SRI LANKA DEVELOPMENT UPDATE

PROTECTING THE POOR AND VULNERABLE IN A TIME OF CRISIS

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Preface

The Sri Lanka Development Update (SLDU) has two main aims. First, it reports on key developments over the past 12 months in Sri Lanka's economy, places these in longer term and global contexts, and updates the outlook for Sri Lanka's economy. Second, the SLDU provides a more in-depth examination of selected economic and policy issues. It is intended for a wide audience, including policymakers, business leaders, financial market participants, think tanks, non-governmental organizations and the community of analysts and professionals interested in Sri Lanka's evolving economy.

The SLDU was prepared by a team consisting of Richard Walker and Kishan Abeygunawardana (Senior Economists, Macroeconomics, Public Sector, Trade and Investment (MPSTI)), with inputs from Tatsiana Kliatskova (Financial Sector Economist, Finance, Competitiveness & Innovation (FCI)), Gonzalo Varela (Senior Economist, MPSTI) and Biying Zhu (Consultant, MPSTI). The special focus section was prepared by a team consisting of Francesca Lamanna (Senior Economist, Social Protection and Jobs (SPJ)), Cesar Cancho (Senior Economist, Poverty and Equity (POV)), Nandini Krishnan (Lead Economist, POV), Kelly Johnson (Senior Strategy and Operations Officer, SPJ), and Thomas Walker (Lead Economist, SPJ), with inputs from Tiloka De Silva (Consultant, POV), Shalika Subasinghe (Consultant, SPJ), Julie Perng (Consultant, SPJ), and Thisuri Jinadhi Wanniarachchi (Extended Term Consultant, SPJ). The team thanks Mathew Verghis (Regional Director, Equitable Growth, Finance and Institutions (EFI), South Asia Region), Faris Hadad-Zervos (Country Director for Maldives, Nepal and Sri Lanka), Chiyo Kanda (Country Manager, Maldives and Sri Lanka), Shabih Ali Mohib (Practice Manager, MPSTI), Ximena del Carpio (Practice Manager, POV), Stefano Paternostro (Practice Manager, SPJ), Tae Hyun Lee (Program Leader and Lead Country Economist, EFI), Rene Leon Solano (Program Leader, Human Development), for their guidance and comments on the report. Sashikala Jeyaraj provided administration support and was responsible for the layout, design, and typesetting. Dilinika Peiris, Buddhi Feelixge, and Samitha Senadheera led dissemination efforts. For questions, please contact: infosrilanka@worldbank.org

The report was prepared based on published data available on or before September 15, 2022. Data sources include the World Bank, Ministry of Finance, Central Bank of Sri Lanka, Department of Census and Statistics, and press reports.

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Abbreviations

ASPI	All Share Price Index
CBSL	Central Bank of Sri Lanka
CCB	Capital Conservation Buffer
CCPI	Colombo Consumer Price Index
CEB	Ceylon Electricity Board
CIT	Corporate Income Tax
CKDU	Chronic Kidney Disease of Unknown Cause
CPC	Ceylon Petroleum Corporation
CRM	Compliance Risk Management
DB	Disability Benefit
DCS	Department of Census and Statistics
DS	Divisional Secretary
EB	Elderly Benefit
EFF	Extended Fund Facility
EMDEs	Emerging Markets and Developing Economies
GDP	Gross Domestic Product
GFN	Gross Financing Needs
HIES	Household Income and Expenditure Survey
IMF	International Monetary Fund
LMICs	Lower Middle-Income Countries
MDS	Multi-Deprivation Score
MoDM	Ministry of Disaster Management
MoF	Ministry of Finance
NCPI	National Consumer Price Index
PIM	Public Investment Management
PIT	Personal Income Tax
SAFTA	South Asia Free Trade Agreement
SLA	Staff Level Agreement
SLAL	Sri Lankan Airlines
SLDBs	Sri Lanka Development Bonds
SLDU	Sri Lanka Development Update
SOEs	State-Owned Enterprises
UMIC	Upper Middle-Income Country
VAT	Value Added Tax
WBB	Welfare Benefits Board

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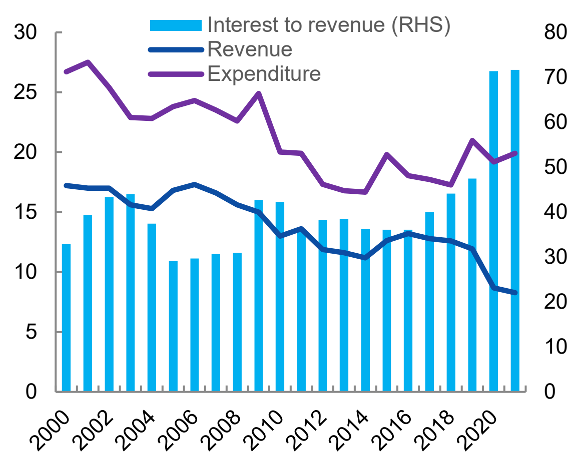
Executive Summary

A. Macroeconomic Developments

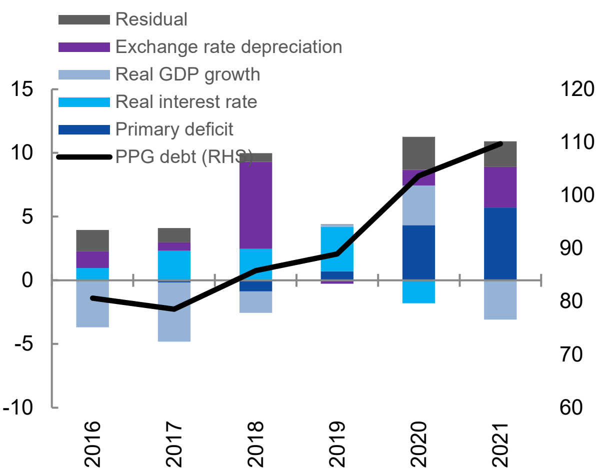
Sri Lanka is facing an unprecedented macroeconomic crisis. Years of fiscal indiscipline and risky commercial borrowing have led to unsustainable levels of public debt. Official reserves and net foreign assets in the banking system have been depleted, as the country continued to service debt and facilitate imports without access to international financial markets. The foreign exchange liquidity constraint has translated into shortages of fuel, food, medicines, cooking gas, and inputs needed for economic activity. Amid depleted reserves, Sri Lanka announced an external debt service suspension in April 2022, and appointed financial and legal advisors to support debt restructuring. Unprecedentedly high inflation has adversely affected real incomes, food security and living standards. The economy contracted in the first half of 2022 (Figure 1, Figure 2, Figure 3 and Figure 4)

Figure 1: Government revenue and expenditure
(Percent of GDP) *(Percent of total)*



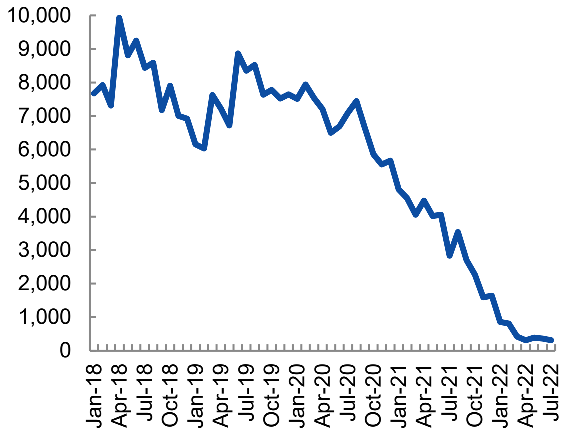
Sources: Ministry of Finance; World Bank staff calculations

Figure 2: Contributors to change in public and publicly guaranteed debt
(Percent of GDP) *(Percent of GDP)*



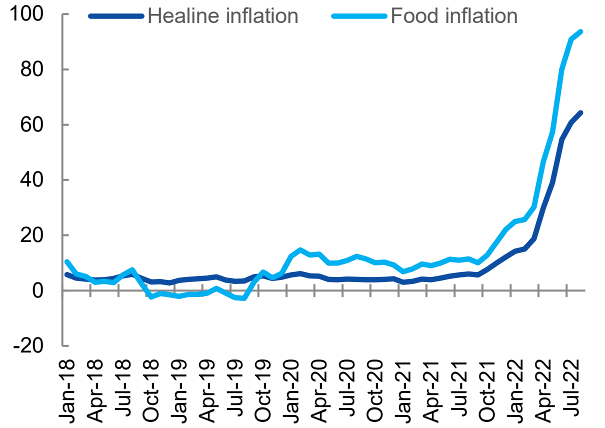
Source: Ministry of Finance; World Bank staff calculations

Figure 3: Gross official reserves
(US$ million)



Sources: Central Bank of Sri Lanka; official reserves are excluding a currency swap with the People's Bank of China.

Figure 4: Inflation (Colombo Consumer Price Index)
(Percent, y-o-y)



Source: Department of Census and Statistics

The economy was already showing signs of weakness before the COVID-19 pandemic. Growth and poverty reduction had slowed in the five years leading into the pandemic. A restrictive trade regime, weak investment climate, episodes of loose monetary policy and an administered exchange rate had contributed to external imbalances. The fiscal indiscipline, driven primarily by low revenue collections, had led to high fiscal deficits and large gross financing needs. Combined with these pre-existing fiscal imbalances, the tax cuts in 2019 contributed to a rapid growth in debt, to unsustainable levels. Following credit rating downgrades, Sri Lanka then lost access to international financial markets in 2020. A delayed response by the authorities to these issues allowed the crisis to spread to all key sectors of the economy.

As the crisis deepened, Sri Lanka sought support from the IMF. A staff-level agreement between the IMF and authorities – on a 48-month Extended Fund Facility program of about US$2.9 billion – was reached in September 2022. However, financing assurances to restore debt sustainability from official creditors and making a good faith effort to reach a collaborative agreement with private creditors are crucial before the IMF can provide financial support.

The fluid political situation and heightened fiscal, external, and financial sector imbalances pose significant uncertainty for the outlook. A significant economic contraction is likely in 2022 and 2023. Thereafter, the recovery depends on progress with fiscal consolidation, debt restructuring, and growth enhancing structural reforms. Despite tightened monetary policy, inflation will likely stay elevated. The fiscal deficit is expected to gradually fall over the medium-term due to consolidation efforts. The current account deficit is expected to decline due to import compression. Additional resources will be needed in 2023 and beyond to close the external financing gap. Poverty is projected to remain above 25 percent in the next few years. A slow debt restructuring process, limited external financing support, and the scarring effects of the economic contraction could prolong the crisis.

To emerge from the current economic crisis and improve long-term growth prospects, Sri Lanka needs to enhance fiscal and debt sustainability, and implement growth enhancing structural reforms. These measures need to be accompanied by tighter and more consistent monetary policy to contain inflationary pressures. The financial sector needs to be carefully managed, given heightened exposure to government and State-Owned Enterprises (SOEs) debt. A gradual restoration of a market-determined and flexible exchange rate is required to facilitate external adjustments and rebuild international reserves. Mitigating the impacts on the poor and vulnerable would remain critical during the adjustment period. These reforms and the necessary adjustments may adversely affect growth and poverty initially, but will correct the significant imbalances, and subsequently provide a foundation for sustainable growth and renewed access to international financial markets.

The international episodes of other countries with similar experiences suggest that unless the root causes are addressed, these crises tend to keep reoccurring. Firm resolve of political leadership and the Sri Lankan citizens would be needed to overcome the crisis through structural reforms. To weather the crisis, significant burden sharing by all citizens is also essential. Higher income groups will need to take more of the burden to protect the poor and vulnerable, as Sri Lanka embarks on this journey to emerge from the crisis as a strong and resilient economy. Meaningful outcomes of debt restructuring and collective support of international partners would also be needed to close the financing gap and maintain the reform momentum.

B. The welfare impacts of the economic crisis and the role of social protection in protecting the vulnerable

The ongoing economic crisis is estimated to have doubled the poverty rate in the country between 2021 and 2022. The current crisis has doubled the poverty rate from 13.1 to 25.6 percent ($3.65 per capita, 2017 PPP) between 2021 and 2022, increasing the number of poor people by 2.7 million. The COVID-19 crisis had already increased poverty from 11.3 percent in 2019 to 12.7 percent in 2020, a change that translated into over 300,000 new poor people in that year. The country is now experiencing its highest poverty rate since 2009, and an erosion of the steady gains in welfare made between 2006 and 2019. While 80 percent of the poor still live in rural areas, the poverty rate in urban areas has tripled from 5 to 15 percent between 2021 and 2022, and half the population in estate areas is now living below the poverty line. Across districts, Mullaitivu continues to be the poorest (57 percent poverty in 2022), followed by Kilinochchi and Nuwara Eliya.

A sharp increase in the cost of basic needs is one of the key mechanisms through which welfare has been impacted, whilst livelihoods and productive potential are also being substantially eroded. Relative to 2021, the median poor household in 2022 experienced an increase in the cost of their consumption bundle of 66.4 percent, compared with 56.2 percent for the median non-poor household. The industry and services sectors are expected to decline by 11 percent and 8 percent in 2022, respectively, which would lead to the overall destruction of over half a million jobs. Among those who continue to be employed, the real value of their earnings is expected to have declined by over 15 percent between 2021 and 2022. Remittances from workers abroad, which represent a source of income for 7.2 percent of households in the country, have also declined in real terms during 2022. Finally, the disruption to normal life due to the lack of imported goods (especially fuel) and the protests, and related security measures, have made it difficult for households to continue accessing basic public services such as education and health. To the extent that households have to rely on negative coping mechanisms in the face of falling incomes, a further deterioration in human capital outcomes is also likely.

The government's social assistance response to the COVID-19 pandemic and economic crises has been unprecedented, and it has helped somewhat mitigate the impact on poverty. Social assistance cash transfer programs[1] coverage has been expanded temporarily from 2.28 million to 3.2 million beneficiary families and individuals, or 63 percent of the population, and top-up transfers to offset inflation have been provided to all beneficiaries, tripling the overall monthly spending on cash transfers. Microsimulations show that without the country's main poverty targeted social assistance program (Samurdhi) expansion in 2022, in terms of beneficiaries and benefits amounts, poverty would have further increased by 3.1. percentage points this year.

Differently from most countries around the world, Sri Lanka could not rely on existing systems and institutions to rapidly and effectively respond to the crises which generated some inefficiencies. Many countries around the world relied on well-functioning and robust social registries to respond to the pandemic, making responses faster, more effective, and efficient. The government of Sri Lanka was limited in the impact of its response by a lack of data on which households were worst affected, as well as manual identification and payment systems. The Welfare Benefits Board (WBB) – the institution responsible for coordinating the management of data on welfare applicants and beneficiaries and advising

[1] Referring to the poverty and categorically targeted main country programs: Samurdhi, Elderly Allowance, Disability Allowance, and chronic kidney disease patients' allowances.

on selection mechanisms for welfare programs – was dormant during the pandemic. In the absence of a well-functioning social registry and payment system, assistance was provided based on existing lists of current program beneficiaries and waiting lists assembled between 2016 and 2019. This meant that social assistance did not reach the newly poor – who had not earlier needed assistance – and that some beneficiaries received more transfers and top-up than planned (deduplication could only be processed manually).

Even before the pandemic, the main cash transfer programs were poorly targeted and the cost of their poor targeting performance is borne by the most vulnerable households. The main social assistance programs (Samurdhi, Elderly Allowance, Disability Allowance) suffered from significant exclusion and inclusion errors in 2019. Just under 49 percent of households in the poorest quintile received social assistance, while 12 percent of the richest quintile also received a transfer, indicating that there are some inclusion errors. Meanwhile, recent simulations show that some groups remain more vulnerable than others (such as female-headed households). Inflation has further compounded this effect. Resources that are hemorrhaged to less deserving households could instead be redirected to those in the bottom 20 percent of households who do not receive any social assistance.

The impact of the emergency social assistance response could have been even more effective if the adequate social protection institutional and delivery systems had been in place. Since the WBB and social registry were not in place yet, the COVID-19 and economic crises response relied on existing programs with their weak targeting and set payment systems. Microsimulations show that the 2022 impact on poverty reduction could have been more than double if Samurdhi cash transfers had been perfectly targeted to the poorest quintile or if the budget spent on the program in 2022 had been distributed equally to the poorest, compared with the status quo. Having a centralized payment system in place would have limited duplications of payments from the outset.

The already low generosity and effectiveness of social assistance programs is further undermined by the inflation and volatility in the price of basic needs through commodity markets. The contribution of social assistance in Sri Lanka to the poorest quintiles' consumption is less than three times that of upper-middle-income countries (ASPIRE 2022). Cash transfer amounts are very low for all social assistance programs in Sri Lanka, and the program with the highest transfer amounts, Samurdhi, still provides over five times less than other countries' main poverty targeted cash transfer programs. The poorly regulated nature of the country's essentials markets leaves poor households vulnerable to sudden price hikes. The real value of the benefit amounts has been progressively eroded by inflation, rendering it even more inadequate relative to the needs of the beneficiaries. Benefit amounts are fixed in nominal terms and adjusted only occasionally (usually prior to elections). There is also evidence that tailoring the benefit amount according to need could help improve the poverty reduction impact of social protection. Current simulations also show evidence of a substantial concentration of people living just below the poverty line, who would need a moderate transfer to be lifted out of poverty, while the poorest decile of the population lives well below the poverty line and would need a substantially larger transfer. In recent years, the government has preferred to increase the number of beneficiaries in the program rather than focusing benefits on the poorest and increasing their generosity.

Recommendations

During the macroeconomic adjustment period, it will be imperative to protect the poor and vulnerable by providing immediate additional assistance to the poorest in need, while comprehensively reforming the social protection system.

In the short run, increasing financing for social assistance should be a priority. Poverty has increased sharply since 2021, and it is likely to increase further in the absence of effective mitigation measures. In order to ensure protection for the poor and most vulnerable – and partially mitigate the impact of the crisis upon the poor and vulnerable – spending on social assistance will have to remain at higher levels than pre-COVID-19.

The government will need to invest in the establishment and operationalization of the Welfare Benefits Board and a Social Registry. The Board of Directors of the Welfare Benefits Board (WBB) was appointed in July 2022 to oversee the update of the social registry and co-ordinate information sharing, registration, and targeting of beneficiaries for all social protection programs. The WBB is now overseeing the nation-wide collection of data on poor and vulnerable households to create an up-to-date social registry, and has adopted a poverty scorecard to enable prioritization of assistance to the poorest. Experience from other countries suggests that once the social registry is operational, it will play a key role in ensuring effective targeting and support for the poor and vulnerable in Sri Lanka. The WBB will also be responsible for designing any emergency support program targeted to the most needy during the crisis.

The generosity of cash transfers needs to be revisited, particularly for some vulnerable groups. The benefit amount should be increased given the high inflation, to a level that would safeguard all households' basic needs and insulate them against future shocks. This is especially urgent for the Elderly Benefit, the level of which is much lower than for the other cash transfer programs. Benefit amounts should then be indexed to inflation, to prevent future erosion of beneficiaries' purchasing power. Once the social registry is established, there will be scope to differentiate payment amounts based not only on household size, but also on households' poverty and vulnerability profiles. The results of microsimulation as seen in the analysis below show that this would improve the capacity of programs to reduce poverty while containing the overall fiscal cost of social protection.

Sri Lanka also needs to adopt more modern payment systems for cash transfer programs. Payments to beneficiaries during the pandemic and subsequent crisis have been predominantly cash-in-hand, which comes at a significant administrative cost and increases the risk of fraud, errors and corruption. Sri Lanka's digital payment systems have advanced significantly in recent years and offer a more efficient and beneficiary-friendly means of delivering cash. A centralized, well-regulated electronic payment system would promote efficient disbursement and coordination between the central government and program implementing agencies, and would also reduce payment times, leakages, and operating costs.

Given its increasing vulnerability to shocks, Sri Lanka would also benefit from developing a social protection system that can scale up and phase out where needed. The goal is to have programs that can expand temporarily during crises or following natural disasters. This can reduce the risk of shock-affected families being forced to resort to negative coping strategies that erode human capital (like skipping meals), a known cause of chronic poverty and transmission of poverty across generations.

In the medium to long term, Sri Lanka needs to transition to a more fiscally sustainable and inclusive social insurance and aged care system. Reforms are needed to rebalance the high amount of spending on public service pensions towards more equitable assistance, broadening coverage, and limiting the impact on the budget by seeking contributions from employers and employees.

Sri Lanka also needs to strengthen its productive inclusion programs. While there are many government and NGO-run programs empowering the poor at a small scale, the government's flagship Samurdhi program has had a limited impact. The scheme needs to be reformed with close attention paid to incentivizing Samurdhi officers to achieve measurable results, promoting access to quality training, opening up access to micro-loans, and partnering with local NGOs for on-the-ground implementation given that they are often better informed about local economic opportunities and can tap private sector support. Evaluation of the ongoing Samurdhi graduation pilot and productive inclusion of best practices from around the world should inform the way forward for this critical agenda in Sri Lanka.

Finally, a social protection strategy is needed to guide the overall social protection reform. In addition to articulating the priorities for future program design, targeting, and addressing the above-mentioned gaps, a social protection strategy is also needed to ensure coordination across government. Fragmentation and limited information sharing are currently impediments to effective program implementation and informed planning. A strategy that is broadly endorsed can also guide more carefully crafted and less politicized policy decisions and commit government to allocating the needed resources to ensure programs provide adequate protection and achieve the best possible results.

A. Macroeconomic Developments

1. Context

Rising debt vulnerabilities and weak competitiveness, resulting from years of risky borrowing and poor fiscal and monetary policy choices, along with weak governance, led to an unsustainable debt and a severe balance of payments crisis. A delayed response allowed the crisis to spread to all key sectors of the economy.

