

Interest payments on public debt in 1983 consisted of Rs. 5,314 million on domestic debt and Rs. 1,279 million on foreign debt. During the year, interest payments on domestic debt increased by 27 per cent over the last year while those on foreign debt increased by 40 per cent. Interest on domestic debt was made up of Rs. 3,228 million on rupee loans, Rs. 2,082 million on Treasury bills and Rs. 3 million on administrative borrowings. Interest payments on rupee loans recorded an increase of 49 per cent, while those on Treasury bills increased by 4 per cent over the last year. Interest paid on administrative borrowings remained unchanged. Interest payments on foreign loans consisted of Rs. 299 million on project loans, Rs. 441 million on commodity loans and Rs. 539 million on other loans. While interest payments on project loans and commodity loans increased by 39 per cent and 27 per cent respectively, interest payments on other loans increased by 53 per cent over last year. Under other loans the total interest payment on Euro Dollar commercial loan amounted to Rs. 497 million in 1983 as compared with Rs. 344 million in 1982, Rs. 252 million in 1981 and Rs. 4 million in 1980. Euro currency commercial loans were obtained on three contracts. The first loan amounting to US \$ 50 million was obtained in 1980 at a rate of interest of 0.875 per cent over London Inter Bank Offered Rate (LIBOR) in respect of the first four years of the grace period allowed on capital repayment and at an interest of 1 per cent over LIBOR during the balance four year period. The second loan amounting to US \$ 75 million was obtained in 1981 at a rate of 0.625 per cent over LIBOR for first six years and 0.75 per cent over LIBOR for the balance two years. A grace period of five years has been provided for capital repayment on this loan. The third loan contracted in 1982 amounting to US \$ 100 million was partially disbursed in 1982 and 1983. This loan was obtained at a rate of interest of 0.5 per cent over LIBOR for the first two years and 0.625 per cent over LIBOR for the balance six years. This loan has a grace period of five years on principal repayments. While the commitment charges on account of non-disbursements on both the 1st and 2nd loans were 0.5 per cent, those on the third loan were 0.375 per cent. Interest payment on the Japanese yen loan amounted to Rs. 29 million in 1983, as compared with Rs. 0.3 million in 1982. This loan was obtained at a rate of interest of 9.4 per cent per annum and is repayable over 15 years including a grace period of 5 years on principal repayments.

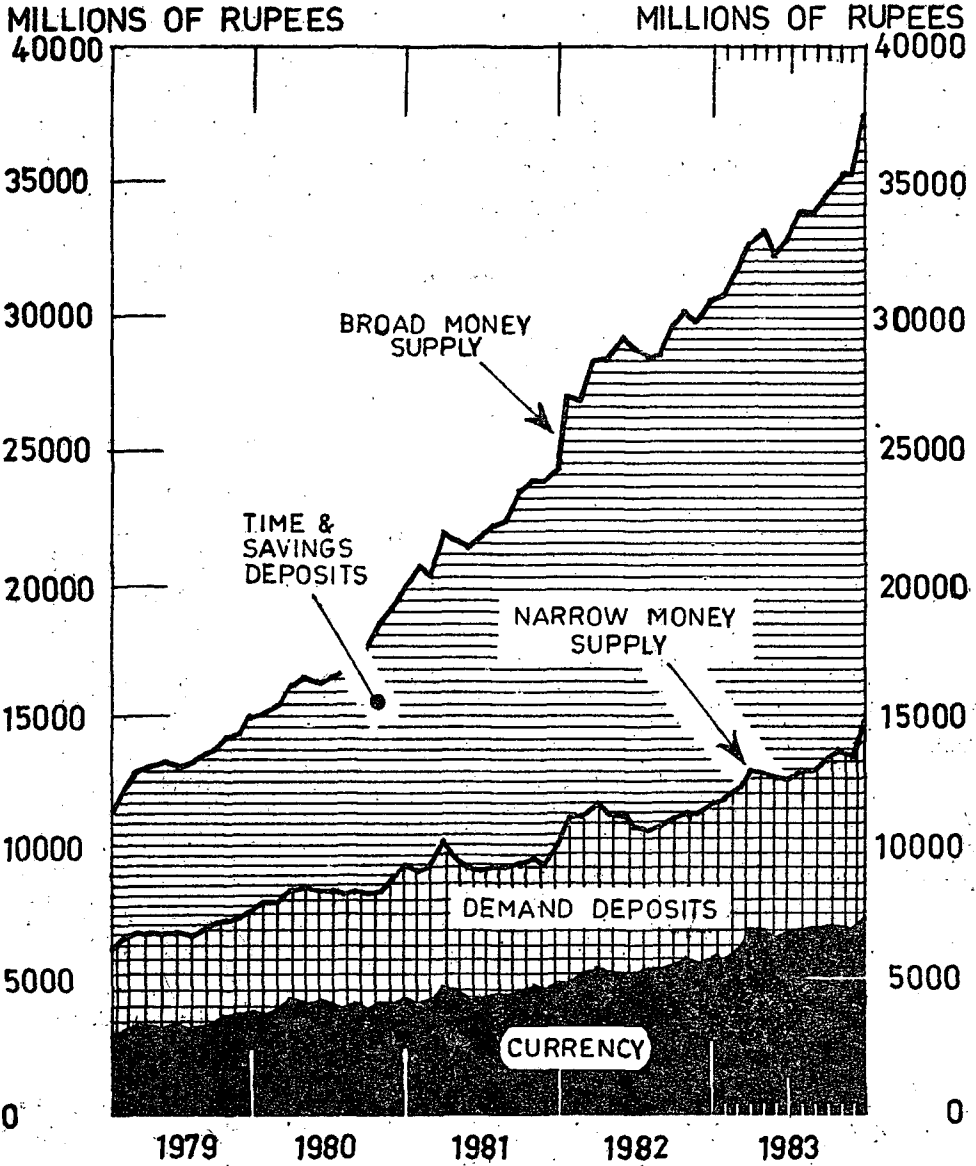
## **MONEY AND BANKING**

### **Money Supply**

In 1983 there was an increase in broad money supply ( $M_2$ ) accompanied by a lower rate of growth in quasi-money.  $M_1$  consists of currency and demand deposits held by the public while quasi-money includes time and savings deposits of the private sector held with commercial banks. During the year,  $M_1$  rose by Rs. 2,988 million or 25 per cent when compared with an increase of Rs. 1,735 million or 17 per cent in 1982 while quasi-money rose by Rs. 3,759 million or 20 per cent as against an increase of Rs. 4,328 million or 30 per cent in 1982. The decline in the rate of growth of quasi-money was partly due to the out-flow of deposits from

# MONEY SUPPLY

MONTHLY



commercial banks to other deposit mobilising institutions following the downward adjustment in deposit rates of banks. Broad money supply ( $M_2$ ) consisting of  $M_1$  and quasi-money rose by Rs. 6,747 million or 22 per cent when compared with an increase of Rs. 6,063 million or 25 per cent in 1982.

