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இலங்கை மத்திய வங்கி
CENTRAL BANK OF SRI LANKA

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Press Release

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Monetary Policy Review – May 2014

Since December 2012, the Central Bank has eased monetary policy with its key policy interest rates, the Standing Deposit Facility Rate (SDFR) and the Standing Lending Facility Rate (SLFR), being reduced by 125 and 175 basis points, respectively, and the Statutory Reserve Requirement (SRR) on Rupee deposit liabilities of commercial banks being reduced by 2 percentage points during the period. Responding to the eased monetary policy stance, both market lending and deposit interest rates have adjusted downwards substantially, although there is further room for downward adjustment in long term lending rates.

Benign inflation and favourable inflation outlook, which were the key contributory factors in enabling the maintenance of the current monetary policy stance, continue to remain favourable. In April 2014, year-on-year (y-o-y) headline inflation was 4.9 per cent, which was well within the desired range, while y-o-y core inflation remained unchanged at 3.4 per cent. Inflation is projected to remain benign in the months ahead, supported by favourable expectations although weather related supply disruptions could cause some marginal variation in the behaviour of certain food items.

In the external sector, the trade deficit contracted by nearly 12 per cent for the first quarter 2014 boosted by high export trade volumes recorded in March 2014. Export earnings in March surpassed US dollars 1 billion recording a significant 28.6 per cent growth (y-o-y). Further, the outlook for export earnings remains positive on account of the firming up of the recovery in advanced economies. A modest increase in expenditure on imports was also observed in March due to increased intermediate and consumer goods imports ahead of the April festive season. Inflows on account of workers' remittances recorded a significant increase in March 2014 while earnings from tourism also continued to increase during the first four months of 2014 surpassing the half million mark in tourist arrivals by April 2014. As at end March 2014, gross official reserves were at US dollars 8.1 billion, equivalent to 5.5 months of imports. Since then, the level of reserves has increased further with the inflows from the proceeds of the seventh international sovereign bond issued in April 2014.

Broad money (M_{2b}) continued its moderating trend to record a y-o-y growth of 14.5 per cent in March 2014, moving towards the projected average growth of 14 per cent in 2014. The increase in net foreign assets (NFA) of the banking sector by Rs. 24.8 billion as well as the significant increase in net credit to the government (NCG) by Rs. 48.6 billion, mainly contributed to the growth of broad money during the month of March. Public corporations continued to settle their liabilities to the banking sector, with total reduction in credit to public corporations during the first three months of the year amounting to Rs. 35.1 billion. Credit extended to the private sector increased by Rs. 7.6 billion in March 2014. An increase of Rs. 15.3 billion was observed in the credit extended to the private sector from the domestic banking units (DBUs), while repayments by BOI companies to offshore banking units (OBUs) dampened the overall credit growth. The sharp decline in pawning advances contributed largely to the continued low growth of credit to the private sector.

Having considered the above, the Monetary Board, at the meeting held on 19th May 2014, was of the view that the current monetary policy stance is appropriate and therefore, decided to maintain the policy interest rates of the Central Bank, namely

the SDFR and the SLFR of the Central Bank unchanged at their current levels of 6.50 per cent and 8.00 per cent, respectively. In order to counter the effect of the continued decline in pawning advances on productive sectors of the economy, the Monetary Board also granted approval to implement a credit guarantee scheme on pawning advances on behalf of the government. At the same time, the Central Bank expects commercial banks to pass the benefit of the eased monetary policy stance to borrowers without further delay.

The date for the release of the next regular statement on monetary policy would be announced in due course.