Sri Lanka’s Road to Recovery: Debt and Governance

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Dr. Nandalal Weerasinghe, Governor, Central Bank of Sri Lanka.

In March 2023, Sri Lanka entered into a 48-month Extended Fund Facility (EFF) Arrangement with the International Monetary Fund (IMF) to support the country’s

economic policies and reform agenda. The program seeks to restore and maintain macroeconomic stability and debt sustainability while safeguarding the poor and vulnerable, rebuilding external buffers, and promoting growth-oriented structural reforms, particularly through strengthened governance.

As of the third program review in February 2025, the IMF expressed satisfaction with Sri Lanka's progress, noting that performance under the arrangement had been strong. Notable achievements include the fulfillment of all quantitative targets set for December 2024. Moreover, most structural benchmarks due by January 2025 were either met or implemented with minor delays.

The successful completion of Sri Lanka's bond exchange marked a critical milestone in the path to debt sustainability, marking a significant step in the broader debt restructuring process. The government actively pursues reform initiatives proposed by the IMF, with early indicators showing positive outcomes. Nevertheless, given the economy's continued vulnerability, the IMF and the government acknowledge the importance of maintaining reform momentum. Sustained recovery and long-term debt sustainability remain contingent upon effectively implementing the full reform agenda.

At this pivotal stage, IMF Deputy Managing Director Dr. Gita Gopinath visited Sri Lanka to reaffirm the IMF's commitment to the country's recovery and reform efforts. She served as the Guest of Honor at the conference titled "Sri Lanka's Road to Recovery: Debt and Governance," co-hosted by the Ministry of Finance, the Central Bank of Sri Lanka, and the IMF. The event offered a retrospective examination of one of the most significant economic transformation efforts in Sri Lanka's recent history. Discussions centered on lessons learned in restoring macroeconomic stability, implementing debt restructuring, and advancing governance reforms while outlining the expectations and challenges ahead.

The conference commenced with opening remarks from Dr. Nandalal Weerasinghe, Governor of the Central Bank of Sri Lanka, President Anura Kumara Dissanayake, and Dr. Gita Gopinath. The forum brought together ministers and deputy ministers, financial sector leaders, representatives of international agencies, members of the diplomatic corps, central bank officials, state institution representatives, academics, and policy think tanks.

In his welcome address, Governor Dr. Nandalal Weerasinghe highlighted the significance of the conference as it coincided with the midpoint of the four-year IMF-

supported program. He noted that the gathering provided a timely opportunity to assess achievements, draw lessons, and outline the critical next steps required to secure long-term economic stability, social resilience, and institutional credibility. He emphasized that a meaningful path forward begins with honest reflection on the challenges faced at the outset of the crisis.

The Path to Recovery

Dr. Weerasinghe, provided a comprehensive overview of the country's economic crisis and the decisive measures undertaken since its onset in 2022. He attributed the crisis to deep-rooted structural impediments, prolonged macroeconomic mismanagement, and persistent fiscal imbalances that ultimately led to unsustainable debt levels and a full-blown balance of payments crisis. As a result, inflation soared to record highs, and foreign reserves dwindled to critically low levels. That compelled the government to declare a temporary standstill on external debt servicing and initiate a sovereign debt restructuring process. For the first time in its post-independence history, Sri Lanka faced a dual crisis—sovereign debt and balance of payments.

With the support of the IMF through the EFF and in close coordination with creditors and the international community, the government and the Central Bank embarked on an ambitious program of macroeconomic stabilization and structural reform. Dr. Weerasinghe emphasized that the objective of these reforms is not only to recover from the crisis and restore macroeconomic stability but also to build a more resilient, inclusive, and robust economy for the future.

He noted that by the second half of 2023, Sri Lanka had reversed six consecutive quarters of economic contraction and has since registered positive growth. Inflation returned to single-digit levels within a year. The external current account recorded surpluses for two straight years. Foreign reserves, while still modest, have seen notable improvement. However, sustained effort is required to build reserve buffers supported by a flexible exchange rate regime.

