The fiscal strategy formulated by the government will result in a budget deficit of 5.8% in 2013.

1. Recovery from the drought
   - Provide the seed paddy requirement for the Maha cultivation free of charge to all farmers of drought affected areas as relief.
   - Banks requested to defer the recovery of agricultural loans from affected areas till the end of the Maha harvest.
   - The interest charged on the respective loans to be written off by the banks all together.
   - Implement a crop insurance scheme for all farmers who are using the fertilizer subsidy from 2013.
   - The necessary legal amendments will be introduced to make it mandatory for banking, finance & insurance institutions to pay a levy of 1% from their annual profits to the National Insurance Trust Fund to facilitate the crop insurance scheme for farmers.
   - Further the farmers who receive the fertilizer subsidy will be required to pay LKR.150.00 per every 50kg of chemical fertilizer issued under the subsidy scheme as the respective farmers will be made policy holders of the compulsory insurance scheme.

2. Pesticides & Fertilizer
   - Encourage Ceylon Fertilizer Corporation to procure organic fertilizer from small & medium scale manufactures of fertilizer who have complied with recognized quality standards at a guaranteed price of LKR.400.00 per 50kg bag.
   - Encourage private sector investment to the organic fertilizer exempt all transactions connected with manufacturing, distribution & marketing of organic fertilizer & pesticides from all direct & indirect taxes.

3. Renewable Energy
   - Exemption from taxes imposed on imported solar power systems & other similar renewable energy equipment at the point of import.
   - Reduction of income tax to 12% on such projects.
   - Grant a lump sum depreciation on capital assets used to generate renewable energy for industries, provided at least 30% of the related energy requirement is generated through renewable sources.

4. Self Sufficiency in Agriculture
   - Raise the guaranteed price for paddy from LKR.28.00 - LKR.30.00 per 1Kg to LKR.32.00-LKR.35.00 per 1Kg from next maha cultivation season.
   - A guaranteed amount of LKR.40.00 per 1Kg for organic fertilizer used paddy.

5. Promoting high value added agriculture
   - Strictly enforce the decision not to permit the filling of abandoned paddy lands
   - Allocation of abandoned paddy lands among those who are willing to cultivate short term fruits, vegetables & floriculture on lease arrangements with the government.
   - This will be done if the owners of the abandoned paddy land do not put them to productive agricultural use before 30th June 2013.

6. Marketing Network
   - A capital contribution of LKR.500Mn will be made to expand the Lak Sathosa retail network up to 1000 outlets over the next 3 years.
   - The corporative system will be encouraged to expand their Coop City market network.

7. Sugar Industry
   - Import taxes on sugar will be maintained
8. Dairy & Livestock Industry
   - Maintain high taxes on imported milk powder
   - Guarantee a farm gate price of LKR.50.00 per liter of fresh milk
   - The expansion of the factory capacity of the factories of National Milk Board & MILCO located in Digana, Polonnaruwa & Ambewela at a cost of USD.40Mn.
   - Reduction of taxes on poultry industry to 10%.

9. Fisheries & Aquatic Resources
   - The development of 4 fisheries harbors & the rehabilitation of a further 5 fisheries harbors for which a provision of LKR.2,000Mn will be provided.
   - Maintain high taxes on imported canned fish & lower the tax on required raw material to encourage the local fish canning industry.

10. Plantation Economy
    **Tea**
    - Increase the replanting subsidy from LKR.300,000 to LKR.350,000 per hectare from 2013.
    - Increase the subsidy to LKR.250,000 per hectare for new plantations.
    - The lands identified as under-utilized by plantation companies through a 2012 budget proposal to be distributed on a 30 year lease basis among 12500 entrepreneurial youth of low income families.
    - Mechanical instruments for tea plucking will be popularized among tea smallholders.
    - Lease terms of plantation companies to be extended & long term funding arrangements to be facilitated for companies which have performed well in terms of best practices in plantation, value addition & welfare of workers, while imposing new conditions on lesser performing companies.
    - Reduction of income tax to 12% for organic tea exports.
    **Rubber**
    - Accelerate rubber cultivation in Moneragala, Ampara, Vavuniya & Mullativue districts
    **Coconut**
    - Replacement of all draught affected coconut trees free of charge by the government.

11. Small Enterprise Economy
    - Exemption of small businesses from NBT & Value Added Tax (VAT).
    - Annual turnover for taxation to be raised to LKR.500Mn.
    - Maintain tax differential between outputs & inputs at the point of customs.

