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இலங்கை மத்திய வங்கி
CENTRAL BANK OF SRI LANKA

MARKET OPERATIONS REPORT

December 2025

CENTRAL BANK OF SRI LANKA

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Overview

In accordance with the provisions of the Central Bank of Sri Lanka Act, No. 16 of 2023, monetary policy in Sri Lanka is conducted within a Flexible Inflation Targeting (FIT) framework, supported by a flexible exchange rate regime. Under the FIT Framework, the Central Bank of Sri Lanka (the Central Bank) conducts monetary policy with the objective of maintaining domestic price stability by maintaining the quarterly headline inflation rate at 5 per cent.

The Central Bank achieves price stability primarily through adjusting the Overnight Policy Rate (OPR) and conducting Open Market Operations (OMOs). The Central Bank deploys these policy instruments to manage liquidity conditions in the banking system and guide short-term interest rates along a desired path.

Following the transition from a policy rate corridor framework to a single policy rate mechanism in November 2024, the OPR is the primary monetary policy instrument of the Central Bank, serving as the key signaling tool of the monetary policy stance. Within the current operating framework, the Average Weighted Call Money Rate (AWCMR) functions as the operating target, where monetary operations are calibrated to maintain the AWCMR at or closer to the announced level of OPR. Reflecting the prevailing monetary policy stance and market conditions, movements in short-term market interest rates are transmitted to the broader economy through the financial system, ultimately influencing growth and inflation outcomes in the economy.

The Central Bank maintains a flexible exchange rate regime, allowing the exchange rate to be determined by demand and supply conditions in the domestic foreign exchange market. The Central Bank does not aim to maintain a specific level or path of the exchange rate, but allows the exchange rate to act as an automatic stabiliser of the economy.

While allowing market forces to determine the exchange rate, the Central Bank intervenes in the domestic foreign exchange market to curtail excessive volatility of the exchange rate, when required. Such interventions are not intended to influence the path of the exchange rate, but prevents disorderly adjustments in the exchange rate, which also affects price stability.

Further, the Central Bank intervenes to purchase foreign exchange from the domestic foreign exchange market to augment foreign reserves of the Country. In addition to these foreign exchange operations, the Central Bank also executes foreign exchange swap transactions to facilitate banks in addressing their liquidity positions and hedging requirements. These transactions also affect the foreign reserves and rupee liquidity conditions.

‘The Market Operations Report (MOR) - December 2025’ summarises key policy measures, liquidity trends, short-term interest rate and exchange rate movements, money market and domestic foreign exchange market operations, particularly focusing the second half of 2025. The MOR also presents two feature articles on the role of the money market for effective monetary transmission and reforms to the current Statutory Reserve Requirement (SRR) Framework in Sri Lanka.

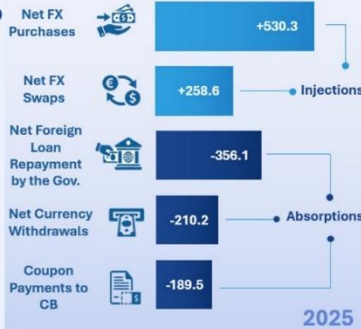
Snapshot of the Monetary Operations and Market Dynamics

Money Market Trends

Central Bank Liquidity (Weekly average/ Rs. bn)



Key Factors Contributed to Change in Central Bank Liquidity (Rs.bn)



Money Market remained in a continued surplus throughout 2025...

