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Statement by the Hon. **MANGALA SAMARAWEERA**,
Governor of the Fund and the Bank for **SRI LANKA**

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Governor of the Fund and the Bank for Sri Lanka**

Annual Meetings – 12th October 2018

Mr. Chairman,

The global economy continues its recovery, but economic growth has become increasingly uneven and less synchronized. The risks have increasingly shifted to the downside and challenges have intensified. This calls for more timely policy action to effectively tackle them to protect and enhance sustainable growth prospects and improve resilience. In particular, the impact of trade frictions between key economies and the impact of recent global financial market volatility on emerging market economies remain among the key concerns.

Active dialogue and cooperation among the international community through the multilateral system is paramount to address these key concerns and obtain mutual benefit to the global community.

In the context of the IMF, we are concerned about the slow progress of the 15th General Review of Quotas to-date and look forward to their completion within the envisaged time frame, and a revised formula that further shifts quota shares to dynamic emerging markets and developing economies (EMDEs) to reflect the new realities in the global economy.

Mr. Chairman, let me now briefly highlight recent economic developments and prospects in my own country.

Sri Lankan economy is expected to record a modest growth of around 4 per cent in 2018 as the economy still grows below potential. However, the growth is expected to recover and gradually move to a higher path, benefiting from the ongoing structural reforms, improved productivity and enhanced investments with improved investor confidence.

The reform initiatives are supported by the 3-year arrangement under the Extended Fund Facility (EFF) program of US\$ 1.5 billion that Sri Lanka entered in to with the IMF in June 2016. It aims to strengthen the external and fiscal balances of the economy.

The EFF program involves institutionalizing frameworks related to monetary policy in line with flexible inflation targeting framework, new exchange rate management framework as well as

fiscal rules for managing fiscal policy to continue and strengthen fiscal consolidation process beyond the EFF program to ensure sound macroeconomic policies, and support economic growth and strengthen stability.

Although headline inflation moved to the upper limit of the desired 4-6 per cent band in July/August 2018 reflecting upward adjustments in administered prices, sharp depreciation of the rupee and impact of low base prevailed in the previous year, it moderated thereafter as envisaged with the onset of harvest. The pressure on the inflation is expected to moderate in the remainder of 2018.

A significant improvement has been achieved on the fiscal front, reflecting strong commitment of the government towards the ongoing revenue based fiscal consolidation process. We have now balanced the primary account of the budget and expect a considerable primary surplus in 2018 and beyond.

The new landmark tax policy reforms and improvement in tax administration, and prudent expenditure management, coupled with the improvement in public debt and public financial management, as well as reforms in the state-owned enterprises (SOEs), are expected to strengthen the country's fiscal position further.

The external sector performance was mixed during the first half of the year, mainly owing to significant external pressures. Export earnings continued to grow during this period, but higher import demand, driven mainly by the surge in fuel, personal motor vehicles and gold imports, widened the trade deficit significantly.

The current account deficit also widened reflecting the expansion in the deficits in trade and primary income accounts. Foreign investment outflows from the government securities market and the Colombo Stock Exchange (CSE) since the second quarter of 2018 exerted pressure on the balance of payments.

The country's gross official reserves stood at US\$ 8.6 billion by end August 2018 compared to the historically high level of US\$ 9.9 billion recorded at end April 2018 amid volatile market conditions.

The exchange rate regime in Sri Lanka is now flexible and market-oriented. The higher import growth and capital outflows, in the context of a strengthening US dollar, exerted significant pressure on the exchange rate in the recent past. Accordingly, in line with several other peer countries, the Sri Lankan rupee depreciated at a faster pace of 9.7 per cent against the US dollar during the year up to 01 October 2018.

The Central Bank intervened to contain disorderly adjustment in the exchange rate, particularly during the first weeks of September 2018. This was complemented by several policy measures implemented by the central bank and the government to ease the excessive demand for foreign currency and the pressure in the domestic foreign exchange market. We remain committed to pursuing a flexible exchange rate regime, aligned with macroeconomic fundamentals, to absorb shocks with intervention confined to avoid wide fluctuations.

