



Review of the Monetary Policy Stance

July 2021

Economic Research Department
Central Bank of Sri Lanka

Monetary Policy Decision

THE CENTRAL BANK OF SRI LANKA MAINTAINS POLICY INTEREST RATES AT THEIR CURRENT LEVELS

The Central Bank will continue to monitor domestic and global macroeconomic and financial market developments and stand ready to take appropriate measures, as and when necessary, with the aim of maintaining inflation in the targeted 4-6% range under the flexible inflation targeting framework in the medium term, while supporting sustained economic recovery...

Policy interest rates remain unchanged

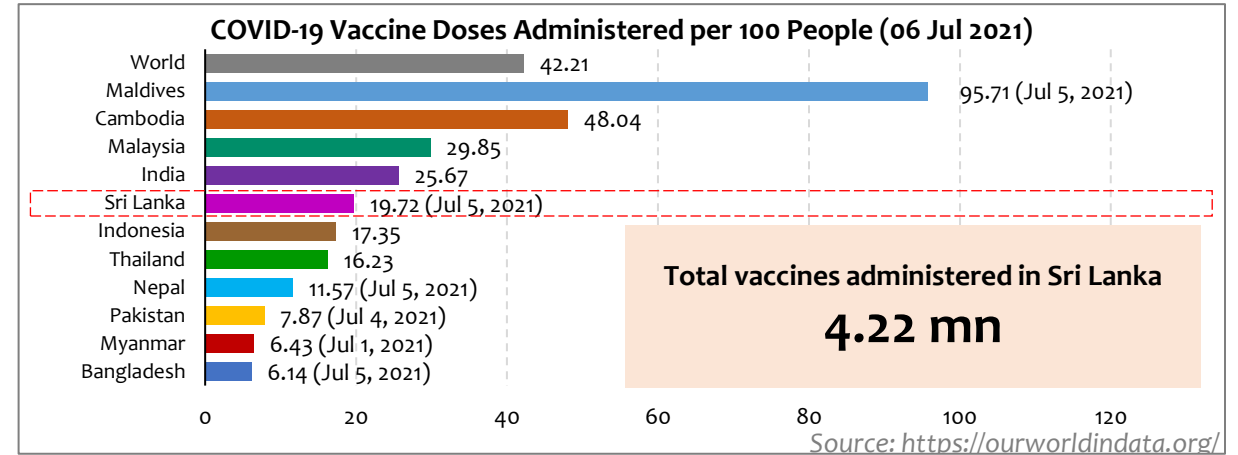
