Chapter 2

REVIEW OF CENTRAL BANK POLICIES

Summary

The Central Bank's mandate of achieving and maintaining domestic price stability and securing financial stability is reinforced by the Central Bank of Sri Lanka Act No. 16 of 2023 (CBA) that came into effect in September 2023. CBA stipulates price stability as the prime objective of the Central Bank and financial stability as the other objective. It recognises Flexible Inflation Targeting (FIT) as the monetary policy framework supported by a flexible exchange rate regime. Moreover, the Central Bank has been designated as the macroprudential authority. CBA was enacted amidst a myriad of economic challenges that emerged with the severe economic crisis in the country in 2022. The crisis response and prudent policy measures implemented by the Central Bank and the Government, supported by the IMF-EFF programme, helped restore macroeconomic stability to a great extent in 2023. On the monetary front, in view of benevolent inflation developments and improvements in the external sector, there was a shift from a tight monetary policy stance to an accommodative stance since June 2023. The imposition of interest rate caps on selected lending products, effective monetary policy communication amidst uncertainty, and measures taken to improve liquidity conditions in the market resulted in accelerated monetary policy transmission and a notable downward adjustment in market interest rates by end 2023. Showing signs of spillover of easing monetary conditions to the real economy, a reversal of the trend of private sector credit contraction was observed since June 2023. On the external front, the Central Bank, having discontinued the daily guidance given to the market since mid-2022, allowed greater flexibility in the determination of the exchange rate in March 2023. In line with improved foreign exchange liquidity in the market, the exchange rate was allowed to be determined by market forces thereafter. Intervention by the Central Bank in the domestic foreign exchange market was only aimed at preventing any unwarranted excessive volatility and accumulating Gross Official Reserves (GOR). Reflecting the improved external sector position and the return of confidence, the Sri Lanka rupee appreciated, while GOR improved notably. In the meantime, the majority of the administrative controls that the Central Bank and the Government had put in place during the foreign exchange crunch were progressively loosened in 2023. In the financial sector, prudential regulatory measures and crisis-preparedness of the Central Bank enabled financial institutions to weather the impact of economic turmoil, thus safeguarding domestic financial system stability. During 2023, an Asset Quality Review (AQR) was completed for nine key banks to identify structural weaknesses in

the banking sector and build resilience. Meanwhile, frameworks and methodologies are being prepared along with strengthening interorganisational coordination for the Central Bank to effectively play the role of the macroprudential authority of the country. Complying with the requirements under CBA, the promotion of financial inclusion in Sri Lanka emerged as a policy priority of the Central Bank pertaining to regional development. Further, the Central Bank forged ahead with promoting digital payments and e-money services, while actively facilitating cross border transactions. Regulations enabling the Central Bank to start market conduct monitoring were released in order to guarantee effective financial consumer protection. Meanwhile, the Sri Lanka Deposit Insurance Scheme was strengthened through a financing mechanism offered by the World Bank, while backstop funding arrangements were established with the Ministry of Finance.

2.1 Monetary Policy Framework

The Central Bank's mandate of maintaining domestic price stability is reinforced by the newly enacted Central Bank of Sri Lanka Act, No. 16 of 2023 (CBA) in September 2023. CBA stipulates achieving and maintaining domestic price stability as the primary objective of the Central Bank. CBA formally recognises Flexible Inflation Targeting (FIT) as the monetary policy framework and requires the signing of a monetary policy framework agreement by the Minister of Finance and the Central Bank, setting out the inflation target to be achieved. Although the Central Bank gradually moved towards FIT as its monetary policy framework over time, the legislative enactments required to formally adopt FIT as the monetary policy framework came into effect only with the enactment of CBA. Accordingly, the Central Bank entered into an agreement with the Minister of Finance in October 2023 to maintain headline inflation at a target of 5 per cent.[1] The target for inflation is to be reviewed every three years, or before that if exceptional circumstances warrant it. CBA includes provisions for enhanced transparency and public accountability by the Central Bank. Accordingly, if the Central Bank fails to meet the inflation target,[2] the Monetary Policy Board of the Central Bank shall submit a report to the Parliament, which shall also be made available to the public. The report will set out the reasons for the failure to achieve the inflation target, the remedial actions proposed to be taken by the Central Bank, and an estimate of the time period within which the inflation target shall be achieved. Meanwhile, CBA allows increased operational and financial independence to the Central Bank, thereby strengthening policies targeted at fulfilling its mandate effectively. Accordingly, monetary financing of the budget deficit is prohibited with the exception of circumstances specified by the CBA. Limits were also introduced on provisional advances to finance government expenditure. The provisions in CBA would help ensure that inflation in Sri Lanka would be maintained at low and stable levels in the period ahead, while ensuring that inflation expectations remain well anchored, thereby benefiting all stakeholders of the economy. Meanwhile, CBA provides for the coordination of fiscal, monetary, and financial stability policies through the establishment of the Coordination Council, where the Governor of the Central Bank, who also acts as the Chairperson, and the Secretaries to the Treasury and the Ministry of the Minister assigned the subject of Economic Policy[3] serve as members.

1 Communicated to the public under the Extraordinary Gazette Notification No. 2352/20 dated October 5, 2023.

2 If quarterly average (year-on-year) headline inflation (CCPI-based) misses the target rate by a margin of ±2 percentage points for two consecutive quarters.

3 In the event that such subject is assigned to a Minister other than the Minister of Finance.

The Coordination Council meets quarterly to exchange views on recent macroeconomic developments, outlook, and risks.

2.2 Monetary Policy Stance and Measures

The Central Bank's monetary policy stance in 2023 saw a gradual transition from the significant tightening of monetary policy in 2022 to an accommodative stance in the latter half of 2023. The notable moderation of inflation and well anchored inflation expectations, subpar economic activity amidst subdued domestic demand conditions, and the easing of external sector pressures paved the way for the Central Bank to pursue a relaxed monetary policy stance during the year. As inflation peaked in September 2022, in line with the anticipated disinflation trajectory, the Central Bank initiated moral suasion to reduce interest rates from their peak levels in late 2022. Despite the gradual moderation of excessive market interest rates from late 2022, the Central Bank was compelled to raise policy interest rates, i.e., the Standing Deposit Facility Rate (SDFR) and the Standing Lending Facility Rate (SLFR) by 100 basis points in early March 2023 to fulfil the 'prior action' that was required to be met to finalise the International Monetary Fund - Extended Fund Facility (IMF-EFF) arrangement. However, the magnitude of this increase was notably below the level of adjustment envisioned in the initial round of negotiations. Despite this increase in policy interest rates, active communication by the Central Bank alleviated the impact of such increase on market interest rates. Upon observing signs of a sustained moderation of inflation, the Central Bank commenced easing monetary policy in early June 2023, and policy interest rates were reduced by a total of 650 basis points over four occasions during the year. Considering the somewhat sluggish downward adjustment in overall market lending interest rates, caps on interest rates of selected lending products were imposed by the Central Bank in late August 2023, forcing a reduction in excessive interest rates of those products in line with the accommodative monetary policy stance. In order to induce a downward adjustment in overall market interest rates on rupee loans and advances, broader guidelines were issued for banks requiring lending interest rates to be reduced by at least 350 basis points by end 2023 compared to the levels that prevailed at end July 2023. These measures were reinforced in frequent dialogue with the banking sector to ensure that overall market lending interest rates declined to levels consistent with the policy interest rates. In March 2024, measures were taken to loosen monetary policy further by way of reducing the policy interest rates by 50 basis points, which is expected to support credit growth and revival of economic activity through the expected further reduction in market lending interest rates in the backdrop of low inflation.

Measures were taken to improve liquidity conditions in the domestic money market in 2023. Overall liquidity in the domestic money market remained largely at deficit levels during the period leading up to August 2023, which is expected to have hindered the effective transmission of monetary policy easing measures to market interest rates. Accordingly, in line with the easing of the monetary policy stance, the Central Bank implemented several policy measures to address the persistent liquidity deficit in the domestic money market. Consequently, the Statutory Reserve Ratio (SRR) applicable to licensed commercial banks (LCBs) was reduced to 2.00 per cent from 4.00 per cent with effect from 16 August 2023, which released around Rs. 200 billion of liquidity to the domestic money market. Further, the Central Bank provided special liquidity assistance facilities with a view to improving the liquidity positions of stressed licensed banks. Furthermore, as a precaution, the Central Bank strengthened its Emergency Liquidity Assistance (ELA) Framework enabling it to provide funds to licensed banks in the event of any imminent financial panic. The Central Bank also conducted active open market operations (OMOs) injecting liquidity on a term basis through term reverse repo auctions as needed in addition to the overnight reverse repo auctions. Moreover, with a view to injecting liquidity on a permanent basis, auctions for outright purchase of Treasury bonds were conducted in 2023, which followed into the first few weeks of 2024.

Measures were also taken to reactivate the money markets by reducing LCBs' overreliance on the overnight funding facilities of the Central Bank. With effect from 16 January 2023, restrictions were imposed on the accessibility of the standing facilities to LCBs. Accordingly, the usage of the Standing Deposit Facility (SDF) was limited to a maximum of five (05) times per calendar month, while the Standing Lending Facility (SLF) was limited to 90 per cent of SRR of each LCB on any given day. These restrictions prompted licensed banks to explore alternative options for liquidity management. As a result, a reactivation in domestic money market activity was observed, while LCBs reduced their reliance on Central Bank facilities. In view of the improvements observed in the money markets, steps were taken to ease restrictions on the usage of the standing facilities gradually, where the restriction on SLF was removed, while the restriction on SDF was initially relaxed to ten (10) times during a calendar month with effect from the reserve maintenance period from mid-February 2024 and a policy decision was taken to remove it completely with effect from April 2024.

