

1950-2020 **Stability**
Sustainability
Shared Prosperity



Review of the Monetary Policy Stance

August 2020

Economic Research Department
Central Bank of Sri Lanka

Decision

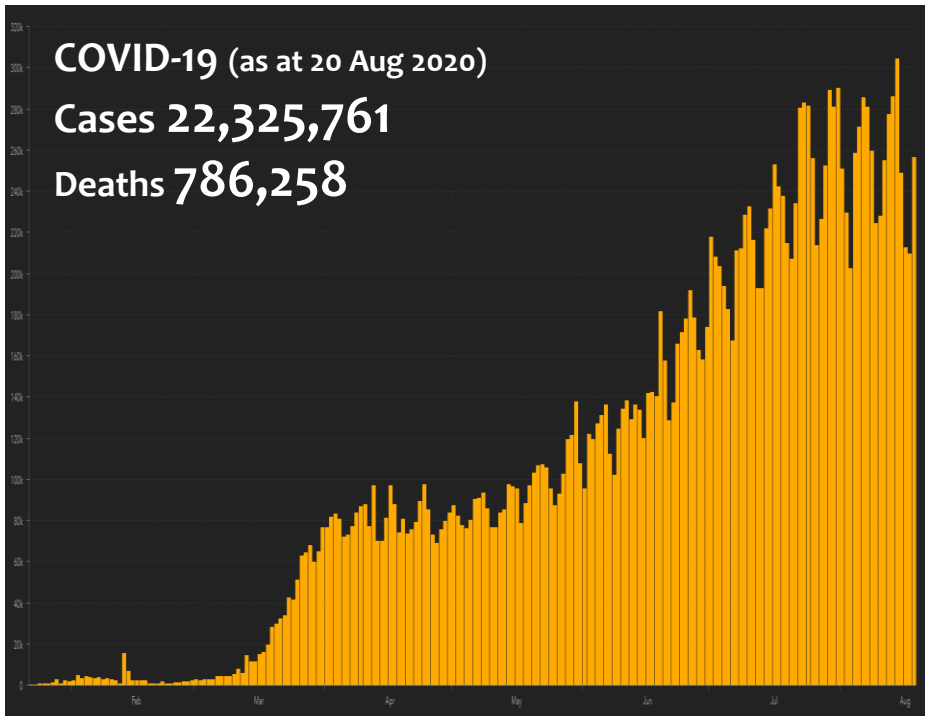
Policy rates and SRR unchanged

Standing Deposit Facility Rate (SDFR)	4.50%
Standing Lending Facility Rate (SLFR)	5.50%
Bank Rate	8.50%
Statutory Reserve Ratio (SRR)	2.00%

Regulated interest rates revised downwards

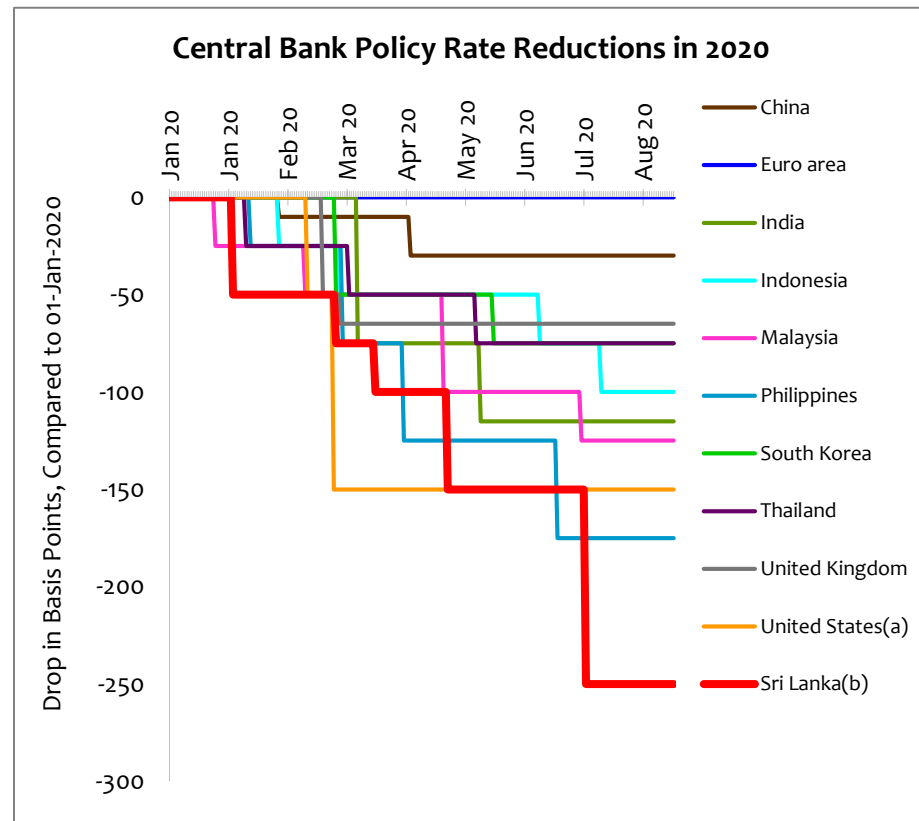
Maximum interest rate on Credit Cards	18.00%
Maximum interest rate on Pre-arranged Temporary Overdrafts	16.00%
Maximum interest rate on Pawning Facilities	10.00%
Penal interest rate over the regular interest rate	2.00 p.p

Global monetary easing continued amidst the rapid spread of the COVID-19 pandemic...



Source: Johns Hopkins University

Most advanced countries have recorded significant contractions in Q2 2020

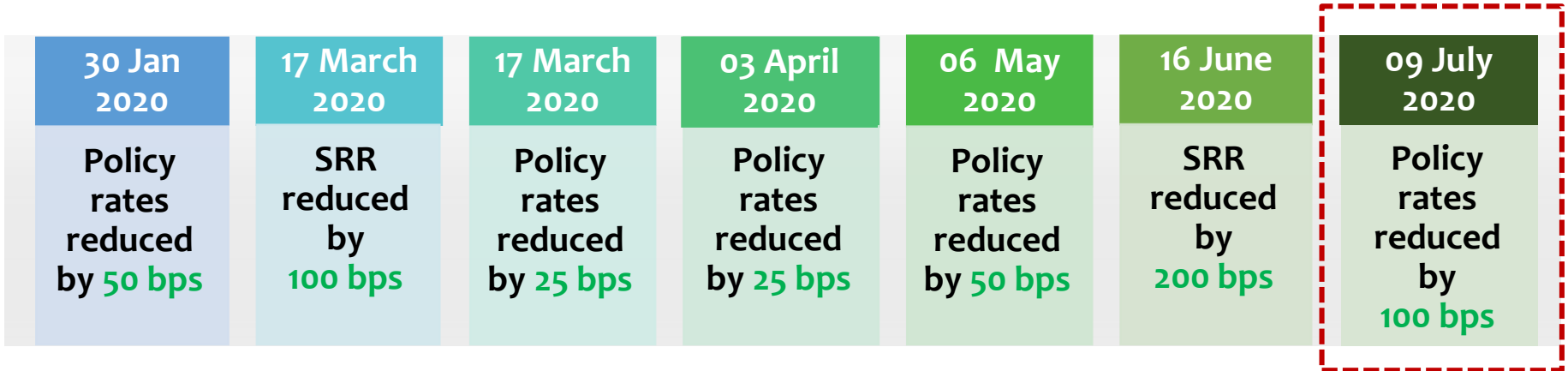


Notes: (a) Mid Point of Target Federal Funds Range (b) Mid Point of SDFR & SLFR

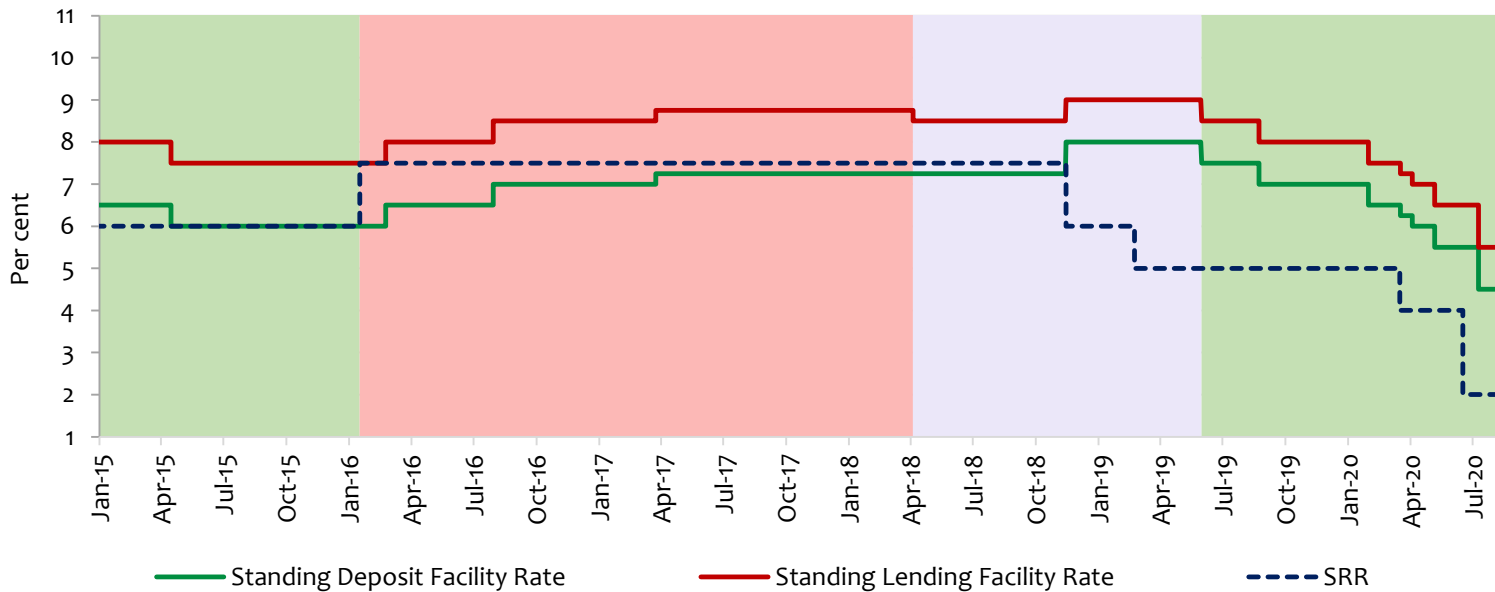
Central banks around the world continued to implement monetary easing measures, alongside fiscal stimulus by respective governments, in support of the recovery of economic activity