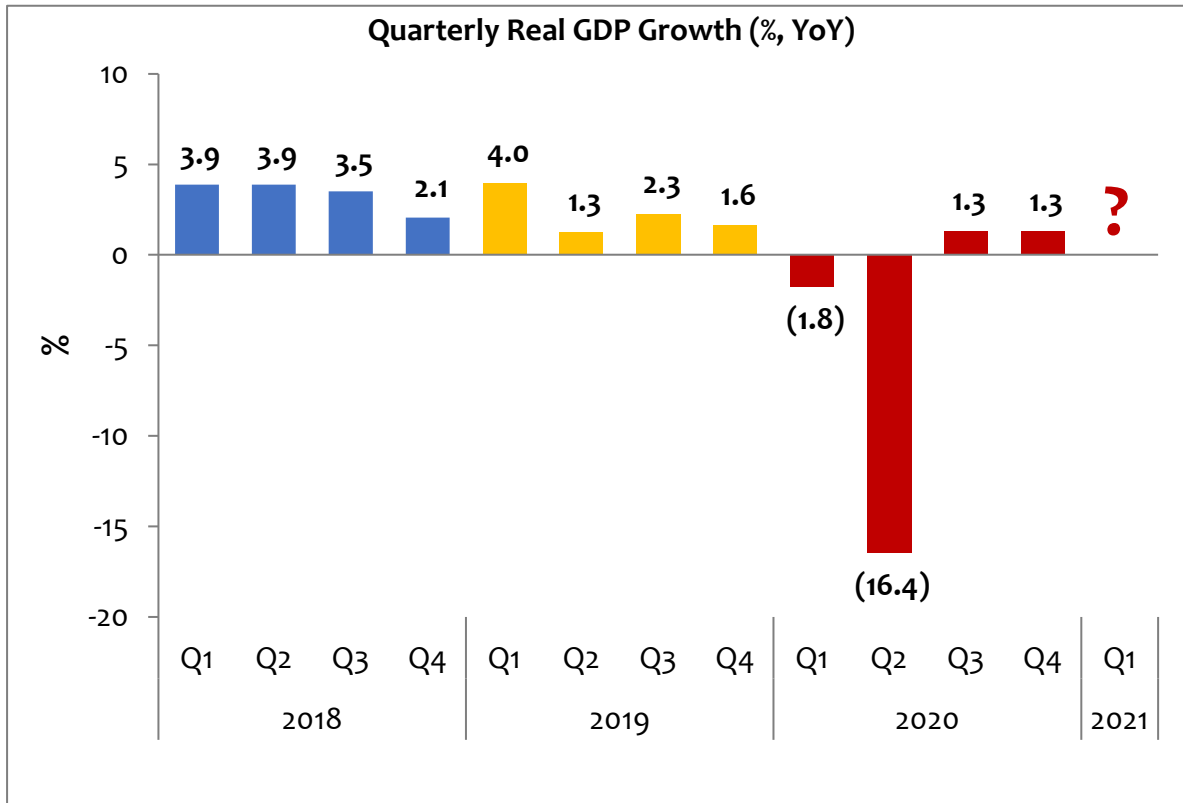
Standing Deposit Facility Rate (SDFR)	4.50%
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Standing Lending Facility Rate (SLFR)	5.50%
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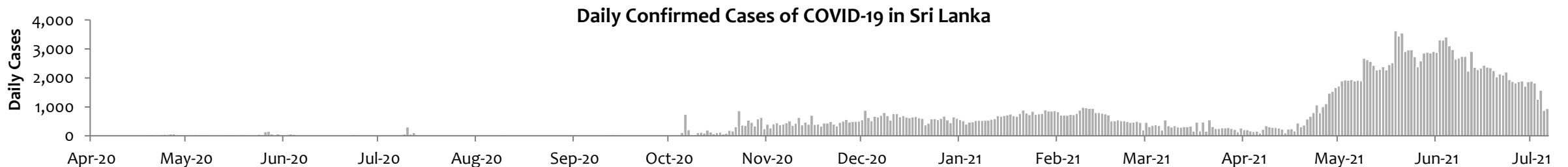
Bank Rate	8.50%
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Statutory Reserve Ratio (SRR)	2.00%
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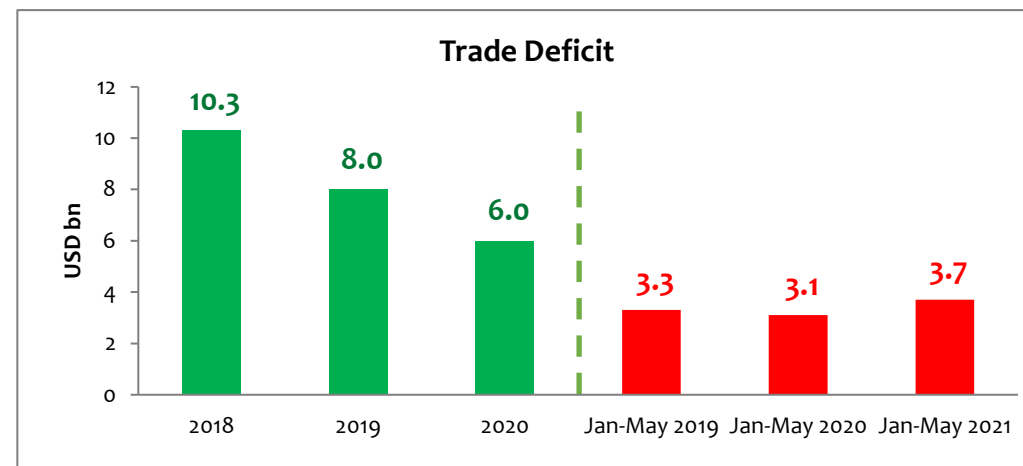
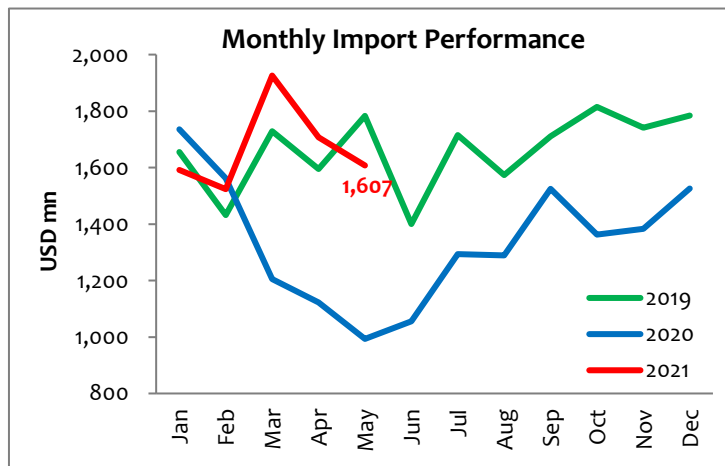
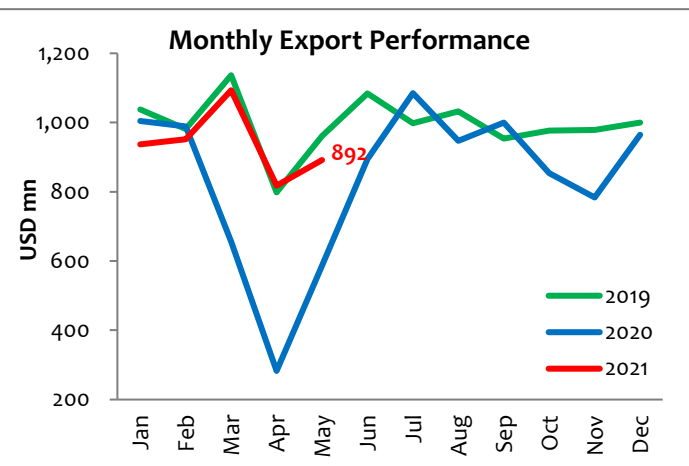
The Sri Lankan economy is likely to have recorded a higher growth than expected in the first quarter of 2021...