12. Export Industry
    - Two year depreciation allowance for apparel & other manufacturing industries.
    - Reduction of the port & airport levy from 5% to 2.5% on the daily used consumable items

13. Local Authorities
    - Amend relevant legislation to enable municipal councils that have a budget surplus to issue medium term municipal bonds upto a maximum of LKR.500Mn.

14. Provincial Councils
    - Motor vehicle revenue license fee to be increased with effect from January 2013.

15. Sports Economy
    - Exempt hotel expenses of sportsmen, trainers & sponsors from VAT to attract international sports events to Sri Lanka.
    - Exemption of go-carts & specially designed racing vehicles from the applicability of the special excise provision act.
16. Tourism Industry
- A 25% discount on the lease rental determined by the Government chief valuer for the entire term
- Concessions for land leasing for an equity partnership of at least 30% formed with a foreign investor
- Sale of state land to foreign nationals to be prohibited
- Lease of state land to foreign nationals will be permitted subject to a payment of 100% tax on the lease value for the entire lease period
- Permit up to 40% of production of exporters that are capable of replacing imports to sell such goods in the domestic market (subject to VAT & NBT).
- Allow the sale of locally made high value products such as artwork, handlooms & garments in foreign currency

17. The construction industry
- The cost of imported machinery and equipment to be brought down through the reduction of the prevailing tax at the point of imports.
- Additional guarantees will be provided by the construction guaranty fund for small construction companies to increase finance sources.
- Permits to all well established local road construction companies to import bitumen.
- A part of the Northern expressway construction to be awarded to local construction companies.
- To promote local construction materials manufactured locally, adequate tariff gap maintained between imported finish goods & associated raw materials.
- Direct involvement of local contractors required with regard to foreign investment in the local construction industry.

18. Health care industry
- LKR.125 bn has been allocated for the health care services.
- Further funds have been allocated to increase the capacity of the pharmaceutical manufacturing corporation.
- Required investment incentives & procurement contracts with the state pharmaceutical corporation will be arranged to encourage domestic pharmaceutical manufacturing companies to expand their capacity & to maintain high quality drugs.
- Propriety will be given to conserve traditional indigenous medicine in the next 3 years.
- LKR.300 mn allocated for this purpose.
- Strict quality enforcement measures will be taken at the point of the customs to prevent inferior pharmaceuticals & ayurvedic products entering the domestic market.

19. Differently abled people
- Guidelines will be issued for Easy access to ATM machines to disabled people.
- It will be Mandatory that all public places should ensure priority access to such people.

20. Education industry
- LKR.306 bn will be allocated for education (4.1% of the national income)
- LKR.900 mn will be allocated for the provincial teacher training program & LKR.1600 mn to setup 20 technical colleges.
- National school of business management will commission its new complex at Homagama as Asia first green University at a cost of LKR.7.2 bn.
- A supplementary allocation of LKR.4 bn will be allocated for university education, bulk of this will be used to be on account of salaries of university staff.
- LKR.500 mn will be allocated to expand the Naval Academy in Trincomalee.

21. Research & Technology development
- Further LKR.250mn will be allocated to the National Research Council to strengthen research interest among scientists.
- Triple deduction will be granted for research expenditure and a lump sum depreciation for capital expenditure on equipment granted to encourage private sector engagement in research & innovation.
22. Knowledge Services industry
   - IT & enabling services industry professionals’ maximum income tax rate will be limited at 16%.
   - Telecommunication levy applicable on internet tariff reduced to 10% from 20%.
   - LKR.300 mn will be allocated for promotion & training to improve the quality on the industry.
   - LKR.750 mn will be allocated to set up “Nenasala” centers in every Grama Niladari division.

23. Foreign Employment & welfare
   - Housing loans facilities will be given through Samurdhi banks with a guarantee from foreign employment bureau to those who are returning from foreign employment.
   - Lending scheme will also provided through Samurdhi & Regional development banks up to LKR.250,000 at 10% interest rate.
   - Two technical colleges will be set up to enhance skill skills at a cost of LKR.3.00 mn.