Supported by the aforesaid monetary policy measures and operations, market interest rates eased, and overall credit conditions improved in 2023. The Average Weighted Call Money Rate (AWCMR), which is the short term interest rate closely monitored by the Central Bank as the operating target to guide the market interest rates under the FIT framework, declined towards the lower bound of the Standing Rate Corridor (SRC) during 2023. With these developments and the finalisation of the Domestic Debt Optimisation (DDO) operation and the associated decline in risk premia, yields on government securities declined significantly during the year paving the way for the notable reduction in overall market interest rates. As a result, the interest rate structure of the economy normalised with retail market lending rates reducing to levels supporting some expansion of credit to the private sector. Accordingly, credit to the private sector, which suffered continued contractions since mid-2022, marked a turnaround from June 2023, recording an expansion of credit on a monthly basis until the end of the year supporting the recovery of domestic economic activity. Despite the recovery, credit to the private sector recorded a contraction of 0.6 per cent, year-on-year, by end 2023, as credit declined significantly during the period from January to May 2023. Meanwhile, credit granted by the banking system to the public sector comprising the Government and State Owned Business Enterprises (SOBEs) also witnessed a contraction in 2023. The Central Bank's policy on monetary financing underwent a complete overhaul with the enactment of CBA. Despite the transitional provisions allowing for monetary financing to continue for 18 months from the enactment of CBA, the Central Bank phased out the outstanding Net Credit to the Government (NCG) by reducing its holdings of government securities, which is also in line with the IMF-EFF arrangement. With the gradual unwinding of the Central Bank's holdings of government securities and the reduction in funds obtained by LCBs and Primary Dealers (PDs) from the SLF owing to improvements in domestic money market liquidity and restrictions on the usage of SLF, NCG by the Central Bank contracted in 2023. At the same time, to build up the Gross Official Reserves (GOR), the Central Bank's purchases of foreign exchange from the domestic foreign exchange market contributed to enhancing the Net Foreign Assets (NFA) of the Central Bank.

The monetary policy communication strategy of the Central Bank during 2023 was focused on the continuation of the disinflation process, reduction of market interest rates in line with the reduced risk premia following the DDO operation and effecting a faster transmission of the accommodative monetary policy stance during the second half of the year. During the first half of 2023, the Central Bank's communication strategy focused on ensuring the continuation of the disinflation process by anchoring inflation expectations and persuading financial institutions to reduce the large spread between market interest rates and policy interest rates, which was caused by the substantial premium that persisted on yields on government securities amidst the uncertainties associated with the DDO operation. During the second half of the year, the Central Bank's communication was focused on expediting the transmission of accommodative monetary policy for the benefit of the masses. A mix of conventional channels and social media was used by the Central Bank to enhance monetary policy communication during the year. Monetary policy announcements were communicated via press releases in all three languages, and they were complemented by press conferences chaired by the Governor of the Central Bank. These press conferences were livestreamed via social media, and important messages were made available on the Central Bank's social media channels as short video snippets. The practice of publishing the inflation fan chart in the press releases on monetary policy and inflation was continued throughout the year, in order to guide the stakeholders of the economy about the anticipated developments of inflation, thereby helping the anchoring of medium term inflation expectations. This approach marked an important development in the monetary policy communication strategy of the Central Bank, consistent with the FIT framework, where forward-looking information plays a major role. Meanwhile, the Governor and senior officials of the Central Bank participated in various events and programmes to raise awareness on monetary policy. Simultaneously, regular publications of the Central Bank, including the Annual Report, were completed in a timely manner. The publication of the first Monetary Policy Report (MPR) of the Central Bank in July 2023 marked an important step in the monetary policy communication strategy of the Central Bank. The main aim of this publication is to communicate the rationale for the monetary policy decisions taken during the relevant period, thereby contributing to enhancing the accountability of monetary policymaking of the Central Bank. In addition, MPR serves a key purpose in the FIT framework by providing an important means of communicating anticipated developments of key macroeconomic variables, thereby helping the stakeholders of the economy to make informed economic decisions, incorporating forward-looking information. As per the statutory requirement in CBA, the Central Bank is required to publish the MPR bi-annually, and accordingly, the first MPR as a statutory publication was published in February 2024. Along with the publication of this MPR, short non-technical video clips highlighting the key messages of the publication were made available via the Central Bank's social media channels with the aim of improving the reach of the content of the Report to a wider audience. In addition, the releases of the two MPRs were also complemented by separate technical awareness sessions for journalists, and the academia and professionals. Effective monetary policy communication helps in anchoring inflation expectations, enhancing policy transmission, and reducing uncertainty, all of which are essential for achieving the Central Bank's prime objective of maintaining domestic price stability. Moreover, clear communication enhances the credibility and effectiveness of monetary policy, contributing to economic stability and resilience. Accordingly, among other factors, the efforts of the Central Bank during 2023 to enhance the effectiveness of monetary policy communication contributed to the disinflation process, reduction in risk premia in market interest rates, and faster transmission of the accommodative monetary policy stance to the financial sector and the real economy.

2.3 External Sector Policies

2.3.1 Exchange Rate Policy

Sri Lanka followed a flexible exchange rate regime during most of 2023. The Central Bank allowed greater flexibility in the determination of exchange rate with effect from 07 March 2023 by discontinuing the daily guidance given to the market since May 2022, considering the improvement in the liquidity in the domestic foreign exchange market. Accordingly, the exchange rate was allowed to be determined based on the demand and supply conditions in the domestic foreign exchange market only with limited interventions by the Central Bank aimed at preventing any excessive volatility in the exchange rate and accumulating GOR through purchases of foreign exchange from the market. Previously, during 2021 and in early 2022, the Sri Lanka rupee was maintained at stable levels before being allowed a measured adjustment in the exchange rate in early March 2022. However, the outcome of this adjustment fell short of expectations due to the large overshooting of the exchange rate. Accordingly, the Sri Lanka rupee depreciated significantly by end April 2022. Due to this instability, the Central Bank commenced providing daily market guidance to the interbank foreign exchange market from 13 May 2022 onwards that helped stabilise the exchange rate from significant intraday volatility. This was implemented by publishing a middle spot exchange rate and a variation margin on either side (+/-) of the middle spot exchange rate on a daily basis. The margin varied in a range of Rs. 1.00 – Rs. 10.00 and was set either symmetrically or asymmetrically on the middle spot exchange rate from time to time. With these measures, greater stability of the exchange rate was observed during the period reflecting the effectiveness of this policy. With a view to encouraging activity in the domestic foreign exchange market and restoring a market-driven exchange rate in line with its FIT framework, the Central Bank commenced a gradual relaxation of the daily variation band, while loosening the mandatory sales requirement. By early March 2023, the daily guidance given to the market was discontinued while the policies relating to forex conversions implemented in 2022, such as the mandatory requirement imposed on licensed banks (to sell foreign exchange to the Central Bank on a weekly basis) on account of converted inward workers' remittances and service sector related export receipts and the residual value of converted export proceeds of goods, were revoked in March 2023. Accordingly, the liquidity conditions and sentiments in the domestic foreign exchange market improved notably. Moreover, operating instructions issued in 2020 to licensed commercial banks on the Inward Investments Swaps (IIS) Scheme were also revoked in 2023. The above measures helped improve foreign exchange liquidity conditions as well as market sentiments leading to appreciation of the Sri Lanka rupee in 2023.

The enactment of CBA reiterated the importance of a flexible exchange rate regime to complement the FIT framework. According to CBA, the Central Bank is charged with the implementation of a flexible exchange rate regime in line with the FIT framework in order to achieve and maintain domestic price stability. A flexible exchange rate regime is also expected to foster a deeper and more liquid foreign exchange market. With the adoption of the flexible exchange rate policy mandated by CBA, the anti-export bias that prevailed in the past through an overvalued currency would be eliminated in the future and the exchange rate would move in line with the demand for and supply of foreign exchange in the domestic foreign exchange market. With the adoption of the flexible exchange rate policy, the market confidence improved notably, resulting in significant net inflows to the domestic foreign exchange market. Consequently, the exchange rate appreciated against the US dollar by 12.1 per cent in 2023 and by 7.6 per cent by end March 2024 in line with market fundamentals. These developments enabled the Central Bank to purchase, on a net basis (based on value date), US dollars 1.7 billion in 2023 and around US dollars 1.1 billion during the first quarter of 2024. Further, this policy will safeguard the country from the extreme impacts of external shocks to Sri Lanka, since the exchange rate will be allowed to adjust in response to shocks, thus external sector stability will be restored eventually through the Balance of Payments (BOP) adjustments.

2.3.2 Exchange Restrictions and Capital Flow Management Measures (CFMs)

Most administrative measures introduced at the time of the foreign exchange crunch were gradually relaxed in 2023. During the time preceding and during the economic crisis in 2021 and 2022, the Government, in consultation with the Central Bank, imposed a number of exchange restrictions and capital flow management measures to overcome the severe shortage of foreign exchange in the domestic foreign exchange market. In addition, the Central Bank itself implemented several measures to limit foreign exchange outflows from the country, while encouraging more inflows. Most of such exchange restrictions and other limitations were eliminated in 2023 in line with the gradual improvement in the liquidity conditions in the domestic foreign exchange market and in view of improving the external sector outlook on multiple fronts. In May 2023, the unremunerated cash margin deposit requirement imposed a year earlier on imports of certain items on payment terms of Letters of Credit (LC), Documents against Payment (DP), and Documents against Acceptance (DA) were removed. Other such restrictions that were withdrawn include the rationing of foreign exchange by the Central Bank and the Central Bank's informal guidance to authorised dealers to prioritise access to foreign exchange for the imports of essential items. The Minister of Finance and the Central Bank issued necessary regulations and directions under the provisions of the Foreign Exchange Act (FEA) No. 12 of 2017 for the purpose of removing certain restrictions on the conversion of Sri Lanka rupees into foreign exchange for certain current international transactions and for removing certain limits on the repatriation of proceeds derived from current transactions by emigrants. The previous regulations that were in place under the repealed Exchange Control Act No. 24 of 1953 on mandatory requirement to repatriate goods export proceeds were reissued, under FEA in October 2019. In February 2021, the mandatory conversion requirement on such repatriated export proceeds was introduced. In addition to goods exports, proceeds of services exports were also included in the requirement of repatriation and mandatory conversion of export proceeds in October 2021. However, the conversion requirement in relation to services export proceeds was removed in August 2022.

