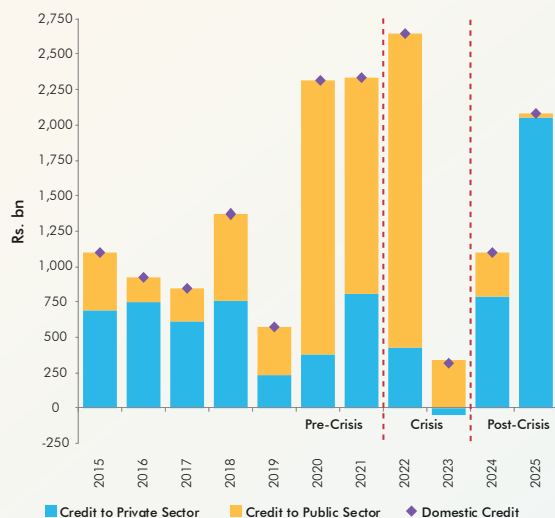


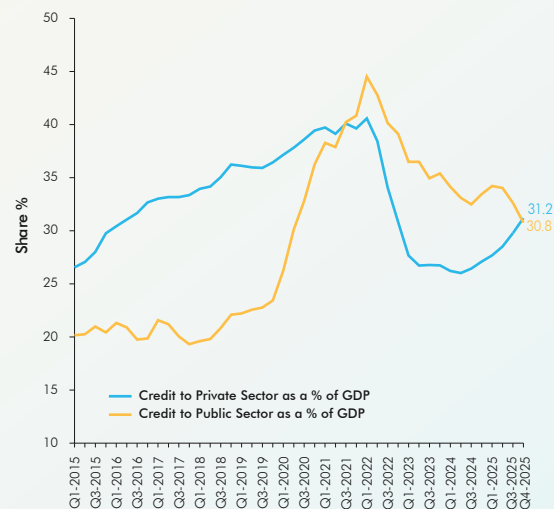
Featured Chart 1.5 Rebalancing Domestic Credit: Public vs. Private Sector Dynamics



Domestic Credit Expansion (Private vs Public)



Private and Public Sector Credit as a Share of GDP



Note: 1. Domestic credit refers to the total gross loans and advances extended to both the private and public sectors by the banking system. The public sector component includes credit extended to the Government, including investments in government securities and credit extended to State-Owned Business Enterprises (SOBEs).

Sources: Central Bank of Sri Lanka
Department of Census and Statistics

2. Credit-to-GDP ratio is derived as the ratio of total outstanding credit to the annualised nominal GDP of the corresponding quarter.

In the years preceding the economic crisis, persistent structural imbalances in the fiscal sector led the Government to increasingly rely on financing from the domestic banking sector, including borrowings from the Central Bank, to meet its growing financing requirements. This contributed to a crowding-out effect on private sector credit, irrespective of changes in the monetary policy stance. These pressures intensified during the crisis period as sovereign credit rating downgrades and debt distress constrained the Government's access to external financing, forcing it to rely almost entirely on domestic sources. However, fiscal consolidation efforts and legislative reforms aimed at improving the institutional autonomy of the CBSL, including the prohibition of

monetary financing, following the recent economic crisis have yielded favourable results in the post-crisis economy.

The resulting moderation in public sector credit has created space for private sector borrowing, giving rise to crowding-in effect in private sector credit. Accordingly, private sector credit-to-GDP, having declined during the crisis, gradually recovered to 31.2% by end 2025, supported by the recovery in economic activity and the lower cost of borrowings under an accommodative monetary policy stance. However, the private sector credit-to-GDP ratio remains below pre-crisis levels. Meanwhile, the public sector credit-to-GDP ratio continued to exhibit a downward trend during this period.