The ongoing vaccination drive throughout the country and the likely removal of mobility restrictions are expected to ease the impact of the current wave of COVID-19 on overall economic activity, thereby facilitating a sustained economic recovery towards achieving a GDP growth rate of around 5% in 2021...



In spite of the resilience shown by merchandise exports, the trade deficit widened during the period from January to May 2021, over the same period last year...



Export Sectors recorded increases during Jan-May 2021 were:

Textiles & Garments by USD 532 mn 34.5% (y-o-y)	Rubber Products by USD 137 mn 50.8% (y-o-y)	Machinery & Mechanical App. by USD 81 mn 69.4% (y-o-y)
Spices by USD 79 mn 95.9% (y-o-y)	Tea by USD 70 mn 15.3% (y-o-y)	Food, Beverages & Tobacco by USD 50 mn 32.1% (y-o-y)

Import Sectors recorded increases during Jan-May 2021 were:

Fuel by USD 588 mn 51.9% (y-o-y)	Textiles & Textile Articles by USD 284 mn 32.0% (y-o-y)	Machinery & Equipment by USD 253 mn 30.0% (y-o-y)
Chemical Products by USD 150 mn 47.3% (y-o-y)	Base Metals by USD 139 mn 88.4% (y-o-y)	Plastic & Articles by USD 123 mn 61.8% (y-o-y)

Category	Jan-May (USD mn)		
	2019	2020	2021
Exports Earnings	4,915	3,519	4,692
Expenditure on Imports	8,196	6,619	8,356
Trade Balance	-3,281	-3,101	-3,663

Challenges emanating from multiple waves of COVID-19 globally and domestically continued to stifle the recovery of the tourism industry...

Tourist Arrivals (Jan-Jun)

2019 - 1,008,449
 2020 - 507,311
 2021 - 16,908

Earnings from Tourism (Jan-Jun)

2019 - USD 1,900.7 mn
 2020 - USD 681.9 mn
 2021 - USD 22.7 mn

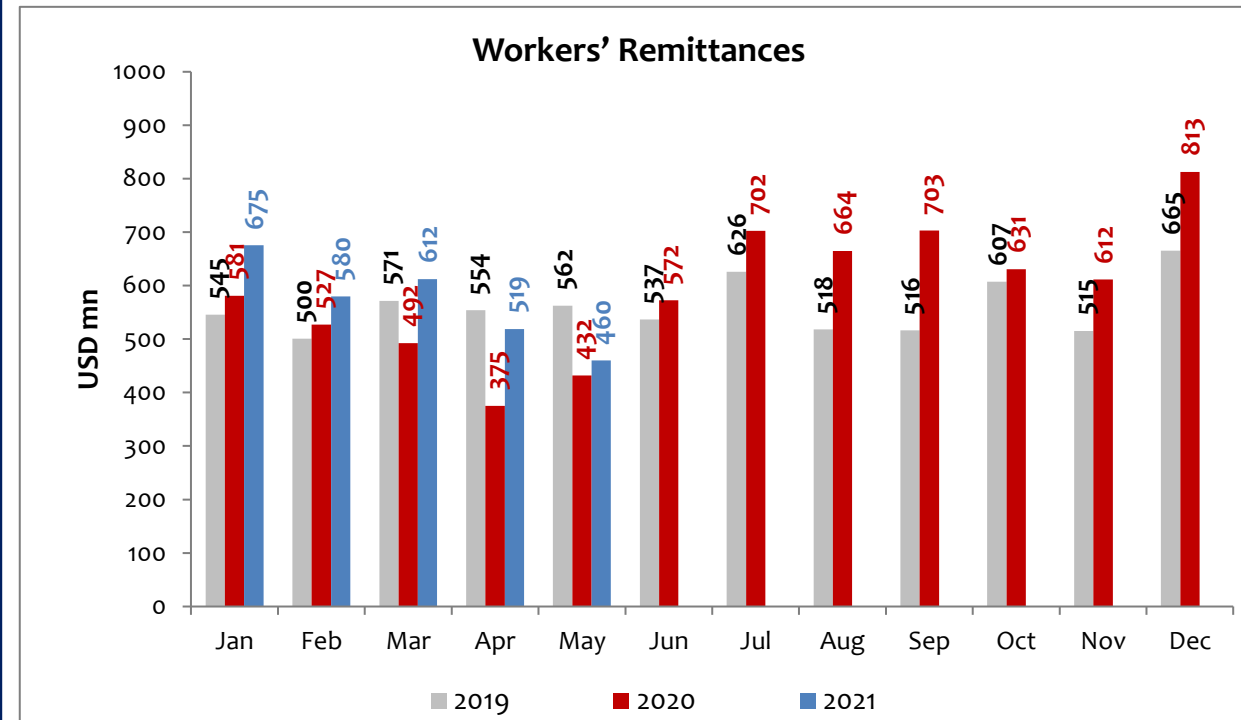
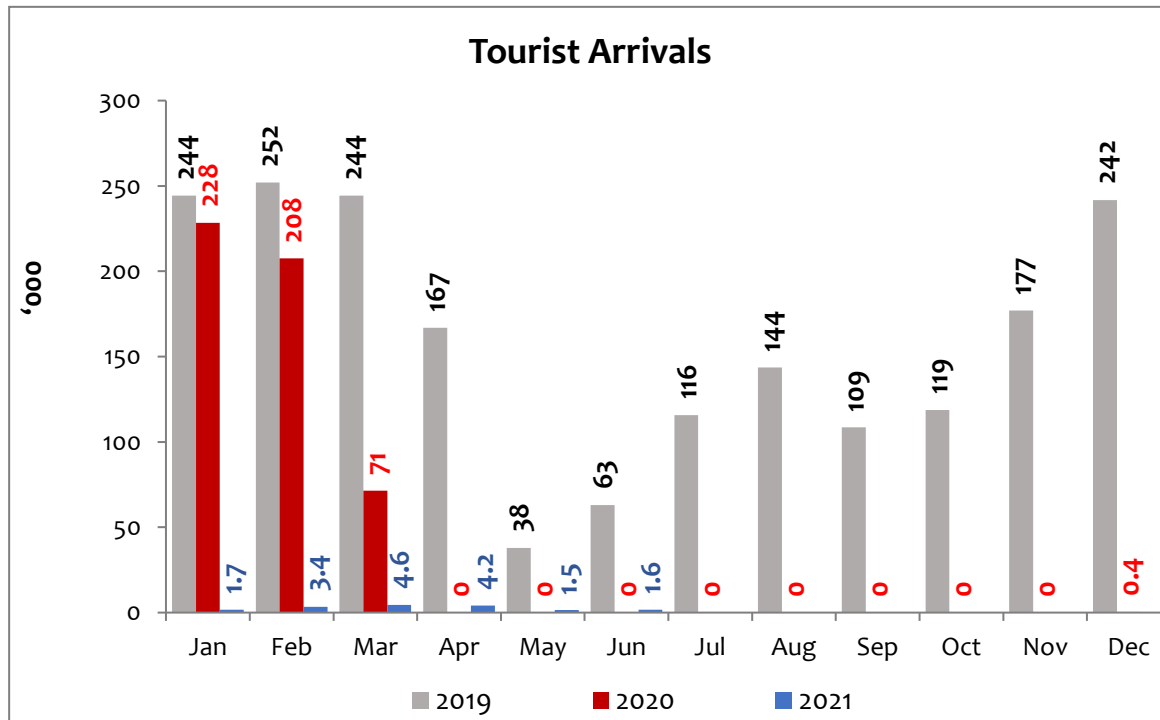
The notable improvement in workers' remittances continued to provide support for the external current account...