The financial sector continued to expand with improved stability and soundness. The capital adequacy, liquidity and asset quality of the banking sector remain robust. Measures are also being taken to strengthen the non-bank financial sector.

Our broad development strategy focuses on a three-pillared agenda i.e. democratization, reconciliation, and sustainable and equitable development with employment generation that transmits the benefits of growth across the wider society.

We continue to facilitate the private sector, which we consider as the major driver in Sri Lanka's growth model. Our efforts are continuously directed towards facilitating exports and Foreign Direct Investments (FDI) as key pillars in the growth process. We are also working to reap the opportunities created by the technological advancement and innovation with appropriate mechanisms to manage the associated risks.

In expanding exports as a key priority, we recently introduced a new 'National Export Strategy', focusing on improving competitiveness and innovation in the medium term.

In this context, we also strongly pursue our efforts to obtain the preferential access to markets with over 3 billion people, which will help boost domestic and foreign investments through leveraging the trade/investment nexus.

In line with this, we recently concluded a free trade agreement (FTA) with Singapore, which will expand the horizon in the international trade and attract more FDI. Similarly, measures are being taken to boost market access through deepening and widening the current FTA with India; invigorating the FTA with Pakistan and signing a new economic partnership agreement with China.

FDI related reforms are also being introduced under the Road Map to Improve Investment Climate in Sri Lanka to attract and sustain investments.

The above measures are expected to position Sri Lanka as an export-oriented economic and financial hub at the center of the Indian Ocean, effectively leveraging its strategic location.

Sri Lanka has achieved significant progress in its social development indicators due to the government's continued efforts and the support of the development partners.

In continuing these achievements and supporting the growth efforts, we have given the priority to develop human capital and skills while improving physical infrastructure. We are also committed to set up globally recognized regulatory mechanisms and investment practices, and create the best possible enabling environment for Sri Lanka to attract more businesses, trade and investment to become a higher income country.

Going forward, we are also committed to introduce measures to help better face the frequent occurrence of natural calamities, such as drought and floods. This entails measures such as mainstreaming sustainability into the planning and budgeting processes and improving disaster preparedness, mitigation and adaptation, supplemented by an appropriate natural disaster risk financing framework.

We will also continue to work with the UN and other institutions by aligning the government's policy strategy with the "Sustainable Development Goals (SDGs) and Targets" to be achieved by 2030.

I take this opportunity to thank the World Bank Group for their continued support to Sri Lanka in terms of financial assistance for development projects and technical assistance for analytical and advisory services.

As I believe, the World Bank Group's Country Partnership Framework (CPF) in Sri Lanka aims to make the development of the country with more systematic, evidence-based, selective approach, and focused on the World Bank's twin goals of ending extreme poverty and increasing shared prosperity in a sustainable manner.

Sri Lanka was graduated from "International Development Association (IDA) eligible" status to "International Bank for Reconstruction and Development (IBRD) eligible" status in 2017 and has access for borrowing under both IBRD and IDA Transitional Support Facility during IDA 18 cycle.

Even though, the graduation from IDA is a significant event, it ceases to have access to IDA grants and concessional resources resulting a financing gap as IBRD lending may not reach the IDA levels.

Therefore, the government and the World Bank have prepared World Bank Project Pipeline for 2017-2020, optimizing the increased financing cost associated with the graduation of Sri Lanka from concessional IDA borrowing to IBRD borrowing.

However, together with the financing gap, the accelerated repayment clause will create an extra burden on our external debt service obligations, which will be at the highest during 2019-2025, and this is mainly due to principal repayment obligations for commercial borrowings. However, considering the above implications, IDA deputies last year agreed to suspend the acceleration clause for Bolivia, Vietnam and Sri Lanka till the Mid Term Review (MTR) of IDA this year.

In view of the above, I take this opportunity to strongly request your support for the elimination of the IDA acceleration clause.

Also, we welcome the capital increase for the IBRD and the International Finance Corporation (IFC) of the World Bank Group. For the IBRD shareholding review scheduled in 2020, we look forward to outcomes that will achieve equitable voting power and enhance the voice and representation of developing countries.

Thank you, Mr. Chairman!