In 1983, currency held by the public rose by Rs. 1,212 million (20 per cent) when compared with Rs. 1,165 million (24 per cent) in 1982. The highest monthly increases were in March and December amounting to 10 and 6 per cent, respectively, indicating the increased preference for cash balances pending the festive seasons in April and December. On the other hand, the demand deposits of the public rose by Rs. 1,776 million (31 per cent) as against a much lower increase of Rs. 571 million (11 per cent) in 1982. Consequently, the share of demand deposits in  $M_1$  increased from 49 to 51 per cent during the year. Correspondingly, the share of currency in  $M_1$  declined from 51 per cent in 1982 to 49 per cent in 1983.

**TABLE 1.50**  
**Monetary Aggregates 1981—1983**

(Amount in Rs. Million)

	Narrow Money Supply $M_1$						Broad Money Supply $M_2$					
	1981	1982	1983	% Change (1981 over 1980)	% Change (1982 over 1981)	% Change (1983 over 1982)	1981	1982	1983	% Change (1981 over 1980)	% Change (1982 over 1981)	% Change (1983 over 1982)
January	9,208	11,046	11,852	+17.3	+20.0	+7.3	20,532	26,890	30,802	+35.8	+31.0	+14.5
February	9,288	11,178	12,234	+17.9	+20.4	+9.4	20,199	26,758	31,708	+30.4	+32.5	+18.5
March	10,125	11,671	12,986	+20.9	+15.3	+11.2	21,984	28,240	32,874	+36.9	+28.5	+16.4
April	9,573	11,276	12,842	+14.2	+17.8	+13.9	21,555	28,395	33,114	+31.6	+31.8	+16.6
May	9,168	11,132	12,606	+10.6	+21.5	+13.2	21,437	29,128	32,491	+31.3	+35.9	+11.5
June	9,033	10,815	12,589	+9.1	+19.8	+16.4	21,681	28,739	32,798	+32.0	+32.6	+14.1
July	9,097	10,710	12,964	+11.0	+17.8	+21.4	22,065	28,459	33,846	+32.5	+29.0	+18.9
August	9,197	10,892	12,977	+11.6	+18.5	+19.1	22,165	28,494	33,732	+29.6	+28.6	+18.4
September	9,445	11,171	13,322	+16.1	+18.3	+19.3	23,460	29,781	34,620	+32.5	+27.0	+16.2
October	9,520	11,413	13,572	+13.4	+19.9	+18.9	23,837	30,161	35,314	+29.7	+26.6	+17.0
November	9,459	11,452	13,544	+5.3	+21.1	+18.3	23,842	29,860	35,324	+24.9	+25.3	+18.3
December	10,024	11,760	14,748	+6.3	+17.4	+25.4	24,447	30,510	37,257	+23.0	+24.9	+22.1
Monthly Average	9,429	11,210	13,020	+12.7	+18.9	+16.1	22,267	28,785	33,657	+30.7	+29.3	+16.9

Source : Central Bank of Ceylon.

Although in absolute terms there has been a continuous increase (except in May and August 1983) the rate of growth in quasi-money has shown a declining trend during the past few years. The absolute increase in quasi-money during 1983 was mainly on account of increases in time and savings deposits of the other private sector (private sector proper) which rose by Rs. 3,824 million (27 per cent) when compared with an increase of Rs. 2,815 million (25 per cent) in 1982.

**TABLE 1.51**  
**Monetary Aggregates and Causal Factors**

(Amount in Rs. Million)

Item	December 1981	December 1982	December 1983	Change 1981/1982		Change 1982/1983	
				Amount	Percentage	Amount	Percentage
<b>Monetary Aggregates</b>							
1. Currency held by the public ..	4,822.9	5,987.7	7,200.1	+ 1,164.8	+ 24.1	+ 1,212.4	+ 20.3
2. Demand deposits held by the public ..	5,201.5	5,772.1	7,547.8	+ 570.6	+ 10.9	+ 1,775.7	+ 30.8
Narrow Money Supply (M <sub>1</sub> ) ..	10,024.4	11,759.8	14,747.9	+ 1,735.4	+ 17.3	+ 2,988.1	+ 25.4
3. Time and Savings deposits of the private sector held with Commercial banks ..	14,422.5	18,750.1	22,509.0	+ 4,327.6	+ 30.0	+ 3,758.9	+ 20.0
3.1 Co-operative Institutions ..	334.5	357.3	469.2	+ 22.8	+ 6.8	+ 111.9	+ 31.3
3.2 Government Corporations ..	2,768.4	4,257.8	4,081.1	+ 1,489.4	+ 53.8	- 176.7	- 4.2
3.3 Other Private Sector Constituents ..	11,319.6	14,135.0*	17,958.7*	+ 2,815.4	+ 24.8	+ 3,823.7	+ 27.1
Broad Money Supply (M <sub>2</sub> ) ..	24,446.8	30,509.9	37,256.9	+ 6,063.0	+ 24.8	+ 6,747.0	+ 22.1
<b>Causal Factors</b>							
1. Domestic Credit ..	33,966.6	42,397.6	49,293.0	+ 8,431.0	+ 24.8	+ 6,895.4	+ 16.3
1.1 Net Credit to Government ..	12,789.1	17,150.2	17,533.1	+ 4,361.0	+ 34.0	+ 382.9	+ 2.2
1.1.1 Gross credit to Government ..	15,667.4	19,719.8	20,972.1	+ 4,052.3	+ 25.8	+ 1,252.3	+ 6.4
by Central Bank ..	14,104.4	18,000.5	19,393.0	+ 3,896.0	+ 27.6	+ 1,392.5	+ 7.7
by Commercial Banks ..	1,563.0	1,719.3	1,579.1	+ 156.3	+ 9.9	- 140.2	- 8.2
1.1.2 Government deposits and cash balances ..	- 2,878.3	- 2,569.6	- 3,439.0	+ 308.7	+ 10.7	- 869.4	- 33.8
1.2 Gross Credit to the Private Sector ..	21,177.4	25,247.4	31,759.9	+ 4,070.0	+ 19.2	+ 6,512.4	+ 25.8
1.2.1 Co-operative Institutions ..	1,293.9	1,187.7	1,822.7	- 106.2	- 8.2	+ 634.9	+ 53.5
1.2.2 Government Corporations ..	4,487.7	4,677.4	4,385.2	+ 189.7	+ 4.2	- 292.3	- 6.2
1.2.3 Other Private Sector Constituents ..	15,395.8	19,382.3	25,552.1	+ 3,986.5	+ 25.8	+ 6,169.8	+ 31.5
2. External Banking Assets (net) ..	2,940.3	2,371.8	3,186.9	- 568.5	- 19.3	+ 815.1	+ 34.4
3. Other items (net) ..	-12,460.0	-14,259.5	-15,223.0	- 1,799.5	-	- 963.5	-
3.1 Other liabilities (net) of the Central Bank ..	- 7,615.5	- 9,382.7	- 9,417.4	- 1,767.2	-	- 34.6	-
3.2 Other liabilities (net) of Commercial Banks ..	- 4,702.2	- 4,891.2	- 6,319.3	- 189.0	-	- 1,428.1	-
3.3 Adjustments for items in transit ..	- 142.3	14.4	513.7	+ 156.7	+ 24.8	+ 499.3	+ 22.1
Broad Money Supply (M <sub>2</sub> ) ..	24,446.8	30,509.9	37,256.9	+ 6,063.0	+ 24.8	+ 6,747.0	+ 22.1