...AWCMR picked up in the 2nd half 2025, but was reversed in January 2026

Liquidity Distribution

A persistent asymmetry in liquidity distribution was observed in 2025

Domestic Banks



Domestic banks showed a mixed liquidity condition

Foreign Banks



Major foreign banks held the largest share of liquidity

Standalone Primary Dealers



Liquidity of Standalone Primary Dealers improved

Reserve Money & Currency in Circulation

2025 : Rs. 1,796.5 bn | Growth : 17% y-o-y



Reserve Money grew notably

2024 : Rs. 1,539.3 bn | Growth : 16% y-o-y

2025 : Rs. 1,568.9 bn | Growth : 15% y-o-y

Currency in Circulation (CIC) increased

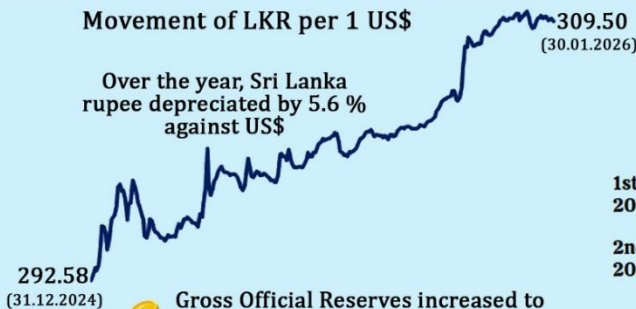


2024 : Rs. 1,358.7 bn | Growth : 15% y-o-y

Exchange Rate Movements, FX Intervention and Gross Official Reserves

Movement of LKR per 1 US\$

Over the year, Sri Lanka rupee depreciated by 5.6 % against US\$



Gross Official Reserves increased to

US\$ 6.8 bn by end of 2025

(with PBOC swap proceeds of US\$ 1.4 bn)

CBSL FX Intervention on Value Date Basis (US\$)

Purchases



1.1 bn

Sales



0.06 bn

Net Absorption
US\$ **2.0 bn**

1st Half 2025

2nd Half 2025

1.0 bn

0.05 bn

Net foreign exchange purchases of **US\$ 2 bn** helped gross official reserves to reach **highest level since crisis**

Highlights

- The Central Bank maintained an accommodative monetary policy stance throughout 2025. Accordingly, the Central Bank further eased the monetary policy stance in May 2025 by reducing the OPR by 25 basis points with the view to steering inflation towards the targeted level.
- Reflecting relaxed monetary conditions, overall liquidity position of the domestic money market remained in surplus throughout 2025, primarily reflecting substantial foreign exchange purchases of the Central Bank undertaken to strengthen the foreign reserve position of the Country. However, liquidity surplus of the money market was partly absorbed through foreign loan repayments of the Government, coupon payments to the Central Bank on account of its Treasury bonds holdings, as well as due to increased currency withdrawals of banks from the Central Bank throughout 2025.
- Similar to the first half of the year, the Central Bank did not intervene in the domestic money market through its OMOs, even during the second half of 2025.
- While the AWCMR broadly hovered closer to the OPR during the first half of 2025, somewhat tightened liquidity conditions in the second half, and the concentration of liquidity within certain banks resulted in the AWCMR to increase from mid July 2025. As this deviation was considered tolerable, the Central Bank refrained from providing additional liquidity to tame the uptick in short-term rates. The AWCMR realigned with the OPR in January 2026.
- During the second half of 2025, reflecting demand and supply conditions, the Sri Lanka rupee depreciated modestly against the US dollar, continuing the trend observed during the first half of the year. While the rupee gradually depreciated against the US dollar during 2025 compared to end 2024, some intermittent volatility was observed in certain periods, stemming from domestic developments and external dynamics.

- The Central Bank intervened in the domestic foreign exchange market during the second half of 2025 as well to purchase foreign exchange in order to build foreign reserves amidst multiple challenges. When required, the Central Bank also intervened to curtail undue volatility in the exchange rate by way of supplying foreign exchange in order to ensure smooth functioning of the market.

