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# Two Resets, One Crisis: Jamaica's Debt Reckoning & Lessons for Sri Lanka

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FIRST CAPITAL RESEARCH

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*\*\*Please refer page 25 for an important disclaimer*

# Why Jamaica?



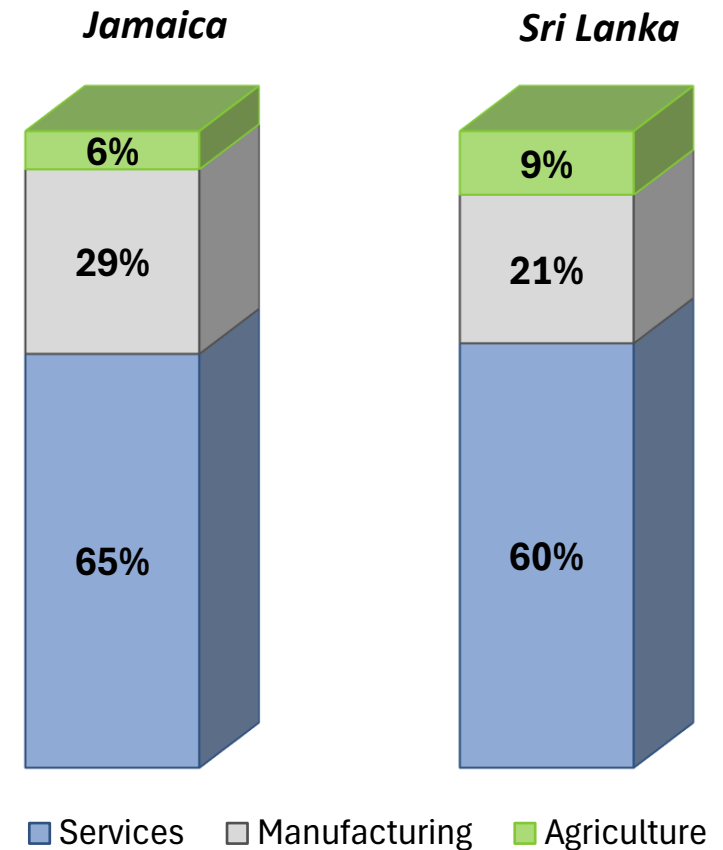
- Sri Lanka undertook a restructuring of its domestic debt through the Domestic Debt Optimization (DDO) program unveiled in 2023.
- In the period since, the authorities have demonstrated notable fiscal consolidation alongside legislative reforms that have reshaped the domestic capital market under the supervision of the IMF.
- However, constrained access to external financing has heightened reliance on domestic funding, altering the composition of public debt and concentrating risks within the local financial system.
- With the expiration of the ongoing IMF program drawing closer, questions surrounding policy continuity and debt sustainability warrant careful scrutiny.
- This report therefore turns to Jamaica not to revisit the origins of its crisis, but to examine the policy gaps and structural weaknesses that culminated in a second consecutive restructuring of its domestic debt, and to assess whether comparable warning signs may confront Sri Lanka.
- Jamaica has undertaken **two major domestic debt restructuring operations** to address an unsustainable debt burden that peaked at nearly 135% of GDP.
- **The first, the Jamaica Debt Exchange (JDX) in 2010**, was a voluntary, par-neutral swap of domestic bonds for new instruments with lower coupons and longer maturities.
- **The second, the National Debt Exchange (NDX) in 2013**, was a deeper intervention required after the initial program failed to restore sustainability.

# A snapshot of the economy: Jamaica Vs Sri Lanka



Latest Available Data	Jamaica	Sri Lanka
Geography	Island Nation (10,991km <sup>2</sup> )	Island Nation (65,610km <sup>2</sup> )
Population	2.8Mn	21.8Mn
GDP (Current)	USD 22.0Bn	USD 108.8Bn
GDP Per Capita (Current)	USD 7,753.8	USD 5,003.0

Jamaica Vs Sri Lanka: Economic Composition



# Genesis of Jamaica's domestic debt crisis



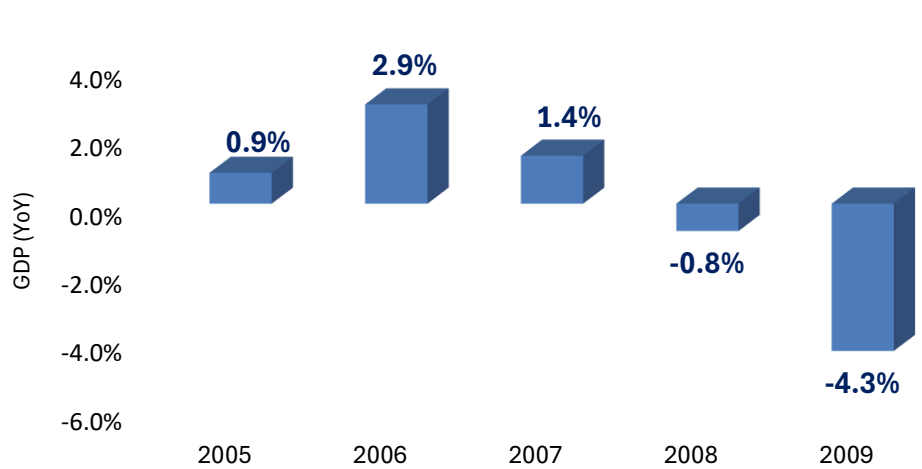
- **Fiscal Expansion Without Productive Transformation:** The 1970s democratic socialist agenda expanded the state dramatically through nationalization, public employment, and social spending, pushing deficits to unsustainable levels without generating offsetting growth.
- **External Shocks on a Narrow Economic Base:** Oil price spikes (1973-74 & 2008-09) and weakened demand for bauxite and sugar exposed structural fragilities, depleted reserves, and entrenched reliance on external borrowing.
- **Costly Financial Sector Collapse:** Premature financial liberalization and weak oversight led to a mid-1990s banking crisis; the bailout (over 30% of GDP) was financed largely through domestic debt issuance, permanently enlarging the sovereign balance sheet.
- **High-Interest Rate Debt Trap:** Tight monetary policy (especially from 1995) in a context of chronic fiscal borrowing drove interest rates sharply upward, accelerating domestic debt accumulation and crowding out private investment, thereby suppressing growth and weakening the tax base.
- **Sovereign–Financial Sector Interdependence:** Local banks and pension funds concentrated in high-yield government paper, deepening systemic exposure and locking the economy into a self-reinforcing debt–interest spiral.
- **Crisis and Inevitable Restructuring (2010):** By FY 2009, total Central Government Debt had reached 131.6% of GDP and interest payments absorbed roughly two-thirds of tax revenue. Moreover, S&P downgraded Jamaica's sovereign credit rating to 'SD' in Jan-2010. Consequently, restructuring the domestic debt stock became the only viable path to avert systemic collapse.

