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CENTRAL BANK OF SRI LANKA

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# Press Release

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## Monetary Policy Review: No. 4 – 2019

### Policy interest rates of the Central Bank of Sri Lanka to remain unchanged

The Monetary Board of the Central Bank of Sri Lanka, at its meeting held on 11 July 2019, decided to maintain the Standing Deposit Facility Rate (SDFR) and the Standing Lending Facility Rate (SLFR) of the Central Bank at their current levels of 7.50 per cent and 8.50 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 the global economy. The decision of the Monetary Board is consistent with the aim of maintaining inflation in the desired 4-6 per cent range while supporting economic growth to reach its potential over the medium term.

### Softening global growth spurs a dovish turn in monetary policies

Amidst expectations of softening global growth due to increased trade and geopolitical tensions, monetary policies in advanced economies have turned increasingly dovish since the beginning of this year. A number of central banks in emerging market economies have also reacted by relaxing their monetary policies, with a view to supporting domestic economic growth amidst subdued inflationary pressures and volatile global market conditions.

### Sri Lankan economy to recover gradually, following the Easter Sunday attacks

The Sri Lankan economy grew at a relatively healthy rate of 3.7 per cent (year-on-year) during the first quarter 2019, compared to 1.8 per cent recorded in the fourth quarter

2018, according to provisional estimates published by the Department of Census and Statistics. Weaker than originally envisaged growth in tourism and related services in the aftermath of the Easter Sunday attacks could affect economic growth in the near term, while subdued global growth is likely to hamper the medium term growth prospects of the economy. However, the ongoing recovery in the tourism sector as well as the performance of exports provide some confidence of a speedy recovery, with the support of actions taken by the sectoral authorities, as well overall fiscal and monetary policies.

### **Narrowing trade deficit amidst a challenging global climate**

The continued growth of exports along with the sharp decline in imports led to a further contraction in the trade deficit during the first four months of 2019. In relation to other inflows to the current account, earnings from tourism suffered a setback following the April terror attacks, while inflows from workers' remittances remained moderate. In the meantime, the successful issuance of the International Sovereign Bonds (ISBs) in June 2019 reflected investors' continued confidence on Sri Lanka's medium term growth prospects. Following the receipt of the proceeds of the ISBs, gross official reserves reached US dollars 8.9 billion by end June 2019, which provide an import cover of 5.1 months. The contraction in the trade deficit and the receipt of the proceeds from the ISBs, along with the continuation of the Extended Fund Facility Programme with the International Monetary Fund (IMF-EFF) have eased the pressure on the exchange rate, resulting in the Sri Lankan rupee recording a cumulative appreciation of 4.1 per cent against the US dollar thus far in 2019. This appreciation of the rupee has partially corrected its sharp depreciation observed in late 2018.

### **Private sector credit to pick up gradually towards the latter part of 2019**

The year-on-year growth of credit extended to the private sector by commercial banks continued to decelerate during the first five months of 2019, while recording an absolute cumulative decline during the period. Following this trend in the growth of credit, the year-on-year growth of broad money (M<sub>2b</sub>) also decelerated thus far in 2019. Credit to the private sector is expected to gradually pick up in the latter part of 2019, with the expected decline in market lending rates.

### **A sizable downward adjustment in market lending rates is expected in the near term**

Market deposit rates have declined in response to the measures already taken to ease monetary policy and monetary conditions. In particular, the reduction of policy interest rates in May 2019, coupled with sizable liquidity injections through the reduction in the Statutory

Reserve Ratio (SRR) and the imposition of maximum interest rates on deposit products in April 2019, have resulted in a notable drop in the Average Weighted Call Money Rate (AWCMR), yields on government securities, new deposit rates as well as the Average Weighted Prime Lending Rate (AWPR). However, the transmission of recent easing of monetary conditions to market lending rates, including AWPR, is not yet complete. It is expected that the ongoing downward adjustment in market lending rates would expedite in the immediate future, thus supporting the revival of demand for credit by the private sector and the recovery in economic activity.

### **In spite of near-term upticks, the medium-term inflation outlook remains favourable**

Both year-on-year headline and core inflation, measured using the Colombo Consumer Price Index (CCPI), decelerated in June 2019, while those based on the National Consumer Price Index (NCPI) are also expected to decline in June. In the near term, some price pressures could emerge, reflecting elevated fuel prices, possible increases in global food commodity prices and a rise in domestic food prices due to adverse weather conditions. Such hikes in inflation are likely to be transitory, and in general, inflation is projected to remain well anchored in the desired 4-6 per cent range. With subdued economic activity, aggregate demand pressure on inflation is not expected in the near term, while the favourable medium-term inflation outlook will be supported by appropriate monetary policy measures.

### **Policy interest rates maintained at current levels**

Considering the current and expected macroeconomic conditions, the Monetary Board was of the view that there is ample space for market lending rates to adjust downwards in response to the policy measures already taken. Accordingly, the Monetary Board decided to maintain the Standing Deposit Facility Rate (SDFR) and the Standing Lending Facility Rate (SLFR) of the Central Bank at their current levels of 7.50 per cent and 8.50 per cent, respectively. The Central Bank will continue to monitor the developments in the global and domestic financial markets and take appropriate further action as necessary to support economic growth in the context of well-anchored inflation and inflation expectations.