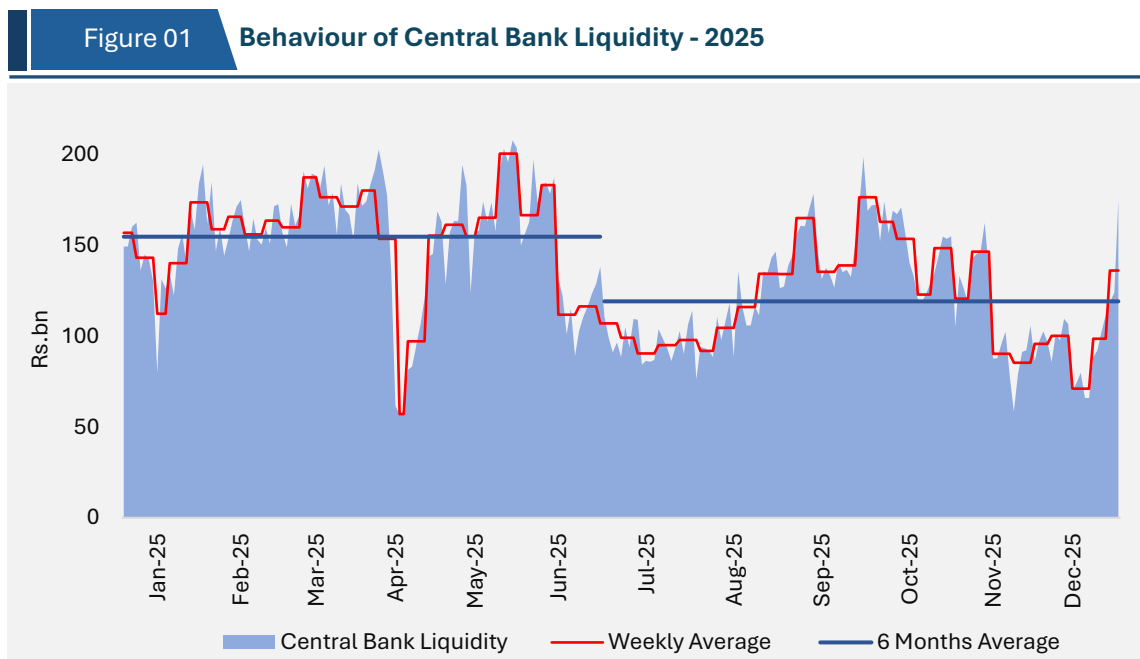
Monetary Policy Stance and Exchange Rate Policy

- Continuing the accommodative monetary policy stance that was in place since mid-2023, the Central Bank further eased monetary policy, and reduced the OPR in May 2025 by 25 basis points to 7.75 per cent. Consequently, the SDFR and SLFR, which form a symmetric margin of ± 50 basis points around the OPR, were revised to 7.25 per cent and 8.25 per cent, respectively. Supported by the relaxed monetary policy stance, short-term market interest rates also declined, with the AWC MR largely hovering around the OPR during the first half of 2025 and reaching 7.75 per cent by end-June 2025. A divergence between the AWC MR and OPR was observed from mid July 2025, which persisted throughout the second half of the year, reflecting tighter liquidity conditions and concentration of liquidity within certain banks.
- The Central Bank allowed money markets to operate amidst a sizeable liquidity surplus, and abstained from injecting further liquidity to the money market through monetary operations.
- The Central Bank operated a flexible exchange rate regime, allowing the exchange rate to be determined by market forces in the domestic foreign exchange market. Accordingly, the Sri Lanka rupee recorded a modest depreciation of 3.1 per cent against the US dollar during the second half of the year, thereby recording an overall depreciation of 5.6 per cent against the US dollar during the year.

- The Central Bank intervened in the domestic foreign exchange market to augment foreign reserves during opportune times, while curtailing excessive volatility in the exchange rate. On value date basis, the Central Bank reported a total net purchase of US dollars 2.0 billion during the year 2025, despite challenges stemming from external sector developments and domestic market dynamics mainly driven by import related demand and global uncertainties. Net purchases of foreign exchange by the Central Bank have helped the Country’s gross official reserves to reach US dollars 6,827.2 million¹ by end 2025, which is the highest level of reserves recorded during the post crisis period.

Movements in Central Bank Liquidity

- Central Bank liquidity remained consistently in surplus throughout 2025, though some fluctuations were observed from time to time².