24. Capital market Developments
   - 3 year, half tax holiday for new companies that will list in CSE before December 2013 and maintain a minimum of 20% of its share with the public.
   - With holding Tax (WHT) exempt on interest income earned from investing in bonds & debentures listed in the CSE
   - Small time investors & Sri Lankans working overseas will be allowed to directly invest in foreign currencies in unit trusts without having to channel through Securities Investment Account (SIA).
   - Unit trust & trust Management companies’ tax will be reduced to 10% from 28%.
   - Stamp duty exempt on shares transferred to margin trading account.
   - Presidential task force to implement the capital market development master plan by mobilizing all stakeholders involved in the capital market.
   - Stock brokers will be permitted to claim a lump sum depreciation for IT expenditure, Branch Networking & such other capital items.
   - Re-insurance premium charged by the National Insurance Trust fund to be increased to 30% from 20% and transfer the entire amount to set up a separate re-insurance fund to meet re-insurance requirement of Sri Lanka’s insurance industry.

25. Foreign exchange management
   - Corporate entities will be permitted to borrow up to USD 10 mn per annum over the next 3 years without obtaining exchange control department approval.
   - LCB’s permitted to borrow up to USD 50 Mn per annum over the next 3 years without obtaining exchange control department approval.
   - All suppliers of goods and services to tourism & foreign business will be allowed to accept foreign currency provided such earnings will be deposited within 7 working days.
   - Said people also allowed to maintain foreign exchange earners’ accounts.
   - Enable those who were affected by the armed conflict particularly those who live abroad to take a long term view in Sri Lanka by raising the prescribed limit for tax exemption from tax and exchange control to LKR.300Mn.
   - Permit the transfer of foreign savings of resident Sri Lankas as well as expatriates to investments in instruments up to USD.5Mn without the approval from the Exchange Control Department
   - A three year tax holiday for such investments
   - The duration to be classified as nonresident will be brought down from 365 days to 180 days.

26. Development finance
   - DFCC & NDB bank will be allowed to raise long term foreign development finance up to USD250mn each over 10 years to provide long term funding for SME’s, Plantations, the construction industry and other manufacturing industries.
   - The government will underwrite the exchange risk of such borrowings. Further income tax will be exempt from interest income on such borrowings.
   - Government will also facilitate such borrowings by floating domestic bonds, enabling these institutions to invest excess funds until the loan proceeds are fully utilized.

27. The tax system
The businesses having an annual turnover less than LKR.12 mn are exempt from Nations Building tax (NBT) & Value Added Tax (VAT) with effect from January 2013.

NBT & VAT will be imposed to supermarkets and large scale trading operations generating a quarterly turnover in excess of LKR.500 mn.

High & small boutiques & shops will not be liable for these taxes.

The concessions will be expanded to tax payers who are maintaining a 10 year minimum tax payment of LKR.250,000 per annum.

Airport tax will be raised by USD.10 & online Visa fee by USD.5 from January 2013.

Import duties of all vehicles imported under concessional schemes will be increased by 10%-20%.

Betting businesses registration fee will increase by LKR.2 mn and gaming activities registration fee will be increase to LKR.100 mn.

Further 5% turnover tax will imposed on gaming business.

Import duty on foreign liquor and sprites will increase by 25%.

28. Retired Public Servants

- Special allowance of LKR.750 per month (those who retired before 2004) & LKR.500.00 (who retired from 2005-06) will be granted. (50% of the increase from January 2013 & rest from July 2013).
- Increase cost of living allowance by LKR.500 per month to all pensioners from January 2013.

29. Labour relations

- LKR.250 mn will be allocated to finance initiatives to raise labour productivity, employment opportunities and welfare schemes, collectively formulated by the national labour council.
- State owned companies are encouraged to have own fund raising strategy.
- A new pay commission to setup to re-examine the overall salary structure of the public sector and formulate a national wage policy.
- Public servants allowances to increase by minimum of LKR.1500 per month from next year (a Cost of Living allowance of LKR.750 per month paid). The balance will be provided by granting a further 5% of the basic salary subject to a minimum of LKR.750 and a maximum of LKR.2500.
- 50% paid from may 2013, balance from September 2013.

Budget 2013 - Capital Market Developments

The 2013 budget proposals will bring in considerable positives for the development of the capital market of Sri Lanka we believe. The equity market as well as the corporate debt market benefit to a great extent through the proactive proposals of the 2013 budget. The following have been proposed:

- 3 year, half tax holiday for new companies that will list in CSE before December 2013 and maintain a minimum of 20% of its share with the public.

