Sri Lanka's Post-Crisis Transition: Comparative Insights from Greece

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FIRST CAPITAL RESEARCH

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***Please refer page 30 for an important disclaimer*

Overview

- We compare Sri Lanka's post-crisis experience (since 2022) with Greece's post-debt crisis period (from 2010).
- We identify common economic, political, and bond market patterns, including real, fiscal, and external-sector dynamics, to help anticipate Sri Lanka's post-crisis trajectory.

Purpose

- At First Capital Research, we aim to extract lessons from Greece's recovery path by identifying **what worked**, **what failed**, and what **Sri Lanka should avoid or prioritize** over the **next three to five years**.

Greece as a Benchmark for Sri Lanka's Recovery

- Greece's economy is only modestly larger (about 3 times) than Sri Lanka's and shared similar structural vulnerabilities both before and during the crisis.
- Both countries experienced slow-building fiscal vulnerabilities ahead of their crises, driven largely by debt-fueled growth and widening macroeconomic imbalances.
- Their post-crisis paths show strong similarities:
  - IMF-led stabilization programs
  - Austerity-driven hardship (income squeeze, unemployment, poverty)
  - Political shifts during the crisis
  - Slow recoveries, heavily dependent on credible and sustained reforms

Structural Context and Crisis Evolution

Greece & Sri Lanka

Similar Economic Structures, Relevant Comparisons

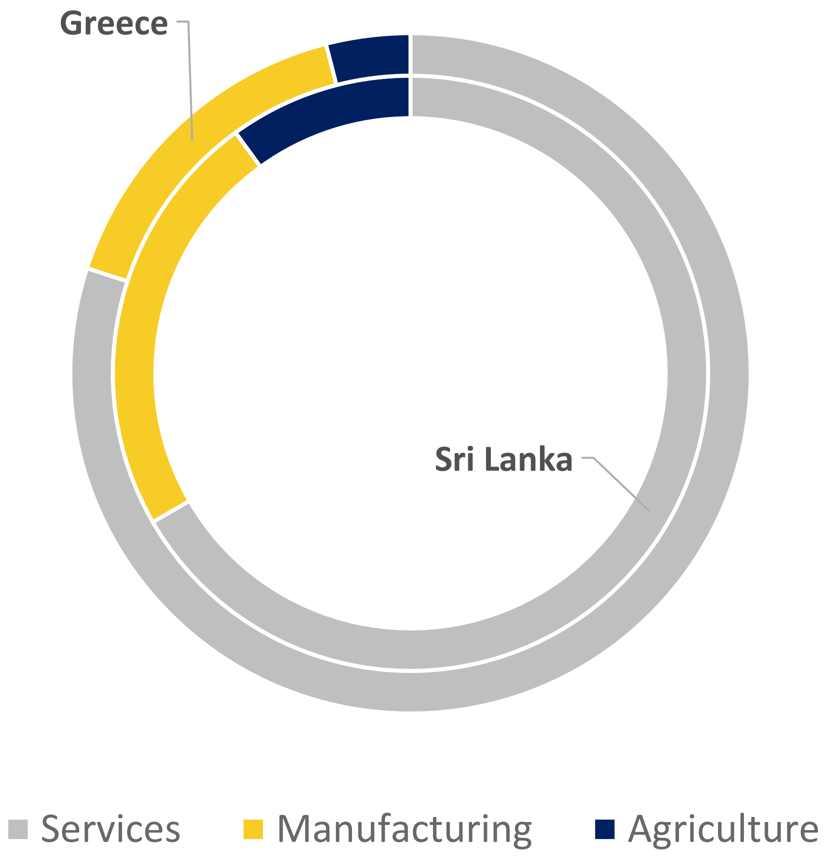
Key Contributors to the GDP

Greece

Services
Tourism; Shipping

Manufacturing
Food processing; Chemicals; Pharmaceuticals

Agriculture
Olive Oil; Fruits



Sri Lanka

Services
Tourism; ICT/BPO; Financial Services

Manufacturing
Apparel & Textiles, Construction; Rubber-based Products

Agriculture
Tea, Rubber

Greece: Key Structural Weaknesses Ahead of the Debt Crisis

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Sources: Molho (2023); Mckinsey & Company (2012); Galanos, Kotios & Koutoulakis (2017); World Bank

Greece: Economic Crisis & Recovery — Timeline

2009
Crisis breaks

May 2010
Normal issuance breaks down; 1st EU/IMF bailout for Greece.

2011
The economy is in a deep recession; yields started to spike.

Mar. 2012
2nd EU/IMF program private-sector debt restructuring within the 2nd program; debt stock reduced but recession persists.

2013
The economy is still in recession; consolidation continues; tentative stabilization begins

Jan–July 2015
Second Crisis (2015)
Breakdown in negotiations led to bank closures and capital controls; the referendum rejected creditor terms, Greece missed an IMF payment, and bond yields spiked again.

Aug. 2015
3rd ESM program signed with IMF advisory; fiscal targets and reforms reset

2017
Primary surpluses over-achieve targets; **Greece returns to bond markets** (July 2017 five-year issue)

2021–present
Continued consolidation

Sri Lanka: Economic Crisis — Timeline

2010–2020

Crisis Build-up

2020–2021

COVID-19 shock plus tourism collapse; credit ratings downgraded; external financing tightens as reserves fall

2022

(Mar): Authorities seek IMF assistance; stabilization steps begin; sharp yield increases; exchange rate allowed to float

2022

(Apr): “Pre-emptive” suspension of external debt service (moratorium) announced by the Ministry of Finance

2023

(Mar): IMF Extended Fund Facility approved (USD 3 bn, 48 months); program anchors **fiscal consolidation, SOE/energy reforms, and debt restructuring**

2024

(Jul): Agreement in principle with ISB bondholder groups on a state-contingent (macro-linked) restructuring framework.

2025

(Mar & July): IMF Third and Fourth Reviews completed; Sri Lanka meets quantitative targets adequately.

2025

(Dec): Cyclone Ditwah impact; IMF says Fifth Review postponed pending damage/impact assessment

Policy Cycles, Market Perception, and Credit Dynamics

Greece & Sri Lanka

POLITICS OF GREEK ECONOMIC CRISIS - TIMELINE

CENTRE- LEFT PASOK (PRO-AUSTERITY)
OCT 2009-NOV 2011

PROTESTS & LOSS OF SUPPORT

TEMPORARY GOVERNMENT - LUCAS PAPEDOMOS
NOV 2011 - MAY 2012

ELECTIONS, NO CLEAR MAJORITY TO TRADITIONAL PARTIES

NEW DEMOCRACY/CENTRE RIGHT COALITION WITH PASOK (PRO-AUSTERITY CONTINUATION)
JUN 2012 - JAN 2015

RECESSION AND PUBLIC DISSATISFACTION

LEFT WING SYRIZA (ANTI-AUSTERITY PROMISE, BUT LATER ACCEPTED IMF FISCAL CONSOLIDATION)
JAN 2015 - JUL 2019

ANTI - AUSTERITY BACKLASH
&
LATER STABILISATION UNDER EU/IMF

SLOW GROWTH & AUSTERITY FATIGUE

CENTER-RIGHT NEW DEMOCRACY
2019 - PRESENT

POLITICS OF SRI LANKAN ECONOMIC CRISIS - TIMELINE

POPULIST/STRONG STATE GOVERNMENT
2019-2022
(ECONOMIC INSTABILITY CAUSED THROUGH TAX CUTS AND MONETARY FINANCING)