Certain suspensions and limitations on capital transactions imposed as CFMs were also relaxed during 2023. During the crisis period, several CFMs were rolled out by the Government and the Central Bank to discourage the outflows of foreign exchange in order to support BOP conditions in the country. Once BOP conditions started to improve, some of the previously imposed CFMs were gradually relaxed. Accordingly, the temporary suspension of payments made through Outward Investment Accounts (OIAs) for the purpose of making overseas investments by persons resident in Sri Lanka was relaxed up to a certain level. However, limitations on making payments through OIAs for selected capital transactions continue to remain. In addition, limitations on outward remittances for capital transactions made via Business Foreign Currency Accounts (BFCAs) held by persons resident in Sri Lanka were also further relaxed. However, temporary restrictions imposed on outward remittances for capital transactions made via Personal Foreign Currency Accounts (PFCAs) held by persons resident in Sri Lanka continue. In addition, limitations on the transfer of funds outside Sri Lanka by emigrants under the migration allowance were further relaxed. The Government and the Central Bank have formulated a plan for the phased removal of remaining CFMs, subject to reaching some milestones in the external sector conditions.

In addition, the Central Bank introduced further policy measures during the year considering current and expected developments in the domestic foreign exchange market. As a measure for encouraging foreign exchange inflows into the country, authorised dealers were permitted to open and maintain Special Foreign Currency Accounts (SFCA) – Investee, for companies in Sri Lanka, out of the proceeds received as equity. Directions were also issued in relation to the BFCAs and accommodations to BFCAs, broadening certain foreign currency transactions between the entities engaged in the business of marine fuel (bunker), transport and logistics. Moreover, the automated export proceeds monitoring system which was implemented in June 2022 was further improved during the year to give access for selected exporters to reconcile their exports with remittances as an avenue to strengthening the monitoring of the repatriation of export proceeds to the country. In addition, measures such as (i) unremunerated cash margin deposit requirement on imports of certain items made under payments terms of LC, DA and DP payment terms; (ii) the use of the weekly volume weighted average rate for Central Bank's foreign exchange sales in bilateral non-request for quote outright spot transactions with authorised dealers; (iii) providing an incentive for inward workers' remittances such as the reimbursement of transaction cost of workers' remittances that result in a more favourable effective exchange rate for such transactions, which were identified by the IMF as multiple currency practices, were eliminated in 2023.

2.3.3 Relaxation of Import Restrictions

The Government removed import restrictions in 2023, on the broad recommendation from the Central Bank to effect relaxation on a priority basis, apart from restrictions on vehicle imports. The Central Bank recommended to the Ministry of Finance in May 2023 to relax the restrictions on imports of temporarily suspended items, except personal motor vehicles after careful consideration of the improvements observed in the domestic foreign exchange market and the gradual buildup of GOR, while also considering the dampening impact of continued import restrictions on economic activity. Accordingly, restrictions on imports of temporarily suspended items were removed in three stages in June, July, and October 2023, keeping only motor vehicles under temporary suspension. The restrictions on imports under certain payment terms that were imposed in May 2022, mainly on open account terms, were continued throughout 2023. However, the requirement to obtain prior approval from LCBs for imports under DA and DP terms was removed by the end of February 2024. These relaxations, together with the easing of import restrictions by the Government from mid-2023, resulted in a gradual increase in imports that supported the revival of economic activities and a reduction in price levels of import items.

The above policy measures adopted in 2023 helped the external sector achieve greater stability during the year. These market-driven policy measures encouraged more foreign exchange inflows to the country and as a result, the liquidity conditions and market sentiments in the domestic foreign exchange market improved notably, leading to a sharp appreciation of the Sri Lanka rupee. These conditions enabled the Central Bank to buildup international reserves substantially during the year by purchasing forex from the domestic market.

2.4 Financial Sector Policy Measures

2.4.1 Designation of the Macroprudential Authority

CBA designates the Central Bank as the Macroprudential Authority in Sri Lanka. The Act empowers the Central Bank with a mandate to exercise, perform and discharge powers, duties, and functions in pursuing the macroprudential objectives to achieve financial stability. Three intermediate macroprudential objectives are articulated in the Act as maintaining the resilience of the financial system in a manner that supports the provision of financial services even under adverse economic and financial conditions; containing risks from unsustainable increases in credit and leverage; containing risks from interconnectedness within the financial system and control the risk of failure of individual systemically important institutions. The Central Bank, as the macroprudential authority, is vested with powers, amongst other things, to monitor, identify or assess the buildup of risks and vulnerabilities in the financial system; request, collect, compile, analyse or publish data, information and statistics in order to achieve the macroprudential objectives; conduct stress testing and simulation exercises; designate systemically important financial sector participants; adopt and apply the macroprudential instruments to financial institutions regulated and supervised by the Central Bank; formulate strategies and policies to mitigate or address identified systemic risks; identify gaps in regulation that could pose systemic risks. Furthermore, the Act outlines provisions for the establishment of the Financial System Oversight Committee (FSOC) to contribute to securing the stability of the financial system in line with the macroprudential policy by bringing aspects of the sector that are not under the direct supervision or regulation of the Central Bank and ensuring a coordinated approach in policy recommendations. In addition to the suite of quantitative and qualitative macroprudential instruments identified by CBA, novel instruments and measures may be adopted as necessary to safeguard the resilience of the financial system.

During 2023, the Central Bank continued to develop its macroprudential instruments to be implemented as part of broad policy actions to mitigate or eliminate systemic risks. Accordingly, the Central Bank has developed methodologies and frameworks to introduce a Debt-Service-to-Income (DSTI) ratio for the household sector; caps on Loan to Value (LTV) for credit facilities for housing purposes and the Counter Cyclical Capital Buffer (CCyB). The DSTI and LTV, which are borrower based macroprudential instruments, are envisaged to curb excessive credit demand and to mitigate the buildup of systemic risks while curtailing potential credit losses of banks and minimising the risks associated with excessive indebtedness. The CCyB aims to address the procyclicality in the financial system, thereby shielding the banking sector from excessive credit growth during the upswings in the cycle and facilitating the supply of credit to the economy during a downturn. The Central Bank will vigilantly monitor macrofinancial developments to implement macroprudential instruments designed and calibrated in 2023 when required to address systemic imbalance to enhance the resilience of the financial system.

2.4.2 Policies Related to Licensed Banks

During 2023, the Central Bank continued to introduce policy measures and regulations to strengthen financial and operational resilience, thereby ensuring the safety and soundness of the banking sector. Banking Act Directions on Restrictions on discretionary payments of Licensed Banks were introduced to mitigate the possible adverse impact on liquidity and capital position of Licensed Banks stemming from macroeconomic conditions that prevailed at the time, while seeking to ensure the maintenance of appropriate levels of liquidity and capital. As per these directions, Licensed Banks were required to defer payments of cash dividends and profit repatriation for 2023 until the completion of the external audit of financial statements/interim financial statements for 2023. Further, Licensed Banks were also required to refrain from engaging in share buybacks, increasing management allowances, and payments to Boards of Directors (BOD), and incurring non-essential and/or non-urgent expenditure, while exercising extreme due diligence and prudence when incurring capital expenditure until end 2023. Licensed Banks were further required to form a Board-Level Sub Committee, to operate during the year and in 2024, to evaluate and approve non-essential, non-urgent and/or capital expenditure to be incurred by the bank. Amendments were subsequently made requiring Licensed Banks to refrain from increasing management allowances of Chief Executive Officers (CEO), Key Management Personnel (KMP), and payments to BODs, unless the increase is recommended by the Human Resource and Remuneration Committee and approved by BOD, subject to the considerations stipulated therein.

Several microprudential measures were also targeted at addressing issues pertaining to the liquidity conditions of banks. To proactively address probable liquidity constraints and their impact on the stability of individual banks and the overall financial sector, a Banking Act Determination was issued determining qualifying non-financial corporate debt securities and qualifying non-financial common equity shares, as defined in the Banking Act Directions on the Liquidity Coverage Ratio under Basel III liquidity standards, to be treated as liquid assets in the computation of the Statutory Liquid Asset Ratio of Licensed Banks.

Amendments were made to the Banking Act Direction on 'Regulatory Framework on Technology Risk Management and Resilience for Licensed Banks' during the year with the aim of enhancing the information security and resilience requirements for critical information systems while establishing a higher risk management measure for the banking sector. The amendments were pertinent to the identification of critical information systems, requirements related to the recognition of third party service providers, frequency of user access privilege reviews, criteria for determining ownership, and management of information system infrastructure. Further, with a view to encouraging Micro, Small and Medium Enterprises (MSMEs) and individuals with the potential to revive their businesses or income streams to commence repayment of loans, while preventing any elevated strain on the financial sector, licensed banks were requested to provide appropriate concessions on a case-by-case basis through their branch network to the affected borrowers due to extraordinary macroeconomic conditions that prevailed during the year.

2.4.3 Policies related to Licensed Finance Companies (LFCs) and Specialised Leasing Companies (SLCs)

A guideline on the declaration of dividend/ repatriation of profits was issued during the year to streamline the existing approval process of LFCs when declaring dividends considering the profitability, capital adequacy and shareholder returns. It is envisaged to strengthen the resilience and capacity of LFCs to absorb economic shocks that could arise during times of uncertainty, while ensuring their ability to facilitate the credit needs of customers.

The LFCs and SLCs sector was requested to grant concessionary measures with the view of safeguarding MSMEs and individuals amid the challenging macroeconomic conditions that were prevalent in recent years. These measures were focused on facilitating the recovery of MSMEs and individuals who possessed the potential to revive their business or income streams and thereby would be able to commence repayment of loans. Such concessions extended by the LFCs and SLCs encompassed restructuring and rescheduling of credit facilities of performing and non-performing borrowers, suspension of recovery actions against non-performing credit facilities on a case-by-case basis and encouraging early settlement of existing performing or rescheduled credit facilities by applying reduced rates for early settlement charges and recovery of future interest.

The Masterplan for the Consolidation of Non-Bank Financial Institutions, which was unveiled in 2020, will continue to create strong, dynamic, and resilient LFCs over the medium term, thereby safeguarding the interest of depositors and preserving financial system stability. Further, LFCs that are unable to comply with the directions and rules issued under the Finance Business Act No. 42 of 2011 and adhere to the Masterplan will be directed to exit from the market upon cancellation of their licences.

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Regulatory and resolution actions were initiated during the year in an expeditious manner, on companies, which were non-compliant with prudential directions and whose licences had been cancelled or suspended. These early interventions during the year mitigated the likelihood of financial distress or failure and helped curb any undue burdens on the deposit insurance fund. The regulatory actions implemented in this regard included the imposition of restrictions on non-compliant LFCs regarding deposits and borrowings, extension of the business suspension of a primary dealer, and appointment of liquidators in accordance with the orders given by the Commercial High Court for four failed LFCs, whose licences have been cancelled or suspended.