1. **Sri Lanka's economy was subject to several exogenous shocks in the last five years.** After the end of the civil war in 2009, the economy grew at an average of 6.4 percent between 2010 and 2017, spurred along by a debt driven and increasingly inward-oriented economic model. However, several macroeconomic shocks followed since then. The country experienced a political crisis in 2018 and then the Easter bombings in 2019. The COVID-19 pandemic exerted a profound, long-lasting impact on output, the labor market, and poverty. As a result, Sri Lanka's economy contracted by 3.5 percent in 2020 – the worst performance on record – and those below the $3.65 poverty rate increased to an estimated 13.1 percent in 2021 from 11.3 percent in 2019. The collapse of the tourism sector also exerted significant pressure on the balance of payments, and the pandemic likely elevated the liquidity and solvency risks in the financial sector – although the full impact cannot yet be observed due to continued regulatory forbearance. Recently, the Ukraine crisis[2] and rising global commodity prices have added additional pressure on the import bill in 2022.

2. **The economy was already showing signs of important structural weakness before the pandemic.**

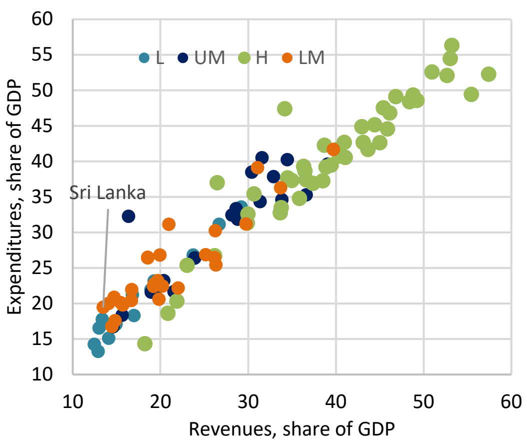
- Low government revenue mobilization has been a major source of fiscal vulnerability. Sri Lanka has one of the lowest tax revenue-to-GDP ratios in the world, reflecting a decline from 24.2 percent in 1978 to 11.2 percent in 2014 (Figure 5). Revenue collection increased to 12.6 percent of GDP by 2018 thanks to VAT reforms, including a rate hike. Sri Lanka's revenue structure has been characterized by: (i) a reliance on distortionary taxes; (ii) comparatively low redistributive effects of fiscal policy, driven by low direct tax revenue and a substantial incidence of indirect taxes on the bottom 40 percent; (iii) an eroded base due to a large number of exemptions and a compliance gap in VAT; and (iv) high income tax thresholds.[3]

[2] The main transmission channel of the Ukraine crisis is through global oil prices, rather than from the direct, bilateral trade relationships.
[3] World Bank, "Sri Lanka Public Expenditure Review (Public finance)", 2019.

- While expenditures have not been high (on average 18.4 percent of GDP per year in the last decade), interest cost has been rising. In 2021, the interest cost was 30 percent of the total expenditure and was equivalent to 72 percent of revenues. Sri Lanka's overall fiscal deficit averaged 6.9 percent of GDP in the last decade.
- Years of fiscal indiscipline and risky commercial borrowing[4] had led to high public debt and debt service. As a share of GDP, the public and publicly guaranteed (PPG) debt rose from 78.6 percent in 2017 to 109.7 percent in 2021. As a result, Sri Lanka became one of the most highly indebted developing nations (86th percentile), and the government's financing needs continue to be among the highest in emerging markets (Figure 6, Figure 7 and Figure 8).
- Weak export competitiveness has been hampering Sri Lanka's export growth for two decades. The country has become a more inward-looking economy since the turn of the century, which shows in the ratio of trade to GDP falling from 88 percent in 2000 to 39 percent in 2020. During the same period, exports as a share of GDP fell from 39 to 17 percent. The World Bank estimates Sri Lanka's missing exports at US$ 10 billion annually, almost as high as the current level of merchandise exports (Box 2). The increasing gap between actual and potential exports is driven by a combination of an overvalued real exchange rate and trade policy frictions that increase costs of trading, as well as the benefits of selling domestically. Sri Lanka's import duty levels are among the highest in the world, and the structure is also complex, with multiple para-tariffs and various exemption schemes. The current account deficit averaged 2.8 percent of GDP between 2012 and 2021 due to large trade deficits despite strong remittances and tourism flows.
- Continued monetization of fiscal deficits and episodes of loose monetary policy created further macroeconomic imbalances (Figure 9 and Figure 10). These imbalances, combined with pre-Covid-19 tax cuts in 2019, contributed to unsustainable debt and, as a result, Sri Lanka lost access to international financial markets in 2020 due to credit rating downgrades.[5] Despite rising foreign financing needs, an overvalued exchange rate, increasing trade and investment barriers, and a complex business environment created an anti-export environment, slowing down the growth of export earnings.

Figure 5: Average revenue and expenditure, 2015–19

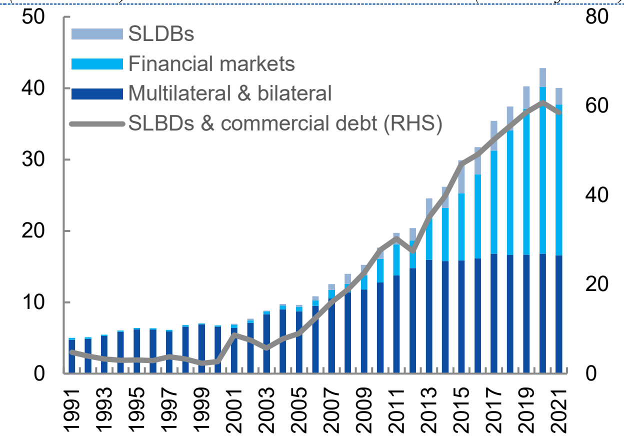
(Percent of GDP)



Sources: IMF Fiscal Monitor; World Bank staff calculations; L = low-income; LM = lower-middle-income; UM = upper-middle-income; H = high-income.

Figure 6: Rising foreign currency–denominated commercial debt

(US$ billion) *(Percent of Total)*



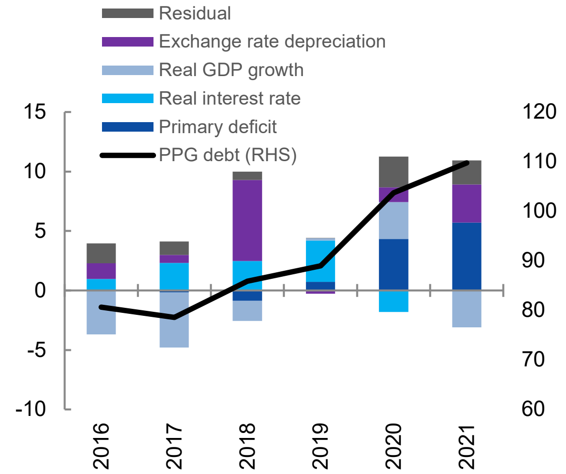
Source: Central bank of Sri Lanka, World Bank staff calculations

[4] The country had increasingly relied on relatively short-term, foreign currency denominated commercial debt since 2007. It used two instruments: (i) international sovereign bonds or Eurobonds (ISBs) issued outside the country; and (ii) Sri Lanka Development Bonds (SLDBs) issued within the country, denominated in US dollars. This foreign currency denominated commercial debt carried higher interest rates and shorter maturities (1-10 years) than multilateral and bilateral sources. At the end of 2021, the total outstanding Eurobonds stood at US$13.1 billion (15 percent of GDP) and the total outstanding SLDBs reached US$2.3 billion (3 percent of GDP).

[5] Credit rating agencies downgraded Sri Lanka to the substantial risk investment category: (i) Moody's by two notches to Caa1 with a stable outlook in September; (ii) S&P to B- in September and to CCC+ with a stable outlook in December; and (iii) Fitch to B- in April and to CCC in November

Figure 7: PPG debt growth decomposition

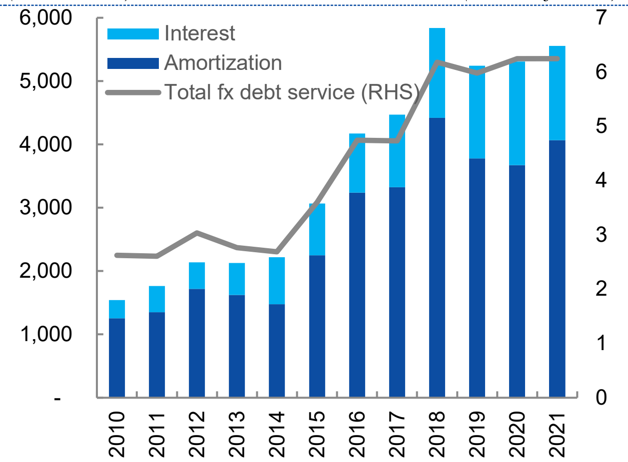
(Percent of GDP) *(Percent of GDP)*



Source: Central Bank of Sri Lanka; World Bank staff calculations

Figure 8: Foreign currency-denominated debt service of the central government

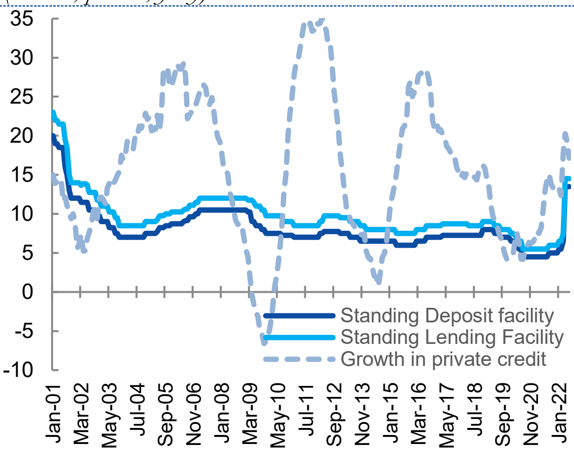
(US$ million) *(Percent of GDP)*



Source: Central Bank of Sri Lanka; World Bank staff estimates

Figure 9: Policy rates and private credit growth

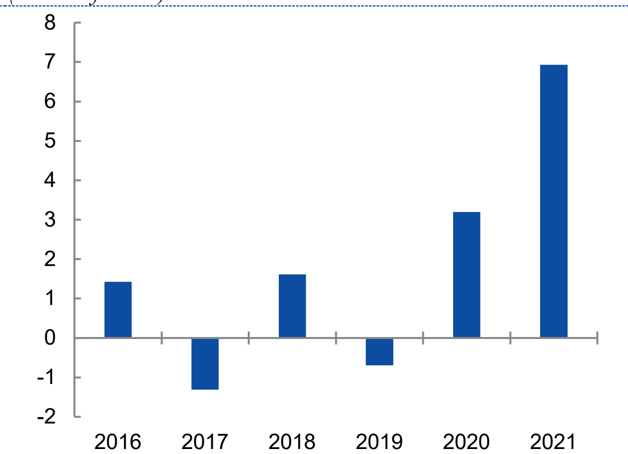
(Percent, percent, y-o-y)



Source: Central Bank of Sri Lanka; World Bank staff calculations

Figure 10: Net credit to government by CBSL

(Percent of GDP)



Source: Central Bank of Sri Lanka; World Bank staff calculations

3. **Amid unsustainable debt and critically low reserves, Sri Lanka suspended external debt service.** Without market access, Sri Lanka continued to service its external debt and pay for imports using official reserves and financing from the domestic banking sector. The central bank's six-month road map (presented in October 2021) did not raise funds as envisaged. Official reserves went down from US$ 7.6 billion in 2019 to less than US$ 400 million (excluding a currency swap equivalent to US$ 1.5 billion from China that has specific conditions for its use)[6] in June 2022. Net foreign assets in the banking system also deteriorated to US$ -5.9 billion in June 2022. The impact of severe forex liquidity constraints is being felt across the economy, particularly from the second quarter of 2022, with shortages of fuel, food, cooking gas, and inputs needed for the agriculture and industry sectors. Amid depleted usable reserves, on April 12, 2022, Sri Lanka announced an external debt service suspension and later appointed legal and financial advisors to help with debt restructuring.

[6] The proceeds cannot be used unless Sri Lanka has foreign reserves sufficient for three months, according to media reports.

4. **As the crisis deepened, Sri Lanka reached a Staff Level Agreement (SLA) in September 2022.**[7] The SLA is for a 48-month Extended Fund Facility (EFF) program of about US$ 2.9 billion, which requires IMF board approval. The EFF is expected to restore macroeconomic stability and debt sustainability, while safeguarding financial stability, protecting the vulnerable, and stepping up structural reforms to address corruption and unlock Sri Lanka's growth potential. However, IMF Board approval of the EFF would require financing assurances from official creditors, good progress on a collaborative agreement with private creditors, and the completion of prior actions.[8]

5. **The economic crisis is weighing on political stability.** The incumbent president resigned following massive protests on July 9, 2022. Although parliament appointed a new president to complete the remaining two and a half-year term and the new government announced its commitment to a reform program supported by the IMF, political tensions remain elevated as the economic crisis continues to deepen. Underlying tensions are further elevated by perceived weak governance, corruption, and elite capture.

2. Recent Economic Developments

The crisis is broad-based. The economy shows signs of a severe contraction leading to income and job losses. Unprecedentedly high inflation is adversely affecting real incomes, food security and living standards. Stress on balance of payments and fiscal and debt vulnerabilities have threatened macroeconomic stability.

Sri Lanka's economy contracted in the early part of 2022

6. **The budding recovery in 2021 – with real GDP growing by 3.3 percent (y-o-y) – was halted in the first half of 2022 by the looming crisis.** The economy contracted by 4.8 percent (y-o-y) in the first half of 2022, due to large contractions in the agriculture and industry sectors, while services also contracted modestly (Figure 11). Shortages of inputs, due to the sudden import ban of inorganic fertilizers and other chemical inputs from May to November 2021,[9] substantially reduced the overall agriculture sector output during the first half of 2022. Supply chain disruptions and limited access to inputs severely affected the industrial activity, particularly food and beverage manufacturing and construction. The gradual recovery of tourism from a low base somewhat offset the impact of significant contractions in financial and personal services in the services sector.

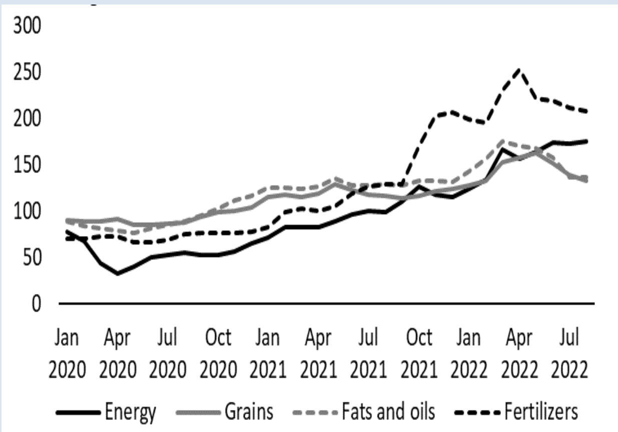
[7] In its 2021 Article IV Consultation report, the IMF assessed Sri Lanka's debt as unsustainable. However, according to proceedings of the Parliamentary Committee on Public Enterprises (May 2022), the IMF had already communicated to government around March 2020 that Sri Lanka's public debt was unsustainable; although no tangible actions were taken at that time to address the issues.
[8] IMF press release: https://www.imf.org/en/News/Articles/2022/09/01/pr22295-imf-reaches-staff-level-agreement-on-an-extended-fund-facility-arrangement-with-sri-lanka
[9] The government imposed this ban with immediate effect in May 2021 to move to organic and green agriculture. Amid widespread protests against this policy, the ban was lifted from 30 November 2021, allowing the private sector suppliers to import fertilizers and agrochemicals.

Box 1: Deterioration in global and regional developments

Global economy is facing turbulent times. Commodity prices have remained elevated since late 2021. The World Bank commodity price indices for energy and fertilizers have more than doubled compared to the levels in 2019, while the price indices for edible fats and oils and for grains remain 60 percent above 2019 levels. In addition, major global economies are slowing down: in the U.S. and Europe due to sentiment shifts related to the Russia-Ukraine war and rising inflation, and in China due to continued COVID-19 related lockdowns. Heightened global uncertainty and monetary tightening by advanced economies have led to capital outflows from regional economics and, thus, exacerbated balance of payments tensions.

Figure 11: Commodity price indices

(Index value, average 2011-2019=100)



Source: South Asia Economic Focus, October 2022

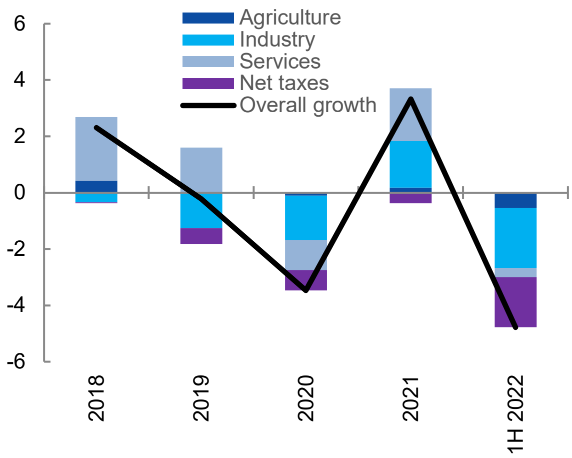
As South Asia trudges ahead on the road to recovery, the region faces extremely difficult economic challenges. Internally, economies are weighed down by scars from the COVID-19 pandemic, as supply bottlenecks and uncertainty over asset quality deterioration in the financial sector persist. Externally, all challenges manifest as balance of payments problems. Elevated global food and energy prices, as well as trade restrictions imposed in response, have led to broad-based increases in domestic inflation, contributed to food insecurity in the region and, together with recovering domestic **demand,** have raised **import** bills for all South Asian countries.

A slowdown in the global economy has reduced momentum in the region's export growth, contributing to trade imbalances and balance of payment pressures. Falling or stagnating **remittance** inflows through official channels may have worsened the situation further for countries that depend on remittances. Heightened uncertainty in the global markets, together with monetary tightening in advanced economies, have shifted investor sentiment and increased net **capital** outflows from the region in the first half of 2022, exacerbating balance of payments pressures. In turn, these pressures have resulted in dwindling foreign exchange reserves and led to requests by Sri Lanka, Pakistan, and Bangladesh to the IMF for support. Countries have also resorted to restrictive measures to curb imports, but with potentially detrimental effects for economic recovery.

Source: South Asia Economic Focus, October 2022

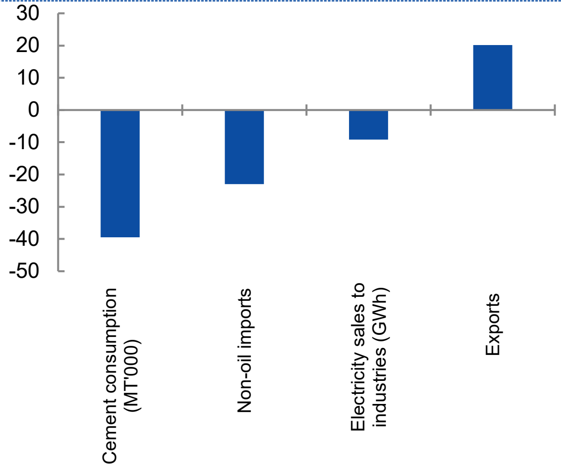
7. **Several leading indicators showed a significant deterioration of economic activity (Figure 13).** Electricity sales to industry sectors in the second quarter of 2022, declined by 9.2 percent (y-o-y), due to rolling power cuts. In May 2022, the monthly cement consumption reached a five-year low (excluding April 2020 during which the country was fully locked down due to COVID-19). Overall, cement consumption contracted by 40 percent (y-o-y) in the second quarter of 2022 amid decelerating construction activity. Purchasing managers' indices (both manufacturing and services) have also significantly deteriorated since the end of the first quarter. In contrast to this general deterioration, the export sector continued to perform well in the first half of 2022 as exporters were able to source inputs with export earnings while demand for Sri Lanka's textiles remained robust.

Figure 12: Contributors to growth (production side)
(Percentage point contribution)



Source: Department of Census and Statistics; World Bank staff calculations

Figure 13: High frequency indicators (Q2 2022)
(Percent, y-o-y growth)



Source: Central Bank of Sri Lanka; World Bank staff calculations

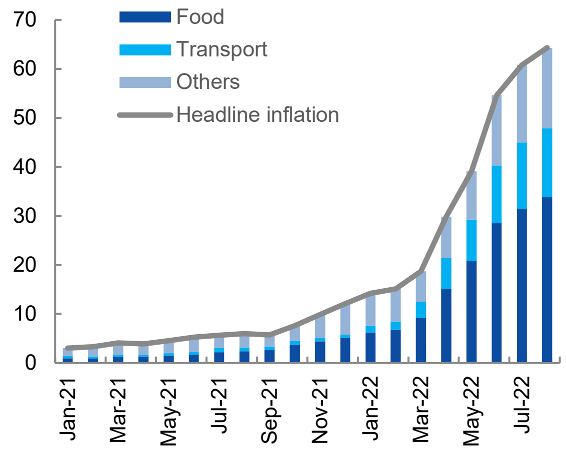
8. **Despite removing the ban on agrochemicals since November 2021, fertilizer remains scarce due to forex shortages, which constrains the productivity of agriculture and related manufacturing sectors**. This ban to dismantle the established system of conventional agriculture within a short period, hit an economy already affected by the global pandemic. While there are few quantitative assessments of the exact impact, various stakeholders have predicted yield drops of 20–50 percent in 2022 for major crops such as paddy, vegetables and other food crops. As a result, this drop in productivity is leading to high levels of food insecurity, as well as income losses for over a million small farmers and agricultural workers who now live on the brink of poverty. While the ban was removed, the supplies are yet to recover amid the forex shortages in the market.