PROTESTS & LOSS OF SUPPORT

TECHNOCRATIC GOVERNMENT
2022-2024
(SLOW GROWTH AND ECONOMIC CONSOLIDATION)

ELECTIONS AND THE RISE OF ANTI-AUSTERITY AND ANTI-CORRUPTION POLITICS

LEFT - WING POPULIST COALITION
2024 - PRESENT
(ANTI - AUSTERITY PROMISES BUT LATER OPERATED WITHIN THE IMF)

Rating Trajectories — Greece vs Sri Lanka

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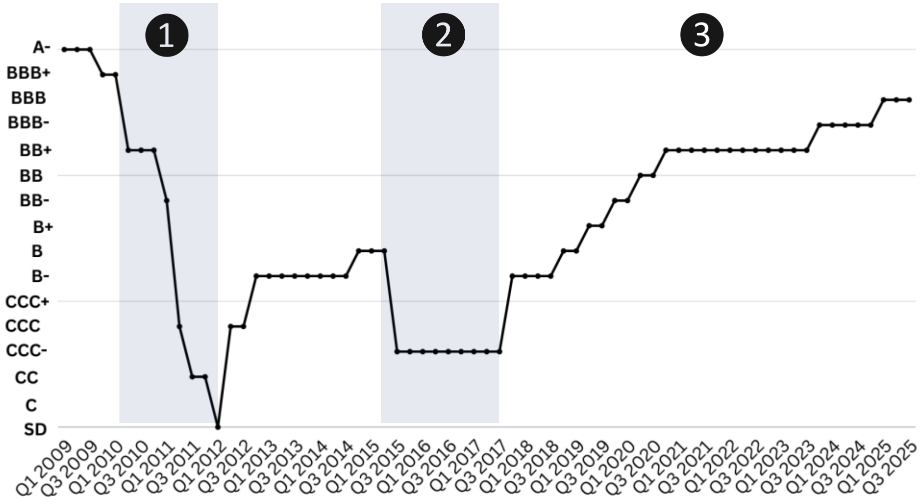
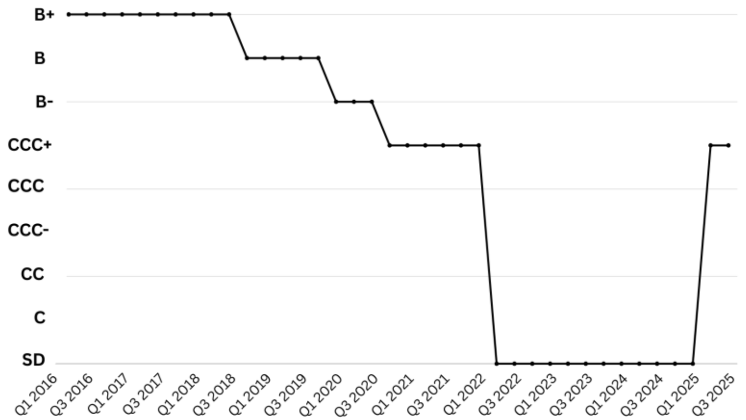
- Both saw rapid multi-notch downgrades to distressed levels during crisis periods.
- Greece:
  1. Initial upgrades after the first program
  2. A setback amid second crisis
  3. Gradual, multi-year upgrades back toward investment grade as reforms anchored and market access improved.
- Sri Lanka: early upgrades post-program, but the path depends on reform delivery, debt-deal execution, and durable market access.

GREEK CREDIT RATING HISTORY



SOURCE - STANDARD & POOR'S (S&P)

SRI LANKAN CREDIT RATING HISTORY



SOURCE - STANDARD & POOR'S (S&P)

Sri Lanka - What's Holding Ratings Down (Why CCC+ Despite Recovery)?

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- High debt-to-GDP

  ⟹ The growth needs to pick-up so that the Debt to GDP ratio will drop below 90%

- Interest burden on Government Revenue

  ⟹ Interest payments consume larger portion of government revenue , still far above the 'CCC' median

- External debt servicing cliff from 2029

  ⟹ ISB amortizations jump to US$544 million in 2028 from US$330 million in 2026–2027; macro-linked bonds start amortizing from 2029

- Revenue still structurally low

  ⟹ Revenue/GDP at 15% remains far below the CCC median of 22.5%, limiting fiscal space

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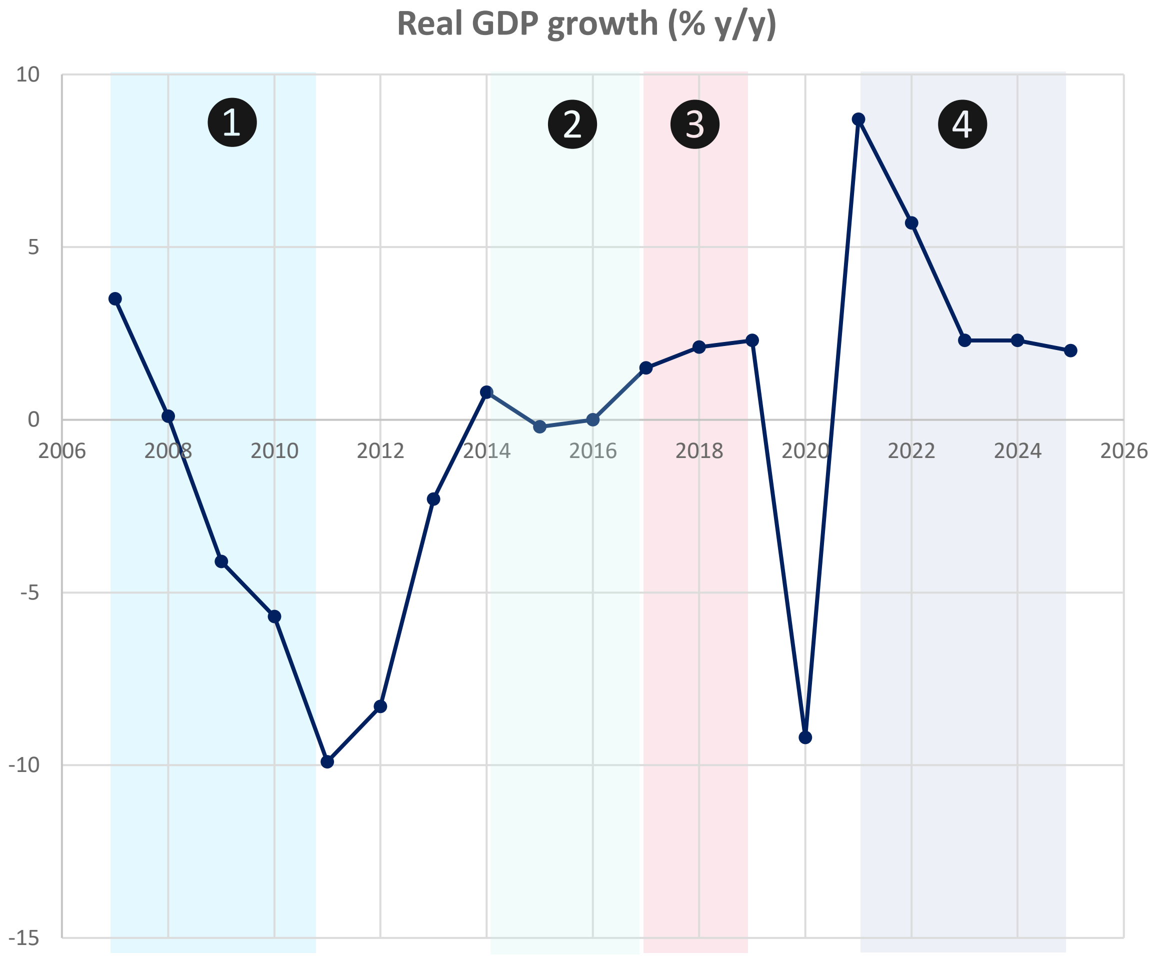
Economic Cycles

