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**N** MARKET PULSE WITH NDBS

# Salient Points from Sri Lanka's IMF EFF Report

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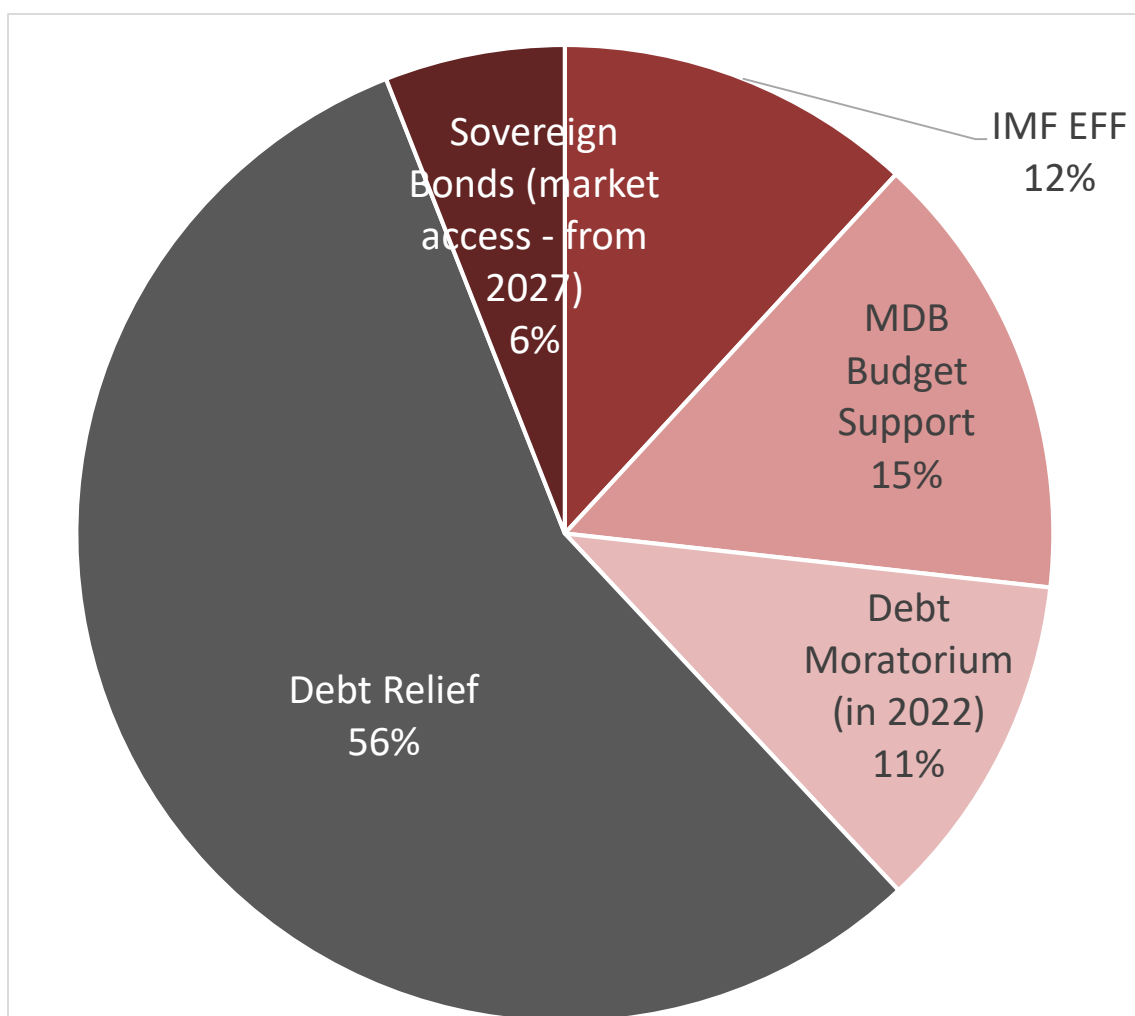
 **NDB**  
Securities

On 20<sup>th</sup> March 2023, the IMF's Board approved Sri Lanka's \$ 3 Bn, 48-month Extended Fund Facility (EFF) Program.



The fund proceeds can be used to finance the budget (~\$ 660 Mn per annum).

