up to our next ten year expectation. They are productive assets and must be fully utilised. Right now, these zones are not fully utilised, including Katunayake which are prime properties with well developed infrastructure. Unless we get the maximum return for these infrastructures, the country will lose. Therefore, zone management towards optimum use to the satisfaction of investors is a primary responsibility. We have suggested the BOI to have a dedicated Zone Management Division which should not be bureaucratic. Freedom of managers of each zone must be protected, to respond to investor needs in the zone and make sure that the zone is optimally used. That is one.

The second issue is that the BOI needs to facilitate the investors who are looking for investment opportunities in this country in urban development, tourism, agriculture, livestock, energy, housing, pharmaceutical and IT. Therefore, we must have a dynamic Investment Branch, which can coordinate with other line ministries and resolve problems. The approval procedure needs to be streamlined. The BOI cannot get away from this responsibility. The BOI, the Ministries of Finance and Planning and Economic Development must get together and put the house in order because we need very dedicated and committed people.

We have experience to learn from. We have made mistakes in certain areas in the past, and have success stories in many areas. We must be able to speak to all successful BOI investors who are already here. We must ask from them what they can do for another ten years. Probably it is easy to promote the investors who are already here rather than getting a new investor.

New investors are also responding strongly to the post conflict prospects in this country. The BOI should be able to grab these opportunities. Shangri-La has shown interest in Sri Lanka. That is an almost USD 500 million investment which is not only on tourism, but also on property development, shopping facilities and several integrated investment activities in urban development. Similarly, there are several investors who are looking at agriculture, livestock, plantations, tourism and such. In my view, there are unnecessary delays in BOI.

The BOI must also concentrate on follow up and monitoring. The existing investor portfolio needs assistance, because they have come here under different conditions. Therefore, whenever they request something, it should be responded timely.

Thus, the Zone Management Division, an investment arm and monitoring and follow up unit should be managed by professional dynamic teams. We need a new outlook and a new team because some of the executives are not responding. They have to change their lifestyle, their attitudes and ensure that the BOI is client friendly and investor friendly and that is what the restructuring is all about. President Mahinda Rajapaksa is not talking of any retrenchment or winding up. It is essentially to reorient the organisation, to serve in the best interest of Sri Lanka, particularly because we have set a very ambitious target for FDI. FDI will not just come unless the BOI is absolutely dynamic and I remain committed as the line ministry secretary to ensure that happens.

### **What about privatisation of education?**

The President has very clearly stated in this Budget too that nothing will be privatized. That is a policy of this Government. So there is no room for privatization of educational establishments or universities. The structure in Sri Lanka is such people have access to private education and health as well. It is provided in two ways. One, people can go abroad and acquire these services, there are no restrictions, anyone can go to any university outside Sri Lanka, provided they have money. Similarly, there are recognised universities providing educational services to Sri Lankan students to obtain foreign degrees. It is the same with health. Sri Lanka has a number of well established private health facilities. What the Ministry of Higher Education has said is that they will bring relevant legislations to regulate educational establishments, to ensure that our children get quality education. It does not matter who provides it as long as everybody has access to quality education. Basically, investment in education is a kind of nonprofit activity and those are the ones that the government has recognised to promote in the next several years, while protecting the 100 percent Government ownership in the existing universities. The Government has also proposed to promote well established universities like Peradeniya, Moratuwa, Colombo, Jayawardenapura and Kelaniya to obtain international ranking. There is a 600 million rupees allocation to be given to these universities to meet such expenses and I hope all these universities will apply for international rating and

compete for this important venture. This money will be given only on the basis of the awards and the ratings that they get. It is essentially a performance based reward.

Then, there is also another separate allocation; a three year allocation of three billion rupees has been proposed in 2011 Budget for universities located in the regions like Ruhuna, Rajarata, Wayamba, Uva-Wellassa, East and Jaffna. His Excellency the President is keen to see these universities also develop up to national university level too. They need good infrastructure and the surrounding area to be developed as University Township.