Greece & Sri Lanka

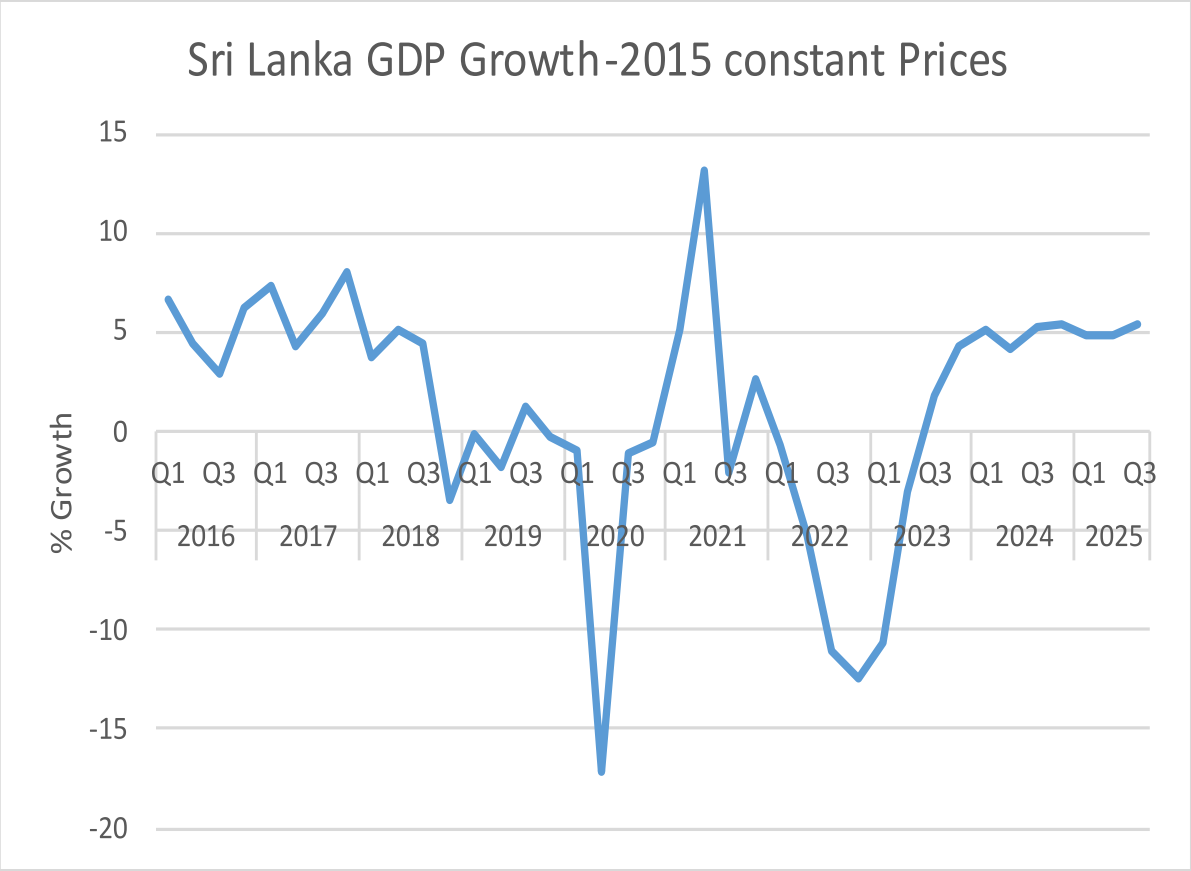
Greece — From Deep Recession to a Steady Growth

- 1 Greece real-GDP growth trajectory shows multi-year contraction amid crisis.
  2 Brief 2014 uptick & flat 2015–2016 amid renewed-crisis.
  3 Stabilization with reforms.
  4 strong post-COVID rebound & normalization.
- The country had a stop-start prior to its steady growth when austerity measures did not couple with reforms and credibility.
- The growth story shows, keep reforms on track and pivot to export/FDI-led growth which mature into durable normalization rather than relapse.



Sri Lanka’s Growth Cycle: Crisis, Collapse, and Early Recovery

- Pre-Crisis growth and slowdown (2016–2018): Growth was positive but structurally fragile, masking fiscal and external vulnerabilities
- Slowdown (2019–2020): Easter attacks (2019) and COVID-19 shock exposed weak buffers and accelerated economic deterioration
- Full-Blown Economic Crisis (2022)
- Post-crisis recovery (2023–2025): IMF-anchored stabilization and debt restructuring restored positive growth, similar to Greece’s early post-crisis recovery but with high vulnerability



“Sri Lanka mirrors Greece’s crisis-recovery cycle, but with faster collapse, faster adjustment, and higher near-term recovery risk.”

Greece — Fiscal Front Budget Deficit

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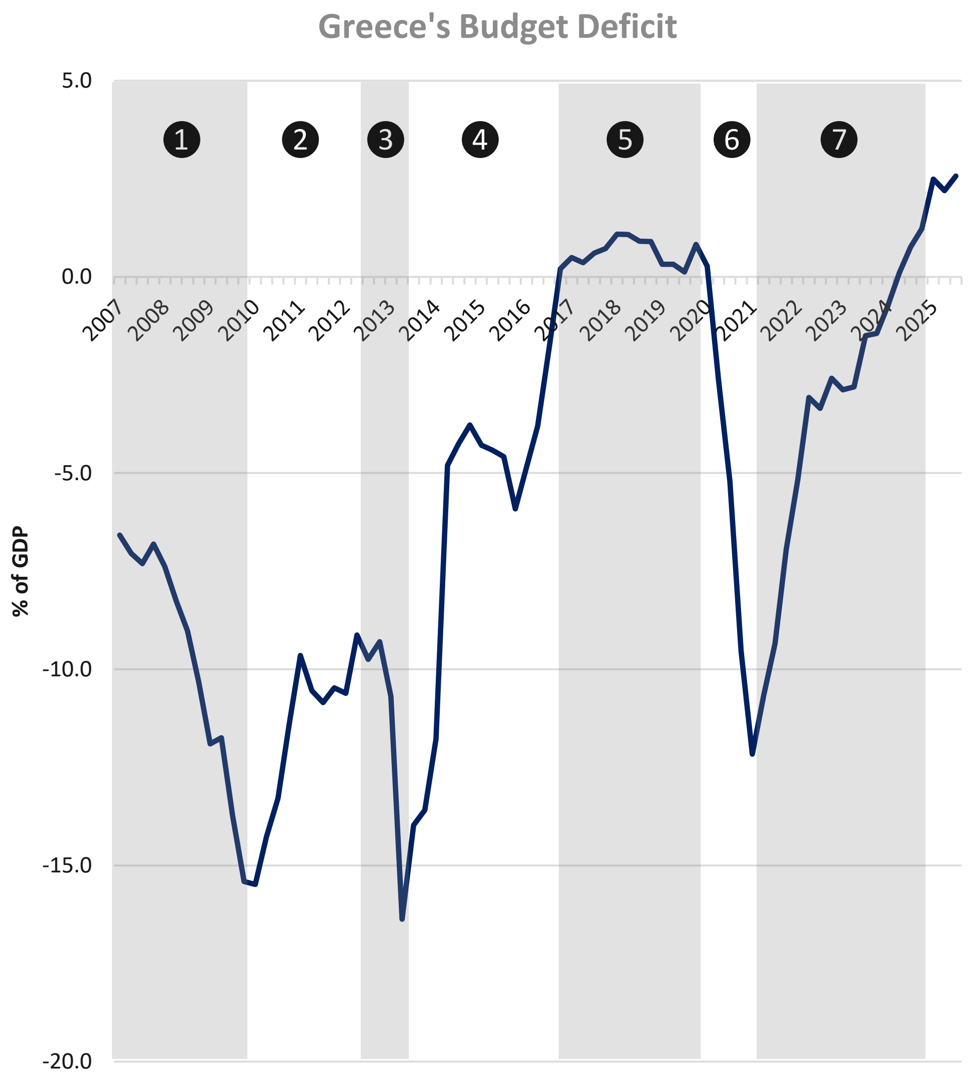
1. 2007-2009: Large structural deficits
2. 2010–2012: Austerity measures with EU-IMF bailouts
3. 2012-2013: Deep Recession
4. 2013–2016: Stabilization and primary surplus fiscal consolidation plus structural reforms acted together
5. 2017–2019: Clear fiscal improvement
6. 2020: COVID-19 Outbreak
7. 2021–2025: Strong recovery and surplus