During 2022 – 2027, Sri Lanka’s external financing gap of \$ 25.2 Bn will be funded by; IMF EFF 12%, MDBs\* 15% & 56% via debt reliefs.



**USD Mn**

IMF EFF	2,982	12%
MDB Budget Support	3,750	15%
Debt Moratorium (a)	2,834	11%
Debt Relief	14,087	56%
Sovereign Bonds (b)	1,500	6%
<b>Total</b>	<b>25,153</b>	<b>100%</b>

(a) Debt moratorium in 2022

(b) Capital market access by 2027

\* MDBs – Multilateral Development Banks such as ADB and World Bank

Multilateral Development Banks are to provide \$ 3.7 Bn during the program period for budget support.

Of which, World Bank (WB) is to provide \$ 1.7 Bn, and ADB \$ 2.0 Bn.

In 2023, WB will provide \$ 250 Mn, and ADB \$ 650 Mn for budget financing.



The total debt relief during  
the program period will be  
\$ 14 Bn.

# Int. Capital Market Access by 2027

The IMF assumes Sri Lanka will get capital market access by 2027 (towards the end of the program).

In 2027, \$ 1.5 Bn Eurobond issuance is assumed (1.8% of GDP). The IMF expects capital market issuances to grow in line with GDP thereafter.

# Key Debt Sustainability Targets:

1. Public Debt / GDP: Below 95% by 2032
2. GFN/GDP: 13% in 2027-32 (34% in 2022)
3. FCY debt servicing/ GDP: 4.5% in 2027-32





The government to  
announce their plans on  
external debt and domestic  
debt operations **before**  
**end-April 2023.**

# IMF Staff's Illustrative Restructuring Scenario

## DOMESTIC DEBT

**IMF's base case scenario is a relatively mild domestic debt restructuring.**

- **CBSL's Balance Sheet:** T-Bills held by the central bank will be exchanged to long term bonds.
- **Domestic Debt:** A select pool of the remaining domestic debt will be reprofiled to reduce GFN, while limiting the impact on financial sector.

# IMF Staff's Illustrative Restructuring Scenario

## EXTERNAL DEBT

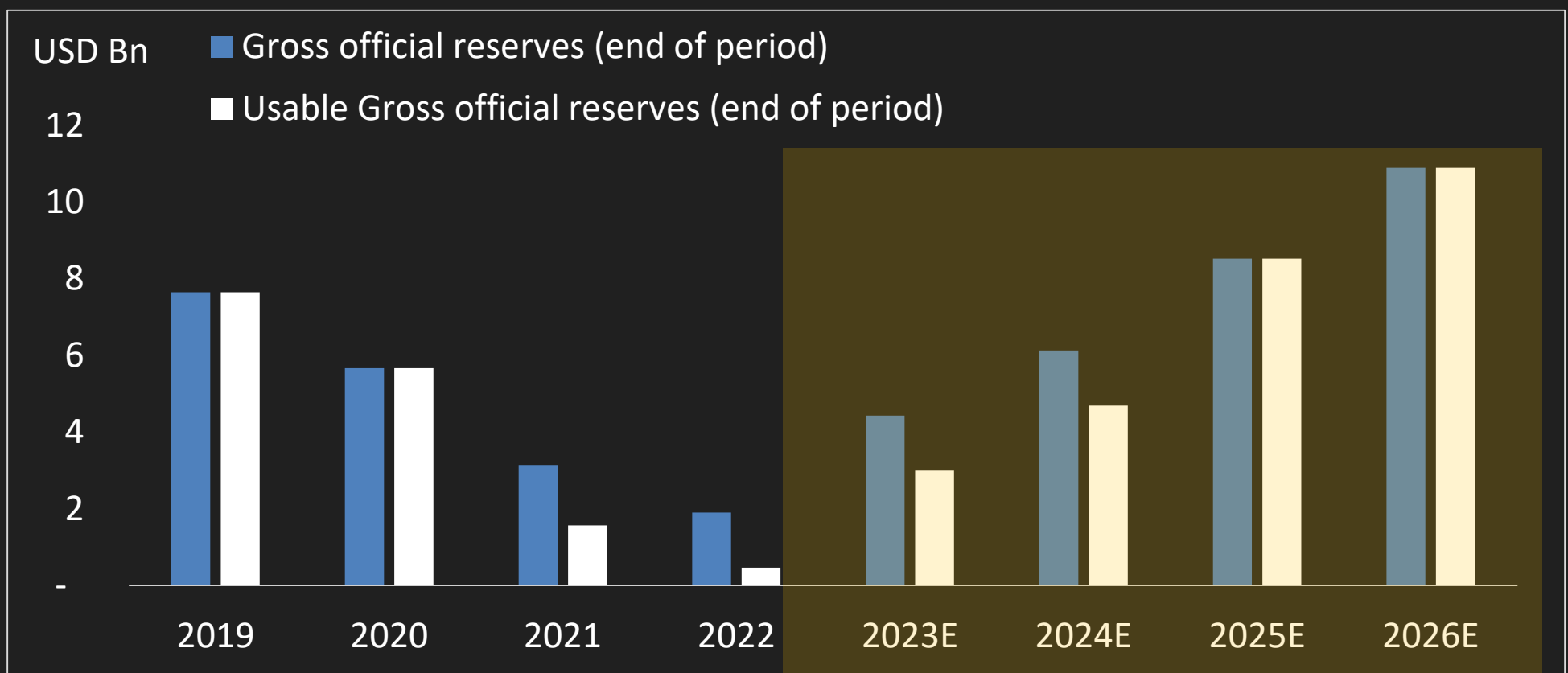
- **Private bondholders:** A large NPV cut is assumed, with principal reduction + amortization beyond the IMF program.
- **Bilateral Creditors:** Similar debt relief in NPV terms implemented through a long maturity extension, with amortization payments starting in 2033.