On the debt restructuring front, he noted that the sovereign debt restructuring process is nearing completion. Once Sri Lanka finalizes bilateral debt restructuring, it can expect critical fiscal space and ease of external debt servicing burden.

Notably, the Governor highlighted that the reform agenda has gone beyond macroeconomic indicators to address institutional credibility and governance. The

government enacted several key legislative reforms to strengthen economic management's institutional and regulatory framework. These include the Central Bank of Sri Lanka Act, the Public Financial Management Act, and the Anti-Corruption Act, among others. While these reforms represent significant progress, he noted that further work is required to ensure their full and effective implementation.

According to Dr. Weerasinghe, stabilization is not an end; it must be the foundation for future growth, resilience, and inclusion. He cautioned that while Sri Lanka's recovery is evidence of what is achievable through sound policymaking, strong partnerships, and broad-based commitment, the path ahead remains uncertain. The country must remain vigilant to emerging domestic and global risks, as recent external shocks have demonstrated the fragility of recovery. To sustain current progress, he stressed, it is essential to maintain reform momentum while ensuring transparency, accountability, and inclusivity across all levels of governance.

The Future Course

Governor Weerasinghe underscored that the road ahead requires unwavering commitment to sustaining the reform agenda, empowering the private sector, safeguarding the most vulnerable segments of the population, and—most critically—ensuring policy consistency. These elements are essential to securing a path toward long-term economic recovery and sustainable debt management over the medium to long term.

Dr. Weerasinghe was resolute in his belief that the success of the journey ahead ultimately rests with Sri Lanka, led from within through national ownership of the reform process. He called for a collective effort driven by national institutions, the private sector, and the public, guided by inclusive, transparent dialogue and unified by a shared commitment to shaping a more resilient and prosperous future for the country.



President Anura Kumara Dissanayake.

Achievements Realized, but Much More to be Done

Addressing Sri Lanka’s Road to Recovery: Debt and Governance conference, President Anura Kumara Dissanayake reflected on the gravity of the economic collapse from which the country is striving to recover. He noted that the conference’s theme aptly captured the extent of Sri Lanka’s journey—from the depths of crisis and institutional breakdown to pursuing a more sustainable and equitable path forward. The President emphasized that the current trajectory represents a deliberate departure from the unsustainable and destructive policies of the past.

While acknowledging that Sri Lanka has made significant strides in its recovery,

President Dissanayake was unequivocal in stating that much work remains. He expressed deep appreciation for the resilience and sacrifices of the Sri Lankan people and for the commitment shown by institutions such as the Central Bank, the Ministry of Finance, and the broader political leadership in steering the country toward a measure of stability.

The President observed that notable achievements include the stabilization of the Sri Lankan rupee against the US dollar, the strengthening of foreign exchange reserves, and the attainment of key revenue targets.

However, the President cautioned that while these developments signal progress, they represent only the surface-level healing of a much deeper economic wound. The underlying structural weaknesses of the economy remain, and lasting recovery will only be possible through comprehensive reforms to rebuild the country's economic foundation.

President Dissanayake went on to identify three critical areas his administration has prioritized to address the more entrenched challenges obstructing sustained economic growth and development. These, he explained, are fundamental to healing the internal economic fractures and securing long-term stability.

Reforming State Institutions: A Pillar of Economic Transformation

President Dissanayake identified the reform of state institutions as the first and most significant factor in Sri Lanka's long-term recovery and structural transformation. He acknowledged the critical role played by the public sector in supporting the nation's initial path to stability and recovery. However, he also underscored a pressing reality: the substantial fiscal burden the State incurs in maintaining the public sector—a cost he believes is no longer sustainable or justifiable.

The President noted that the challenge now is to build a strong and resilient public service that is effective and accessible while ensuring that it operates at minimal cost to the public. He reiterated the political leadership's commitment to establish an efficient, affordable, and service-oriented public administration. In this regard, he emphasized the crucial responsibility of the Central Bank of Sri Lanka and the Ministry of Finance in spearheading institutional reforms.