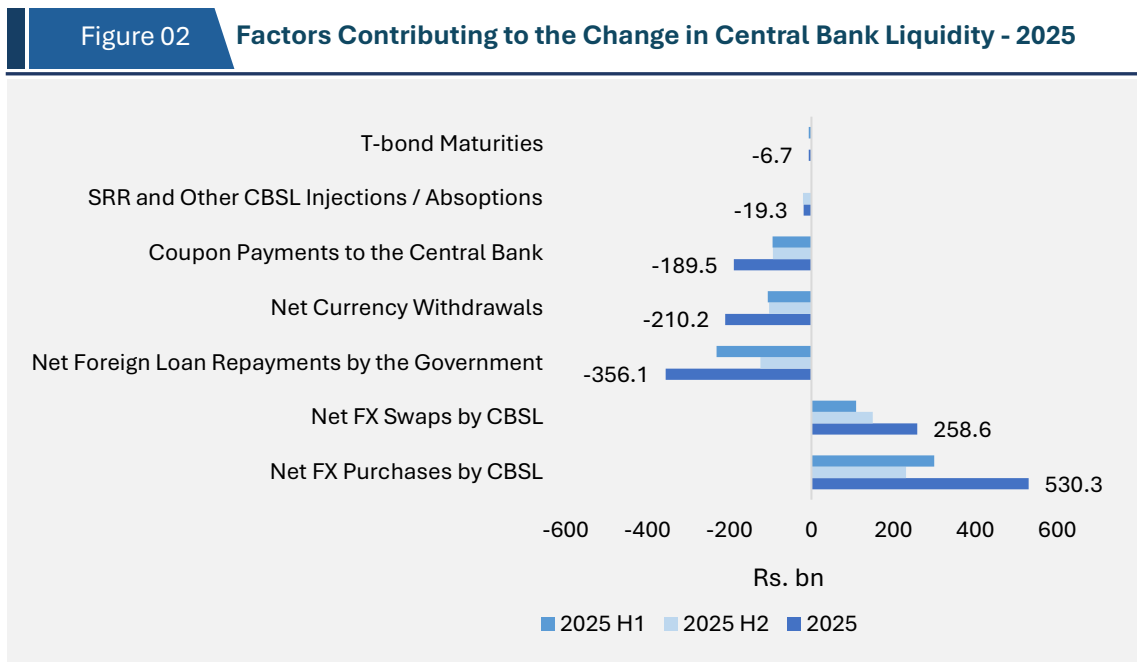
Source: Central Bank of Sri Lanka

¹ This includes People’s Bank of China (PBoC) swap facility equivalent to US dollars 1.4 billion as at 31.12.2025.

² Surplus central bank liquidity refers to the amount of reserves held in reserve accounts of LCBs exceeding the reserves maintained under the statutory reserve requirement (SRR).

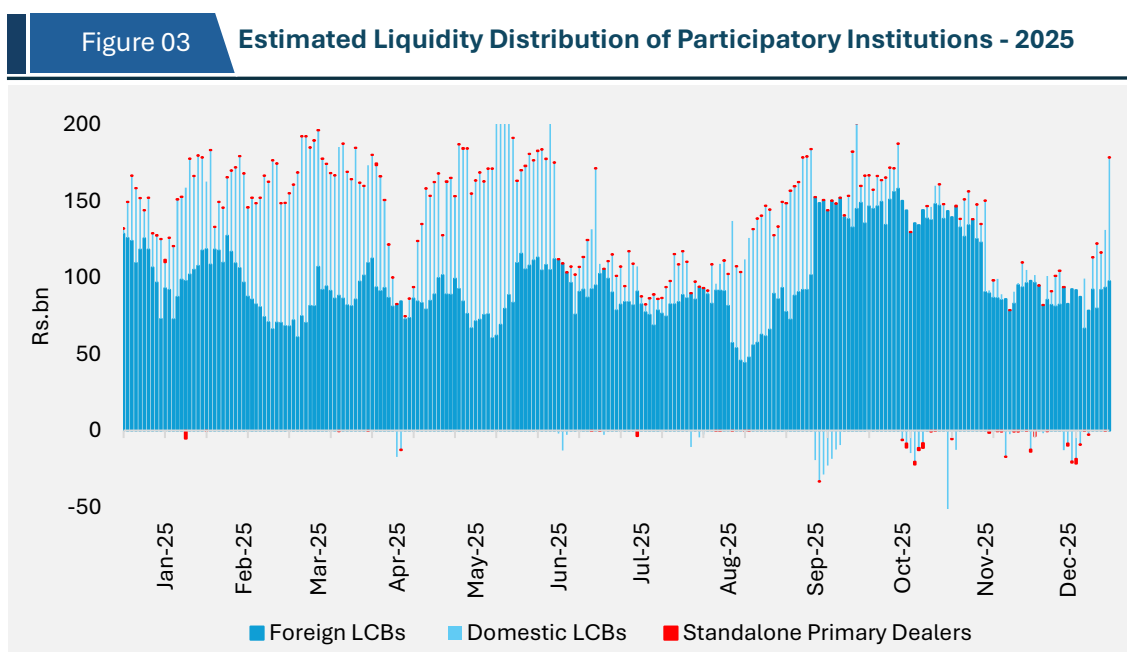
As at end 2025, liquidity surplus stood at Rs. 175.2 billion compared to Rs.168.1 billion reported by end 2024. On average, the liquidity surplus amounted to Rs.119.2 billion during the second half of the year 2025, compared to Rs. 154.6 billion recorded in the first half of the year 2025.