2.4.4 Public Debt Management Policies

The Ministry of Finance, Economic Stabilization and National Policies announced its policy on Sri Lanka's Domestic Debt Optimisation (DDO) operation on 04 July 2023. The DDO operation is a key initiative in efforts to restore Sri Lanka's public debt sustainability under the IMF-EFF arrangement. Accordingly, eligible Treasury bonds held by eligible holders, Treasury bills held by the Central Bank, Provisional Advances made by the Central Bank to the Government of Sri Lanka, Sri Lanka Development Bonds (SLDBs), excluding those held by individual investors and foreign currency denominated bank loans of the Government

Table 2.1 Summary of the Domestic Debt Optimisation (DDO) Operation

Item	Execution Date	Volume Optimised (Rs. Billion)
SLDBs	15 August 2023	252
Treasury bonds	14 September 2023	3,204
Treasury bills held by the Central Bank and Provisional Advances provided by the Central Bank to the Government	21 September 2023	2,713

Source: Central Bank of Sri Lanka

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issued under the local law were converted or exchanged into longer term Treasury bonds, as applicable. The DDO operation was executed in several phases. All outstanding SLDBs were either converted or settled in full by the end of November 2023. The restructuring of remaining foreign currency denominated bank loans issued under local law is currently underway. The execution of the DDO operation helped create much needed fiscal space for the Government in the short to medium term. The recent local currency credit rating assessments by international credit rating agencies also acknowledged these developments in their forward looking opinion about Sri Lanka's creditworthiness on local currency obligations, following the completion of the DDO. In the meantime, the Central Bank continued to support the Government and the appointed financial and legal advisors on the external debt restructuring process.

2.4.5 Policies for Financial Inclusion

Following the enactment of CBA, the promotion of financial inclusion in Sri Lanka, in line with the need for a more inclusive and sustainable financial system has emerged as a policy priority of the Central Bank pertaining to regional development. The National Financial Inclusion Strategy (NFIS) Action Plan is successfully in operation in collaboration with stakeholders. Phase I of NFIS, which commenced in 2021, is expected to be concluded in 2024. Meanwhile, the Financial Literacy Roadmap for Sri Lanka will soon be launched to nurture the creation of a financially literate community.

The Central Bank envisages to continue existing MSME loan schemes, which were implemented on behalf of the Government and donor agencies, until the conclusion of such loans despite its policy decision to phase out new loan schemes, following the enactment of CBA. The operational periods of several loan schemes were extended during the year considering the funding needs of the youth segment of the market and smallholder agribusinesses. Operating Instructions were amended to expand the scope of the definition of community based financial intermediaries aiming to extend the reach of loan schemes that were previously provided on behalf of the Government. Further, on behalf of the Government, a loan scheme was introduced for Sri Lankan migrant workers in 2023, in collaboration with the Sri Lanka Bureau of Foreign Employment, to encourage migrant workers to remit foreign exchange earnings to the country through formal channels.

2.4.6 Policies on Payments and Settlements

The Central Bank implemented various policy measures to promote digital payments, while ensuring the safety and stability of payment systems during the year. The Central Bank continued its efforts to promote and enhance digital payments, focusing on transactions made through the Instant Payment System, the Common Electronic Fund Transfer Switch (CEFTS). Accordingly, the Multi-tiered Liability Manager Limit structure applicable to CEFTS was revised to accommodate a larger volume of transactions.

The Central Bank directed Licensed Banks to integrate with the LankaPay Online Payment Platform (LPOPP) in 2024 to facilitate online payments to government institutions, enhancing efficiency and accessibility for the public. Additionally, the Central Bank instructed Licensed Banks to join the Government Digital

BOX 5

Financial Literacy Roadmap of Sri Lanka (2024-2028): Towards A Financially Literate Sri Lanka

1. Introduction

Financial literacy that encompasses the knowledge and skills required to make informed financial decisions, is integral to individual and societal economic well-being across the globe. The significance of financial literacy extends across various dimensions. It influences the economic outcomes of individuals by empowering them to navigate the complex world of financial services, make prudent investment choices, manage debts effectively, and plan for future financial stability (Lone & Bhat 2022). Beyond personal financial well-being, it plays a critical role in shaping the macroeconomic landscape by fostering informed consumer behaviour, enhancing the efficiency of financial markets, reducing systemic risks, promoting financial inclusion, and supporting sustainable economic growth (Lusardi & Mitchell 2013).

2. Global Advocacy and Experience in Improving Financial Literacy and its relevancy for Sri Lanka

The global advocacy for enhancing national financial literacy levels is a multifaceted endeavour, which signifies a collaboration of innovative strategies, professional alliances, and a commitment to sustainable development. International entities such as the Organisation for Economic Cooperation and Development (OECD), United Nations Development Programme (UNDP) World Bank, International Finance Corporation (IFC) and Alliance for Financial Inclusion (AFI) play pivotal roles in setting international standards and providing guidelines, resources, and support to countries aiming to enhance their financial education frameworks.

Overall, these entities emphasise the importance of tailored, targeted and inclusive financial literacy programmes that cater to the diverse needs of the general public, especially vulnerable groups (AFI 2021; OECD 2005). As a holistic tool, National Financial Literacy Strategies or Financial Literacy Roadmaps have been utilised globally by governments and policymakers to drive a positive change towards enhanced financial inclusion landscapes through improved financial literacy levels (World Bank 2014).

In the context of Sri Lanka, the advantages which could be obtained by the implementation of this kind of a national initiative are substantial and multifaceted. With the introduction of the Central Bank of Sri Lanka Act No.16 of 2023 (CBA), the Central Bank is vested with the statutory obligation to promote financial inclusion. Thus, on a broader footing, a national scale financial literacy initiative could be considered as the most appropriate tool to reach higher financial inclusion levels.

3. Current Financial Literacy Landscape of Sri Lanka

In order to identify the financial literacy landscape of Sri Lanka, in 2021, the Central Bank jointly with the IFC of the World Bank Group (WBG) conducted the first ever nationally representative Financial Literacy Survey in Sri Lanka under the Action Plan of the National Financial Inclusion Strategy (NFIS).

Results of the Financial Literacy Survey revealed that when compared to the other countries with comparable survey results, Financial Knowledge of Sri Lankans are at satisfactory levels. However, Financial Behaviour is lagging behind, demanding careful consideration of the policymakers. Translating financial knowledge into actual financial behaviour, is a multifaceted issue stemming from a range of reasons such as issues in financial attitudes, behavioural biases, lack of practical experience, socioeconomic barriers, and emotional factors. These elements collectively contribute and widen this gap, making it challenging for individuals to apply their understanding of financial principles in real-world scenarios effectively. Poor financial behavior intensifies the vulnerability of individuals to economic shocks, contributes to macroeconomic instability through reduced savings and higher debt, increases inequality, and also impacts public resources due to increased reliance on government assistance programmes.

Moreover, even though there is no gender gap observed in financial inclusion, a modest gender gap was observed in the financial literacy levels of Sri Lanka (CBSL 2021a; 2021b). Accordingly, gender sensitive approaches should be introduced to bridge the gender divide. Thus, introducing targeted behavioural interventions to support the translation of financial literacy, i.e., financial knowledge and skills, into positive financial behaviour of Sri Lankans should be considered a policy priority in the current context.

4. The Policy Framework: Financial Literacy Roadmap of Sri Lanka

Based on the findings of the Financial Literacy Survey 2021, the Central Bank in collaboration with over 40 stakeholders, including financial sector regulators, ministries, academia and other public and private sector institutions, led the development of the first ever Financial Literacy Roadmap of Sri Lanka (the Roadmap).

5. Operationalisation of the Financial Literacy Roadmap: Action Plan and Operational Pillars

The Roadmap consists of a 05-year Action Plan to be implemented from 2024 to 2028 with the fundamental objective of improving the financial behaviour of Sri Lankans. The Action Plan currently consists of 48 actions developed to reach 10 objectives across the 04 Strategic Priorities of the Roadmap.

These actions will be mainly focused on, inter alia, strengthening the coordination, standardising the financial literacy materials used by the stakeholders, supporting the transformation of the school children to financially capable individuals by the time they leave school in collaboration with national level public and private education partners, and utilising existing resources for the effective delivery of the financial literacy interventions. The NFIS Secretariat established in the Regional Development Department of the Central Bank supports to operationalize the Action Plan. The existing governance structure of the NFIS is to oversee and ensure effective implementation of the Roadmap.

Addressing the changing and dynamic financial literacy needs of the economy is of paramount importance for the successful implementation of such national level financial literacy initiatives. Thus, the Action Plan of the Roadmap would be a living and open document that could be updated to address such requirements, as necessary.

6. The Way Forward

Despite the remarkable policy commitment and the successful development of the Roadmap, the path ahead is fraught with challenges albeit promising opportunities awaiting to be optimised. The success of the Roadmap depends on several critical factors; aligning with national policies, adapting to the evolving financial landscapes and global trends, creating accessible and

Policy Framework of the Financial Literacy Roadmap of Sri Lanka (2024-2028)

Vision	"A Financially Literate Sri Lanka"
Mission	Empower all Sri Lankans towards greater financial inclusion with requisite financial knowledge, skills and confidence to make well-informed and responsible financial decisions to increase financial wellbeing of the people
Strategic Priorities	(i) Effective Coordination and Harmonised Content (ii) Increased Positive Financial Behaviour (iii) Vigilant and Protected Financial Consumers (iv) Generational Behaviour Change
Target Groups	(i) Youth and School Children (ii) Identified vulnerable groups (Women, Migrant Workers, etc.) (iii) MSMEs (iv) Professionals and Government Employees
Key Contents	(i) Economic and Financial Environment (ii) Digital Financial Literacy (iii) Financial Management (iv) Consumer Protection

inclusive financial literacy interventions, fostering partnerships, and establishing effective monitoring and evaluation frameworks, etc. These steps are crucial to maximise the impact and sustainability of financial literacy interventions, ultimately leading to a financially literate and empowered population. Moreover, leveraging existing resources such as current levels of financial knowledge and skills, widespread access to financial services, and increased digital penetration can catalyse the impact of the interventions.

