



IMF Staff Completes Review Mission to Sri Lanka

April 11, 2016

End-of-Mission press releases include statements of IMF staff teams that convey preliminary findings after a visit to a country. The views expressed in this statement are those of the IMF staff and do not necessarily represent the views of the IMF's Executive Board. Based on the preliminary findings of this mission, staff will prepare a report that, subject to management approval, will be presented to the IMF's Executive Board for discussion and decision.

A staff team from the International Monetary Fund (IMF) led by Todd Schneider visited Colombo during March 31- April 11 to hold the 2016 Article IV consultation discussions and to discuss the authorities' request for a Fund supported arrangement. The mission made significant progress toward a staff level agreement with the government on an economic program that could be supported by a 36-month Extended Fund Facility (EFF). Program discussions will continue in Washington D.C. on the margins of the Spring Meetings of the IMF and World Bank, with the objective of concluding a staff-level agreement with the authorities, subject to approval by IMF Management and the Executive Board, in the next two weeks.

At the end of the visit Mr. Schneider made the following statement:

“Macroeconomic performance in 2015 reflected a mix of positive underlying growth momentum, the impact of domestic policies, and an increasingly difficult external environment. The fiscal deficit expanded, public debt increased, and the balance of payments position deteriorated despite an improvement in the terms of trade. Real GDP growth in 2016 is expected to remain around 5 percent and inflation in the low single digits. Over the medium term, there is potential for growth to rise closer to Sri Lanka's estimated potential output level, but prospects will hinge on a policy upgrade in the near term and removing bottlenecks to trade and investment.

“The authorities' proposed economic program aims to achieve high and sustained levels of inclusive economic growth, restore discipline to macroeconomic and financial policies, and rebuild fiscal and reserve buffers. Key objectives underlying the reform agenda include: (i) improving revenue administration and tax policy; (ii) strengthening public financial management; (iii) state enterprise reforms; and, iv) structural reforms to enable a more outward-looking economy, deepen foreign exchange markets, and strengthen financial sector supervision.

“A durable reduction of the fiscal deficit and public debt through a growth-friendly emphasis on revenue generation is the main priority for fiscal policy. In this context, the mission welcomed the cabinet’s decision to reduce the 2016 fiscal deficit to 5.4 percent of GDP, and advised to move quickly on tax and expenditure policy decisions endorsed by the Cabinet. Other near-term steps include a clear strategy to define and address outstanding obligations of state enterprises, start broadening the tax base by reducing tax exemptions, and introduction of a new Inland Revenue Act. The medium-term revenue effort will be based on further reform of tax and expenditure policies, supported by modernizing revenue administration and public financial management (including implementation of key IT systems (RAMIS, ITMIS, and ASYCUDA ++).

“The mission welcomed the recent tightening of monetary policy given the steady increase in core inflation and high private credit growth. Given the long lags in monetary transmission and continued increase in core inflation and private credit growth, however, the Central Bank of Sri Lanka (CBSL) should be prepared to tighten policies further if these trends continue. The mission also recommends the CBSL take active steps to rebuild non-borrowed reserve buffers.

“The financial system appears well capitalized and liquid, but the authorities should nevertheless remain vigilant to the risk of a potential rise in non-performing loans. The mission welcomes steps toward supervision on a consolidated basis and shifting to Basel III and concurs with continued efforts needed to strengthen the legal framework for crisis preparedness and resolution.

“Achieving medium-term growth and reserve objectives and building greater resilience to external shocks will require a renewed effort toward greater integration into regional and global supply chains, higher levels of foreign direct investment, and enhancing prospects for private sector investment. To boost trade and private sector development, the mission recommends addressing protectionism by reviewing tariffs and para-tariffs. The mission welcomes ongoing efforts to enhance competitiveness through other means, including removal of the EU fisheries import ban, and the reinstatement of Generalized System of Preferences Plus status. Further steps are needed to increase the efficiency of trade facilitation (including through full implementation of use of electronic customs documentation), remove barriers to foreign investment entry and establishment, enhance access to finance, and strengthen financial market infrastructure.

“The mission met with Prime Minister Wickremesinghe, Finance Minister Karunanayake, Minister of Development Strategies and International Trade Samarawickrame, Governor of the Central Bank of Sri Lanka Mahendran, other public officials, and representatives of the business community, civil society and international partners.”