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இலங்கை மத்திய வங்கி
CENTRAL BANK OF SRI LANKA

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Press Release

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The Central Bank publishes “Recent Economic Developments: Highlights of 2019 and Prospects for 2020”

The Central Bank of Sri Lanka today published “Recent Economic Developments: Highlights of 2019 and Prospects for 2020” on-line. The publication can be downloaded via the CBSL website in Sinhala, Tamil and English languages.¹

An overview of the performance of the Sri Lankan economy in 2019, as reflected in “Recent Economic Developments”, is given below:

The growth of the Sri Lankan economy moderated in the first half of the year amidst challenges emanating mainly in the domestic front, including the spillover effects of the Easter Sunday attacks. Accordingly, the economy grew at a slower pace of 2.6 per cent in real terms in the first half of 2019, compared to 3.9 per cent recorded in the corresponding period in 2018. The unemployment rate also increased during the first half of 2019 in line with subdued economic growth.

Headline inflation continued to remain within the anticipated range thus far during the year, with occasional volatilities due to supply side developments. Core inflation accelerated in January 2019, mainly due to a one-off adjustment in house rentals, and the impact of this adjustment is expected to wear off in January 2020.

The Central Bank continued to conduct monetary policy in a forward looking manner within an enhanced monetary policy framework aimed at stabilising inflation in mid-single digit levels,

¹ Weblink to the English Version: <https://www.cbsl.gov.lk/en/publications/economic-and-financial-reports/recent-economic-developments/recent-economic-developments-2019>

while progressing rapidly towards transitioning to full fledged Flexible Inflation Targeting (FIT). Against the backdrop of well anchored inflation and inflation expectations, the Central Bank adopted an accommodative monetary policy stance in 2019, considering sluggish economic growth, the continued slowdown in monetary and credit expansion and global monetary policy easing. However, forward guidance on monetary policy needs to be tempered by the salary increase in the pipeline.

In spite of monetary easing, market interest rates remained high in both nominal and real terms, prompting the Central Bank to impose caps on deposit interest rates of financial institutions, in April 2019, to expedite monetary policy transmission. With deposit interest rates and cost of funds declining, the Central Bank removed the caps on deposit interest rates of licensed banks and imposed caps on lending rates, in September, to support economic activity. The financial sector in the meantime, remained sound, while measures were taken to decisively address issues in a few distressed finance companies.

The external sector remained resilient amidst the setback in the tourism sector following the Easter Sunday attacks. The trade deficit contracted significantly during the first eight months of 2019 in comparison to the corresponding period of 2018, with lower import expenditure and increased earnings from exports. The contraction of the trade deficit and healthy inflows to the services account helped record a surplus in the current account in the first quarter of the year, although a notable moderation in tourism earnings and workers' remittances in the second quarter caused a marginal deficit in the current account in the first half of the year.

Meanwhile, the financial account improved, particularly with the issuance of International Sovereign Bonds (ISBs). With these developments, gross official reserves increased to US dollars 7.6 billion by end September 2019 from US dollars 6.9 billion at end 2018 and the Sri Lankan rupee has appreciated against the US dollar thus far during the year.

On the fiscal front, budgetary operations weakened as reflected in the movement of key fiscal indicators during the first seven months of 2019, despite continued efforts of the government towards fiscal consolidation. The government revenue declined during the period, reflecting the impact of policy measures to curtail imports of personal motor vehicles, sluggish economic activity following the Easter Sunday attacks and the delay in implementing certain revenue proposals announced in the Budget 2019. Nevertheless, the collection of income tax improved due to the implementation of new Inland Revenue Act. With reduced revenue and increased expenditure, the overall budget deficit deteriorated to 4.4 per cent of the estimated GDP during the first seven months of 2019 from 3.2 per cent in the same period of 2018, while the current account deficit widened, indicating government dissavings. The primary balance, i.e., the difference between revenue and non interest expenditure,

