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1.0 FISCAL STRATEGY

- The Government's fiscal strategy focus on phasing out fiscal deficits and associated debt, to support the development objectives in the Medium-Term Macro Fiscal Framework which aims on containing the fiscal deficit to 4.0% of GDP and debt to GDP ratio to around 75.5% by 2025. Budget 2021 is a litmus test for the current government as the impact of COVID-19 remains a key challenge in the implementation of the budget while government also encounters the task of converting the contracting economy to a positive, high growth economy. As such, the fiscal strategy is primarily designed to address the much-needed requirement for growth. In budget 2021, revenue tax increases seem to be more concentrated on the direct tax and other taxes such as Special Goods and Service Tax and CESS rather than being widespread similar to previous years. Government is expected to register a revenue deficit of 2.9% of GDP in 2021. Further, Budget deficit is also expected to increase to 8.9% with Debt to GDP ratio estimated to rise to 96.0%.

- The Government plans to generate a total revenue and grants of 11.5% of GDP amounting to LKR 2,029Bn for 2021 with 85% of the revenue expected through taxes, while Taxes on Goods & Services continuing to take the top slot contributing 47.7% of tax revenue and 40.5% of total revenue and grants. Non-tax revenue is forecasted to be 11.2% of the total expected government revenue.

- The total planned expenditure for 2021 is LKR 3,594Bn resulting in 20.4% of GDP, growing from 17.8% of GDP in 2020. Recurrent expenditure is forecasted to be controlled at 70.5% of total expenditure constituting 14.4% of GDP lesser than 2020 figure of 15.3% of GDP. Salaries and interest payments are expected to be the largest components of recurrent expenditure amounting to 35.7% and 33.9% of recurrent expenditure respectively.

- Government plans on spending public investments at 6.1% of GDP amounting to LKR 1,070Bn growing from a low of 2.6% of GDP in 2020.

1.1 Budget Summary for 2021

Summary of the Budget: 2020-2021	2020 Estimate	LKR 'Bn 2021 Budget
Total Revenue & Grants	**1,588**	**2,029**
Total Revenue	**1,580**	**2,019**
Tax Revenue	1,358	1,724
Income Tax	324	371
Taxes on Goods & Services	631	823
Taxes on External Trade	403	530
Non-Tax Revenue	162	227
PC Tax Sharing and Devolved Rev	60	68
Grants	**8**	**10**
Total Expenditure	**2,854**	**3,594**
Recurrent	**2,445**	**2,534**
Salaries & Wages including PCs	846	905
Other Goods & Services incl. PCs	172	188
Interest	866	860
Subsidies & Transfers	561	581
Public Investment	**419**	**1070**
Other	**-10**	**-10**
Under Expenditure	**-**	**13**
Revenue Surplus(+)/Deficit (-)	***-865***	***-515***
Primary Surplus (+)/Deficit(-)	**-400**	**-705**
Budget Surplus (+)/Deficit(-)	**-1,266**	**-1,565**
Total Financing	**1,266**	**1,565**
Total Foreign Financing	***-225***	***99***
Foreign Borrowings - Gross	325	606
Project and Programme Loans	128	342
Foreign Commercial	197	264
Debt Repayments	-550	-507
Total Domestic Financing	***1,491***	***1,466***
Non-Bank Financing	1,106	1,086
Foreign Inv. in T-Bills & T-Bonds	-78	60
Bank borrowings	464	319

Summary of the Budget (2020-2021) (Percentage of GDP)	2020 Estimate	2021 Budget
Revenue and Grants/GDP (%)	**9.9**	**11.5**
Total Revenue/GDP (%)	**9.9**	**11.4**
Tax Revenue/GDP (%)	8.5	9.8
Non Tax Revenue/GDP (%)	1.0	1.3
PC Tax Sharing and Devolved Rev/GDP (%)	0.4	0.4
Grants/GDP (%)	**0.1**	**0.1**
Total Expenditure/GDP (%)	**17.8**	**20.4**
Recurrent Expenditure/GDP (%)	**15.3**	**14.4**
Non Interest/ GDP (%)	9.9	9.5
Interest/ GDP (%)	5.4	4.9
Public Investment/GDP (%)	**2.6**	**6.1**
Revenue Surplus (+)/Deficit (-)/GDP (%)	**-5.4**	**-2.9**
Primary Surplus (+)/Deficit (-)/GDP (%)	**-2.5**	**-4.0**
Budget Surplus (+)/Deficit (-)/GDP (%)	**-7.9**	**-8.9**

