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Sri Lanka's Agreement with IMF

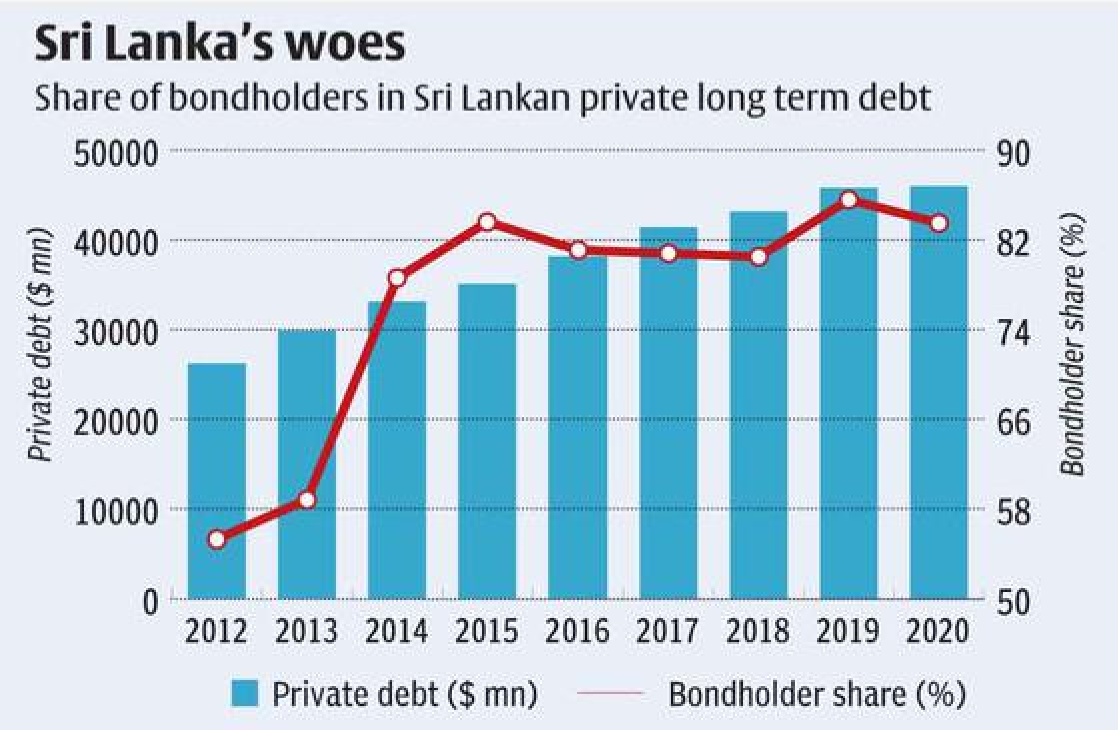
Why in news?

Sri Lanka has reached a staff-level agreement (formal arrangement) with the IMF that promises access to 29 billion dollar over a 4-year period.

What is the case with Sri Lanka?

- **Sri Lanka's economic crisis**- Sri Lanka's economic situation has worsened with 51 billion dollars of external debt.
- So, the country has reached an agreement with IMF to access credit under IMF's Extended Finance Facility.
- **Conditions**- It comes with a host of conditions varying from
    - Raising fiscal revenue
    - Reducing corruption vulnerabilities
    - Safeguarding financial stability
    - Persuading the country's multiple creditors to restructure and reschedule past debt
- **Significance**- The agreement is a step towards convincing foreign creditors and investors to return to the country.
- **Steps taken**- The Central Bank has
    - Floated the rupee
    - Raised interest rates sharply
    - Increased electricity tariffs and fuel prices
    - Restored tax cuts

Chart 1



What are the challenges?

- The outstanding long-term debt had risen from 26.2 billion dollar from 2012 to 46 billion dollar in 2022.
- The share of private creditors had risen to 37%.
- The bondholders in private credit had risen to 84%.
- Private bondholders would be less willing to accept any deal that requires them to take some losses.
- Talks with International Sovereign Bond (ISB) holders is a more complex exercise, with geopolitical dimensions.

How can Sri Lanka's crisis be compared with other countries?

- **Similiarities**- Private long-term external debt outstanding of countries identified by the World Bank belonging to the low and middle income category more than doubled from 2012 to 2020.
- The share of bondholders in that debt rose from 63% in 2013 to 80% in 2020.
- **Differences**- The variation is based on bond-based borrowing by government in the different regions.
- Overall, the share of governments in foreign currency bond issues across emerging market and developing economies (EMDEs) has fallen between 2002 and 2021.
    - The fall has been largely driven by declines in developing Europe and Latin America and the Caribbean.
- The share of government issuance has risen in Africa and the Middle East and in developing Asian and the Pacific.
- But foreign currency bonds may not be the best channel to mobilise resources as foreign borrowing requires debt service commitments to be covered in foreign currency.
- Increased dependence of less developed nations on sovereign bondholders has not

only contributed to a debt crisis but made resolution near impossible.

References

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2. https://www.thehindu.com/news/international/the-international-monetary-funds-staff-level-agreement-with-sri-lanka/article65849757.ece