Workers' Remittances

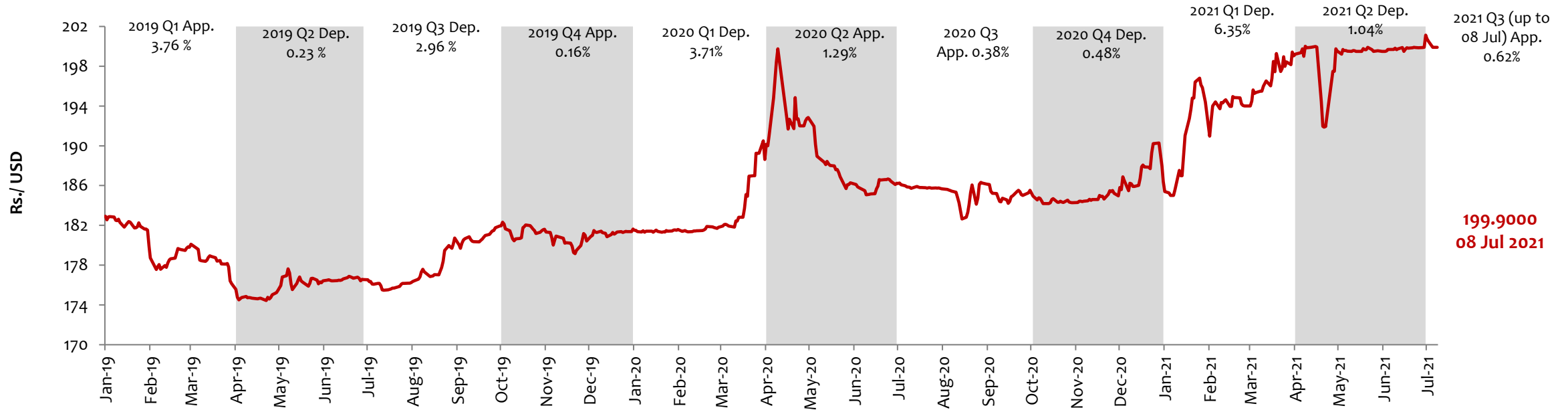
2021 May USD 460 mn
 (6.6% y-o-y)

2019 (Jan-May) : USD 2,733 mn
 2020 (Jan-May) : USD 2,407 mn
 2021 (Jan-May) : USD 2,846 mn
 (18.2% y-o-y)

