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Press Release

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Monetary Policy Review: No. 7 – 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 28 November 2019, decided to maintain its accommodative monetary policy stance with the Standing Deposit Facility Rate (SDFR) and the Standing Lending Facility Rate (SLFR) of the Central Bank remaining at their current levels of 7.00 per cent and 8.00 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 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.

Monetary policy in several key economies has become increasingly accommodative in view of the bleak global economic outlook

While mounting geopolitical and trade tensions have led to a significant deterioration of global growth and its outlook, resultant subdued demand pressures and low commodity prices have posed notable downside risks to the global inflation outlook. In response, most central banks of advanced economies as well as emerging market economies have continued to ease monetary policy with a view to stimulating aggregate demand and boosting consumer and investor confidence.

A gradual revival in domestic economic activity is expected over the medium term

Economic growth is predicted to be modest during the remainder of the year, with likely subpar growth in Industry and Services activities as implied by leading indicators. However, improved investor confidence, supported by political stability and fiscal stimulus driven boost to aggregate demand, is expected to drive short term growth. The introduction of an appropriate policy mix, which utilises the available limited policy space prudently, would support the economy to reach as well as enhance its potential over the medium term.

External sector remains resilient

External sector performance was buoyed by the cumulative contraction of the trade deficit over the first nine months of 2019, largely driven by the decline in import expenditure. Tourist arrivals continued to show a gradual yet steady improvement after the Easter Sunday attacks. The rupee denominated Government securities market experienced foreign inflows in recent weeks, but recorded a cumulative net outflow thus far during the year. Although there were net outflows from the stock market, market indices responded positively to political developments in recent weeks. The Sri Lankan rupee displayed increased volatility, following a notable appreciation against the US dollar in the immediate aftermath of the Presidential election. Overall, the rupee has appreciated against the US dollar by 1.0 per cent thus far during the year. Gross official reserves are estimated at US dollars 7.8 billion at end October 2019, providing an import cover of 4.7 months.

Market lending rates continue to decline, responding to the measures taken by the Central Bank

Market lending rates are adjusting downwards, responding to the relaxation of monetary policy and the imposition of caps on lending interest rates of licensed banks. A further decline in market lending rates is expected in the period ahead in line with the measures taken so far and also as a result of reduced cost of funds on account of the recent reduction in effective tax on the banking sector. Specifically, the Average Weighted Prime Lending Rate (AWPR) is expected to reduce by a further 70 basis points to 9.50 per cent by end 2019, while the Average Weighted Lending Rate (AWLR) is projected to decline by around 120 basis points to below 12.50 per cent by March 2020. Interest rates on the stock of deposits continued to decline, while interest rates on new deposits, which declined notably until September 2019, showed some increase in the month of October 2019, following the removal of the cap on deposit interest rates of licensed banks.

Growth of monetary and credit aggregates is expected to recover gradually

Monthly credit disbursements to the private sector continued to expand in absolute terms during August-October 2019. Accordingly, growth of private sector credit, which decelerated sharply during the first ten months of the year, is expected to accelerate gradually in 2020 with the revival of economic activity, the ongoing reduction in market lending rates and improved market sentiments. Meanwhile, credit to the public sector showed a cumulative expansion during the first ten months of the year. Driven by subdued credit expansion to the private sector, broad money growth (M_{2b}) also continued to moderate during the period under review.

Despite near term volatilities, inflation is expected to remain in the desired range of 4-6 per cent in the near term as well as the medium term

Headline inflation, as measured by the year-on-year changes in Colombo Consumer Price Index (CCPI) as well as National Consumer Price Index (NCPI), accelerated recently due to increased food prices driven by domestic supply disruptions. These transitory supply side disruptions are expected to cause continued volatility in inflation in the near term together with tax revisions and possible revisions to administratively determined prices. Meanwhile, the planned public sector wage increases could have a direct upward impact on aggregate demand in 2020. However, with the prevailing negative output gap expected to close only gradually in the medium term, and supported by well anchored inflation expectations, inflation is projected to remain within the desired range over the medium term.

Policy interest rates maintained at current levels

The Monetary Board, at its meeting held on 28 November 2019, was of the view that the policy measures adopted by the Central Bank in recent months are being transmitted to the economy through the financial market with market lending rates declining as envisaged. While noting the fiscal slippages thus far during the year, the Monetary Board observed that the recent tax revisions would support lower inflation and higher economic growth in the short term, but was of the view that greater clarity with regard to the medium term fiscal path of the government is required to assess the impact on the economy over the medium term. Accordingly, considering the current and expected conditions in the economy and the financial market, 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 7.00 per cent and 8.00 per cent, respectively.