1.2 Medium Term Macro Fiscal Framework

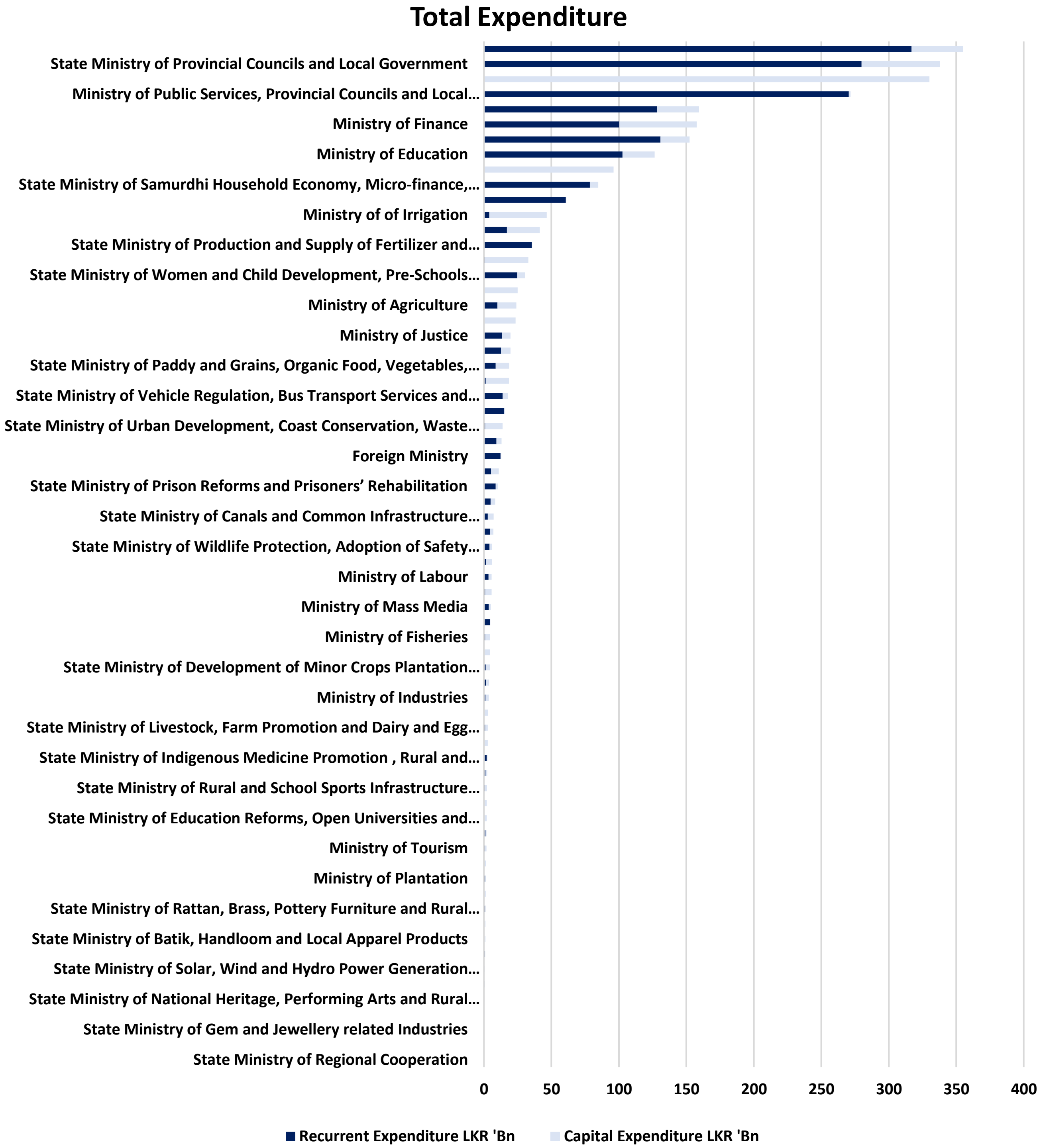
Medium Term Macro Fiscal Framework : 2019-2024 (As a % of GDP)	2019	2020 (Provisional)	2021 (Estimated)	2022	2023 Projections	2024
Total Revenue and Grants	**12.6**	**9.5**	**10.7**	**12.1**	**12.5**	**13.3**
Total Revenue	12.6	9.5	10.6	12	12.5	13.3
Tax Revenue	11.6	8.5	9.4	10.5	10.9	11.6
Income Tax	2.8	1.9	2.1	2.2	2.4	2.6
Taxes on Goods and Services	6.5	4	4.5	5.3	5.5	5.9
Tax on External Trade	2.2	2.5	2.8	2.9	3	3.1
Non Tax Revenue	1	1	1.3	1.5	1.6	1.7
Grants	0.1	0	0.1	0.1	0.05	0.04
Expenditure	**22.2**	**17.5**	**19.5**	**18.4**	**18.0**	**17.9**
Recurrent Expenditure	16.1	14.9	14.2	13.5	12.9	12.5
Salaries and Wages	4.6	5	4.9	4.7	4.4	4.3
Goods and Services	1.2	1	1.1	0.8	0.7	0.7
Interest Payments	6	5.4	4.9	4.9	4.7	4.7
Subsidies and Transfers	4.4	3.5	3.3	3.2	3	2.8
Capital Expenditure and Net Lending	6.1	2.6	5.3	4.9	5.1	5.4
Public Investment	6.2	2.6	5.4	5	5.2	5.5
Current Account Balance	-3.6	-5.4	-3.6	-1.5	-0.4	0.8
Primary Balance	**-3.6**	**-2.5**	**-3.9**	**-1.4**	**-0.7**	**0.0**
Budget Deficit	**-9.6**	**-7.9**	**-8.8**	**-6.4**	**-5.4**	**-4.6**
Deficit Financing	9.6	7.9	8.8	6.4	5.4	4.6
Foreign Financing (Net)	3.6	-1.4	0.5	-0.2	0.1	-0.1
Domestic Financing (Net)	6	9.3	8.3	6.5	5.4	4.8
Government Debt (% of GDP)	**86.8**	**95.1**	**96.3**	**92.4**	**88.1**	**82.3**

