



Sri Lanka Equities

JOHN KEELLS STOCK BROKERS

2008 Budget Proposals

The third budget of the Rajapakse administration was presented on the 7th of November 2007. There were no major increases in subsidies but broad changes were seen in tax holidays for investment projects. Revisions to fuel taxes were also made in order to dampen recent increases in energy prices.

Overall spending will increase by 21% from 2007 and the 2008 deficit has been forecast at 7% of GDP.

Revenue proposals

Government revenue for 2008 is budgeted at Rs.751 billion or 18.0% of GDP compared to the previous year's revenue figure of 17.1%. This year's revenue growth has been forecast at 24.0% as compared to the previous year's growth of 26.6%. Revenue as a percentage of GDP has shown consistent growth over the last few years with the average over the last five years hovering around 15-16%.

Tax revenue is expected to rise by 25% for 2008. Tax revenue has increased by an average of 23.6% over the last four years compared to 2007's increase of 26.4%.

Key revenue measures	Rs.m
Reducing VAT on petrol to 5%	(7,400)
Collection of arrears prior to Mar 07	5,000
Cigarette rate revisions	4,000
Liquor rate revisions	3,200
Excise duty increase on vehicles/consumer durables	3,000
Increase in surcharge on Custom Duty	2,300
Levy on wireless phones	2,200
Administrative changes- Custom Revenue	2,000

Expenditure proposals

Budgeted expenditure for 2008 will increase by 21% with recurrent expenditure increasing by 13% which is lower than the previous year's increase of 15%.

Key expenditure measures	Rs.m
CoL allowance for public servants	6,000
Graduate Employment Scheme	1,850
Distress loans to govt servants	1,500
"Api wennuwen api" Fund	750
Organic fertilizer production and usage	500

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Fiscal effects

The budget deficit for 2008 is estimated at Rs.293 billion up from Rs.257 billion this year. 53% of this will be financed domestically with net foreign borrowings financing 37%.

In Rs. blns	2006	2007 Budget	2007 Revised	2008 Budget
Revenue	477.8	599.8	605.3	750.7
Recurrent Expenditure	548.0	596.2	630.2	712.9
Public Investment	177.4	303.6	233.5	335.7
Total Expenditure	713.6	898.0	862.0	1,044.2
Budget Deficit (as % of GDP)	-8.1	-7.2	-7.2	-7.0

November 2007

Key Proposals

- Tax holidays granted from April 2008 onwards will be restricted to three years. The three years following the tax holiday will have concessionary tax rates. These limitations will not apply to tax holidays on special flagship projects which have been identified to be of National Importance.
- All key development projects will be free from VAT and those paying ESC will be exempt from Withholding tax.
- A 5 year tax holiday (regardless of the above) to be granted to investments in the Eastern Province which exceed Rs.50m and employ over 50 people. Equipment imported for such projects will be exempt from VAT and Customs Duty. Interest income on loans granted for such investments by the banks will be exempt from income tax.
- The 15% VAT on petrol will be reduced to 5% from Jan 2008. In the event oil prices continue to rise the excise duty on petrol will also be removed.
- The 10% tax on mobiles will be extended to CDMA phones. Telecommunications license fees will also be increased.
- Excise duty on motor vehicles and other non essential imports will be increased. The surcharge on Import Duty will be increased to 15%.
- A Free Trade Zone for building material will be opened in the Kelani Valley and Rs.250m has been allocated for this.
- Export income arising from gems imported and thereafter cut and polished, will be exempt from income tax. Credit concessions will also be given to the gem industry.
- Tax concessions will be given to promote the shipping industry. Ships registered under the Sri Lankan flag will be exempt from Customs duties and Port and Airport Development Levy
- Public servants will get a cost-of-living allowance of Rs. 2,500 from January 2008 and to Rs.2,875 from July 2008 in addition to their monthly salary.
- Milk products made out of milk manufactured in Sri Lanka, products made out of rice manufactured in Sri Lanka, locally manufactured sugar, import of yarn for textile industry and locally produced prawns will all be exempt from VAT.
- ESC on the sale of motor vehicles and alcohol will be increased from 0.5% to 1%.
- Any tax losses arising from leasing can only be set off from income arising from the leasing business alone.