Monetary Policy Decision: Policy rates and SRR unchanged

Standing Deposit Facility Rate (SDFR)	7.00%
Standing Lending Facility Rate (SLFR)	8.00%
Statutory Reserve Ratio (SRR)	5.00%

INFORMATION NOTE:

A press conference with Governor Dr. Indrajit Coomaraswamy will be held on 29 November 2019 at 11.30 am at the Atrium of the Central Bank of Sri Lanka.

The release of the next regular statement on monetary policy will be on 27 December 2019.

Data Annexure:

Table 01: Inflation

Month		Dec 18	Mar 19	Jun 19	Jul 19	Aug 19	Sep 19	Oct 19
Headline Inflation (Year on year % change)	CCPI (2013=100)	2.8	4.3	3.8	3.3	3.4	5.0	5.4
	NCPI (2013=100)	0.4	2.9	2.1	2.2	3.4	5.0	5.6
Core Inflation (Year on year % change)	CCPI (2013=100)	3.1	5.6	5.8	5.7	5.6	5.6	5.5
	NCPI (2013=100)	3.1	5.8	6.1	6.1	5.9	5.6	5.6

Source: Department of Census and Statistics

Table 02: Monetary Sector Developments (Provisional)

Indicator	Outstanding Amount (Rs. billion)					Year - on - Year % Change				
	Jun 19	Jul 19	Aug 19	Sep 19	Oct 19	Jun 19	Jul 19	Aug 19	Sep 19	Oct 19
Reserve Money	875	888	913	915	908	(12.4)	(11.3)	(9.1)	(9.5)	(9.0)
Broad Money (M _{2b})	7,338	7,355	7,397	7,443	7,456	8.7	8.2	7.7	7.4	6.7
Net Foreign Assets (NFA)	99	105	102	113	102	(2.2)	(39.0)	(39.0)	1,374.4	698.7
Net Domestic Assets (NDA)	7,239	7,251	7,295	7,331	7,355	8.9	9.5	8.9	5.8	5.0
Net Credit to the Government (NCG) ^(a)	2,668	2,704	2,752	2,732	2,729	17.3	21.4	21.1	12.5	12.6
Credit to Public Corporations	730	729	747	755	789	17.9	14.6	16.8	15.1	12.5
Credit to the Private Sector	5,605	5,604	5,626	5,680	5,706	8.7	7.7	7.2	6.1	5.1
Broad Money (M ₄)	9,051	9,082	9,133	9,211	9,244	9.2	9.0	8.7	8.3	8.1

(a) Revised

Source: Central Bank of Sri Lanka

Table 03: Interest Rates

Interest Rate (%)	End Mar 19	End Jun 19	End Jul 19	End Aug 19	End Sep 19	End Oct 19	As at 28 Nov 19
Policy Rates of the Central Bank							
Standing Deposit Facility Rate	8.00	7.50	7.50	7.00	7.00	7.00	7.00
Standing Lending Facility Rate	9.00	8.50	8.50	8.00	8.00	8.00	8.00
Average Weighted Call Money Rate (AWCMR)	8.51	7.86	7.70	7.43	7.45	7.45	7.39
Treasury bill yields (Primary market)							
91-day	9.39	8.24	7.85	7.63	7.62	7.49	7.45
182-day	9.67	8.49	7.94	7.70	7.75	7.65	7.67
364-day	10.40	8.70	8.21	8.22	8.41	8.35	8.29
Lending Rates							
Average Weighted Prime Lending Rate (Weekly)	12.23	11.52	10.89	10.66	10.49	10.44	10.20
Average Weighted Lending Rate (AWLR)	14.49	14.36	14.22	14.04	13.91	13.71	-
Average Weighted New Lending Rate (AWNLR)	14.64	14.43	13.91	13.84	13.50	13.19	-
Deposit Rates							
Average Weighted Deposit Rate (AWDR)	8.98	8.94	8.88	8.73	8.51	8.37	8.27
Average Weighted Fixed Deposit Rate (AWFDR)	11.11	11.07	10.97	10.74	10.46	10.27	10.14
Average Weighted New Deposit Rate (AWNDR)	11.42	9.85	8.58	8.40	8.41	8.66	-

Source: Central Bank of Sri Lanka