A massive sum of money has been committed to revive skills education and vocational training. The Youth Affairs and Skills Development Ministry is targeting 300,000 new skills not because the government wants to produce 300,000 skilled youths in different fields but due to heavy demand for such skills from tourism, construction, plantation, apparel, IT, pharmaceuticals and clinical research. In this background, the Ministry of Education, Ministry of Youth Affairs and Skills Development, Ministry of Higher Education and Ministry of Research and Technology are expected to work very closely and coordinated by the Senior Minister in charge to give that leadership and navigate Sri Lanka as a knowledge economy in the coming decade.

**Incentives will be provided to only priority sectors. Can you elaborate on this?**

Incentives are available, and the whole new tax regime is an incentive, the whole new security environment in the country is an incentive and the whole new infrastructure development is an incentive for investment. Then the whole institutional reform in the BOI, Tourism Authority and the line ministries are all incentives for investment. We are basically creating an enabling environment as much as we can. We are taking up the challenge.

In the meantime, we recognise that there are certain areas that need large investments. Such incentives are provided under strategic investment law and relevant tax statutes. These are fairly comprehensive incentives. It does not matter from where the investment comes from and to what sectors as long as they comply with national laws, rules, regulations, and above all the national interest. Further it should not be harmful to domestic entrepreneurs and domestic

economy. We should not attract investors who will marginalize local entrepreneurs. For instance we cannot allow somebody to import tea and set up tea processing and packaging industry because we have our own homegrown value added tea industry in Sri Lanka. The Sri Lankan brands should be promoted.

**Incentives Are Available And The Whole New Tax Regime Is An Incentive, The Whole New Security Environment In The Country Is An Incentive And The Whole New Infrastructure Development Is An Incentive For Investment.**

Some of the approvals given to spas have ruined the country's image. I do not see any reason why you should give approval for spas to open and tarnish our country's image when we have high quality local investors who have developed Ayurvedic world class and traditional spas. National identity should not be compromised. These are lessons we have to learn from the past investment approvals. The quality of investment is what matters, to alter the landscape of Sri Lanka towards realizing the emerging wonder of Asia objective.

**Would you like to speak of the Shangri-La investment a little more?**

The Shangri-La investment is an integrated investment. The land is made available at the valuation given by the Government Chief Valuer. The Government has taken a policy decision that land will not be given to investors free of charge. Up to now, all the investments we have given are on the basis of free land. We get a very nominal lease and the non-performing industries do not pay even the lease. The Shangri-La investment on the land is almost 125 million dollars. Generally, according to the industry analysis, 15 to 20 percent investment is on land. Thus, you can imagine the size of the investment. The investment is basically to create a world class hotel facility complying with the architectural values that have to be preserved particularly for the location. The investor has to keep in mind that the most prestigious Sri Lankan Treasury building, Presidential Secretariat when designing the facility. We do not want investors to tarnish the value of these buildings. On the other side there is the Galle Face Hotel which is also a heritage building in Sri Lanka. Then there is the Galle Face Green and on the other side the Beira Lake. These locational characters should not be changed. That is the kind of investments that will be promoted and Shangri-La is one such investment. We expect the physical investment to happen within 24 to 36 months.

**A new pension fund will be introduced for the private sector, where the mechanism for generating funds for this pension is 2 percent contribution by both the employee and employer. Then there will be a pension for those working overseas. Could you elaborate on the rationale behind this?**

This is where I value this Government, over all previous Governments. Governments are required to take a longer-term view, not managing just five years. Any government if they manage people for five years will win. But the country will not develop. The previous governments have had successive two or three terms but the country did not grow. Average growth rate was below five percent, why? They postponed the development of infrastructure because it was risky and politically dangerous. Upper Kotmale was delayed, Norochcholai was delayed and road building was delayed. But this President has taken a different view. He actually takes a longer-term view. I am so grateful to him as a citizen, not as the Secretary Finance, because he has built a port for the next 50 years. Nobody will talk about port requirement because you can see the capacity that is being created with the port. We have built a 20-year power generation capacity.