**The IMF highlights that their debt restructuring scenario is purely for illustrative purposes,** and the final design of debt restructuring will be decided depending on the negotiations between the government and creditors.

# Gross official reserves to rise to \$ 4 Bn in 2023 and \$ 11 Bn by 2025

The central bank expects to rebuild reserves via fx purchases from the market (\$ 1.4 Bn on a net basis in 2023), non-interest current account surplus and new external financing.

## Estimates - Year end Gross Official Reserves and Usable Gross Official Reserves



Source: IMF

# Ambitious Fiscal Targets

- **Revenue to GDP:** Increase to 15.0% by 2025 (from 8.5% in 2022).
- **Primary Balance:** A surplus of 2.3% of GDP from 2025 onwards (from a deficit of 3.8% in 2022).
- **Budget Deficit:** A target of 5.0% of GDP by 2025 (from 10.4% in 2022).

# A property tax to be introduced.

The government intends to revamp the property tax system and introduce a wealth transfer tax and a gift & inheritance tax.

# Expenditure Rationalization

The government is to develop strategies to limit growth in public sector wage bill and public pension spending.



# Social Safety Net (SSN) to be revamped

- As per a study done by the World Bank, in 2019, only 38% of the poorest income quintile received cash transfers under the Samurdhi program. Not only the poor, but 12% of the richest income quintile too received Samurdhi benefits.
- **IMF program sets a floor on SSN spending of LKR 187 Bn in 2023 (0.6% of GDP). Beyond 2023, the minimum SSN spending should be at least 0.6-0.7% of GDP.**

# Energy and Utility Prices



Retail fuel prices will be set to cost-recovery level with formula-based **monthly adjustments.**



Electricity tariff schedule will be set to cost recovery level with formula-based **semi-annual adjustments.**



# Other SOE Reforms Targets

- Restructure the balance sheets of Ceylon Petroleum Corporation, Ceylon Electricity Board, Road Development Authority and SriLankan Airlines by **June 2023**.
- Prohibition of new fx borrowing by non-financial SOEs with **less than 20% of their revenues denominated in fx**.

# Restoring Price Stability

- Price stability will be achieved via tight monetary policy stance and discontinuing monetary financing (money printing).
- **Headline inflation is expected to be at the CBSL's target band of 4-6% by early 2025.**



# CBSL to refrain from money printing

- The IMF program will ensure that the central bank **refrains from direct financing of the budget** and **unwinds its large stock of treasury securities**.
- **This will be monitored through a ceiling on the central bank's net credit to the government.**
- Under the IMF program, monetary financing (money printing) could be provided **ONLY** if there is a shortfall in budget support from multilateral development banks **during the first six months of the program**.