- Surplus liquidity conditions in 2025 were mainly supported by net foreign exchange operations of the Central Bank with banks. Accordingly, foreign exchange purchases and swap transactions contributed to injecting rupee liquidity amounting to approximately Rs. 788.9 billion, on a net basis. However, liquidity in the domestic money market was partially absorbed by factors such as net foreign loan repayments by the Government utilising foreign exchange obtained from the Central Bank amounting to Rs. 356.1 billion, net currency withdrawals of around Rs. 210.2 billion and the coupon payments to the Central Bank of around Rs.189.5 billion on account of its holdings of Treasury bonds.



Source: Central Bank of Sri Lanka

- In terms of the liquidity distribution, a larger share of liquidity was concentrated with the main foreign banks, leading to an asymmetry in liquidity distribution. In contrast, state banks' liquidity level declined during the latter part of the year 2025 owing to the increase in government funding requirements resulting from relief measures related to *Cyclone Ditwah*, while the liquidity level of domestic private banks somewhat improved. In comparison to deficit liquidity observed in 2024, liquidity positions of Standalone Primary Dealers (SPDs) improved throughout the year 2025. Nevertheless, on average, liquidity conditions of SPDs remained in a marginal deficit during the year 2025.
- The asymmetry in liquidity among participants amidst somewhat tighter liquidity conditions and fragmented interbank participation exerted some upward pressure on AWCMR during the second half of the year 2025. Nevertheless, as the upward pressure on short-term interest rates was tolerable, the Central Bank did not inject additional liquidity to the market through monetary operations.



Source: Central Bank of Sri Lanka

Importance of the Money Market in the Monetary Policy Implementation

Financial markets play a pivotal role in the implementation of monetary policy, as policy measures are primarily executed through operations conducted within these markets. Central banks carry out monetary policy by operating in financial markets, rather than dealing directly with households or businesses. Accordingly, the effectiveness of monetary policy transmission to the real economy depends critically on the structure, depth, and efficiency of the financial system, particularly the degree of development, and smooth functioning of financial markets. Among such financial markets, the money market occupies an important role, as the main channel through which a central bank designs, implements, and translates on its policy decisions to the rest of the economy.

A central bank influences short-term money market interest rates by using tools such as Open Market Operations (OMO), Standing Facilities, and other liquidity management instruments. By doing so, a central bank effectively controls the amount of money/liquidity available in the banking system, which then affects borrowing, spending, and investment in the wider economy, which ultimately affects aggregate demand, enabling the central bank to achieve the price stability objective in line with its mandate.

Role of Money Market Rates as the First Step of Transmission

In Sri Lanka, the Central Bank conducts monetary policy by influencing short-term interest rates in the money market. The key operational tool used in this process is the Average Weighted Call Money Rate (AWCMR), which reflects the average cost at which banks lend to and borrow from each other on an overnight basis in the uncollateralised interbank money market. The Central Bank guides the AWCMR to move closer to the Overnight Policy Rate (OPR) through liquidity management operations. These operations include OMOs through repurchase (repo) and reverse repo transactions, and the use of standing facilities. By injecting liquidity to the banking system or absorbing excess liquidity, the Central Bank ensures that short-term interest rates remain aligned with its monetary policy stance.

Once money market rates respond to policy actions, the impact translates to other short-term interest rates in the economy. In particular, movements in the AWCMR influence short-term interest rates such as treasury bill yields, repo rates, prime lending rates, etc., which serve as key benchmarks for pricing of financial instruments and cost of credit across the financial system. Over time, the movements in short-term rates are transmitted on to retail and longer-term interest rates, including bank deposit rates and lending rates.

Changes in lending rates directly affect borrowing costs faced by businesses and households,

thereby influencing investment and consumption decisions. Low interest rates tend to stimulate credit expansion and economic activity, while high rates lead to moderate or discouraged borrowing and spending. Similarly, the movements in deposit rates shape saving behaviour, thus reinforcing transmission of monetary policy to the real economy. Through these channels, money market interest rates ultimately affect aggregate demand and inflation. Accordingly, when money market rates closely follow the monetary policy stance, monetary policy signals are transmitted effectively and promptly across the financial system, making monetary policy more impactful in achieving price stability.