# Key economic indicators of Jamaica prior to the 1<sup>st</sup> restructuring: 2005-09

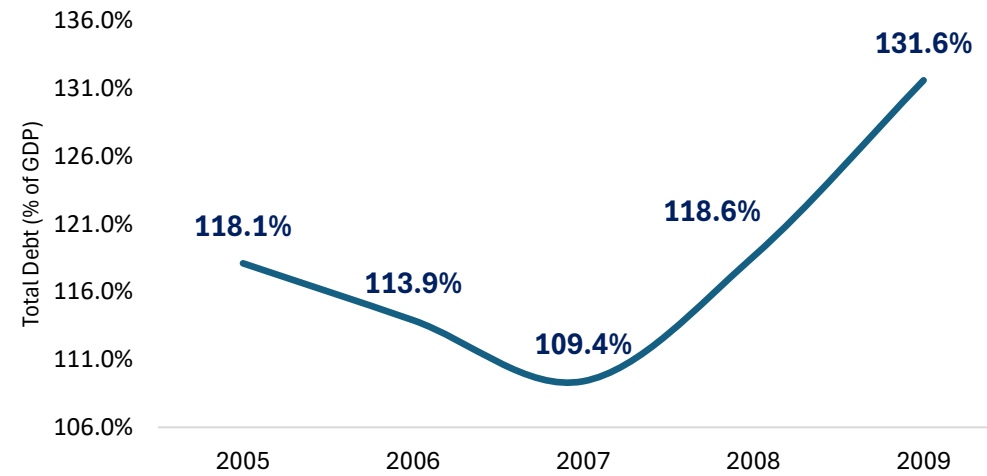


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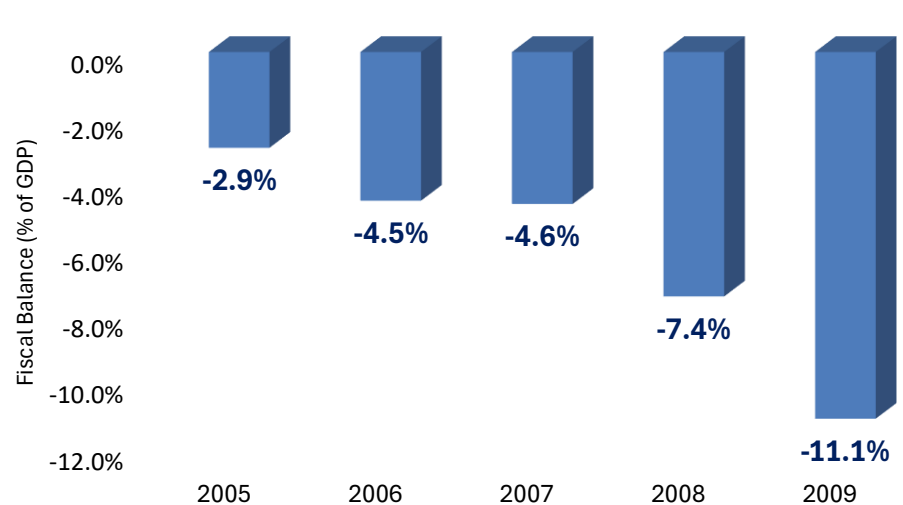
**GDP growth dipped to -4.3% in 2009**



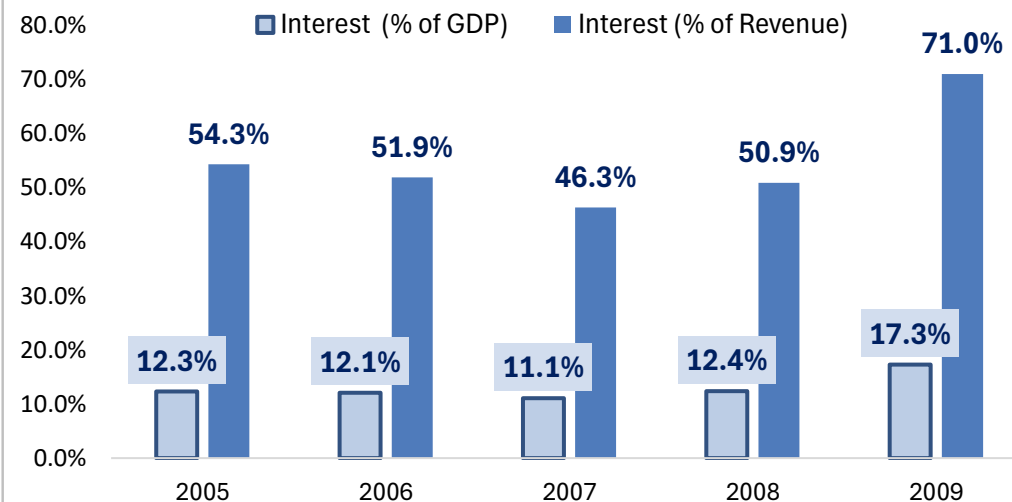
**Government Debt reached 131.6% of GDP in 2009**



**Fiscal deficits reached 11.1% of GDP in 2009**



**Interest Payments peaked in 2009**





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# ***Jamaica's First Domestic Debt Restructuring (2010): Jamaica Debt Exchange (JDX)***

# Jamaica's first domestic debt restructuring: Jamaica Debt Exchange (2010)



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- ✓ The Jamaica Debt Exchange (JDX), launched in January 2010, was a cornerstone of a 27-month IMF Stand-By Arrangement.
- ✓ The initiation of the JDX also helped Jamaica exit its 'SD' rating by S&P in Jan-2010 and earn a 'B- (Stable)' state as early as Feb-2010.
- ✓ The first restructuring focused on three pillars:

## 1. Fiscal Consolidation:

**Structural Changes:** Establishment of the Fiscal Responsibility Framework (FRF) and the Central Treasury Management System (CTMS).

**Public Sector Wage Freeze:** Wage and salary increases for the public sector were frozen.

**Primary Surplus Target:** Primary surplus targets were established, starting from 2010.

**Interest Savings:** 3.5% of GDP.

**Maturity & Amortization:** Reduce debt maturities by 65% over the coming 3 years.

**Public Entity Deficits:** Limit deficits of public entities to 1% of GDP.

## 2. Public Debt Restructuring:

**Target:** About USD 700.0Mn in domestically issued bonds (about 65% of GDP).

**Par-to-Par Voluntary Exchange:** Expensive old debt swapped for a menu of 25 new benchmark securities.

**Lower Coupon:** Averaging 12.5% from around 19.0% seen earlier.

**Maturity Extensions:** Average maturity extended to 8.3 from 4.7 years.

The government used the threat of exercising call options on old bonds, ensuring 100% participation.

## 3. Financial Sector Reform

This pillar focused on establishing measures to prevent the collapse of the local financial system during the period of restructuring.