# Financial Sector Stability

- Large state banks' fx debt to the government and SOEs are expected to be restructured or repaid in LKR.
- The diagnostic exercise for nine major banks including Asset Quality Review (AQR) for the two largest state banks and three largest private banks will be completed by April 2023.
- CBSL will develop a roadmap for financial sector restructuring and recapitalization (to address capital and fx liquidity shortages) by July 2023.
- The government will determine conditions for any potential use of public funds to support the roadmap and to close capital shortfalls at viable banks by October 2023.

# Governance

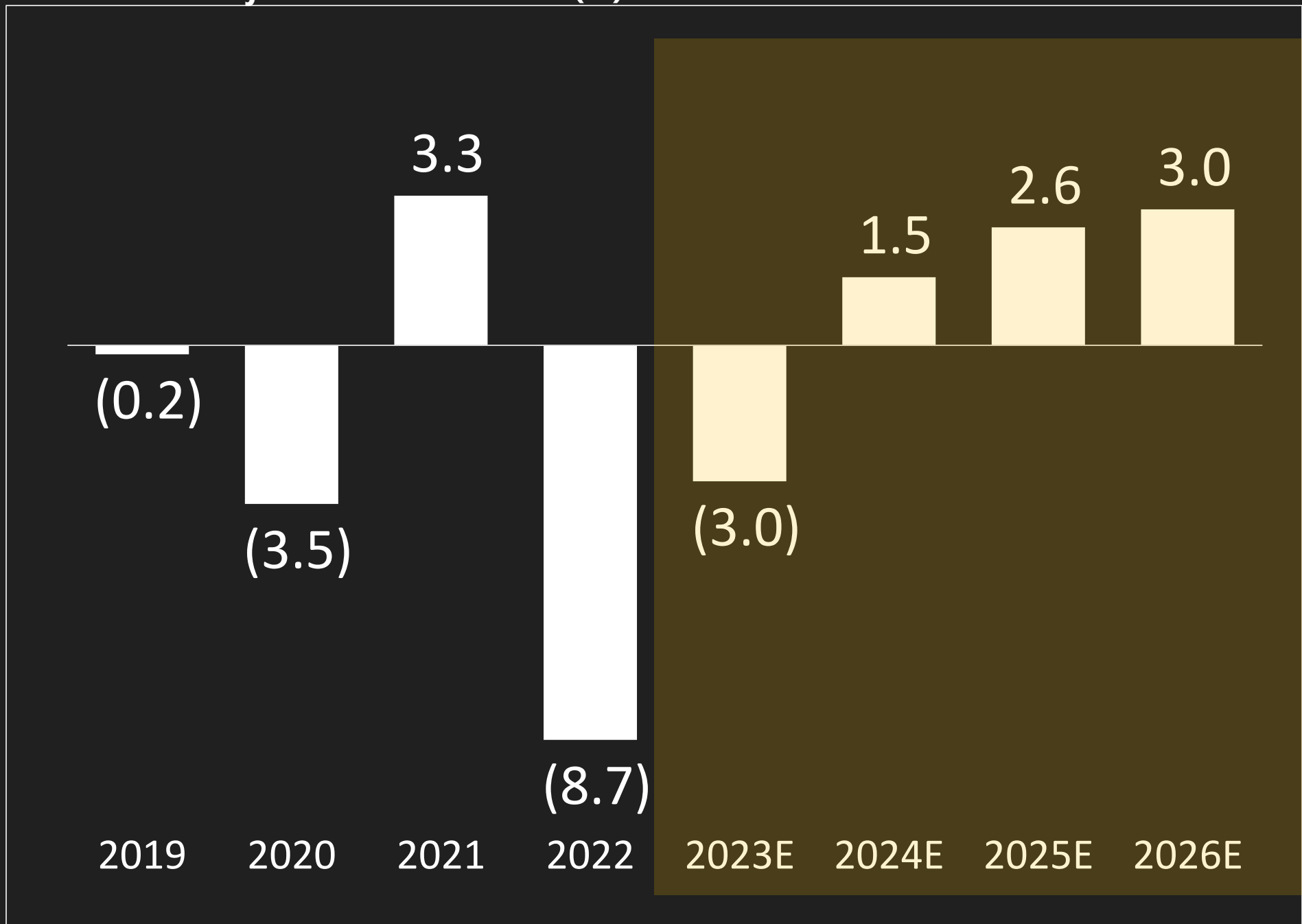
- Enact new anti-corruption legislation to harmonize it with the UN's Convention Against Corruption.
- IMF-led governance diagnostic mission to be established.
- Publish on a semi-annual basis about; all significant govt procurement contracts, a list of firms getting tax exemptions via the BOI, a list of individuals who are getting tax exemptions on luxury vehicle imports.