Sri Lanka-Budget Deficit

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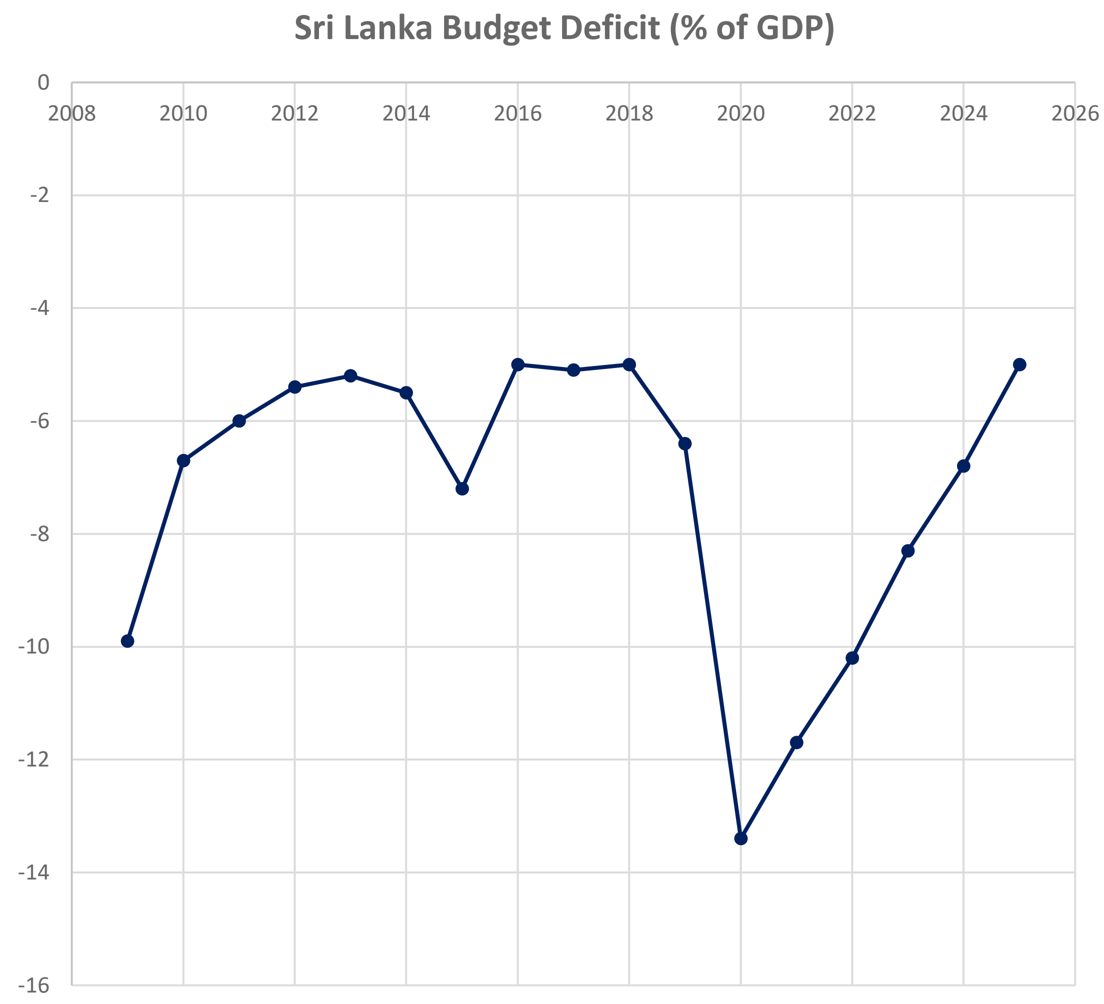
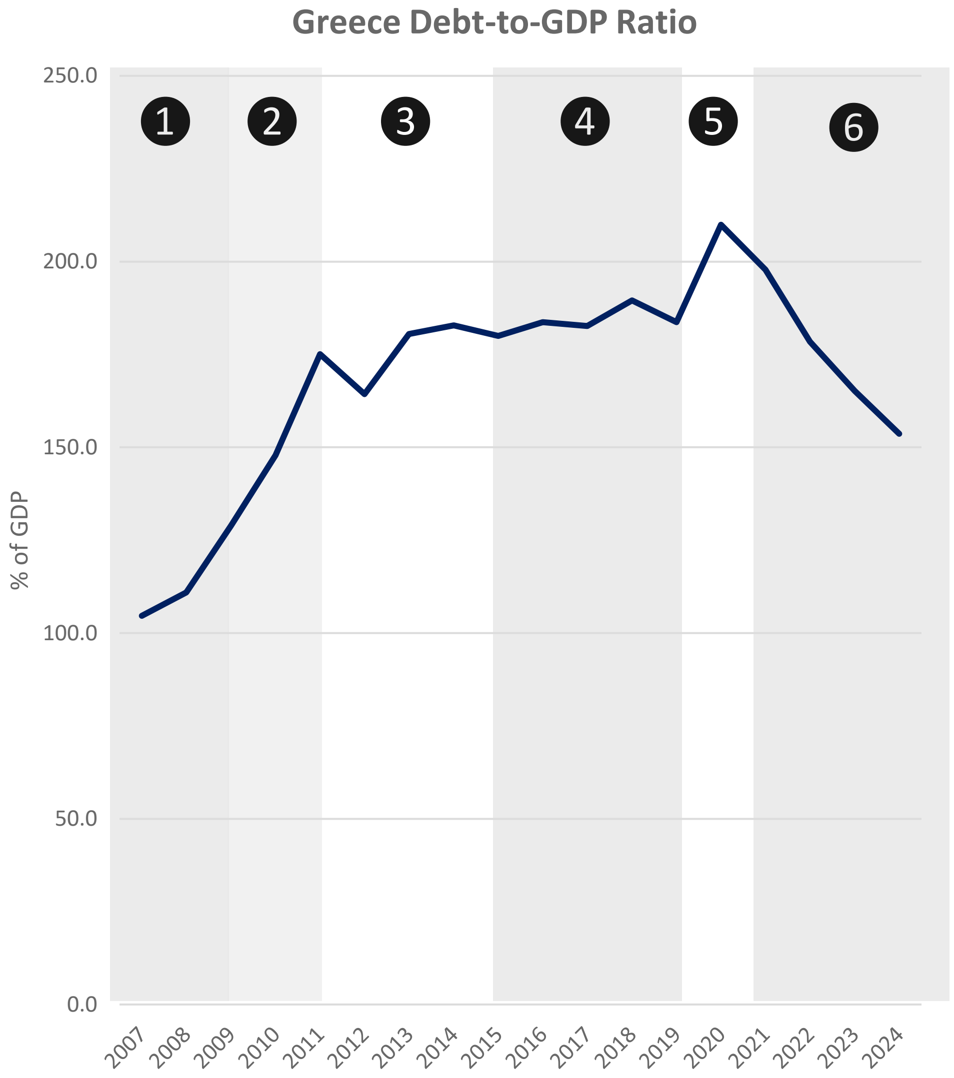
- Greece precedent shows front-loaded austerity deepened the recession, eroded revenues, and triggered renewed stress.
- Sri Lanka needs to avoid over-tightening that chokes growth and should instead pair fiscal consolidation with exports, productivity, and reform-led recovery.



