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Press Release

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Monetary Policy Review: No. 1 – 2019

The Monetary Board of the Central Bank, at its meeting held on 21 February 2019, decided to reduce the Statutory Reserve Ratio (SRR) applicable on all rupee deposit liabilities of commercial banks by 1.00 percentage point to 5.00 per cent with effect from 01 March 2019. The Board also decided to keep the policy interest rates of the Central Bank unchanged at their current levels, and accordingly, the Standing Deposit Facility Rate (SDFR) and the Standing Lending Facility Rate (SLFR) of the Central Bank will remain at 8.00 per cent and 9.00 per cent, respectively. The Board arrived at this decision following a careful analysis of current and expected developments in the domestic economy and the financial market as well as in the global economy, with the broad aim of stabilising inflation at mid single digit levels in the medium term to enable the economy to reach its potential.

Economic growth remains below potential

Available leading indicators and current projections suggest that Sri Lanka's real economic growth will continue to remain subdued during the fourth quarter of 2018 as well, and economic growth in 2019 is also expected to be modest. The economy is expected to gradually reach its potential in the medium term benefitting from the low inflation environment, competitive exchange rate and appropriate policies to support investment.

Despite an uptick in inflation in January 2019, inflation outlook remains favourable in the medium term

Headline inflation and core inflation as measured by the year-on-year change in both Colombo Consumer Price Index (CCPI, 2013=100) and National Consumer Price Index (NCPI, 2013=100) increased in January 2019 mainly due to the increase in non-food inflation driven by higher expenditure on certain items such as house rentals and education. Recent upward adjustments to fuel prices as well as possible increases in administratively determined prices of certain commodities could exert some transitory price pressures in the coming months. However, domestic supply side developments are expected to be favourable in the period ahead. Projections indicate that inflation is likely to remain in the desired 4-6 per cent range in 2019 and beyond.

External sector has witnessed some improvements so far in 2019 amidst challenging global economic conditions

Amidst a modest growth in exports, a slowdown in import expenditure was observed, particularly during the latter part of 2018, resulting from policy measures adopted by the government and the Central Bank to curtail motor vehicle and non-essential goods imports. These developments contained the trade deficit significantly in November and December 2018. The noticeable growth of earnings from tourism continued to support the current account of the balance of payments (BOP), although workers' remittances recorded a marginal decline in 2018. In the financial account, foreign investments to the government securities market recorded a net inflow thus far during 2019. The Sri Lankan rupee strengthened somewhat underpinned by net inflows to the government securities market and the slowdown in imports along with changing global financial conditions. Meanwhile, Sri Lanka met the scheduled repayment of the maturing International Sovereign Bond of US dollars 1 billion in January 2019. By end January 2019, gross official reserves stood at US dollars 6.2 billion, which was sufficient to finance 3.4 months of imports.

Persistently tight liquidity conditions in the domestic money market

Deficit liquidity conditions in the domestic money market continued to persist at high levels, despite the liquidity injection through the reduction in SRR by 1.50 percentage points to 6.00 per cent in mid-November 2018. In the tight liquidity environment, the Central Bank continued to conduct open market operations appropriately, while allowing the short-term money market rates to remain around the upper bound of the policy rate corridor. Other market interest rates also remained at elevated levels both in nominal and real terms.

Expansion in credit to both public and private sectors was more than expected in 2018 irrespective of tight market liquidity conditions and high interest rates. This was partly attributable to the private sector borrowers' short term responses to policies adopted to limit imports and related expectations. The government also relied more on domestic sources of financing, while the weak financial performance of state-owned business enterprises also contributed to credit growth. However, driven by the contraction in net foreign assets of the banking sector, the year-on-year growth of broad money (M_{2b}) decelerated by end 2018 as envisaged.

The monetary policy decision is expected to reduce the liquidity deficit in the domestic money market

Given the current and expected conditions in the domestic economy and financial market, the Monetary Board observed that the continuation of the current neutral monetary policy stance is appropriate. However, the Board was of the view that some policy intervention by the Central Bank to address the large and persistent liquidity deficit in the domestic money market is warranted. Accordingly, the Monetary Board decided to reduce the Statutory Reserve Ratio (SRR) applicable on all rupee deposit liabilities of commercial banks by 1.00 percentage point to 5.00 per cent from the current level of 6.00 per cent with effect from the next reserve maintenance period commencing 01 March 2019. The Standing Deposit Facility Rate (SDFR) and the Standing Lending Facility Rate (SLFR) of the Central Bank will remain unchanged at their current levels.