Inflation reached historic highs, prompting a tightening of monetary policy

9. **Headline inflation, measured by the Colombo Consumer Price Index (CCPI, 2013=100), reached an unprecedented level of 64.3 percent (y-o-y) in August 2022**. This was largely due to high food (93.7 percent) and transport (148.6 percent) inflation (Figure 14). The ban on agrochemicals impacted domestic food prices through reduced productivity and increased cost of fertilizer in the informal market. The pass-through of global oil prices, with the implementation of a fuel price formula since March 2022, raised prices across sectors, particularly for transport. The impact of high global commodity prices, partial monetization of the fiscal deficit, and currency depreciation also contributed to rising inflation. Core inflation (computed excluding food and energy prices) was 46.6 percent (y-o-y) in August 2022. The National Consumer Price Index (NCPI, 2013=100) shows a similar trend to the CCPI.

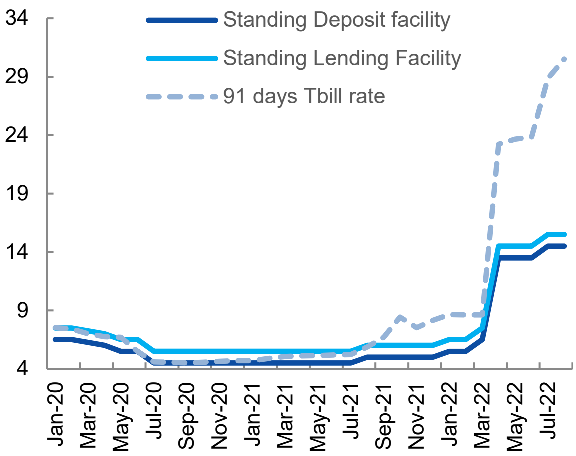
10. **Rising inflation prompted the Central Bank of Sri Lanka (CBSL) to tighten monetary policy.** Since July 2021, CBSL has increased policy rates by 1,000 basis points (Standing Deposit Facility to 14.5 percent and Standing Lending Facility to 15.5 percent) and the statutory reserve ratio by 200 basis points to mitigate the inflationary pressures (Figure 15). This policy rate tightening includes a 700-basis point increase in April 2022 and a 100-basis point increase in July 2022, after the government requested IMF support. As real interest rate remains negative with high levels of inflation, further tightening of monetary policy is warranted. Already interest rates on Treasury bills have increased over and above policy rates, for example, 91-days Treasury bills were auctioned at above 30 percent in the primary market in August 2022.

Figure 14: Contributors to CCPI inflation
(Percentage point contribution/percent, y-o-y growth)



Source: Department of Census and Statistics; World Bank staff calculations

Figure 15: Policy rates and 91 days T-bill rate
(Percent)



Source: Central Bank of Sri Lanka

Financial sector stability is being severely tested by the ongoing crisis

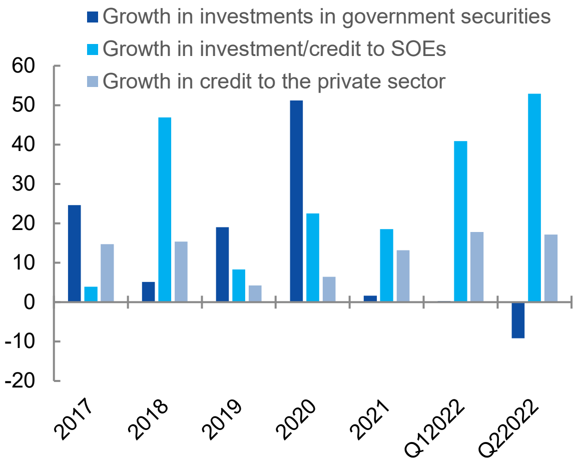
11. **Current financial stability concerns revolve around an acute foreign exchange liquidity shortage and the financial sector's exposure to the distressed sovereign.** While credit to the government from commercial banks slowed down (Figure 16), banks substantially increased financing of distressed State-Owned Enterprises (SOEs), by 52.9 percent (y-o-y) in June 2022. Since 2021, private credit started reviving, with growth reaching 17.1 percent (y-o-y) in June 2022. However, there was a substantial slowdown in private credit growth in the second quarter of 2022 on a month-on-month basis. Despite these changes in credit dynamics, the commercial banks' exposure to the sovereign and SOEs remains high (33 percent of total assets), with losses on these exposures yet to be recognized. State-owned banks are particularly affected, with exposures exceeding 50 percent of total assets. Furthermore, the financial sector has been affected by acute foreign exchange shortages, as sovereign credit downgrades have led overseas creditor banks to cut down swap lines to SL banks and CBSL's foreign reserves reached a low point, affecting its capacity to provide forex liquidity to the banking sector. In contrast, the shortage of LKR in the financial sector has been covered by injecting liquidity through the overnight Standing Lending Facility window – this has been rapidly scaled up since August 2021.

12. **Banks are facing elevated asset quality pressures and thinning capital buffers.** During the first quarter of 2022, banks reported non-performing loans ratio of 8.4 percent. Capital also deteriorated, with the capital adequacy ratio decreasing from 16.5 percent end-2021 to 15.1 percent in the first quarter of 2022 (Figure 17). Of greater concern, however, is that reported indicators of financial strength are likely overstated due to COVID-related forbearance measures being in place for some sectors and on a case-by-case basis,[10] as well as unaccounted losses on banks' SOE and sovereign portfolios. To further mitigate pressures on the financial sector, CBSL reintroduced moratoria on debt repayment for all sectors (in July 2022) and introduced other flexibilities (in May 2022).[11] Notwithstanding these efforts, higher interest rates and the overall challenging economic environment in Sri Lanka will likely result in a further deterioration in the health of the financial sector.

[10] For example, the moratorium on the tourism sector was extended by end-June 2022 (as per Circular No10 of 2021, September 2021). Recovery actions were deferred by end-March 2022 (as per Circular No13 of 2021, December 2021).

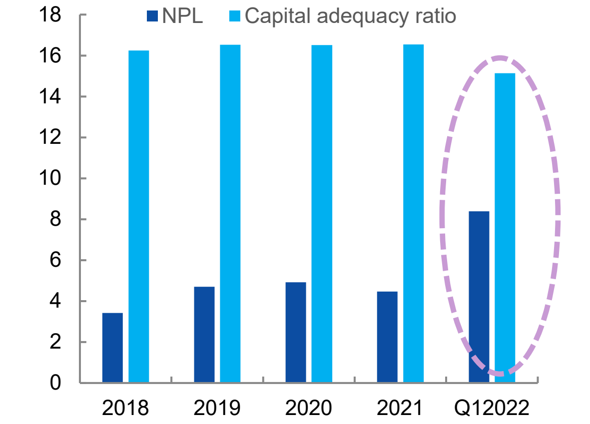
[11] Apart from restricting discretionary payments, the CBSL extended the deadline for enhancement of minimum capital requirements to end-2023, introduced flexibilities to recognize losses on government securities, relaxed liquidity requirements, and allowed banks to draw down the Capital Conservation Buffer (CCB) (as per Circular No2 of 2022, July 2022). Moratorium on all economic sectors on a case-by-case basis was reintroduced until end-2022 (as per Banking Act Direction No4 of 2022, May 2022).

Figure 16: Credit by sector
(Percent, y-o-y growth)



Source: Central Bank of Sri Lanka; World Bank staff calculations
Note: (i) Figure 16 reports credit by licensed commercial banks; (ii) For Q12022, Figure 16 reports impaired assets/Stage 3 loans as NPLs. The numbers might not be directly comparable, as normally impaired assets/Stage 3 loans include impaired restructured loans and certain other risky exposures not included as non-performing loans.

Figure 17: Banking sector performance
(Percent)



Source: Central Bank of Sri Lanka; World Bank staff calculations

13. **The stock market has been highly volatile in response to the political and economic uncertainties, with some revival seen recently.** The market had been in decline and volatile since mid-January 2022, with the All Share Price Index (ASPI) falling by 36.8 percent in the first seven months of 2022. Since then, the market has begun to stabilize, with ASPI slowly recovering and excessive market turnover moderating. Net foreign capital outflows from the stock market slowed down in the first quarter of 2022 and there was a net foreign capital inflow of about US$1.5 million in the second quarter of 2022.

External sector performance remained weak

14. **The goods trade deficit declined by 18.6 percent (y-o-y) in the first half of 2022, as exports grew faster than imports. Yet, this did not prevent a widening of the current account deficit.** Despite the weak performance of tea exports – which experienced productivity losses due to input shortages – goods exports grew by 14.3 percent to US$ 6.5 billion, driven largely by the robust performance of textiles (Figure 20). The total import bill (US$ 10 billion) remained at the level of the first half of 2021, as a 44.6 percent increase in the fuel bill was offset by a reduction in imports of consumer and investment goods. Despite limited foreign exchange in the domestic market, Indian support of approximately US$ 3.8 billion[12] helped Sri Lanka finance its imports in the first half of the year. Remittances declined by US$ 1.5 billion, which was only partially offset by the recovery in tourism receipts from a very low base. Overall, the current account deficit is estimated to have widened in the first half of 2022. This widening may slow down or reverse in the next six months. Reduced demand for imported goods amidst high LKR prices, limited trade financing and import restrictions[13] is expected to lead to import compression in the remainder of the year. Already, imports contracted by one fourth in June and July 2022 on a y-o-y basis. While the correction of external imbalances is largely expected through import compression in the short term, declining growth contribution of exports over the last two decades warrants urgent trade policy and administrative reform to enhance export competitiveness to raise and sustain growth over the medium term (Box 2).

[12] Indian financial support includes: (i) a currency swap of US$ 400 million; (ii) deferment of Asian Clearing Union (a regional trade netting arrangement) payments of US$ 1.9 billion; and (iii) credit lines worth US$ 1.5 billion.
[13] During 2022, the government introduced several import restrictions, including additional duties, surcharges, licensing requirements and temporary suspensions. The items covered under these restrictions included dairy products, fish and meat items, fruits, household equipment, computer accessories, sweets and chocolates, beer and tobacco, cosmetics, other personal care items, textiles, footwear, sports equipment, ceramics and electrical appliances.

Box 2: Turning on all the engines of growth

A more outward looking Sri Lanka will be crucial to speed up economic recovery. Sri Lanka has become more inward looking over the past two decades. An increase in trade barriers led a decline in the share of exports in GDP, which fell from 39 in 2000 to 17.7 in 2021, and with it, the contribution of exports to overall growth fell. Between 2010 and 2020, export growth accounted for 11 percent of the total growth. Between 2015 and 2020, export growth accounted for only 7.6 percent of the total growth. Sri Lanka has the potential to turn the export engine on, reverse the inward turn, and accelerate growth.

Sri Lanka's untapped merchandise export potential is estimated at US$10 billion annually. This results from comparing actual merchandise export levels with the potential that emerges from the estimation of a gravity model of trade.[14] Given Sri Lanka's observable characteristics, it is estimated that the untapped export potential stands at US$10 billion annually. Tapping into the potential is not unrealistic. Indeed, earlier in the century, Sri Lanka was exporting at potential. The increase in missing exports is a relatively recent phenomenon (Figure 18).

The largest portion of untapped export potential lies in Asia (Figure 18). Seventy percent of 'missing exports' for Sri Lanka are accounted for five destinations: China (US$3.5 billion), India (US$1.5 billion), Japan (US$1 billion), Indonesia (US$0.7 billion) and Korea (US$0.5 billion). Missing exports are mostly in manufacturing, and particularly in machinery, equipment, and chemicals. They are also in foodstuffs, wood, or animal products. Consistent with the historical pattern of specialization, clothing exports are substantially above potential (Figure 19). Yet, this does not imply that the clothing sector faces a ceiling for exports as suggested by the model. FDI, innovation and productivity upgrading will help the sector to continue outperform the model.

Figure 18: Sri Lanka's Missing Exports – A Recent Phenomenon (2000 – 2020)

(US$ million)

Source: World Bank staff estimates

The opportunity cost of Sri Lanka's 'missing exports' is estimated at 142,500 jobs in the export-oriented sector. The merchandise export sector in Sri Lanka could create an additional 142,500 jobs if the export potential is tapped into. Of these, 19,000 jobs are in agriculture, and 123,500 jobs in manufacturing.[15] Some of these jobs could be newly created, while others may imply the reallocation of labor from relatively lower productivity, domestic oriented firms, to higher productivity, export-oriented ones.[16]

To tap into the potential, Sri Lanka needs to make exports a policy priority.

- **Negotiate deep agreements with high potential trading partners.** Preferential trade agreements that go beyond tariff reductions and cover provisions on services trade, investment, trade facilitation and the harmonization of standards, have proven effective tools to boost exports. Yet, Sri Lanka only has (shallow) trade agreements with India and Pakistan, one that covers investment, services, and other provisions with Singapore, and it is also negotiating another agreement with China. Sri Lanka is also a member of the South Asia Free Trade Agreement (SAFTA).
- **Reduce the anti-export bias of trade policy.** Sri Lanka ranks among the top 5 of most protected economies in the world in terms of import duties on consumer goods. High trade protection incentivizes domestic firms to sell in the domestic market rather than in global markets as it makes it more profitable. Reducing effective

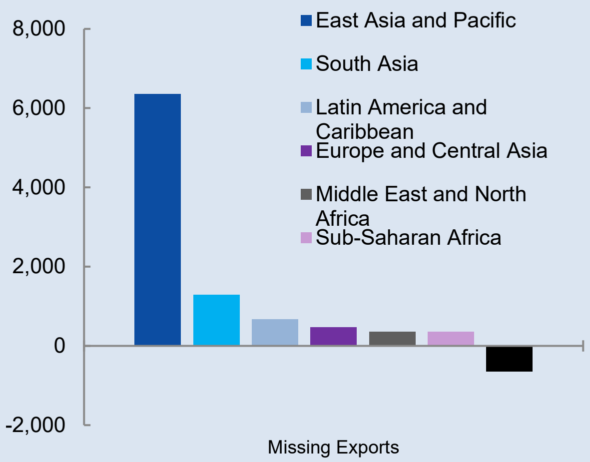
[14] For a detailed description of the methodology of estimation of export potentials, see Mulabdic, A. and Yasar, P. (2021). Gravity Model-Based Export Potential: An Application to Turkey. Policy Research Working Paper No. 9557. World Bank, Washington, DC.
[15] Cali, M. et al (2016). The Labor Content of Exports Database. Policy Research Working Paper; No. 7615. World Bank, Washington, DC, The elasticity of jobs with respect to exports is obtained from the "Jobs Content of Exports" (JOCEX) dataset. The JOCEX dataset uses global input-output tables and aggregate data from the Global Trade Analysis Project (GTAP), to calculate the number of jobs embedded in exports for 65 countries and 11 sectors.
[16] Export oriented firms in Sri Lanka are likely substantially more productive than comparable domestic oriented firms. This is a pattern observed across the world.

rates of protection will create incentives for firms to go global. It will also incentivize FDI in export-oriented rather than in market seeking segments.

- **Reduce barriers to FDI, particularly in efficiency enhancing sectors.** FDI inflows are crucial to build an export base and better integrate into global value chains. Barriers to FDI, such as placing equity limits for foreign investors in specific sectors, such as logistics, limit the extent of competition and innovation in the sector, thus increasing the costs that domestic firms face to export and reducing their competitiveness.
- **Invest in smart export promotion and branding.** Smart export promotion reduces the 'discovery' costs that the potential exporters face. Regularly updated trade information portals as well as matchmaking services to connect global buyers with local sellers have proven helpful in export promotion. Branding also matters if it increases the willingness to pay of global clients. A geographical indication for Ceylon tea, just like it was obtained for Ceylon Cinnamon in February 2022, could be a path to increased value added.

Figure 19: Most of the untapped potential lies in the region

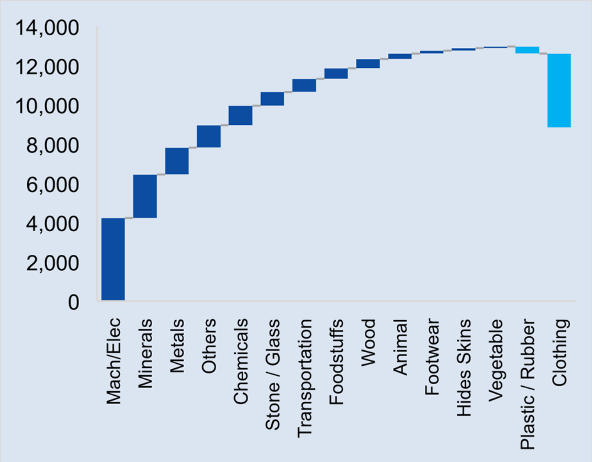
(US$ million)



Source: World Bank staff estimates

Figure 20: All sectors show untapped export potential except for clothing and rubber

(US$ million)



Source: World Bank staff estimates

Source: Staff elaboration

Foreign exchange and official reserves dried up leading to a debt suspension

15. **Official reserves declined to critical levels.** Without foreign exchange inflows amid lost market access,[17] Sri Lanka continued to service its external debt[18] and pay for imports using official reserves and foreign assets of the banking sector. Moreover, the exchange rate was kept broadly fixed at an unsustainable level from August 2021 to March 2022 through market interventions and moral suasion. As a result, gross international reserves declined from US$ 7.6 billion (end-2019) to US$ 400 million[19] (end-2021), a level equivalent to approximately a week of imports. In April 2022, the government acknowledged that usable reserves were almost fully depleted. To help address this liquidity shortage, CBSL floated the currency on March 7, 2022 but returned to a managed float on May 12, as the LKR depreciated by about 78 percent over only two months.[20] Loss of market confidence has made it difficult to bring back export earnings and remittances to Sri Lanka, particularly through formal channels, despite tighter foreign exchange controls, and mandatory repatriation and conversion rules imposed by CBSL.[21]

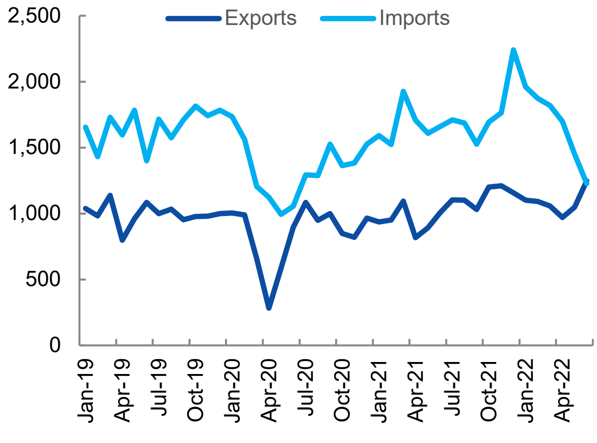
[17] Following the 2020 downgrades, further downgrades took place in 2021: (i) Moody's to Caa2 in October; and (ii) Fitch to CC in December. In 2022, the country's rating was downgraded to default category.
[18] Including a US$ 500 million Eurobond payment in January 2022.
[19] Excluding the currency swap with China.
[20] The LKR has depreciated against the US$ by 80 percent year-to-date.
[21] Main exchange controls include: (i) a repatriation requirement for exports of goods and services; (ii) a surrender requirement for exporters on proceeds from exports of goods and services; (iii) a surrender requirement for banks on purchases of export proceeds; (iv) a surrender requirement for banks on purchases of inward worker remittances; (v) suspension of outward remittances on capital transactions; (vi) restrictions on purchases of Sri Lankan ISBs by local banks; and (vii) restrictions on outward transfers of funds for emigrants.

16. **Facing unsustainable debt and critically low reserves, the government suspended external debt service payments from April 12, 2022.** The suspension includes: (a) outstanding Eurobonds; (b) bilateral credits, excluding swap lines between CBSL and foreign central banks; and (c) foreign currency-denominated loan agreements or credit facilities with commercial banks or institutional lenders for which the government has provided a guarantee. Following the debt service suspension, S&P cut Sri Lanka's sovereign rating to 'selective default'. Since then, Sri Lanka has defaulted on a Eurobond of US$ 1 billion and other coupon payments and, as a result, the sovereign rating has been further cut by Fitch to 'restricted default'. Legal (Clifford Chance) and financial (Lazard) advisors to support the debt restructuring process were appointed in May (Refer paragraph 22).

17. **The impact of the foreign exchange liquidity crisis is being felt across the economy, even as the government tries to control external outflows.** Depleted net foreign assets in the banking system, already at US$ -5.9 billion in June 2022 (Figure 22), reflects increasing challenges to meet the demand for foreign exchange needed for economic activity and day-to-day living. As a result, sporadic shortages of fuel, cooking gas, milk powder, and wheat flour have caused severe socio-economic disruptions. Most economic sectors have experienced shortages of intermediate goods, such as cement, agrochemicals, machinery parts and other industrial inputs. The health sector is also experiencing a shortage of important medicines. As episodes of limited fuel supply caused a crippling effect on transport and economic activity, caps were imposed on the volume that can be purchased at fuel stations based on vehicle category (three wheelers, motorcycles, and cars), and a Quick Response (QR) code system was introduced to ease long queues at fuel stations. Rolling power cuts have also been implemented across the country due to insufficient fuel to generate electricity – although falling demand for electricity amidst suppressed economic activity and increased hydro capacity have reduced pressure on thermal power generation requirements since April 2022. In the absence of fresh capital and financial inflows, tighter foreign exchange measures were put in place, including through mandatory conversion of foreign exchange inflows (exports and remittances) and import prioritization and rationing.