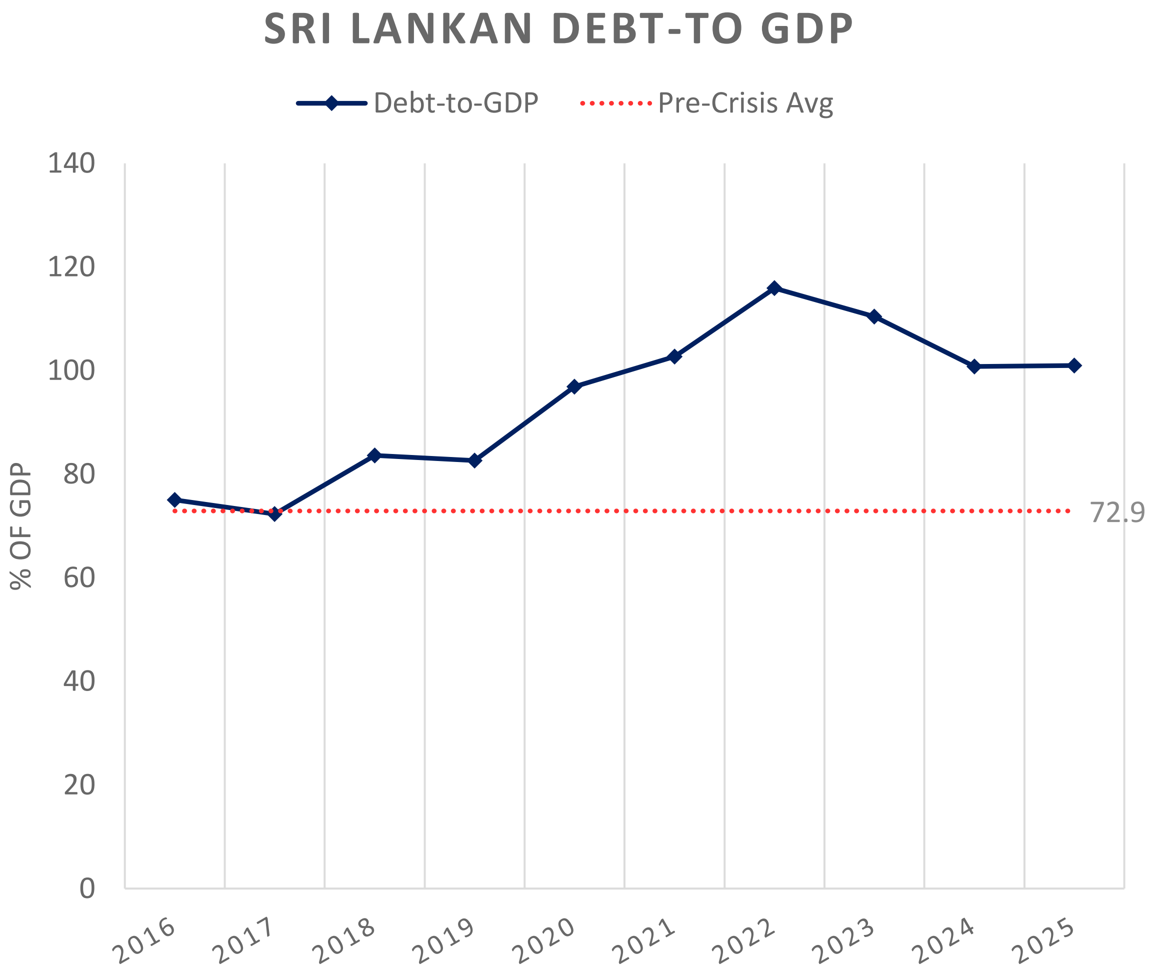
Greece — Fiscal Front Debt-to-GDP Ratio

1. 2007–2009: Debt increased and GDP fell
2. 2010–2012: Austerity caused a deep depression while the debt load was not reduced immediately (stagnant debt load and weaker growth)
3. 2012–2014: Partial stabilization (reduction in debt growth with debt restructuring but with reduction in GDP growth)
4. 2015–2019: Full stabilization and plateau (Debt growth is balanced off by GDP growth)
5. 2020: Temporary destabilization with COVID-19 shock
6. 2021–2024: Rapid improvement(GDP grows faster than debt)