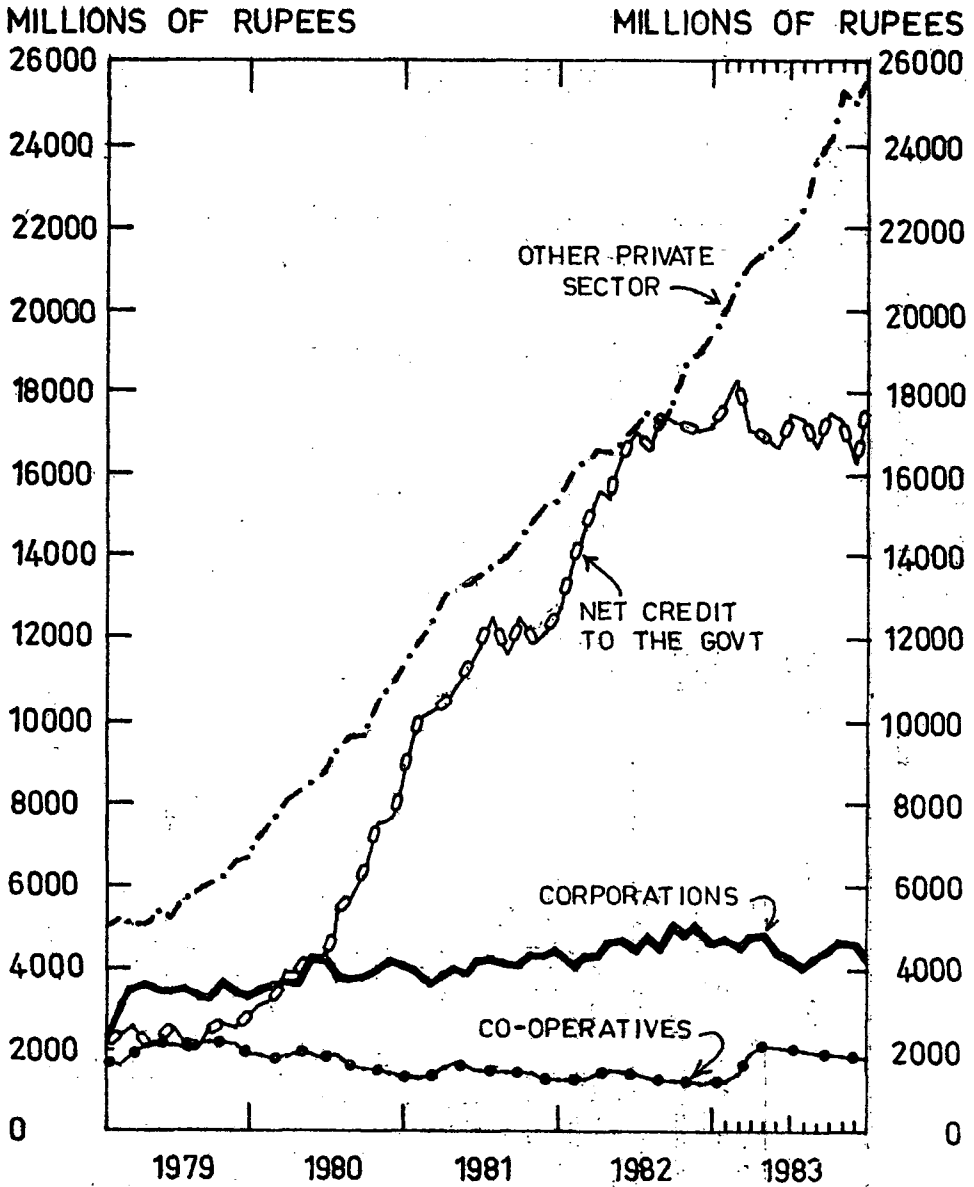
Note: Signs indicate the effect on M<sub>2</sub>.

\* Excludes Non Resident Foreign Currency Deposits.

Source: Central Bank of Ceylon.

# DOMESTIC CREDIT

MONTHLY



The decline in the rate of growth of quasi-money was wholly reflected in a substantial decrease in the quantum of deposits of government corporations. In contrast to an increase of Rs. 1,489 million (54 per cent) in 1982, these deposits dropped by Rs. 177 million (4 per cent) and the decline was more marked during the latter part of the year. Meanwhile, the time and savings deposits of the co-operative institutions rose sharply by Rs. 112 million (31 per cent) as against a much lower increase of Rs. 23 million (7 per cent) in 1982.

The decline in the rate of monetary growth in 1983 was partly caused by a deceleration in domestic credit. Compared to an increase of Rs. 8,431 million (25 per cent) in 1982, domestic credit expansion (DCE) amounted to Rs. 6,895 million (16 per cent) in 1983. Meanwhile, the impact of DCE on monetary aggregates was accentuated by the increase in external banking assets (net) by Rs. 815 million (34 per cent). However, the expansionary effect of these developments was partly moderated by an increase in other items (net) of the banking system amounting to Rs. 964 million largely due to an increase in other liabilities of commercial banks.