The road network is expanding rapidly. When I was a child, I used the Puttalam-Kandy road which was built during the colonial era. It remained the same till 2007. Now of course there is a two lane road. One can travel in no time. You just have to go to the Internet to see how new roads are coming up in all the major townships. People are talking about it.

Then our population. Every leader must realise that day by day our nation is facing an ageing challenge. The life expectancy is close to 80 years. By 2030, Sri Lanka will have quite a large number of elderly people. Imagine the challenges in time to come.

There is no pension whatsoever for the overseas employees. Roughly 1.5 million people are working outside Sri Lanka remitting four billion dollars to the country. They go there and work for two to three years depending on the time, earn big money but, no one knows how they manage retirement life. Similarly in the case of one million farmers, people in small holdings and self employment activities. All these people are a part of our population.

Right now our population is 20 million, hopefully let us say even at one percent growth in another 20 years our population is going to grow. In the meantime the



present population is not getting younger. We have in the government alone more than 450,000 pensioners and there is longevity because of good health now. There is no war and no casualties. The country is improving roads day by day and accidents are reducing. Liquor consumption is reducing and health standards are improving with reduced maternal mortality. All these things mean we have a healthy and longer life.

The President of 2030 in Sri Lanka will be too late to deal with this. He can give only a handout, but no decent living. For that too he will have to increase taxes. That is why this President who has a vision for 2030 has come up with a contributory pension scheme for all. That is how this was targeted. It shouldn't be a handout and it should be a viable one. Both employer and employee must contribute while they earn.

**This President Has Taken A Different View. He Actually Takes A Longer-Term View. I Am So Grateful To Him As A Citizen, Not As The Secretary Finance, Because He Has Built A Port For The Next 50 Years.**

Therefore, both the employer and employee will contribute to this fund and the money is there to provide lucrative savings. Of course transitional provisions will be made for those who are already close to 60, or at retirement age because they cannot pay ten years of contribution. It is voluntary. Those who are below the retirement age will be required to contribute because they must think that 2030 is not far away.

**Sri Lanka is the emerging wonder of Asia, we envisage a growth rate of 10 percent in the coming decade. How will this be achieved?**

Of course the economic growth rate depends on several factors among which the level of investment is one critical determinant as explained in the vision document of the Government. The level of investment of around twenty five to twenty seven percent is to be raised to above thirty five percent over the next decade. This is expected from three critical sources; first is to preserve the public investment that is the investment undertaken by the Government and state enterprises at six to seven percent. Then FDI, which is currently around two percent, is to be raised to five percent and the domestic private investment will fulfil the residual investment. The total will be raised in excess of thirty five percent. That is one critical factor.

The second is the efficiency of investment, for which the policy reforms in the areas of taxation, trade and tariff, institutional efficiency and public sector support for private sector expansion are being undertaken. The third is the public investment targeted critically towards expanding much needed strategic investments like ports, roads and electricity.

As the Government has consistently highlighted in all its policy documents, the future of the country depends heavily on knowledge and productivity. Therefore, the entire educational system, the institutional arrangement, primary to higher education, skills education and productivity related programmes will have further improvements in the investment outcomes towards high economic growth. In the immediate three to four years, there is the advantage of having the excess capacity in the economy largely because of the Sri Lankan economy suffered heavily due to the conflict. Now those areas are available for production. We expect substantial expansion in agriculture, livestock and fisheries, in the first two to three years followed by an expansion in value added manufacturing activities and service related investments.

**Poverty has reduced substantially but the number of Samurdhi beneficiaries are increasing, why is this?**

The Samurdhi scheme is essentially designed to provide a social safety net for the lower end of the population. So the poverty reduction strategies of the Government can help reviving income of those people. Even if poverty disappears the lower end of the population needs a social security system. The Government has taken steps to increase the income of the lower end of the population and more seriously the poor people, particularly in the rural areas, plantation sector and some of the urban poor. The Samurdhi benefits underline a minimum level of income so the total income of these people are essentially the sum of Samurdhi plus what they earn from various other sources. Therefore, I do not expect the reduction in Samurdhi beneficiaries as a measure of poverty reduction.