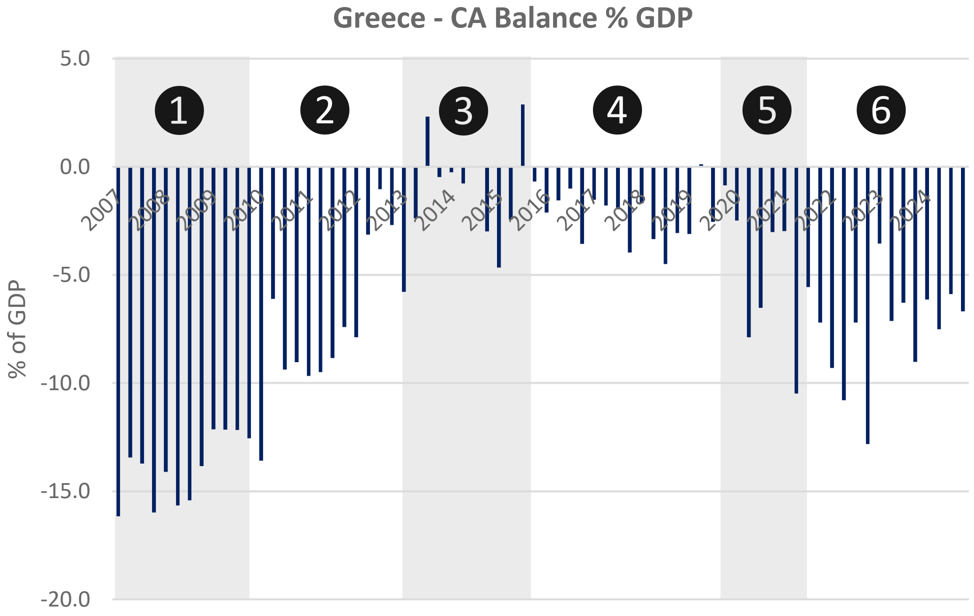
Sri Lanka Debt to GDP

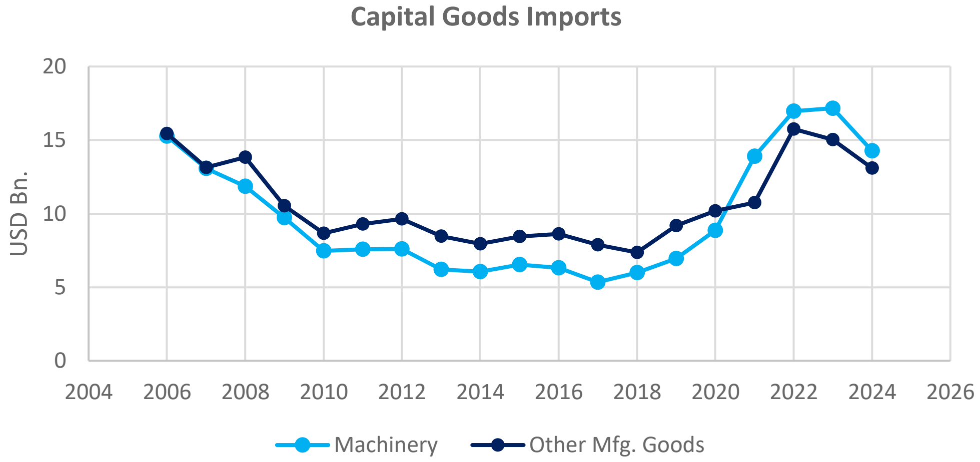
- Sri Lanka's debt-to-GDP is about 60% above its pre-crisis average (since 2007), peaked after default, and is now gradually declining as growth resumes.
- While still below Greece's crisis peak, the level remains high and highly sensitive to growth outcomes.
- Greece's experience shows debt ratios fall ***only with sustained GDP growth***:
  - ⇒ High debt can remain manageable if investor confidence is maintained.
  - ⇒ Continued reforms are essential to support growth and avoid a second crisis.



Greece — External Sector and Current Account Adjustment

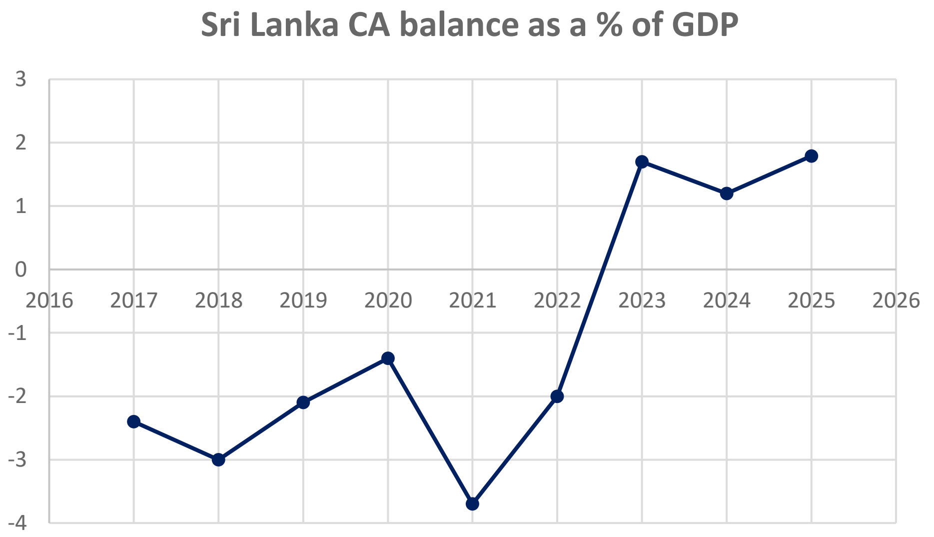
1. 2007–2009: Large deficits driven by cheap credit and consumption led imports
2. 2010-2012: The CA improved because the economy collapsed
3. 2013–2016: Temporary positive balance due to recession (“internal devaluation” adjustment)
4. 2017–2019: The growth driven deficits
5. 2020: Temporary Improvement during COVID as the imports slowed down
6. 2021–2024: Persistent structural deficit driven by energy and capital good imports.

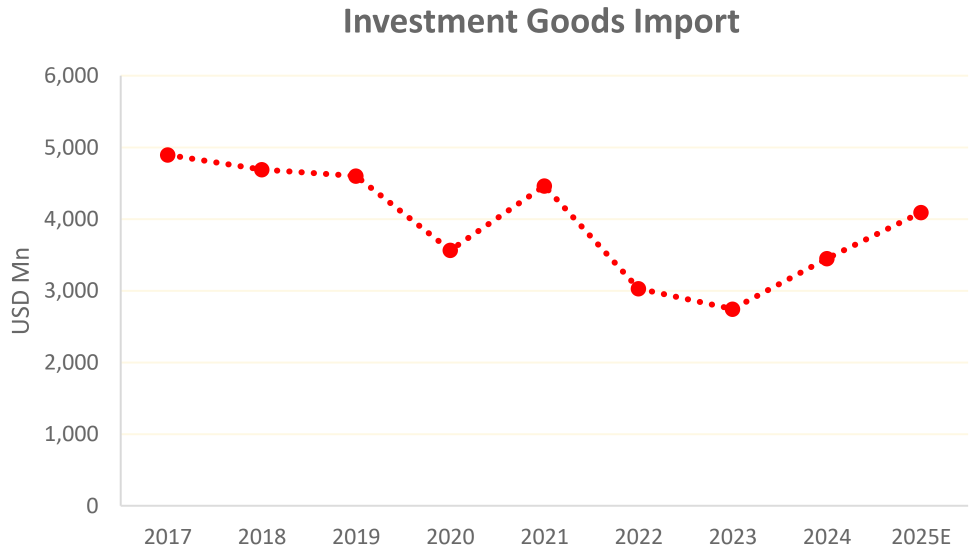




Sri Lanka's Current Account Surplus Reflects Doing Less Rather than Selling More.

- The current-account surplus was driven by import compression and lower investment, supported by tourism and remittances, not particularly through an export boom.
- This mirrors Greece's early post-crisis phase, where CA gains came from weak demand, not stronger competitiveness.
- Without export growth and FDI-led capex, the CA surplus is fragile and likely to narrow as growth resumes.
- As growth normalizes, a moderate current-account deficit would be healthy, reflecting higher investment and capital formation rather than macro stress.