The above proposal will have a significant impact on the equity market of the country. The Colombo stock Exchange’s (CSE) market capitalization & liquidity has lagged behind compared to other regional and emerging markets over the years. However with this initiative it is quite clear that the liquidity of the market will be enhanced notably as a 50% tax reduction for a period of three years is a sizable saving for corporates primarily the large scale companies. This will no doubt entice several large companies across most industries to seek a listing in the CSE during 2013, thereby making the CSE a more attractive market for foreign investors as well as local investors as stock diversity provides investors with more options and also helps to mitigate the risks involved in equity investments. Further higher liquidity will also help the CSE to experience less volatility we believe.

- With-holding Tax (WHT) exempt on interest income earned from investing in bonds & debentures listed in the CSE.
The Sri Lankan corporate secondary debt market has been largely inactive over the years. The ending of the armed conflict and the consequential economic environment resulted in the primary debt market to witness robust growth however the corporate secondary debt market remained inactive to a great extent. We believe the above proposal will assist the corporate secondary debt market to become more active & witness considerable growth in the medium term.

- Small time investors & Sri Lankans working overseas will be allowed to directly invest in foreign currencies in unit trusts without having to channel through Securities Investment Account (SIA).
- 10% tax applicable to unit trusts has been extended to unit trust management companies.
- Stamp duty exempt on shares transferred to margin trading account.

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**Total Revenue & Grants**

- 2011: LKR 949.90 bn
- 2012: LKR 1,075.00 bn
- 2013E: LKR 1,277.90 bn

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**Revenue Break down-2013**

- Income Tax: 24%
- Taxes on Goods & Services: 55%
- Taxes on External Trade: 2%
- Grants: 19%

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**Total Expenditure**

- 2011: LKR 1,400.10 bn
- 2012: LKR 1,540.20 bn
- 2013E: LKR 1,785.40 bn

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**Expenditure Breakup-2013**

- Recurrent: 35%
- Salaries & Wages: 13%
- Other Goods & Services: 7%
- Interest: 15%
- Subsidies & Transfers: 2%
- Public Investment: 13%
- Education & Health: 12%
- Infrastructure: 4%

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**Revenue & Expenditure Account 2011-2013**

<table>
<thead>
<tr>
<th></th>
<th>2011</th>
<th>2012</th>
<th>2013 Proposed</th>
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<tbody>
<tr>
<td>Total Revenue &amp; Grants</td>
<td>949.90 bn</td>
<td>1,075.00 bn</td>
<td>1,277.90 bn</td>
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<tr>
<td>Total Expenditure</td>
<td>1,400.10 bn</td>
<td>1,540.20 bn</td>
<td>1,785.40 bn</td>
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<td>Budget Deficit Surplus (+)/Deficit</td>
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<td>(465.20)</td>
<td>(507.40)</td>
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**Revenue & Expenditure as % of GDP**

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<thead>
<tr>
<th></th>
<th>2011</th>
<th>2012</th>
<th>2013P</th>
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<tbody>
<tr>
<td>Revenue &amp; Grants /GDP %</td>
<td>14.5</td>
<td>14.2</td>
<td>14.7</td>
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<tr>
<td>Revenue/GDP %</td>
<td>14.3</td>
<td>14.0</td>
<td>14.5</td>
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<tr>
<td>Tax/GDP %</td>
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<td>12.2</td>
<td>13.0</td>
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<tr>
<td>Expenditure /GDP %</td>
<td>21.4</td>
<td>20.4</td>
<td>20.5</td>
</tr>
<tr>
<td>Current Expenditure/GDP %</td>
<td>15.4</td>
<td>14.7</td>
<td>14.6</td>
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<tr>
<td>Public Investment/GDP %</td>
<td>6.2</td>
<td>5.8</td>
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<tr>
<td>Revenue Surplus (+)/Deficit (-) GDP</td>
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<td>-0.8</td>
<td>-0.1</td>
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<tr>
<td>Budget Surplus (+)/Deficit (-)GDP (%)</td>
<td>-6.9</td>
<td>-6.2</td>
<td>-5.8</td>
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</tbody>
</table>
Budget 2013 - Sector Summary

Travel & Tourism

- Corporate entities will be permitted to borrow up to USD 10 mn per annum over next 3 years without obtaining exchange control department approval.
- All suppliers of goods and services to tourism & foreign business will be allowed to accept foreign currency provided such earnings will be deposited within 7 working days.
- A 25% discount on the lease rental determined by the Government chief valuer for the entire term.
- Concessions for land leasing for an equity partnership of at least 30% formed with a foreign investor.
- Sale of state land to foreign nationals to be prohibited.
- Lease of state land to foreign nationals will be permitted subject to a payment of 100% tax on the lease value for the entire lease period.
- Permit up to 40% of production of exporters that are capable of replacing imports to sell such goods in the domestic market (subject to VAT & NBT).