**That Is Why This President Who Has A Vision For 2030 Has Come Up With A Contributory Pension Scheme For All.**

Strictly speaking, a) poverty reduction should be measured in terms of access of the poor people to engage in gainful economic activities. That access will come from having access to electricity, road networks, market places, production

places, seed, credit and input markets. The entire package has been tailor made towards less income people and communities under Gama Neguma and various other rural development initiatives of this Government. b) Poverty standards depends on the level of education and health standards of these people. Therefore education and health facilities have been expanded to rural communities so that they will have access to develop their skills and knowledge towards economic production. c) Poverty in Sri Lanka is very much confined to the rural sector because they do not have irrigation facilities, proper seeds or land to cultivate. Sometimes they do not get remunerative prices for their produce. Their production activities are confined to one or few crops, so they do not have opportunities to diversify their economic activities to earn subsidiary income. For that reason the Government has introduced diversified agricultural activities with a minimum level of income to these people. The producer prices are now quite attractive. d) Because economic activities keep expanding in the construction, tourism, agriculture, fisheries and plantation sectors, the average daily wage rates of people have increased considerably over the last five years whether the people work in plantation, in tea plucking, coconut sector activities, rubber tapping or construction.

This multicity of factors contribute to poverty reduction. In the meantime of course if you see from the Samurdhi beneficiary group, we have also seen a remarkable increase in Samurdhi savings. Their Samurdhi allowances are being diverted to mobilise a considerable amount of savings among the Samurdhi families. The total volume of savings of around Rs 35 billion have been deposited by the Samurdhi Bank in Bank of Ceylon, Peoples' Bank and in the Regional Development Bank. In fact some of these savings are being diverted to expand their own activities. In the meantime the Government provides the ten billion rupee per annum for Samurdhi programs as they themselves need capital.

**Sri Lanka the Emerging Wonder of Asia, the development policy framework of the Government outlines how the Mahinda Chintana - Vision for the Future will become a reality. Can you tell us the thinking behind this?**

Well, this was done based on the experiences of five years of solid development on the ground and the two political manifestos placed before the country by His Excellency the President, one at the 2005 Presidential Election and the other at the 2010 Presidential Election where he articulated his development vision, a

vision which is essentially a paradigm shift from the strategies that the Sri Lankan Government followed till 2005. This framework recognised the need for rural empowerment strategies, poverty reduction programs and the provision of equal opportunities for everyone in the country through the development of islandwide infrastructure.

**There will be an introduction of pro-regional, pro-growth bias programmes, can you elaborate on this?**

The Mahinda Chintana - Vision for the Future document is based on some of the experiences gained in regional development progress launched since 2005. With the liberation of the Eastern Province the Government launched the Nagenahira Udanaya programme - an accelerated regional development programme, which integrated the Eastern Province economically with the rest of the country.

Equally Uthuru Wasanthaya was launched under the Presidential Task Force headed by Hon Basil Rajapaksa to fast track development in the five districts in the North. Resettlements of people, demining activities and identification of small, medium and large scale infrastructure development have progressed. We have seen the transformation that has taken place within a period of one year in placing livelihood programmes in those areas to revive the activities in the conflict affected areas.

Having realised the success of these two, the Government also recognised that all other provinces also need to be reached through specific development instruments. We have national programmes, provincial programmes and rural programmes, but there are gaps in development activities. Therefore to interface with these provincial needs, nine provincial initiatives including Negenahira Udanaya and Uthuru Wasanthaya have been launched.

The 2011 Budget, has provided about Rs 15 billion over and above the provisions made in the National Budget through line ministries to various development activities in the country. Further Rs.15 - 20 billion has been provided under provincial councils while about Rs. 20 billion have been earmarked under the Gama Neguma programme implemented under the supervision of District Secretaries.