A series of policy measures implemented during 2020 in view of the spread of COVID-19 pandemic to support economic activity...



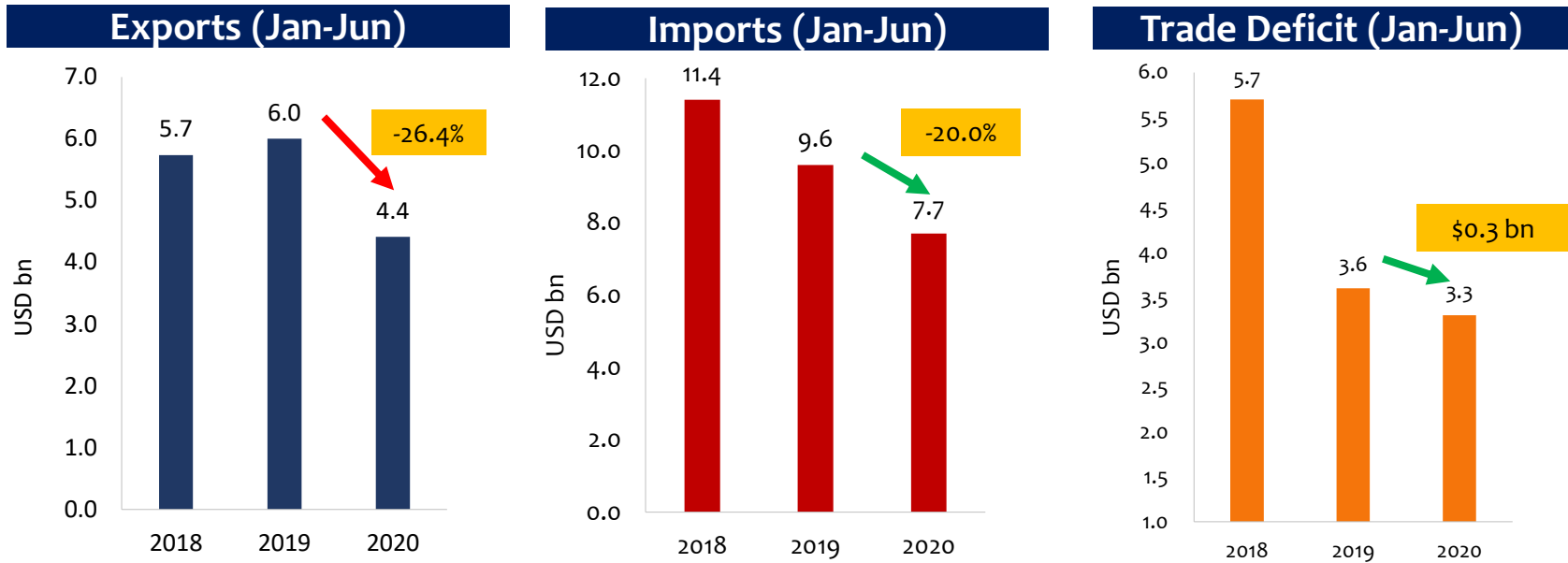
The Monetary Policy Cycle



- The Central Bank reduced policy interest rates by **250 bps** so far in 2020 and **100 bps** in 2019
- SRR reduced by **300 bps** in two occasions so far in 2020
- The bank rate reduced by **650 bps** in 2020

External sector has improved with the support of proactive policy measures...

The trade deficit has narrowed during 1H 2020, as the contraction of imports outpaced the contraction of exports, supported by import restrictions and subdued global petroleum prices



The contraction of the trade deficit during 1H 2020 was mainly due to the **decline in imports** of:

Fuel
USD 758 mn
(-37.9%)

Textiles and textile articles
USD 329 mn
(-23.6%)

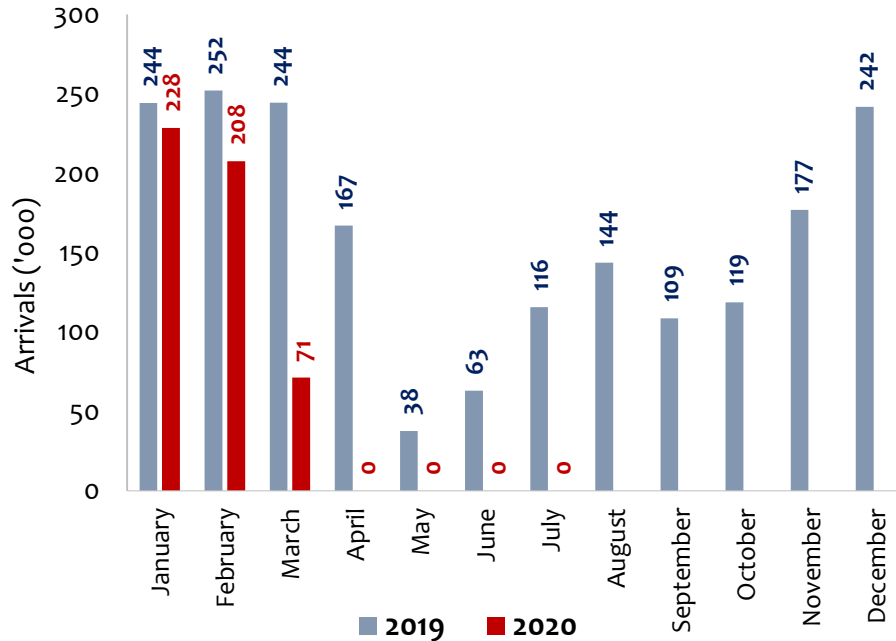
Machinery and equipment
USD 242 mn
(-19.7%)

Building Materials
USD 230 mn
(-31.7%)

Base metals
USD 106 mn
(-38.3%)

Tourism sector is the most affected sector while workers' remittances are also expected to record a decline....

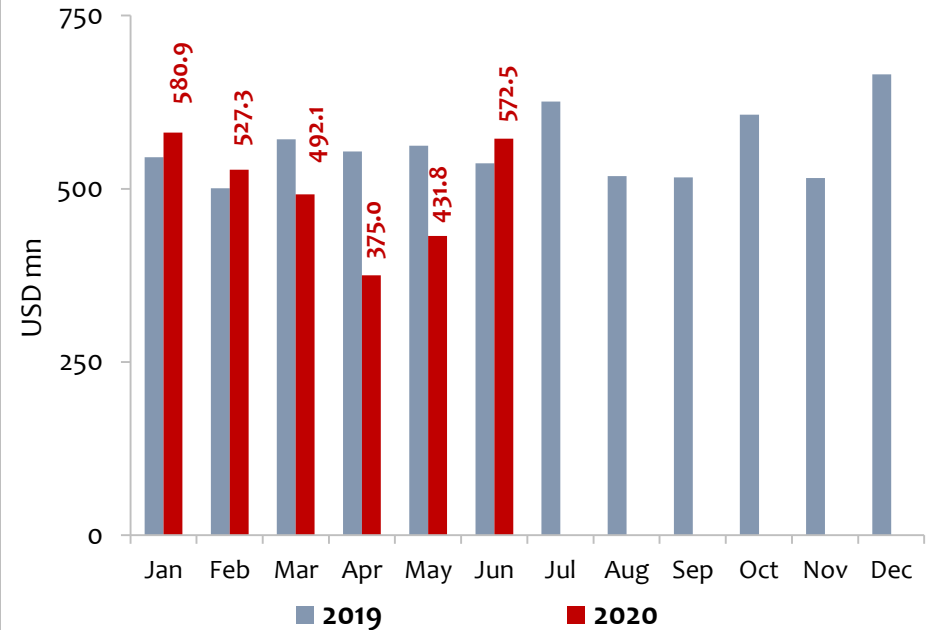
Tourist Arrivals



No tourist arrivals recorded since April 2020 due to the suspension of visa issuances