The DCE was the combined outcome of increases in net credit to Government (NCG) and gross credit to the private sector (GCPS). Of this, NCG increased only by Rs. 383 million or 2 per cent as against 34 per cent in the previous year. The significant feature experienced during 1983 was the substantial decline in the share of NCG in the total DCE from 40 per cent in 1982 to 36 per cent in 1983, reflecting the reduced reliance of the Government on the banking system.

Gross credit to Government by the Central Bank rose only by Rs. 1,393 million (8 per cent) during the year when compared with Rs. 3,896 million (28 per cent) in 1982. Credit to Government by commercial banks declined by Rs. 140 million (8 per cent) as against an increase of Rs. 156 million (10 per cent) in the previous year. However, the increase in gross credit to Government by the banking system was partly mitigated by a considerable build-up of government deposits and cash balances with the banking system amounting to Rs. 869 million (34 per cent) when compared with a decline of Rs. 309 million (11 per cent) in 1982.

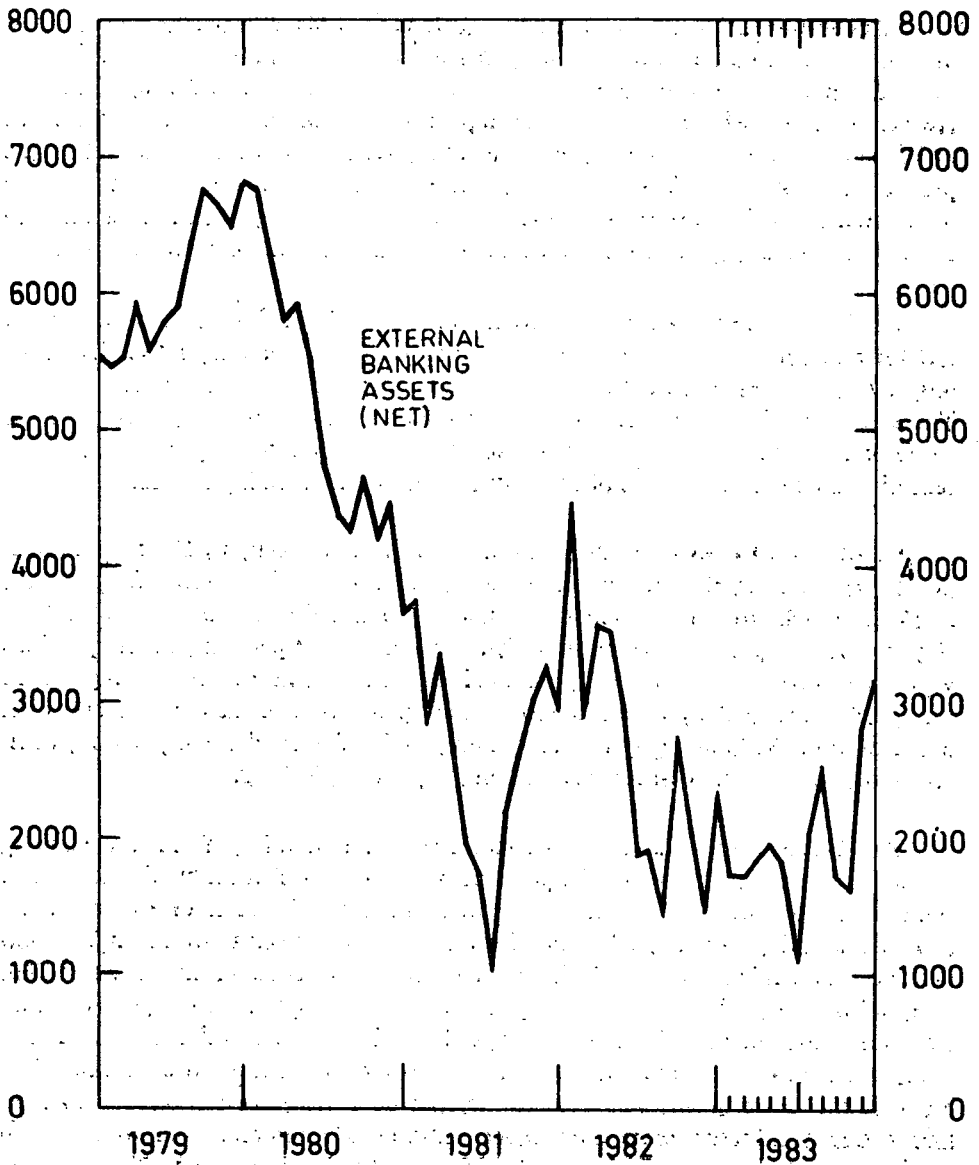
The Government was able to contain its net borrowings from the banking system to a marginal increase of 2 per cent on account of favourable developments, both in the domestic and external sectors. Firstly, utilisation of Central Bank profits amounting to Rs. 1,500 million in March, 1983 reduced Government's dependence on the banking system which was reflected in the reduction in other liabilities (net) of the Central Bank. Secondly, increased subscriptions to rupee securities by captive sources (The National Savings Bank, The Employees' Provident Fund, Sinking Funds etc.) enabled the Government to reduce recourse to bank financing. Thirdly, the Government was able to increase its revenue collection due to high import duties and turnover taxes introduced in early 1983 and on account of increased receipts from tea ad-valorem taxes. Further, a reduction in the capital expenditure and the utilisation of the Japanese Yen loan and the part proceeds of the Euro-Currency loan helped the Government to minimise its borrowings from the banking system.

### EXTERNAL BANKING ASSETS (NET)

MONTHLY

MILLIONS OF RUPEES

MILLIONS OF RUPEES



During the year under review, gross credit to the private sector (comprising government corporations, the co-operatives and the other private sector) rose sharply by Rs. 6,512 million or 26 per cent, when compared with an increase of Rs. 4,070 million or 19 per cent in the preceding year. Of the total increase in gross credit to private sector (GCPS), a major share (95 per cent) was on account of an increase in credit granted to the other private sector constituents (OPSC). Gross credit to this sector rose by 32 per cent when compared with 26 per cent last year. The increase in private sector credit in the first quarter may have been due to increased economic activities following the elections in the latter part of 1982. The increase in demand for credit due to reduction in short term interest rates in mid year was further accentuated by the impact of July disturbances. A delay in the repayments (Rs. 800 million approximately) of loans and advances by some business concerns in the private sector due to the disturbances and the maximum utilization of the approved over-draft limits kept the outstanding credit at high levels. At the same time, there was a delay in the receipt of export proceeds during the third quarter. In addition to the existing loans, the banks were also compelled to provide new loans to the affected business concerns to commence production. The outstanding loans and advances also rose on account of banks stepping in to meet the credit needs of the services sector which were hitherto greatly financed by operations of the Pettah Kerb Market.

