

**(F) CENTRAL BANKING**

The international reserve of the Central Bank which declined to a low point of Rs. 69 million in January, 1964, from Rs. 114.2 million in December 1963, increased to Rs. 116.9 million in February, 1964. This increase reflected the acquisition of foreign assets with a face value of Rs. 53.3 million from the Post Office Savings Bank which received domestic assets of an equal value from the Central Bank in return. The international reserve declined again to Rs. 100 million in April, but showed a steady improvement in the last quarter of the year. In December the reserve stood at Rs. 135.9 million reflecting an increase of Rs. 21.7 million or 19.0 per cent over the year as compared with a decline of Rs. 37.9 million or 24.9 per cent in 1963. However, in 1964, total external assets declined by Rs. 111.3 million or 24.1 per cent, as against a decline of Rs. 41.6 million or 8.2 per cent in 1963. As a proportion of the Central Bank's total currency and demand liabilities, the international reserve improved from 9.3 per cent in 1963 to 10.4 per cent in 1964.

The domestic assets of the Central Bank increased by Rs. 155 million or 12.0 per cent to Rs. 1,449.2 million. In 1963 the increase amounted to Rs. 194 million or 17.6 per cent. Within this increase, Government and Government guaranteed securities accounted for Rs. 123.2 million; an increase of 12.0 per cent as against 15.8 per cent in 1963 in the portfolio of these securities held by the Central Bank. Loans and advances to the Government increased by Rs. 6.8 million whereas advances to commercial banks declined by Rs. 18.8 million.

Total deposit liabilities of the Central Bank increased by Rs. 47.1 million in 1964 and was accounted for largely by an increase in deposits of commercial banks amounting to Rs. 39.4 million.

The currency issue of the Central Bank increased by only Rs. 31.2 million or 3.5 per cent as against an increase of Rs. 111.5 million or 14.1 per cent in 1963. The currency held by the banks and the private sector increased by Rs. 7.2 million and Rs. 24.6 million respectively, whereas currency held by the Government declined by Rs. 0.6 million.

**Credit Policy**

In 1964, the increase in the total volume of bank credit extended to the private sector amounted to Rs. 92 million as against an increase of Rs. 136.9 million in 1963. The intensification and extension of import control measures in 1963 and 1964 had given rise to a situation in which the continued increase in bank credit was likely to generate excessive inflationary pressures within the economy. The Central Bank had on the one hand to take account of

the possible emergence of a condition of excess monetary demand, aggravated by a speculative tendency to hoard goods, with the continued increase in bank credit. On the other hand, the Central Bank was anxious not to retard the trends towards expansion of production, particularly with regard to industry. The Central Bank had also to take account of the continued effort of the Government to rely less on the credit extended by the banking system as a method of financing its increasing expenditure.<sup>1</sup>

The credit policy of the Central Bank had to reflect the several factors mentioned above. Although bank advances showed a continuing upward trend there was no direct evidence of an increase in advances for consumption or other inessential purposes. Of the total increase in loans and overdrafts by commercial banks of Rs. 106.8 million in 1964, Rs. 22.6 million represented an increase in credit extended to Government Corporations, Rs. 25.7 million increase in credit extended to Co-operative Institutions and Rs. 58.5 million an increase in credit extended to private business and individuals. It is possible that in situations of inflationary pressure there would be an increased demand for credit for the purpose of financing the holding of stocks. It is difficult to assess the extent to which the financing of stockholding for speculative purposes played a part in the overall expansion of credit in 1964. The increase in advances under the category 'other purposes' in the purpose-wise classification and the increase in both unsecured advances and advances against stock in trade in the classification by type of security may indicate an increase in credit for speculative purposes. Pending a detailed examination of the expansion of credit which is now in process, the Central Bank desisted from introducing any further measures of quantitative credit control. The measures of credit control introduced previously continued to be in force. In addition, the power of moral suasion is also an effective instrument in influencing the channelling of credit by the commercial banks for productive rather than for inessential purposes.

### Banking Development

The Medium and Long-term Credit Fund was established in July 1964 by the transfer of Rs 10 million from the General reserve of the Central Bank. The intention was to encourage lending by credit institutions<sup>2</sup> for productive purposes<sup>3</sup> by making available refinance facilities. However, up to the end of 1964, no application for refinance was received by the Fund. This may be due

1. Government indebtedness to the Central Bank (loans, advances and investments) increased by Rs 178.9 million in 1962, Rs. 146.5 million in 1963 and Rs 130.4 million in 1964. Government indebtedness to commercial banks increased by Rs. 71.4 million and Rs. 20.3 million in 1962 and 1963 respectively but decreased by Rs. 25.4 million in 1964.
2. Credit institutions in this context mean any banking institution as defined in sub-section (1) of Section 127 of the Monetary Law Act and includes the Development Finance Corporation of Ceylon.
3. Productive purposes mean any purpose relating to the promotion and the development of industry, agriculture, trade, commerce or business as the Monetary Board may from time to time determine.

to several reasons. In the first place, import restrictions on raw materials and capital goods might have tended to dampen demand for long-term credit; secondly commercial banks themselves may on account of their improved liquidity have been in a position to accommodate such demand as did arise, whilst in addition, the short period in which this scheme has been in operation and its relative novelty might also have been of significance.

The Central Bank examined the feasibility of establishing a scheme of Loan insurance and is formulating a limited scheme.

The Bankers' Training Institute, which grew out of the earlier training programme conducted by the Central Bank in co-operation with commercial banks, was expanded with the shift of the Central Bank to the new building in 1964. As at the end of December, 1964, 900 students were on the roll of the Institute. The Institute also provided a special short term course of instructions for new recruits of the People's Bank, in 1964.