**Financial System Support Fund (FSSF):** Backed by about USD 950Mn of IMF funds. Provided liquidity support for institutions that participated in at least 90% of the exchange offer.

**Social Safety Net:** 2011 budget increased welfare spending by 40% YoY.

*Yet, within 3 years the JDX failed...*

# Why did the JDX fail?



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## Fiscal slippage

- ✓ While the JDX reduced the interest bill by about 3.5% of GDP, this "breathing room" was quickly consumed by slippages in public sector wage costs.
- ✓ The government failed to meet its primary balance target for 2011 (5.3% of GDP) as the primary balance shrunk to 3.1% of GDP.

## Assumption of SOE debt

- ✓ In 2010, the government took over the debt of several large state-owned enterprises to facilitate the gradual privatization of these entities.
- ✓ Moreover, throughout 2010, the government also recorded previously unrecorded "skeleton" debts and issued debt to settle interest arrears to the Bank of Jamaica.
- ✓ The government continued to guarantee loans for public entities, which further inflated the debt burden.
- ✓ By 2012, government-guaranteed debt had risen to approximately 9.0% of total public debt.

## Economic stagnation

- ✓ Constrained capital infusion, weak external demand for Jamaican exports and crowding out hindered economic growth.
- ✓ In fact, in 2012 the Jamaican economy shrank by 0.6%.

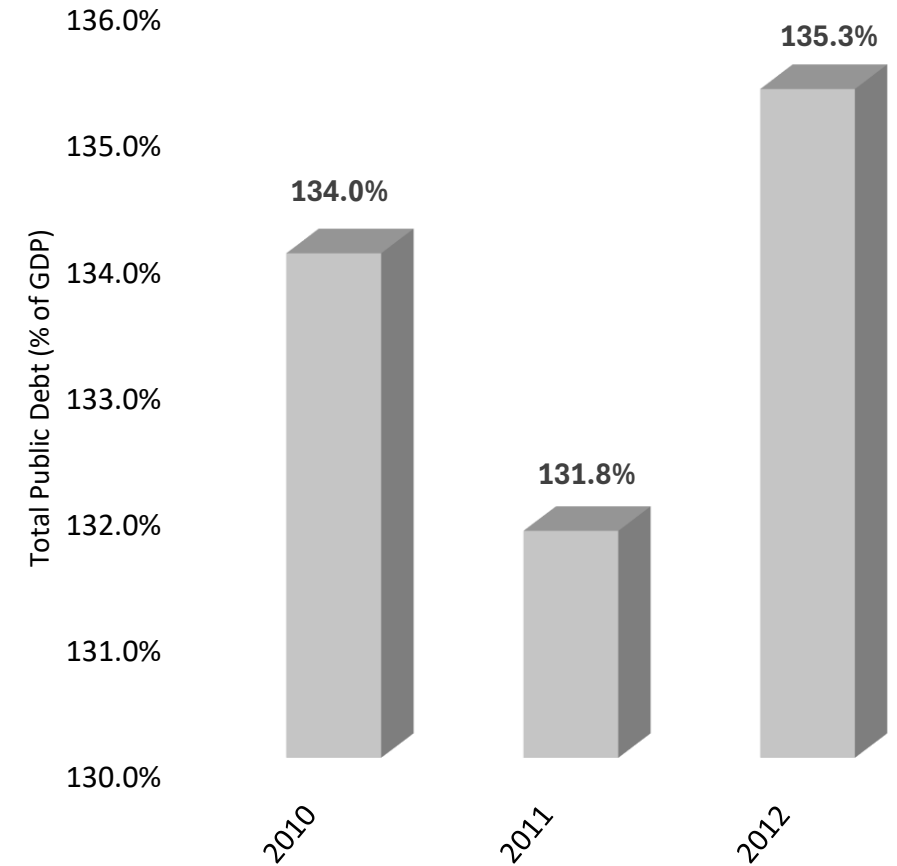
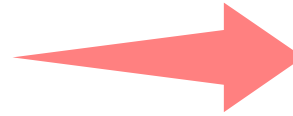
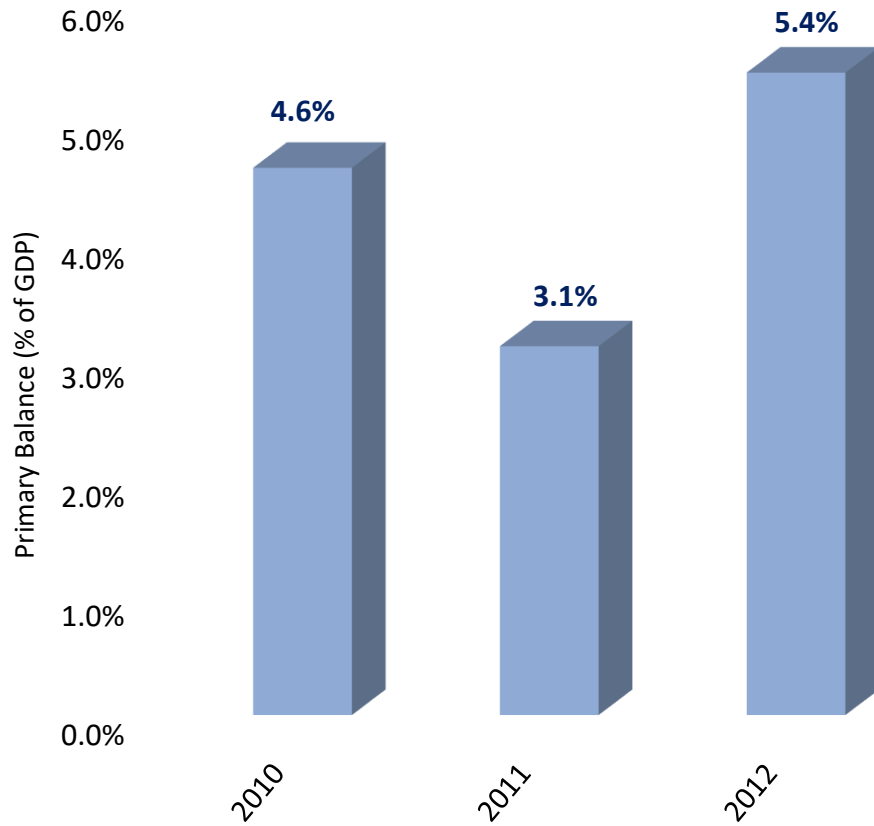
*The JDX did not include a principal haircut. Reduced rates and extended maturities did little to address Jamaica's debt woes, especially given their lack of fiscal discipline and economic growth. At the end of 2012, the overall debt stock had inflated beyond its pre-restructuring level, demanding further action.*

# Lack of fiscal discipline and assumption of SOE debt caused the debt stock to inflate further



As early as 2011, Jamaica failed to meet its primary balance target due to fiscal slippage, leading to new financing needs in 2011 & 2012...