Outlining the government's roadmap for reform, President Dissanayake detailed a

three-pronged strategy aimed at transforming the public sector:

Closure of Obsolete Institutions: The government has identified a number of state institutions that were established decades ago to address economic and social conditions specific to that era. Many of these institutions have lost relevance in today's vastly altered socio-economic context. The President stated that such institutions no longer serve a meaningful purpose and phase them out in the interest of fiscal responsibility and administrative efficiency.

Consolidation of Redundant Entities: Several state institutions perform overlapping functions under different mandates. This duplication of roles leads to inefficiency and unnecessary expenditure. To address this, the government plans to merge institutions with similar or redundant objectives, streamlining service delivery and reducing bureaucratic fragmentation.

Redefinition of Institutional Mandates: In recognition of evolving national priorities, the government intends to revise various state institutions' objectives and operational goals. This recalibration will align their functions more closely with contemporary socio-economic realities and national development goals.

President Dissanayake emphasized that these institutional reforms are vital to ensuring the sustainability of the economic gains achieved thus far. He affirmed his government's unwavering commitment to implementing these changes as a cornerstone of Sri Lanka's broader reform agenda. Such transformation, he concluded, is essential to building a leaner, more effective State apparatus capable of supporting lasting economic stability and inclusive growth.

Rooting Out Corruption: A Prerequisite for Reform

President Dissanayake articulated the second key pillar in Sri Lanka's path to sustainable recovery as the government's clear commitment to eradicating corruption. He acknowledged that systemic inefficiencies, driven by pervasive bribery and corruption across various levels of the public sector, remain one of the most formidable barriers to overcoming the country's economic challenges.

President Dissanayake pointed to the alarming frequency with which news reports highlight serious allegations involving high-ranking public officials. He stressed that corruption is not an isolated issue but a deeply entrenched structural problem that has significantly hindered Sri Lanka's development.

The President identified inefficiency, bribery, and corruption as significant impediments to economic recovery and core contributors to the crisis. He defined corruption as an institutional disease that extends far beyond the illicit transactions surrounding public projects. Corruption, he noted, also manifests in the persistent failure of decision-makers to implement necessary initiatives on time and in the execution of unproductive or non-essential projects—many of which have become long-term fiscal burdens to the State.

President Dissanayake argued that only a fundamental transformation of the public sector will address this culture of inefficiency and mismanagement. He reaffirmed his government's determination to undertake this transformation, asserting that the fight against corruption is essential to restoring institutional integrity, public trust, and the effectiveness of State governance.

State Control of Critical Sectors: Balancing Oversight and Public Interest

The third key priority outlined by President Dissanayake in Sri Lanka's ongoing recovery strategy is the State's continued involvement in select critical sectors of the economy—most notably, the energy sector. Given the relatively small size of Sri Lanka's energy market, he emphasized that the risk of monopolistic dominance is a significant concern. To mitigate this, the government believes retaining a strategic stake in such sectors is imperative to ensure fair competition and safeguard public interest.

President Dissanayake clarified that this involvement should not translate into an undue burden on citizens. For instance, he noted that institutions such as the Ceylon Electricity Board (CEB) and and the Ceylon Petroleum Corporation (CPC) are intrinsically linked to the economy and the daily lives' of citizens. Because of that intrinsic connection, the President emphasized the importance of government oversight and control to ensure these entities serve the public effectively and equitably.

At the same time, he acknowledged that public ownership must not result in inefficiencies or financial burdens that are transferred to the people. The President advocated for a pricing structure aligned with production costs to address this. For example, he proposed that the price of a unit of electricity should reflect the actual cost of generation, thereby ensuring transparency and financial sustainability.

President Dissanayake reaffirmed the government's commitment to protecting its

stake in critical state-owned enterprises to deliver reliable, reasonably priced services to the public. Concurrently, he expressed the government's intention to improve operational efficiency and implement cost-reduction strategies to provide services at or near cost without compromising quality.

Supporting the Vulnerable Amidst Reform: A Commitment to Justice and Inclusion

In addressing the government's commitment to protecting Sri Lanka's most vulnerable citizens during the implementation of economic reforms, President Dissanayake placed significant emphasis on inclusive social protection measures. He stated that the State must safeguard the differently abled, older people and those unable to engage in economic activity due to their circumstances. He asserted that any credible discourse on economic development must incorporate these groups—not as an afterthought but as a core responsibility.