- Thus far 2020: 507,311 (-54.9%, y-o-y)
- 2019: 1,913,702.0 (-18.0%, y-o-y)

Workers' Remittances



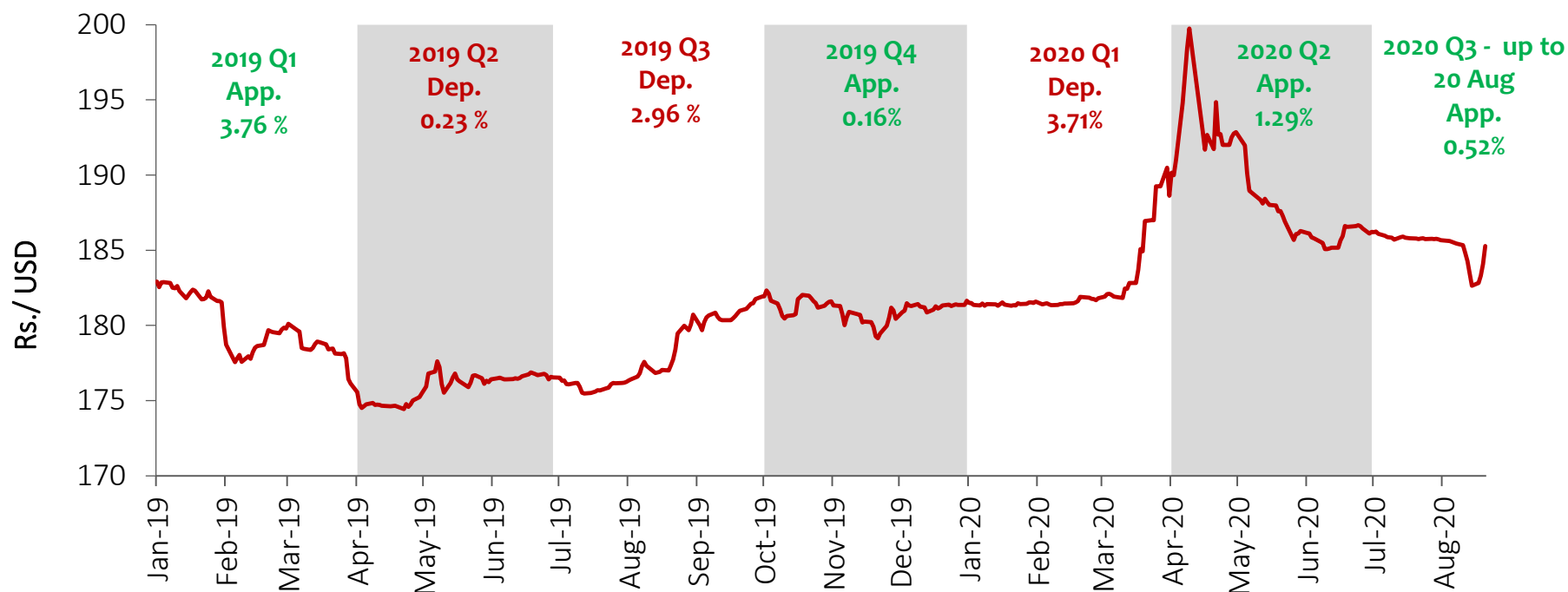
Workers' remittances increased by 6.7% (y-o-y) to USD 572.5 mn in June 2020

- Thus far 2020: USD 2,979.6 mn (-8.9%, y-o-y)
- 2019: USD 6.7 bn (-4.3%, y-o-y)

Improved trade balance and political stability appear to have helped stabilise the Sri Lankan rupee...

The Sri Lankan rupee which appreciated sharply in the immediate aftermath of the election showed some correction thereafter

Movement of Sri Lankan Rupee against USD (up to 19 Aug 2020)



Gross official reserves were estimated at USD 7.1 bn by end July 2020, providing an import cover of 4.7 months

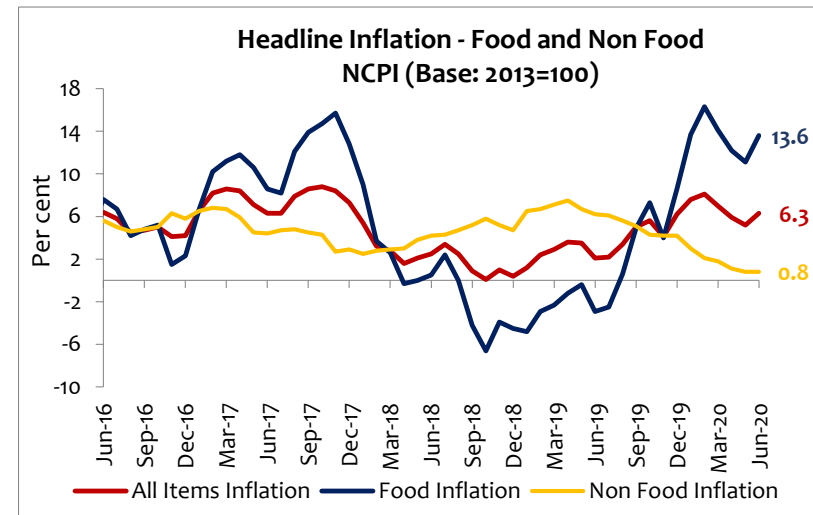
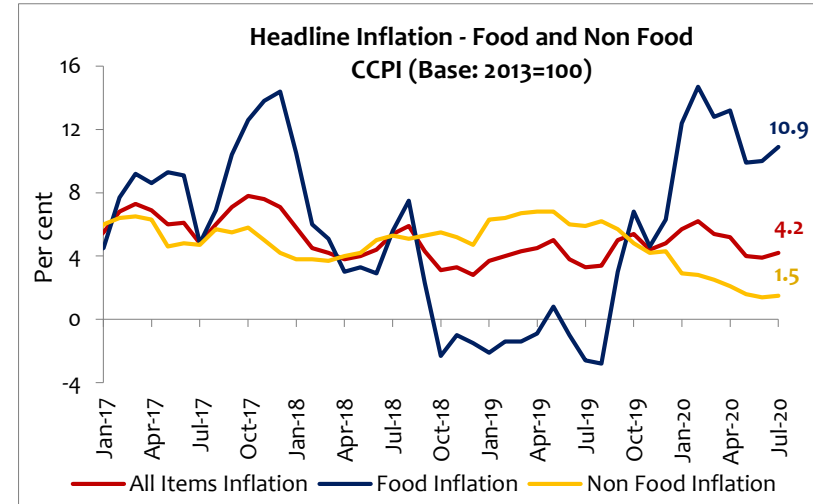
Headline and core inflation, based on CCPI accelerated marginally in July 2020, yet remaining at relatively low levels...

Headline Inflation (%)

	Dec-17	Dec-18	Nov-19	Dec-19	Jan-20	Feb 20	Mar-20	Apr-20	May-20	Jun-20	July-20
based on CCPI (2013=100)											
Y-o-Y	7.1	2.8	4.4	4.8	5.7	6.2	5.4	5.2	4.0	3.9	4.2
Annual average	6.6	4.3	4.1	4.3	4.5	4.6	4.7	4.8	4.7	4.7	4.8
based on NCPI (2013=100)											
Y-o-Y	7.3	0.4	4.1	6.2	7.6	8.1	7.0	5.9	5.2	6.3	
Annual average	7.7	2.1	3.0	3.5	4.1	4.5	4.9	5.1	5.2	5.6	

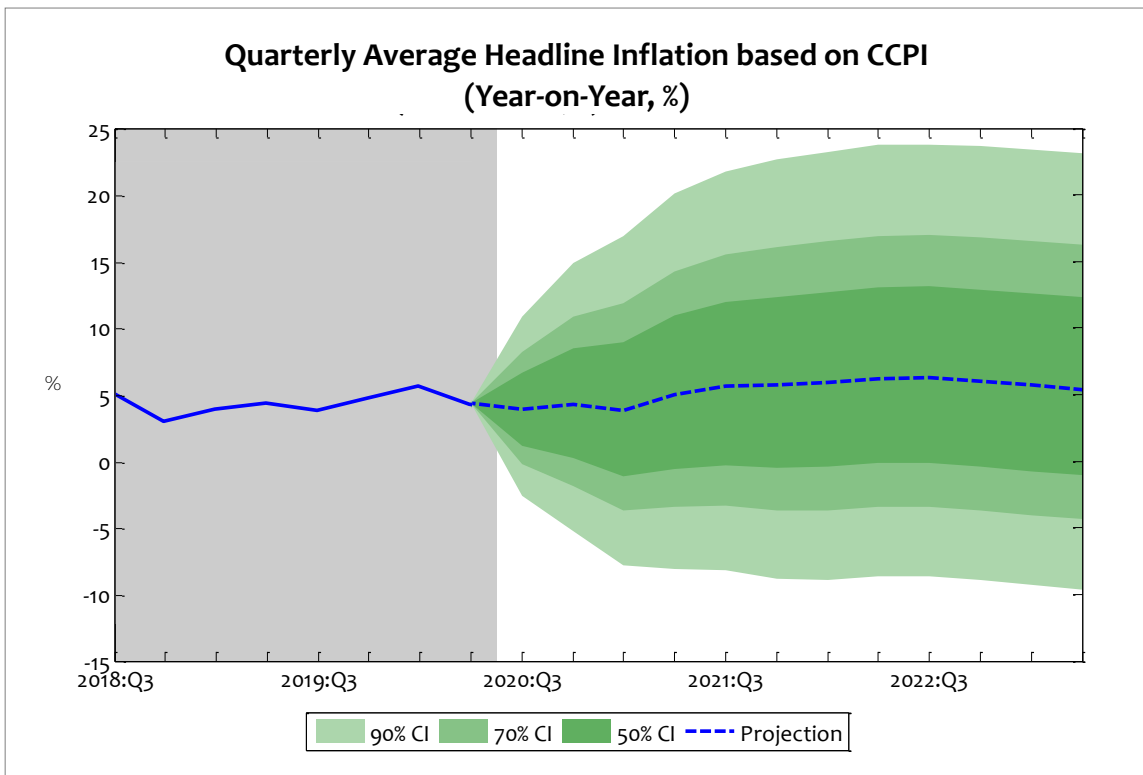
Core Inflation (%)

