

EBS/14/90
Supplement 2
Correction 1

July 30, 2014

To: Members of the Executive Board

From: The Acting Secretary

Subject: **Sri Lanka—Staff Report for the 2014 Article IV Consultation and Second Post-Program Monitoring Discussion—Informational Annex**

The attached corrections to EBS/14/90, Sup. 2 (7/10/14) have been provided by the staff:

Factual Errors Not Affecting the Presentation of Staff's Analysis or Views

Page 10, section on National Accounts:

for **"National accounts.** The Department of Census and Statistics (DCS) released a new Consumer Price Index for Colombo—the CCPI(N)—in 2007, replacing the Sri Lanka Consumer Price Index (SLCPI) and the Colombo Consumer Price Index (CCPI). The CCPI(N) is based on the spending pattern reflected in the 2002 Household Income and Expenditure Survey. It is based on the spending patterns of all urban households in the Colombo district. A core inflation index based on the CCPI(N) is also compiled by the DCS. It excludes all food and fuel prices to provide a measure of underlying inflation. The Central Bank of Sri Lanka (CBSL) produces a Wholesale cum-Producer Price Index (WPI/PPI).

The national accounts suffer from insufficient data sources and undeveloped statistical techniques. The country does not have periodic comprehensive benchmarks or a system of regular annual surveys of establishments. A statistical business register, which would serve as the main basis for conducting sample surveys, is not available. As a result, the few surveys that are conducted do not have good sample frames. Most of the data used are obtained on a timely basis. However, detailed data needed to measure both output and intermediate consumption are mostly unavailable or not collected. As a result, the estimates of gross value added are prepared directly relying on outdated fixed ratios established from the base year 1996, often with outdated studies or ad hoc assumptions. Quarterly indicators are used for compiling quarterly value added estimates. The methodology for deriving GDP at constant prices is not satisfactory. Expenditure estimates are available only annually and rely mostly on commodity flow techniques. Whenever possible, estimates are validated and checked with other sources."

read **"National accounts.** The Department of Census and Statistics (DCS) released a new Consumer Price Index for Colombo in 2007, based on the spending pattern reflected in the 2006-07 Household Income and Expenditure Survey. It is based on the spending patterns of all urban households in the Colombo district. A core inflation index is also compiled by the DCS to provide a

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Typographical Errors

Page 3, last paragraph, line 5: for "value Added Tax" read "Value Added Tax"

Page 4, para. 1, line 1: for "National Building tax" read "Nation Building Tax"

Questions may be referred to Mr. Schneider (ext. 35662), Mr. Jonas (ext. 38674), and Mr. Ghazanchyan (ext. 37689) in APD.

This document will shortly be posted on the extranet, a secure website for Executive Directors and member country authorities. This correction is not being disseminated in hard copy. It can be accessed in the Institutional Repository. A link to this document can be found in the daily list (<http://www-int.imf.org/depts/sec/services/eb/dailydocumentsfull.htm>) for the issuance date shown above.

Att: (3)

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Department Heads

Exchange Rate Arrangement

The de jure exchange rate arrangement is free floating since its introduction by the Central Bank of Sri Lanka (CBSL) on January 23, 2001. The CBSL intervenes in the foreign exchange market to limit volatility in the exchange rate. Since October 2013, the Sri Lanka rupee has stabilized within a 2 percent band against the U.S. dollar. Accordingly, the de facto exchange rate arrangement has been reclassified from floating to a stabilized arrangement, effective October 1, 2013. Sri Lanka maintains an exchange system free of exchange restrictions on the making of payments and transfers for current international transactions, except for the exchange restrictions imposed by Sri Lanka solely for the preservation of national or international security.

Safeguards Assessment

Under the Fund's safeguards assessment policy, the Central Bank of Sri Lanka (CBSL) was subject to an update safeguards assessment with respect to a Stand-by Arrangement approved in July 2009. The assessment, completed in July 2009, found that the CBSL continues to have a relatively strong safeguards framework, especially in the external audit, financial reporting and control areas. The assessment recommended measures to improve the process of program data reporting to the Fund and to modernize and strengthen the internal audit function. Also the external audit arrangements were not fully institutionalized. The authorities have implemented majority recommendations of the report. However, staff has not received 2012-2013 Management Letters issued by the CBSL's external auditor. Delivery of this monitoring information by the CBSL is required under the safeguards policy.

Article IV Consultation

It is proposed that the next Article IV consultation take place in 12 months.

FSAP and ROSC Participation

- MFD: Both the FSSA and the FSAP reports were completed in 2002.
- MCM: An FSAP update took place in July 2012.
- STA: A data ROSC was completed and the report published in 2002.
- FAD: A fiscal transparency ROSC was completed and the report published in 2002. A ROSC update was completed and the report published in July 2005.

Resident Representative

Mrs. Eteri Kvintradze has been the resident representative since March 2014.

Technical Assistance

- **FAD.** A number of TA missions in tax policy and administration took place during the 2000s. A series of TA missions in revenue administration were conducted in 2003. Tax policy missions took place in 2001 and 2009, to provide advice on the reform of the tax system. In 2012, a mission visited Sri Lanka to evaluate the state of the Inland Revenue Department, with a particular focus on the effectiveness of the administration of the ~~value~~-Value Added Tax (VAT) and

secondarily the National Building ~~tax~~ Tax to identify measures to staunch and reverse the decline in VAT collections and improve the overall performance of the VAT system and taxpayers compliance. In addition, a number of missions took place during 2012–2014 to strengthen Public Financial Management, improving oversight of the State-Owned Enterprises, strengthening budget preparation and improving the commitment control system.