Fiscal slippages and assumption of SOE debt caused the debt stock to inflate further

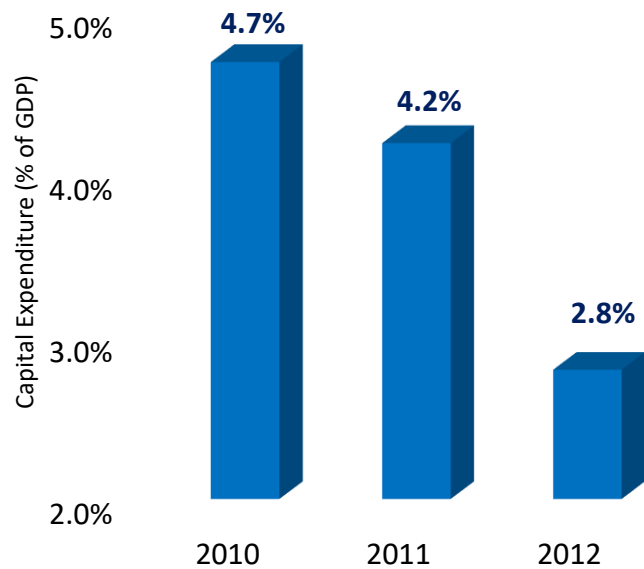


# Austerity measures also induced a state of stagnant growth, further deteriorating the debt to GDP ratio

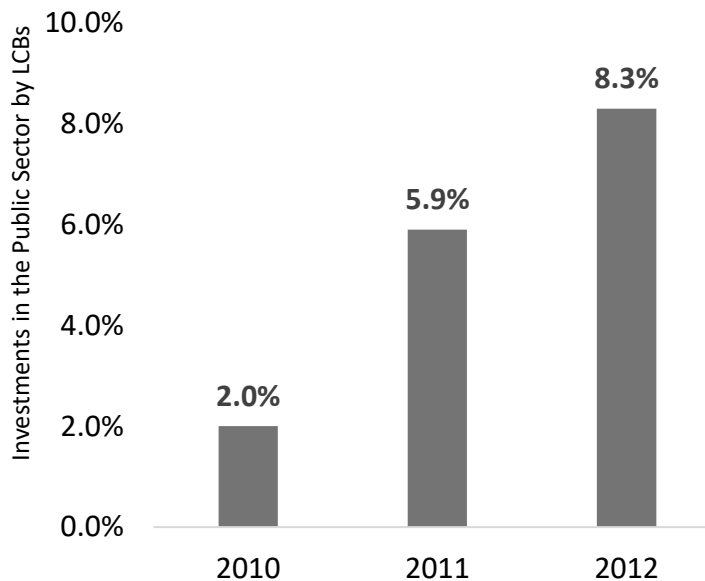


- ✓ While the wage bill eroded fiscal discipline, Jamaica constrained its capital expenditure in 2011 and 2012 to contain a further slippage in fiscal consolidation.
- ✓ On the other hand, the widening of the debt stock due to lack of fiscal discipline and the assumption of SOE debt, continued to crowd out private investment.
- ✓ Driven by these adverse conditions, Jamaica's GDP contracted by -0.6% in 2012.

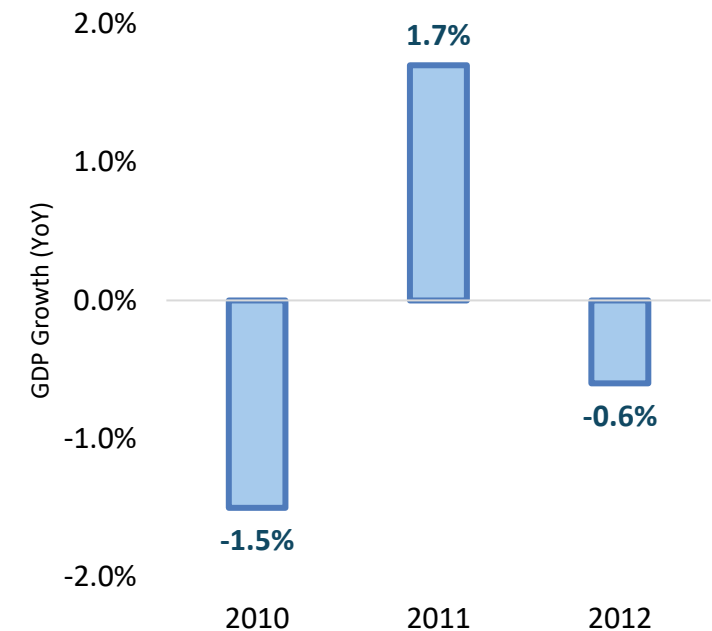
**Capital Expenditure dipped to 2.8% (of GDP) in 2012**



**Higher investments in the public sector by banks crowded out private investments**



**Leading to stunted growth, adversely affecting Debt/GDP**



# The apparent ineffectiveness of the JDX pushed Jamaica's Sovereign Credit Rating back to SD status, warranting a second restructuring



	Rating	Outlook	
Present	BB	Stable	
Jun-2014	B	Stable	
Sep-2014	B-	Positive	
Mar-2013	CCC+	Stable	
Feb-2013	B-	Stable	After 10 days since the SD downgrade, Jamaica was upgraded to B-status (outlook:Stable) given the enactment of the NDX.
<b>Feb-2013</b>	<b>SD</b>		On the 14th of Feb-2013, when Jamaica's debt woes had worsened compared to before the JDX, it was again downgraded to SD status.
Oct-2011	B-	Negative	As Jamaica showed signs of derailing from the JDX, S&P downgraded Jamaica's outlook to 'Negative' from 'Stable'.
Feb-2010	B-	Stable	However, soon after the JDX, Jamaica was upgraded to B- status and the outlook was sited 'Stable'.
<b>Jan-2010</b>	<b>SD</b>		On the 14 <sup>th</sup> of Jan-2010, S&P downgraded Jamaica to SD status.
Nov-2009	CCC	Negative	
Mar-2009	B-	Negative	



# ***Jamaica's Second Domestic Debt Restructuring (2013): National Debt Exchange (NDX)***

# The launch of the NDX



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- ✓ As the first restructuring (JDX 2010) failed to address Jamaica's debt sustainability woes, in 2013, the Jamaican government, with the help of the IMF (via an Extended Fund Facility) formulated its second domestic debt restructuring program called the 'National Debt Exchange' (NDX). Through the NDX, Jamaica had a target of bringing its public debt down to 60.0% of GDP by 2026.
- ✓ While the 2<sup>nd</sup> restructuring also didn't include a haircut, several other factors made it more effective:
  1. **Solving the Wage Bill Problem:** Concluding a multi-year agreement with unions to limit nominal wage increases was a "prior action" required for the EFF program with the IMF. The government committed to a legislated target to reduce the central government wage bill to 9.0% of GDP by FY 2015/16.
  2. **Legally binding fiscal targets:** The authorities adopted a legally binding fiscal rule to be incorporated into annual budgets, ensuring a sustainable balance and a specific pace of debt reduction.
  3. **Elimination of Discretionary Waivers:** As another prior action, the government ceased the granting of discretionary tax waivers, which had previously eroded the tax base.
  4. **Five-Year Investment Program:** To ensure capital spending was efficient and aligned with national priorities, the government introduced a 5-year Public Sector Investment Program (PSIP).
  5. **Addressing deficits of SOEs:** It was mandated that the overall balance of public entities be zero (balanced) starting in FY 2013/14.
  6. **Inclusion of Guaranteed Debt:** For the first time, reporting on public debt was expanded to include domestically guaranteed debt and PetroCaribe debt, providing a more transparent view of the nation's total obligations.
  7. **Further reduction of rates:** The NDX also included a further reduction in rates attached to restructured debt, ranging between 75 to 500bps.