The 2013 budget proposal regarding foreign borrowings for corporate will benefit the tourism industry considerably in particular as most of the existing hotel operators are either seeking to construct new hotels or renovate the existing property which would need sizable capital investments. Further new investors have been eying this sector as one of the industries that would be in the forefront to witness robust growth in the next couple of years. However with interest rates on the rise, raising debt finance locally will put pressure on the bottom-line of the respective companies, hence we believe the above proposal will help to bring down the cost of funding expansions if the companies can find a foreign source to borrow. However the potential exchange risk will have to be managed well in order to gain the full advantage of this initiative.

Bank Finance & Insurance

- DFCC & NDB bank will be allowed to raise long term foreign development finance up to USD250mn each over 10 years to provide long term funding for SME’s, Plantations, the construction industry and other manufacturing industries.
- The government will underwrite the exchange risk of such borrowings. Further income tax will be exempt from interest income on such borrowings.
- Government will also facilitate such borrowings by floating domestic bonds, enabling these institutions to invest excess funds until the loan proceeds are fully utilized.
- LCB’s permitted to borrow up to USD 50 Mn per annum over the next 3 years without obtaining exchange control department approval.

DFCC (DFCC: LKR.109.00) & NDB (NDB: LKR.138.50) will benefit considerably from the above proposals. The two banks in concern will be at a significant advantage as the proposals will enhance their earnings capability as the interest income will be tax free whilst eliminating a significant portion of risks involved in raising of funds through foreign institutions as the exchange risk will be underwritten by the government.

- The necessary legal amendments will be introduced to make it mandatory for banking, finance & insurance institutions to pay a levy of 1% from their annual profits to the National Insurance Trust Fund to facilitate the crop insurance scheme for farmers.

The above proposal will have a marginal impact on the profitability of banks.
Beverage Food & Tobacco

- Corporate entities will be permitted to borrow up to USD 10 mn per annum over the next 3 years without obtaining exchange control department approval.
- Imposing NBT & VAT to supermarkets and large scale trading operations generating a quarterly turnover in excess of LKR.500 mn.

We believe Cargilles [CARG:LKR145.0], Keells Super (retail arm of Johh Keells Holdings [JKH:LKR.213.50] and Arpico (Richard Peries's [RICH:LKR.8.30] retail chain) will have an adverse impact by this.

- A capital contribution of LKR.500Mn will be made to expand the Lak Sathosa retail network up to 1000 outlets over the next 3 years.

We believe CARG will have negative impact by this proposal specially, Lak Sathosa will be a major competitor out-side the urban areas. Further, CARG’s bargaining power on suppliers could also get affected as Lak Sothosa will also tap the same supplier group.

- 25% imports duty increase on foreign liquor and sprites.

LION Brewery's (LION: LKR.260) future business prospects could have a negative impact as LION has tied up with Diageo to distribute Diageo’s products in Sri Lanka. However, LION also can mitigate this by producing some of Diageo products locally with their License. Further Perciel (subsidiary of Distillers Company of Sri Lanka [DIST: LKR145.0]) could also have slight impact as the company also imports a few foreign liquor brands.

- Reduction of taxes on poultry industry to 10%.

Bairaha Farms (BFL: LKR.155.0) & Three Acre Farms (TAFL: LKR.56.0) can maximize their profitability by this proposal in the future.

- Maintain high taxes on imported milk powder

Lanka Milk Foods (LMF: LKR.92.0) imports Milk powder and distributes the same under ‘Lakpray’ brand. Kotmale (LAMB: LKR.38.60) too could get affected by this proposal. The segment is already highly taxed. This will continue to tighten the respective companies profitability. However, this proposal will encourage Nestle (NEST:LKR) who own 'Nespray' brand to expand their operation as the company produces milk powder locally.

- Reduction of income tax to 12% for organic tea exports.

HVA foods (HVA:LKR.14.20) and Ceylon Tea Services (CTEA: LKR.6.50) could benefit by this proposal.