Utilising the already established delivery channels and networks like the Community Health Network, Network of Women Development Officers, and Agrarian and Samurdhi Societies to deliver the financial literacy programmes under the Roadmap, will optimise the resource utilisation. Further, with the participation of over 40 national level stakeholders, the outreach of the Roadmap is expected to be significantly wide. In this regard, long-term commitment of the stakeholder institutions is required to ensure the effectiveness and the continuity of the Roadmap implementation. More importantly, the commitment of the multilateral development partners is used to obtain much needed technical and financial assistance, considering the unprecedented nature of this national endeavour.

Nonetheless, the implementation process is challenging, as harmonised efforts towards successful implementation are critical. As a national level programme, aligning the Roadmap with broader economic and social policies demand effective coordination among key stakeholders including the Government, financial institutions, and educators, to ensure the Roadmap is given high priority. Addressing the diverse needs of the audience, keeping pace with the rapid advancements of financial innovations and ensuring effective engagement of the target groups and their accessibility to the interventions can threaten the effective implementation.

In light of the above, it is evident that significant attention of all the stakeholders is needed for advancing the efforts put forward through the Financial Literacy Roadmap, since there is an unwavering promise for substantial economic and social advantages by effectively combating financial scams, reducing over indebtedness, alleviating poverty, and breaking poverty traps. It further encourages greater savings and investments on both individual levels and national scales, which in turn, encourage internal capital formation and facilitate economic growth.

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Payment Platform (GDPP), facilitated by LankaPay through LPOPP. This integration will enable government institutions, without existing internal IT systems, to accept digital payments from the public, particularly at the local government level.

In order to promote digital transactions in remote areas, the Central Bank implemented measures to enhance the use of e-money services for transactions and remittances. These measures entailed raising the maximum value permitted for basic and enhanced e-money accounts, aiming to promote greater financial inclusion and convenience for individuals in remote areas and fostering the adoption of digital payment methods. Further, the Central Bank decided to maintain the LANKAQR Merchant Discount Rate (MDR) at 0.5 per cent to encourage small and medium-sized merchants to accept digital payments at a minimal cost.

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To facilitate cross border retail payments, the Central Bank granted approval for LankaPay (Pvt) Ltd (LPPL), the national payment network operator, to integrate with payment networks in China and India considering their importance as source destinations of tourists visiting Sri Lanka. These integrations allow tourists from China and India to make payments to merchants who have LANKAQR codes in Sri Lanka. With the view of creating a level playing field to balance the higher interchange fee to be paid by Sri Lankan merchants to financial institutions in India and China, a maximum MDR per transaction amount has been decided for LANKAQR transactions initiated through such foreign payment apps.

The Central Bank implemented several measures to enhance the safety of digital payments, aiming to improve the overall quality of digital transactions and encourage greater adoption of digital payment methods. These measures include mandating real time notifications for credit and debit transactions, as well as ensuring immediate updates for credit card settlements made through digital channels. Additionally, Licensed Banks were instructed to make the reference field mandatory for digital transactions, and Licensed Financial Acquirers were advised to instruct their merchants not to pass the MDR to customers. The Central Bank mandated that mobile payment applications facilitating JustPay transactions request a One Time Password (OTP) from the issuer of the linked account if the transaction amount equals or exceeds Rs.10,000. JustPay enables users to link accounts at any financial institution to their mobile payment application and make payments by retrieving funds from these linked accounts.

2.4.7 Anti-Money Laundering and Countering Financing of Terrorism

During 2023, the Financial Intelligence Unit (FIU) in line with the recommendations of the Financial Actions Task Force (FATF), coordinated and concluded the National Risk Assessment (NRA) 2021/22 with the aim to identify, assess and better understand the Money Laundering (ML) and Terrorist Financing (TF) risks faced by the country. The NRA highlighted the most significant ML/TF threats, vulnerabilities, and risks faced by Sri Lanka. The NRA assessed the overall ML/TF risk for the country as 'Medium'. Based on the findings of the NRA, the National AML/CFT Policy for 2023-2028 was prepared and approved by the Cabinet of Ministers. Aiming at preparing the key stakeholders for the Mutual Evaluation of AML/CFT framework, which is scheduled to commence in March 2025, the Stakeholder-wise Action Plans for 24 relevant stakeholder institutions were also approved by the Cabinet of Ministers to improve the effectiveness and technical compliance level of AML/CFT framework of the country. The FIU conducted a series of follow-up meetings to discuss the progress of the Action Plans with the relevant stakeholders. A Task Force for AML/CFT was appointed by the Cabinet of Ministers to follow up on the progress of implementation of the said Action Plans and to ensure that identified gaps are addressed comprehensively, timely and effectively, while effectively coordinating among relevant stakeholders.

In addition to risk based supervision, the FIU continued to maintain its joint supervision policy in 2023. In order to strengthen the AML/CFT supervision process and institutional compliance, the FIU issued circulars and guidelines to Reporting Institutions, namely Licensed Banks, LFCs, Real Estate Institutions, Licensed Insurance Companies, Licensed Stockbrokers, and Attorneys-at-Law and Notaries. Furthermore, during the year, 5 red-flag indicator lists were issued, which included the identification of suspicious transactions relating to bribery or corruption, drug trafficking, and red flags for the insurance sector, securities sector and money or value transfer services sector.

BOX 6

Mutual Evaluation of Sri Lanka 2025: Its National Significance

1. Introduction

Money Laundering (ML) and Terrorist Financing (TF) pose significant challenges to the world's financial systems, as well as to national security and economic stability. ML and TF affect countries around the world by weakening their economies and societies. While some countries are at higher risk due to weak governance and corruption, no country is entirely free from the risks associated with ML and TF. Given the increasing prevalence of financial crimes worldwide, fighting against ML and TF has become a global priority. It requires cooperation among governments and law enforcement agencies, financial institutions, designated non-finance businesses and professions, and international organisations to protect the financial system and combat the risks of these crimes.

The Financial Action Task Force (FATF), the global policy setter in Anti-Money Laundering and Countering the Financing of Terrorism (AML/CFT), plays a vital role in combatting ML and TF by establishing global standards and promoting collaboration among nations.

As a proactive step, FATF and FATF-Style Regional Bodies (FSRBs) conduct Mutual Evaluations (MEs) to assess countries' technical compliance with the FATF standards and their effective implementation of AML/CFT measures. This evaluation process has significant national importance for member countries as it identifies weaknesses in national systems and identifies areas for improvement within their AML/CFT frameworks. At the same time, it promotes a level playing field among countries and encourages them to implement AML/CFT measures on a consistent basis, globally.

Sri Lanka will face its third ME in 2025. Given the country's past experience of two MEs which resulted in it being included in the FATF "Grey List" and subsequent economic and financial repercussions, the upcoming ME will be a significant event in the country's economic and financial progression.

2. Mutual Evaluation Process

The ME process involves an in-depth analysis of a country's AML/CFT system undertaken as a peer review. MEs are conducted over a period of 14 – 18 months and consist of two main components: technical compliance assessment and effectiveness assessment.

- **Technical compliance:** *Implementation of the specific requirements of FATF Recommendations, including the framework of laws and enforceable means; and the existence, powers and procedures of competent authorities.*
- **Effectiveness assessment:** *Effectiveness is the extent to which financial systems and economies mitigate the risks and threats of money laundering, and financing of terrorism and proliferation. This could be in relation to the intended result of a given (a) policy, law, or enforceable means; (b) programme of law enforcement, supervision, or intelligence activity; or (c) implementation of a specific set of measures.*

The stages in the ME process throughout which the technical compliance and the effectiveness are assessed, are outlined below.

i. **Assessing technical compliance (4 months):** The country provides information about its laws and regulations.

ii. **Scoping:** In preparation for the effectiveness assessment and the on-site visit, assessors undertake a preliminary scoping exercise to determine the areas of focus of the on-site visit.

iii. **On-site visit (2 weeks):** The assessors travel to the country for the on-site visit.

iv. **Report drafting:** Immediately following the on-site visit, the assessors finalise the mutual evaluation report with the findings of the effectiveness and technical compliance assessment.

v. **Plenary discussion (15 months after technical compliance assessment):** The assessors present the draft report to the FATF Plenary at one of the three meetings it holds every year.

vi. **Final quality review (2 months after approval):** Following Plenary approval, the report is reviewed for technical quality and consistency before it is published on the website.

vii. **Follow-up:** After adoption, the countries are required to address the shortcomings identified in the report which are followed-up annually until the next ME.

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3. National Significance of Mutual Evaluations

The ME process requires countries to implement the AML/CFT framework efficiently and effectively ensuring a safe and robust financial system. Accordingly, achieving a favourable outcome in the ME process ensures a secure financial system by protecting the country's position in the global financial system and thereby accelerating economic growth.

The following are some of the factors which show the national significance of MEs:

i. **Preserving Financial Stability:** Effective AML/CFT measures play a vital role in preserving the integrity and stability of the financial system. By adhering to FATF recommendations, countries mitigate the risk of being a high-risk jurisdiction, which could adversely affect their access to international banking services and capital markets.

ii. **Enhancing National Security:** A robust AML/CFT regime is essential for national security, preventing the use of illicit funds for financing terrorism and other criminal activities. By undergoing MEs and rectifying identified weaknesses, countries strengthen their capacity to disrupt illicit financial flows, thereby safeguarding national security interests.

iii. **Compliance with International Standards:** Participation in MEs is vital for countries to showcase their commitment to adhering to international AML/CFT standards. Maintaining these standards enhances a country's reputation in the global financial community while promoting trust among international partners and investors.

iv. **Facilitating International Cooperation:** Successful MEs promote greater international cooperation and information sharing among countries in combating financial crime. Enhanced compliance with the FATF standards improves a country's standing within the global financial system, facilitating efficient collaboration with other jurisdictions in investigations and enforcement actions. This collaboration strengthens the collective efforts to combat ML and TF on a global scale, leading to more effective outcomes in preventing and deterring financial crimes.

v. **Identification of Weaknesses:** MEs enable countries to identify weaknesses and gaps in their AML/CFT frameworks. Countries are informed of vulnerabilities such as legislative gaps or deficiencies in enforcement which is crucial for preventing exploitation by criminals and enhancing the effectiveness of AML/CFT measures.