**The government intends  
to lift import restrictions  
gradually.**



# Real Sector: GDP to contract by 3.0% in 2023 before recovering in 2024

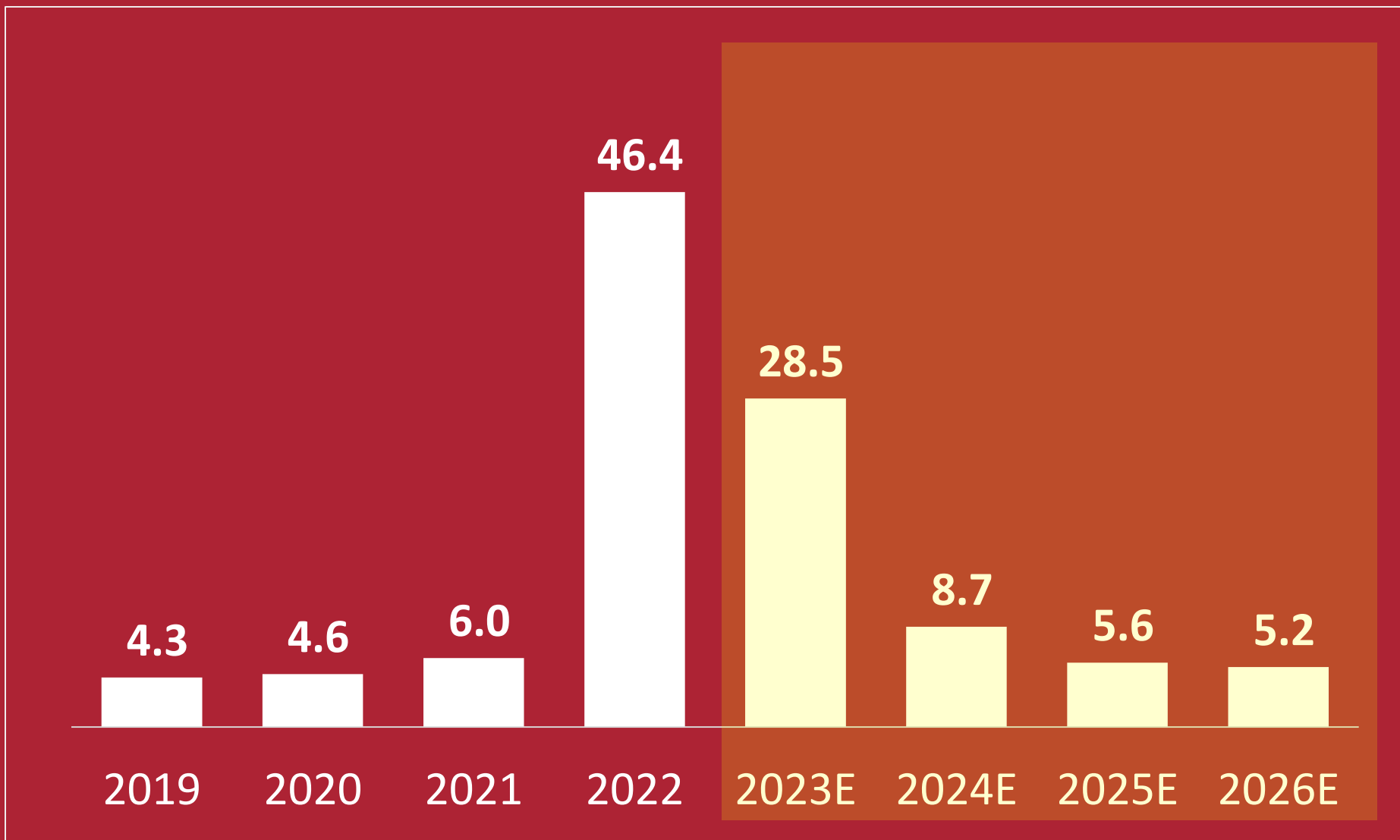
IMF's GDP Projections 2023 – 2026 (%)