Chemicals & Pharmaceuticals

- Corporate entities will be permitted to borrow up to USD 10 mn per annum over the next 3 years without obtaining exchange control department approval.
- Required investment incentives & procurement contracts with the state pharmaceutical corporation will be arranged to encourage domestic pharmaceutical manufacturing companies to expand their capacity & to maintain high quality drugs.

This proposal will encourage PC Pharma (PCHH: LKR.10.90) to initiate local production of medicine.

Construction & Engineering

- The cost of imported machinery and equipment to be brought down through the reduction of the prevailing tax at the point of imports.
- Permits to all well established local road construction companies to import bitumen.
- A part of the Northern expressway construction to be awarded to local construction companies.
- DFCC & NDB bank will be allowed to raise long term foreign development finance up to USD250mn each over 10 years to provide long term funding for SME’s, Plantations, the construction industry and other manufacturing industries.
We believe, MTD Walkers (KAPI: LKR 27.50), Access Engineering (AEL: LKR 19.80) and Lankem Development (LCEM: LKR 7.90) will be benefited by the proposals in the future. Further these companies can fund their projects at a lower cost.

### Major Economic Parameters in the Domestic economy 2012-2015

<table>
<thead>
<tr>
<th>Item</th>
<th>Unit</th>
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<th>2012</th>
<th>Revised Estimate</th>
<th>Projections</th>
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<tr>
<td>Economic Growth</td>
<td>%</td>
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<td>6.8</td>
<td>7.5</td>
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<tr>
<td>Inflation (GDP Deflater)</td>
<td>%</td>
<td>7.8</td>
<td>8.2</td>
<td>7</td>
<td>6</td>
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<tr>
<td>Nominal GDP Growth %</td>
<td>%</td>
<td>16.7</td>
<td>15.6</td>
<td>15</td>
<td>14.5</td>
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<tr>
<td>Nominal GDP</td>
<td>Rs. Bn.</td>
<td>6,543</td>
<td>7,561</td>
<td>8,697</td>
<td>9,956</td>
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Source: Treasury Dept; Budget Speech 2013

### Gross Borrowing Requirements -2013

<table>
<thead>
<tr>
<th>Item</th>
<th>Rs. Billion</th>
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</thead>
<tbody>
<tr>
<td>Total Receipts other than government borrow</td>
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<tr>
<td>Total payments including debt repayments</td>
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<td>Provisions for advanced accounts</td>
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<td>Risk provision</td>
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<tr>
<td>Total gross borrowings requiremnt to be recor</td>
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<tr>
<td>of which</td>
<td></td>
</tr>
<tr>
<td>Total debt repayments</td>
<td>747</td>
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</tbody>
</table>

### Information Technology Industry

- LKR 300 mn will be allocated for promotion & training to improve the quality on the industry.
- LKR 750 mn will be allocated to set up “Nenasala” centers in every Grama Niladari division.

We believe, PC House (PCH: LKR 6.00) will be benefited by this proposals. Further it will encourage other companies who are involved in the IT industry (Softlogic [SHL: LKR 10.90], Metropolitan resources Holdings [MPRH: LKR 21.40], Singer [SINS: LKR 105.0] & JKH ) to expand their presence.

### Investment Trusts

- Unit trust & trust Management companies’ tax will be reduced to 10% from 28%.
- With holding Tax (WHT) exempt on interest income earned from investing in bonds & debentures listed in the CSE.

We believe, this proposals will encourage Ceylon Guardian (GUAR: LKR 175.0), Ceylon Investment (CINV: LKR 88.0) & other unit trusts to in crease their presence in debt instruments.

### Manufacturing Industry

- Corporate entities will be permitted to borrow up to USD 10 mn per annum over the next 3 years without obtaining exchange control department approval.
- Two year depreciation allowance for apparel & other export related manufacturing industries.
We believe, Orient Garments (OGL: LKR:15.50), Textured jersey (TJL: LKR:8.70), Hayles Exports (HEXP: LKR:28.60), Richard Peiris Exports (REXP:LKR.33.0) will be benefited by the 2 year depreciation allowance.

- To promote local construction materials manufactured locally, adequate tariff gap maintained between imported finish goods & associated raw materials.

Further, Sirra cables (SIRA: LKR2.7), Kelani Cables (KCAB: LKR:72.70), Tokyo Cement (TKYO: LKR:27.50) will be benefited by this proposal.