	Dec-17	Dec-18	Nov-19	Dec-19	Jan-20	Feb 20	Mar-20	Apr-20	May-20	Jun-20	July-20
based on CCPI (2013=100)											
Y-o-Y	4.3	3.1	5.1	4.8	3.0	3.2	2.9	3.1	2.9	3.1	3.2
Annual average	5.9	3.5	5.4	5.5	5.3	5.1	4.9	4.7	4.4	4.2	4.0
based on NCPI (2013=100)											
Y-o-Y	2.7	3.1	5.5	5.2	3.9	3.4	3.2	3.2	3.7	4.4	
Annual average	4.9	2.4	5.6	5.7	5.6	5.5	5.2	5.0	4.8	4.6	



No demand driven inflationary pressure is expected during the forecast horizon...

- Headline inflation (CCPI based) is projected to remain subdued in the near term.
- Impact of the measures to stimulate economic growth and the normalisation of global oil prices could exert upward pressures on inflation towards mid-2022.

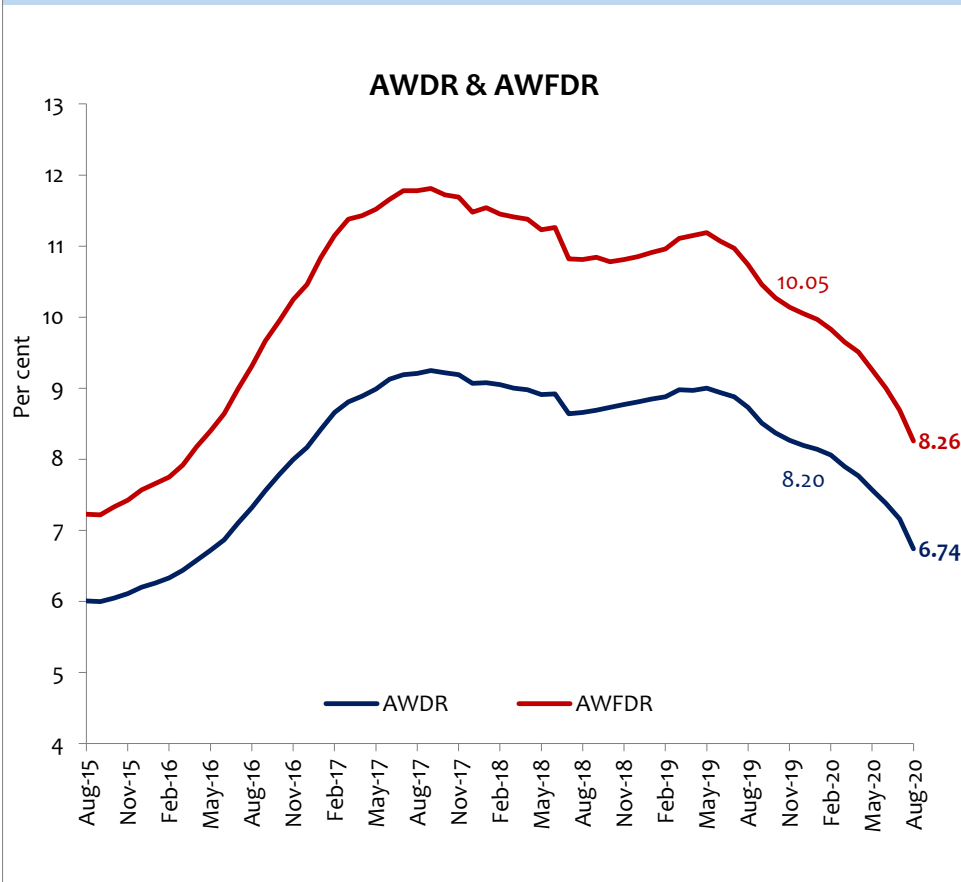


Note: A forecast is neither a promise nor a commitment.

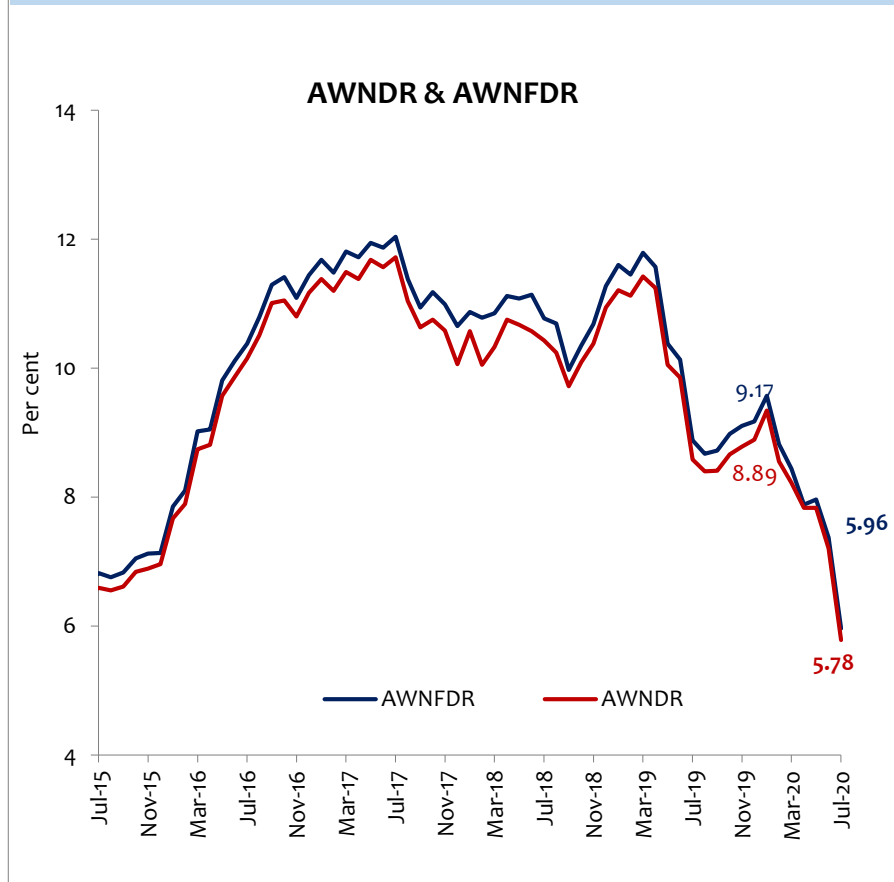
- The fan chart illustrates the uncertainty surrounding the baseline projection path using confidence bands of gradually fading colors. The projection reflects the available data and assumptions and judgments made at the August 2020 forecast round.
- The confidence intervals (CI) shown on the chart indicate the ranges of values within which inflation may fluctuate over the medium term. Specially, the thick green shaded area represents 50% confidence interval, implying there is a 50% probability that the actual inflation outcome will be within this interval. The confidence bands show the increasing uncertainty in forecasting inflation over a longer horizon.

As a result of various monetary easing measures, market interest rates are adjusting downwards...

