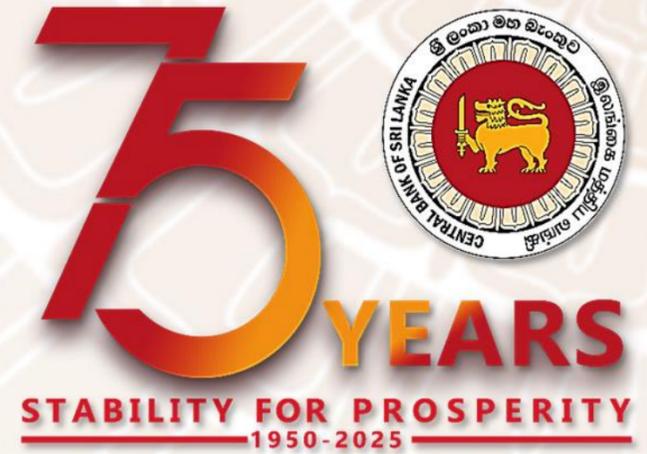


**75<sup>th</sup> Anniversary Oration of the Central Bank of Sri Lanka**



# **Why Central Bank Independence Matters**

*– in Crisis, in Recovery, and Beyond*

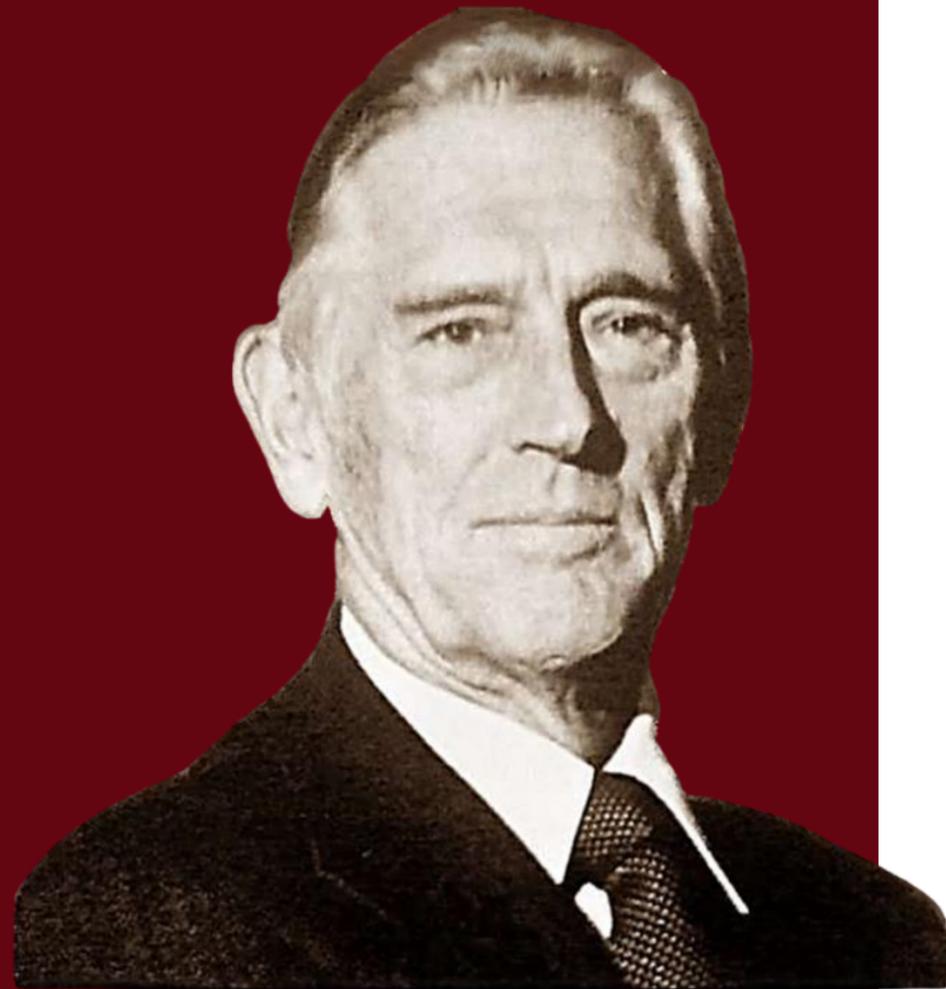
**by**

**Governor Dr. Nandalal Weerasinghe**

29 August 2025

# Establishment of the Central Bank of Ceylon

Seven and a half decades ago,  
in **1950**, our nation took a  
momentous step towards economic  
sovereignty with the establishment  
of the **Central Bank of Ceylon...**



John Exter, Founder Governor, Central Bank of Sri Lanka

# OUTLINE

**Understanding Central Bank Independence**

**From the MLA (1949) to CBA (2023)**

**Addressing Common Myths and Criticism**

**Concluding Remarks – Preserving Independence**

# OUTLINE

## Understanding Central Bank Independence

- What is central bank independence?
- Why does independence matter?
- Role of Accountability
- Global Case Studies

From the MLA (1949) to CBA (2023)

Addressing Common Myths and Criticism

Concluding Remarks – Preserving Independence

# What is central bank independence?

**“Independence is part of  
the DNA of central banks”**

**-Joachim Nagel, President of Deutsche Bundesbank**

**“The record is pretty clear” that central bank independence is “a good institutional arrangement that serves the public well.”**

**- Jerome Powell, Chairman of the Federal Reserve**

**Empirical evidence shows that central bank  
independence is associated with  
LOWER AND MORE STABLE INFLATION  
without THE TRADE-OFF OF LONG-TERM  
GROWTH STAGNATION...**

# Why does independence matter?

**Central bank independence matters because it allows monetary policy to be shaped to support**

**LONG-TERM ECONOMIC STABILITY**

**without being subject to**

**SHORT-TERM POLITICAL PRESSURE...**

**Central bank independence is also a critical  
requirement for maintaining  
FINANCIAL SYSTEM STABILITY...**