# Following the NDX, the secondary market stayed frozen till about mid-2015



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*The freeze was not caused by a single event but by a combination of investor psychology and technical liquidity shifts:*

- 1. Heightened Risk Premium:** Because the NDX was the second restructuring in only three years, investors demanded a much higher risk premium on government instruments. There was a lingering perception that another restructuring could happen if reforms failed again.
- 2. Reluctance to Trade at Discounts:** Market participants were unwilling to restart trading at "overly discounted prices" that would force them to realize further capital losses on their portfolios.
- 3. Confidence Gap:** Against a decades-long history of reform failure, many investors required a longer track record of success before they were convinced the current program would be sustained.
- 4. Reduced Cash Flow:** The successful reduction of the government's interest bill meant that the regular flow of cash from the government to the financial sector (interest and principal payments) significantly declined.
- 5. Technical Liquidity Squeeze:** Tight conditions were exacerbated by Bank of Jamaica (BOJ) sterilization (to meet reserve targets) and the implementation of the Central Treasury Management System (CTMS), which moved government balances out of commercial banks and into a single treasury account.

*Actions taken to address the liquidity freeze:*

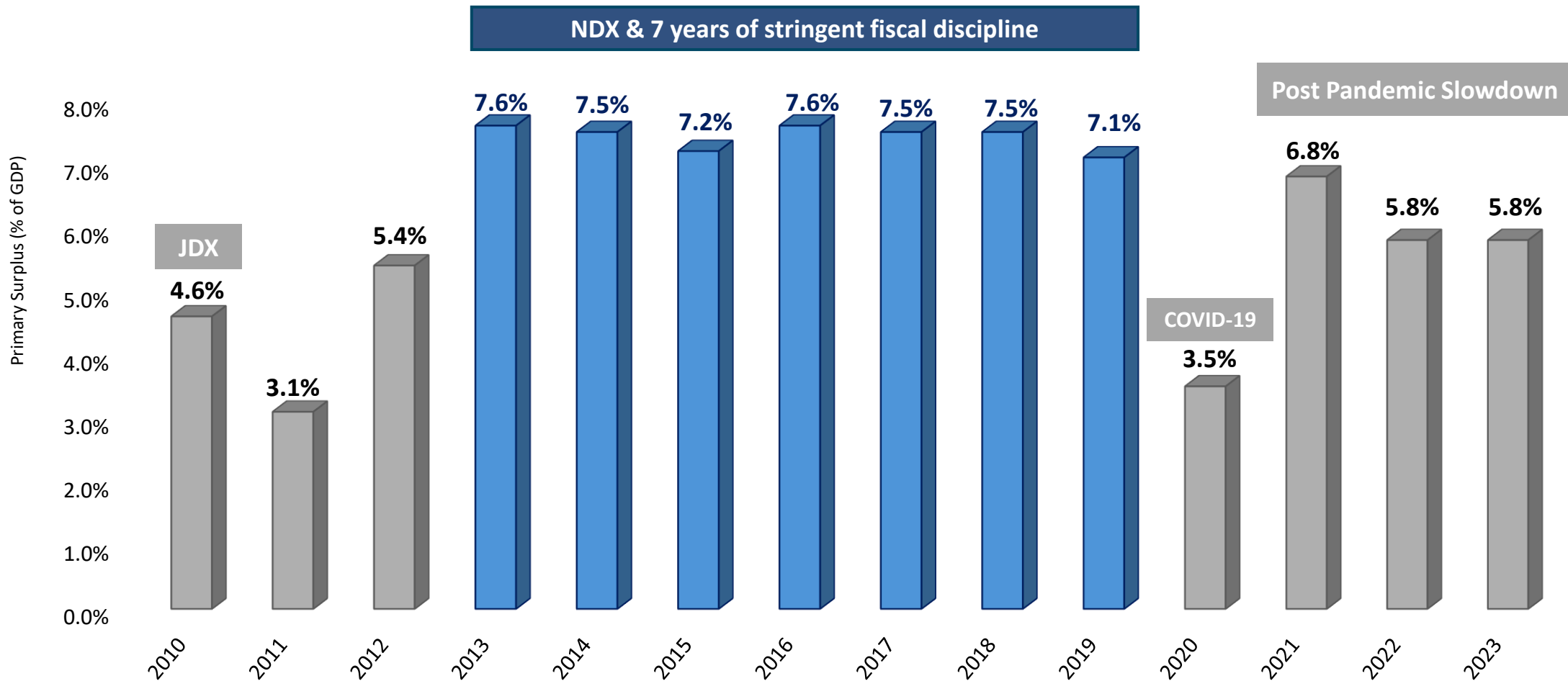
- ✓ **BOJ Liquidity Injections:** To prevent a full-blown credit crunch, the BOJ introduced several new facilities.
- ✓ **Interest Rate Management:** The BOJ moved from managing quantities of money to interest rate targeting by narrowing the interest rate corridor (lowering rates by 75 basis points in early 2015) to provide clearer guidance to the market.
- ✓ **Direct IMF Budget Support:** Because the government could not borrow from a frozen domestic market, the IMF rephased its disbursements to provide direct budget support to meet short-term cash flow needs in 2014.
- ✓ **Price Discovery Efforts:** The authorities explored "unfreezing" the market by having the BOJ offer to purchase securities via variable rate auctions to catalyze price discovery between institutions.

# The framework legislated a path to reduce the debt-to-GDP ratio to 60.0% by 2026



*Stringent fiscal discipline was key...*

Since the NDX in 2013, an average primary surplus of 7.4% was maintained up to 2020...