Structure of the Domestic Money Market in Sri Lanka

The domestic money market in Sri Lanka consists of several institutions that help manage short-term funding and liquidity in the financial system. The main participants in Sri Lanka's domestic money market are Licensed Commercial Banks (LCBs) and Standalone Primary Dealers (SPDs). These institutions actively engage in borrowing and lending transactions to manage liquidity positions, comply with regulatory requirements, and support smooth settlement of financial obligations. Accordingly, they play a vital role in ensuring efficient circulation of funds across the financial system and supporting effective transmission of monetary policy.

LCBs use several financial instruments in the domestic money market to manage short-term liquidity requirements. One of the most important avenue is the interbank money market transactions (also known as call market), where LCBs lend and borrow funds from each other on an unsecured basis, usually on overnight basis or for very short periods. This market enables banks to address temporary liquidity mismatches arising from payment flows and need for maintaining reserve requirements. Repo transactions, which are secured lending and borrowing arrangements where government securities are used as collateral, are also used by market participants to fulfill their requirements.

At the same time, certain money market instruments, including Commercial Papers (CP), continue to be less attractive. Limited market depth, low issuance volumes, and constrained participation have restricted their effectiveness in contributing to liquidity management. As a result, these instruments have yet to play an impactful role in strengthening money market activities in Sri Lanka.

Scope for Market Developments

At present, the Sri Lankan interbank market remains segmented, resulting in liquidity imbalances across market segments due to reserve hoarding and zero or limited counterparty exposures stemming from stringent liquidity risk management measures imposed by parent companies.¹, As a consequence, the interbank market remains relatively shallow, impacting transaction volumes and interest rate dynamics. Though the Central Bank relies on the interbank market to influence short-term interest rates, such segmentation disrupts the flow of funds and poses an impact the effectiveness of monetary policy tools, therefore hindering smooth transmission of monetary policy.

In this context, enabling active participation of foreign banks in the money markets remains important for deploying idle funds in the market. Accordingly, measures are required to address prevailing liquidity distribution asymmetries, including the activation and deepening of the repo market, the standardization of repo documentation and related market practices in line with international norms, and the development and promotion of other money market instruments. Further, the availability of a dedicated electronic platform for matching and executing money market transactions could result in reduced reliance on manual and fragmented processes for trade execution, confirmation, clearing, and settlement. This will also improve operational efficiency, and promote market discipline. Collectively, these measures would enhance certainty and market confidence, strengthen risk management practices, encourage wider market participation, and support the overall development, resilience, and stability of Sri Lanka’s domestic money market.

Conclusion

Sri Lanka’s money market plays a critical role in the Country’s financial system by providing mechanisms for short-term liquidity management, serving as a channel for monetary policy transmission, and creating dynamics of the interest rates structure. However, for the market to reach its full potential, several constraints must be addressed, including reducing market segmentation, improving financial market infrastructure, and diversifying the base of participants and instruments. Addressing existing structural and infrastructural gaps would facilitate more transparent price discovery, improve the allocation and distribution of liquidity, and better align the domestic money market with international best practices, thereby supporting the Country’s broader macroeconomic and financial stability objectives.

