IMF lowers Sri Lanka's growth forecast

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29 December 2016

Released on December 9, the International Monetary Fund's latest review of the Sri Lankan economy raised concerns about the situation facing the island-nation and reduced its previous growth forecast for 2016, from 5 percent to 4.5 percent, and from 5.5 percent to 4.8 percent for 2017.

Addressing the Sri Lankan media via video link from Washington, Jaewoo Lee, head of the IMF mission team for Sri Lanka, said, "The external environment is not as favourable as we used to think, that is the main reason for the downward revision … The Central Bank should be ready to tighten policy if global vulnerabilities grow. We emphasise this readiness."

Jaewoo's "unfavourable external environment" comment is a reference in particular to the US Federal Reserve's recent 0.25 percent rate increase and anticipated rate hikes as the incoming Trump administration's boosts infrastructure investments in the US.

The IMF report warned that one of the key risks facing the Sri Lankan government was the "weaker than expected capital inflows or a reversal of capital flows." Moody's investor service has also reported that Sri Lanka is in the highest category of "overall, vulnerability to the direct and indirect effects of sustained capital outflows."

On December 18 the *Business Times* revealed that foreign investment in Sri Lanka was $336 million for January–August 2016, down by 37.1 percent from $534 million in the same period last year. It warned that Foreign Direct Investment (FDI) in 2016 could be below the $681 million invested in 2015.

FDI in Sri Lanka, the publication noted, was "minuscule when compared to similar, emerging and former war-ravaged economies like Vietnam ($15 billion in 2015) and Myanmar ($9.4 billion 2015/16)."

The IMF report noted a sharp fall in Sri Lanka's foreign currency reserves, down from $5.07 billion to $4.23 billion between October and November. Gold reserves also dropped by 8 percent to $848 million. Sri Lankan export earnings are also falling fast. In the first eight months of 2016, they fell by 4.1 percent to $6.865 billion from the same period 2015.

The IMF estimates that Sri Lanka currently has $2 billion tied down in currency swaps and wants the remaining foreign currency reserves to be held in cash.

The IMF pointed out that capital outflows were pushing down the value of the Sri Lankan rupee, which has depreciated 3.1 percent during the current year, and warned that this would adversely impact on overall economic activity in Sri Lanka.

These are not mere statistics but find their reflection in the devastation of the social conditions of Sri Lankan workers and the poor whose wages and income remain static while the prices of basic items are climbing to intolerable levels.

The IMF also warned that depreciation of the rupee produces slow growth, which, in turn, will negatively impact on the IMF's current estimates of Sri Lanka's external debt. The agency expects the external debt to be reduced by 6 percent to 49 percent of GDP by 2021.

The IMF also noted that the Sri Lankan government would face difficulties fulfilling its commitment to repay a series of commercial loans by 2019.

"Sri Lanka's public debt and gross funding needs were high compared with its peers, with the ratio of gross financing needs to GDP being the fifth largest among emerging economies," the report said. It emphasised Sri Lanka's public debt reached 80.4 percent of GDP at the end of 2015 with 47 percent denominated in foreign currencies.

In early December, Sri Lankan Finance Minister Ravi Karunanayake said that the World Bank had agreed to provide $1.34 billion to the government, with $440 million in development assistance at 2 percent interest and the rest defined as "normal assistance" on a higher interest rate.

Karunanayake also said exchange control laws would be liberalised to allow anyone to bring money into the country as long as it was earned through “legitimate” means. He did not elaborate what he meant by “legitimate.”

In line with IMF demands, the government is slashing public spending. Karunanayake has announced that the finance ministry is establishing a special unit to review the overheads of all government ministries. On top of the already reduced budgetary allocations, each ministry will have to submit an expenses report to the Cabinet every three months.

The health and education budgets have already been slashed in the 2017 budget, along with cuts to fertilizer subsidies for farmers, clothing subsidies for school children and food subsidies to the poorest sections of Sri Lankan society.

The IMF report hailed the government’s increase in the value-added tax—from 11 percent to 15 percent—and hikes in other taxes. “Fiscal performance has been encouraging,” it declared. “The reinstatement of the amendments to the value-added tax will help boost revenues … The new Inland Revenue Act scheduled for early next year should result in a more efficient, transparent, and broad-based tax system.”

The IMF insisted, however, that “complementary structural reforms in tax administration, public financial management, and the governance and oversight of state-owned enterprises are critical for durable fiscal consolidation.” It also referred to “lower than expected growth and larger than expected losses at State-owned Enterprises [SOEs]” and stressed the need for the privatisation of several SOEs and “proactive management” of SOE debt.

The IMF noted the government was already preparing Statements of Corporate Intent for Sri Lanka’s six largest SOEs. While these were not named it is a clear sign of the government’s readiness to step up the IMF’s privatisation demands.

Commenting on the moves to privatise the national airline, the agency said: “A resolution strategy for Sri Lankan Airlines is to be adopted by December 2016 (with delay), including finding a strategic partner and a comprehensive cost-cutting.”

The Sri Lankan government has already signed a framework agreement with China’s Merchant Port Holdings Company Limited to sell the Hambantota port, offering 80 percent of the port’s share value to the Chinese company for $1.1 billion.

Colombo’s determination to impose the IMF’s demands and crush all resistance to its socially-regressive policies, was made clear early this month when it mobilised the police, the armed navy soldiers and blacklegs backed by court orders and a virulent media campaign to break up strike action by Hambantota port workers. The casual workers were fighting for job permanency when the new company takes control of the facility.

The ruthless character of the government attack on the Hambantota port workers is in response to the growing hostility of other sections of the working class, rural poor and student youth towards its regressive measures.