1.3 Jan – Aug 2020 Fiscal Outlook

Summary of the Budget (Jan - Aug): Economic Classification			
LKR 'Mn	2019	2020	YoY (%)
Revenue and Grants	**1,206,477**	**908,876**	**-24.7%**
Revenue	1,205,036	906,359	-24.8%
Tax	1,105,402	801,340	-27.5%
Non Tax	99,634	105,020	5.4%
Grants	1,440	2,516	74.7%
Expenditure	**1,927,104**	**1,883,706**	**-2.3%**
Current	1,500,534	1,670,356	11.3%
Salaries	446,451	516,354	15.7%
Interest Payments	599,612	653,498	9.0%
Other	454,471	500,504	10.1%
Public Investments	435,270	227,939	-47.6%
Other	-8,699	-14,590	-67.7%
Revenue Deficit (-)/Surplus (+)	**-295,498**	**-763,997**	**-158.5%**
Overall Deficit (-)/Surplus (+)	**-720,628**	**-974,831**	**-35.3%**
Financing	**720,628**	**974,831**	**35.3%**
Net Foreign Financing	142,349	-92,289	-164.8%
Net Domestic Financing	578,279	1,067,119	84.5%

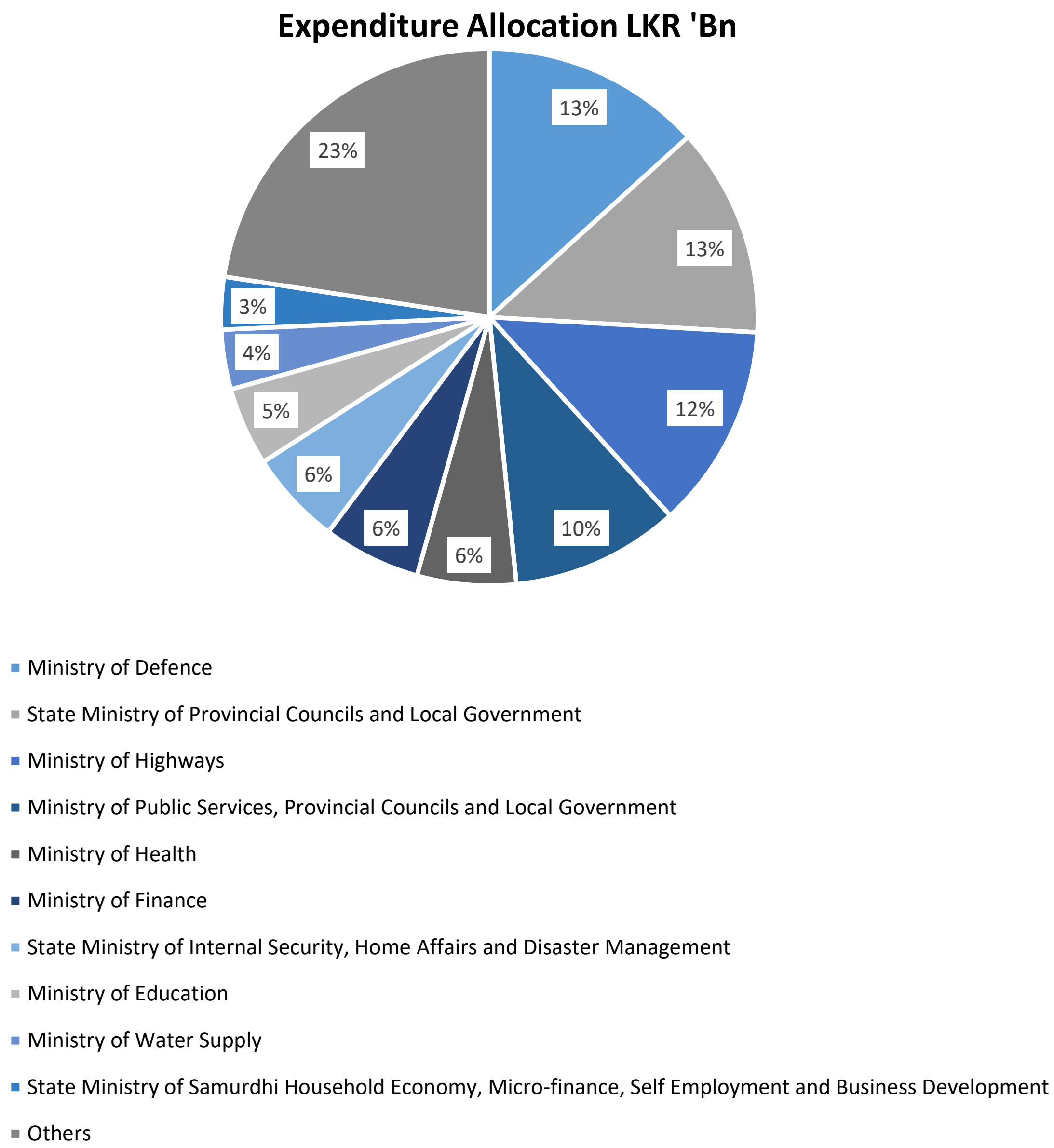
2.0 ANALYSIS ON APPROPRIATION BILL

2.1 Government Expenditure



Recurrent Expenditure LKR 'Bn

Capital Expenditure LKR 'Bn



- With the aim of reviving the economy, the Appropriation Bill for 2021 projected a total Government expenditure for 2021 to be LKR 3.6Tn (20.4% of GDP) as opposed to LKR 2.9Tn for 2020 estimate. The highest allocation of expenditure in the 2021 Budget is for the Ministry of Defence which is LKR 355.2Bn, of which 89% is recurring expenditure (LKR 316.8Bn).