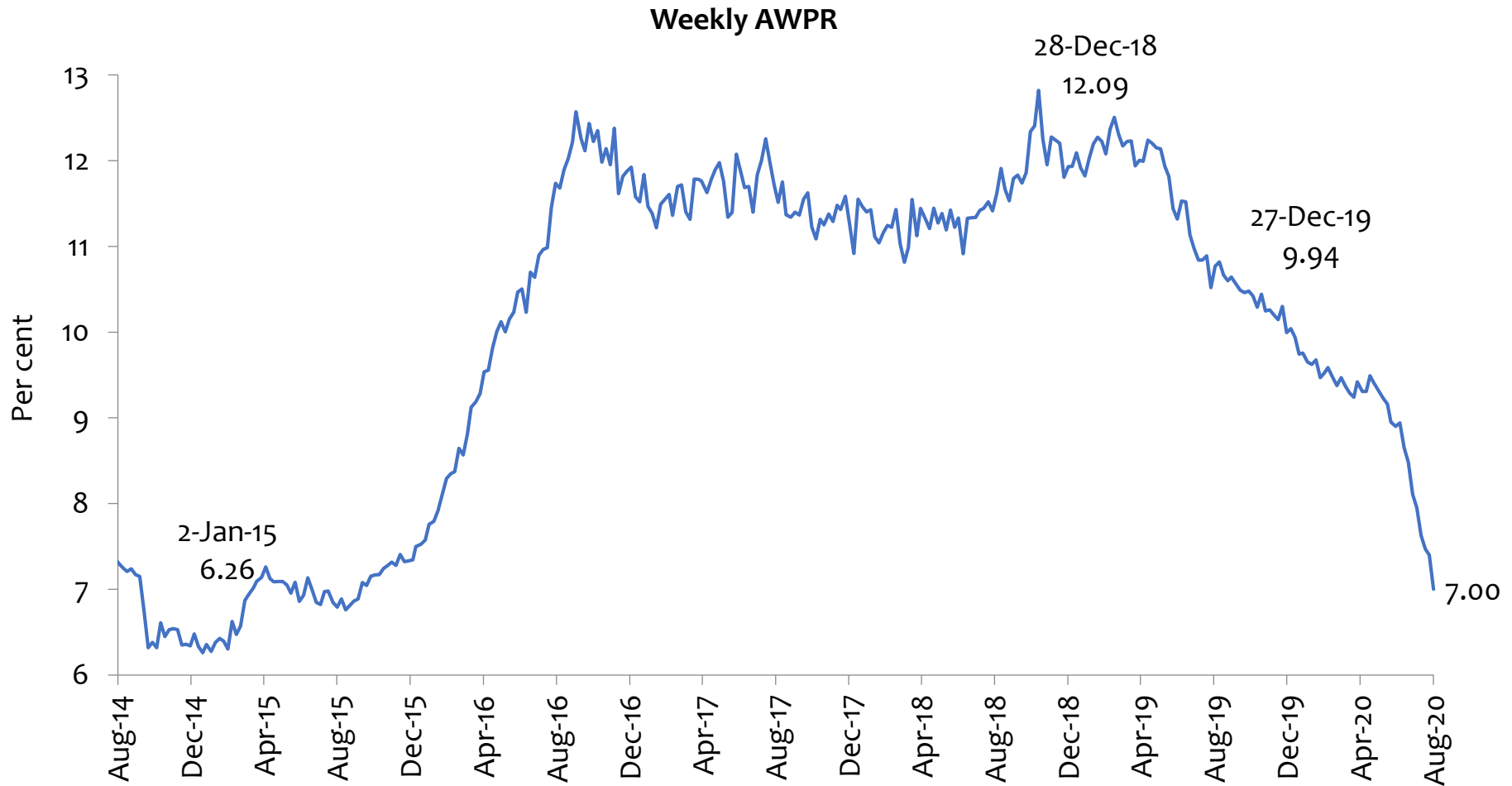
AWDR for Aug 2020 (based on Jul 2020 data) declined by 42 bps to 6.74% from the previous month [Declined by 146 bps during 2020]



AWNDR declined by 142 bps to 5.78% in July 2020 compared to the previous month [Declined by 311 bps during 2020]

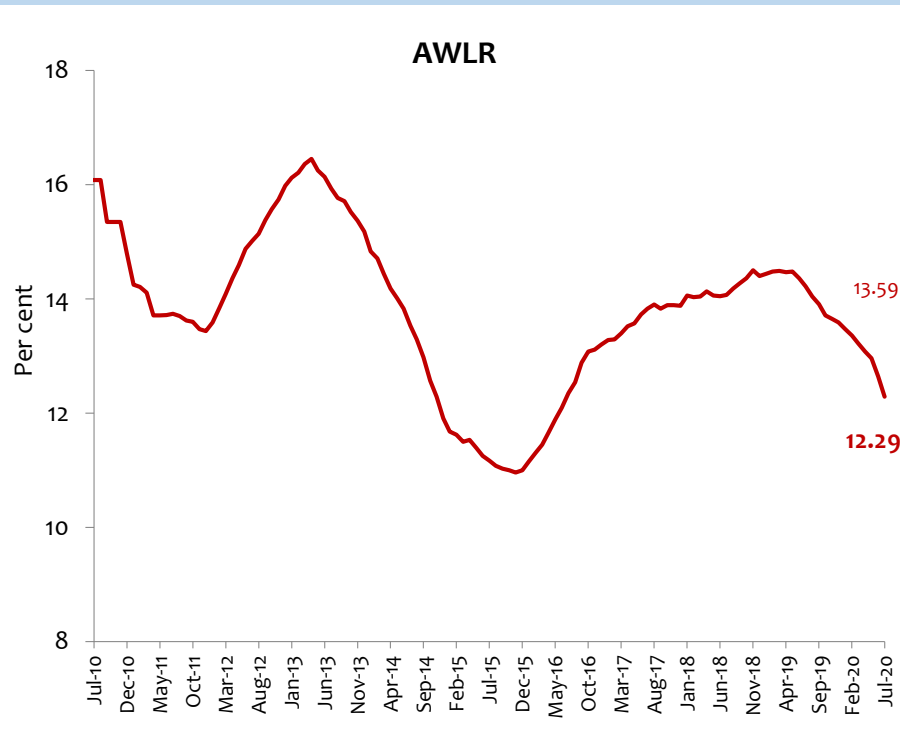


The Average Weighted Prime Lending Rate (AWPR) has also declined significantly in recent weeks...

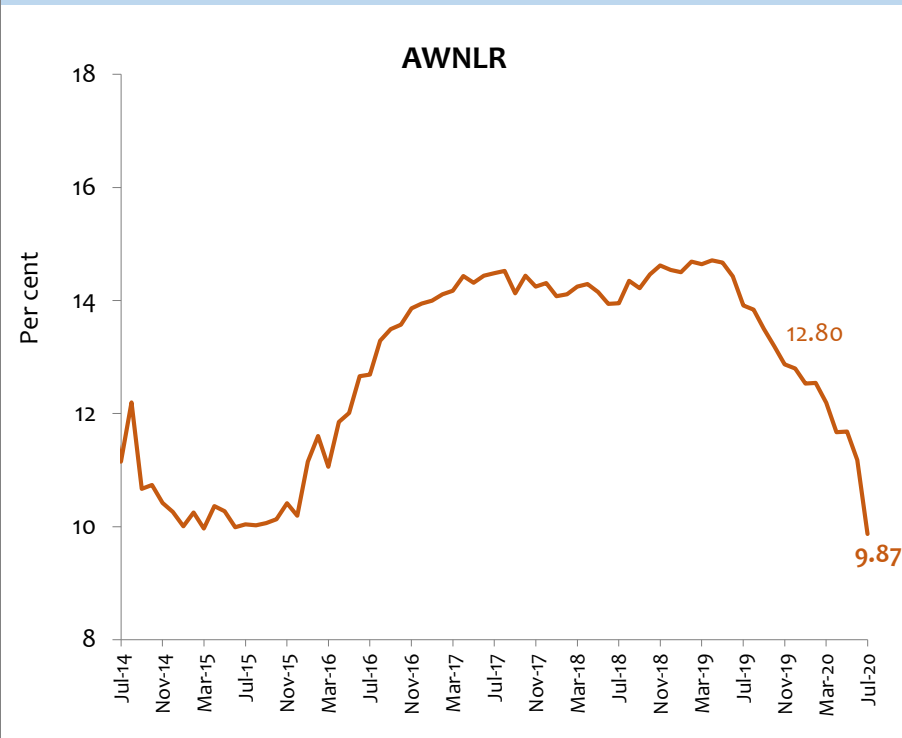


The impact of monetary easing measures is reflected in the noticeable decline in market interest rates.....

AWLR declined by 35 bps to 12.29% in July 2020 from the previous month [Declined by 130 bps during 2020]