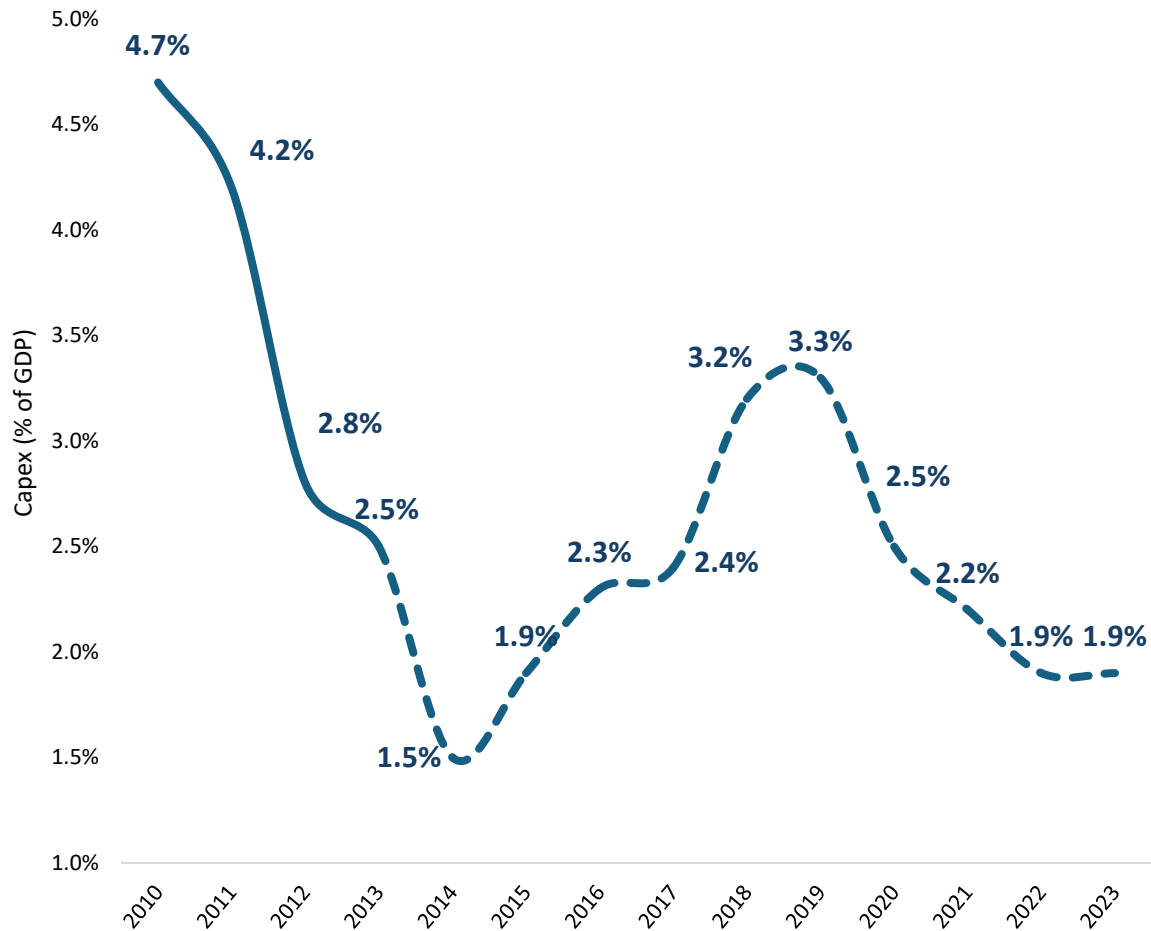


# Capital expenditure stagnated at the hands of persistent fiscal consolidation



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Primary surplus targets of the NDX induced a stagnation of capex, marking 2013-2023 as the "lost decade" for investments



- ✓ Constrained capital expenditure stalled the development of roads, water systems and general physical infrastructure.
- ✓ This also created a "major educational deficit," with underfunded early childhood programs producing generations ill-equipped for a knowledge-driven economy.
- ✓ The scarcity of resources contributed to persistent social issues, including high youth unemployment and a homicide rate that remains among the highest in Latin America and the Caribbean.



# Moreover, the treasury's cash buffers (savings from the NDX) were not efficiently re-directed to the real economy to stimulate private investments



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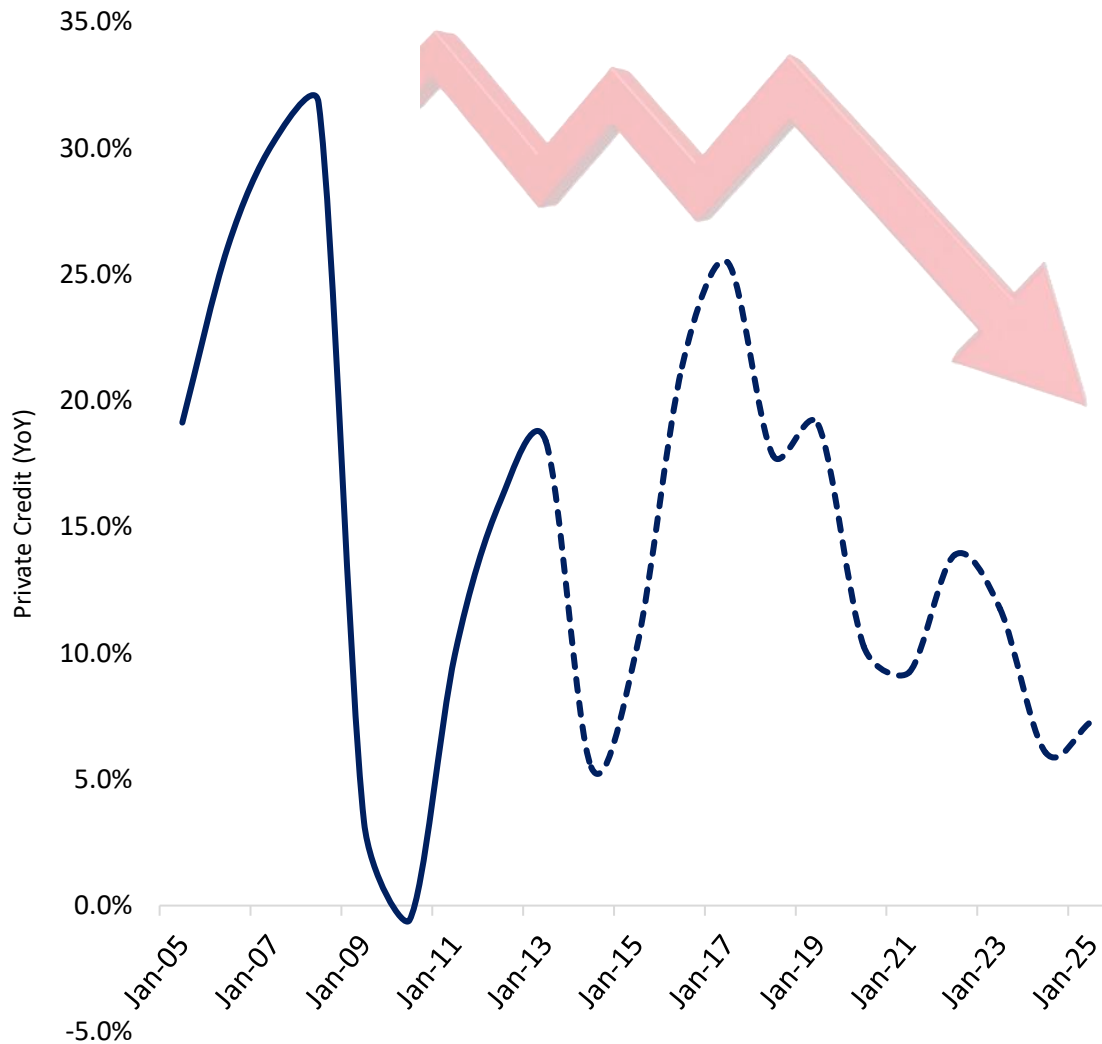
- ✓ A major objective of the NDX was to minimize the crowding out of private funds and re-direct the primary surpluses, or rather the savings from the NDX to the real economy.
- ✓ However, Jamaica lacked an efficient mechanism through which this re-direction could take place.
- ✓ The "excess funds" generated by Jamaica's primary surpluses were managed through the Central Treasury Management System, which utilized a single account (Treasury Single Account OR TSA) at the Bank of Jamaica.
- ✓ A Financial Sector Support Fund (FSSF) was also established to extend liquidity support to deposit taking institutions that engaged in the NDX. However, this existed more as a mechanism to support financial institutions that faced vulnerabilities due to the restructuring.
- ✓ While the BoJ regularly conducted auctions to manage systemic liquidity, the cash buffers from the Treasury were largely held at the BoJ to provide the government with the fiscal space to manage debt and respond to external shocks without needing to borrow further from the private market (these cash buffers were mainly put to use during the pandemic and in 2023 when Jamaica issued its first Jamaican Dollar denominated International Bond).