Monetary Policy Decision: SRR reduced and policy rates unchanged

Standing Deposit Facility Rate (SDFR)	8.00%
Standing Lending Facility Rate (SLFR)	9.00%
Statutory Reserve Ratio (SRR)	5.00%

INFORMATION NOTE:

A press conference with Governor Dr. Indrajit Coomaraswamy will be held today (22 February 2019) at 11.30 am at the John Exter International Conference Hall (JEICH) of the Central Bank of Sri Lanka.

The release of the next regular statement on monetary policy will be on 10 April 2019.

Data Annexure:

Table 01: Inflation

Month		Mar 18	Jun 18	Sep 18	Oct 18	Nov 18	Dec 18	Jan 19
Headline Inflation (Year on year % change)	CCPI (2013=100)	4.2	4.4	4.3	3.1	3.3	2.8	3.7
	NCPI (2013=100)	2.8	2.5	0.9	0.1	1.0	0.4	1.2
Core Inflation (Year on year % change)	CCPI (2013=100)	3.4	3.4	3.8	3.8	3.4	3.1	5.5
	NCPI (2013=100)	1.9	1.8	3.1	3.4	3.1	3.1	5.1

Source: Department of Census and Statistics

Table 02: Monetary Sector Developments (Provisional)

Indicator	Outstanding Amount (Rs. billion)					Year - on - Year % Change				
	Mar 18	Jun 18	Sep 18	Nov 18	Dec 18	Mar 18	Jun 18	Sep 18	Nov 18	Dec 18
Reserve Money	997	999	1,011	942	961	11.8	12.0	11.2	3.3	2.3
Broad Money (M _{2b})	6,607	6,748	6,933	7,043	7,128	16.4	14.9	13.1	13.9	13.0
Net Foreign Assets (NFA)	106	101	8	(43)	(67)	128.6	141.1	(27.0)	(163.9)	(155.1)
Net Domestic Assets (NDA)	6,500	6,646	6,926	7,086	7,195	7.5	8.6	13.1	15.8	16.3
Net Credit to the Government (NCG)	2,278	2,273	2,427	2,464	2,515	2.9	1.7	9.2	14.0	16.0
Credit to Public Corporations	557	619	656	715	755	(2.6)	8.5	27.1	41.7	40.7
Credit to the Private Sector	5,022	5,156	5,356	5,509	5,561	15.3	14.9	15.4	16.2	15.9
Broad Money (M ₄)	8,112	8,292	8,502	8,612	8,730	16.7	14.8	12.5	12.4	12.0

Source: Central Bank of Sri Lanka

Table 03: Interest Rates

Interest Rate (%)	End Mar 18	End Jun 18	End Sep 18	End Nov 18	End Dec 18	End Jan 19	As at 21 Feb 19
Policy Rates of the Central Bank							
Standing Deposit Facility Rate	7.25	7.25	7.25	8.00	8.00	8.00	8.00
Standing Lending Facility Rate	8.75	8.50	8.50	9.00	9.00	9.00	9.00
Average Weighted Call Money Rate (AWCMR)	8.41	8.50	8.40	8.96	8.95	9.00	8.99
Treasury bill yields (Primary market)							
91-day	8.17	8.32	8.56	10.01	-	-	9.55
182-day	-	8.85	-	9.99	9.99	9.87	9.87
364-day	9.69	9.39	9.51	11.20	11.20	10.69	10.73
Lending Rates							
Average Weighted Prime Lending Rate (Weekly)	11.55	11.33	11.74	12.03	12.09	12.27	12.08
Average Weighted Lending Rate (AWLR)	14.04	14.05	14.27	14.50	14.40	-	-
Average Weighted New Lending Rate (AWNLR)	14.25	13.94	14.22	14.51	14.44	-	-
Deposit Rates							
Average Weighted Deposit Rate (AWDR)	9.00	8.92	8.69	8.77	8.81	8.85	-
Average Weighted Fixed Deposit Rate (AWFDR)	11.41	11.26	10.84	10.81	10.85	10.91	-
Average Weighted New Deposit Rate (AWNDR)	10.33	10.57	9.72	10.38	10.94	-	-

Source: Central Bank of Sri Lanka