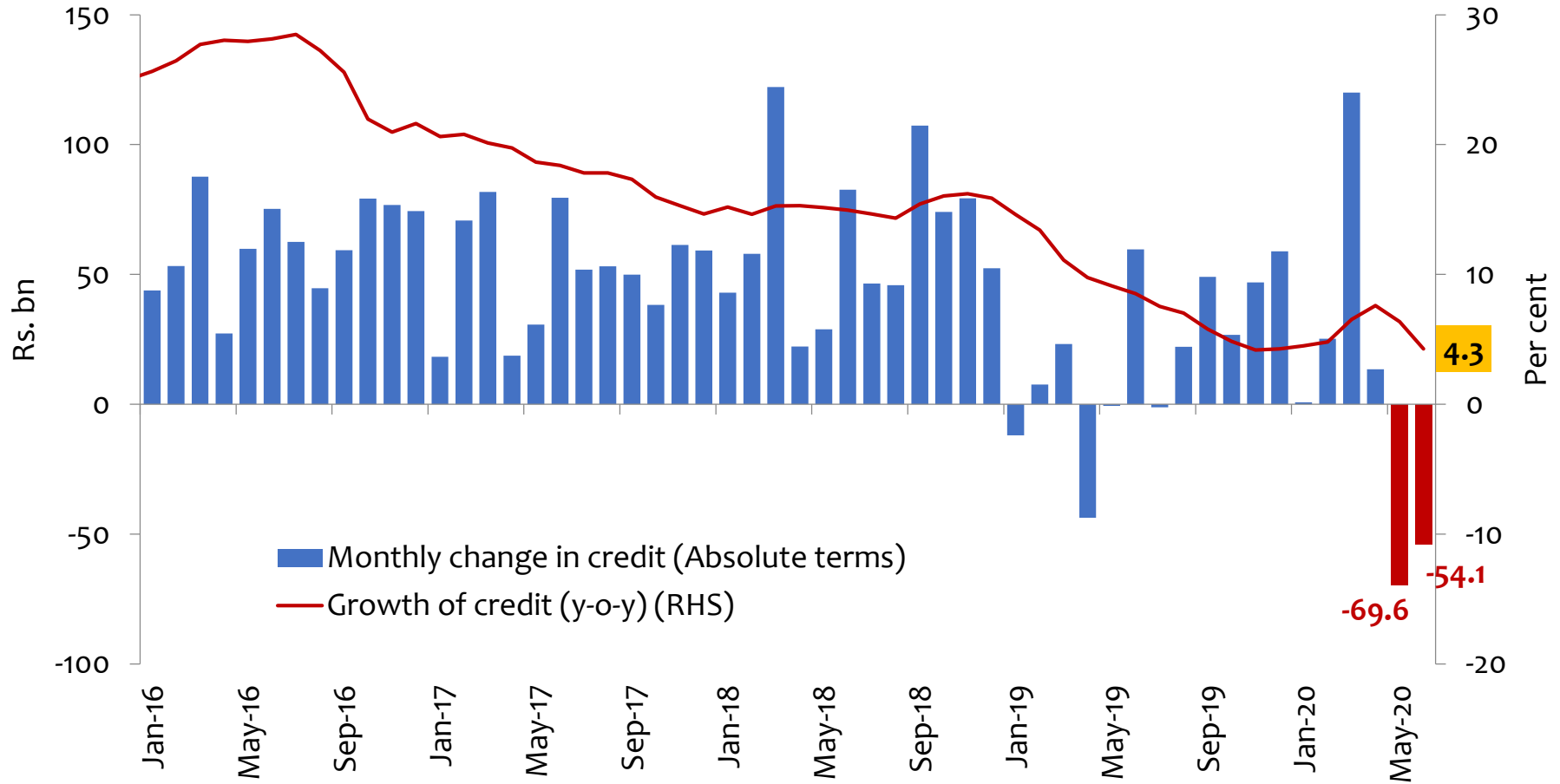
AWNLR declined by 131 bps to 9.87% in July 2020 from the previous month [Declined by 293 bps during 2020]



However, some market lending rates still remain excessive, affecting marginal borrowers in particular

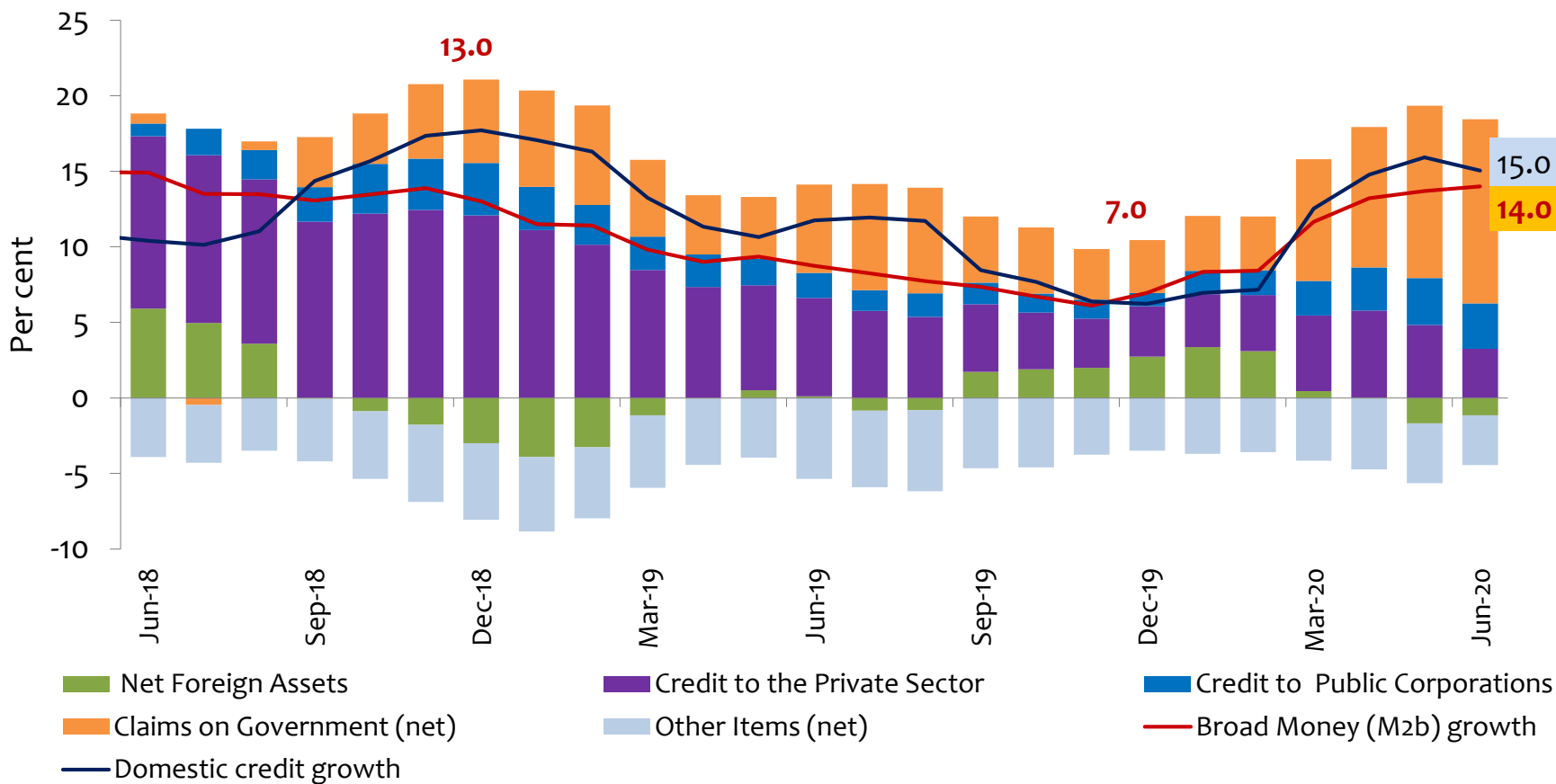
The growth of credit to the private sector is expected to recover in the period ahead...

Credit granted by Commercial Banks to the Private Sector

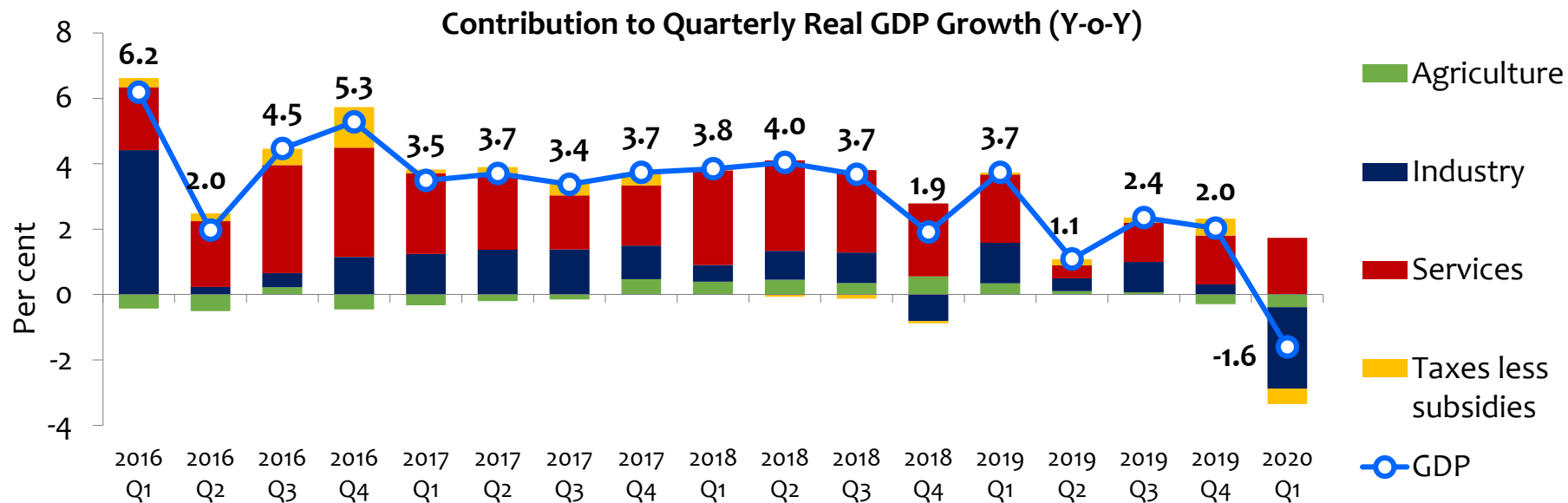


Credit to the public sector soared in recent months reflecting the government's heightened funding requirement, thereby causing a notable expansion in broad money thus far in 2020...