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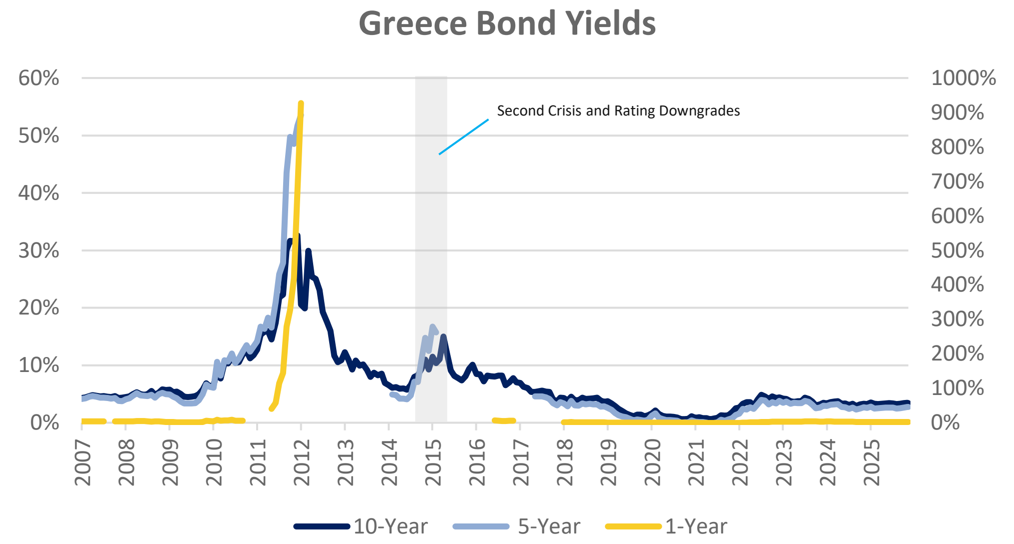
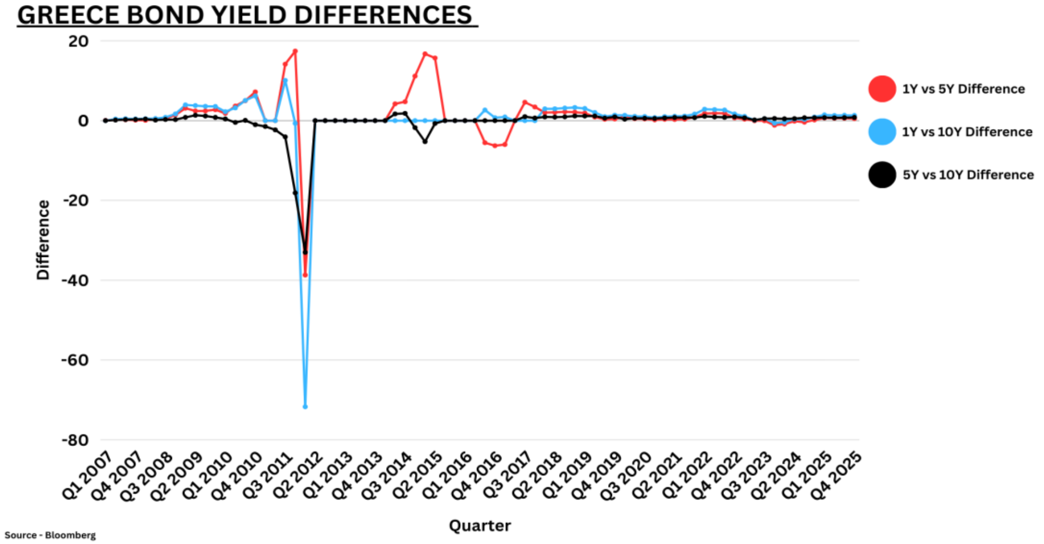
Financial Markets:
Yield Curve Movement

Yield Curve Movement — Greece

- Crisis period saw extreme bear-steepening (rising yields, long end rising faster as risk premia surged)
- Gradual credibility gains shifted the curve to bull-flattening (falling yields, long end compressing faster)
- Sustained reforms resulted in durable normalization after repeated stress episodes.





Source - Bloomberg

Yield Curve Movement — Sri Lanka

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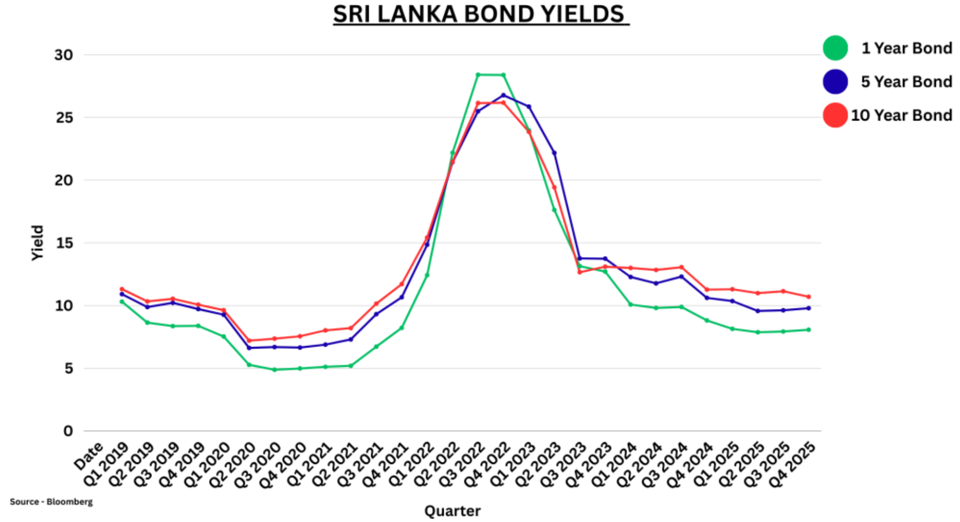
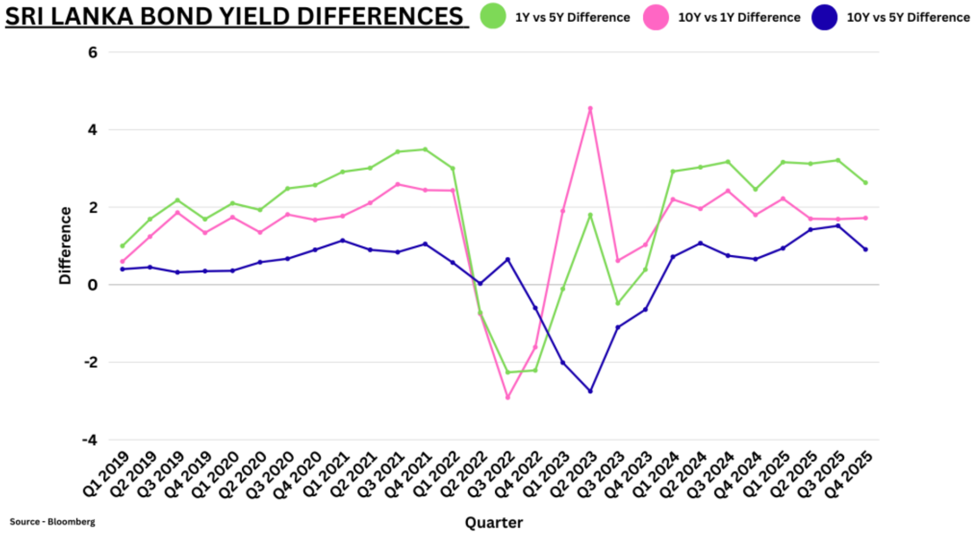
Yield Curve Movement

- The curve has flattened from its peak, though term premia remain elevated relative to pre-crisis levels.
- The curve has shifted from bear-steepening (crisis-driven rise in yields) to early-stage bull-flattening (gradual risk compression).
- Progress remains fragile and uneven across maturities.



Takeaway

- Sri Lanka's yield curve is likely to continue bull-flattening if reforms are sustained (consistent with Greece's later-stage adjustment).
- Reform slippage risks a reversal into bear-steepening, similar to Greece-style relapse episodes during 2014-2016.



