AMBEON SECURITIES

FIRST REVIEW OF IMF EXTENDED FUND FACILITY PROGRAM COMPLETED

Key highlights

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The International Monetary Fund (IMF) has announced that it did not reach a staff-level agreement with Sri Lanka during its first review under a USD2.9 billion bailout package. The primary reason cited for the lack of agreement is a potential shortfall in government revenue generation. Following a two-week visit to the country, the head of the IMF delegation explained that the release of a second tranche, approximately USD330 million, under the lending program would be contingent upon reaching a staff-level agreement. Importantly, there is no predetermined timeline for when this agreement might be reached. This development highlights the critical importance of addressing revenue generation challenges in Sri Lanka as the country navigates its economic recovery under the IMF-supported program. Given below are the key highlights.

Economic Challenges and Progress

The IMF acknowledges that Sri Lanka has faced significant economic challenges, including high inflation and a contraction in GDP. However, it also highlights that there have been commendable efforts to implement reforms, leading to some positive signs of stabilization, such as reduced inflation and increased international reserves.

Fiscal Reforms and Revenue Mobilization

The IMF expresses concern about revenue mobilization in Sri Lanka, emphasizing that there is a substantial gap between government expenditures and revenue collection. Revenue mobilization gains are expected to fall short of initial projections by nearly 15% by year end. It underscores the importance of tax policies and administration reforms to bridge this gap. The government has already taken steps to reverse tax cuts made in 2019, but further reforms are necessary to meet revenue targets.

Debt Sustainability and Restructuring

The IMF emphasizes the need for a stable path toward debt sustainability. This involves discussions and negotiations with both official creditors (such as the Paris Club) and commercial creditors (private bondholders). The IMF seeks assurance that debt restructuring will align with program targets and be conducted in a timely manner.

Social Safety Nets

The IMF acknowledges the impact of economic challenges on the poor and vulnerable in Sri Lanka. It notes that the IMF program includes measures to protect these groups, such as spending floors on cash transfers and a progressive tax system that excludes the poor from tax burdens. IMF wishes to see a minimum social spending of 0.6% of GDP to continue into the next year.

State-Owned Enterprise (SOE) Reform

The IMF discusses the importance of SOE reform to ensure that these entities operate on a commercial basis and do not accumulate additional financial liabilities for the government. It highlights steps taken to address losses in SOEs, such as adjustments to fuel and electricity prices.

Professional Exodus and Tax Reforms

The press briefing mentions the exodus of professionals from Sri Lanka and the difficulty citizens face in handling the tax burden resulting from reforms. While it acknowledges the challenges faced by the population, it emphasizes the need for tax reforms to increase revenue collection.

Renegotiation of the Agreement

The question of whether the IMF agreement with the government of Sri Lanka can be renegotiated is raised. The response suggests that while it's possible to make adjustments to the program, it depends on whether the objectives of the program can still be achieved.

Disbursement of Tranche

The timing of the disbursement of the second tranche of the IMF loan is contingent on reaching agreements on policies and reforms, as well as progress in debt negotiations. There is no fixed timeline for this process.

Source: IMF, Press Releases

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