Source: IMF

# Real Sector: Annual average inflation to remain at 29% in 2023 and to fall to a single digit level from there onwards.

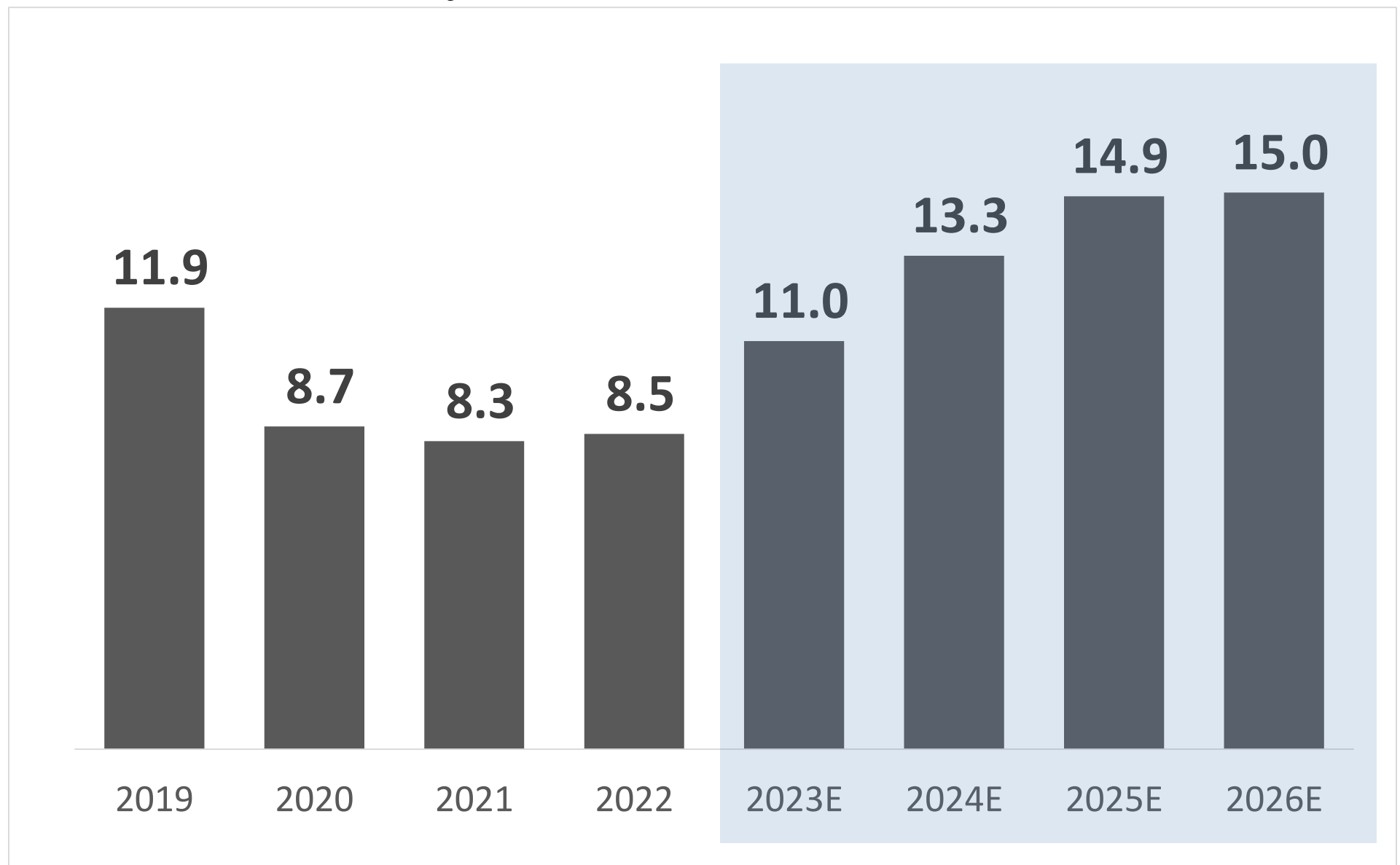
IMF's Annual Average Inflation Forecast (%)