- DFCC & NDB bank will be allowed to raise long term foreign development finance up to USD250mn each over 10 years to provide long term funding for SME’s, Plantations, the construction industry and other manufacturing industries.

Overall Manufacturing companies will able to access to the lower cost funding through above proposals.

**Motors industry**

- Corporate entities will be permitted to borrow up to USD 10 mn per annum over the next 3 years without obtaining exchange control department approval.
- The concessions will be expanded to tax payers who are maintaining a 10 year minimum tax payment of LKR.250,000 per annum.
- Import duties of all vehicles imported under concessional schemes will be increased by 10%-20%.
- Motor vehicle revenue license fee to be increased with effect from January 2013.
- Exemption of go-carts & specially designed racing vehicles from the applicability of the special excise provision act.

Vehicle demand will further drop with the proposal to increase import tariffs on vehicle imports under concessional schemes. However, the broadening of concessions to tax payers who maintaining a 10 years minimum tax payment of LKR.250k p.a will somewhat nullify the negative impact of the new import tariff. We believe, the motor sector will continue to experience a challenging period.

**Plantation**

- Corporate entities will be permitted to borrow up to USD 10 mn per annum over the next 3 years without obtaining exchange control department approval.
- Increase the replanting subsidy from LKR.300,000 to LKR.350,000 per hectare from 2013.
- The lands identified as under-utilized by plantation companies through a 2012 budget proposal to be distributed on a 30 year lease basis among 12500 entrepreneurial youth of low income families.
- Increase the subsidy to LKR.250,000 per hectare for new plantations.
- Mechanical instruments for tea plucking will be popularized among tea smallholders.
- Lease terms of plantation companies to be extended & long term funding arrangements to be facilitated for companies which have performed well in terms of best practices in plantation, value addition & welfare of workers, while imposing new conditions on lesser performing companies.
- Reduction of income tax to 12% for organic tea exports.

We anticipate the plantation companies will be benefited by the above proposals. Further we believe, plantation companies will utilize the uncultivated lands to maximize the profitability.

**Telecommunications Industry**

- Corporate entities will be permitted to borrow up to USD 10 mn per annum over the next 3 years without obtaining exchange control department approval.
- Telecommunication levy applicable on internet tariff reduced to 10% from 20%.

We believe, Dialog (DIAL: LKR8.6) & Sri Lanka Telecom (SLTL: LKR.43.0) will be benefited from the proposal through increased volume. Further lower internet cost will push up the internet penetration.
The 2013 budget proposals which was presented to the parliament yesterday contains several proposals that would facilitate long term growth across most of the sectors of the economy with higher weightage given to capital market development, SME sector, reduction of exchange controls on foreign funding for corporate s& foreign currency transactions.

It is our view that the 2013 budget proposals contain proactive measures to enhance the contribution from the financial services sector to the economy. The proposals brought forward to develop the debt & equity market will have considerable positives in the medium to long term we believe. The government in its’ 2013 budget proposals have focused extensively on initiatives that would facilitate solid growth in the country’s equity market which would help to lure more foreign investments to the economy through the CSE & also broad base the equity market among local investors.

The budget deficit is expected to narrow down to 5.8% in 2013 from 2012’s revised budget deficit estimate of 6.2% through the initiatives proposed. However we believe it would be a challenging task for the government to achieve this goal as some of the revenue estimates seem to be a somewhat too optimistic.

The revenue including grants for 2013 is estimated at 14.7% against the GDP whilst the tax revenue is estimated at 13% of GDP. Taxes on goods 7 services will contribute the highest tax revenue (estimated growth of 22% over 2012) whilst taxes on external trade will witness the highest growth of 25% over the 2012 figure.

The government proposes to spend LKR.470Bn on infrastructure development (26% of total expenditure) which will see a climb of 20% over the 2012 budgeted amount. Recurrent expenditure is estimated to increase by 13% over the 2012 figure to LKR.1,267.4Bn in 2013.