# As a result, growth in private credit was also limited



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Major reasons for the poor credit performance post-restructuring:

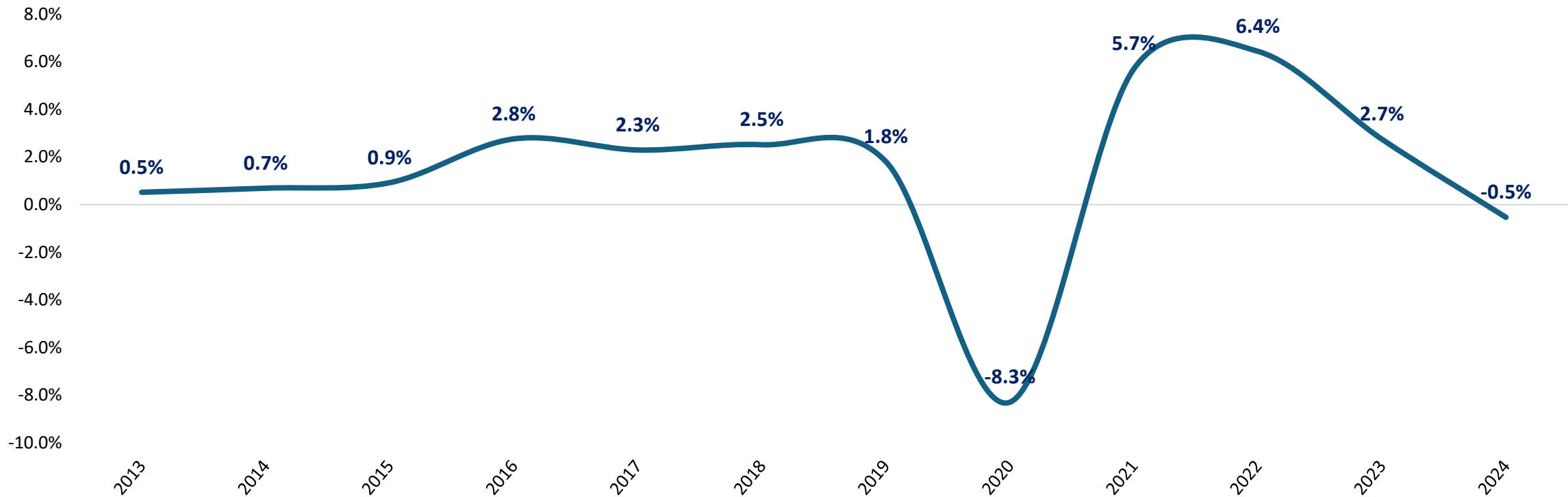
- **Frozen Bond Market:** The inactivity of the secondary market for government bonds since the 2013 exchange reduced the liquidity of what was once the financial sector's primary asset.
- **Liquidity Squeeze:** Financial market conditions tightened due to liquidity sterilization by the Bank of Jamaica (BoJ) and lower government debt-service payments following the restructuring.
- **Impact of the NDX on Banks:** The 2013 exchange imposed direct income and fair value losses on banks through coupon cuts and maturity extensions.
- **Shift in Credit Composition:** New credit became increasingly concentrated in retail credit (consumer loans). Banks were notably reluctant to extend credit at longer maturities to fund corporate investment, which hindered the productive capacity of the economy.

# After the economic contraction in 2012, growth was largely positive, but visibly sluggish



- ✓ Following the National Debt Exchange (NDX) in February 2013, Jamaica's economic growth shifted from contraction to a fragile and gradual recovery, though it remained sluggish throughout the early years of the reform program.
- ✓ While the economy broke a cycle of negative growth, the recovery was frequently hampered by environmental shocks and the near-term costs of aggressive fiscal consolidation.