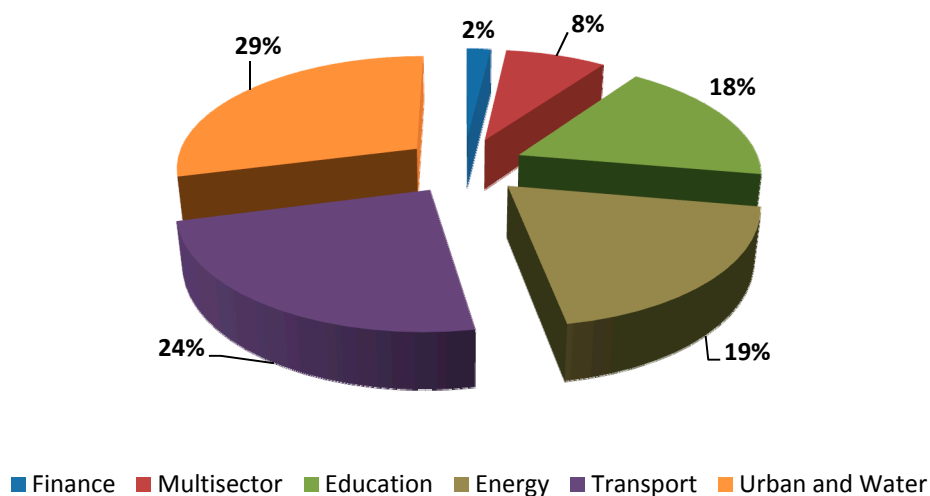
- **MCM.** In August 2001, a TA mission to develop a strategy for strengthening the framework and implementation of monetary and foreign exchange cooperation took place. In May 2002, an IMF/World Bank mission advised the government of Sri Lanka on options for reform of People's Bank. In 2003, TA mission on financial sector issues and financial sector reforms took place, followed by 2005 mission to provide advice on the introduction of new deposit insurance scheme.
- **STA.** In November 2012, a mission visited Sri Lanka to report on data dissemination practices with respect to the requirements of the Special Data Dissemination Standards (SDDS). During 2013–2014, Sri Lanka has received TA provided by the IMF/STA as part of the Asia module of the JSA Project on the Improvement of statistics in the Asia and Pacific Region. This TA focused on improving data collection and compilation of ESS including balance of payments, IIP, EDS, and Reserves Data Template (RDT), and supporting the authorities in their transition to the *BPM6* format. In 2013, TA missions also took place to review work on methodological improvements to the consumer price index and the development of the new producer price index, and to provide guidance on rebasing of GDP estimates and quarterly national accounts. In 2014, a mission took place to review the Government Financial Statistics (GFS) compilation system and make recommendations on the implementation of the GFSM 2001 and its 2014 update (GFSM 2014).

- Greater Colombo Water And Wastewater Management Improvement Investment Program - Tranche 1 (\$70 million from OCR and \$18 million from ADF)

- **Portfolio Performance:** As of 31 December 2013, ADB has approved a total of 166 loans, with cumulative lending of \$5.8 billion to Sri Lanka. In addition, ADB has provided \$358 million grant assistance (including ADB-administered co-financed grants) for projects and \$123 million through 259 technical assistance grants.

The current portfolio includes 49 ongoing loans and grants for 29 projects with a net loan amount of \$2.1 billion. Cumulative contract awards reaches \$1.0 billion, and disbursements \$0.7 billion. 80% of the ongoing portfolio are in transport, urban and water, and energy sectors. The sector composition of the ongoing loan portfolio is in Figure 1.

Figure 1 : Sectoral Distribution



Source: Asian Development Bank

STATISTICAL ISSUES

Macroeconomic statistics are broadly adequate for surveillance, but weaknesses remain in the timeliness and coverage of certain statistical series. Sri Lanka is a participant in the General Data Dissemination System (GDDS) since July 2000.

National accounts. The Department of Census and Statistics (DCS) released a new Consumer Price Index for Colombo—~~the CCPI(N)~~—in 2007, ~~replacing the Sri Lanka Consumer Price Index (SLCPI) and the Colombo Consumer Price Index (CCPI).~~ ~~The CCPI(N) is~~ based on the spending pattern reflected in the ~~2002 2006–07~~ Household Income and Expenditure Survey. It is based on the spending patterns of all urban households in the Colombo district. A core inflation index ~~based on the CCPI(N)~~ is also compiled by the DCS. ~~It excludes all food and fuel prices~~ to provide a measure of underlying inflation. The Central Bank of Sri Lanka (CBSL) produces a Wholesale cum-Producer Price Index (WPI/PPI).

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Government finance. In May 2003, a STA mission followed up on the ROSC recommendation to develop a migration path to compile data in accordance with the *Government Finance Statistics Manual 2001* (GFSM 2001). As part of that plan, the authorities agreed to revise (beginning in end-2003) the budgetary classifications and the accounting structure to eventually match the GFSM 2001 classifications of stocks and flows and to apply that chart of accounts to all general government units. In April 2014, a STA mission took place in the context of the Japan-funded IMF project on implementing GFSM 2001 and its update (GFSM 2014), for compiling, analyzing and reporting fiscal data.

Monetary statistics. Foreign Currency Banking Units (FCBUs) are classified as resident institutions in the monetary survey since 1998. To adjust for the proportion of nonresident foreign currency deposits (NRFC), which are actually held by residents (mainly returning migrant workers), 50 percent of these deposits are reclassified from foreign liabilities to domestic deposits.

In June 2003, a STA mission followed up on issues raised during the 2001 ROSC mission. In particular, the mission clarified the methodology for the treatment of Fund accounts; recommended that repos be treated