**This Was Done Based On The Experiences Of Five Years Of Solid Development On The Ground And The Two Political Manifestos Placed**

## **Before The Country By His Excellency The President.**

In a nutshell, the regional development initiatives are designed essentially to ensure that development will spread to every single household in the country. The President does not believe that the increase in GDP alone means development to people. It involves many aspects and the benefits must move to every household, it is only then that economic growth can be described as development. Therefore, it is in that context that these regional development initiatives have been selected as special intervention programmes to support much more balanced development activities in the country.

**The private sector is lagging, where personal enrichment is considered greater than national interest, however encouragement of private sector has been outlined?**

When you come to think about it, the Sri Lankan economy is predominantly a private sector economy. If you take our agriculture it is entirely in the hands of the private sector, if you take our industries the public sector does not have any industries anymore. If you take the transport, quite a large percentage of transportation - goods transportation - is in the hands of the private sector. In case of passenger transportation apart from the thirty to forty percent provided by CTB, everything is private. Banking is a 50-50 arrangement and insurance except Sri Lanka Insurance and the National Insurance Trust Fund which is about 40 percent of the market, the rest is in the hands of the private sector. This tourism is entirely in the hands of the private sector. Even now there is a private sector presence in Education and Health. Then many areas such as advertising, marketing, printing, packaging and beauty care industry, all are from the private sector. Therefore, I do not know why the private sector emphasis is necessary over and above what the economy has already created. Of course few strategic enterprises are owned by the Government. All over the world strategic enterprises either remain in the Government or are being regulated by the Government. Private - Public partnership has been encouraged. The Colombo Port is a classic example where critical infrastructure is done by the Government enabling the private sector to invest in commercial activities though there is criticism now in certain areas that the Government is only doing the critical infrastructure and the commercial part is given to the private sector, but the private sector is given enough encouragement.

The 2011 Budget is a landmark in terms of taxation reforms, which are essential to create an enabling environment for the private sector. The vision of the Government is that people do not need to look at Hong Kong or Singapore, but to simply look at Sri Lanka, we have more or less wider incentive structures than those countries. The taxation system is geared towards that. Infrastructure is being provided, the environment is much more attractive than anywhere else and the economic opportunities are more diverse. The private sector is also encouraged by low interest rates, and stable exchange rate arrangement. The private sector is provided with opportunities with a more liberal trade regime in the country. India, Pakistan and Sri Lanka are very much with the free trade world. With SAARC and ASEAN Sri Lanka is in a liberal trade framework. The foreign investment and the private investment is encouraged by providing various incentives and opportunities for them to undertake investment. Foreign exchange regime is designed to facilitate the free flow of money. Essentially, in my view, the private sector is being promoted under this development strategy.

In Sri Lanka, within the private sector, quite a large number are small holders, individuals and SMEs. Therefore the private sector is individual in a way. The self-employment sector is a part of the private sector. The private sector - public sector operations should not be unduly overplayed in my view, both should co-exist.

The private sector needs a government. After all, every country has a government that should recognise the private sector. Why? Because certain things can be provided by the private sector on its own.

**In policy framework, sports, e-commerce and art have also been identified. How will these contribute to the economy?**

The Mahinda Chintana is a holistic approach to development. This is how I would describe it, because it not only speaks on economic growth and investment, but also about art, culture, music, value systems, the community, family - all these aspects of a modern society. That is why the programmes like Mathata Thitha, the anti-drug campaigns are aggressively being pursued.

Then speaking of a sports economy, the international stadium facilities are being developed outside Colombo; in Dambulla, Pallekele, Ridigama, Sooriyawewa and Duraiappa Stadium in Jaffna. All these are facilities to satisfy the needs of the

diversified community in our country since the development involves not only the physical infrastructure and the conventional economic sectors but also art, religion, culture and sports. They are all part of economic development and high value creation activities.

Tourism is very much linked to art, culture, religion, festivals and various events, and need not only be limited to beaches, wildlife and adventures. Tourism also involves people enjoying Sri Lanka's ancient cities and temples. They are being recognized in the Government's development strategy.

The Budget also stipulates that the overall budget deficit will be maintained below 5 Percent?