- The bulk of the Budget's total expenditure is allocated for recurrent expenditure, amounting to LKR 1.7Tn (14.4% of the GDP). 34.0% of the recurring expenditure reflects interest payments (LKR 860.0Bn) while 36.0% is allocated for salaries and wages (LKR 905.0Bn).

- Total capital expenditure stands at LKR 963Bn while the highest capital expenditure allocation is for Ministry of Highways, which is allocated LKR 330.0Bn of capex, which represents 99.9% of its total allocated expenditure. Finance ministry has been allocated a sum of LKR 157.6Bn while Ministry of Provincial Councils and Local Government was allocated LKR 338.1Bn of which bulk of the expenditure still reflects recurring expenditure.

2.2 Government Revenue Changes for 2021

- Special Goods and Service Tax in place of the various goods and service taxes and levies, on Alcohol, Cigarettes, Telecommunication, Betting and Gaming and Vehicles.
- Mandatory for all Companies to file their taxes only on an "E-Filing" system with effect from 01 April 2021, and the use of the Tax Identification Number (TIN) in all tax and tax related transactions.
- Simplify the Taxes on Capital Gains, where such taxes will be calculated based on the sale price of a property or the assessed value of a property whichever is higher.
- Businesses and factories with more than 50 employees, to contribute 0.25% of the turnover to the proposed insurance fund. It is intended to use this insurance scheme for retail and wholesale shops with more than 5 employees and hotels.
- To impose CESS to provide the required protection on the imports and exports of domestic production.
- All entrepreneurs to utilize the funds hidden locally or internationally in order to evade laws relating to taxes and foreign exchange. It is expected to make legal provisions to provide a tax pardon to entrepreneurs thus utilizing funds for any investment facilitated by this budget under the payment of taxes amounting to 1%.

3.0 BUDGET & THE CAPITAL MARKET

3.1 Capital Market – Bills, Bonds, Corporate Debt, Equity

- *Samurdhi Bank to credit the Samurdhi benefit to a newly opened Samurdhi Life Savings Account. Mandatory to invest these savings in Government Securities similar to the laws governing the NSB & EPF.*

- *Treatment of medical insurance, interest on housing loans, investments in Government Securities and shares of listed companies incurred up to LKR 100,000 per month as deductible expenditures in the calculation of personal income tax.*

- *Sri Lanka Real Estate Investment Trust (SLREIT) regulated by the SEC investments are exempted from capital gains tax, dividends are exempted from income tax, and stamp duty reduced to 0.75%.*

- *50% tax concession for the years 2021/22 for such companies that are listed before 31 December 2021 and to maintain a corporate tax rate of 14% for the subsequent 3 years.*

- *Tax Exemption on dividends of foreign companies for 3 years if such dividends are reinvested on expansion of their businesses or in the money or stock market or in Sri Lanka International Sovereign Bonds.*