The President framed this inclusion as a matter of humanity, justice, and fairness. He proposed establishing a government-led intervention program specifically designed to support vulnerable populations. Crucially, he stressed that such initiatives must be free from political interference. For too long, the politicization of social assistance schemes targeting low-income groups in Sri Lanka was the norm, serving the interests of elected officials rather than those they were intended to help.

President Dissanayake made a clear commitment that any future assistance programs under his administration will focus on protecting the rights and welfare of the country's most disadvantaged individuals. These efforts, he stated, are vital for fostering social security and ensuring equitable development outcomes.

Growing FDI and Reviving SMEs: Catalysts for Economic Renewal

As the country advances toward economic recovery, the President highlighted the critical importance of foreign direct investment (FDI) as a necessary lever for sustainable growth. While acknowledging that Sri Lanka has achieved several reform benchmarks, he stressed that progress in attracting FDI has been insufficient. Despite periods of favorable global investment conditions, Sri Lanka has historically underperformed in drawing meaningful levels of foreign investment.

The President attributed this underperformance to continued structural and market

challenges. Although Sri Lanka has made gains in key macroeconomic areas—such as reserve stability and improved access to essential goods—these improvements alone are insufficient to instill investor confidence. Restoring trust in the country's financial markets and regulatory environment remains critical.

To address this, he revealed that the government is actively discussing with the IMF the design and implementation of targeted incentives for prospective investors. These measures aim to reposition Sri Lanka as an attractive and competitive investment destination. The President underscored the urgency of shifting the current paradigm by giving greater consideration to the needs and expectations of foreign investors and by adopting a more investor-centric policy framework.

In parallel, the government emphasizes revitalizing domestic production, particularly by recovering small and medium-sized enterprises (SMEs). President Dissanayake noted that over 90 percent of SMEs in Sri Lanka had either collapsed or faced severe operational difficulties during the peak of the economic crisis. Recognizing their integral role in national economic development, he stressed that the revival of the SME sector is indispensable to achieving broad-based and inclusive economic recovery.

Driving Economic Expansion and Reclaiming Sovereignty

President Dissanayake reiterated that broad-based economic growth and expansion remain central to Sri Lanka's path to recovery. He emphasized the need to shift greater attention towards the rural economy—a sector that has long been marginalized, even as the urban centers, particularly the metropolis, have benefited disproportionately from economic interventions and development focus.

While acknowledging the achievements in urban economic performance, the President underscored the imperative to expand growth drivers to include rural regions. He noted that the narrative of national progress often overlooks the untapped potential in these areas. The government intends to establish a strategic roadmap that integrates rural populations as active economic stakeholders. He asserted that such inclusion is essential for sustaining the momentum of macroeconomic stability and strengthening the foundations of long-term growth.

In concluding remarks, President Dissanayake expressed his aspiration that the current IMF-supported debt sustainability program will be the last of its kind. He outlined his vision for an economy capable of meeting its debt obligations through

domestic strength and resilience. He called for a renewed sense of national purpose, stating that now is the time for Sri Lanka to reclaim the independence and sovereignty compromised during the economic collapse.

This vision, he noted, requires unwavering dedication, institutional resolve, and a collective attitude. The President affirmed that Sri Lanka's future success depends on the continued commitment of political leadership, state institutions, and—most critically—the people of Sri Lanka.

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A Gathering at a Critical Juncture

Dr. Gita Gopinath, Deputy Managing Director of the IMF, acknowledged that the conference coincides with a pivotal moment in the country's economic trajectory. It also coincides with significant global economic shifts— marked by rising protectionism, increasing tariffs, and a rapidly evolving and uncertain international order. She noted that the challenge of building economic resilience is not unique to Sri Lanka but is shared globally as nations confront mounting volatility and geopolitical disruptions. Sri Lanka's experience is particularly noteworthy in this context.



Dr. Gita Gopinath, Deputy Managing Director, IMF.