# Role of accountability

**“Because monetary policy actions have profound effects on the lives of ordinary people, a central bank in a democracy owes these folks an explanation of what it is doing, why, and what it expects to accomplish. It’s their economy, not ours.”**

**- Alan Blinder, Former Vice Chair of Federal Reserve (1998)**

**Central banks must ensure that the public and  
politicians see our decisions as  
UNDERPINNED BY OUR MANDATE and the  
BROADER INTEREST OF SOCIETY...**

**TRANSPARENCY** helps bridge  
**INDEPENDENCE** and **ACCOUNTABILITY**...

**“For society to appreciate our roles, we... have got to take society along with us, such that when central banks come under attack, it is not just going to be us defending our independence”**

**- Lesetja Kganyago, Governor of South African Reserve Bank**

A faint, light-colored world map is centered in the background of the slide, showing the outlines of all continents.

# Global case studies

# When Independence has worked: Some examples



# When Independence was compromised

**“Through history, we have had quite substantial episodes where monetary policy mismanagement has led to devastating effects - in inflation, in financial systems, affecting the wellbeing of individuals and firms, oftentimes bringing countries to the brink.”**

**- Agustín Carstens, Former General Manager of BIS**

# When Independence was compromised: Some examples



Germany



Argentina



Zimbabwe



United States



Note: Images are sourced from the web

**The ability of a central bank to**  
**ACT DECISIVELY,**  
**MAINTAIN CREDIBILITY,**  
**and provide a STEADY ANCHOR** in the storm  
**of economic uncertainty, is the result of**  
**INDEPENDENCE...**

# OUTLINE

## Understanding Central Bank Independence

### From the MLA (1949) to CBA (2023)

- Pressing need for new legislation on central banking
- An Aside: What if the new CBA had been in place during the crisis?
- How the Central Bank helped stabilise the economy following the crisis – even under the MLA

