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CENTRAL BANK OF SRI LANKA

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# Press Release

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## Monetary Policy Review – August 2015

Headline inflation remained in the negative territory for the second consecutive month, recording -0.2 per cent in August 2015 on a year-on-year basis. Headline inflation, on an annual average basis, moderated further to 1.0 per cent in August 2015 from 1.3 per cent in the previous month. Meanwhile, core inflation, which reflects the underlying price movements in the economy, increased to 3.9 per cent in August 2015 on a year-on-year basis, from 3.5 per cent in the previous month. Going forward, the inflation outlook and expectations remain favourable for the remainder of the year, supported by improved domestic supply conditions and subdued global commodity prices.

Although some pressures in the short term interest rates were observed along with declining liquidity levels in the domestic money market, most market interest rates continue to remain at low levels. Supported by the prevailing low interest rates, the year-on-year growth of credit extended to the private sector by commercial banks accelerated to 19.4 per cent in June 2015 compared to 17.6 per cent in May 2015. Credit disbursed in absolute terms increased by around Rs. 55 billion during the month of June, while on a cumulative basis, credit to the private sector increased by around Rs. 205 billion during the first half of 2015 compared to a decline of Rs. 53 billion during the corresponding period in 2014. The expansion in private sector credit in the first half of the year was largely due to higher disbursements of credit to the Industry and Services sectors. Nevertheless, the rapid increase in the imports of consumer durables including motor vehicles driven by credit available at low interest rates, among other things, has raised some concerns. The Central Bank is

closely monitoring these developments in order to ensure that credit continues to be available to support productive economic activity while avoiding excessive expansion in credit in the period ahead. Meanwhile, driven by the expansion in private sector credit along with increased bank borrowings by the public sector, the year-on-year growth of broad money ( $M_{2b}$ ) remained at 15.3 per cent in June 2015 compared to 15.4 per cent in the previous month.

In the external sector, increased expenditure on imports relative to earnings from exports widened the trade deficit in the month of June 2015 as well as on a cumulative basis during the first half of the year. However, regular inflows of remittances and earnings from tourism continued to support the current account balance. In the meantime, net inflows to the financial account moderated further during this period, largely responding to expected developments in the advanced economies. In addition, reflecting the repayments made under the IMF's Stand-By Arrangement (SBA) and the payments made to the Asian Clearing Union (ACU), as well as the intervention by the Central Bank to reduce excess volatility in the domestic foreign exchange market, gross official reserves, which stood at US dollars 7.5 billion at end June 2015, are estimated to have decreased to US dollars 6.8 billion by end July 2015. However, official reserves are expected to increase during the remainder of the year with higher inflows arising from improved business outlook and investor confidence along with the realisation of the remaining proceeds of the currency swap arrangement with the Reserve Bank of India (RBI) amounting of US dollars 1.1 billion and long term financial flows to the government, including the planned term loan of US dollars 500 million. Reflecting the domestic and global developments, the Sri Lankan rupee has depreciated by 2.3 per cent to Rs. 134.30 against the US dollar so far during the year.

Taking the above developments in the economy into consideration, the Monetary Board, at its meeting held on 31 August 2015, was of the view that the current monetary policy stance is appropriate. Accordingly, the Monetary Board decided to maintain the Standing Deposit Facility Rate (SDFR) and the Standing Lending Facility Rate (SLFR) of the Central Bank unchanged at 6.00 per cent and 7.50 per cent, respectively.

<b>Monetary Policy Decision:</b>	<b>Policy rates unchanged</b>
Standing Deposit Facility Rate (SDFR)	6.00%
Standing Lending Facility Rate (SLFR)	7.50%
Statutory Reserve Ratio (SRR)	6.00%