4. Sri Lanka's Past Experience of Facing Mutual Evaluations

Sri Lanka has undergone two MEs by the Asia/Pacific Group on Money Laundering (APG), the regional FSRB for the Indo-Pacific. The two MEs were in 2006 and 2014/15. Both these evaluations resulted in Sri Lanka being listed by the FATF as a "jurisdiction with strategic deficiencies" in its AML/CFT framework, commonly referred to as "Grey Listing". The grey-listing resulted in adverse economic and financial consequences on both occasions.

Subsequent to Sri Lanka's "Grey Listing" by the FATF after 2015, the European Commission also listed Sri Lanka as a high risk third country with AML/CFT strategic deficiencies in February 2018, which affected Sri Lanka's correspondent banking relationships.

As Sri Lanka took steps to significantly improve its AML/CFT system subsequent to 2015, Sri Lanka was delisted by the FATF and the European Commission in October 2019 and May 2020, respectively.

5. Sri Lanka's Preparedness for the Upcoming Mutual Evaluation

Given the adverse impacts of past evaluations, the upcoming ME will require Sri Lanka to further strengthen the country's AML/CFT regime. This requires collective action from stakeholders including the government and law enforcement agencies, financial institutions, designated non-finance businesses and professions, coordinated by the Financial Intelligence Unit of Sri Lanka (FIU-SL).

In this context, the country's preparedness is vital to showcase its dedication to combating financial crimes. This evaluation provides a thorough assessment of Sri Lanka's AML/CFT frameworks, highlighting strengths, weaknesses, and areas for future improvement. Accordingly, several key initiatives have been taken by the FIU-SL, in preparation for the ME.

i. **Establishing an AML/CFT Task Force:** A task force for AML/CFT was appointed by the Cabinet of Ministers, comprising five members under the chairmanship of a retired Supreme Court Justice, to oversee the progress of implementation of the stakeholder-wise action plans to address the identified gaps and coordination among relevant stakeholders.

ii. **Collaboration with the National Coordinating Committee:** The AML/CFT National Coordinating Committee (NCC) is the advisory body that maintains national level coordination among stakeholders in implementing AML/CFT measures in Sri Lanka. With the leadership of the NCC and AML/CFT task force, all work relating to the upcoming ME is being coordinated.

iii. **Conducting National Risk Assessment (NRA) in 2021/22:** In line with the FATF recommendations, the FIU coordinated the completion of the second NRA in 2021/22 to identify, assess and understand the ML/TF risks faced by the country. Accordingly, the country's overall ML/TF risk was assessed as "medium" which is a combination of medium level of threat and medium level of vulnerability.

iv. **Development of AML/CFT National Policy 2023 – 2028:** Based on the findings of the NRA, the National AML/CFT Policy for 2023 – 2028 was prepared, which was approved by the Cabinet of Ministers, to address the gaps identified to effectively combat ML and TF in the country.

v. **Developing stakeholder-wise action plans:** With the purpose of preparing the key stakeholders for the next ME, the stakeholder-wise action plans for relevant 24 stakeholder institutions were approved by the Cabinet of Ministers to improve the effectiveness and technical compliance level of AML/CFT framework of the country. The action plans were distributed among stakeholders with regular updates being provided by them to the NCC and to the AML/CFT task force.

vi. **Carrying out legislative amendments:** In order to further strengthen the legal framework on AML/CFT and to ensure adherence to the international standards, the FIU is in the process of amending key legislations which includes the Financial Transactions Reporting Act, No. 06 of 2006; the Prevention of Money Laundering Act, No. 05 of 2006; the Convention on the Suppression of Terrorist Financing Act, No. 25 of 2005. The FIU is also assisting in making the amendments to the Companies Act, No. 07 of 2007. These amendments are expected to be completed by the third quarter of 2024.

6. Conclusion

FATF MEs are events of national significance for member countries, as they play a vital role in assessing compliance with international AML/CFT standards, identifying weaknesses in national frameworks, enhancing national security, facilitating international cooperation, and preserving financial stability. By actively participating in the ME process, countries can strengthen the measures against financial crime and contribute to a safer and more secure global financial environment. Accordingly, collective efforts of all key stakeholders will ensure that Sri Lanka's AML/CFT framework is implemented efficiently and effectively, enabling the country to achieve a better compliance level at the upcoming ME while strengthening its position within the global financial community.

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2.4.8 Policies for Financial Consumer Protection

The Central Bank took initiatives to strengthen the financial consumer protection framework in 2023. Regulation on Financial Consumer Protection was issued during the year for Financial Service Providers. The regulation underscores the commitment of the Central Bank to uphold the interests and rights of financial consumers, while emphasising transparency, fairness, and responsible business practices across the financial sector. Alongside the prescribed two-tier complaint handling procedure, the Regulation empowers the Central Bank to initiate market conduct supervision, a crucial mechanism for ensuring effective financial consumer protection. The Central Bank envisages to rollout consumer protection regulations throughout 2024 to maintain the integrity and stability of the financial system, while prioritising the welfare of financial consumers in Sri Lanka. Contemplating the need to safeguard the rights and interests of the financial consumers and promoting ethical standards among financial service providers, the Central Bank envisages to commission Market Conduct Supervision as a strategic priority in 2024.

2.4.9 Policies on Deposit Insurance and Resolution of Financial Institutions

CBA designates the Central Bank as the resolution authority of licensed financial institutions. The Banking (Special Provisions) Act No. 17 of 2023 defines the resolution authority of the Central Bank and stipulates the measures that can be implemented to resolve a licensed financial institution in a timely manner; to revive such financial institutions as a going concern to ensure the interests of the depositors and creditors thereof ensuring the financial system stability and winding up process for such licensed banks. The Central Bank initiated preparatory measures to implement the provisions of the Banking (Special Provisions) Act and to operationalise the resolution function. These measures include the development of a Resolution Handbook, the establishment of resolution triggers, the creation of a database for licensed financial institutions and the formulation of data templates for resolution planning during 2023. These steps are aimed at facilitating the preparation of resolution plans for licensed financial institutions, ultimately ensuring alignment with global standards and bolstering the stability of the financial system in Sri Lanka.

CBA and the Banking (Special Provisions) Act recognise the establishment of the Sri Lanka Deposit Insurance Scheme (SLDIS) as a means of upholding public confidence and promoting and contributing to the stability of the financial system in Sri Lanka. The Banking (Special Provisions) Act articulates operational procedures for the administration and management of SLDIS and entrusts powers, duties and functions related to the Deposit Insurance Fund. The Financial Sector Safety Net Strengthening Project (FSSNP), which was initiated with the collaboration of the Government and the World Bank, seeks to fortify the financial and institutional capacities of SLDIS in accordance with international standards. Under the FSSNP initiative, SLDIS was strengthened through a financing mechanism offered by the World Bank and backstop funding arrangements were established with the Government. A new investment policy is being drafted to expand SLDIS' investment portfolio across a range of instruments in both local and international financial markets. These policy driven enhancements aim to align SLDIS with the Core Principles for Effective Deposit Insurance Systems outlined by the International Association for Deposit Insurers, fortifying Sri Lanka's financial sector safety net.

2.4.10 Financial Sector Policy Reforms

The financial sector is undergoing significant policy reforms as part of the IMF-EFF arrangement and in collaboration with multilateral agencies, with the view of addressing structural weaknesses, building resilience, and maintaining stability in the financial system. Independent Asset Quality Review (AQR) components of bank diagnostic exercise for nine domestic banks accounting for 90 per cent of the domestic bank assets were completed during the year. The scope of the AQR encompassed rupee loans and advances, foreign currency loans, advances, and foreign currency denominated financial instruments. The Central Bank developed a roadmap for addressing banking system capital and foreign currency liquidity shortfalls for five large banks subject to AQR through a careful assessment of the findings of AQR, forward looking stress testing and envisaged impact of sovereign debt restructuring. A similar process is underway for the other four banks subject to AQR. Strategies have been formulated for government recapitalisation of viable banks that are unable to close the capital shortfalls from private sources. Accordingly, under Budget 2024, an allocation of Rs. 450 billion has been made to support the capital augmentation process of the banking sector. Further, amendments to the Banking Act No. 30 of 1988 were introduced for further strengthening and streamlining the provisions which are under submission to the Parliament.

The Financial Sector Crisis Management Committee and Technical Committee on Financial Management were established to strengthen the crisis preparedness frameworks of the sector. These committees consisted of officials from the Central Bank and the Ministry of Finance to facilitate interagency coordination and communication. The committees are vested with the responsibility of addressing potential systemic crises in the financial sector and their effects on the real economy and to minimise possible damages to the financial sector. Two committees will operate in two phases. The committees will closely monitor the liquidity risks and capital levels of regulated financial institutions during the first phase. During the second phase, a permanent framework will be established for crisis preparedness, crisis management and to minimise the impact of a financial crisis.

2.4.11 Other Policies

Several measures were undertaken during the year to improve public awareness regarding both positive and negative developments in the financial system. To address customer concerns regarding digital payment methods, the Central Bank has taken proactive steps. A trilingual web form was introduced on the Central Bank's website to create public awareness regarding unsafe, unsound, or unfair practices relating to payment services. The Central Bank also remains active on all forms of social media to ensure that essential messages, not only on monetary policy, but also those related to the financial system, including scams and prohibited financial schemes, are disseminated promptly.

During the year, steps were taken to improve stakeholder engagement. In addition to monitoring engagement on all media platforms, several surveys and other focus groups were undertaken to continuously assess the effectiveness of strategies that were already in place. The establishment of these feedback loops has helped to identify areas for improvement, gauge public sentiment, and fine-tune communication strategies to meet evolving needs. Building confidence in the financial system via prudent communication strategies is crucial for maintaining stability. Several educational outreach programmes were also conducted to a wide range of audiences to supplement the aforementioned efforts.