Workers' remittances increased by 5.8% (y-o-y) in 2020
 4.3% (y-o-y) in 2019

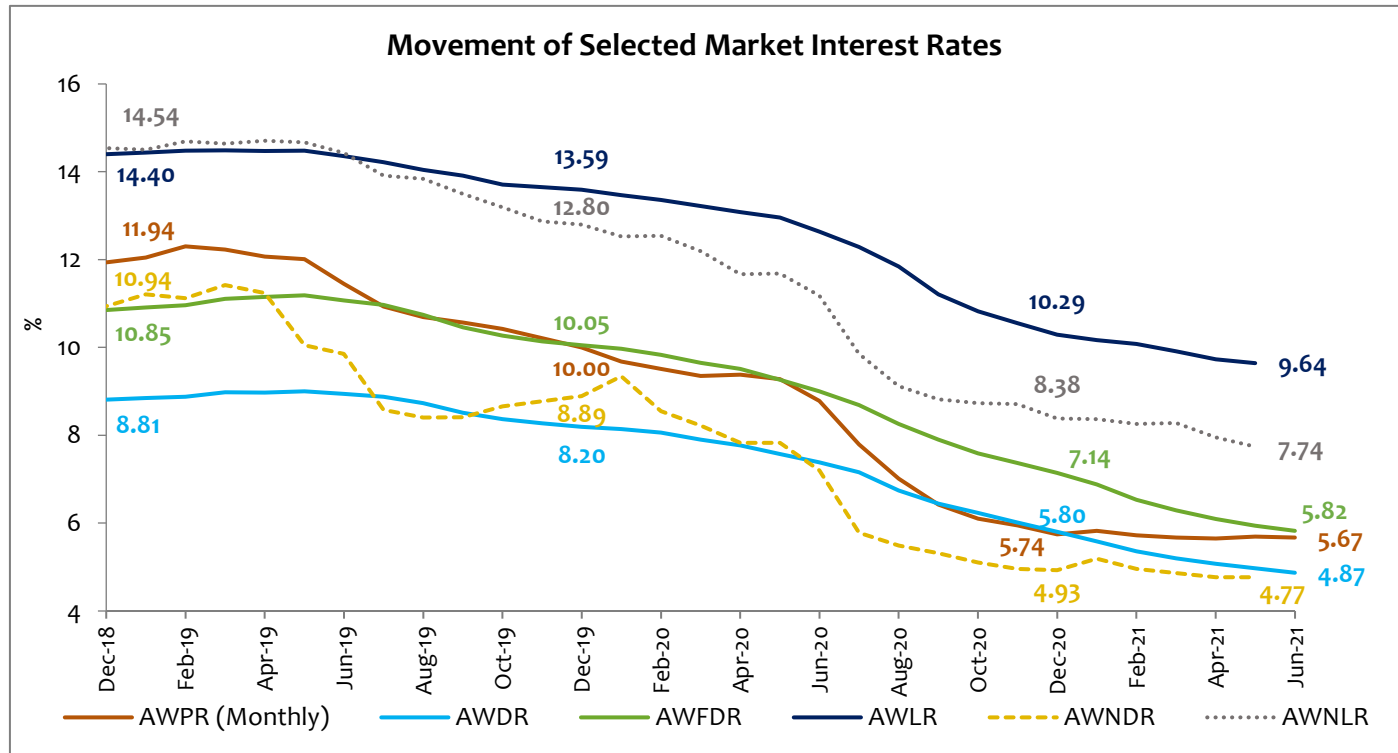


The exchange rate has recorded a depreciation of 6.7% thus far during the year...



- Speculative behaviour and frontloading of imports have caused undue pressures in the domestic foreign exchange market
- As of end June 2021, the gross official reserves were estimated at USD 4.0 bn, similar to the levels observed at end May 2021 (*this does not include the bilateral currency swap facility amounting to CNY 10 bn (equivalent to approximately USD 1.5 bn) between PBoC and the Central Bank*)
- Although the level of foreign reserves could experience some variations in the period ahead, such developments are expected to be temporary, with the adequate financing strategies lined up to maintain reserves at sufficient levels and to meet all maturing debt servicing obligations of the Government on time

Market interest rates remain low, facilitating increased credit flows to the private sector...