Figure 21: Monthly merchandise trade

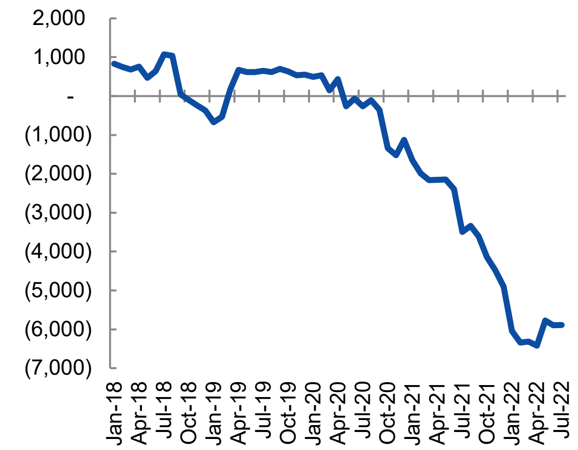
(US$ million)



Source: Central Bank of Sri Lanka

Figure 22: Net foreign assets in the banking system

(US$ million)



Source: Central Bank of Sri Lanka; World Bank staff calculations

Initial reforms have been announced to reverse the continually high fiscal deficits

18. **The fiscal deficit, in nominal terms, remained broadly unchanged in the first four months of 2022 and continued to be largely financed by CBSL.**[22] Primary expenditures (expenditure minus interest payments) increased by 14.4 percent, in nominal terms, due to additional livelihood support to beneficiaries of social protection schemes, public servants and pensioners; it was announced in January (Table 1). The primary deficit, however, has declined compared to the same period in 2021 due to a significant increase in nominal revenues. The revenue increase was largely driven by increased consumption-based tax (reflecting high inflation) and one-off measures introduced in the final 2022 Budget. The collection of surcharge tax in April 2022, a one-off tax on large taxpayers, and central bank profit transfers increased revenues by 30.9 percent in the first four months of 2022, compared to the corresponding period of 2021. Despite a reduction in the primary deficit, the overall deficit remained broadly unchanged, in nominal terms, due to the rising interest bill. As a share of GDP, however, the deficit is estimated to have declined as nominal GDP is expected to have increased along with a higher level of inflation. The deficit was mainly financed by CBSL in the first four months of 2022, largely through purchase of Treasury bills in the primary market.

Table 1: Budget outturn – January to April

LKR million	2021	2022	Change (percent)
Revenue and Grants	**482,289**	**631,129**	30.9
Revenue	481,722	630,908	31.0
Tax revenue	427,261	543,649	27.2
Income tax	55,245	149,163	170.0
Domestic consumption based tax	145,305	180,091	23.9
Import based tax	200,710	203,582	1.4
License taxes and others	26,000	10813	(58.4)
Non Tax Revenue	54,461	87,259	60.2
Grants	567	221	(61.0)
Expenditure	**1,002,832**	**1,155,229**	15.2
Recurrent	890,085	1,016,810	14.2
Salaries and Wages	274,044	316,051	15.3
Pension Payment	87,345	99,659	14.1
Interest Payment	366,240	426,786	16.5
Other	162,455	174,313	7.3
Capital expenditure and net lending	112,748	138,419	22.8
Primary balance	**-154,303**	**-97,314**	(36.9)
Overall balance	**-520,543**	**-524,100**	0.7
Financing	520,543	524,100	0.7
Foreign Financing	16,994	-126,985	(847.2)
Domestic Financing	503,549	651,084	29.3

Source: Ministry of Finance

19. **The government announced several revenue mobilization measures on May 31, 2022, to reduce the fiscal deficit.** These measures included: (i) raising the marginal personal income tax (PIT) rate and reducing the tax-free allowance; (ii) raising the standard corporate income tax (CIT) rate from 24 to 30 percent and removing some tax holidays; (iii) raising the standard value added tax (VAT) rate from 8 to 12 percent, lowering the VAT registration threshold, and removing some VAT exemptions; and (iv) reinstating the mandatory withholding of income tax. The VAT rate hike took effect on June 1, while the income tax rate hikes are expected to be implemented on October 1, subject to parliamentary approval.

[22] In 2021, the fiscal deficit increased to 11.6 percent of GDP from 10.5 percent in 2020 on account of weak revenue collection (8.3 percent of GDP in 2021), reflecting the continuing impact of the pre-pandemic tax cuts implemented in December 2019 and the lasting impact of the pandemic on economic activity. Without access to international financial markets, the fiscal deficit was mostly financed by domestic resources, mainly by the CBSL

20. **The parliament passed an interim budget in September for the remainder of 2022, which included additional measures to reduce the fiscal deficit and address certain causes and outcomes of the crisis.** The interim budget, which revised the final 2022 Budget that was approved in January 2022, included an additional VAT rate hike from 12 to 15 percent and several other policy announcements, such as trade and investment reforms, SOE reforms, introducing several important legal frameworks, establishing a national debt management agency, and improving social welfare systems (Table 2).

Table 2: Key highlights/proposals of the interim budget

Area	Proposal
Macroeconomic framework	• Increase revenue to around 15 percent of GDP by 2025 • Target a primary surplus of more than 2 percent of GDP in 2025 • Reduce public sector debt from around 110 percent of GDP as at end-2021 to no more than 100 percent of GDP in the medium term • Bring back inflation to mid-single digit levels gradually and reduce interest rates • Return to a growth path of 5 percent over the medium-term • Develop a more prudent and evidence-based prioritization mechanism for capital expenditure projects
SOE reforms	• Establish a "State-Owned Enterprise Restructuring Unit" • Re-activate the Statement of Corporate Intent (SCI) process • Allotment of 20 percent shareholding in state banks to the depositors and staff of those banks to meet recapitalization requirements
Debt management	• Establish a National Debt Management Agency under the Treasury
Trade and investment	• Phase out para-tariffs gradually and implement a trade adjustment program • Support the National Export Strategy formulated in 2018 • Resume efforts to engage in regional trade agreements • Establish a National Agency for Public Private Partnership • Facilitate access to land
Financial sector	• Put in place a Bankruptcy Code
Public sector and governance reforms	• Introduce a Public Finance Management Act (PFM Act) that will include stronger Fiscal Rules • Establish a Parliamentary Committee on Ways and Means to make proposals to raise government revenue • Establish a comprehensive legal framework to strengthen governance and fight corruption • Conduct a work study covering the entire public service to help rationalize number of government employees
Social welfare	• Data collection to establish the social registry • Establish a new mechanism for identifying beneficiaries through objective and verifiable criteria
Other proposed legislative changes	**New laws (details of the content are not yet available)** • Food Security Bill • Public Asset Management Bill • Economic Stabilization Bill • Offshore Economic Management Bill • Public Service Employment Bill • Public Finance Management Bill • Recovery of Possession of the Premises Given on Lease (Special Provisions) Bill • Contributory National Pension Fund Bill • Agency for Overseas Sri Lankans Bill • Bankruptcy Code to reorganize businesses in distress due to indebtedness **Revision of laws** • Agrarian Development Act • Excise Ordinance • Finance Act • Foreign Exchange Act • Termination of Employment of Workman Act

Source: Interim Budget, 2022

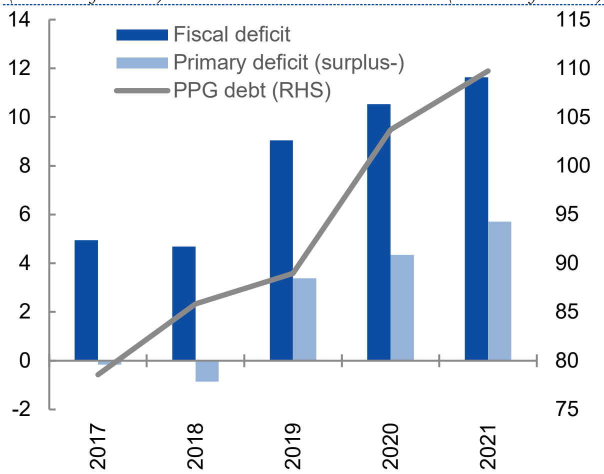
21. **Further actions are needed to bring the fiscal path to a sustainable trajectory.** Given Sri Lanka's very low tax-to-GDP ratio, fiscal consolidation efforts will likely be primarily revenue-based. Additional measures to increase revenues and reduce low priority expenditures are needed through the 2023 Budget and subsequent budgets to improve the primary deficit to a surplus of 2.3 percent of GDP by 2025, as announced by the IMF Staff Level Agreement, from a projected primary deficit of around 4 percent of GDP in 2022. Additional revenues could be mobilized from key tax instruments including CIT, PIT, and

VAT by raising rates, minimizing exemptions, and, importantly, ensuring greater contributions from high-income earners. Fiscal consolidation should also be supported by continued progress in revenue administration reforms,[23] expenditure rationalization,[24] and stronger budget formulation and execution procedures.

22. **Debt restructuring is required to bring debt back to a sustainable path.** In 2021, Public Publicly Guaranteed debt rose to 109.7 percent of GDP and government's debt servicing (excluding Treasury bill rollover) reached 163 percent of revenue (Figure 23). Projected gross financing needs[25] (GFN) for 2022 were about 30 percent of GDP at the end of 2021, which is among the highest in emerging markets. Restoring a sustainable fiscal path, therefore, would also require reducing the unsustainable level of debt and debt servicing, and significantly reducing the primary deficit through a fiscal adjustment. The debt management function also needs to the strengthened by establishing the proposed debt management agency and improving: (i) the legal framework; (ii) the debt management strategy; (iii) timeliness and coverage of debt reporting; (iv) cashflow forecasting; and (v) borrowing operations.

Figure 23: Key fiscal balances and debt level

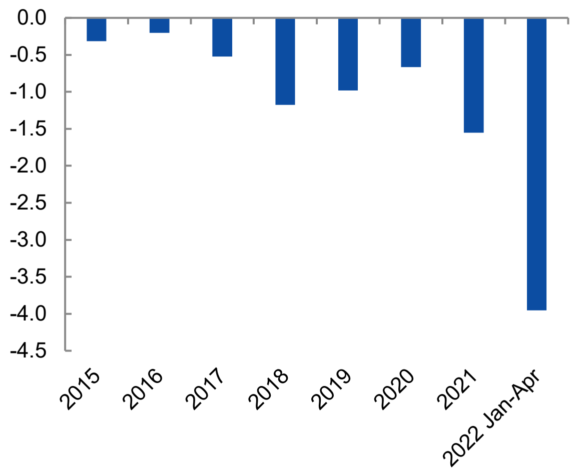
(Percent of GDP) *(Percent of GDP)*



Source: Ministry of Finance; World Bank staff calculations

Figure 24: SOE losses

(Percent of GDP)



Source: Central Bank of Sri Lanka; World Bank staff calculations

23. **SOE reforms are needed to reduce macroeconomic risks.** Several key SOEs have suffered significantly large losses due to a combination of below-cost recovery pricing, operational inefficiencies, valuation loss on foreign currency denominated liabilities amid depreciation, and weak financial management. In 2021, Ceylon Petroleum Corporation (CPC),[26] Ceylon Electricity Board (CEB),[27] and Sri Lankan Airlines (SLAL) incurred a combined operational loss equivalent to 1.6 percent of GDP, and the

[23] Key recommendations: (i) strengthen institutional framework for data sharing; (ii) extend mandatory e-filing of tax returns to individuals initially above 5 million rupees; (iii) expand mandatory withholding and electronic reporting on pay-as-you-earn tax, capital gains, government contracts and rental contracts; (iv) establish the legal framework for mandatory electronic third party reporting on high value transactions; (v) establish a Compliance Risk Management (CRM) unit at the Inland Revenue Department; and (vi) process refunds for individual income tax by crediting them in all cases directly to the bank account of the taxpayer and further giving priority to e-filed returns on issue of refunds.
[24] Key recommendations: (i) develop a reprioritization framework for public investment management (PIM); (ii) develop a PIM component for the new Public Financial Management Act; (iii) formulate PIM guidelines; (iv) develop all project appraisal manuals for key infrastructure sectors; (v) develop the web-based set of national parameters and financial-economic conversion factors that support the uniform application of project appraisal; and (vi) train relevant staff.
[25] The total of overall deficit and amortization payments.
[26] The CPC is the biggest non-financial SOE, with approximately 86 percent of the fuel retailing market share. The CPC Act gives it the exclusive rights to import, export, sell, and distribute refined petroleum products in Sri Lanka, although allows the entrance of a competitor by permission from the minister (this allowed the incorporation of Lanka IOC PLC (LIOC), a subsidiary of the Indian Oil Corporation, to also operate in the market since 2002). While CPC and LIOC both compete in the petrol, diesel, and lubricant markets, CPC has de-facto monopolies in the refining of crude oil and the distribution and supply of kerosene oil, furnace oil, and jet fuel.
[27] CEB has a market share of approximately 70 percent in the electricity generation segment, a monopoly for transmission, and four out of five licenses for distribution. The other license is held by Lanka Electricity Company (LECO), a subsidiary of CEB.

gross outstanding liabilities[28] of these entities were estimated at 10 percent of GDP. The losses of these entities further increased to 4 percent of GDP in the first four months of 2022 (Figure 24). More than two thirds of this loss came from operational losses of CPC due to the large foreign exchange exposure in its balance sheet.[29] Immediate action is needed to restructure key SOEs, improve their governance, and enhance government's oversight role. The implementation of cost-reflective pricing on electricity and fuel in 2022 has been a positive initial reform to reduce losses of SOEs. Moving forward, restructuring balance sheets of CPC, CEB and SLAL will be critical for Sri Lanka's macroeconomic stabilization program.

3. Outlook, Risks and Priorities

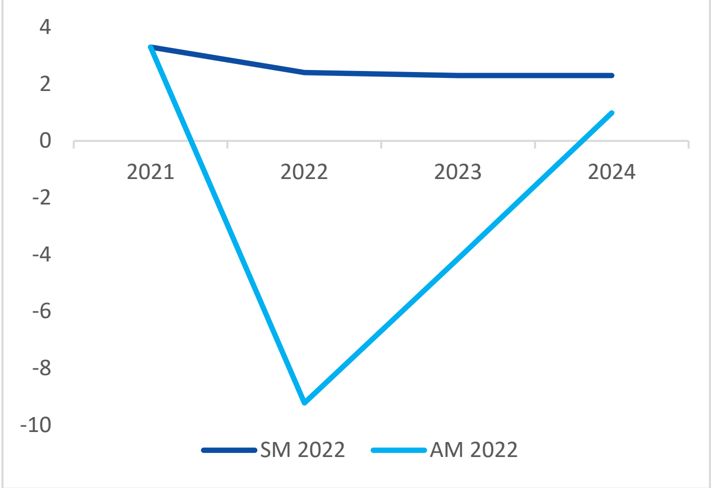
A significant economic contraction is likely in 2022, as the economy undergoes a large correction of fiscal and external imbalances. A strong and credible fiscal and structural reform program is warranted to avoid a prolonged crisis and address the root causes of the current economic difficulties. Firm resolve of political leadership and the Sri Lankan citizens would be needed to overcome the crisis through structural reforms. Meaningful outcomes of debt restructuring, and collective support of international partners would also be needed to maintain the reform momentum and chart the course for a speedy and robust economic recovery with a sustainable growth path.

24. **Significant economic contraction is expected in 2022.** The baseline scenario of the World Bank expects the economy to contract in 2022 (-9.2 percent) and 2023 (-4.2 percent) – as foreign exchange liquidity shortage continues, job and income losses intensify, and supply side constraints adversely affect production. This growth outlook significantly downgrades the World Bank's last projections, reflecting the materialization of fiscal and external risks that were highlighted in the March 2022 Sri Lanka Macro Poverty Outlook (Figure 25). Despite expected further tightening of monetary policy, inflation will likely stay elevated in 2023 due to currency depreciation, high global commodity prices and continued monetization of the fiscal deficit. The fiscal deficit is projected to gradually decline over the medium term, reflecting the revenue mobilization measures announced in 2022 and assuming that additional fiscal consolidation measures will be announced by the 2023 Budget. On the external front, correction of external imbalances is expected on account of exchange rate depreciation and limited supply of foreign exchange liquidity, which will likely lead to significant import compression and improvement in the current account. The gradual revival of tourism will also contribute to the reduction of the current account deficit, while the recovery of remittances is likely to largely depend on how soon confidence in the economy and currency can be restored.

25. **The economic outlook hinges on the pace of fiscal adjustment and the structural reform program, as well as the outcomes of debt restructuring**. The latter will be critical to regaining fiscal and external sustainability and kickstarting economic recovery. Delays in the debt restructuring process could prolong the crisis. Support from international partners for Sri Lanka to implement difficult but required reforms, combined with sufficient financing, would be important to maintain the initial reform momentum and to close the external financing gap.

[28] Gross outstanding liabilities include debt outstanding to banks, project loans from external sources and trade payables.
[29] In the past, CPC did not purchase foreign exchange in the market, but instead borrowed it from state banks to settle fuel bills. This modality led to an accumulation of foreign currency debt on CPC's balance sheet, made CPC vulnerable to currency depreciation through foreign exchange losses, weakened state banks, and contributed to an overvalued exchange rate.

Figure 25: Growth revision – March vs September 2022
(Percent, y-o-y growth)



Source: World Bank staff calculations

26. **The heightened fiscal, external and financial sector imbalances, as well as the fluid political situation, pose significant uncertainty to the outlook.** Additional pressure on foreign exchange liquidity could further restrict the supply of essential goods needed for production and livelihoods, and erode already fragile consumer and business sentiments. Continued shortages of fuel and coal needed for transport and power generation could severely hurt economic activity. Delays in revenue reforms could lead to more pressure on CBSL to monetize the fiscal deficits and, thereby, stoke inflationary pressures. Worse than expected scarring effects of the crisis and slow implementation of stabilization and growth enhancing reforms could contribute to a further deterioration in the medium to long-term outlook. Spill overs from the Russia-Ukraine War and associated sanctions could further increase global commodity prices, disturb supply chains, and adversely impact trade flows. A deterioration of domestic political stability could constrain the government's ability to commit to and implement a strong reform plan.

27. **Sri Lanka needs to implement several important reforms to avoid a prolonged crisis and ensure a future of more equitable and sustainable economic growth and development.** To emerge from the current economic crisis and improve long-term growth prospects, Sri Lanka needs to enhance fiscal and debt sustainability by: (i) strengthening domestic revenue mobilization to reduce fiscal deficits; (ii) rationalizing expenditure and improving budgetary oversight to ensure better development outcomes; (iii) improving debt management transparency and practices; and (iv) addressing fiscal risks associated with SOEs – which includes enforcing cost-reflective utility pricing to limit their losses. These measures need to be accompanied by tighter and more consistent monetary policy to contain inflationary pressures. The financial sector needs to be carefully dealt with, given heightened exposure to the public sector and the impact of the recent currency depreciation on banks' balance sheets. A gradual restoration of a market-determined and flexible exchange rate is required to facilitate external adjustments and rebuild international reserves. Mitigating the impacts on the poor and vulnerable would remain critical during the adjustment period. These reforms and the necessary adjustments may adversely affect growth and poverty initially, but will correct the significant imbalances, and subsequently provide a foundation for sustainable growth and renewed access to international financial markets.

28. **Sri Lanka should use the crisis as an opportunity to build a strong and resilient economy.** The current crisis is not a temporary liquidity shock that can be resolved by external financing support from outside. Instead, the crisis is an important moment to implement deep and permanent structural reforms that may be difficult in normal circumstances. The international episodes of other countries with similar experiences suggest that unless the root causes are addressed, these crises tend to keep reoccurring. To weather the crisis, significant burden sharing by all citizens is also essential. Higher income groups, in

particular, will need to take more of the burden to protect the poor and vulnerable, as Sri Lanka embarks on this journey to emerge from the crisis as a strong and resilient economy.

Table 3: Key Macroeconomic Indicators

	2019	2020	2021	2022 e	2023 f	2024 f
Real GDP growth, at constant market prices	-0.2	-3.5	3.3	-9.2	-4.2	1.0
Private Consumption	3.8	-5.8	6.2	-9.8	-4.0	1.1
Government Consumption	6.6	3.6	3.1	-9.4	-2.2	-2.9
Gross Fixed Capital Investment	-12.1	-9.1	9.6	-16.0	-6.3	1.5
Exports, Goods and Services	1.7	-29.6	10.3	1.8	1.9	2.0
Imports, Goods and Services	-3.5	-20.1	4.1	-9.9	0.4	0.6
Real GDP growth, at constant factor prices	0.4	-3.0	4.0	-9.2	-4.2	1.0
Agriculture	0.5	-1.4	2.5	-9.0	2.4	1.5
Industry	-4.1	-5.3	5.6	-11.2	-5.7	1.0
Services	2.9	-1.9	3.3	-8.2	-4.2	0.9
Inflation (Consumer Price Index)	4.3	4.6	6.0	45.6	23.8	8.0
Current Account Balance (% of GDP)	-2.1	-1.4	-3.8	-1.4	-0.7	-0.4
International poverty rate ($2.15 in 2017 PPP)[a,b]	1.0	1.5	1.5	6.1	6.8	6.7
Lower middle-income poverty rate ($3.65 in 2017 PPP)[a,b]	11.3	12.7	13.1	25.6	28.2	27.7
Upper middle-income poverty rate ($6.85 in 2017 PPP)[a,b]	49.3	50.0	51.2	65.4	67.6	67.3
GHG emissions growth (mtCO2e)	5.2	0.1	4.4	-9.8	-4.7	2.5
Energy related GHG emissions (% of total)	70.2	71.4	71.9	68.8	67.1	67.7

Source: World Bank, Poverty & Equity and Macroeconomics, Trade & Investment Global Practices. Emissions data sourced from CAIT and OECD.
Notes: e = estimate, f = forecast. Poverty data are expressed in 2017 PPP, versus 2011 PPP in previous editions - resulting in major changes. See pip.worldbank.org

(a) Calculations based on SAR-POV harmonization, using 2019-HIES. Actual data: 2019. Nowcast: 2020-2022. Forecasts are from 2023 to 2024.
(b) Projection based on microsimulations for 2020-2022. Projections for 2023-2024 using neutral distribution (2022) with pass-through = 0.87 (Med (0.87)) based on GDP per capita in constant LCU

B. The welfare impacts of the economic crisis and the role of social protection in protecting the vulnerable

The chapter has three main sections: the first presents an analysis of the current crisis on poverty and living standards, then the chapter provides an analysis of the social protection system in country, and its role in difficult times, followed by key recommendations.