There has been considerable pressure on prices during 1983. The Colombo Consumers' Price Index (CCPI) which recorded a moderate increase of 5 per cent (point to point basis) during the 12 month period ended December, 1982 rose by 21 per cent by December, 1983. Meanwhile, the annual average increase in the Index which stood at 11 per cent in 1982 rose to 14 per cent in 1983.

The higher demand for credit was also evident as regards the co-operative institutions which recorded a substantial increase of Rs. 635 million (54 per cent) in contrast to a decline of Rs. 106 million (8 per cent) in 1982. Gross credit to the co-operative sector which rose progressively during the first four months of the year amounting to Rs. 1,001 million (84 per cent) declined only marginally in the subsequent months of the year. The largest monthly increase was in March amounting to Rs. 526 million (37 per cent). The significant increase in credit during the first four months of the year mainly reflected the sharp rise in advances for purchases of paddy under the Guaranteed Price Scheme (GPS) associated with the high level of purchases arising from a successful Maha harvest and the upward revision in the purchase price of paddy under GPS from Rs. 57.50 to Rs. 62.50 per bushel with effect from 1st March, 1983. These developments necessitated a higher level of bank finance to co-operative institutions during the year. A considerable part of co-operative credit was provided to the Paddy Marketing Board (PMB) to meet its higher purchases.

Meanwhile, in contrast to an increase of Rs. 190 million or 4 per cent in 1982, commercial bank credit to government corporations declined by Rs. 292 million (6 per cent) during the year under review. Credit to this sector moved erratically during the year and the largest monthly increases (7 per cent) were recorded in March,



August and September. The decline in credit to this sector was mainly in respect of loans (Rs. 443 million) and import bills (Rs. 289 million). The reduction in bank borrowings by corporations was partly due to the better financial management of certain corporations, substantial inflow of cash from increased sales proceeds and decisions taken by certain corporations to reduce bank borrowings on account of high interest payments. With regard to the Ceylon Petroleum Corporation (CPC) and the Ceylon Shipping Corporation the continuity in the availability of foreign finance reduced their recourse to the domestic banking system. However, borrowings of the Ceylon Electricity Board, the two plantation corporations and the Sri Lanka Cement Corporation remained at high levels during the year.

In 1983, external assets (net) of the banking system rose to a level of Rs. 815 million or 34 per cent when compared with a decline of Rs. 569 million or 19 per cent in 1982. The increase in external banking assets was the outcome of a significant improvement in the country's balance of payments position. The external banking assets, however, showed an erratic behaviour during the year. Of this, the largest monthly increase was in November, 1983. This was mainly due to the purchases of foreign exchange from commercial banks arising from high export proceeds (Rs. 3,948 million), drawings under the IMF Stand-By Arrangement (Rs. 517 million), utilization of the Japanese Yen loan (Rs. 331 million) and part proceeds of the Euro Currency Loan (Rs. 625 million) which raised the holdings of cash and balances abroad of the Central Bank.

### **Commercial Banking**

During the year, commercial banking was characterised by periodic liquidity problems. The liquidity constraints experienced by banks worsened towards the second half of the year. This was primarily caused by an enhanced demand for credit from the other private sector since July, 1983. Credit to this sector which rose by 13 per cent during the first six months of the year, increased by 3 per cent in July and to a further 6 per cent in August which was the highest recorded in any single month in 1983. The sharp rise in credit partly reflected the impact of the downward revision of interest rates effected during the first half of the year. According to commercial bank sources, the high level of credit was also due to lower repayments on the part of the customers who were affected by the July disturbances. The banks also assisted the affected customers by providing fresh credit, extending the maturity periods of loans and lowering the rates of interest on such loans. As revealed by several indicators, liquidity problems became rather acute during the fourth quarter of the year. Due to increased demand for funds, particularly, by foreign banks whose deposit base was narrow, the rates in the inter-bank call money market rose to high levels. These rates which prevailed at a range of 15.75-18.50 per cent per annum at end 1982 rose to a range of 18.5-35.0 per cent per annum by end October and further to 20-37 per cent per annum by end December 1983. Commercial banks also resorted to borrowings from the Central Bank at penal rates to tide over their temporary liquidity problems.

Reflecting the rising demand for credit, the loan/deposit ratio recorded an increasing trend from the beginning of the year. This ratio gradually rose from 0.92 to 0.99 during the first ten months of the year. However, partly due to restrictive monetary measures introduced by the Central Bank the loan/deposit ratio declined to 0.98 and further to 0.93 respectively during the last two months of the year.

The commercial banks continued to attract more deposits, particularly, short-term time and savings deposits during 1983. The preference on the part of commercial banks to attract short term time and savings deposits mirrored the uncertainty in financial circles regarding the future movements of interest rates. Banks also continued to issue Certificates of Deposits (CDs) attracting a fair amount of hoarded money to the banking system. By end 1983, 20 banks had been given formal approval to issue CDs and the outstanding amount of CDs as at the same date amounted to Rs. 610 million. Facilities for encashment of foreign drafts were further widened during the year. The Bank of Ceylon inaugurated a special service for the encashment of such drafts on Saturdays. Meanwhile, the Bank of Credit and Commerce International (Overseas) Ltd. established a Foreign Currency Encashment and Exchange Counter at the Colombo Airport, Katunayake.

Realising the need to expand banking activities to cater to the increasing demand for more sophisticated and complex banking cum financial services, a Merchant Bank with foreign collaboration was established in 1983. This was established as a joint venture of the People's Bank and the Guinness Mahon and Co. Ltd. of London. The People's Merchant Bank in its first year of operation engaged in project identification, project promotion and loan syndication.

The year also witnessed developments in activities of Foreign Currency Banking Units (FCBUs). At end 1983, there were 24 FCBUs operating in Sri Lanka. Their total assets/liabilities rose from Rs. 13,828 million (US \$ 649 million) to Rs. 20,457 million (US \$ 818 million). The operations of the FCBUs mainly included financing projects in the Free Trade Zone, Euro Currency lending to approved residents and provision of foreign currency guarantees on behalf of customers.