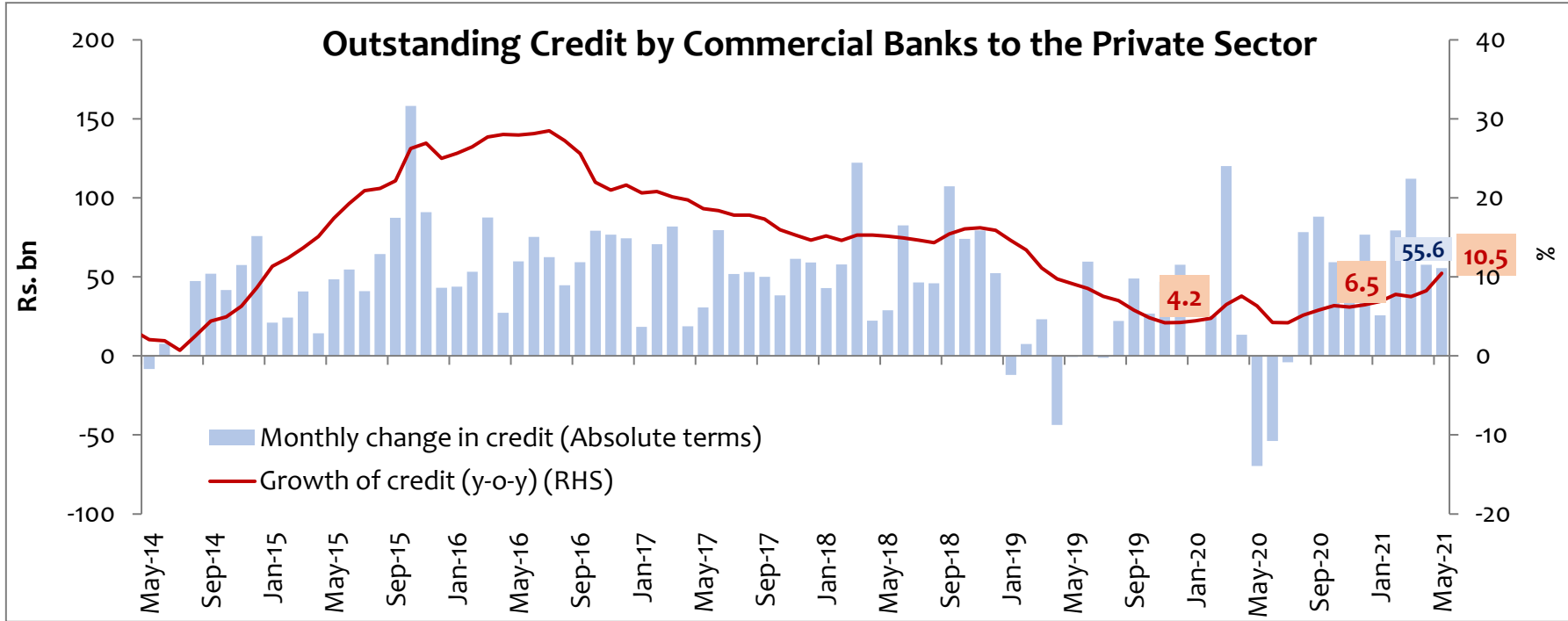


Prevailing low interest rates and the surplus rupee liquidity in the domestic money market enabled the flow of low cost credit to the economy, thus supporting the revival of economic activity

Adjustments in Interest Rates

Interest Rate	End 2020	As at 07 July 2021	From end 2019 to end 2020	From end 2020 to so far in 2021
	%	%	bps Change	bps Change
AWCMR	4.55	4.93	-290	38
91-day T-bill	4.69	5.19	-282	50
182-day T-bill	4.80	5.19	-322	39
364-day T-bill	5.05	5.23	-340	18
Weekly AWPR	5.81	5.51	-393	-30
Monthly AWPR	5.74	5.67	-426	-7
AWLR	10.29	9.64	-330	-65
AWNLR	8.38	7.74	-442	-64
AWDR	5.80	4.87	-240	-93
AWFDR	7.14	5.82	-291	-132
AWNDR	4.93	4.77	-396	-16
AWNFDR	5.08	4.90	-409	-18

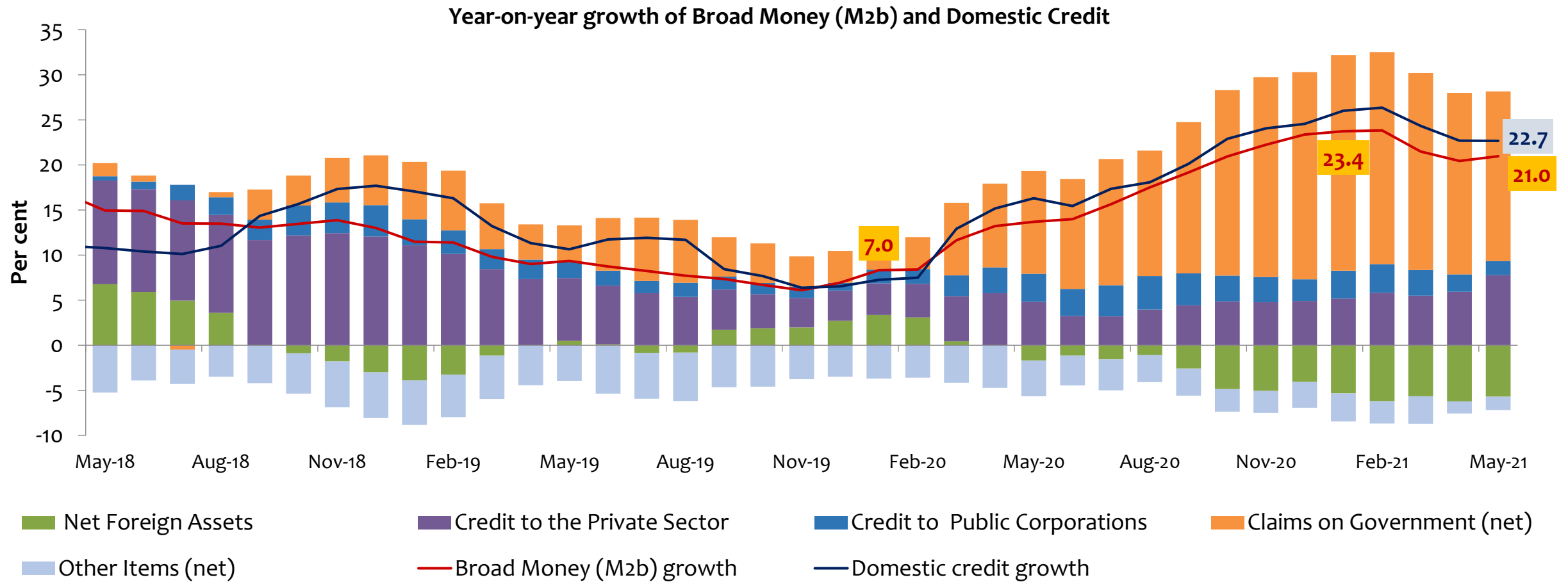
Credit extended to the private sector expanded notably during the period from January to May 2021, and this momentum is expected to sustain through 2021...