## Addressing Common Myths and Criticism

## Concluding Remarks – Preserving Independence

# **Pressing need for new legislation on central banking**

**The MLA was a**

# **PIECE OF LEGISLATION FAR AHEAD OF ITS TIME**

**It incorporated many forward-looking features and provisions designed to facilitate sound central banking practices and principles - some of which that remain relevant even today...**

**While the MLA had served its purpose for decades, it had  
NOT UNDERGONE A COMPREHENSIVE REVIEW**

**in line with the evolving challenges of  
monetary and financial stability**

**...key deficiency of the MLA was that the success of  
policymaking was person dependent...**

**“The effectiveness of co-operation and coordination between the Monetary Board and the Government will depend more upon the men occupying the key positions at particular times than upon any legal formula, no matter how carefully or elaborately it might be worked out.”**

**– John Exter**

**While the autonomy of the Central Bank was compromised from time to time, there were notable instances where the**

**MONETARY BOARD EXERCISED INDEPENDENT**

**JUDGEMENT**

**- even with the Secretary to the Treasury  
as a member...**

**Recognising the deficiencies and evolving needs,  
the CBSL initiated a process to modernise its  
governing legislation in 2017**

**In April 2018, a **CABINET MEMORANDUM** was  
submitted seeking approval in principle for  
reforms to the country's Central Bank law...**

# The drafting of the CBA was guided by three overarching objectives:

- 1** Strengthening the governance of the institution
- 2** Securing independence and accountability to support the adoption of FIT and ensure durable price stability
- 3** Enhancing financial sector oversight and resilience

## **An Aside: What if the New CBA had been in place during the crisis?**

**The failure to enact the new CBA in 2019  
was a MISSED OPPORTUNITY  
of historic proportions...**

**Under the revised framework, the CBSL would have been empowered to resist **EXCESSIVE MONETARY FINANCING**, maintain a credible **COMMITMENT TO PRICE STABILITY**, and allow **GREATER EXCHANGE RATE FLEXIBILITY**.**

**...These institutional safeguards could have prevented the build-up of vulnerabilities that ultimately pushed the economy to the brink...**

**Even if the crisis, rooted in fiscal mismanagement,  
could not have been entirely avoided, an empowered  
and independent Central Bank would have acted  
SOONER and MORE DECISIVELY,  
MITIGATING THE SEVERITY OF THE  
ECONOMIC DISTRESS...**

**Sri Lanka's recent experience has reaffirmed  
a fundamental truth:**

**CENTRAL BANK INDEPENDENCE**

**IS NOT A LUXURY – IT IS A NECESSITY...**

# **How the Central Bank helped stabilise the economy following the crisis - even under the MLA?**

**“Price stability and prevention of crises are indeed the core goals of central banking. But it is the central bank’s ability to react effectively to crisis situations that most test their skills and preparedness. Over the years, failure to contain financial crises has entailed enormous economic costs.”**

**– Patrick Honohan, Former Governor of Bank of Ireland**

**Sri Lanka encountered**  
**an UNPRECEDENTED CRISIS in 2022**  
**marked by severe balance of payments**  
**pressures, social and political unrest, and a**  
**profound loss of confidence in institutions, all**  
**while an external debt default loomed...**

**The Government eventually sought**

**IMF ASSISTANCE**

**and**

**ANNOUNCED A DEBT STANDSTILL**

**as an interim measure, paving the way for debt  
restructuring negotiations...**

**The Government and the Central Bank  
implemented a bold  
STABILISATION PACKAGE**

**Notably, replacing the MLA with the new CBA  
enshrined greater independence and  
accountability in the new legislation...**

**Still under the MLA, the CBSL adopted**  
**AN EXTENSIVE ARRAY OF MEASURES**  
**to stabilise the economy and recover from its dire**  
**straits since the onset of the crisis in early 2022**