Contribution to Year-on-year growth of Broad Money (M2b)

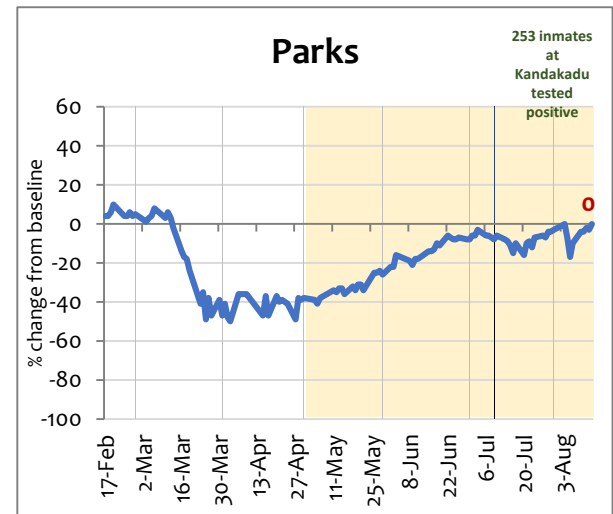
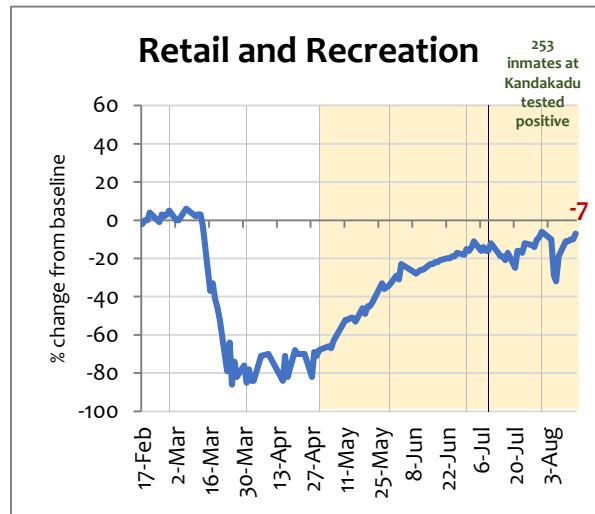
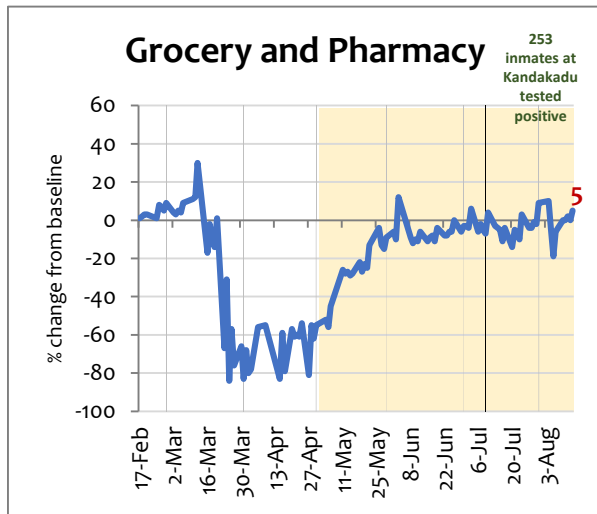
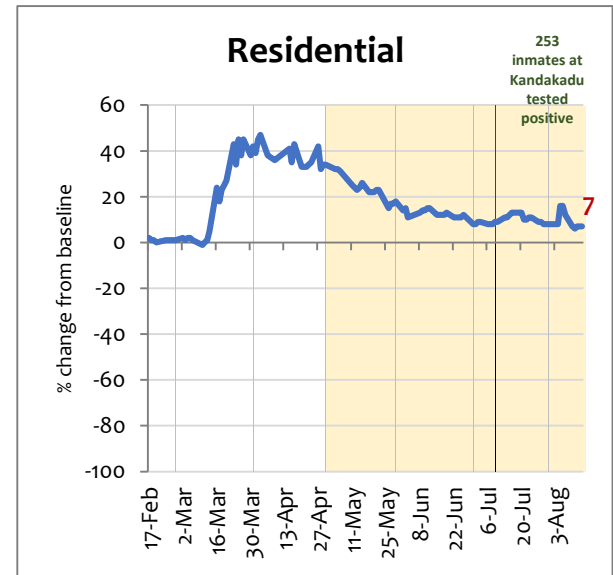
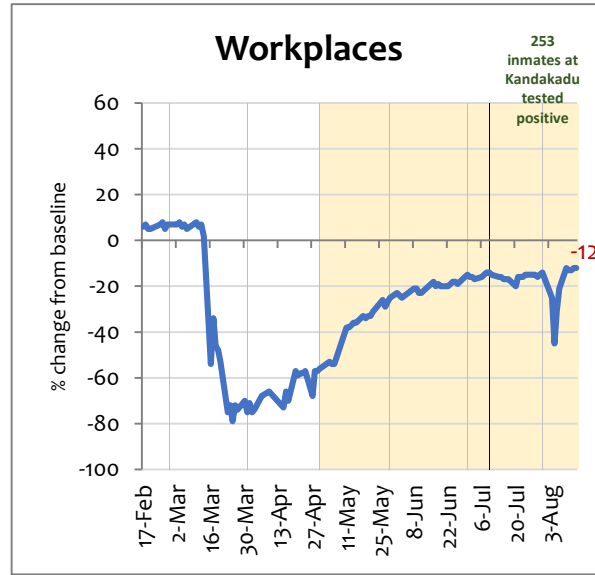
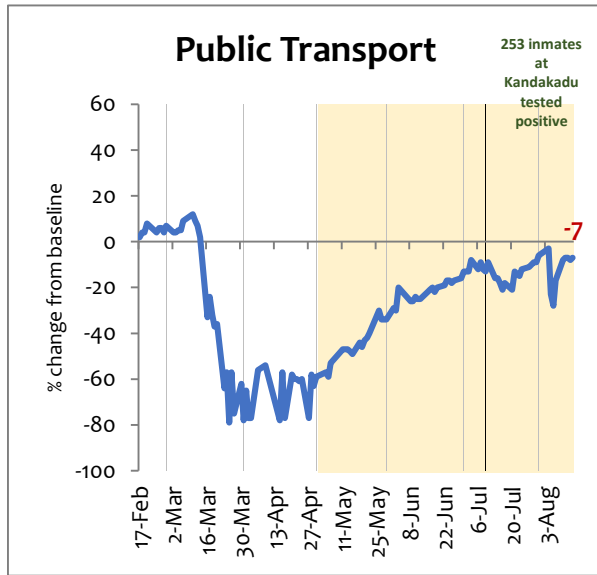


The Sri Lankan economy contracted by 1.6% in Q1 2020, contrary to the expectations of the Central Bank...



- However, a faster rebound of economic activity is expected, especially in Q4 2020, supported by improved political stability, the resultant improvement in business confidence, and the lagged impact of monetary and fiscal stimulus
- This expected rebound in Q4 2020 is essential for the country to record a positive growth rate during this year

Normalcy has returned to most economic activities...

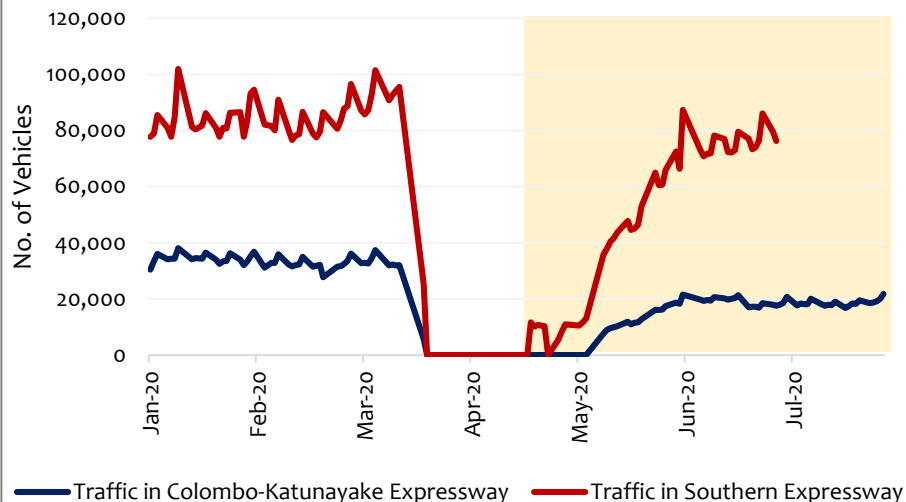


Excludes weekends and holidays

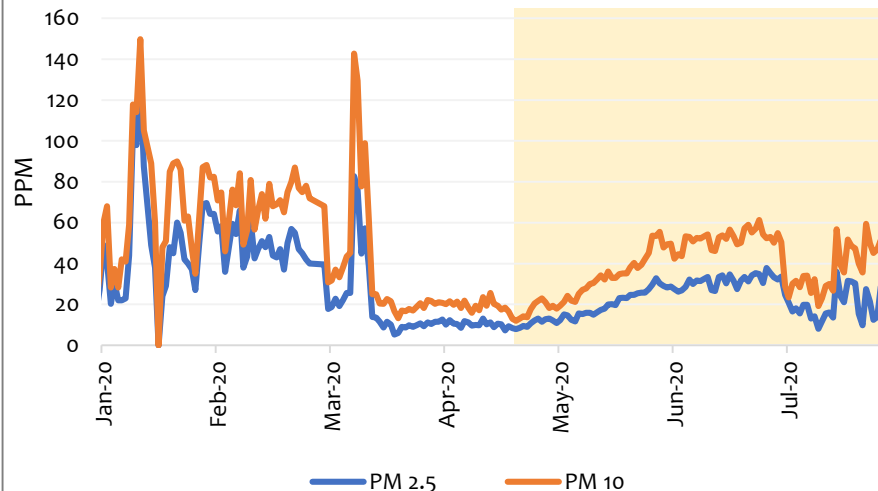
Source: Google Mobility Report as at 14 Aug 2020

Normalcy has returned to most economic activities... (contd.)