1. The impact of the current financial crisis on poverty and living standards

i) In 2021, poverty in Sri Lanka was already elevated due to COVID-19

29. **Sri Lanka's recovery from COVID-19 was uneven and incomplete by 2021, and poverty remained above the pre-COVID-19 level.** The COVID-19 crisis is estimated to have increased poverty in Sri Lanka from 11.3 percent in 2019 to 12.7 percent in 2020 (using the international $3.65 poverty rate, 2017 PPP), a change that translated into over 300,000 new poor people in that year (Figure 26).[30] This increase in poverty was likely cushioned by the substantial expansion in social protection during 2020.[31] By 2021, the economy rebounded, with growth in output in all sectors accompanied by expansion in employment in the services and agricultural sectors.

30. **Employment in the industry sector, however, continued declining, precluding a robust recovery.** A simulation incorporating these changes in employment and labor earnings into household incomes, together with the subsequent withdrawal of the emergency social protection response, shows that poverty in 2021 increased slightly to 13.1 percent, above the pre-COVID-19 and 2020 levels. The average

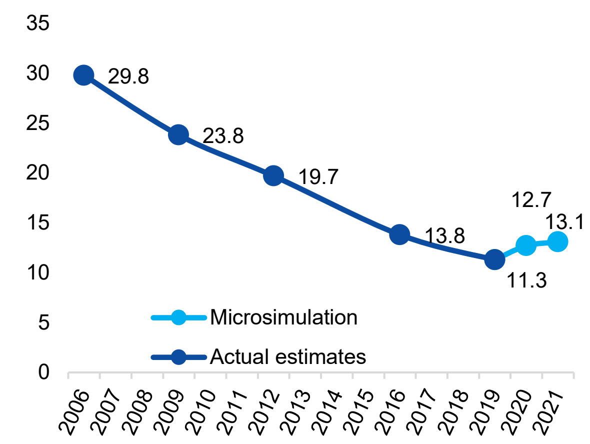
[30] The $3.65 per capita per day (2017 PPP) poverty line is used throughout section 1. A previous estimate, reported in World Bank (2021a) was based on the 2016 HIES and the $3.20 per capita per day (2011 PPP) poverty line. This estimate showed that poverty had increased to 11.7 percent in 2020.

[31] Among roughly 2000 panel respondents to a nationwide phone survey who were interviewed in months September-December 2020, 63 percent reported receiving new or increased assistance since March 2020, of which 71 percent were non-Samurdhi emergency cash transfers. By November-January 2021, the share of people receiving new assistance was 42 percent, of which 71 percent was non-Samurdhi cash transfers (staff calculations based on the SAR COVID monitoring surveys).

distance between the poor and the minimum threshold of consumption measured by the poverty line also increased to 21 percent of the poverty line in 2021. Inequality in expenditures, which had increased between 2019 and 2020, continued to rise slightly to 38.1 Gini points.

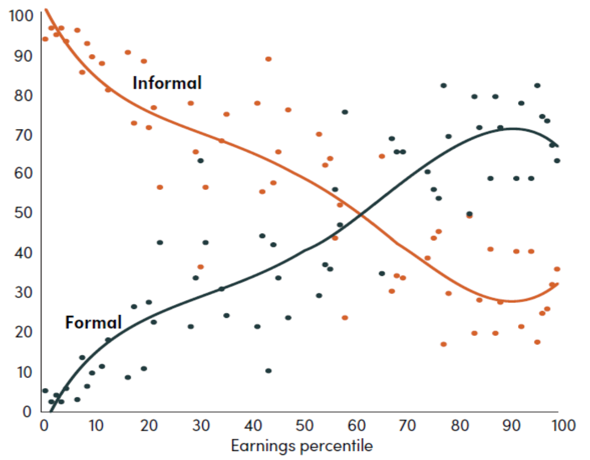
31. **Pre-existing labor market and demographic vulnerabilities continued to affect welfare and may have been exacerbated by COVID-19.** Vulnerabilities that predate the onset of the COVID-19 crisis remained relevant to welfare and may have even worsened by 2021. A large share of workers continued to be engaged in low-productivity jobs, especially in agriculture. The service sector is extremely heterogeneous and comprises both high-skilled workers as well as casual low-skilled workers. Informal workers, many of whom are low-income earners (Figure 27), often do not benefit from social protection. Indeed, those who lost their jobs during 2020 did not have access to job-linked social protection benefits like unemployment insurance (World Bank 2021b). In the context of an aging population, the elderly are also vulnerable to poverty, with limited access to affordable long-term care, pension, and social assistance.

Figure 26: Poverty in 2021 continued above the level observed before the COVID-19 crisis - Poverty rate, 2006-2021
($3.65/day PPP poverty rate)



Source: World Bank staff calculations based on HIES 2002-2019 and LFS 2020-2021

Figure 27: Informality is largely associated with low earnings - Share of workers in informal and formal employment, by percentile of earnings
(Share of workers)



Source: World Bank (2021b) based on LFS 2018 and staff calculations
Note: This figure depicts formality/informality incidence curves by ranking all workers by their earnings from poorest to richest into equally sized percentiles and plotting the share of workers in formal and informal employment within each percentile.

ii) The current economic crisis has had a further and more severe impact on the cost of living and livelihoods

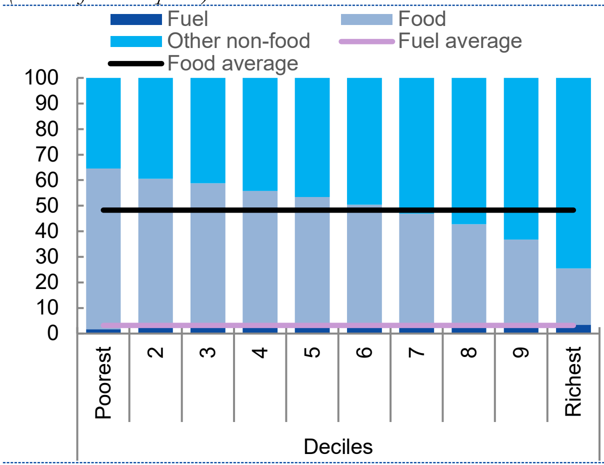
32. **The current crisis is impacting households on multiple fronts, with very limited coping strategies remaining viable to navigate the crisis.** Inflation is eroding their capacity to afford basic items for daily consumption, with potential negative long-term welfare impacts. The shock on the real sector of the economy is also leading to the destruction of employment and a decline in the real value of labor incomes. Due to policies that affected agricultural productivity in 2021 and disrupted flow of remittances to the country, households have been left with levels of income that are insufficient to sustain their usual consumption in real terms. Meanwhile, with limited fiscal space and targeting inefficiencies, the social protection response has been unable to mitigate the massive impacts of the ongoing crisis.

33. **One of the most disruptive impacts on household budgets is the sharp increase in prices.** Driven by global and local factors, the prices of food, gas, and other basic needs have increased substantially, impacting the capacity of households to cover their most essential expenses. The increase in food prices has most severely impacted households at the bottom of the distribution, who dedicate a larger

share of their budgets to food (Figure 28) and is leading to an increase in food insecurity. For instance, it is estimated that the median poor household in 2022 faced an inflation rate of 66.4 percent in the cost of its consumption bundle as opposed to the 56.2 percent inflation faced by the median non-poor household.

Figure 28: The less well-off dedicate a larger share of their consumption to food - Share of fuel and food consumption, by welfare decile

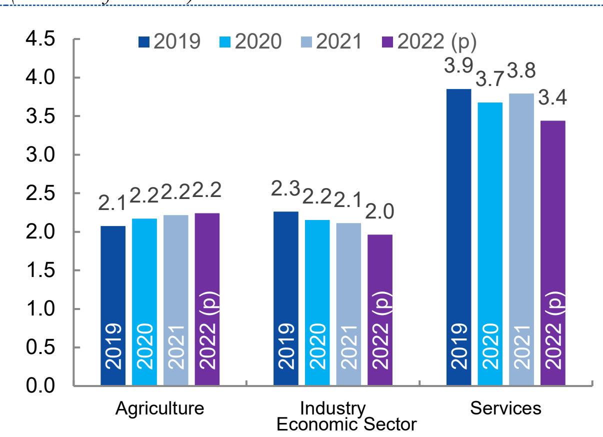
(Share of consumption)



Source: World Bank staff calculations based on HIES 2019

Figure 29: Employment in 2022 is expected to decline in industry and services, while it should marginally increase in agriculture - Employment by economic sector, 2019-2022

(Millions of workers)



Source: LFS 2019-2021. For 2022, projections are based on 2013-2021 growth-employment elasticities by sector

34. **Poor households have to adopt coping strategies (like switching to cheaper products or reducing meal sizes) with potential negative long-term consequences, especially for children's nutrition.** Households dedicated to agricultural activities may have benefited from the increase in food prices, but only 7 percent of households are net sellers of agricultural produce. Moreover, these windfall gains are far from guaranteed, as the distribution chain for agricultural products involves many different actors, so that output price increases are not necessarily passed through to producers. The increase in prices of fuel and non-food consumption has had a more widespread impact across the income distribution, further eroding household purchasing power across the board.

35. **The crisis has led to an economic contraction in all sectors of the economy, resulting in widespread declines in household earnings.** The contraction in output of all sectors of the economy has translated into job destruction (Figure 29) and declines in incomes (in real terms) for workers across the entire income distribution.

36. **The economic sectors could decline by between 8 to 11 percent, depending on the sector.** The industry and services sectors are expected to decline by 11 percent and 8 percent, respectively, in 2022 (Table 3). Based on the sectorial growth-employment elasticities of the last 8 years, this would lead to the overall destruction of over half a million jobs. The agricultural sector, also impacted negatively by the ban of chemical fertilizers in 2021, will also see a decline of 9 percent. In this case, as the agricultural sector plays a role of back-up source of incomes for unemployed workers, employment is expected to increase marginally by close to 1 percent (equivalent to around 25,000 workers), despite the contraction of the sector. However, this employment is of lower productivity and more insecure than the jobs destroyed in the Industry and Services sectors.

37. **While labor incomes have been growing in nominal terms in 2022 for those still employed, if current trends continue, the real value of these incomes can be expected to decline by over 15 percent (compared to 2021) on account of the much higher increases in prices.** Public sector workers, who represent 15 percent of total employment and who received a raise in their nominal salaries of 16

percent in January 2022, can expect the real value of their salaries to decline by over 20 percent in the year if salaries remain at their current nominal level.[32]

38. **Non-labor sources of income have also been impacted negatively, further constraining the ability of households to sustain their levels of consumption.** Remittances from workers abroad, which are a source of income for 7.2 percent of households in the country (4.1 percent of households receive over 25 percent of their incomes from this source), have declined in real terms by close to 30 percent in the first half of 2022, compared to the first half of 2021. Emergency sources of income, such as borrowing or selling assets, have probably increased, as households look for alternatives to compensate for their losses in their income-generating activities. While helpful in the short term, these strategies carry potentially negative impacts for the long term, due to the high interest rates the loans may require and the loss of assets accumulated that can limit the income-generating activities in the future.

39. **Non-monetary aspects of household wellbeing have also been negatively impacted.** The disruption to normal life due to the lack of imported goods (especially fuel), as well as the protests and related security measures, have made it difficult for households to continue accessing basic public services such as education, healthcare, and public administration services. The shortages of imported goods (which prompted long queues to access rationed goods), and the electricity blackouts have disrupted normal economic activities, with impacts on productivity and, ultimately, the ability of workers to generate incomes for their households. All these factors have contributed further to the decline in living standards, with impacts on non-monetary aspects, including curtailing investments in health and education, and pressures on mental and physical wellbeing.

iii) Poverty is estimated to have doubled between 2021 and 2022

Box 3: A microsimulation approach to estimate poverty in 2022

Lacking real-time information about how household consumption has been impacted by the crisis, a microsimulation approach was followed to obtain a first set of estimates for poverty in 2022. The most recent source of information available to calculate household consumption for the country is the 2019 HIES. Given the need to understand the impact of the current crisis, a micro-simulation approach was followed, in the spirit of World Bank (2014) and World Bank (2021a). This approach takes full advantage of the household-level information on different sources of income and prices faced by the households and connects each of them to different indicators of the economy, so that a plausible path for household consumption in 2022 can be obtained. Annex 1 Presents the information used for the calculation in more detail. Alternative approaches based on the historical relationship between GDP, employment, and poverty were also tried, but these required more assumptions to be imposed.

Source: Staff elaboration

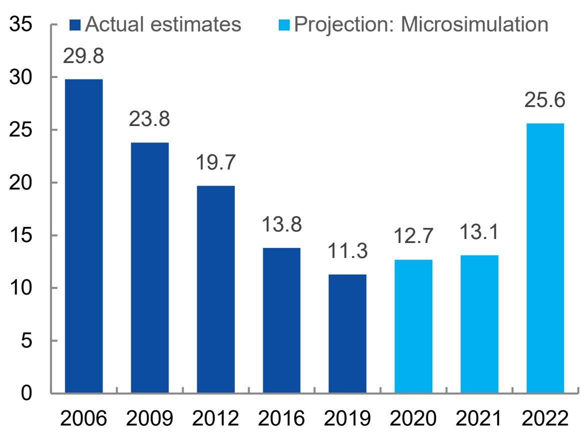
40. **Poverty is expected to increase to over 25 percent in 2022, a doubling of the poverty rate relative to 2021, and reversing the gains of a decade of progress towards poverty reduction.** Results from microsimulations (Box 3) show that the current economic crisis has doubled the poverty headcount for the country, with a point estimate of 25.6 percent (Figure 30) – equivalent to close to 2.7 million people moving below the poverty line between 2021 and 2022. The current crisis has increased poverty in the country to its highest level since 2009 and signifies a reversal of steady welfare gains made between 2006 and 2019.

[32] Estimates of real wages are constructed using projections of nominal wages that maintain the same relative growth to the inflation observed in Jan-May 2022 over the projected monthly inflation until the end of 2022. Nominal wages are expected to move closer to inflation for self-employed and casual workers, compared to salaried workers. https://www.cbsl.gov.lk/sites/default/files/cbslweb_documents/statistics/mei/MEI_202207_e.pdf

41. **Not only are more people living below the poverty line, they have also fallen further in terms of their current living standards relative to the minimum threshold represented by the poverty line.** The average distance between the poor and the poverty line has increased to 27.4 percent of the poverty line in 2022 – up from 18.9 in 2019. This is equivalent to Rs. 202 billion (current) needed to eliminate poverty in the country during 2022 in the form of a direct transfer to the poor. Moreover, while losses in the real value of consumption have been widespread in 2022, these have been more pronounced in the lower part of the consumption distribution, relative to a pre-COVID baseline of 2019 and relative to a more recent baseline of 2021 (Figure 31). This is also reflected in inequality and shared prosperity indicators. The Gini index has increased from 37.7 in 2019 to 39.9 in 2022. Meanwhile, the shared prosperity indicators show that between 2019 and 2022, consumption declined on average 9.5 percent per year for the bottom 40 percent of the population, while it only declined 7.1 percent per year for the top 60 of the population.

Figure 30: The crisis is projected to have more than doubled poverty in 2022 - Poverty rates, 2006-2022

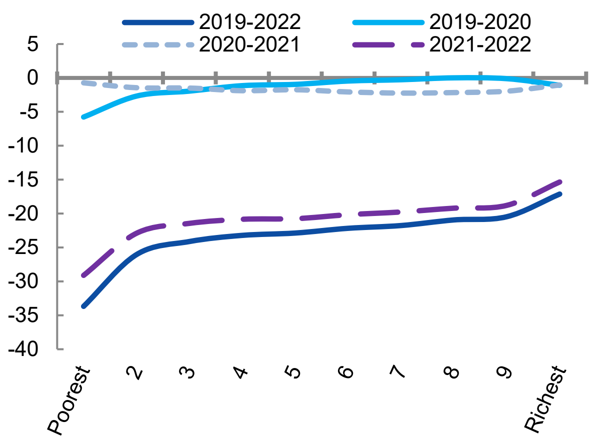
($3.65/day PPP poverty rate)



Source: 2006-2019 based on HIES. 2020-2022 are World Bank staff calculations based on microsimulations

Figure 31: The less well-off have been more severely impacted by the crisis - Change in household consumption, by welfare deciles (2019-2022)

(Percent)

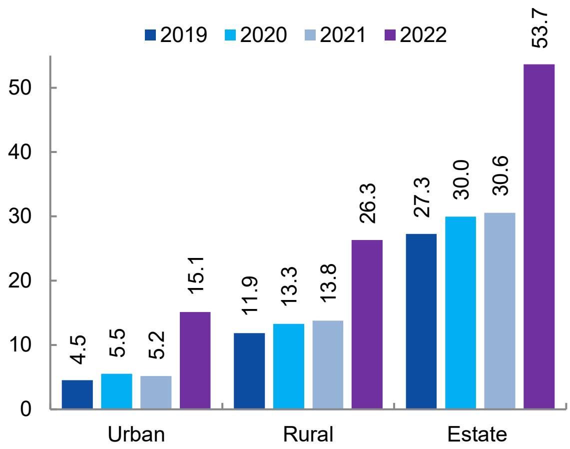


Source: World Bank staff calculations based on microsimulations

42. **The increase in poverty has been widespread across different groups of the population and across all spatial domains, though the crisis has not fundamentally changed the spatial and demographic profile of the poor.** Poverty has increased in urban, rural and estate areas of the country. In urban areas, poverty has more than tripled, albeit from a low base. In estate areas, which were already the poorest, poverty has increased the most in percentage terms, with half of the population living in those regions now falling below the poverty line (Figure 32). In relative terms, the distribution of the poor across the three areas has not varied significantly, though now the share of urban poor is 10 percent, up from 7 percent in 2019. The bulk of the poor still live in rural areas (80 percent), while the estate areas account for an additional 10 percent of the poor. The increase in poverty has been widespread across socio-economic and demographic groups (Figure 33). Poverty has increased more in female-headed households and has doubled across all education levels of household heads. Households headed by someone without complete primary education now have an estimated poverty rate of 42 percent – up from 22 percent in 2019. In households without access to pensions, poverty increased from 12 percent to 27 percent. Households with access to pensions have seen a smaller deterioration in their living standards, probably signaling their relatively more advantaged position in the income distribution. Across districts, Mullaitivu continues to be the poorest (57 percent poverty in 2022), followed by Kilinochchi and Nuwara Eliya.

Figure 32: Poverty has increased in urban, rural and estate areas - Poverty rates by domain, 2019-2022

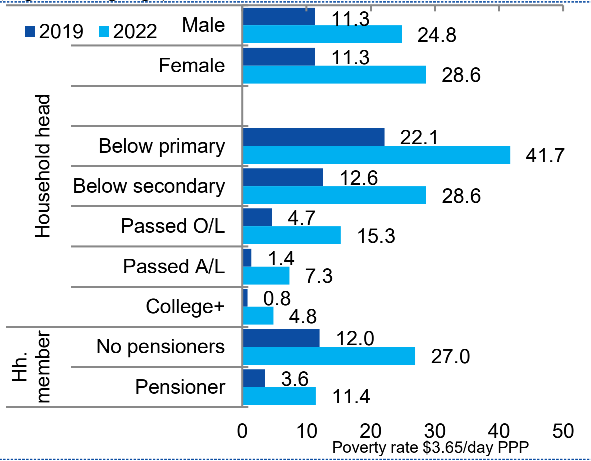
($3.65/day PPP poverty rate)



Source: 2019 based on HIES. 2020-2022 are World Bank staff calculations based on microsimulations

Figure 33: The impact has been widespread across different groups of the society - Poverty rates by group, 2019 and 2022

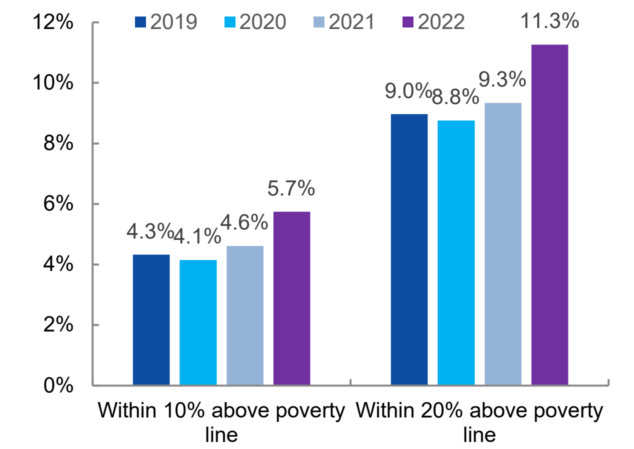
(Population groups)



Source: 2019 based on HIES. 2022 are World Bank staff calculations based on microsimulations

Figure 34: Vulnerability to shocks has increased, particularly in 2022 - Vulnerable population, 2019-2022

(Share of the population)



Source: 2019 based on HIES. 2020-2022 are World Bank staff calculations based on microsimulations

43. **Along with poverty, vulnerability to income shocks has also increased with many non-poor households living close to the poverty line.** The non-poor population living close to the poverty line has risen between 2020 and 2022, with the highest increase observed between 2021 and 2022. It is estimated that aside from the 25.6 percent of the population living below the poverty line, 5.7 percent live less than 10 percent above the poverty line and a further 5.6 percent between 10 and 20 percent above the poverty line (Figure 34). These households are particularly vulnerable to falling into poverty following a negative income shock.

