IMF rejects Sri Lankan request for loan bailout

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The International Monetary Fund (IMF) has rejected a request by the Sri Lankan government of President Maithripala Sirisena for a $US4 billion loan in order to restructure debt repayments on high-interest Chinese loans negotiated by the government of former president Mahinda Rajapakse.

The decision was announced in Colombo on March 4, after a nine-day review of the Sri Lankan economy by the IMF's so-called Post-Program Monitoring Mission team headed by Todd Schneider. The IMF insisted that the government had to maintain its target budget deficit of 4.4 percent of GDP this year.

The IMF's blunt rejection of the loan request, which will mean further austerity measures for Sri Lankan workers and the poor, follows Finance Minister Ravi Karunanayake's meeting last month in Washington with IMF chief Christine Lagarde. As well as a $4 billion loan, the finance minister requested deferral of IMF loan repayment instalments.

Karunanayake told the media after his Washington meeting that "there is a lot of international goodwill and we can get finance from the IMF and World Bank at 0.5 percent [interest rate]."

The finance minister's illusions were quickly shattered, however, on March 4, when Schneider, told the media in Colombo that there was no need for a bailout. Sri Lanka's foreign reserves were "comfortable," he said, and the current situation was different to 2009 when the previous government obtained a bailout loan of $2.6 billion loan to avert a balance-of-payment crisis. While Schneider said the situation could be reviewed, the IMF warned last year that Sri Lanka was vulnerable to external shocks due to high level of commercial loans.

The real reason for the IMF refusal is not Sri Lanka's "comfortable" foreign reserves but disagreement with the Sirisena government's recent budget, which promised salary and pension increases for public sector employees and limited increase of social welfare measures.

Schneider said the Sri Lankan government would have "difficulty in keeping to the budget deficit target of 4.4 percent due to a rise in expenditure caused by salary hikes and poor tax collection". He insisted on the need for "structural reforms" and enhanced productivity and competitiveness. In other words, more privatisation of state-owned enterprises was required and other measures to intensify the exploitation of Sri Lanka's cheap labour workforce.

The IMF insisted that the Sirisena government prepare contingency measures to meet any revenue shortfall. It also voiced its displeasure over a partial reduction of import taxes on some food items and the imposition of various one-off taxes on the super profits of the corporate sector, the telecom sector, alcohol manufacturers, and on newly-built large houses. These one-off tax measures, Schneider said, "do not constitute a step towards a more effective tax system."

Sirisena's election as president in January followed his defection from Rajapakse's cabinet and the support of various opposition parties, including the pro-US United National Party (UNP), in his presidential campaign. This regime-change operation, which also involved former president Chandrika Kumaratunga, was sponsored by Washington and was in order to bring Colombo fully into line with the US "pivot" against China.

Sirisena promised voters that if elected he would introduce a "one hundred days" reform program. The new government faces parliamentary elections in June and is attempting to use its recent budget measures to win popular support.

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The government has promised a 10,000-rupee salary rise for public sector employees with a 5,000-rupee allowance from February and another 2,000-rupee allowance in June. While taxes of some food items have been reduced, the price of rice, the most essential staple, has increased (see: "Sri Lankan president brings down election budget").

The IMF also noted that Sri Lanka's debt was currently equivalent to 88.9 percent of the country's $60 billion economy, a dramatic increase in its debt to GDP ratio, which was at 78.3 percent in 2013.

The IMF also said the Central Bank's intervention into foreign exchange markets to defend the rupee over the past six months should be toned down. "Intervention should be limited to dealing with excessive short-term volatility," Schneider said.

The rupee dropped from 129 against the US dollar in August to 135 in January, and is currently about 132, with continuing downward pressure. Central Bank interventions have slashed Sri Lanka's foreign currency reserves from $9.2 billion in June to $7 billion last month.

The main reason for pressure on the country's exchange rate is because international speculators, who previously bought Sri Lankan treasury bonds, are now selling them and investing in more profitable markets. US portfolio investors are principal foreign investors in the Sri Lankan bond market.

The former Rajapakse regime and the current Sirisena government have intervened to prop up the Sri Lankan rupee in order to prevent a drastic collapse of the currency and rapid price rises that would have added to anti-government discontent among the working class and rural poor.

The IMF's refusal to grant Sri Lanka a bailout loan will see further increases in government debt and heightened demands for further social austerity measures.

Leading Sri Lankan economist Indrajith Kumaraswamy recently told a Colombo seminar: "With no access to that concessional [IMF] money, Sri Lanka is now pushed into borrowing from the far more brutal and potentially oppressive scrutiny of international markets at commercial rates which is sending the country into crippling debt rather than towards development."

Kumaraswamy attacked the government's public sector wage increases and other minor concessions, declaring that the Sri Lanka's "welfare state," was no longer affordable.

The IMF has predicted that Sri Lanka's economic growth will be 6 to 7 percent this year, claiming that it was "relatively robust." This growth, however, is mainly dependent on infrastructure projects, tourism and remittances from expatriate Sri Lankans, sectors acutely sensitive to the global economy and international geo-political pressures.

As the Sirisena government shifts its foreign policy orientation and strengthens its ties with India and US, tensions are increasing between Beijing and Colombo and compounding Sri Lanka's economic crisis. This was highlighted when Colombo suspended the massive $1.4 billion, Chinese-financed, Colombo Port City project. During the past five years China has invested $5 billion in infrastructure and other developments in Sri Lanka. Any suspension of these projects will deepen the Sri Lankan government's crisis.

The IMF's demands for increased social austerity measures will be implemented by whichever party alliance forms government following the forthcoming parliamentary elections in June.

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