Implications

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"Sustained recovery is reform-coupled and credibility-driven, not austerity alone. Financial Markets are likely to follow the risk-based adjustment"

Base Case (Greece 2017–2019 parallel)	**Upside Growth (Greece post-2019 parallel)**	**Downside Growth (Greece 2014–2016 Parallel)**
Reforms stay on track: IMF-EFF programme continues through 2026.	Reforms beyond IMF: SOEs, tax, liberalisation; market access improves.	Reform slippage & political uncertainty with the risk of austerity fatigue, post-cyclone fiscal pressures, or policy slippage.
Growth Outcome: GDP growth of 4–5% in 2026, but the recovery remains fragile.	Growth Outcome: Stronger, more durable growth driven by private investment and improved productivity.	Growth Outcome: Growth underperforms, credibility weakens, and recovery becomes uneven.
Yield curve implication: Yield curve continues bull-flattening. Long-end yields (10Y+) compress gradually from 10.8–11% toward 9.5–10.5% as term premia ease.	Yield curve implication: Faster bull-flattening. 10Y yield could converge toward 8.5–9.5% within 2–3 years	Yield curve implication: Yield curve shifts back to bear-steepening. Long-end yields widen sharply, with the 10-year rising toward 12–14%.

Reforms that Took Place in Greece: When and How

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Stage 1 (IMF-EU Driven)

Public Administration Reform - Public sector employees dropped by 8–10% with compensation dropping by 5-7% on top of earlier cuts. Fragmented manual systems to centralized digital processes with mergers in in overlapping government ministries.

Pension System Restructuring - Increased from early-retirement thresholds toward 67 with lower replacement rate. Multiple pension funds have been merged.

Privatizations – Generated about €5–6 billion through privatizations and transferring assets from state ownership to private or concession control.

Product-market Liberalization – Removed price controls and licensing restrictions in retail, transport, tourism, and energy.

Stage 2 (Domestic-Led)

Corporate tax reductions - cut the corporate tax rate from 29% in 2016 to 24% by 2019

Active labor-market policies (ALMPs) – Implemented job training programs and wage subsidies

E-government platforms - simplifying administrative

Stage 3 (Growth-Led)

Further **expansion of digital platforms -** real-time POS reporting, and mandatory e-invoicing, sharply reducing the VAT gap.

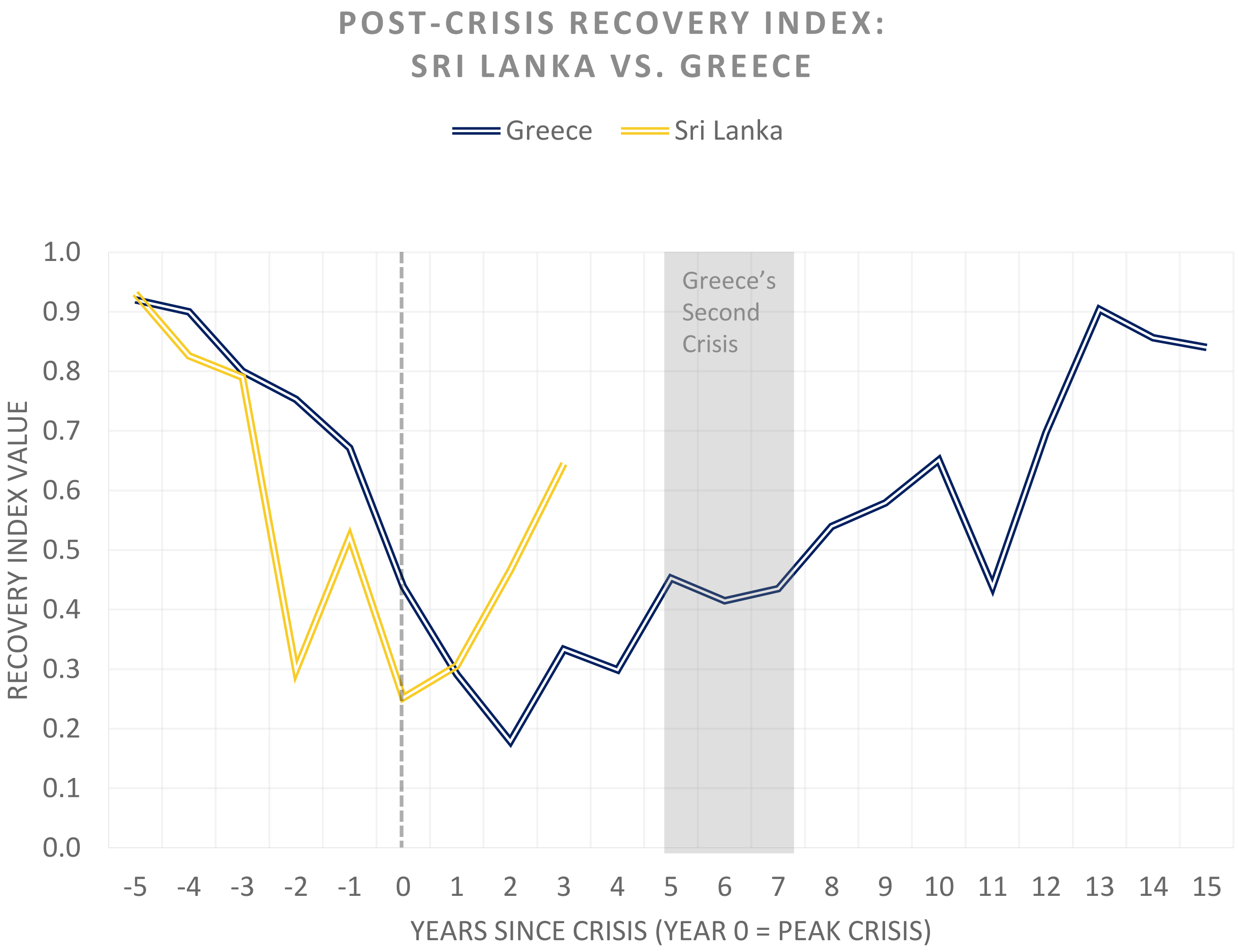
Labour legislation updates - more flexible work arrangements improving match between jobs and skills

Justice system digitalization - Case-tracking, e-filing, and online court management reduce case backlogs by 30% which sped up dispute resolution, lowers legal costs and improves business confidence

Education system modernization - Expanding vocational training linkages

Healthcare and social support reforms - Expanded primary care, improved financing, and digitalized social services to boost access and efficiency.

Recovery From the Crisis: Head-to-Head Comparison



Index Construction

- 30% Stability (Debt-to-GDP and Budget Deficit as a % of GDP)
- 30% External & Investment Recovery (Capital Goods Imports and Exports (% of GDP))
- 20% Growth (Real GDP Growth)
- 20% Sovereign Risk (Sovereign Credit Ratings (forward-looking indicator))

Note that the Index values are normalized (0–1); Year 0 represents each country's peak crisis year.

Conclusion: What We Can Clearly Draw from the Comparison

1. Sri Lanka is at a critical turning point, similar to Greece in 2013–2014, where early stabilization can either translate into sustained recovery or give way to a stop-start adjustment and renewed stress.
2. Key reforms include labour-market improvements, coupled with SOE restructuring, improved tax compliance, and digitalization, which are likely to pave the path for sustained growth.
3. Similar to Greece’s 2010–2015 experience, debt-to-GDP ratios decline only with sustained reforms; austerity alone suppresses growth and delays rating upgrades.
4. High debt and a heavy interest-to-revenue burden, together with delays in core reforms, keep Sri Lanka vulnerable and weaken investor confidence.
5. This creates a medium-term relapse risk (around 2028–2032), similar to Greece’s funding pressures in 2015 if reforms weaken following IMF program exit.

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