	Absolute change (Rs. bn)	Y-o-Y Growth (%)
2019	235.5	4.2
2020	374.1	6.5
Jan-21	25.7	6.9
Feb-21	79.4	7.8
Mar-21	112.2	7.5
Apr-21	57.7	8.2
May-21	55.6	10.5
Jan/May 21	330.6	

The Central Bank expects domestic investors to make use of the low interest rate environment to expand their productive economic activities and explore new opportunities that are being created in the economy aimed at local and international markets

The growth of broad money (M_{2b}) remained elevated...



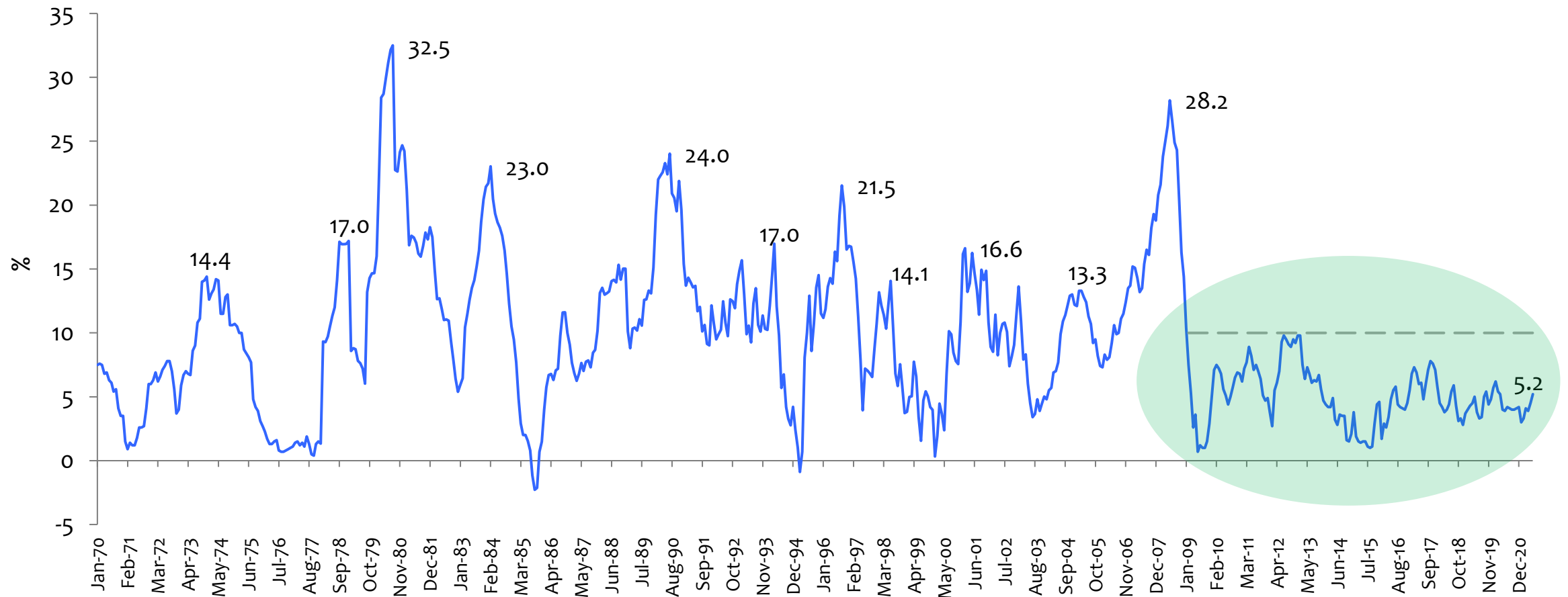
Credit obtained by the public sector from the banking system, particularly the Government, also increased notably, amidst the impact of the pandemic on government revenue and recurrent expenditure

Multiple Indicators of Monetary Easing...

		End 2018	End 2019	End 2020	7 Jul 2021*	Δ 2018/19	Δ 2019/20	Δ 2020/21	*Last data point
Currency in Circulation	Rs. bn	640.9	678.0	834.8	939.3	37.0	156.8	104.5	7-Jul-21
Reserve Money (M ₀)	Rs. bn	961.1	932.6	964.4	1,058.9	(28.5)	31.8	94.4	7-Jul-21
Claims on Government	Rs. bn	473.1	363.5	870.3	1,055.5	(109.6)	506.8	185.1	May-21
Provisional Advances	Rs. bn	198.6	236.6	153.1	198.2	38.0	(83.5)	45.1	May-21
Gross CBSL Holdings of Govt. Sec. (Face value)	Rs. bn	45.8	74.7	725.2	921.9	28.9	650.5	196.7	7-Jul-21
<i>T bills</i>	Rs. bn	44.2	25.9	654.9	864.1	(18.3)	629.0	209.2	7-Jul-21
<i>T bonds</i>	Rs. bn	1.6	48.8	70.6	57.8	47.2	21.8	(12.8)	7-Jul-21
CBSL Holdings of Govt. Sec. (Net of repo)	Rs. bn	274.5	126.9	717.3	857.3	(147.6)	590.4	140.0	May-21
Overnight Liquidity	Rs. bn	(148.4)	37.9	206.8	91.5	186.3	168.9	(115.3)	7-Jul-21
Broad Money (M _{2b})	Rs. bn	7,128.3	7,624.1	9,405.7	10,033.0	495.8	1,781.6	627.2	May-21
	% YoY	13.0	7.0	23.4	21.0				May-21

Inflation remains moderate, given the subdued aggregate demand conditions, although food inflation has accelerated due to supply-side disruptions...