Total resources of commercial banks rose by Rs. 10,188 million in comparison to an increase of Rs. 7,438 million in 1982. Similar to the trends observed in the preceding year, a substantial part of the resource growth in 1983 amounting to Rs. 6,373 million was on account of an increase in all types of deposits. This increase consisted of increases in time and savings deposits (including long term deposits of the two state banks) and demand deposits by Rs. 4,576 million and Rs. 1,797 million, respectively. In 1983, borrowings of commercial banks rose by Rs. 1,624 million. This consisted of increases in interbank borrowings amounting to Rs. 1,121 million (including borrowings from the Central Bank) and foreign borrowings (Rs. 503 million). During the year, borrowings of commercial banks from the Central Bank rose by Rs. 1,462 million reflecting mainly the increase in facilities granted under various refinance schemes.

**TABLE 1.52**  
**Changes in Commercial Banks' Resources and their Utilization**

Sector	Rs. Million	
	End 1981/ End 1982	End 1982/ End 1983
1. Government .. .. .	— 51.4	278.0
2. Central Bank .. .. .	— 315.0	— 41.6
3. Government Corporations .. .. .	1,416.7	532.3
4. Co-operative Institutions .. .. .	127.9	— 527.5
5. Other Private .. .. .	— 719.7	— 1,018.3
6. Inter Bank .. .. .	— 108.9	1,243.8
7. Foreign .. .. .	— 349.6	— 466.7

*Source* : Central Bank of Ceylon.

*Note*: Minus sign indicates net utilization of resources.

Table 1.52 presents the changes in commercial banks' resources and their utilization on a net basis. During 1983, the other private sector emerged as the major user of commercial bank resources utilizing a sum of Rs. 1,018 million. The utilization of bank resources by co-operative institutions also has been at a high level of Rs. 528 million largely reflecting the increases in Goods Receipt advances granted to the Paddy Marketing Board for the purchase of paddy. In contrast to the trend observed in the previous two years the Government sector made a net contribution of Rs. 278 million towards the resource build-up of commercial banks. Meanwhile, the Central Bank absorbed a net amount of Rs. 42 million from commercial banks by way of increased reserve requirements. The transactions in the foreign sector too utilized commercial bank resources to the tune of Rs. 467 million mainly on account of an increase in foreign balances including export bills.

### Bank Branch Expansion

In 1983, commercial banks opened 16 new branches. This was made up of 11 new branches opened by the Bank of Ceylon, 3 by the People's Bank and 1 each by the Commercial Bank of Ceylon Ltd. and Hatton National Bank Ltd. With the opening of these branches, the total number of commercial bank branches stood at 1,034 (including Agricultural Service Centre branches, pay offices, extension offices, Kachcheri branches and overseas branches), at the end of the year. Meanwhile, as in the previous year, the Bank of Ceylon relocated seven of its Agricultural Service Centre (ASC) branches for security and economic reasons thus making a total of 311 relocations by end 1983. The main branches of commercial banks stood at 600, while the operating ASC branches amounted to 79 by the end of the year.

The National Savings Bank (NSB) opened three branches thus bringing the total number of its branches to 50 at the end of the year. Meanwhile, the representative office of the Bankers Trust Company, New York which was given approval in 1982 commenced operations in 1983. This was the second representative office opened by foreign banks in Sri Lanka.

### Interest Rates

The third major interest rate reform effected in August 1981 continued to be in force throughout 1982 but certain marginal revisions were effected in 1983. Compared with the high rates of price increases in 1980/81, a certain stability in the movement of monetary aggregates and prices was observed in 1982 and early 1983. These developments afforded an opportunity for the Central Bank to review its interest rate policy and introduce modifications where necessary to take account of specific needs. With the focus on export-led growth it became necessary to provide concessional credit to the export sector. It was felt that the high interest rate policy pursued for demand management purposes had some unfavourable effects on the working capital requirements of priority sectors due to the high cost of credit. Therefore, with a view to increasing production, certain interest rate changes were effected allowing priority sectors to obtain credit at low cost.

As a part of this policy package the Central Bank initiated a downward movement in short term interest rates. With effect from 24th March 1983, the Central Bank reduced the Bank rate from 14 to 13 percent per annum. The penalty rate structure was reduced from a range of 21-30 percent per annum to a flat rate of 20 per cent per annum on 30th March, 1983.

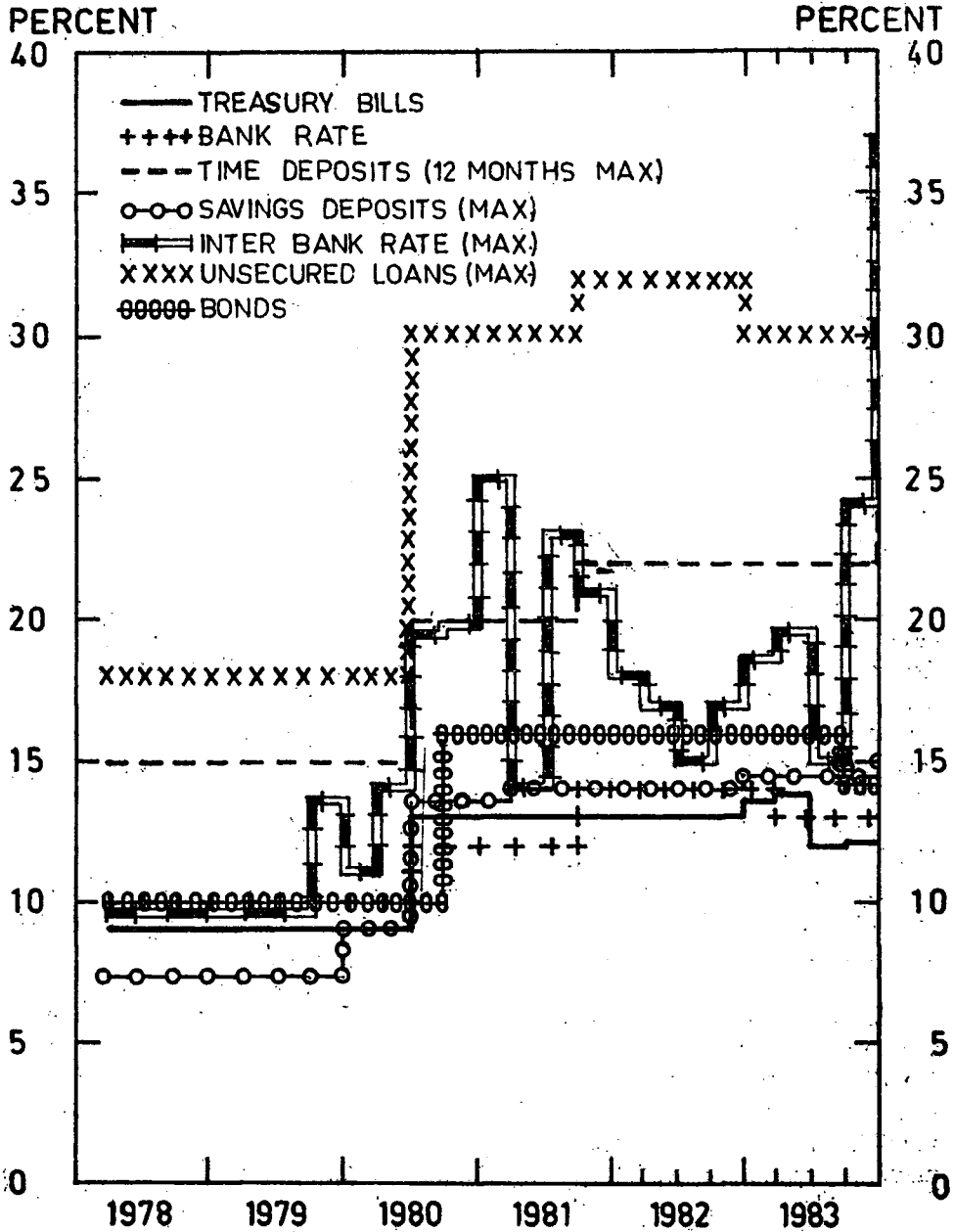
These measures were expected to bring down the cost of funds of commercial banks with respect to their borrowings from the Central Bank thereby enabling them to provide cheaper credit to priority areas.