3.2 Budget 2021 & Listed Securities

Budgetary Move	Counters Affected	Impact
Single Special Goods and Service Tax (GST) in place of the various goods and service taxes and levies, imposed under multiple laws and institutions on alcohol, cigarettes, Telecommunication, betting and gaming and vehicles, which accounts for 50% of the income from taxes and levies.	LION, BREW, DIST, MELS,CTC, DIAL, SLTL and Automobile Sector	Depends on the new tax rate, if no change no impact
Farming, including Agriculture, Fisheries and Livestock Farming will be exempted from taxes in the next 5 years.	Poultry Sector, Plantation Sector, CIC, HAYL	Tax exemptions to boost profitability
Exemptions from income tax on interest or discount paid or allowed to any person on Sovereign Bonds denominated in foreign currency, with effect from April 1, 2018.	Banking Sector	Potential tax benefits
If Commercial banks in Sri Lanka purchase Sri Lanka International Sovereign Bonds subject to a minimum of USD 100 million, the risk weighted provisioning under Central Bank Regulations are suspended for 3 years and profits on capital and interest income of this investments are exempted from taxes.	Banking Sector	Potential tax exemption on capital and interest income
Non-residents could purchase super luxury condominiums utilising, foreign currency earnings made in Sri Lanka, earnings in foreign countries or a loan obtained from a Bank outside Sri Lanka.	OSEA, JKH, AEL, ACAP	Higher demand for condominiums
Expansion of maternity and child clinics, dispensaries and adult service centers, laboratory services, hospitals and research institutes.	Healthcare Sector Construction and Building Material Sector	Private hospitals may face competition that may lead to reduced revenues Increase number of construction projects
New insurance scheme to support those who temporarily loose livelihoods due to the quarantine process related to epidemics including COVID.	Insurance Sector	Increase in revenue of insurance companies
Proposal to get businesses and factories with more than 50 employees, to contribute 0.25% of the turnover to the proposed insurance fund.	All listed entities	Negative impact on profitability
Proposal to extend the concessions and recovery of loans granted under the re-financing facilities of CBSL for tourism sector until September 30, 2021. Banks will be provided with a Treasury guarantee covering 50% of such loans.	Banking Sector Tourism Sector	Debt moratoriums may reduce stress on businesses, but causes a bane for banks as the increase in number of restructuring/ rescheduling facilities due to credit relief schemes increases credit risk. This will benefit the tourism sector
Proposal to pay LKR 2 per dollar above the normal exchange rate for foreign exchange remittances sent by foreign workers to banks in Sri Lanka.	Banking sector	More foreign exchange and related fee for banks
A guaranteed price for farmers to cultivate Rice, Maize, Kurrakkan, Sesame and black gram.	Poultry and Dairy sector TAFL, GRAN, CIC, WATA	A guaranteed price will result in increased cost for maize buying sectors such as Poultry and Dairy
Proposal to allow the deprecation in 2 years of the capital investments done on latest technology to collect local liquid milk in collaboration with local dairy farmers, enhancements to milk related productions and promotion of liquid milk. It was also proposed to provide strategic investment tax concessions for a period of 5 years for capital investments of over USD 25Mn with the view of facilitating these companies to process milk powder exports instead of importing milk powder.	WATA, LMF, LLMP	Increased investment leading to increased production thus improving profitability
Proposal to allocate LKR 200Mn for the development of Fisheries Farm Zones with infrastructure facilities in line with the environmental standards in the Districts of Batticaloa, Jaffna, Puttlam and Mannar which are suitable for fish production such as prawns, lobster, carp, tilapia and modha. It was also proposed to further increase the provisions for developing facilities of fishery habours and modern fishing vessels and for increasing deep sea fishery production during 2021 Medium Term Budgetary Framework.	TESS	Increased investment leading to increased production thus improving profitability