**As a result, inflation was brought down from a peak of**  
**nearly 70% in September 2022 to single digits by**  
**mid-2023, with price stability maintained since then...**

# **SRI LANKA AVOIDED A SYSTEMIC BANKING CRISIS**

- a **REMARKABLE ACHIEVEMENT**

**given the depth of the economic and debt turmoil...**

**CBSL worked tirelessly to**  
**RESTORE PUBLIC CONFIDENCE**  
**- through frequent communications,**  
**press briefings, and transparent explanations of**  
**policy decisions...**

# **Provisions for independence and accountability in the New CBA**

**The enactment of the CBA in 2023**  
**marked a**  
**LANDMARK STRUCTURAL REFORM,**  
**significantly strengthening the**  
**independence of the CBSL**  
**to perform its streamlined mandate...**

# Key provisions on independence and accountability

**Objects of the Central Bank**

**Section 6**

**Monetary Policy Board (Under a FIT framework)**

**Section 11**

**Fiscal-Monetary Coordination**

**Section 83**

**Prohibition of Monetary Financing**

**Section 86**

**Monetary Policy Framework Agreement**

**Section 26**

**Monetary Policy Report & Annual Economic Review**

**Sections 27 & 80**

**Administrative and Financial Autonomy**

**Section 5**

**Appointment of the Governor and other appointed members**

**Sections 15 & 19**

**How do CBA provisions on independence and accountability, and activities since the introduction of the CBA benefit the nation?**

**Monetary financing**  
**NO LONGER OCCURS**  
**under the CBA...**

**Several provisions have been made in the CBA  
to increase the **ACCOUNTABILITY** of the  
Central Bank under the FIT framework...**

**As the **MACROPRUDENTIAL AUTHORITY****  
**in Sri Lanka, the CBSL is empowered**  
**to independently monitor systemic risks and**  
**proactively safeguard financial system stability...**

**Strengthening the**  
**BROADER LEGAL FRAMEWORK**  
**governing Sri Lanka's financial sector...**

**Banking (Amendment) Act, No. 24 of 2024**

**Banking (Special Provisions) Act, No. 17 of 2023**

**CBSL has intensified its efforts to advance**  
**FINANCIAL INCLUSION and**  
**enhance FINANCIAL LITERACY...**

# OUTLINE

Understanding Central Bank Independence

From the MLA (1949) to CBA (2023)

## Addressing Common Myths and Criticism

- Is there no coordination between the Central Bank and the Government?
- Is the CBSL beyond Sovereignty and accountable only to external agencies?
- Is the CBSL's financial independence a new concept?
- Independence vs. expectations: What can the CBSL truly deliver?
- The Central Bank's role in conducting agency functions

Concluding Remarks – Preserving Independence

**“Any public job involves both undue praise and unfair criticism... yet it is the latter that is probably more useful in helping you sharpen your message.”**

**- Raghuram Rajan, Former Governor of RBI (2017)**

## **Myth 01:**

**Is there no coordination between the Central Bank and the Government?**

**Coordination between monetary and fiscal  
authorities remains **ESSENTIAL****

**The CBA ensures this through the  
establishment of a statutory  
**COORDINATION COUNCIL...****

**CBSL works closely with the Government,  
international financial institutions, and  
other regulators, particularly in the areas  
of **CRISIS MANAGEMENT** and  
**FINANCIAL SYSTEM OVERSIGHT...****