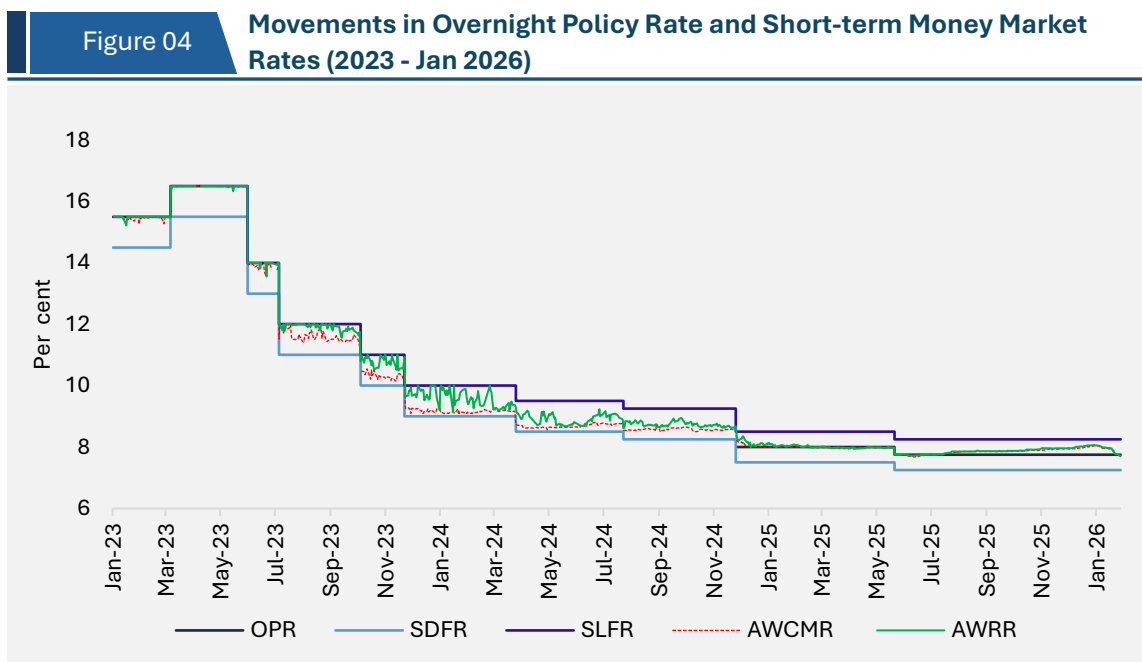
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¹ Interbank market segmentation refers to the division of the interbank market into distinct segments based on various factors such as participant types, credit quality, transaction size, etc.

Movements in Short-Term Interest Rates

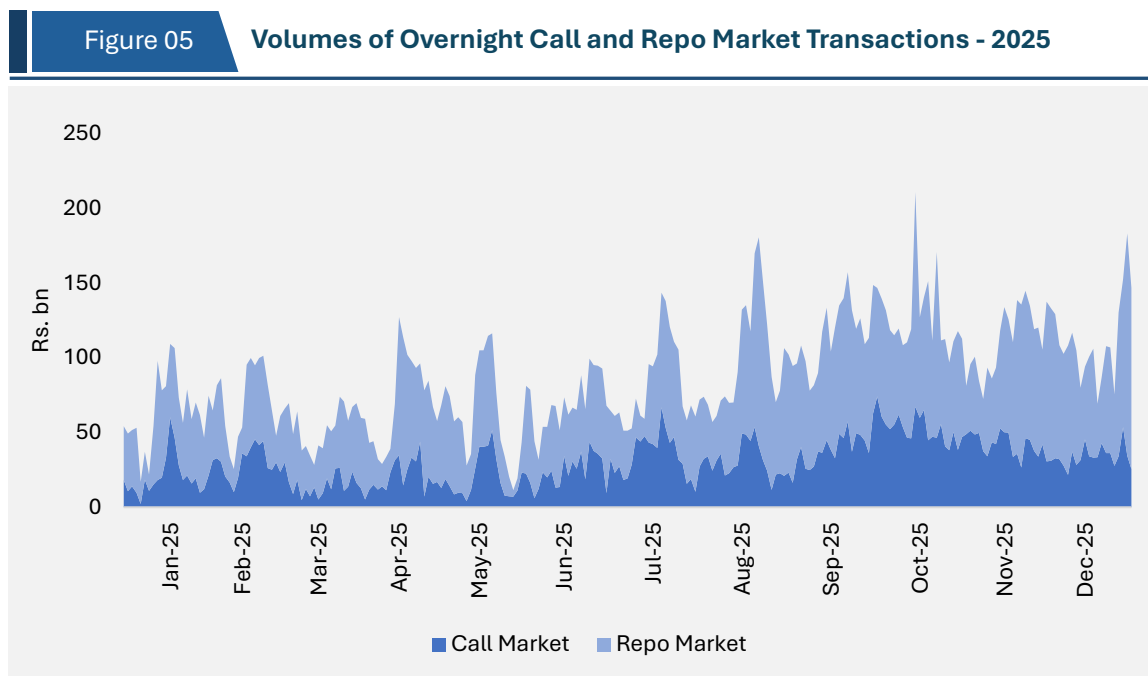
- The overall interest rate structure broadly remained low in 2025, benefiting from the accommodative monetary policy stance of the Central Bank. In terms of market interest rates, both AWCMR and Average Weighted Repo Rate (AWRR) remained broadly aligned with the OPR until mid July 2025, although money market interest rates gradually picked up in the subsequent months due to asymmetry in liquidity conditions. As this deviation was considered tolerable, the Central Bank allowed interest rates to increase and refrained from conducting monetary operations. As at end 2025, AWCMR and AWRR recorded as 8.04 per cent and 8.06 per cent, respectively, while there has been some easing of money market rates thereafter.