Rising from the Ashes

From the depths of a severe economic and debt crisis, the country has made impressive progress within a relatively short period. Dr. Gopinath commended Sri Lanka's achievements as remarkable and deserving of international recognition. She noted that the IMF, which closely monitors the economic performance of its 191 member countries, views Sri Lanka's turnaround as substantial.

However, she also cautioned against complacency. The crisis that engulfed Sri Lanka was not sudden, she reminded the audience, but rather the result of years of eroding tax revenues, unsustainable increases in public debt, and a steady depletion of foreign exchange reserves. These underlying vulnerabilities culminated in one of the most acute economic crises the island had ever faced.

Today, Dr. Gopinath noted that inflation has moderated from double digits to single digits, tax revenues have improved, and meaningful investments have been made in governance reforms—critical for building trust between the government and its citizens and sustaining economic growth. She attributed this progress to the difficult but necessary reforms undertaken and the resilience, endurance, and sacrifices made by the people of Sri Lanka.

Dr. Gopinath acknowledged that while the country still faces significant challenges, the progress thus far in restoring macroeconomic stability and alleviating some of the hardships the public bears is a testament to the power of sound policy, strong partnerships, and national resolve.

Milestones and Lessons from the Reform Program

Dr. Gopinath outlined several key milestones Sri Lanka has achieved under its reform program and reflected on the broader lessons the country's experience offers the global community.

She noted that one of the most significant achievements is strengthening institutional frameworks—particularly the independence of the Central Bank of Sri Lanka, accompanied by improvements in public financial management and a more robust legal framework for combating corruption. These reforms, Dr. Gopinath emphasized, are not merely about building institutions for their own sake but are also economically transformative. According to IMF analysis, if Sri Lanka continues to pursue comprehensive governance reforms, the country could see its GDP rise by

over seven percent within the next decade. At the same time, the debt-to-GDP ratio could decline by more than six percentage points—demonstrating the tangible economic dividends of good governance.

Another significant milestone was the complex yet essential decision to restructure the country's debt. Dr. Gopinath noted that had Sri Lanka not undertaken this process, the consequences for the population would have been significantly more severe. Because of the restructuring, the government was able to provide some relief to citizens. The country has seen approximately USD three billion in external debt cut off. An additional USD 25 billion has undergone restructuring— extending the repayment period over two decades and at lower interest rates. That has led to improvements in Sri Lanka's credit ratings and the reintegration of its bonds into global indices.

Dr. Gopinath also highlighted key lessons that the international community can draw from Sri Lanka's experience:

Designing Effective and Realistic Targets – A critical component of Sri Lanka's debt restructuring was ensuring that the targets set under the program were sufficient to provide meaningful debt relief. Achieving this balance was complex. On the one hand, the depth of the crisis necessitated significant relief; on the other, Sri Lanka possessed strong fundamentals— including robust domestic private savings, tourism revenues, and remittances—that allowed for a tailored approach. As a result, Sri Lanka has halved its external debt servicing obligations as a share of GDP over the next decade. Per projections, the country will reduce its external and total debt stock by 27 and 34 percentage points of GDP, respectively.

Facilitating Coordination Among Diverse Creditors – Sri Lanka's creditor landscape was notably complex, involving many official creditors, many of whom lacked established procedures for sovereign debt restructuring. The Official Creditor Committee—led by France, India, and Japan—played a pivotal role in aligning creditor efforts. Dr. Gopinath acknowledged the challenges encountered, including concerns around information sharing and ensuring comparability of treatment. Despite this, strong coordination among government agencies, the creditor committee, and the IMF helped overcome these barriers. She also recognized China's constructive role in advancing the process, supported by IMF staff who facilitated technical information and collaboration.

Managing Domestic Debt Restructuring with Precision – Dr. Gita Gopinath

stressed that external debt restructuring alone is insufficient; the program must also address domestic

debt, a process that demands careful execution to avoid undermining financial and social stability. In Sri Lanka, the domestic financial sector— including the Central Bank and major pension funds—had significant exposure to sovereign bonds. Implementing domestic debt restructuring was done with careful planning to minimize disruption. As a result, the domestic banking sector has remained stable and is now showing signs of credit growth.