## **Myth 02:**

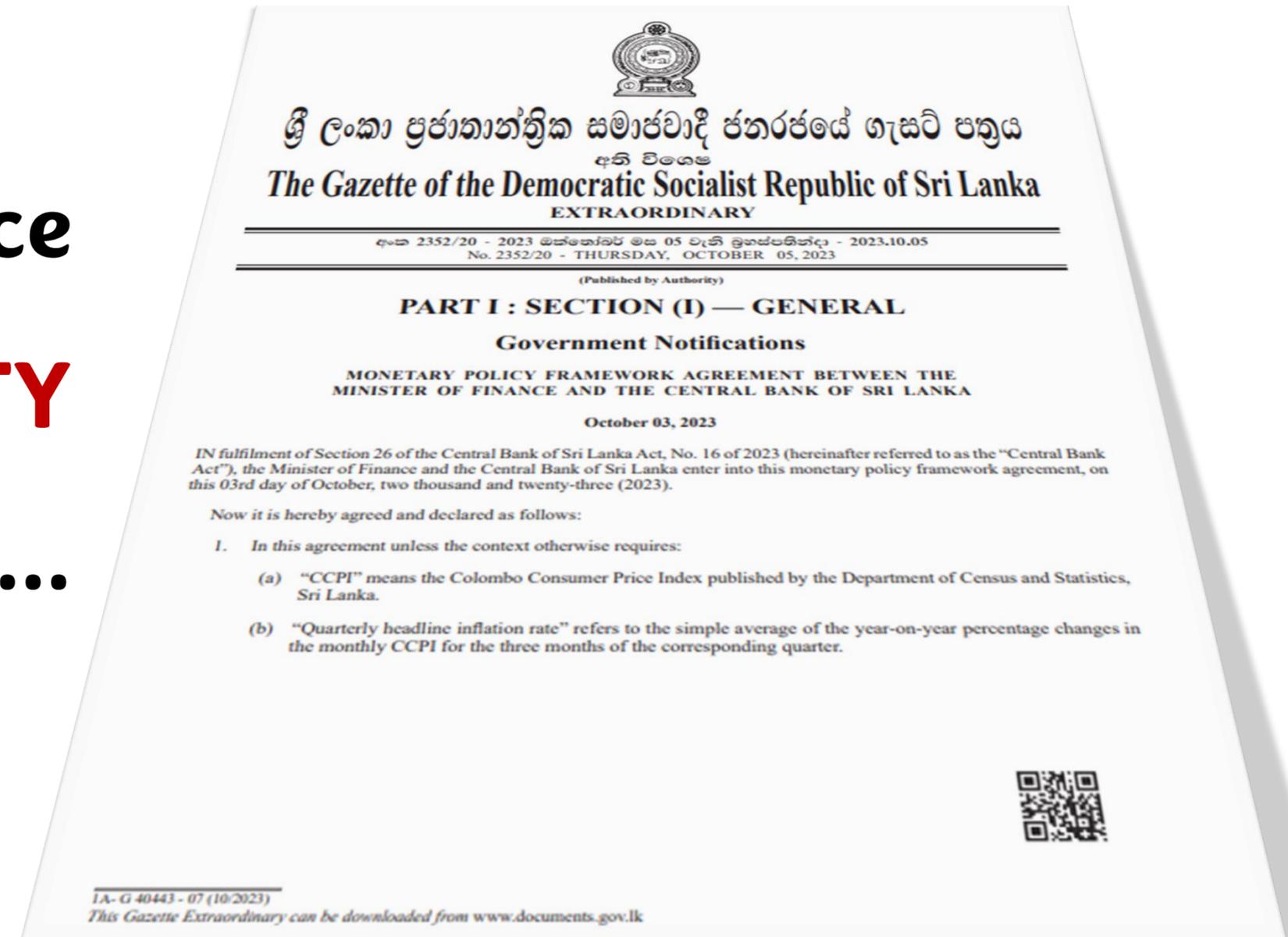
**Is the CBSL beyond Sovereignty and accountable only to external agencies?**

**The CBA provides a**  
**ROBUST FRAMEWORK**  
**to ensure the CBSL's accountability to**  
**Parliament and, ultimately,**  
**to the people of Sri Lanka...**