44. **Further analysis will refine these results as more information is available on the labor market impacts and in the light of potential scale up and reforms to the social assistance response.** The analysis presented is driven by the expected dynamics in labor markets, agricultural output, remittances, and social assistance. As more recent information becomes available on employment, wages and salaries, and other economic indicators, a more precise estimation of the poverty rate for 2022 will be possible. In addition, as more information becomes available about the coverage of social assistance emergency response until the end of the year, it will be possible to fine tune the estimates. Finally, the estimates also

rely on projections of the inflation rate for the second semester of 2022. Any departures from these projections can lead to changes in poverty, as the less well-off are the ones who are more heavily impacted by these variations.

iv) Better designed social assistance programs for more effective targeting

45. **The design of social assistance programs needs to be reformed to maximize the poverty impacts of any emergency response.** While the government launched an important emergency effort to mitigate the impacts of the crisis on the most vulnerable in the country, a significant constraint to this effort was the existing design of the social safety net, which relies on cash transfer programs with inefficient targeting and limited benefit amounts (see Section 2 below). According to microsimulations, with its current design and targeting efficiency, Samurdhi assistance has had a poverty-reducing impact of 3.1 percentage points in 2022. In other words, the poverty rate would have been 28.7 percent instead of 25.6 percent in 2022 in the absence of all Samurdhi transfers. Additionally, the aggregate poverty gap, which is the sum of all resources needed to cover the deficit between the expenditures of the poor and the poverty line is estimated to have increased to LKR 248 billion (current) from LKR 202 billion. However, if the budget envelope planned for 2022 for Samurdhi had been directed entirely to the poor, its impact would have been much larger.

46. **While perfect targeting is not achievable, simulations of some hypothetical scenarios clearly highlight the potential for more substantial poverty impact if the existing Samurdhi resources were better targeted towards those in need.** In one scenario, we simulate the poverty impact when the total budget for Samurdhi is used to maximize the impact on poverty, by prioritizing those closest to the poverty line, who would need small transfers, and then moving on to those further away until the resources were exhausted. A second scenario considers the prioritization of those at the very bottom of the welfare distribution, who would receive the largest transfer, and gradually extending benefits to those closer to the poverty line, until all resources were exhausted. Finally, we consider a scenario where the full budget envelope of the Samurdhi program is distributed as an equal transfer to the poor (LKR 929/month per person).

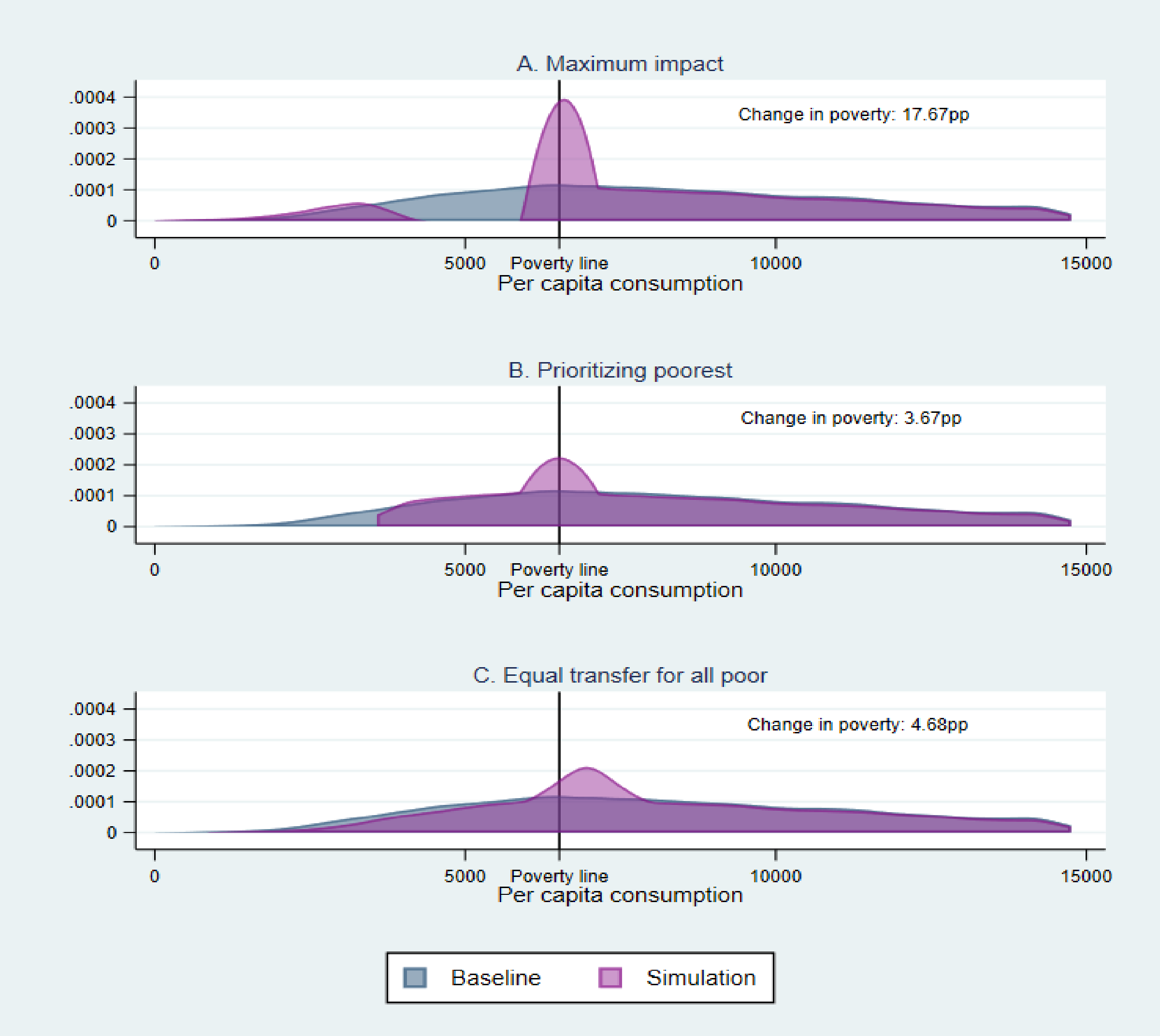
47. **This analysis shows how improving targeting could reduce poverty.** Figure 34 presents the kernel density plots of the consumption distribution of each of these hypothetical scenarios against the baseline for 2022 so that the share of the population moving out of poverty as a result of each change to targeting is represented by the light green areas to the right of the poverty line while the areas to the left of the poverty line shaded in blue represent their original position in the consumption distribution. The first strategy of maximizing the impact on poverty reduction results in the elimination of poverty in all but the lowest 8 percent of the welfare distribution, or in other words, lead to a decline in the poverty rate to 8 percent, with an average transfer of LKR 1270 per person per month (Panel A).[33] The second case of prioritizing the poorest households first involves the largest average transfer of LKR 3906 per person per month and has the smallest impact on the poverty headcount, which is simulated to decline to 22 percent (Panel B). The final scenario of distributing an equal transfer to all poor households results in poverty declining to 21 percent (Panel C).

48. **All these scenarios, while unrealistic in terms of the feasibility of implementation, do highlight that even with existing resources, there is considerable scope for reforming the targeting of social assistance and improving the efficiency and efficacy of social expenditure.** Specifically, these simulations show evidence of a substantial concentration of people living just below the poverty line,

[33] The poorest are excluded from benefits under this (fictitious) scenario because the objective is to reduce the number of households below the poverty line. This means those closest to the poverty line are prioritized first.

who would need a relatively moderate transfer to be lifted out of poverty. On the other hand, the poorest decile of the population lives well below the poverty line and would need a substantially larger transfer.

Figure 35: Reforming the targeting of social assistance could improve the efficiency of social expenditure - Changes to the consumption distribution under different targeting scenarios



Source: 2019 based on HIES. 2020-2022 are World Bank staff calculations based on microsimulations
Note: Density plots are truncated at the 75th percentile.

2. Main features of the social protection system in Sri Lanka and its role in difficult times

Sri Lanka, now more than ever, needs a new approach to social protection. As a result of the Covid-19 pandemic and the economic crisis, poverty rates and vulnerability have increased significantly. As presented in Section 1, social assistance can play a key role in protecting the most in need and partially mitigate the impact of crises. This section reviews the existing social protection system and Section 3 proposes short and medium-term recommendations to protect households against poverty and promote opportunity for all in a riskier environment. The analysis focuses primarily on social assistance cash transfer programs and system strengthening. However, promoting productive inclusion is also key, drawing on lessons learnt from past programs in Sri Lanka and globally.

i) Cash transfer programs played a critical role in protecting the most in need in Sri Lanka

49. **The scope and scale of cash assistance provided since 2020 has been unprecedented.** More than 4.9 million people received a payment of LKR 10,000 during the first COVID-19 lockdown in 2020. Around 1.4 million families received relief payments (or in-kind transfers equivalent to) of LKR 5,000 during the second wave. A total of 27.8 LKR billion was spent on the two COVID-19 lockdown cash transfers. These expenses are in addition to the regular social assistance programs, such as subsidies, free school meals, free education, and health care.

50. **The impact of social assistance could have been even greater with an institutional framework and social registry in place to govern social assistance.** As is discussed further below, the government was limited in the impact of its response by a lack of data on which households were worst affected and the absence of a governing body for social assistance. The Welfare Benefits Board (WBB) – the institution assigned with responsibility for establishing a social registry of households needing social assistance and selection mechanisms for determining their eligibility – was dormant between late 2019 and mid 2022 (Box 4). Assistance was provided based on old records for social assistance (from 2019 or even earlier). This meant that the assistance left out the newly poor (who had not earlier needed assistance) as well as anyone who was eligible but had not applied for benefits or had been denied enrolment and remained on the waiting list for the program. While some efforts were made to assist other households not on the beneficiary rolls or waiting lists, anecdotal reports suggest this effort was not universally effective. Without an updated social registry, the delivery of payments to eligible beneficiaries has been a major challenge.

51. **Looking ahead, changes will be needed to ensure the most needy and vulnerable continue to receive adequate support within the available fiscal envelope, and that the systems are better prepared to respond to future shocks.** The temporary support provided since May 2022 has gone to over 3.2 million beneficiaries. The decision was taken to provide wide-scale support due to limitations in the existing programs, which did not cover many existing and newly poor households and were not equipped to scale up rapidly, and the amount provided higher than standard programs adequacy but still very low in comparison to the needs. While all households have suffered increases in the cost of living due to the economic crisis, a continuation of support at this scale will not be sustainable even as Sri Lanka's fiscal situation improves. Meanwhile, there is also an urgency to reach those who have missed out on assistance under the existing system, due to limited data and weak administrative processes and to review the amount transferred to the most in need in these difficult times. Female-headed households and young children are particularly at risk. Going forward, integrated adaptive social protection with a flexibility to quickly expand coverage will be needed to ensure appropriate and more efficient support to the most in need.

Box 4: Welfare Benefits Board

The Welfare Benefits Act No 24 of 2002[a] was made effective on February 15, 2016[b] to create the Welfare Benefits Board (WBB) under the Ministry of Finance. The WBB consists of a Commissioner of Welfare Benefits and four other members, appointed by the Minister of Finance in consultation with the Constitutional Council for a renewable term of three years.

The WBB assumes the role of beneficiary selection and payment for all social assistance programs. The program administration responsibility lies with the respective line ministry. The WBB will coordinate all activities with the District Secretaries, Divisional Secretaries, and other government officials.

The Legal Draftsman's Office has already drafted the Welfare Benefits Board regulations to facilitate operationalization of the WBB's role in the social assistance landscape.

The program beneficiary eligibility is determined using a set of six objective criteria measured by assessing the status of: (i) education; (ii) health; (iii) economic level (iv) assets; (v) housing condition; and (vi) demography and family conditions which together are used to calculate a multi-deprivation score (MDS)[c]. The Department of Census and Statistics led the development of the MDS.

The WBB also has the power to introduce emergency relief programs arising due to natural or manmade disasters or situations of a temporary nature.

The WBB is also responsible for arbitrating on grievances and appeals from welfare applicants.

References:
a)https://www.lawnet.gov.lk/welfare-benefits-3/;
b)http://documents.gov.lk/Extgzt/2016/PDF/Feb/1952_22/1952_22%20E.pdf;
c)http://documents.gov.lk/files/egz/2019/6/2128-24_E.pdf

52. **A social protection strategy is needed to guide the overall reform.** In addition to articulating the priorities for future program design, targeting, and addressing the above-mentioned gaps, a social protection strategy is also needed to ensure coordination across government. Fragmentation and limited information sharing are currently impediments to effective program implementation and informed planning. A strategy that is broadly endorsed can also guide more carefully crafted and less politicized policy decisions and commit government to allocating the needed resources to ensure programs provide adequate protection and achieve the best possible results.

ii) The main weaknesses of Sri Lanka's social protection system have hindered the full potential of its response

53. **Sri Lanka has aspirations for a strong welfare system that supports vulnerable citizens throughout the life cycle.** Since gaining its independence in 1948 the nation has steadily invested in Social Protection adding new programs to address the needs of different vulnerable groups. As a result, prior to COVID-19 there were 38 state-run social assistance programmes providing either (i) general income support to vulnerable households; (ii) nutrition-related in-kind food assistance; or (iii) support for access to education. There are also several non-contributory cash transfer programmes, run by the Ministry of Women, Child Affairs and Social Empowerment (Annex 2). In addition, The Provincial Councils also run their own public assistance programs, while the Ministry of Disaster Management (MoDM) provides ad hoc assistance in the aftermath of disasters.

54. **The country has an extensive but fragmented social protection system.** Established in 1994, *Samurdhi* is the country's main welfare scheme, providing cash transfers, microfinance, and various community and livelihood development activities. In 2020, the program covered 1.8 million families, or approximately one-third of the population. Samurdhi and its predecessor, *Jana Saviya*, replaced an earlier system based on food stamps. While the transition to cash payments has had benefits for individual choice and reduced wastage (Gentilini, 2014), there are known problems with the Samurdhi program stemming from politicization, lack of exit for graduated beneficiaries, overstaffing and lack of internal control mechanisms (World Bank, 2005). Its coverage is also relatively large compared to the budget, meaning payments to beneficiaries are relatively small. As a result, analysis shows that the program has not had a significant impact on poverty and could be improved significantly.

55. **Samurdhi is complemented by three main categorical cash transfer programs.** These provide modest monthly benefits to: (a) individuals over 70 (Elderly Benefit, or EB), (b) people with disabilities (Disability Benefit, or DB), and (c) people who suffer from chronic kidney disease of unknown cause (CKDU). There are strict limitations on eligibility based on an income threshold, eligibility criteria-based health status, program caps and a cap on one benefit per household. As a result, official waiting lists for the programs are almost as large as the number of beneficiaries, and many more eligible individuals are not even on the waiting list.[34] The country also has a program targeting mothers and young children with nutrition deficiencies, *Thriposha*, a nutrition and in-kind transfer program contributing to life-cycle approach (for more information See Annex 2).

56. **Despite the expansive social assistance, its impact has been questionable due to limited investment in key delivering mechanisms.** Program administrative processes might limit access to

[34] For example, the EB has 417,000 beneficiaries, but 239,000 more who qualify have been on the waiting list since 2019. The situation is similar for the other programs.

assistance. To register for cash transfer benefits, a citizen first needs to apply by supplying supporting evidence to the Divisional Secretary (DS). There is a possibility of excluding any individuals who are marginalized or lack the power to advocate for their needs. Grievance processes are managed at a local level with limited avenues for appeal. There is limited communication and outreach about programs, meaning many citizens may be unaware of the assistance for which they qualify. Budget caps are set and maintained for years at a time which, combined with the lack of exit mechanisms, leads to longstanding waiting lists. Finally, there is limited information transfer from the local administrative level to central government, meaning the actual impact of the programs is hidden and it is difficult to identify and address problems. While these issues are well known, politicization has discouraged successive governments from taking action to improve targeting or registration processes despite sustained efforts of development partners and some in government.

57. **As discussed above, COVID-19 and recent cash transfer crisis responses have been remarkable, with over 5 million beneficiaries receiving support and spending on social assistance over three times pre-COVID-19.** The government expended a substantial budget on mitigating the impact of the pandemic on the poor and vulnerable, tripling the spending on targeted cash transfers. Efforts were carried out mainly through existing welfare schemes such as Samurdhi, EB, DB, and CKDU allowance. The first such programs were implemented across all 25 districts during the first lockdown period, in April and May 2020, and included extending the allowances to wait-listed and newly identified families and individuals, as well as making one-off top-up payments to existing beneficiaries under the Samurdhi, elderly, disabled, and CKDU programs. In addition, for low-income families not covered under the Samurdhi program, cash assistance was provided where one or more members had lost their livelihood directly or indirectly as a result of the pandemic during waves one, two, and three. Following the second wave in October and November 2020, families who were quarantined or in lockdown areas also received an in-kind transfer worth LKR 10,000 (LKR 5,000 per week for two weeks) to strictly adhere to home quarantine rules. A summary of cash transfer programs implemented during COVID-19, expansion of coverage, and increased benefit amount presented in Table 4 (Annex 3 For More details).

Table 4: Summary of cash transfer programs introduced during COVID-19

Program	No of beneficiaries				Benefit amount		Expenditure (for one month) LKR		% GDP	
	Prior to COVID-19	Wait Listed	Newly Identified/ appeals	Total COVID-19 allowance	Existing (LKR)	COVID-19 benefit amount	Prior to COVID-19 expenditure per month (LKR)	Including COVID-19 allowance expenditure (LKR)	Prior to COVID-19	Including COVID-19 allowance
Samurdhi	1,768,600	707,630	728,523	3,204,753	420-3500	5,000	8,843,000,000	7,181,265,000	0.06%	0.048%
Elderly Allowance	417,067	157,805	54,827	629,699	2,000	5,000	836,134,000	2,314,786,000	0.01%	0.015%
Disability allowance	72,000	37,492	14,149	123,641	5,000	5,000	360,000,000	618,205,000	0.00%	0.004%
CKD Patients	25,320	13,348	5,623	44,291	5,000	5,000	126,600,000	94,855,000	0.001%	0.001%
Helpless Community Groups (**first** wave)			1,727,086	1,727,086		5,000		8,635,430,000		0.057%
Helpless Community Groups (**second** wave)			1,343,214	1,343,214		5,000		6,716,070,000		0.045%
Helpless Community Groups (**third** wave)			1,110,792	1,110,792		2,000		2,221,584,000		0.015%
Total	**2,282,987**	**916,275**					**10,165,734,000**	**27,782,195,000**	0.068%	0.185%

Source: Ministry of Finance

58. **To mitigate the impact of the economic crisis this year, cash payments have been provided to all existing and waitlisted Samurdhi, and categorically target cash transfer beneficiaries**. The cash transfer programs to Samurdhi's families, and elders, disabled, and patients with chronic diseases with monthly income less than LKR 6,000 per month covered approximately 3.2 million with existing, waitlisted, and newly identified families. The amounts given to beneficiaries varied depending on: (i) number of family members; and (ii) the current program enrolment status (existing or waitlisted beneficiary). (See Annex 4 for more details.) A summary of programs implementation, expansions and costs is in Annex 4. The cash transfer benefits were initially delivered by using each program's payments existing mechanisms to facilitate a rapid response, and since May 2022 to avoid possible duplication of payments, payments to waitlisted beneficiaries and top-up for all cash transfers programs, via Samurdhi banks. This decision reduced the initial target of beneficiaries and top payments for programs (duplications removed, see Annex 4 For difference between initial target beneficiaries and number of beneficiaries).

59. **The overall social protection system has shown some weaknesses in terms of capacity to rapid scale-up interventions, limited-link to the national Disaster Management framework, and lack of data to enable rapid targeting of shock-affected households**. While the COVID-19 response scaled up existing social assistance programs and their benefit amounts, utilizing existing delivery systems for the respective programs, the scalability and adaptivity challenges of the social protection system of Sri Lanka were evident in its response to the Covid-19 Pandemic. In the absence of a well-functioning social registry, during recent economic emergency and the pandemic, the government response focused on providing funds to existing beneficiaries and used local government agents to identify others in need and adding those who were waitlisted. This process lacks transparency, may miss many households in need, and can lead to significant duplications. Other countries around the world that were able to rely on a well-established social registry could rapidly and more effectively respond to the pandemic and any other crises (Box 5).

Box 5: Investing in effective delivery systems for social protection

Investments to make the delivery systems for social protection programs more efficient include the setup of social registries, investments in management information systems, introduction of digital payments, and increased outreach to vulnerable groups. In particular, social registries collect information on the socioeconomic situation of poor or vulnerable households, thereby providing a central mechanism to identify potential program beneficiaries; they rely on management information systems and can be especially important tools for shock responsive social protection.

Social registries are key building blocks in social protection. They support outreach, intake, registration, and determination of potential eligibility for one or more social protection programs. For example, in Brazil, people can apply for social assistance and be registered in the social registry (Cadastro Único). From that registry, they are assessed and considered for eligibility for numerous social programs. The Cadastro Único currently contains data on more than 74 million citizens and is used by various federal programs, with the largest user program being the conditional cash transfer, Bolsa Familia (Ministerio de Cidadania, Brazil[35]). More than ten years ago, the Cadastro Único was already observed to be a tool that could be widely used due to its three essential characteristics: broad census information (for the poor population), registry data (with identification and address data) and for its broad identification of information about the conditions of these families' lives (Barros, Carvalho, & Mendonça 2009).

The number of countries with effective social registry has grown in the past decade and facilitated significantly the recent pandemic response. Existing information on poor and vulnerable areas and households can facilitate the rapid scale-up of existing programs to new areas that have been affected by a disaster or to non-beneficiary households in the disaster-affected areas. The Listahanan social registry in Philippines is also used to enroll disaster-affected households for a range of new programs, including public works and asset rebuilding. The Listahanan and the Pantawid Pamilya program information system were also used to transfer cash to beneficiaries in affected households by the pandemic and by natural disaster, in addition to the regular transfers. Expanding registries to include geo-referenced household information can provide the informational basis for rapid disaster response.