### **INFORMATION NOTE:**

A press conference with Governor Dr. Indrajit Coomaraswamy will be held today (11 July 2019) at 5.00 pm at the Atrium of the Central Bank of Sri Lanka.

The release of the next regular statement on monetary policy will be on 23 August 2019.

**Data Annexure:**

**Table 01: Real GDP Growth (Provisional)**

Economic Activities	Year - on - Year % Change									
	2017				2018					2019
	Second Quarter	Third Quarter	Fourth Quarter	Annual	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Annual	First Quarter
<b>Agriculture</b>	-2.6	-2.0	7.2	<b>-0.4</b>	5.1	5.6	4.0	4.5	<b>4.8</b>	5.5
<b>Industries</b>	4.7	4.7	4.3	<b>4.1</b>	1.7	2.8	3.1	-3.6	<b>0.9</b>	3.0
<b>Services</b>	3.9	2.8	3.4	<b>3.6</b>	5.5	4.8	4.3	4.3	<b>4.7</b>	4.1
<b>GDP</b>	<b>3.6</b>	<b>3.2</b>	<b>3.7</b>	<b>3.4</b>	<b>4.0</b>	<b>3.9</b>	<b>3.5</b>	<b>1.8</b>	<b>3.2</b>	<b>3.7</b>

*Source: Department of Census and Statistics*

**Table 02: Inflation**

Month		Dec 18	Jan 19	Feb 19	Mar 19	Apr 19	May 19	Jun 19
<b>Headline Inflation</b> (Year on year % change)	CCPI (2013=100)	2.8	3.7	4.0	4.3	4.5	5.0	3.8
	NCPI (2013=100)	0.4	1.2	2.4	2.9	3.6	3.5	-
<b>Core Inflation</b> (Year on year % change)	CCPI (2013=100)	3.1	5.5	5.4	5.6	5.5	6.2	5.8
	NCPI (2013=100)	3.1	5.1	5.5	5.8	6.3	6.3	-

*Source: Department of Census and Statistics*

**Table 03: Monetary Sector Developments (Provisional)**

Indicator	Outstanding Amount (Rs. billion)					Year - on - Year % Change				
	Jan19	Feb19	Mar19 (a)	Apr19 (a)	May19	Jan19	Feb19	Mar19 (a)	Apr19 (a)	May19
Reserve Money	949	963	963	924	849	2.1	2.7	(3.4)	(7.6)	(12.7)
Broad Money (M <sub>2b</sub> )	7,111	7,189	7,253	7,295	7,295	11.5	11.4	9.8	9.0	9.4
Net Foreign Assets (NFA)	(129)	(103)	23	110	103	(201.3)	(189.2)	(78.2)	(7.6)	38.3
Net Domestic Assets (NDA)	7,240	7,292	7,230	7,185	7,192	15.8	15.1	11.2	9.3	9.0
Net Credit to the Government (NCG)	2,625	2,672	2,613	2,584	2,595	18.2	19.0	14.7	11.3	11.6
Credit to Public Corporations	711	715	703	726	726	34.6	31.0	26.2	24.9	19.4
Credit to the Private Sector	5,557	5,565	5,588	5,544	5,542	14.8	13.6	11.3	9.9	9.2
Broad Money (M <sub>4</sub> )	8,741	8,831	8,902	8,968	8,980	10.7	10.7	9.7	9.1	9.4

Source: Central Bank of Sri Lanka

(a) Revised

**Table 04: Interest Rates**

Interest Rate (%)	End Jan 19	End Feb 19	End Mar 19	End Apr 19	End May 19	End Jun 19	As at 10 Jul 19
<b>Policy Rates of the Central Bank</b>							
Standing Deposit Facility Rate	8.00	8.00	8.00	8.00	7.50	7.50	7.50
Standing Lending Facility Rate	9.00	9.00	9.00	9.00	8.50	8.50	8.50
<b>Average Weighted Call Money Rate (AWCMR)</b>	9.00	8.96	8.51	8.49	7.94	7.86	7.80
<b>Treasury bill yields (Primary market)</b>							
91-day	-	9.55	9.39	8.89	8.52	8.24	8.09
182-day	9.87	9.87	9.67	9.09	8.63	8.49	8.21
364-day	10.69	10.67	10.40	9.81	8.88	8.70	8.54
<b>Lending Rates</b>							
Average Weighted Prime Lending Rate (Weekly)	12.27	12.51	12.23	12.20	11.82	11.52	11.13
Average Weighted Lending Rate (AWLR)	14.44	14.48	14.49	14.47	14.48	-	-
Average Weighted New Lending Rate (AWNLR)	14.41	14.60	14.56	14.62	14.59	-	-
<b>Deposit Rates</b>							
Average Weighted Deposit Rate (AWDR)	8.85	8.88	8.98	8.97	9.00	8.94	-
Average Weighted Fixed Deposit Rate (AWFDR)	10.91	10.96	11.11	11.15	11.19	11.07	-
Average Weighted New Deposit Rate (AWNDR)	11.21	11.13	11.42	11.24	10.05	-	-

Source: Central Bank of Sri Lanka