CCPI Based Y-o-Y Headline Inflation

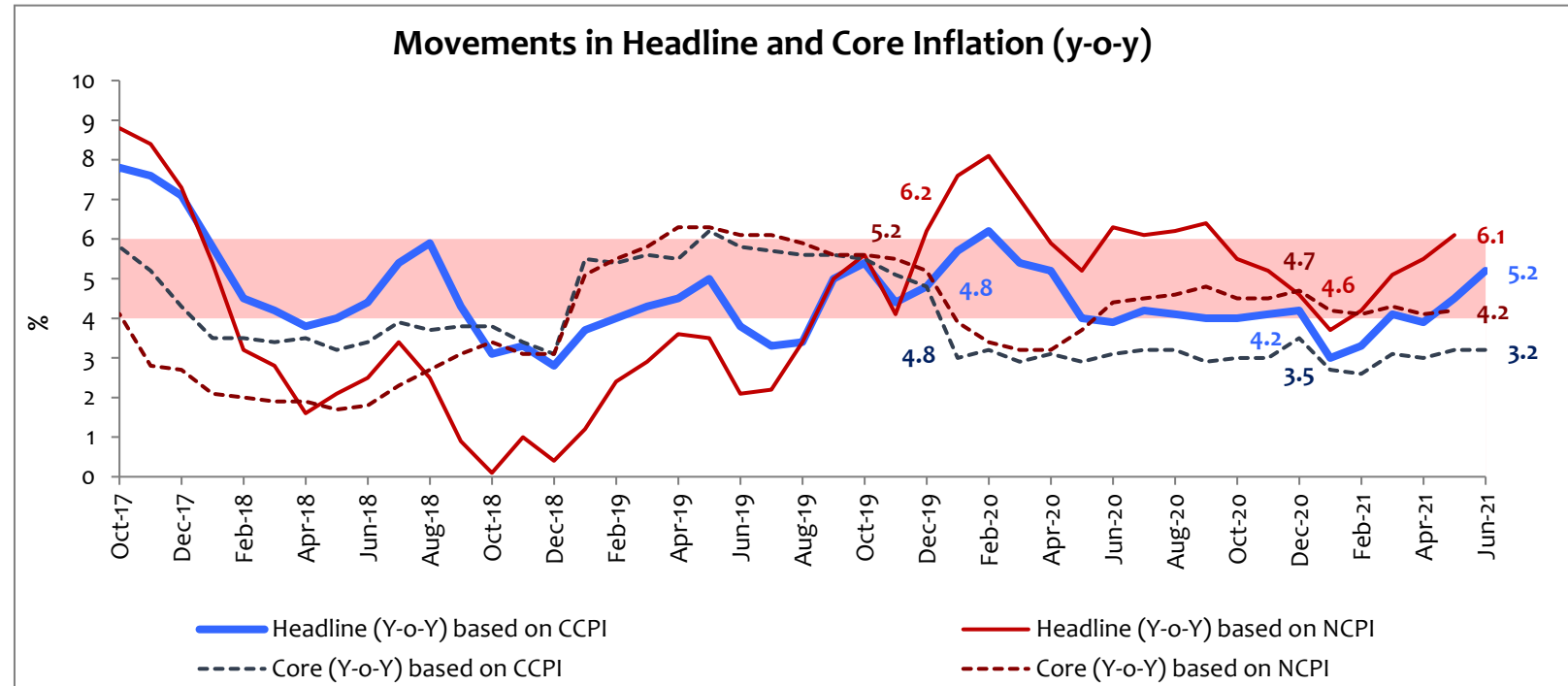


Inflation remains moderate, given the subdued aggregate demand conditions, although food inflation has accelerated due to supply-side disruptions...

- Any buildup of sustained inflationary pressures will be addressed through appropriate measures over the medium term

Headline Inflation (%)					
	Dec-19	Dec-20	Apr-21	May-21	Jun-21
based on CCPI (2013=100)					
Y-o-Y	4.8	4.2	3.9	4.5	5.2
Annual average	4.3	4.6	3.9	3.9	4.1
based on NCPI (2013=100)					
Y-o-Y	6.2	4.6	5.5	6.1	-
Annual average	3.5	6.2	5.3	5.4	-

Core Inflation (%)					
	Dec-19	Dec-20	Apr-21	May-21	Jun-21
based on CCPI (2013=100)					
Y-o-Y	4.8	3.5	3.0	3.2	3.2
Annual average	5.5	3.1	3.0	3.0	3.0
based on NCPI (2013=100)					
Y-o-Y	5.2	4.7	4.1	4.2	-
Annual average	5.7	4.1	4.4	4.4	-



Inflation is expected to remain broadly within the desired 4-6% range during the remainder of 2021, and continue be maintained in this range thereafter with appropriate policy measures as and when required

Thank You