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Featured Box Article
Major Economic Policy Measures Implemented by or Related to the Central Bank of Sri Lanka[1]

Central Banking	
15 September 2023	Enactment of the Central Bank of Sri Lanka Act, No. 16 of 2023, to provide for the establishment of the Central Bank of Sri Lanka; for the repeal of the Monetary Law Act (Chapter 422); and to provide for matters connected therewith or incidental thereto.
03 October 2023	The Monetary Policy Framework Agreement between the Minister of Finance and the Central Bank, gazetted on October 5, 2023, sets an inflation target for the Central Bank, requiring it to maintain the Colombo Consumer Price Index (CCPI) based quarterly headline inflation rate at 5 per cent.
Monetary Policy	
02 January 2023	Effective 16 January 2023, the availability of the Standing Deposit Facility (SDF) to a particular Licensed Commercial Bank (LCB) was limited to a maximum of five (05) times per calendar month, while the availability of the Standing Lending Facility (SLF) to a particular LCB was capped at 90 per cent of the Statutory Reserve Ratio (SRR) of such LCB at any given day.
03 March 2023	Standing Deposit Facility Rate (SDFR) and Standing Lending Facility Rate (SLFR) were increased by 100 basis points to 15.50 per cent and 16.50 per cent, respectively.
01 June 2023	SDFR and SLFR were reduced by 250 basis points to 13.00 per cent and 14.00 per cent, respectively.
06 July 2023	SDFR and SLFR were reduced by 200 basis points to 11.00 per cent and 12.00 per cent, respectively.
09 August 2023	The Statutory Reserve Ratio (SRR) was reduced by 2.00 percentage points to 2.00 per cent to be effective from the reserve maintenance period commencing 16 August 2023.
05 October 2023	SDFR and SLFR were reduced by 100 basis points to 10.00 per cent and 11.00 per cent, respectively.
24 November 2023	SDFR and SLFR were reduced by 100 basis points to 9.00 per cent and 10.00 per cent, respectively.
09 February 2024	Effective 16 February 2024, the restriction on SLF was removed and the restriction on SDF was relaxed from five times (05) to ten times (10) during a calendar month.
26 March 2024	SDFR and SLFR were reduced by 50 basis points to 8.50 per cent and 9.50 per cent, respectively.
	Effective 01 April 2024, the restriction on SDF was removed.
Special Credit Schemes	
15 September 2023	The Central Bank discontinued operations of the Saubagya Loan Scheme and Domestic Agriculture Development Loan Scheme, with the enactment of the Central Bank Act No 16 of 2023.
03 January 2024	The Governing Board of the Central Bank took a policy decision not to implement new Government and Donor funded loan schemes in future.
Payments and Settlements	
01 February 2023	LankaPay (Pvt) Ltd (LPPL) linked with UnionPay International Co., Ltd (UPI), China and NPCI International Payments Ltd (NIPL), enabling Chinese and Indian tourists to use their payment wallets via LANKAQR for transactions in Sri Lanka. Transactions for Chinese tourists were enabled since February 2023 and transactions for Indian tourists were initiated from 12 February 2024.
08 May 2023	A Merchant Discount Rate (MDR) of 1.8 per cent was approved for payments made through LANKAQR using foreign payment apps. MDR of 0.5 per cent remains for domestic LANKAQR transactions.
31 August 2023	A trilingual web form to collect information from the public was developed on unsafe, unsound or unfair practices relating to payment practices or services.
29 December 2023	The Central Bank mandated Licensed Banks (LBs) to participate in various digital transaction initiatives including LankaPay Online Payment Platform (LPOPP), Direct Debit facility, Shared Know-Your-Customer

[1] Includes major economic policy measures implemented since 01 January 2023 until 28 March 2024 and the policy measures that are to be implemented in the near future.

A detailed version of policy measures implemented by or related to the Central Bank of Sri Lanka and major fiscal policy measures implemented since 01 January 2023 until 28 March 2024 are available online

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	(KYC) facility, and Government Digital Payment Platform (GDPP), while emphasising priorities such as enabling real-time notifications for transactions, promoting digital transactions in remote areas, ensuring immediate updating of credit card settlements via digital channels, and mandating the reference field for digital transactions, with Licensed Financial Acquirers instructed not to pass MDR to customers.
29 December 2023	Promoting foreign remittances together with digital transactions via e-money wallets, the enhanced and basic e-money wallet limits were raised from Rs. 50,000.00 and Rs. 10,000.00 to Rs. 150,000.00 and Rs. 20,000.00, respectively, with effect from 01 January 2024.
17 January 2024	The Central Bank mandated mobile payment applications using JustPay to request a One-Time-Password (OTP) from the linked financial institution for transactions equal to or exceeding Rs. 10,000/- starting from April 1, 2024. JustPay facilitates users to link accounts from any financial institution and make payments by pulling funds from linked accounts through the mobile application.
01 February 2024	Approval was granted for LankaPay (Pvt) Ltd (LPPL) to join with the Nepal Clearing House Ltd for the acceptance of LANKAQR transactions made by Nepali tourists through NEPALPAY QR mobile applications.
Anti-Money Laundering (AML) and Countering the Financing of Terrorism (CFT)	
03 March 2023	Circular No. 01 of 2023 was issued on calling for due vigilance on compliance lapses to all LBs and LFCs.
07 June 2023	Circular No. 02 of 2023 was issued on institutional compliance of real estate sector under the Financial Transactions Reporting Act, No. 06 of 2006 to Real Estate Institutions.
13 June 2023	Guideline No. 01 of 2023 was issued on reporting domestic Electronic Fund Transfer (EFT) threshold transactions to the goAML System of the Financial Intelligence Unit.
07 August 2023	Approval of the Cabinet of Ministers was received for adoption of the National Policy on Anti-Money Laundering and Countering the Financing of Terrorism (AML/CFT) of Sri Lanka for 2023-2028.
01 September 2023	Guideline No. 02 of 2023 was issued on AML/CFT compliance for the Attorneys-at-Law and Notaries.
Foreign Exchange Management and International Operations	
26 January 2023	Revocation of Operating Instructions issued on “Inward Investments Swaps - IIS Scheme”.
	Issuance of instructions to LBs on participation at the USD/LKR buy-sell and sell-buy, foreign exchange swaps auctions of the Central Bank.
24 February 2023	Reduction of weekly mandatory foreign exchange sales to the Central Bank by LBs on account of converted inward workers’ remittances, converted service sector related exports proceeds/receipts, and the residual value of mandatorily converted export proceeds of goods from 25 per cent to 15 per cent, effective from 27 February 2023.
27 February 2023	Directions No. 01 of 2023 were issued permitting Authorised Dealers (ADs) to open and maintain Special Foreign Currency Accounts (SFCAs) - Investee
03 March 2023	Revocation of the Operating Instructions issued by the Central Bank to LBs on “Managing Intraday Volatility of the Exchange Rate”, “Incentive Scheme on Inward Worker Remittances” and “Repatriation of Export Proceeds into Sri Lanka” - with effect from 07 March 2023.
28 June 2023	Order under Section 22 of the Foreign Exchange Act No.12 of 2017 (FEA), published in the Extraordinary Gazette Notifications No. 2338/40 dated 28 June 2023 to suspend/limit outward remittances with respect to selected capital transactions for six months commencing from the date of the order.
04 December 2023	Directions No. 02 of 2023 were issued on Business Foreign Currency Accounts (BFCAs), including enterprises permitted to sell goods/products to domestic market in terms of the Finance Act - Commercial Hub Regulations No. 1 of 2019.
	Directions No. 03 of 2023 were issued on Accommodations to BFCA Holders, permitting the payments to the enterprises engaged in business activities in Sri Lanka which are permitted to sell goods/products to the domestic market in terms of the Finance Act - Commercial Hub Regulations No.01 of 2019.
20 December 2023	Order under Section 22 of the FEA, published in the Extraordinary Gazette Notifications No. 2363/26 dated 20 December 2023, progressively easing some of the suspensions/ limitations relating to outward capital and current transactions imposed by the Orders issued earlier for six months commencing from the date of the Order.
01 January 2024	Directions No. 01 of 2024 were issued on Special Foreign Currency Accounts - Investee to facilitate current transactions, by extending the validity of the same until 30 June 2024.
Debt Management	
13 February 2023	The offering of Sri Lanka Development Bonds (SLDBs) under the Direct Issuance Arrangement was suspended.
16 March 2023	"Registered Stock and Securities (Disclosure of Information) Regulations, No.1 of 2023" was issued.