# Ministry of Finance

## SHARES RESPONSIBILITY

### for setting the inflation target...



**CBSL also serves as the**  
**GOVERNMENT'S REPRESENTATIVE**  
**in fostering international relations**  
**with institutions such as the IMF...**

## **Myth 03:**

**Is the CBSL's financial independence a new concept?**

**The CBSL's independence is  
not entirely a new thing, but it has been  
**SIGNIFICANTLY STRENGTHENED**  
under the CBA**

**Even under the MLA, the CBSL was vested with a  
high degree of financial independence...**

## **Myth 04:**

**Independence vs. expectations:  
What can the CBSL truly deliver?**

**Core objective is to achieve and maintain**

**DOMESTIC PRICE STABILITY**

**...also tasked with securing**

**FINANCIAL SYSTEM STABILITY...**

**CBSL's role is to create an**  
**ENABLING ENVIRONMENT OF STABILITY,**  
**within which the Government and other**  
**authorities can implement**  
**growth-oriented policies...**

**Under the current flexible exchange rate regime mandated by the CBA, the value of the Sri Lanka rupee is determined by**

**MARKET FORCES...**

## **Myth 05:**

# **The Central Bank's role in conducting agency functions**

**CBSL has been ENTRUSTED through various statutes with the responsibility of carrying out**

**VARIOUS AGENCY FUNCTIONS**

**on behalf of the Government...**

**This has arisen due to the**  
**PUBLIC TRUST,**  
**as well as the absence of**  
**other acceptable**  
**INSTITUTIONAL ARRANGEMENTS...**

# Concluding Remarks

**Preserving independence is indispensable** to safeguarding the stability and prosperity of a nation

History and global experience demonstrate that central banks with **clearly defined mandates are best positioned to deliver on their promises**.

**Transparency** and **open communication** are essential to building public trust

Effective macroeconomic management requires **constructive dialogue and coordination** between the Central Bank and the Government, particularly on fiscal, monetary, and financial sector policies

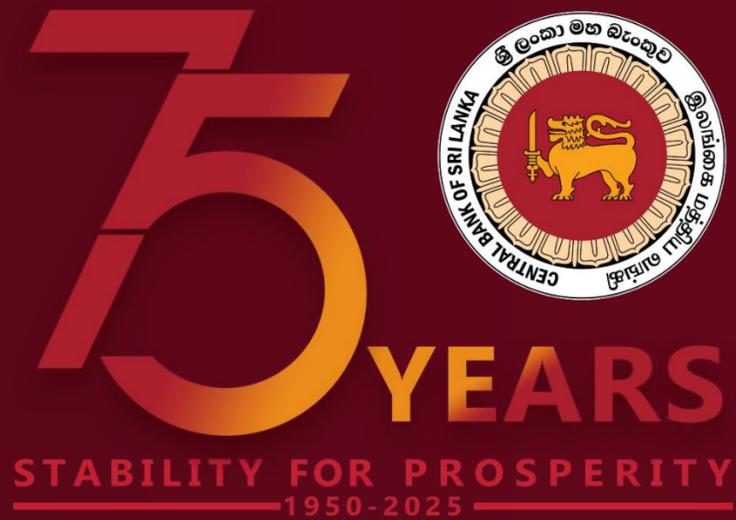
**“While recent research suggests that de jure central bank independence has never been more prevalent than it is today, there is no doubt that the de facto independence of central banks is being called into question in several parts of the world.”**

**- Christine Lagarde, President of ECB**

**“Central bank independence is a fine institution that ought to be preserved where it exists and emulated where it does not.”**

**- Alan Blinder**

It is the  
**RESPONSIBILITY OF FUTURE  
GENERATIONS**  
to  
**PROTECT, PRESERVE, and PROMOTE**  
the independence of the Central Bank  
to serve as a steadfast anchor of stability  
for sustainable growth and  
shared prosperity...



**75<sup>th</sup> Anniversary Oration**  
**Now available at:**



**Thank you**