In order to ensure a rapid response in a time of crisis, counting on adaptive delivery systems would be critical. Having flexible delivery systems in place before a crisis or disaster strikes can significantly reduce emergency response time, by supporting a rapid scale-up of existing programs (e.g., Philippines has the capacity to rapidly expand coverage) or supporting introduction of new programs (e.g., during COVID-19, Thailand set up a new emergency response program).

Source: Authors based on the Ministerio de Cidadania, Brazil and Lindert et al. 2020

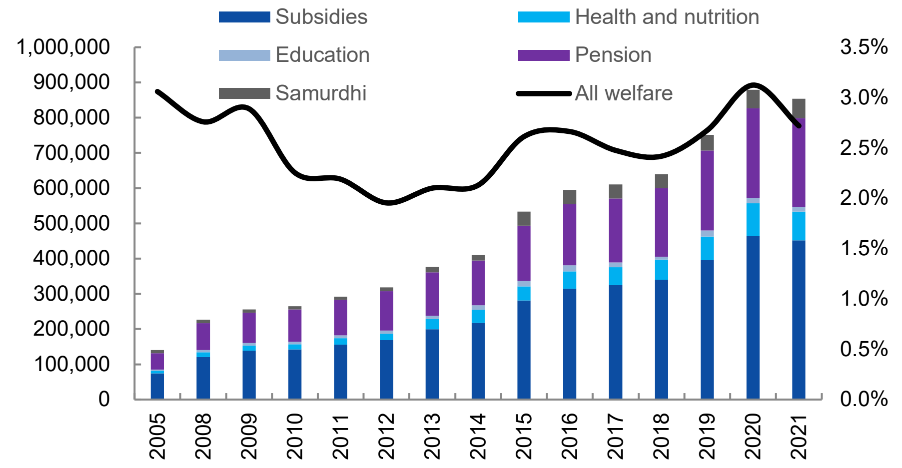
iii) Social protection spending and coverage remains very limited

60. **Even with the increase for COVID-19 assistance, Sri Lanka's total expenditure on social welfare declined over the last fifteen years (Figure 36).** The social welfare expenditure[36] was 3.3 percent of GDP in 2005, declining to 2.7 percent of GDP in 2019. The expenditure increased to 3.1 percent in 2020 due to temporary COVID-19 response programs and again declined to 2.7 percent in 2021. The highest percentage of spending is on subsidies followed by public sector pensions.

[35] https://www.gov.br/cidadania/pt-br
[36] This report uses the Ministry of Finance's definition of social welfare when referring to social protection.

Figure 36: Social welfare expenditure (2021)

(Expenditure in LKR million) *(Percent of GDP)*

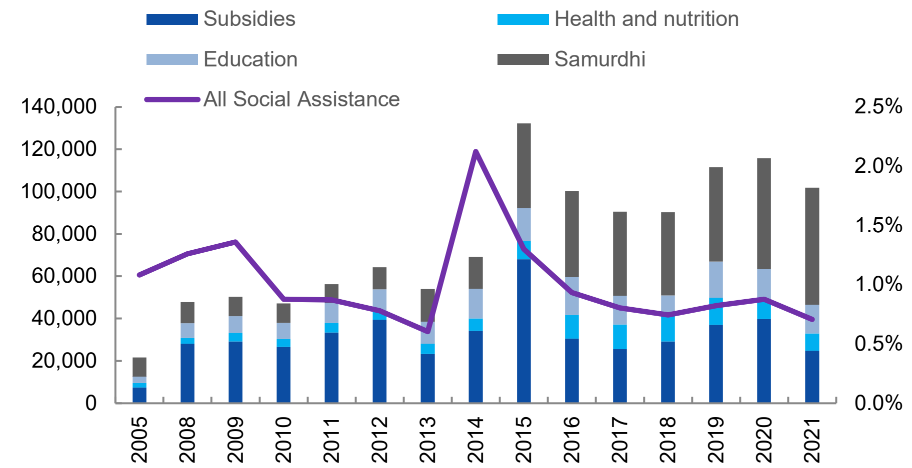


Source: Data from Ministry of Finance Annual Report 2021

61. **A similar downward trend can be seen for social assistance expenditures as a percentage of GDP during the last fifteen years (Figure 37).** Excluding subsidies and pensions, expenditure on social assistance programs was 1.1 percent of GDP in 2005, falling to only 0.7 percent of GDP in 2021. Samurdhi, the largest cash transfer program, accounted for only a third of a percent of GDP in 2021. Finally, support for health and nutrition programs and education programs was approximately 0.6 percent of GDP. Support for health and nutrition programs was 0.05 percent of GDP and for education programs was approximately 0.08 percent of GDP in 2021. On average, high income countries spend nearly 1.8 percent of GDP on these programs, over two times more than Sri Lanka in recent years. Sri Lanka's social assistance expenditure is also significantly lower than the regional average of 1.08 percent of GDP and average of 1 percent in low-income countries (ASPIRE, 2022).

Figure 37: Social assistance expenditure (2021)

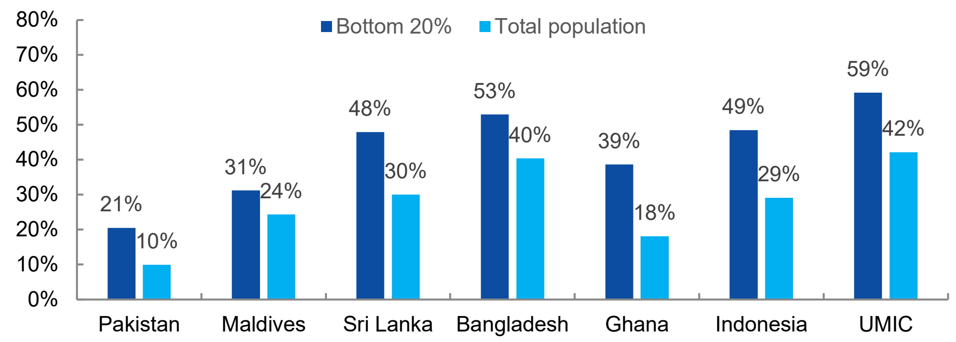
(Expenditure in LKR million) *(Percent of GDP)*



Source: Data from Ministry of Finance Annual Report 2021

62. **Social assistance coverage remains low, particularly among the poor where less than fifty percent of the poor receive social assistance.** Figure 38 shows that less than a third of the population is covered by social assistance in Sri Lanka. While Sri Lanka compares relatively well with other lower middle-income countries (LMICs) like Ghana and Indonesia, its coverage for the bottom 20 percent in 2019 was less than 50 percent, while the average for upper middle-income countries is much higher at 59 percent.

Figure 38: Share of social assistance beneficiaries in Sri Lanka (overall and poorest quintile) and other selected low- middle-income countries from around the world
(Percentage of bottom quintile and total population)

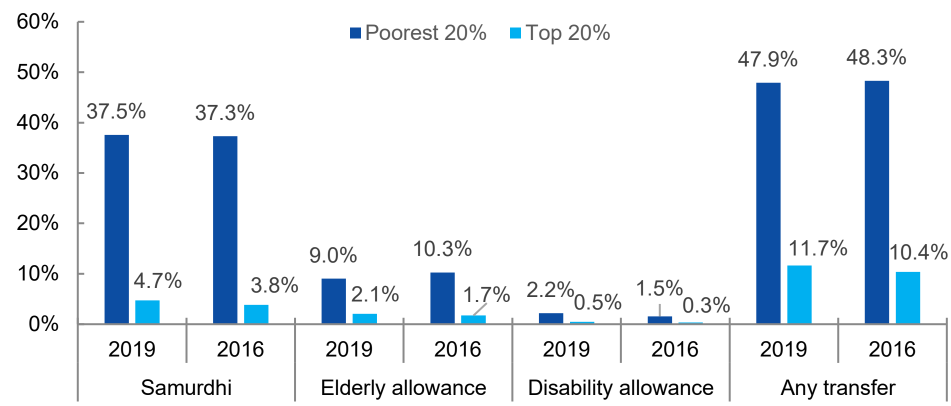


Source: ASPIRE data, 2022 based on latest available data for countries in ASPIRE.
Note: For the South Asia Region and comparisons with low middle-income countries using countries for which data have been updated in ASPIRE over the past 6 years. Bangladesh and Maldives and Ghana 2016, Pakistan 2018, Sri Lanka and Indonesia 2019, upper middle-income country (UMIC) average 2010-2019.

iv) Targeting of main social assistance programs shows a high level of inefficiencies and exclusion of those most in need

63. **Despite admirable goals, the poverty, equity, and economic inclusion impacts of the main social protection programs remain limited due to targeting errors, inadequate benefit levels, as well as a limited ability to respond to shocks.** Only 48 percent of the poorest quintile received a cash transfer in 2019 (Figure 39), while close to 12 percent of the richest quintile received a cash transfer; together, these indicate that there are significant inclusion and exclusion errors (Figure 39).[37,38] The main social assistance programs suffer from significant exclusion and inclusion errors; despite covering close to double the poverty rate for the country, the poorest quintile comprises less than 40 percent of all beneficiaries of these programs, while the richest 40 percent comprise between 16 to 21 percent (Figure 40).

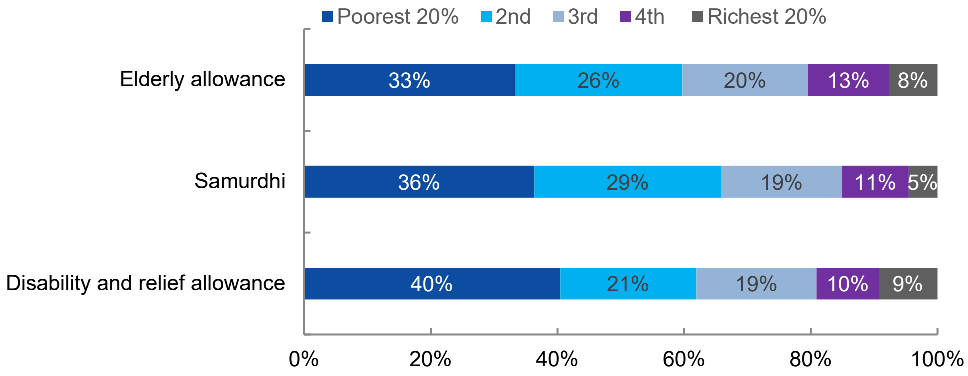
Figure 39: Coverage of the main social assistance programs in 2016 and 2019 for the poorest and richest households
(Percentage for poorest quintile and top quintile)



Source: World Bank staff calculations based on HIES 2019 data

[37] 'Inclusion errors' refer to the fact that cash transfers are made not only to poorest households but also to the richest quintile and 'exclusion errors' that poorest households are not receiving any support.
[38] In particular, the Samurdhi program covers just under 38 percent of the poorest 20 percent of households, while the disability allowance program covers only 2.2 percent, indicating larger exclusion errors. The elderly allowance covers 2.1 percent of the richest households, while Samurdhi covers about five percent, indicating larger inclusion errors (Figure 39).

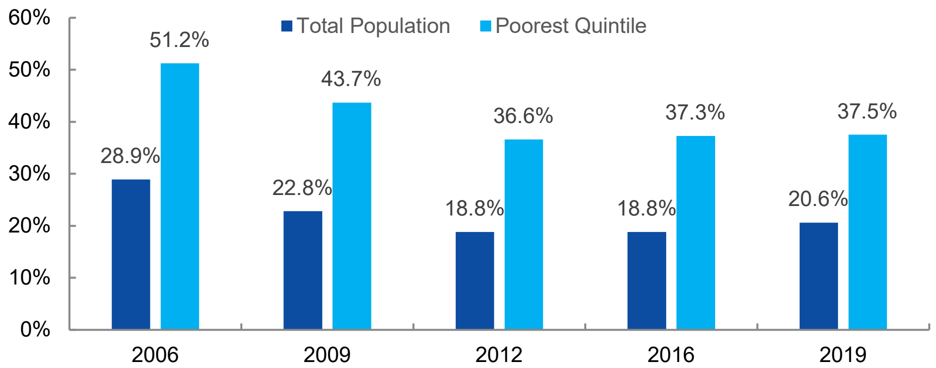
Figure 40: Distribution of social assistance programs beneficiaries by quintile in Sri Lanka
(By quintiles)



Source: World Bank staff calculations based on HIES 2019 data

64. **The targeting performance of Sri Lanka's largest poverty alleviation safety net program remains weak and limits the programs' potential impact on equity and economic inclusion**. In 2020, Samurdhi covered 1.8 million families, over 30 percent of households. The program's targeting has worsened over time, with a lesser proportion of deserving households benefiting each year. Over 50 percent of households in the poorest two income deciles were Samurdhi beneficiaries in 2006. This number declined to less than 38 percent in 2019 (Figure 41).

Figure 41: Trends in coverage of the Samurdhi program, total population, and poorest quintile
(Percentage for total population and poorest quintile)



Source: Staff calculations based on HIES 2019 data

65. **As discussed in the previous section, resources that are spent on less deserving households could be redirected to those in the bottom 20 percent of households who do not receive any social assistance**. This could significantly increase the ability of these households to cope during shocks and make the social protection system more resilient. An optimally targeted system is easier to scale up and out during a shock. Moreover, it creates more space for the system to be more dynamic and make quick adaptations as required by the type of shock.

Box 6: Reforming Samurdhi's Graduation from Poverty Approach

To address the productive inclusion issues in the Samurdhi program, a comprehensive strategy for reform of Samurdhi's graduation programs has been prepared by the Department of Samurdhi Development and piloted in selected districts. The graduation strategy is a comprehensive, time-bound, integrated, and sequenced set of interventions that aim to enable extreme and ultra-poor households to achieve key milestones towards sustainable livelihoods and socio-economic resilience to progress along a pathway out of extreme poverty. This intervention package aims to alleviate extreme poverty by creating assets and enhancing other social development indicators. The plan is to progressively apply the reform program nationwide.

A pilot of the proposed interventions was conducted in five communities (see Table below) and is being evaluated based on data collected using the social registry. Learnings from the pilot will guide the reform of the Samurdhi into a more inclusive and fiscally sustainable social assistance program.

Five Grama Niladhari Divisions selected randomly for piloting the Graduation out of poverty scheme

District	Divisional Secretariat Area	Samurdhi Zone	Grama Niladhari Division	Project ideas
Kurunegala	i.Narammala ii. Paduwas Nuwara East	(i)(Nakalagamuwa (ii)Munamaldeniya	(i)Halwella (ii)Kaduboda	Agriculture/Poultry/Milk production
Gampaha	i.Meerigama ii Minuwangoda	1.Keenadeniya ii. Horompolla	(i)Bothalegama (ii) Medemulla North	Pottery and others Mixed Projects
Colombo	i.Padukka	Tummodara	(i) Udagama	Agriculture/ self employment /trade

Source: Ministry of Women, Child Affairs and Social Empowerment

66. **The Samurdhi program permits considerable discretion in its beneficiary selection process due to lack of clear eligibility criteria and entry and exit mechanisms, undermining the program's main objective**. Without a transparent and accountable system for registration, selection and payment, Sri Lanka's safety net programs have failed to cover most of the poor, and consequently have achieved only modest impacts on poverty. The process for selection of beneficiaries is managed tightly by local and central government officials without transparency or independent oversight. Field assessments of Samurdhi, report politicization of the beneficiary selection process; rationing compounds the problem. In the absence of systematic recertification, a list of applicants is maintained at the divisional secretariat, from which the program manager selects replacements for beneficiaries that have exited the program or died. As there are no clear rules for ranking among these potential beneficiaries, program managers enjoy considerable discretionary power (Tilakaratna and Sooriyamudali 2018, World Bank 2016). Samurdhi is also in the process of pilot testing a graduation approach for existing beneficiaries, that is being piloted and evaluated before being scaled up nationally (Box 6).

v) The amount of cash transfers provided to beneficiaries is very low and insufficient to cover their needs, particularly during these difficult times

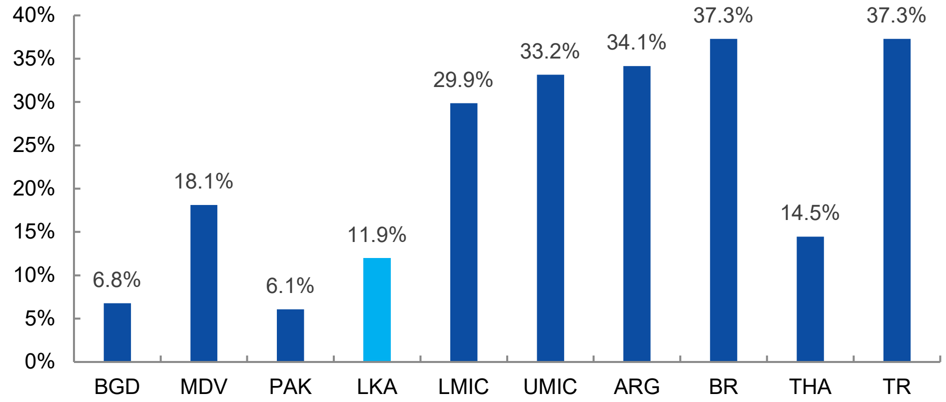
67. **Social assistance generosity is very low in Sri Lanka, and one of the lowest in the region (Figure 42).** The social assistance contribution to the poorest quintiles is significantly below Maldives, Argentina, Brazil, and averages for lower and upper-middle-income countries (ASPIRE, 2022). Figure 42 below shows that social assistance in Sri Lanka represented 12 percent of the beneficiary pre-transfer consumption in 2019, while for low and upper middle-income countries, social assistance represents over 30 percent. Pre-pandemic data indicate that many Sri Lankans lived just above the poverty line and even a common shock such as seasonal flooding could push many thousands into poverty. The current social protection programs are not flexible enough to expand in times of shock (Walsh & Hallegatte 2019).

68. **Cash transfer amounts are very low for all social assistance programs in Sri Lanka.** Despite being the program with highest transfers, Samurdhi program still provides over five times less than comparable programs of other countries in the region. Table 5 shows that the cash transfers from the

Samurdhi program represent less than 5 percent of the post-transfer consumption for the poorest households.

Figure 42: Percent of consumption that social assistance benefits comprise for the poorest quintile of beneficiaries

(Percent)



Source: ASPIRE data, 2022 based on latest available data for countries in ASPIRE
Key: BGD=Bangladesh; MDV=Maldives; PAK=Pakistan; LKA=Sri Lanka; ARG=Argentina; BR=Brazil; THA=Thailand; TR=Turkey.

Table 5: Transfers as shares of consumption for main social assistance programs in Sri Lanka

	Disability and relief allowance	Samurdhi	Elderly allowance	TB+CKD allowance
Poorest 20%	0.2%	4.6%	0.8%	0.2%
2nd	0.1%	2.5%	0.4%	0.1%
3rd	0.1%	1.2%	0.3%	0.1%
4th	0.1%	0.6%	0.1%	0.0%
Richest 20%	0.1%	0.2%	0.1%	0.0%

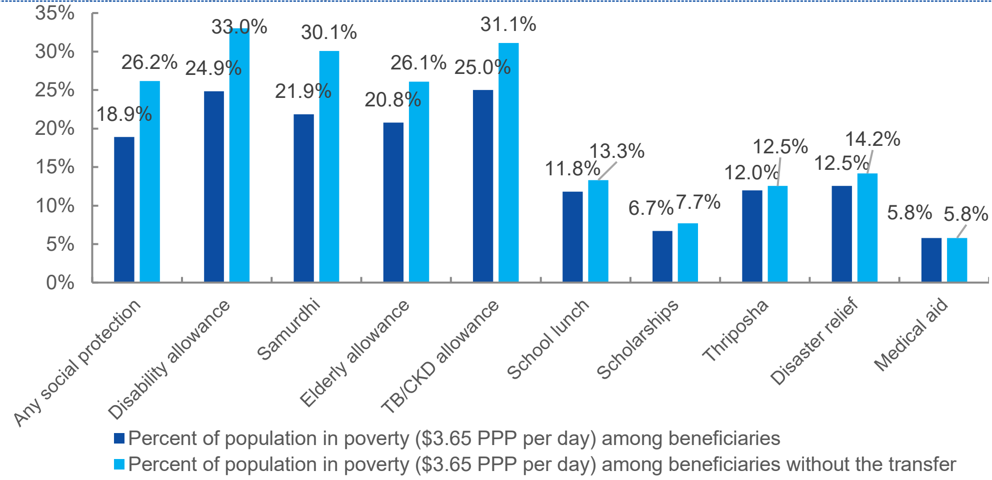
Source: World Bank staff calculations based on HIES 2019 data

69. **In addition, the real value of the benefit amounts has been progressively eroded by inflation, making the benefit amounts even more inadequate relative to the needs of the beneficiaries.** The benefit amounts have been fixed in nominal terms and adjusted only occasionally (usually prior to elections). In recent years, the government has preferred to increase the number of beneficiaries in the program rather than focusing benefits on the poorest and increasing their generosity. This has spread the meager investment even more thinly among more than 30 percent of the population, leaving average benefit amounts for Samurdhi (as an example) at less than LKR 2,500 in 2019, compared with the poverty line consumption bundle in 2019 of almost LKR 30,000. As discussed in the previous section, the median poor household in 2022 experienced an increase in the cost of their consumption bundle of 66.4 percent, keeping same transfer amounts would not provide needed relief.

70. **Despite low transfer values, for those who receive benefits, there appear to be tangible consumption impacts based on the 2019 HIES data.** Poverty rates for beneficiaries (based on the PPP $3.65 per day poverty line) is currently over 18 percent, while removing social assistance transfers could mean an over 26 percent poverty rate for these beneficiaries (Figure 43). Additionally, when looking at the differences in consumption with and without a transfer, the disability and Samurdhi allowances have the biggest differences (8.1 and 8.2 percentage points difference, respectively, in per capita consumption for those with and those without the transfer). Even with the transfer, almost a fifth of social assistance beneficiaries still experience poverty, a testament to the inadequacy of the social assistance benefit amount (Figure 44).