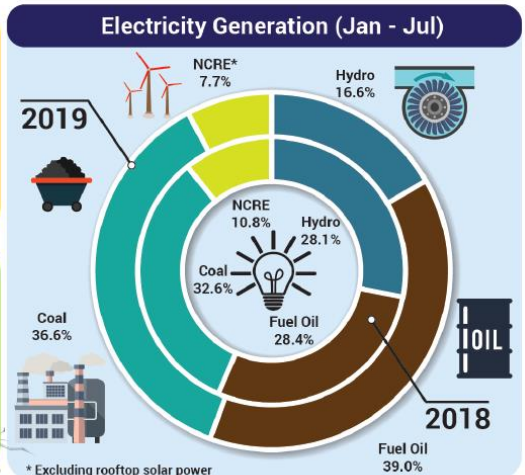
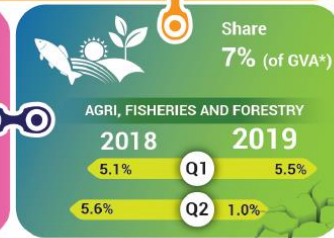
turned to a deficit in the first seven months of 2019, reversing the surplus maintained in 2017 and 2018.

The government's structural reform programme supported by the Extended Fund Facility of the International Monetary Fund (IMF-EFF) continued, and upon the successful completion of the sixth review, the receipt of the seventh tranche under the facility is expected in early November 2019.²

The outlook for the economy, in both the short and medium term, will be determined to a significant extent by the degree of policy discipline maintained during and after the election period.

² On 01 November 2019, the Executive Board of the IMF completed the sixth review under the EFF. The completion of the sixth review, upon the granting of a waiver of non-observance for the end June 2019 performance criterion on the primary balance, enables the disbursement of SDR 118.5 million (about US dollars 164 million), bringing total disbursements under the arrangement to SDR 952.23 million (about US dollars 1.31 billion).

Snapshot of the Sri Lankan Economy



Effect of Easter Sunday Attacks on Services Sector

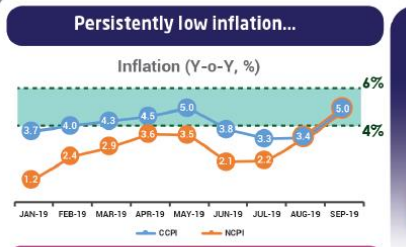
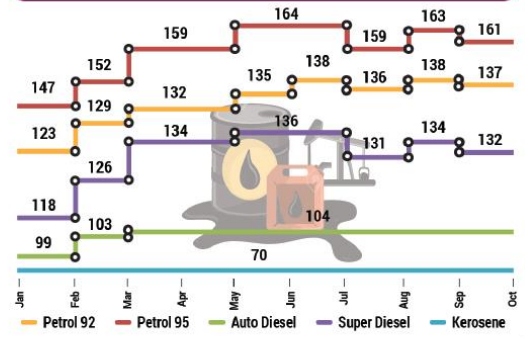
Category	2019Q1	2019Q2
Wholesale and Retail	4.4%	1.3%
Transportation	1.8%	(1.5)%
Accommodation, Food and Beverage	4.5%	(9.9)%

Transport sector slowed down during H1 2019

Road Passenger Kilometrage	(5.9)%
Rail Passenger Kilometrage	(4.4)%
Rail Goods Kilometrage	(3.6)%
Civil Aviation	
Total Passenger Movements	(19.0)%
Total Cargo Handling	(8.0)%



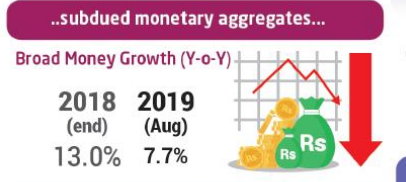
Petroleum Price Revisions of the CPC (Rs./litr) - 2019



Slowdown in global economic activity has prompted many economies to become increasingly accommodative

...high nominal and real interest rates...