Source: IMF

# Fiscal Sector: Revenue to GDP to rise to 15% by 2026 from 8.5% in 2022

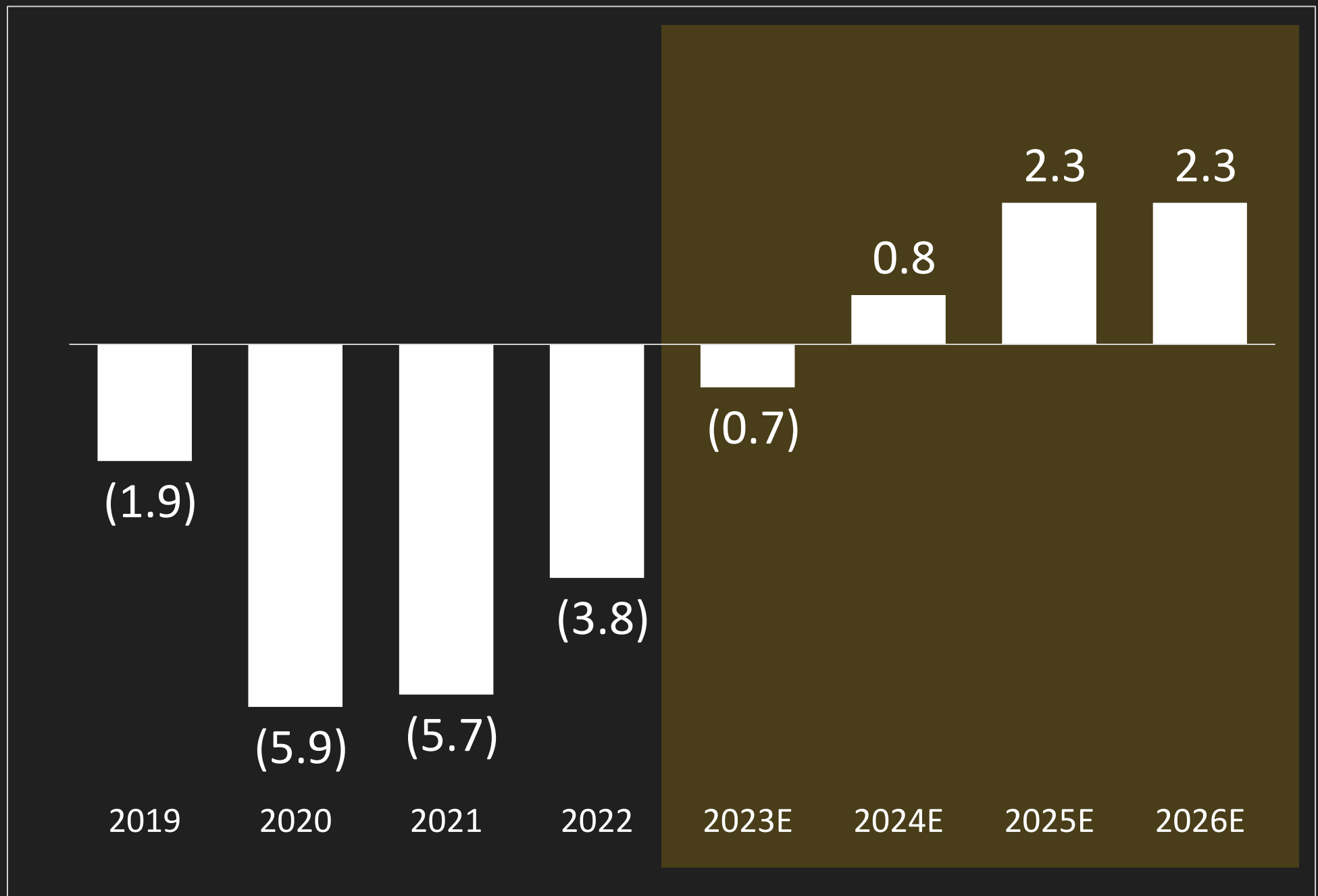
IMF's Revenue to GDP Projections (%)