That is a major responsibility that the Government has to manage. First the legacy, Sri Lanka has been having high budget deficits under successive Governments since 1977. Even prior to that period budget deficit was still a central concern. I can remember Dr N M Perera speaking on the Budget emphasized the need to contain deficits in the 1970s. He was speaking of a revenue account, deficit that will not exceed the capital expenditure. There too he did not want to have a deficit financed from the banking system.

**In A Nutshell, The Regional Development Initiatives Are Designed Essentially To Ensure That Development Will Spread To Every Single Household In The Country. The President Does Not Believe That The Increase In GDP Alone Means Development To People.**

I can remember that the deficit went up to twenty five percent of GDP in this country immediately after the economy was opened. Then during the 87- 88, deficit moved in the range of fifteen percent of GDP despite many measures taken to control it. We had a deficit of around nine to twelve percent of GDP till 2005. So this country has a legacy of high deficit. As a result Sri Lanka had high debt as each year's deficit is added to the debt. It was hundred and five percent of GDP in 2003. So this is not new phenomena, or something newly created. There are reasons for deficits of recent years. The country was fighting against terrorists for 26 years. Revenue was not growing enough. There was not enough infrastructure to generate wealth in the country and so on. The present Government managed to address most of these problems successfully. One is the ending of the costly war. It was taking away a very valuable part of budgetary resources. That is why His

Excellency the President gave it a priority, because on the one hand the country's economy was at a risk and on the other hand the country was at the verge of a division. Second deficits were created because we did not have proper infrastructure. The economy was not capable of generating revenues. Now investments have been made in those areas particularly in ports, roads and electricity which have contributed to economic growth. As a result pressure on the budget is easing. Everybody was trying to compress expenditure, freeze recruitment, stop subsidies and cut development expenditure to manage deficits in those days. That is why Government investment levels were very low in those days. Recruitment to the public service was very low, the service could not be provided. Subsidies were totally eliminated, there were very few subsidies and there were no poverty reduction programmes. Those programmes were compressed and everybody thought a lower deficit could be achieved by cutting expenditure. The President thought the opposite. He thought certain expenditure should be protected and its productivity must be raised. Certain expenditure must increase like investment in public infrastructure. Every country has invested heavily on infrastructure to create income-generating activities.

The third aspect is the revenue. The Government revenue has been narrowly focused. Investments were promoted only by giving tax holidays. The whole country was eventually turned into a tax holiday with only a little revenue being generated. So the President decided that this is not the way to move forward. He thought taxes must be reduced to encourage people to invest, save and engage in economic activities. This may not happen overnight but when people gain confidence lower taxes always increase compliance.

While addressing these concerns the budget deficit has also been targeted at 6.9 percent of GDP compared to 8 percent in 2010. The deficit is to be brought down below 5 percent gradually, on a sustainable basis in the next three years. The Government is also targeting to bring down the total public debt in relation to GDP below 70 percent.

Values in society have been given priority such as a caring society where the children, differently abled and the elderly are looked after. Now the development policy of the government has ensured that while Sri Lanka develops rapidly, we will become a value centric society. Is that possible?

It is possible, because, we are a value centric society. If you go to rural Sri Lanka,



their lifestyle is still based on that. Their social behavioural conditions are value centric. If you look at Sinhala-Tamil New Year, Christmas, our way of thanksgiving at harvesting times or our amazing capacity to get-together at disasters, one can clearly understand our value centric society and its strength.

Overplaying the market economy may have probably tarnished the value centric lifestyles in this country. The violence that took place in this country through the 26 year conflict, the various civil riots and the two insurrections in 71 and 87-88 may have affected us. But, since 2005 our society has been increasingly moving in that direction as the President himself is emphasizing family values in our society.

### **Increase in prices during the festive season?**

The price increase in the festive season is seasonal. But, compared to the previous seasons, the price increases here were less. Take important prices like rice, and essential items, they were not subject to price pressure this time. But there were three key items: chicken and eggs, coconut and the onion. All these are related to the recent phenomena that we have gone through with the weather, bird flu and the structural problems in the coconut industry. In fact, in the Financial Times, I saw the 'Food for Thought' column, which is actually what everybody must think of. Agriculture is the future of the world. It has nothing to do with price increase. This is something that the country must think more seriously from the food security point of view.