In addition, several changes were also effected to accelerate the flow of credit to priority sectors, particularly, to the export sector. Thus the rate of interest on Central Bank refinance to commercial banks on pre-shipment export credit was reduced from 12 to 11 per cent per annum in March and further to 10 per cent per annum in June, 1983. The on-lending margin of 4 per cent was also reduced to 3 per cent along with the downward revision of rates. The interest rate on the supplementary export credit refinance facility for non-traditional exports was revised downward from 8.5 per cent to 7 per cent per annum with effect from March, 1983. The interest rates applicable on loans granted under all categories of the Medium and Long Term Credit Fund (MLCF) were also reduced by 1 per cent in March and the on-lending margin permitted to credit institutions under category III and IV was reduced from 5 per cent to 4 per cent per annum in April, 1983.

Effective April, 1983 the National Savings Bank (NSB), the major competitor of the commercial banks for time and savings deposits reduced its fixed deposit rates from 20 to 18 per cent per annum on one year deposits on which interest was paid at maturity (from 18.6 per cent to 16.8 per cent in the case where interest was paid monthly) and from 15 to 14 per cent on six month deposits. The NSB also discontinued the practice of accepting 24 months fixed deposits.

Following the reduction in the general interest rate structure, certain long term lending institutions also made downward revisions in their lending rates in June, 1983. The Development Finance Corporation of Ceylon (DFCC) reduced its

### INTEREST RATES END QUARTERLY FIGURES



interest rates on all industrial project lendings from 17 to 14 per cent per annum excluding projects entitled for concessionary finance under the refinance schemes. The new rates came into effect since June, 1983. Meanwhile, the National Development Bank of Sri Lanka (NDB) reduced its interest rates on direct lendings from 17 to 14 per cent per annum while the rates applicable on small and medium term industrial projects were reduced from 20 to 14 per cent per annum in June, 1983.

The changes in the interest rate structure during the second half of 1983 were mainly influenced by the policy measures introduced during the first half of the year. Following the downward revision of the interest rate structure in the first half, the two state banks reduced their interest rates on advances by a range of 1-4 per cent in July 1983. In addition, the Bank of Ceylon reduced the interest rates on 12 months fixed deposits from 18 to 16 per cent on deposits on which interest is payable at maturity and from 16.8 to 14.5 per cent on deposits where interest is payable monthly. Along with these revisions, for the first time a monthly interest payment system on six months fixed deposits was introduced at 12.5 per cent per annum.

Resulting mainly from the reduced cost of funds the demand for credit and hence the outstanding credit of the private sector rose to considerably high levels in the latter part of the year. Consequent on the monetary policy measures effected by the Central Bank during the last two months of 1983, the rates on deposits and lendings of some commercial banks and the call money market rose at the end of 1983 reflecting a higher demand for credit, thus exerting pressure on the prevailing interest rate structure.

The interest rates offered in the call money market dropped from a range of 15.75-18.5 per cent per annum in December, 1982 to a lower range of 11.5-15.0 per cent per annum by mid 1983 reflecting the lower demand for short term funds by commercial banks. A high credit demand in the second half of 1983 reduced the liquidity of banks and hence the call money market rates rose to a higher range of 20-37 per cent per annum by the end of the year.

The Treasury bill rate in the primary market was reduced from 13.5 to 12 per cent per annum in May, 1983. Meanwhile, the discount rate in the secondary Treasury bill market (Central Bank's selling rate) was reduced from 12.25 per cent per annum in December, 1982 to 12 per cent per annum in June, 1983. The rediscount rate (Central Bank's purchasing rate) was increased from 13.25 per cent per annum in December, 1982 to 13.75 per cent per annum in March, 1983 and gradually moved downwards to remain at 12.50 per cent per annum at end 1983.

The interest rate on Government Securities was also revised downward from 16 to 14 per cent per annum in July, 1983 together with an extension of the maturity period from 3 to 5 years.

### Central Banking

The total assets/liabilities of the Central Bank of Ceylon as at end December, 1983 amounted to Rs. 33,097 million representing an increase of 10 per cent over the previous year. On the assets side, the largest increases were reflected in all categories of domestic assets while the increases in external assets were marginal.

The increase of Rs. 2,941 million in domestic assets was largely on account of short-term advances granted to commercial banks (Rs. 1,528 million). This revealed the extent of utilization of export credit refinance facilities which were enhanced by the Central Bank during the first half of 1983 and the continuation of the marketing refinance facilities. In addition, holdings of government and government guaranteed securities mainly, Treasury bills (Rs. 738 million), loans and advances to the Government (Rs. 654 million) and Medium and Long - term refinance loans to commercial banks and other credit institutions also recorded notable increases over the previous year. However, net credit to Government (NCG) increased only by a marginal amount due to the substantial build up of deposits by the Government towards the closing months of the year.