Source: IMF

# Fiscal Sector: Primary surplus of 2.3% in 2025 from a deficit of 3.8% in 2022

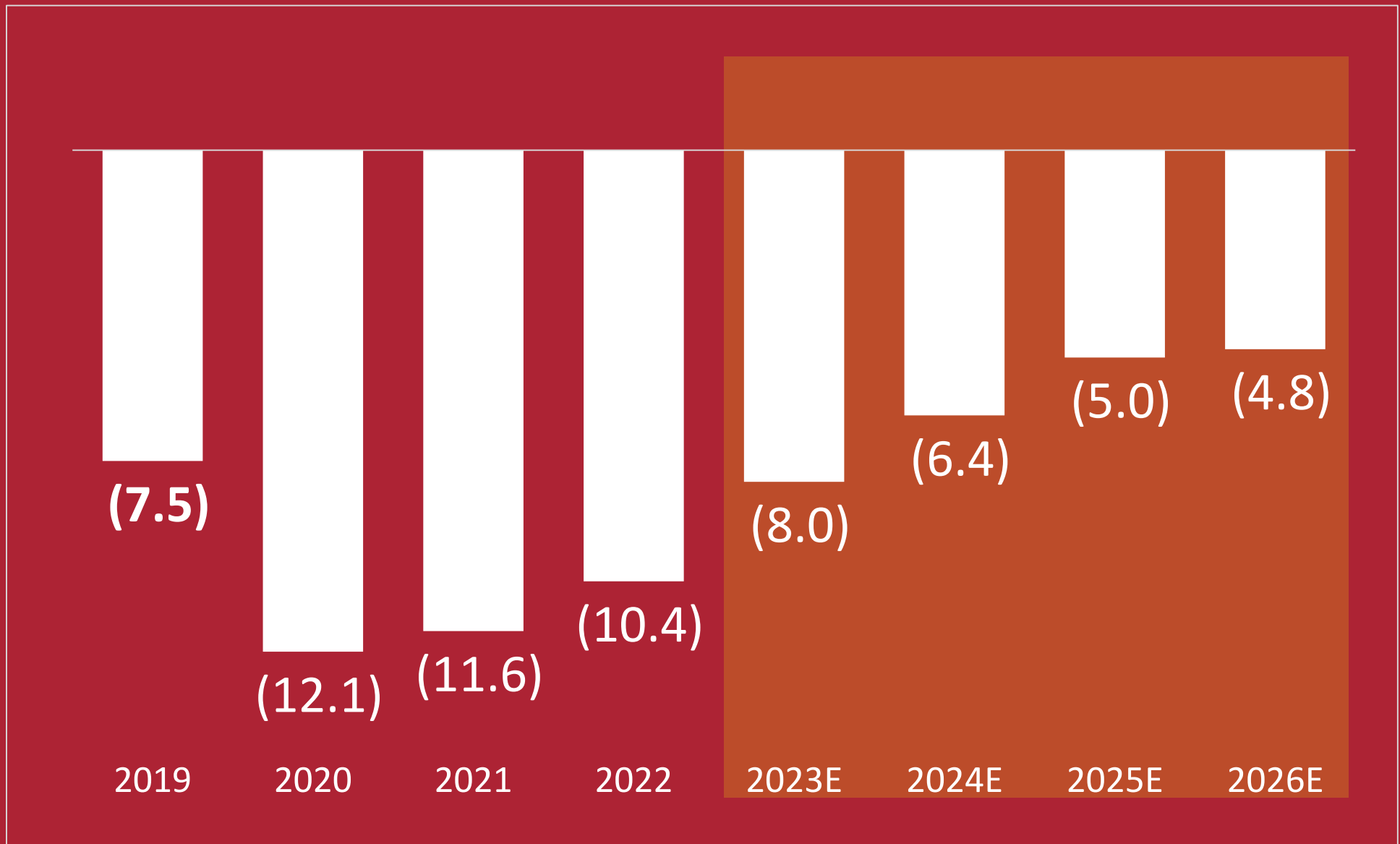
IMF's Primary Balance Projections 2023 – 2026 (%)



Source: IMF

# Real Sector: Budget deficit to come down to 5.0% of GDP in 2025 from 10.4% in 2022

IMF's Budget Deficit Forecast (%)



Source: IMF

# CONTACT US:

NDB SECURITIES (PVT) LTD

NDB Capital Building, Level 2,

No. 135, Bauddhaloka Mawatha, Colombo 04, Sri Lanka.

Hotline: +94 (11) 2 131 000

E-mail: [research@ndbs.lk](mailto:research@ndbs.lk)

Fax: +94 (11) 2 314 181

Website: [www.ndbs.lk](http://www.ndbs.lk)