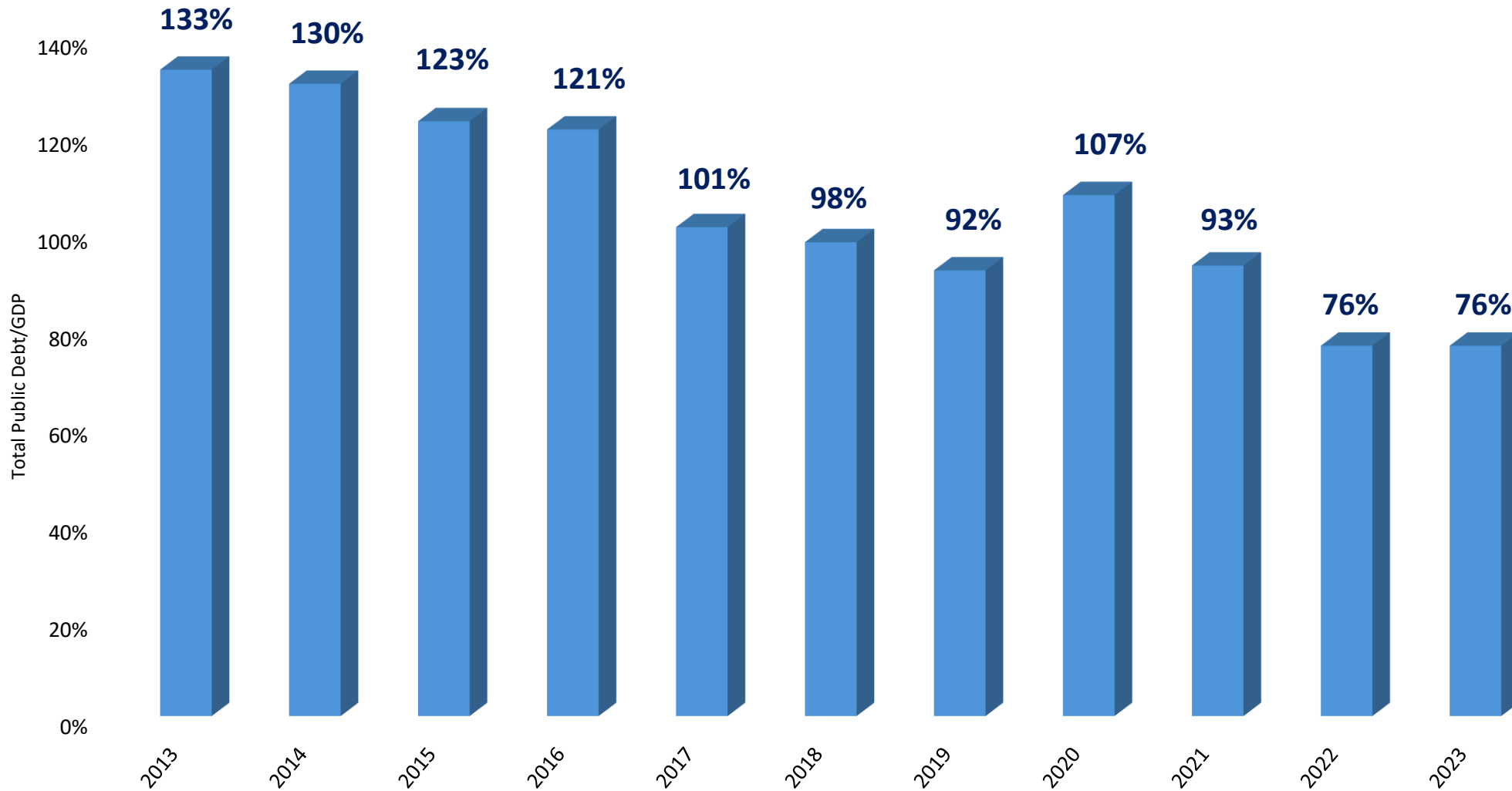
***Jamaica's post-NDX real GDP growth averaged to about 1.5% (2013 to 2024)***



# However, Jamaica did achieve the debt sustainability goals set forth by the NDX



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# ***Where does Sri Lanka Stand?***

DEBT

# Sri Lanka is now at a crucial cross-road...

- ✓ Sri Lanka is now at a unique position compared to Jamaica.
- ✓ Unlike Jamaica's debt woes, which were largely domestic, Sri Lanka has a severe external debt problem.
- ✓ However, at present, similar to post-NDX Jamaica, fiscal discipline seems to be on-going.
- ✓ Moreover, private credit has also remained robust, and growth prospects appear far from stagnant.
- ✓ A slow growth scenario could in fact delay restoration of international confidence and Sri Lanka's entry to the international bond market.
- ✓ Thus, in the face of sluggish growth, Sri Lanka has much more to lose than Jamaica did after its second restructuring.
- ✓ The report discusses 3 potential scenarios that could play out moving forward.



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# Scenario 1: Fiscal discipline continues, but growth remains sluggish



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- ✓ Since Sri Lanka entered an EFF program with the IMF, fiscal discipline has been maintained. Sri Lanka has met its primary balance targets (as a % of GDP) consistently (2023: 0.6%, 2024: 2.2%, 2025: 5.4%).
- ✓ Similar to what Jamaica saw during its second restructuring (NDX), it is probable that Sri Lanka would continue to tread on this path of fiscal discipline.
- ✓ Even beyond the IMF-EFF program, Sri Lanka is still legally bound to and adequately incentivized to remain on a path of fiscal consolidation:

## CBSL Act of 2023

Prohibits deficit financing through CBSL & Makes it challenging to finance fiscal slippages without putting pressure on domestic rates.

## Public Financial Management Act of 2024

Establishes a ceiling on primary expenditure of 13.0% of GDP.

## Contractual Bindings in Sovereign Bonds

The 2024 debt restructuring introduced legal "triggers" that create direct financial consequences for SL.  
Eg: Governance Linked Bonds

- ✓ This continuation of fiscal discipline (similar to NDX, and similar to what SL has seen since 2023) is likely to come at the cost of limited capital expenditure.
- ✓ However, unlike in Jamaica, Sri Lanka so far has managed to re-direct a large chunk of this surplus cash into the private banking system. This is because most of treasury's cash balances are parked at state banks (while Jamaica had a Treasury Single Account), which is then lent to the private banks through the repo market.
- ✓ However, the Public Financial Management Act (PFMA) of 2024, stipulates that Sri Lanka too adopt a Treasury Single Account (TSA). If a TSA is established within the CBSL (similar to Jamaica having one at the Bank of Jamaica), there is a possibility that the transmission of treasury cash surpluses to the financial system will be impaired, hindering private sector credit growth.
- ✓ **If this backdrop materializes Sri Lanka is expected to tread on a similar path to post-NDX Jamaica.**

## Scenario 2: Fiscal discipline continues & growth remains intact

- ✓ This is essentially a scenario in which, the economic stability witnessed in 2024 and 2025 persists in the medium term.
- ✓ Fiscal discipline would hold firm and even amid limited capex infusion, the robust translation of primary surpluses into overall financial sector liquidity (treasury cash buffers parked at state banks being diverted to the private banking system through the repo market) would supplement growth.
- ✓ This scenario primarily hinges on the possibility that private sector credit growth would continue, albeit at a lower pace to what we saw in 2025, oiling the wheels of the real economy.
- ✓ Continued fiscal discipline would restore confidence in Sri Lanka, allowing SL to enter the international bond market in time.
- ✓ While large external debt repayments kicking in from 2028 would pose some friction, a scenario where private sector credit does not stagnate would ensure that the economy would continue to expand in the medium term while holding debt-sustainability intact.

## Scenario 3: Fiscal discipline derails, compromising debt sustainability

- ✓ This scenario takes into account a derailment of Sri Lanka's fiscal consolidation path, particularly following the expiration of the IMF-EFF program.
- ✓ This would not only impair international confidence in Sri Lanka, preventing its entrance to the international bond market, but would also trigger higher interest payments given the criterion embedded in governance linked bonds.
- ✓ Such a scenario would be similar to Jamaica's post-JDX (the failed 1<sup>st</sup> restructuring), where the domestic debt stock would balloon, in turn putting pressure on interest rates, warranting a possible second restructuring.





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