The increase in the International Reserve (IR) amounting to Rs. 150 million was the combined effect of increased investments on foreign securities (Rs. 494 million) and a drop in holdings of Special Drawing Rights (Rs. 128 million) and cash and balances abroad (Rs. 216 million). Utilization of the Japanese Yen loan (Rs. 331 million) also resulted in an increase in the net international reserve of the Central Bank. The drop in cash and balances abroad was mainly due to the repayments under the Standby Loans, payments of service charges on IMF borrowings and other settlements. The category of other assets and accounts also recorded a decline (Rs. 162 million) during the year.

On the liabilities side, the increase was mainly due to the increased amount of deposit liabilities (Rs. 1,757 million) and currency in circulation (Rs. 1,317 million). The significant increase in deposit liabilities was largely on account of enhanced reserve requirements effected since mid December, 1983. This was further augmented by the introduction of a new reserve requirement of 16 per cent on unused balances of overdrafts held by the private sector with the commercial banks. Marginal increases were reported in borrowings abroad (Rs. 22 million) and capital accounts (Rs. 1 million). The decline in the other liabilities and accounts during the year was the result of transferring profits from the Central Bank to the Government.

### The National Credit Plan—1983

With the 1983 National Credit Plan Sri Lanka entered into its third successive year of credit planning. As in the two previous years the credit plan dealt with commercial bank lendings to the private sector including public corporations. The plan also emphasized the provision of sufficient credit for on-going economic activities in the economy. Accordingly, the two major objectives of the 1983 Credit Plan were in the first place to make available the necessary credit facilities to the

vital and growing sectors of the economy by rationalising the availability of bank credit to the private sector and secondly to identify the direction of credit and divert more credit to priority areas.

As in the previous two credit plans the monetary targets were estimated taking into account the projected real growth, the rate of inflation and the new monetisation in the economy. The monetary targets were then translated into a permissible level of credit in the economy having taken into consideration the developments that are likely to occur in the external sector. After allowing for the credit requirements of the Government, the balance resources were allocated to the private sector.

Accordingly, the outstanding credit to the private sector was estimated at Rs. 31,408 million by end 1983. This represented an increase of 24 per cent over the level that prevailed at end 1982. Agriculture, industry and export sectors continued to be priority areas in the sectoral allocation of credit. Credit allocation to the agriculture sector was Rs. 3,902 million which represented an increase of 26 per cent over the previous year. The industrial sector was allocated Rs. 8,041 million which indicated an increase of 22 per cent during the planned year. The export sector was considered the most vital sector in the 1983 credit plan and the outstanding credit to this sector was projected to be at Rs. 4,414 million, an increase of 30 per cent. The sectoral allocation of credit to the export and industrial sectors which stood at 25 and 13 per cent at end 1982 was raised to 26 and 14 per cent, respectively, in the 1983 credit plan. The share of the agriculture sector remained constant at 12 per cent. The outstanding credit for import purposes was estimated to be at Rs. 4,157 million providing an increase of 9 per cent over the last year.

Quarterly allocations of credit were made after allowing for the seasonal variations associated with sectoral credit. Sector-wise, actual performance has been on line with targets set by the plan. The actual total credit level deviated marginally (1.5 per cent) from the planned targets.

### **Monetary Policy**

The degree of monetary and price stability achieved during 1982 called for a moderation in the restrictive monetary policy measures introduced in the early part of 1983. The new policy measures introduced in the first part of 1983 mainly aimed at mitigating the adverse effects of high interest rates on activities of the priority sectors and stimulating growth in the economy. Accordingly, the Central Bank initiated a downward revision in the short term interest rates with a view to introducing a certain degree of flexibility in the interest rate structure, thereby enabling it to adjust to the changing economic conditions.

As a first step, the Central Bank reduced the Bank rate from 14 to 13 per cent per annum with effect from 24th March, 1983. Along with this revision, the penal rate structure that prevailed in the range of 21-30 per cent per annum was replaced with a flat rate of 20 per cent per annum with effect from 30th March, 1983. The downward revisions were designed to enable commercial banks to lower their lending rates.



In addition to these changes, several positive measures were taken to accelerate the flow of credit to the priority areas particularly, the export sector. Accordingly, effective 24th March, the rate of interest on Central Bank refinance to commercial banks on pre-shipment export credit was reduced from 12 to 11 per cent per annum. In the case of medium and long term refinance facilities, the interest rates on all categories of the Medium and Long-term Credit Fund (MLCF) were reduced by 1 percentage point. In addition to these concessions, the Central Bank introduced a supplementary refinance facility on 16th March, 1983 with a view to catering to the needs of the non-traditional export sector (excluding petroleum products, garments, gems and marine products). At the inception of the scheme, the Central Bank discounted promissory notes executed by exporters and tendered to commercial banks at 8.5 per cent per annum while commercial banks were allowed to rediscount at a rate not exceeding 12 per cent per annum. Effective 24th March, 1983, the discount rate was reduced to 7 per cent per annum while commercial banks were permitted to rediscount promissory notes at 11 per cent per annum. The latter was further reduced to 9.75 per cent per annum with effect from 9th June, 1983. However, in the case of promissory notes pledged with banks by way of security for pre-shipment advances, the applicable interest rate was prescribed at 10.80 per cent per annum. The scope of this scheme was expanded in July 1983, to include certain categories of marine, rubber and coconut products and again in October to include the re-export of diamonds. Another important step taken by the Central Bank for the promotion of the export sector was the establishment of an Export Credit Cell (ECC) within the Central Bank with the objective of considering representations of exporters on problems in connection with export finance, in particular, and export development, in general. The ECC is expected to examine representations made by the exporter community and attempt to find appropriate solutions to their problems.

Effective 20th April, 1983, the extent of refinance granted for the promotion and development of exports under category II of the MLCF was reduced from 100 to 70 per cent in order to bring the scheme in line with the cost of medium and long term funds offered by foreign agencies. Meanwhile, the on lending margin permitted to credit institutions under category III and IV of the MLCF was reduced from 5 to 4 per cent per annum.

In May 1983, the terms and conditions for the issue of rupee securities were revised and the maturity period of new issues was increased from 3 to 5 years while the rate of interest was reduced from 16 to 14 per cent per annum.

In order to provide further relief to the export sector the Central Bank decided to enhance the limit on the total amount of refinance granted to commercial banks from Rs. 590 million to Rs. 1,200 million with effect from 1st June, 1983. Along with this revision, with the objective of reducing the cost of credit at the pre-shipment stage, the Central Bank reduced the refinance rate on pre-shipment export credit from 11 per cent to 10 per cent while the on-lending margin permitted to commercial banks was also reduced from 4 to 3 per cent per annum. With effect from 22nd September, the overall limit for export credit refinance was further increased by 10 per cent.