Budgetary Move	Counters Affected	Impact
Plans to increase the production capacity of the Lanka Sugar Company by 70,000MT, to modernize sugar production factories and to modify the distilleries to enhance Ethanol and related products.	DIST, MELS	Supply chain limitations will be eliminated while also resulting in reduced cost of procurement
Proposal to increase the daily wage of plantation workers to LKR 1,000 from January 2021.	Plantation Sector	Increased wage cost resulting in decline in profitability
Under the expansion of expressway network, the construction of Kerawalapitiya-Meerigama as well as Kurunegala-Dambulla and Pothuhera-Galagedara sections of the Central Expressway and the construction of Ingiriya- Kahathuduwa section being the first phase of Ruwanpura Expressway are expected to be completed by 2024.	Construction and Building Material Sector	Increase construction projects and material volume
Allocated public Investments to develop bridges and by roads to ease the traffic congestion in Colombo and its suburbs and implementation of the 3 year Road Development Programme which covers all 25 districts.	Construction and Building Material Sector	Increase construction projects and material volume
Proposal to increase renewable energy capacity to 1,000MW by the expeditious implementation of both off shore wind and floating solar power plants exceeding 100MW, with incentives provided by the Board of Investment. Propose to allow a tax holiday of 7 years for all renewable energy projects.	Companies into Renewable energy such as VLL, PAP, HPWR, VPEL, LPL	Potential to increase the power generation through renewable energy sources
Under the "Water for All" national plan, it is planned to invest LKR 1.0Tn (LKR 1,000Bn) in 2021-2024 in 1,000 community water projects, 171 major projects aimed at enhancing the production capacity, new water supply schemes and expedite on going projects with the objective of ensuring access to drinking water to the entire population.	CIND	More demand for pipes and Fittings
Proposal to allow the import of high technology and equipment of developed countries as well as unique raw materials and intermediate products that cannot be manufactured in the country which could result in development of high value addition exports.	All manufacturing companies which exports goods	Increased investment resulting in high volumes
Formulating bilateral trade agreements that will expand the market for exports of our country's specific agricultural products such as tea, cinnamon, pepper, traditional ornaments and consumer goods, as well as toxic free vegetables, grains and fruits.	Tea, cinnamon, pepper plantation companies	Increased demand for the mentioned crops
Limiting importation of agricultural commodities except the items that cannot be produced domestically (negative List).	Agricultural and plantation related companies counters	Increased demand for locally produced crops
Impose the Special commodity levy to balance the supply and demand of domestic production for selected agricultural products	Agricultural and plantation related counters	Increased demand for locally produced crops
Impose CESS to provide the required protection on the imports and exports of domestic production	Domestic manufacturing companies	Increased demand for locally produced products
Remove import taxes on the raw materials not available in the country, machineries and equipment with modern technology, to boost exports, and also to encourage domestic industries to produce value added goods	Domestic manufacturing companies	Increased production of domestic industries
In order to encourage the exports of multi-national companies which are import based for requirements of the domestic market, it is proposed to reduce the tax imposed on their dividends by 25% in 2021 and 50% in 2023 under the condition that they increase their exports by 30% and 50% in the respective years	NEST, LLUB, BOGA	Increased volumes of production resulting in increased profitability

Budgetary Move	Counters Affected	Impact
Provide investment incentives for rubber and coconut related industries, building materials and office equipment and furniture as major industries. Proposed to provide incentives for investments on household needs as well as coconut related industries including brooms, ekel brooms, rugs and rubber related products including agricultural and consumer needs, building materials, office furniture, to support them as main industries.	BPPL, HAYC, HEXP, REXP, DIPD	Increased industry prospects
Proposed to reduce the import taxes levied on vehicle spare parts required for new production sectors to incentivize entrepreneurs in automobile industries engaged in vehicle repairing and vehicle assembly. Further, it is proposed to develop railway compartment production as a domestic industry.	Automobile Sector	Incentivising local automobile dealers to engage in vehicle repairing and vehicle assembly
Certain raw materials such as cement, premix, iron rods, bitumen that cannot be produced domestically will be imported in bulk without import duties, to be used to for the construction of mega housing schemes, highways and also to ensure the smooth and continuous availability of such materials for small and medium construction activities at a competitive price.	Construction and Engineering	Lower imported raw material costs as a result of removal of import duties
TIEP scheme will be implemented to export high quality goods through high value addition to local inputs by providing temporary import facilities for raw materials which are not available in Sri Lanka, spare parts, processing and packing materials, labels, stickers, catalogues and brochures to promote the products of direct and indirect exporters.	CARE, ACME, CPRT, PARA, KZOO	TIEP scheme will permit businesses to obtain relief from customs duties and import VAT on goods that are imported to be used as inputs to manufacture/process/assemble produce for export purposes
Proposal to provide separate docks, dockyard access facilities and long-term credit facilities to promote boat and shipbuilding activities which has high development prospects. It is also proposed to grant a tax break of 7 years for local boat and shipbuilding.	DOCK	Encouraged Investments in boat and shipbuilding activities

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About us:

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