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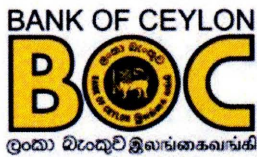
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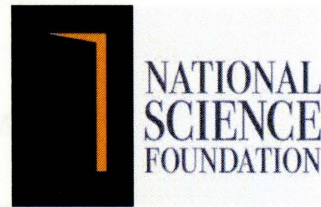
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Government Tax Revenue, Expenditure, and Debt in Sri Lanka: A Vector Autoregressive Model Analysis

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Introduction

Sri Lanka has been unable to constrain the growth of its debt to ensure that sufficient revenues remain available after debt service payments to finance other vital recurrent and development expenditures of the Government. In 1960, Government tax revenue, expenditure and debt were 17%, 27%, and 34% of GDP respectively. In 2015, Government tax, expenditure and debt were 12%, 20% and 76% respectively (Annual Report of Central Bank of Sri Lanka (ARCBSL), 2015). The tax revenue and Government expenditure as a percentage of GDP have decreased by 5% and 7% between 1960 and 2015, but Government debt as a percentage of GDP has increased by 42% during the same period. Between 1950 and 2015, the highest value of tax revenue as a percentage of GDP was 24% (in 1978) while the highest value of Government expenditure was 42.6% as a percentage of GDP in 1980, but the highest value of government debt was 109% of GDP in 1989. When considering the contemporary issues of economics the study should focus the relationship between these macroeconomic variables, tax revenue, Government expenditure, and Government debt.

Review of Literature

Keynesian economists say that Governments can control aggregate demand and the level of national income through spending and tax policies. The current budget balance of the Government is the difference between its spending and revenues. It is given by the following formula.

$$B_t = G_t - T_t \quad (1)$$

Where B_t is the balance at time t , G_t is the level of Government expenditure at time t , and T_t is the tax revenue at time t . Government debt can be expressed by the following equation.

$$D_t = (1 + r)D_{t-1} + B_t \quad (2)$$

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