Domestic funding will contribute LKR.421.4Bn to finance the budget deficit of LKR.507.4Bn whilst foreign funding will contribute LKR.86Bn.
Revenue & Expenditure Account

<table>
<thead>
<tr>
<th></th>
<th>Rs. Billion</th>
<th></th>
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</thead>
<tbody>
<tr>
<td></td>
<td>2011</td>
<td>2012</td>
<td>2013E</td>
</tr>
<tr>
<td>Total Revenue &amp; Grants</td>
<td>949.9</td>
<td>1075</td>
<td>1277.9</td>
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<tr>
<td>Total revenue</td>
<td>934.8</td>
<td>1055</td>
<td>1257.9</td>
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<tr>
<td>Income Tax</td>
<td>157.3</td>
<td>184.3</td>
<td>221.9</td>
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<tr>
<td>Taxes on Goods &amp; Services</td>
<td>468</td>
<td>515.5</td>
<td>632.9</td>
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<tr>
<td>Taxes on External Trade</td>
<td>187.3</td>
<td>221.1</td>
<td>277.2</td>
</tr>
<tr>
<td>Grants</td>
<td>15.1</td>
<td>20</td>
<td>20</td>
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<tr>
<td><strong>Total Expenditure</strong></td>
<td><strong>1400.1</strong></td>
<td><strong>1540.2</strong></td>
<td><strong>1785.4</strong></td>
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<tr>
<td>Recurrent</td>
<td>1006.6</td>
<td>1113.3</td>
<td>1267.4</td>
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<tr>
<td>Salaries &amp; Wages</td>
<td>319.6</td>
<td>364.4</td>
<td>414.4</td>
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<tr>
<td>Other Goods &amp; Services</td>
<td>113.7</td>
<td>123.3</td>
<td>140.4</td>
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<tr>
<td>Interest</td>
<td>356.7</td>
<td>393.7</td>
<td>444.8</td>
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<tr>
<td>Subsidies &amp; Transfers</td>
<td>216.6</td>
<td>231.9</td>
<td>267.8</td>
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<tr>
<td>Public Investment</td>
<td>407.5</td>
<td>437.3</td>
<td>529.6</td>
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<tr>
<td>Education &amp; Health</td>
<td>37.1</td>
<td>46.4</td>
<td>59.6</td>
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<tr>
<td>Infrastructure</td>
<td>370.4</td>
<td>390.9</td>
<td>470</td>
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<tr>
<td>Other</td>
<td>-14</td>
<td>-10.4</td>
<td>-11.7</td>
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<tr>
<td><strong>Revenue Surplus (+)/Deficit (-)</strong></td>
<td>-71.8</td>
<td>-58.3</td>
<td>-9.4</td>
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<tr>
<td><strong>Budget Deficit Surplus (+)/Deficit</strong></td>
<td><strong>-450.2</strong></td>
<td><strong>-465.2</strong></td>
<td><strong>-507.4</strong></td>
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<tr>
<td><strong>Total Financing</strong></td>
<td><strong>450.2</strong></td>
<td><strong>465.2</strong></td>
<td><strong>507.4</strong></td>
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<tr>
<td>Total Foreign Financing</td>
<td>194</td>
<td>205.6</td>
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<tr>
<td>Net Foreign Borrowings</td>
<td>84.5</td>
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<tr>
<td>Foreign Borrowing-Gross</td>
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<tr>
<td>(-)Debt Repayments</td>
<td>88.4</td>
<td>166</td>
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<tr>
<td>Foreign Commercial</td>
<td>109.5</td>
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<tr>
<td><strong>Total Domestic Financing</strong></td>
<td><strong>256.2</strong></td>
<td><strong>259.6</strong></td>
<td><strong>421.4</strong></td>
</tr>
</tbody>
</table>

Non Bank Borrowings 39.4 84.6 289.4
Foreign Investments in T-bills and Bank Borrowings 25 100 62
Bank Borrowings 191.8 75 70

Source: Treasury dept

Income Tax Regime

<table>
<thead>
<tr>
<th>Description</th>
<th>Tax Rate %</th>
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<tbody>
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<td>Up to Rs. 500,000</td>
<td>Exempted</td>
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<tr>
<td>On the Balance</td>
<td></td>
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<tr>
<td>First Rs. 500,000( of the taxable income)</td>
<td>4.0</td>
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<tr>
<td>Second Rs. 500,000</td>
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<tr>
<td>Third Rs. 500,000</td>
<td>12.0</td>
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<tr>
<td>Fourth Rs. 500,000</td>
<td>16.0</td>
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<td>Fifth Rs. 500,000</td>
<td>20.0</td>
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<tr>
<td>Balance</td>
<td>24.0</td>
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</tbody>
</table>

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