Figure 43: Percent of beneficiaries in poverty with and a hypothetical situation without the transfers

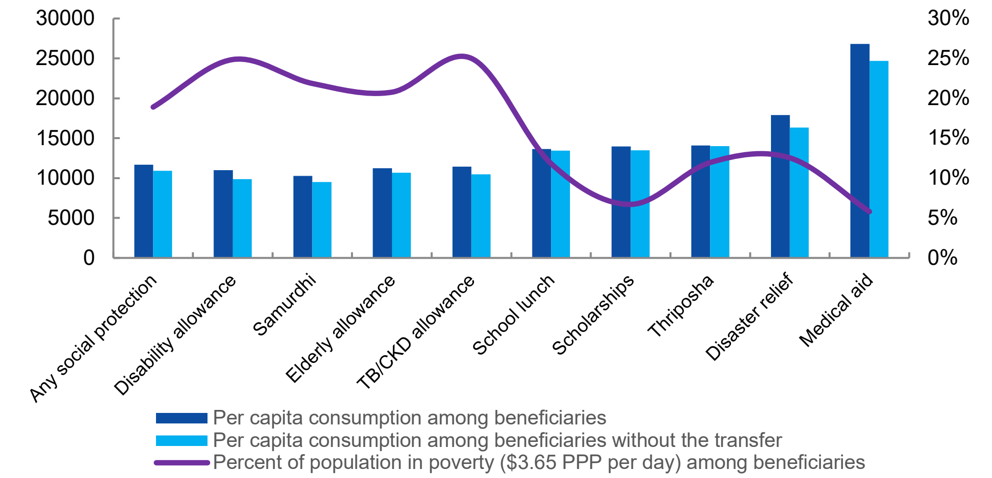
(Share of population in poverty with poverty lines US$3.65 PPP per day)



Source: World Bank staff calculations based on HIES 2019 data

Figure 44: Poverty rates and real per capita consumption among beneficiaries

(Per capita consumption in LKR and percentage of population in poverty)



Source: World Bank staff calculations based on HIES 2019 data

3. Recommendations

71. **The urgency of the current crisis necessitates swift action to improve the ability of the social protection system to deliver effective and affordable assistance to the most in need.** A continuation of the current schemes (and the emergency programs enacted in 2020 and again in 2022) is not efficient and affordable over time. In the short run, while high spending on social assistance would be needed to mitigate the impact of the crisis, the focus should be on having in place the key social protection delivery systems (social registry, payment system), and investing in adaptive systems. In the medium to long run, a more substantive rethink of the existing social protection policy mix is needed. These structural changes will help to address the major gaps in the current social protection system, including lack of access to pensions among many of the elderly, weak employment-related social insurance (e.g., disability and unemployment insurance) and a lack of effective productive inclusion programs.

72. **Ensuring adequate financing for social assistance should be a priority.** Poverty has more than doubled over the past few years, and poverty and vulnerability will continue to rise without appropriate support (see Section 1). The spending on social assistance before the COVID-19 pandemic was very low.

In order to best protect the poor and vulnerable, and partially mitigate the impact of the crisis on those most in need during these difficult times, the spending on social assistance will have to remain at higher levels than before the pandemic.

73. **In the short run, immediate action is needed to improve the key delivery mechanisms and impact of main cash transfer programs.** This includes strengthening the institutional capacity of the government to establish and manage an up-to-date, computerized registry of social assistance beneficiaries and applicants; improving eligibility criteria; delivering payments to the poorest using electronic bank transfers; improving communications; and putting in place a transparent mechanism for lodging and responding to grievances and appeals. The government of Sri Lanka has appointed members to the WBB to oversee this reform and co-ordinate information sharing and registration of beneficiaries for all social assistance programs. The WBB has powers under its own Act to work independently to collect data, introduce temporary emergency cash transfer programs to mitigate the impacts of crises on the poor and vulnerable, and to advise existing program administrators on whom to select based on a poverty scorecard.

74. **The first step is to determine the current needs of the population in a transparent and unbiased manner.** To this end, the government will collect data on households receiving or needing assistance, sufficient to ensure they are properly identified and that assistance to the poorest is prioritized. The data will be collected by government officials on mobile devices, using a secure process and with a transparent grievance and appeals mechanism (Box 4). A wide outreach campaign needs to be conducted to ensure all who are in need can apply to be registered and assessed for assistance. A process will be put in place to update these data on a regular basis (at least once every two years). This will ensure that immediate assistance goes only to those who need it most, given the budget constraints, and make it possible to regularly review the status of social assistance beneficiaries to ensure those who graduate out of poverty can make way for others who are more in need of help.

75. **With the establishment of the Social Registry, the targeting of all poverty targeted programs is expected to improve significantly and move away from the current discretionary approach used by many programs.** The political sensitivities around social protection programs such as Samurdhi have been a challenge to reforming programs so that they provide social assistance to citizens who need it the most. The Welfare Benefits Act and the upcoming approval by Parliament of the regulations and selection criteria to identify low-income families for welfare payments would provide the necessary legal framework to implement this needed reform.

76. **The social registry should be complemented by a modernized payment system.** Payments to beneficiaries are made using programs-specific (often manual) payment systems, which have been subject to delays, leakages and inefficiencies. The payments are delivered predominantly through the Samurdhi banking system, which is set up as a community bank and not regulated by the Central Bank of Sri Lanka. A centralized, well-regulated digital payment system would ensure efficient disbursement and coordination between the central government and program implementing agencies. The strengthening of payment systems would facilitate more rapid and effective response in times of crisis or disaster which, given the country's exposure to a wide range of hazards and shocks, has the potential to significantly increase the resilience of Sri Lanka's population.

77. **Given its increasing vulnerability to shocks, Sri Lanka would benefit from developing a social protection system that can scale up and phase out where needed.** Programs should only provide routine assistance to those who genuinely need government support to survive. However, these same programs can be designed to be 'shock-responsive' – extending access temporary assistance to other citizens if they suffer an unexpected shock (such as a natural disaster). Such programs can prevent shock-affected families from falling into poverty and suffering a loss of human capital, a known cause of chronic poverty and transmission of poverty across generations. Scaling up assistance in response to shocks will be made easier by the existence of a social registry and more accessible and efficient registration processes. However, it also requires government to pre-commit fiscal space to expand assistance in the event of a shock, as well as institutional arrangements that determine when such a scale-up can occur and the eligibility criteria for support.

78. **The generosity of benefits needs to be reconsidered and better tailored to needs.** This should start with an assessment of the fiscal envelope, and a clear decision by authorities on the appropriate level of assistance to provide. While benefit levels that are too high can disincentivize work and individual initiative, this concern is often exaggerated. It is important to ensure that assistance ensures that no household is unable to meet their basic needs, and this should not rest on an assumption that informal support mechanisms will pick up the slack. In an environment with limited fiscal resources, it is better to focus meaningful assistance on fewer households, than to operate a broadly targeted or universal program with minimal benefits.

79. **While regular cash transfers are more effective when targeted, social assistance can still provide universal insurance to all citizens against poverty.** Universality can be provided on a contingent basis, by insuring all households against shocks through an adaptive safety net. This can be complemented by a well-targeted antipoverty cash transfer program, and categorical programs that assist vulnerable groups and groups such as young children, to promote inclusion and economic opportunity for all. The fiscal capacity of the country and the sustainability of the social assistance program design must be given due consideration, and it is important to ensure that any scale-up of assistance in response to a crisis is temporary in nature, giving the new beneficiaries a time-bound path to graduate from the program.

80. **In the medium to long term, Sri Lanka needs to transition to a more fiscally sustainable and inclusive contributory social insurance and aged care system.** Sri Lanka's population is aging rapidly. The existing social insurance (pension) system is focused on public servants and formal private sector workers (employment provident fund), leaving out all those who work in the informal sector. Approximately 70 percent of the informal sector workers do not receive any old age protection. It disproportionately benefits public servants, who receive lifetime assistance at the taxpayer's expense. The cost of this scheme to the treasury is rising exponentially as the population ages. Those who have not worked, or worked in the formal sector on a low wage, or had interrupted careers (the case for many Sri Lankan women) often retire with little or no savings. This leaves them highly vulnerable, often depending on children or other family members who are increasingly struggling themselves. Aged care is similarly limited to expensive private offerings or limited slots in public and charitable centers. Reforms are needed to rebalance the high level of spending on public service pensions towards more equitable assistance, and limiting the impact on the budget by seeking contributions from employers and employees.

81. **Sri Lanka also needs to reconsider productive inclusion.** The existing model delivered through Samurdhi is less than optimal. As discussed, many poor households are excluded from the program, and many of those who are beneficiaries report being unable to take microloans or access the program's economic inclusion activities. The scheme needs to be reformed, paying close attention to incentivizing Samurdhi officers to achieve tangible results, ensure open access to micro-loans, and partner with local NGOs that often know the local economic opportunities better and can tap private sector support. A detailed program for reform of Samurdhi's graduation programs has been prepared by the Department of Samurdhi Development and piloted in selected districts, and this reform program should be applied nationwide. There is scope to consider other modalities of productive inclusion interventions as well, such as public works targeted to low-skilled and marginalized individuals focusing on enhancing their skills and employability.

82. **Finally, a comprehensive, overarching strategy is needed to guide social protection reform in a systematic manner.** In addition to articulating the priorities for future program design and targeting, and addressing the above-mentioned gaps, a social protection strategy will ensure coordination across government. Fragmentation and limited information sharing are currently impediments to effective program implementation and informed planning. A strategy that is broadly endorsed can also guide more carefully crafted and less politicized policy decisions and commit government to allocating the needed resources to ensure programs provide adequate protection and achieve the best possible results.

ANNEX 1: MICROSIMULATION APPROACH TO ESTIMATING POVERTY

To understand the impact of the current crisis, a micro-simulation based on the Household Income and Expenditure Survey 2019 (the latest available data source on household consumption) was carried out. The simulation follows approaches adopted in World Bank (2014) and World Bank (2021a) and makes use of information on different sources of household income including earned income by broad economic sector income from transfers and remittances, ad-hoc income, and income in-kind. The method combined macro-level information in the years subsequent to the survey on wage growth, GDP growth and employment growth by sector, remittances from abroad, and transfers paid by the government as social assistance to project household income and household consumption for the years 2020-2022.

Employment and earned income

The first stage of the microsimulation simulated the changes to employment observed in the three main sectors (agriculture, industry, and services) as reported in the DCS Labour Force Survey for 2020 and 2021. The computation of employment changes for 2022 was based on the historical linear relationship between sectorial GDP and employment by sector. Private sector workers were shifted out of or into employment from a given sector based on the probability of them being employed as estimated by logistic models of employment. Newly employed workers into agriculture were assigned as contributing family workers with earnings corresponding to the 10th percentile of agricultural income among own account workers in their province of residence. Newly employed workers into the services sector in 2021 (the only other case in which employment expanded between 2020 and 2022) were selected from the pool of those who lost their jobs in 2020 and were reassigned their original wage or income.

Once the employment outcomes were simulated for each year, earned incomes were adjusted using wage indices published by the Central Bank. Earned income includes wages or salaries paid to public or private employees as well as the profits earned from agricultural or non-agricultural activities by self-employed or own account workers, employers, and contributing family workers. The wages of public sector employees were adjusted using the public sector wage index while wages of private sector workers were adjusted using informal sector wage indices for broad industrial sector. Agricultural profits of own account workers were adjusted using GDP growth rates for the agriculture sector.

Income from transfers

The government responses to the COVID-19 pandemic in terms of one-off social assistance in 2020 and 2021, as well as expansions to coverage, were also incorporated into the microsimulation. Programs considered in the microsimulation were Samurdhi, the elderly allowance, disability allowance, the CKD allowance, and the Graduate employment scheme which commenced in 2020, as well as one-off payments made to beneficiary or waitlisted households and those affected by the COVID-19 lockdowns. Here too, the first stage involved assigning households to beneficiary status (under an assumption of a targeting that follows the current targeting performance of Samurdhi) until the numbers in the administrative reports were matched, after which all beneficiary households were assigned the respective additional transfers.

Other sources of income

Foreign remittances were adjusted in line with monthly data on remittances published by the Central Bank. *Ad hoc* income, which includes sources such as proceeds from sale of assets, loans, and withdrawal of savings, as well as in-kind income (which is the value of household consumption that is freely received or produced at home) were scaled in line with overall GDP growth rates.

Changes in HH consumption

Once the income aggregate was constructed for each year, household income growth rates were computed. The computed change in household income was then applied to household consumption (excluding imputed rent). These projected household consumption aggregates were then used to estimate poverty and inequality measures for the 2020-21 period. For 2022, all the steps above were followed, but the values were kept in nominal terms.

Inflation impacts in 2022

In contrast to 2020 and 2021, given the high value of inflation in 2022, it was important to capture its distributional impacts. To this end, a household-specific inflation rate was calculated for 2022, based on the shares of food and non-food items of each household. This household-specific inflation rate was then applied to the projected nominal consumption for 2022. This projected household consumption aggregate was used to estimate poverty and inequality in 2022.

ANNEX 2: SELECTED SOCIAL PROTECTION PROGRAMS IN SRI LANKA

(Implemented by the Central Government)

Main implementing agency in 2022	Program	Target audience	Targeting mechanism	Number of beneficiaries (2020)	Expenditure (LKR million) (2020)	Benefit provided (2020)
Cash transfers						
MWCASE/Dept of Samurdhi Development	Samurdhi	Low-income families	Means tested	1,770,086	52,434.31	Based on the number of family members
MWCASE/National Secretariat for the Persons with Disabilities	Chronic kidney disease allowance	Low-income patients with chronic kidney disease	Categorical and means tested	39,169	1776.25	LKR 5,000 per month
MWCASE/National Secretariat for the Persons with Disabilities	Disability allowance	Low-income disabled	Categorical and means tested	72,000	4292.8	LKR 5,000 per month
MWCASE/National Secretariat for the Elders	Elderly allowance	Low-income elderly over 70 years	Categorical and means tested	417,067	9,875	LKR 2,000 per month
MWCASE/National Secretariat for the Persons with Disabilities	Housing Assistance for Persons with Disabilities	Low-income disabled without houses	Categorical and means tested	227	18.078	LKR 250,000 to build a new house and LKR 150,000 to renovate a house
MWCASE/National Secretariat for the Persons with Disabilities	Medical Assistance for Persons with Disabilities	Low-income disabled chronic disease patient	Categorical and means tested	822	12.162	LKR 20,000 per family to attend clinics, purchase medication
MWCASE/National Secretariat for the Persons with Disabilities	Educational Assistance for Persons with Disabilities	Low-income disabled student	Categorical and means tested	913	7.972	LKR 10,000 maximum per disabled student to purchase educational items
MWCASE/National Secretariat for the Persons with Disabilities	Assistance for single parent families	Low-income single parent and at least one family member disabled	Categorical and means tested	445	11.62	Assistance for self-employment and to purchase educational material
Food and in-kind transfers						
MWCASE/Thriposha Ltd	Thriposha program	Pregnant mothers and malnourished children below 5 yrs	categorical	1.06 million	1,122	2 packs per month (1500 grams)

MWCASE/National Secretariat for the Early Childhood	Poshana Malla pregnant mothers' allowance	Pregnant and lactating mothers	categorical	178,000	3,560	LKR 2,000 per month for 10 months
MWCASE/National Secretariat for the Persons with Disabilities	Providing assistive devices for disabled	Low-income disabled	Categorical	17	3.5	Assistive devices for walking, seeing, hearing etc.
Ministry of Defence / National Disaster Relief Services	Flood and drought relief	Victims of disasters	Geographical	1.5 million	161.29	3 days cooked meals and thereafter 7 days dry rations
Ministry of Education	School Textbooks	Universal	Universal	4.18 million	4,550	Textbooks
School Feeding Programs						
Ministry of Education/ Provincial Ministries of Education	School meal program	Schools in malnourishment hotspots	Categorical	1 million	2,299	Midday meal All children attending targeted school
Labour market programs						
MWCASE/National Secretariat for the Persons with Disabilities	Self-employment assistance for disabled	Low-income disabled	Categorical and means tested	913	7.972	LKR 25,000 onetime payment
MWCASE/National Secretariat for the Persons with Disabilities	Vocational training assistance for disabled	Low-income disabled	Categorical and means tested	130	4.22	LKR 15,000 per month as trainee allowance for maximum of 2 years

Notes:
The current name of the main implementing agency is presented here. The names of the ministries that implemented programs have changed from 2020 to 2022.
MWCASE= Ministry of Women, Child Affairs and Social Empowerment.

ANNEX 3: SUMMARY OF SOCIAL PROTECTION PROGRAMS IMPLEMENTED DURING THE COVID-19 PANDEMIC IN 2020

Program	Beneficiaries				Benefit Amount		
	Prior to COVID-19	Wait-listed Prior COVID-19	Newly Identified during COVID-19	Total number of beneficiaries supported	Existing benefit amount (LKR)	Top Up (LKR)	Benefit amount given during COVID-19 (LKR)
Elderly Allowance	416,667	157,720	54,827	629,214	2000	3000	5,000
Centenarian allowance	400	85		485	5000		5,000
Allowance for Persons with Disabilities	72,000	37,492	14,149	123,641	5000	-	5,000
CKD Patients	25,320	13,348	5,623	44,291	5000	-	5,000
Samurdhi	1,793,553	735,975		2,529,528	420-3500	varied	5,000
Helpless Community Groups whose livelihoods are directly or indirectly lost (wave 1)			1,924,967	1,924,967		5000	5,000
Helpless Community Groups whose livelihoods are directly or indirectly lost (wave 2)			1,343,214	1,343,214		5000	5,000
Helpless Community Groups whose livelihoods are directly or indirectly lost (wave 3)			1,110,792	1,110,792		2000	2,000
Farmers Pension	160,675			160,675	1000-5000	varied	5,000
Fisherman's Pension	4,600			4,600	1000-4166	varied	5,000
Total	2,473,215	944,620	1,999,566				

Source: Ministry of Finance
Notes: Exchange rate USD 1= LKR 190
Benefit amount Rs. 5000=USD 26.32
Farmer's and Fisherman's pension are two contributory pension schemes. The benefit amount was increased to LKR 5,000 by adding a top up for all eligible pensioners.

ANNEX 4: ECONOMIC CRISIS PACKAGE PROGRAM DETAILS (MAY, 2022)

Allowance Category		Payment Amount per person (LKR)	Number of Beneficiaries		Total Funding (Existing+ Top up) Requirement for Targeted Beneficiaries per month (LKR)	Actual Expenditure (May 2022)	
			Targeted Beneficiaries	Actual Beneficiaries (May 2022)		LKR	USD
Samurdhi Allowance							
	Existing	1900 3200 4500	1,702,603	1,696,323	5,441,747,700	5,411,097,000	15,030,825
	Top up	1900 - 3100 3200 - 3100 4500 - 3000			5,210,394,600	5,191,562,300	14,421,006
	Waiting list	5,000	731,975	726,449	3,659,875,000	3,632,245,000	10,089,569
Total Samurdhi			**2,434,578**	**2,422,772**	**14,312,017,300**	**14,234,904,300**	**39,541,401**
Categorical programs							
Elderly Allowance over 70 years							
	Existing	2000		416,416	833,334,000	832,832,000	2,313,422
	Top up	3000	416,667	248,126	1,250,001,000	744,378,000	2,067,717
	Waiting list	5000	238,640	132,500	1,193,200,000	662,500,000	1,840,278
	Sub Total		**655,307**	**548,916**	**3,276,535,000**	**2,316,755,000**	**6,435,431**
Elderly Allowance over 100 years							
	Existing	5000		445	2,390,000	2,225,000	6,181
	Top up	2500	478	289	1,195,000	722,500	2,007
	Sub Total		**478**	**445**	**3,585,000**	**2,947,500**	**8,188**
	Total NSE		**655,785**	**549,361**	**3,280,120,000**	**2,319,702,500**	**6,443,618**
Disability Allowance							
	Existing	5000		71,882	360,000,000	359,410,000	998,361
	Top up	2500	72,000	23,837	180,000,000	59,592,500	165,535
	Waiting list	5000	62,457	25,327	312,285,000	126,635,000	351,764
	Total PWDs		**134,457**	**97,209**	**852,285,000**	**545,637,500**	**1,515,660**
Chronic Kidney Disease Patients (CKD) Allowance							
	Existing	5000		38,945	195,750,000	194,725,000	540,903
	Top up	2500	39,150	21,003	97,875,000	52,507,500	145,854
	Waiting list	5000	5,798	3,256	28,990,000	16,280,000	45,222
	Total CKDu		**44,948**	**42,201**	**322,615,000**	**263,512,500**	**731,979**
	Total NSPD		**179,405**	**139,410**	**1,174,900,000**	**809,150,000**	**2,247,639**
Total Categorical			**835,190**	**688,771**	**4,455,020,000**	**3,128,852,500**	**8,691,257**
Total (for May)			**3,269,768**	**3,111,543**	**18,767,037,300**	**17,363,756,800**	**48,232,658**

Source: Ministry of Finance
Notes: Exchange rate USD 1=LKR 360
"Payment details:
* Samurdhi and categorical program waiting list beneficiaries received LKR 5000
Samurdhi Program top up: (i) LKR 1900 recipients received LKR 3100; (ii) LKR 3200 recipients received LKR 3100; (iii) LKR 4500 recipients received LKR 3000
Categorical cash transfer programs beneficiary top up: (i) existing elderly program beneficiaries received LKR 3000; (ii)existing cash program for elderly over 100 years received LKR 2500; (iii) existing cash transfer program for disabled received LKR 2500; (iv) existing cash transfers for chronic kidney disease patients received LKR 2500

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