04 April 2023	In instances where the Monetary Policy announcement of the Central Bank is due during the normal Phase II window, Phase II of the respective Treasury bill auction is executed for a period of one hour immediately post a Treasury bill auction or close of business of the auction day whichever falls later.
12 May 2023	A resolution to increase the limit on issuance of Treasury bills from Rs. 5,000.0 billion to Rs. 6,000.0 billion in terms of the Local Treasury Bill Ordinance No. 08 of 1923 was approved by Parliament.
19 June 2023	The new web-based Treasury bill issuance system was introduced with effect from 21 June 2023.
04 July 2023	The Ministry of Finance (MOF) announced a policy on Sri Lanka's Domestic Debt Optimisation (DDO), consistent with the Extended Fund Facility, to contribute to meeting the Debt Sustainability targets agreed upon with the International Monetary Fund.
21 August 2023	The Appropriation (Amendment) Bill to amend the maximum borrowing limit of the Government from Rs. 4,979.0 billion as set out in Section 2(1)(b) of the Appropriation Act, No. 43 of 2022, to Rs. 13,979.0 billion, was approved by the Parliament.
14 September 2023	As per the Exchange Memorandum for Treasury bonds issued under the DDO programme, the settlement of the Treasury bonds exchange was carried out. Accepted offers were converted into new Treasury bonds amounting to Rs. 3,204.5 billion which had longer maturities. Furthermore, an accrued interest of Rs. 110.9 billion was paid to investors for their accepted Treasury bond amounts.
20 September 2023	The new web-based system for Direct Issuance Window for Treasury bonds was introduced with effect from 25 September 2023.
21 September 2023	Outstanding credits (the "provisional advances") of Rs. 344.7 billion from the Central Bank to the Government and outstanding Treasury bills amounting to Rs. 2,368.4 billion of the Government purchased by the Central Bank in the primary market were converted into ten (10) step-down fixed coupon new Treasury bonds denominated in LKR amounts to Rs. 2,492.3 billion and twelve (12) existing Treasury bills amounts to Rs. 220.8 billion and settled on 21 September 2023 in terms of the section 129 (2) of the CBA and the Appropriation (Amendment) Act, No. 12 of 2023.
03 November 2023	The Foreign Currency Banking Unit (FCBU) Loan exchange under the DDO programme was executed for People's Bank in terms of the Memorandum of Understanding (MOU) for restructuring of the FCBU loan balance of People's Bank signed on 18 August 2023. The loan amount of Rs.27.7 billion was allocated to five existing Treasury bonds that were issued under DDO.
11 March 2024	The amount offered at Phase II of Treasury bill auctions was reduced to the aggregate auction shortfall and 10 per cent of the aggregate amount offered or Rs. 5.0 bn whichever is higher in terms of the amended Directions issued on 07 March 2024 which were in force effective from 11 March 2024.
	The amount offered at Direct Issuance Window (DIW) of Treasury bond auctions was reduced to 10 per cent of the amount offered from ISINs which are fully accepted at Phase I in terms of the amended Directions issued on 07 March 2024 which were in force effective from 11 March 2024.
Financial Sector	
Licensed Banks	
02 January 2023	A Circular was issued with effect from 03 January 2023 adjusting the Bank Rate in line with the latest available Average Weighted New Deposit Rate (AWNDR) published by the Central Bank with a margin of +300 basis points.
31 January 2023	Banking Act Determination was issued determining qualifying non-financial corporate debt securities and qualifying non-financial common equity shares as liquid assets in the computation of the Statutory Liquid Asset Ratio of LCBs and Licensed Specialised Banks (Licensed Banks - LBs), given that such instruments shall satisfy the conditions specified in the Banking Act Directions on the Liquidity Coverage Ratio under Basel III liquidity standards.
02 February 2023	Banking Act Directions were issued restricting discretionary payments of LBs considering the prevailing macroeconomic conditions and the importance of maintaining appropriate level of liquidity and capital to ensure sustainability in LBs.
16 February 2023	In addition to the existing list of HS Codes covered by the Order dated 19 May 2022, an Order was issued to all LCBs on the requirement of maintaining a 100 per cent Cash Margin Deposit Requirement against Letters of Credit for newly added 64 HS Codes.
17 February 2023	Amendment to the Banking Act Directions No. 03 of 2022 on Margin Requirements Against Imports was issued, extending the applicability of the cited Directions to 64 new HS codes.
07 March 2023	LBs were requested to provide appropriate concessions to affected borrowers on a case-by-case basis with a view to encouraging Micro, Small and Medium Enterprises (MSMEs) and individuals with a potential to revive their businesses/income streams.

21 April 2023	A circular was issued to LBs informing to discontinue the recognition of ICRA Lanka Ltd as an eligible/ acceptable credit rating agency for regulatory purposes pertaining to LBs.
25 April 2023	Amendments to the Banking Act Directions No. 01 of 2023 on Restrictions on Discretionary Payments of LBs were issued. Accordingly, LBs were required to refrain from increasing management allowances of Chief Executive Officers (CEO), Key Management Personnel (KMP) and payments to the Board of Directors, without meeting the cited requirements.
17 May 2023	A Circular was issued to withdraw the minimum cash margin deposit requirements against Letters of Credit, imposed on 19 May 2022 and 16 February 2023.
18 May 2023	Banking Act Directions were issued, revoking the Banking Act Directions No. 03 of 2022 and the Banking Act Directions No. 02 of 2023 on Margin Requirements Against Imports.
25 August 2023	A Monetary Law Act Order was issued on the interest rates applicable on Sri Lankan Rupee (LKR) denominated lending products of LBs, imposing maximum interest rates on certain lending products and requiring LBs to reduce the interest rates of all other new and existing rupee denominated lending products by specific percentages on target dates.
15 November 2023	The Banking (Special Provisions) Act No. 17 of 2023 (BSPA) was certified by the Parliment on 14 September 2023 and by order published in the Gazette No. 2358/46, the provisions of the aforesaid Act came into operation effective from 15 November 2023.
	The Banking (Special Provisions) Act Directions No. 01 of 2023 was issued to Member Institutions of the Sri Lanka Deposit Insurance Scheme.
23 November 2023	A Banking Act Determination on annual license fee was issued to LBs informing the new license fee structure applicable for the years 2024 and 2025.
27 November 2023	Determinations made under the BSPA were issued to the general public under the Gazette Notification No. 2360/02.
08 December 2023	Amendments to the Banking Act Directions No. 16 of 2021 on Regulatory Framework on Technology Risk Management and Resilience for LBs were issued *inter alia* extending the general deadline and certain specific timelines, considering the extraordinary circumstances prevailed during the recent past.
29 February 2024	Amendments to the Circular No.08 of 2019 on "List of Qualified Auditors to Audit the Accounts of Licensed Commercial Banks and Licensed Specialised Banks" were issued by replacing Picewaterhouse Coopers and SJMS Associates as Deloitte Partners and Deloitte Associates, respectively with the changes of names of aforesaid audit firms.
25 March 2024	Banking Act Directions were issued on "Large Exposures of Licensed Banks", to be implemented with effect from 01 January 2026, with a view to mitigating the credit concentration risks, ensuring safety and soundness of the banking sector.
28 March 2024	A circular was issued on "Guidelines for the Establishment of Business Revival Units in Licensed Banks", with a view to facilitating the sustainable revival of businesses affected by the extraordinary macroeconomic circumstances and to improve the asset quality of LBs.
Forthcoming	Banking (Amendment) Act
	Revised Directions on Corporate Governance

Licensed Finance Companies (LFCs), Specialised Leasing Company (SLC), Licensed Microfinance Companies (LMFCs), and Primary Dealer Companies (PDCs)

05 January 2023	The Monetary Board of the Central Bank, in terms of the Regulations made under the Registered Stock and Securities Ordinance and the Local Treasury Bills Ordinance, extended the suspension of Perpetual Treasuries Limited (PTL) from carrying on the business and activities of a Primary Dealer for a further period of six months with effect from 05 January 2023, in order to continue with the investigations being conducted by the Central Bank.
18 January 2023	The registration of Swarnamahal Financial Services PLC as a registered finance leasing establishment was cancelled in terms of Section 9.1. (h) of the Finance Leasing Act, No.56 of 2000 (FLA).
31 January 2023	Subsequent to the amalgamation of the LOLC Development Finance PLC (LDFP) with LOLC Finance PLC (LOFP) as a part of the Masterplan for Consolidation of Non-Bank Financial Institutions (the Masterplan), the Monetary Board of the Central Bank cancelled the licence issued to LDFP to carry on finance business under the Finance Business Act, No.42 of 2011 (FBA). Further, the registration of LDFP issued under the FLA was cancelled by the Director, Department of Supervision of Non-Bank Financial Institutions (D/DSNBFI).
	Guideline on declaration of dividends or repatriation of profits was issued to LFCs as a measure to strengthen resilience and capacity of LFCs to absorb economic shocks that could arise in the time of uncertainty and continue to support credit needs of customers, by maintaining sufficient capital.

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02 February 2023	LFCs were informed that ICRA Lanka Ltd. was removed as an acceptable credit rating agency for specified purposes.
08 February 2023	The Commercial High Court of Colombo ordered to appoint a liquidator to The Standard Credit Finance Limited whose license cancelled by the Monetary Board on 25 July 2018 under FBA subject to supervision of court.
03 March 2023	LFCs and SLC were requested to provide appropriate concessions to micro, small and medium enterprises and individuals affected by the present macroeconomic conditions.
21 March 2023	The Commercial High Court of Colombo ordered to appoint a liquidator to The Finance Company Ltd of which licence cancelled by the Monetary Board on 22 May 2020 under FBA subject to supervision of court.
25 April 2023	Notice of cancellation of the finance business licence of Bimputh Finance PLC (BFP) was issued with effect from 25 April 2023 as directed by the Monetary Board of the Central Bank under section 37 (1) of FBA.
09 June 2023	The Commercial High Court of Colombo ordered to appoint a liquidator to Central Investments and Finance Ltd whose licence cancelled by the Monetary Board on 05 March 2018 under FBA subject to supervision of court.
05 July 2023	The Monetary Board of the Central Bank, in terms of the Regulations made under the Registered Stock and Securities Ordinance and the Local Treasury Bills Ordinance, extended the suspension of PTL from carrying on the business and activities of a Primary Dealer for a further period of six months with effect from 05 July 2023, in order to continue with the investigations being conducted by the Central Bank.
31 July 2023	As a part of the Masterplan, Kanrich Finance Ltd was merged with Nation Lanka Finance PLC (NLFP) with effect from 31 July 2023 and the remaining entity is NLFP.
01 September 2023	Finance business licence issued to BFP was cancelled with effect from 01 September 2023 as directed by the Monetary Board of the Central Bank due to no satisfactory progress made by BFP to revive the critical condition faced by BFP.
15 December 2023	The Commercial High Court of Colombo ordered to appoint a liquidator to ETI Finance Ltd under FBA subject to supervision of court.
05 January 2024	The Governing Board of the Central Bank, in terms of the Regulations made under the Registered Stock and Securities Ordinance and the Local Treasury Bills Ordinance, extended the suspension of PTL from carrying on the business and activities of a Primary Dealer for a further period of six months with effect from 05 January 2024, in order to continue with the investigations being conducted by the Central Bank.
13 February 2024	A Direction was issued on periodic reporting requirements with the objective to obtain timely, accurate, consistent and complete information of LFCs to ascertain the manner in which the business and corporate affairs of LFCs are being conducted or for any other specified purpose.
Forthcoming	Implementing Phase II of the Masterplan ensuring long term sustainability of small to medium scale LFCs in the medium term.
	Amending the existing regulatory framework in line with the current market developments, including amendments to the FBA and FLA.
	Introducing rules and regulations to improve stability of the non-banking sector while strengthening the supervisory review process.

Other Financial Sector Related Policy Measures

08 August 2023	Regulations on Financial Consumer Protection were issued under Section 10 (c) of Monetary Law Act, No. 58 of 1949 (MLA), which are applicable to Financial Service Providers (FSPs) regulated by the Central Bank to promote fair, transparent, and ethical business conduct of FSPs and provide the basis for the Central Bank to carry out market conduct supervision and enforcement.
31 January 2024 01 February 2024 06 February 2024	Loan Agreements were signed between the International Development Association (IDA) which is a member of the World Bank Group, MOF and the Central Bank under the Financial Sector Safety Net Strengthening Project of the World Bank.