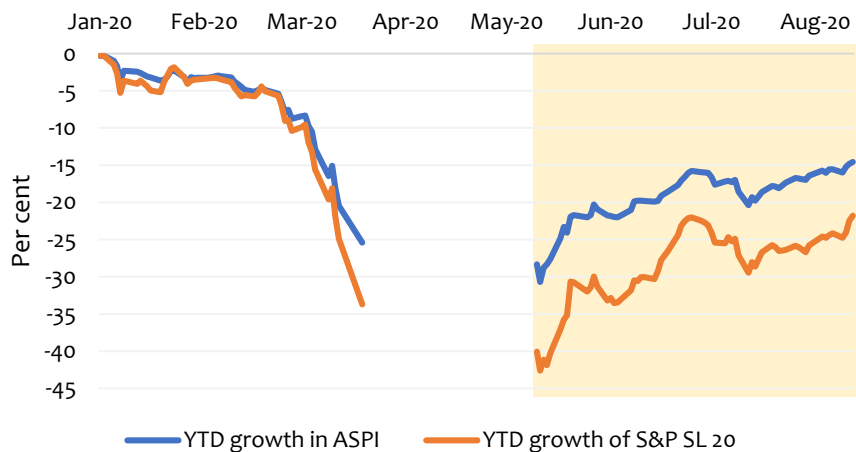
Expressway Traffic



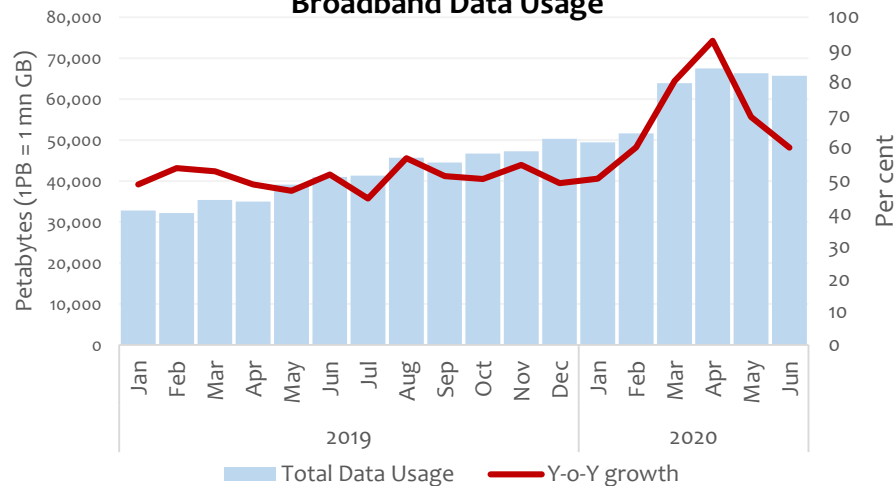
Air Pollution in the Colombo District



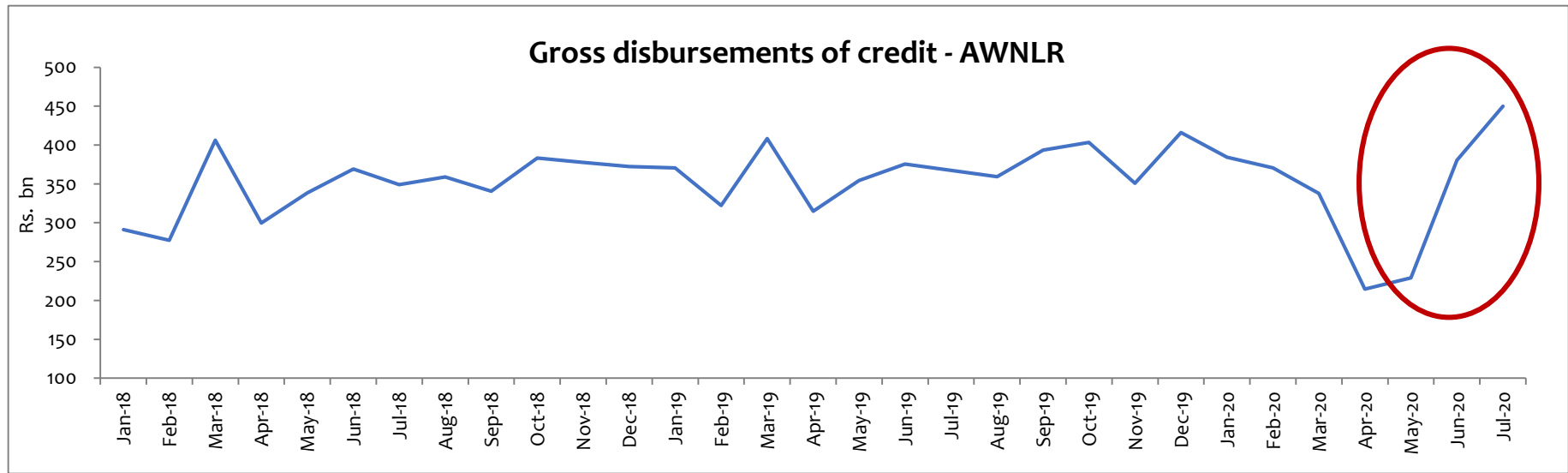
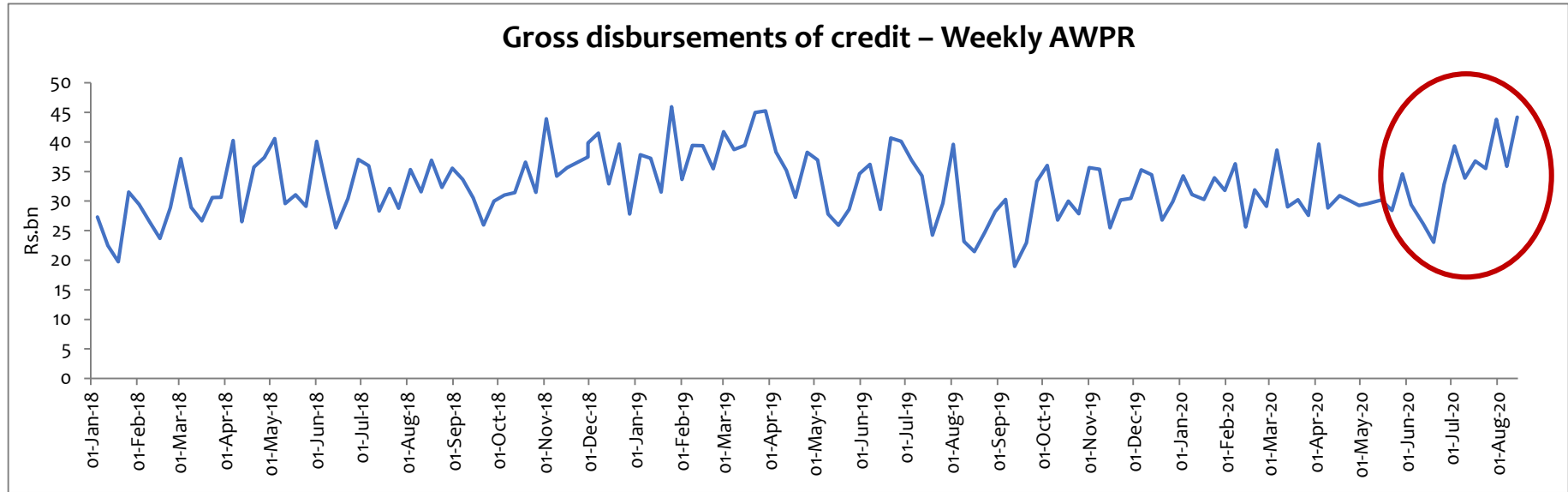
Stock Market Developments



Broadband Data Usage



Normalcy has returned to most economic activities... (contd.)



Decision

- The Monetary Board was of the view that the **current accommodative monetary policy stance is appropriate**
- Considering bank lending rates of certain financial products which continue to remain high, the Board decided to **revise downward the caps on interest rates on credit cards, pre-arranged temporary overdrafts and pawning facilities**
- **Penal interest rates are capped at 2 percentage points over the regular interest rates** charged on the relevant credit facility.
- Directions to effect these regulated interest rates will be issued shortly

Thank You