IMF's Deputy Managing Director affirmed that Sri Lanka's experience is a valuable blueprint for other nations navigating similar debt crises. It offers critical insights into setting realistic targets, coordinating effectively among diverse creditors, and ensuring responsible external and domestic debt restructuring management. She added that the IMF has drawn essential lessons from Sri Lanka's experience—leading to improvements in its debt policy frameworks, including greater emphasis on contingency instruments, coordination, timeliness, and the design of future restructuring programs.

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Lessons for Sri Lanka: A Path Towards Enduring Stability

Dr. Gopinath stated that the most critical lesson for Sri Lanka is to ensure that it never again descends into an economic crisis so severe that it necessitates sovereign debt restructuring. She acknowledged that the achievements over the past two years—while commendable—came at a considerable cost. She emphasized that the burden of the crisis was disproportionately borne by the most vulnerable segments of the population. The reforms introduced were essential to address the underlying structural deficiencies that led to the situation, and she reiterated that such sacrifices must not be in vain.

Referring to President Dissanayake’s remark that the economic wound is deep and cannot be healed overnight, Dr. Gopinath stressed that reforming entrenched inefficiencies—such as removing unsustainable subsidies—is vital. In particular, she cited cost-reflective energy pricing as a long-overdue but necessary measure to rectify distortions in the energy sector. She warned that failure to implement such reforms could risk a recurrence of future crises. While these reforms may test the resilience of Sri Lanka’s social fabric, they lay the foundation for a stronger, more self-reliant economy.

Looking ahead, Dr. Gita Gopinath underscored the importance of transitioning from stabilization to inclusive and resilient growth, particularly given the current global economic climate. While the nation has achieved a degree of macroeconomic stability, significant work remains. For instance, the World Bank estimated Sri Lanka’s poverty rate at 24.5 percent in 2024—a figure that she described as alarmingly high and in urgent need of redress. Addressing poverty, she said, will require a dual focus on maintaining macroeconomic discipline and implementing far-reaching structural reforms.

Tackling corruption is among the most critical of these reforms. Dr. Gopinath praised the Sri Lankan government ’s recognition of governance as a cornerstone of its reform agenda, supported by a concrete action plan. She noted that the governance diagnostic conducted in Sri Lanka was the first for an Asian country. The roadmap developed from it ensures that the right reforms are pursued and effectively implemented. She further emphasized the importance of maintaining sound fiscal policy, par ticularly amid external uncertainties—such as rising global tariffs, geopolitical tensions in the Middle East, and their potential implications for global energy prices. Under such conditions, Sri Lanka cannot afford policy missteps.

The Road Ahead: Staying the Course for Lasting Reform

In her concluding remarks, Dr. Gopinath highlighted the critical importance of sustaining the reform momentum to ensure that Sri Lanka’s current recovery effort does not echo past failures. She pointed out that the IMF has had 16 previous programs with Sri Lanka, half of which ended prematurely due to reform fatigue—often resulting in a reversal of hard-won gains. She emphasized that Sri Lanka cannot afford a repeat of history. Sri Lanka must advance the reforms underway in an inclusive and accountable manner. She advocated for open dialogue with civil society and transparent engagement with diverse stakeholders within Colombo and

across all regions. She noted that such a participatory approach would help ensure that policies are technically sound, socially responsive, and broadly supported.

Dr Gopinath acknowledged ‘Sri Lanka’s Road to Recovery: Debt and Governance’ conference as a meaningful step in this direction. By convening policymakers, financial experts, international agencies, and public sector and civil society members, the conference created a valuable platform to critically assess what has worked, what challenges remain, and how to carry the reform agenda forward effectively.

Reaffirming the IMF’s commitment to Sri Lanka, she reiterated the organization’s role as a steadfast partner in the country’s ongoing recovery. She underscored that the program’s ultimate goal is to enhance the well-being of all Sri Lankans—both today and for future generations.

Quoting President Anura Kumara Dissanayake, she echoed the aspiration that this current reform program must be the last of its kind for Sri Lanka. Achieving that goal, she concluded, is entirely possible—provided the nation remains resolute in staying the course.