The Mahinda Chinthana Development Strategy speaks of food security and energy security. Unless we address related structural issues particularly in agriculture, the nation will be subjected to severe instability, in terms of nutritional problem, food security, economic instability, and welfare. This government has got its priorities towards promoting food production. We have taken far reaching measures regarding rice and several other crops.

Sri Lanka's agriculture must target beyond self sufficiency. The entire policy must work towards producing more than 14 months of rice requirement as far as paddy is concerned. For certain other essential items we must have excess production. Coconut being a critical vegetable in this country, priority must be given towards accelerated production.

2011 Is A Beginning Of A Peace Decade That Support A Development And A

Prosperous Decade. That Decade Will Make The Mahinda Chinthana The Emerging Wonder Of Sri Lanka A Reality.

New plantations take time, new seeds must be found and new research must be undertaken to drive agriculture. Onions are not available even in India as recent floods have resulted in supply variations. But the message from these climatic changes plus various natural disturbances is that you have to produce more than what you need and maintain proper stocks and inventories in the country at all times. There is a cost, but it is a justifiable cost rather than leaving people in hunger. That is the direction the country has to go and I think the Food for Thought message column of Financial Times is admirable.

### **What can the people of Sri Lanka expect in 2011?**

In 2011 Sri Lankan people can expect more opportunities than before, more economic opportunities. The Sri Lankan economy will reflect much stronger growth in all sectors in 2011 than in 2009. The income is bound to rise in agriculture, livestock and fisheries sectors in 2011 which is also a year in which many of the infrastructure facilities that the Government has started in the last five years will be commissioned for public use. There will be better roads and almost everyone will have electricity. 2011 will also be a year during which the SME sector will be revived drastically. The Asian economies will be better than it was in 2009 and 2010 which will support our export activities. In terms of income and employment, and also more importantly for the society, benefits of lower taxation will be an opportunity for savings and investments that the people will experience in 2011.

**2011 is special because it is the beginning of a new decade, a decade of rapid development for Sri Lanka and Asia. We had peace only for one and a half years which has given us the meaning of security, stability and peace, and how much a country can do when such conditions prevail. Therefore, 2011 is a beginning of a peace decade that support a development and a prosperous decade. That decade will make the Emerging Wonder of Asia a reality.**

We have seen that Finance Ministry officials worked very hard, sometimes more than the private sector as well. How do you encourage them to work, what is their motivation?

Our Ministry works very hard because, of course we have, a charismatic and inspiring Minister. Our Minister is the President. On the very first day in office in 2005 he asked us to do what is right and to do it properly. That was our Minister's message to all of us in the Ministry..

He provides visionary guidance under which we work towards realization of his vision. He admired us. Whenever we go to meet him, we never come back without a meal. We are all motivated. We love him and admire him. He is a caring personality. We were well rewarded. The officers are recognized. So we have a very pleasant working environment at a political level.

At an official level, we have a senior management team and the junior officers, all of them work like a family. We have delegated work but we do review all their work. At difficult times we get together and finish our work. The budget was very difficult. We have to maintain confidentiality, we have to work with the President and we have to do technical work but everything was well managed.

Those are the things that motivate us and we work long hours, but we are quite happy. We did not have any problems with the budget, not a single budget proposal was leaked before the budget. Confidentiality was maintained at all levels. We have our difficulties, but we work through them. We are paid at the same rate as any other public servant. We have the same number of leave as the other officials have. But, nevertheless, we are happy the way our Ministry is being looked after by the government. We face many difficulties working with line ministries, the private sector, lending agencies and foreign governments. Everyone is demanding. But we manage, our people work under tremendous stress but as a institution we can be proud for what we have done.

Our officials have maintained the integrity of the public service. I can say, that all of the Finance Ministry officials are so a part of one team. Except me all are relatively young and can take a long term view.