...Central Bank of Sri Lanka adopted an accommodative monetary policy stance in 2019

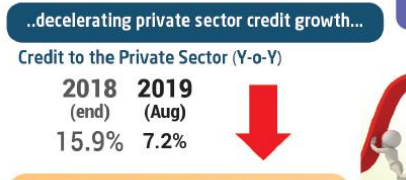


Over 60 Central Banks reducing policy rates (As of 30 September 2019)

..below potential economic growth

14 Nov 2018: SRR 1.5 percentage points (w.e.f. 16 Nov 2018), SDFR 75 bps and SLFR 50 bps

1 March 2019: SRR 1.0 percentage point



04 April 2018: SLFR 25 bps

Large and persistent liquidity deficit

Further measures to improve monetary transmission

- Caps on deposit rates (w.e.f. 26 Apr - 24 Sep 2019)
- Caps on market lending rates (w.e.f. 24 Sep 2019)

All market lending rates are expected to reduce in line with the reduction in deposits interest rates



End to Monetary Tightening cycle

Neutral Monetary Policy

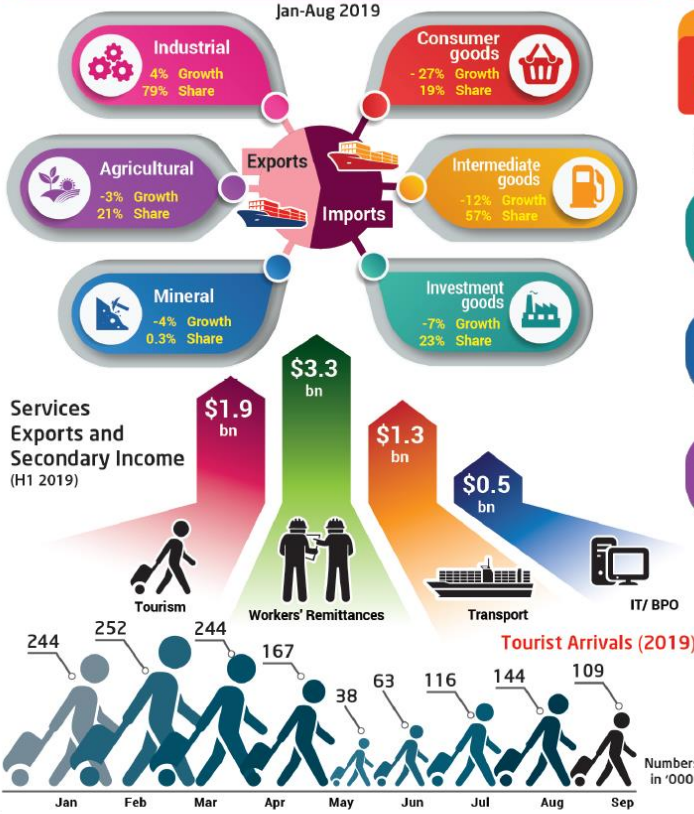
31 May 2019: SDFR and SLFR 50 bps

23 Aug 2019: SDFR and SLFR 50 bps

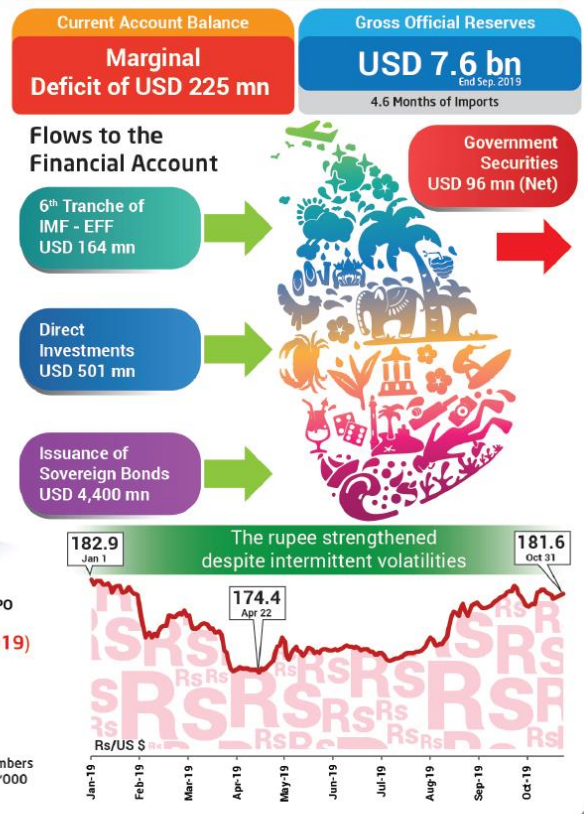
Monetary Relaxing

Progressing towards transitioning to Flexible Inflation Targeting (FIT) by 2020

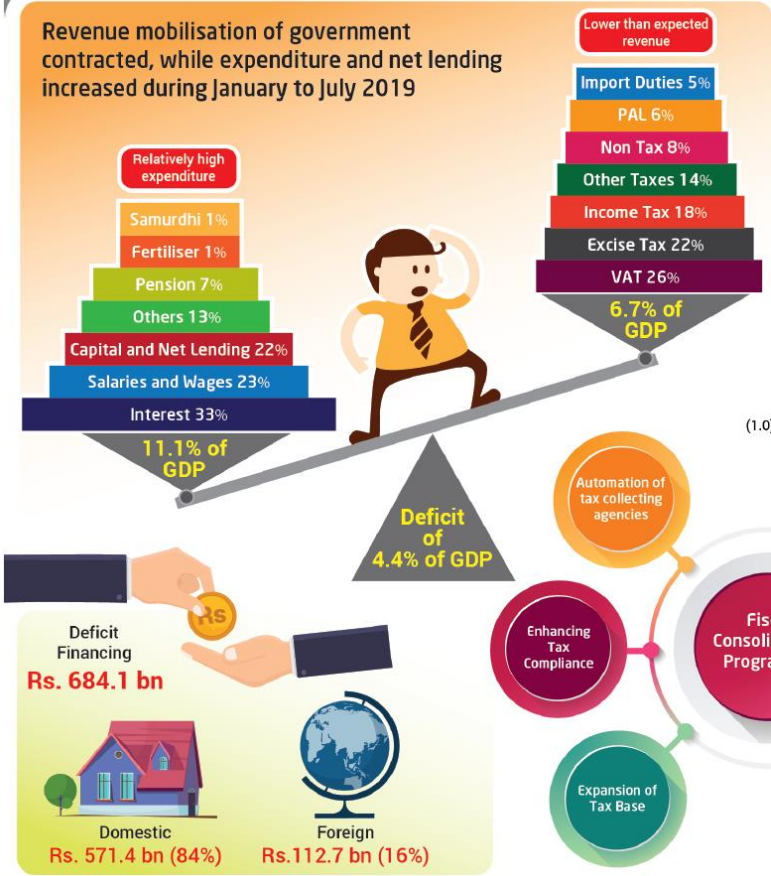
Total Exports 8,031 (USD mn) | Total Imports 12,886 (USD mn)



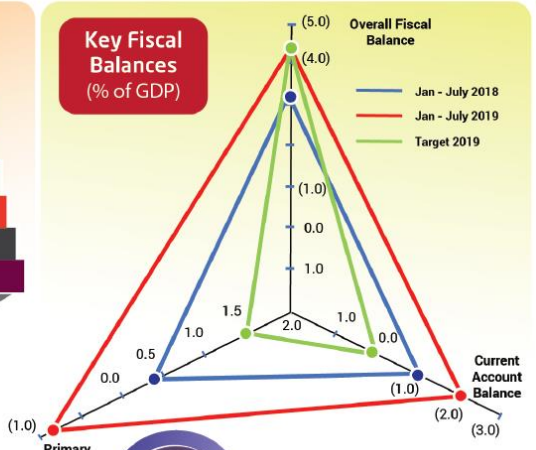
Balance of Payments, H1 2019



Revenue mobilisation of government contracted, while expenditure and net lending increased during January to July 2019



Key Fiscal Balances (% of GDP)



Central Government Debt (Rs. bn)