Source: Central Bank of Sri Lanka

- In terms of money market activity, with the Central Bank not readily providing liquidity through OMOs, banks traded more actively in the call and the repo markets, with increased transaction volumes. Transaction volumes in the call money market significantly improved compared to the pre-crisis level,

on average, from around Rs. 19.7 billion in 2019 to Rs. 30.5 billion by 2025. Repo transactions remained dominant over call money trades due to risk considerations and exposure limits of Licensed Commercial Banks (LCBs).



Source: Central Bank of Sri Lanka

Monetary Operations of the Central Bank

Open Market Operations

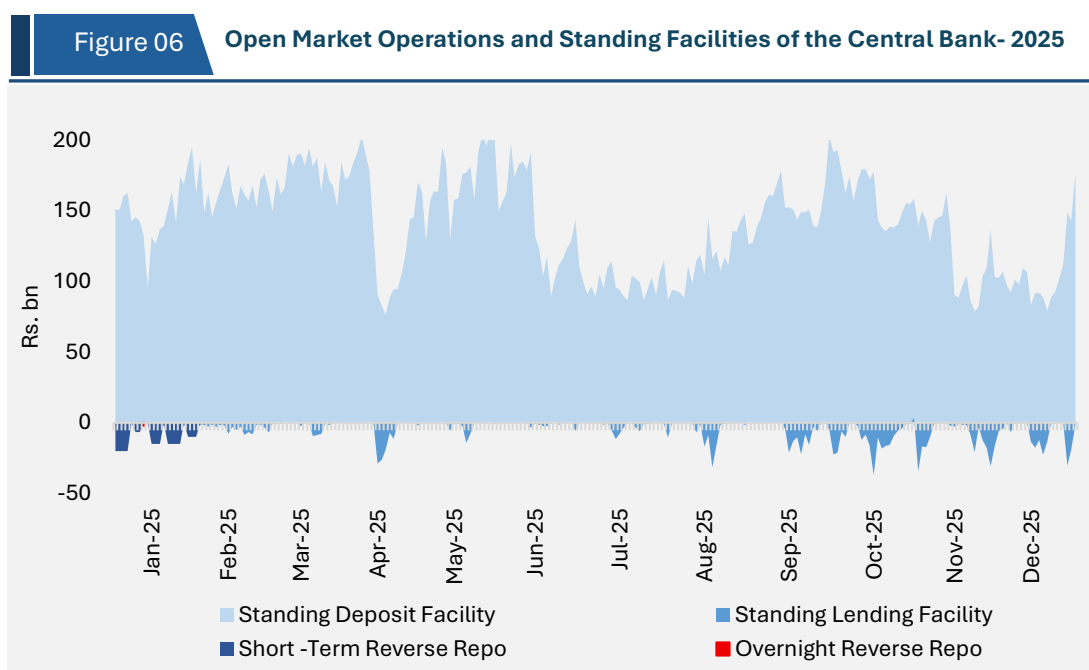
- The Central Bank refrained from conducting OMOs since end January 2025 given the persistent liquidity surplus in the domestic money market.

Standing Facilities

- The Central Bank enables Standing Deposit Facility (SDF) to deposit excess funds of Participatory Institutions (PIs) at the end of the day at the Standing Deposit Facility Rate (SDFR), and allow Standing Lending Facility (SLF) at the Standing Lending Facility Rate (SLFR) for PIs to borrow from the Central Bank to meet their residual overnight liquidity needs.
- The average amount granted under SLF during the year 2025 was Rs. 4.5 billion compared to the average of Rs. 7.1 billion reported during 2024. The dependence on the SLF by the SPDs and as well as other participants was

minimal in 2025 as they managed most of their funding requirements through the market.

- During the year 2025, banks continued to access the SDF in large volumes and the average amount accepted under SDF to facilitate depositing excess funds was Rs.140.9 billion compared to Rs.134.4 billion during 2024. With surplus liquidity in the domestic money market, SDF placements, especially by the foreign banks and state banks remained relatively high.



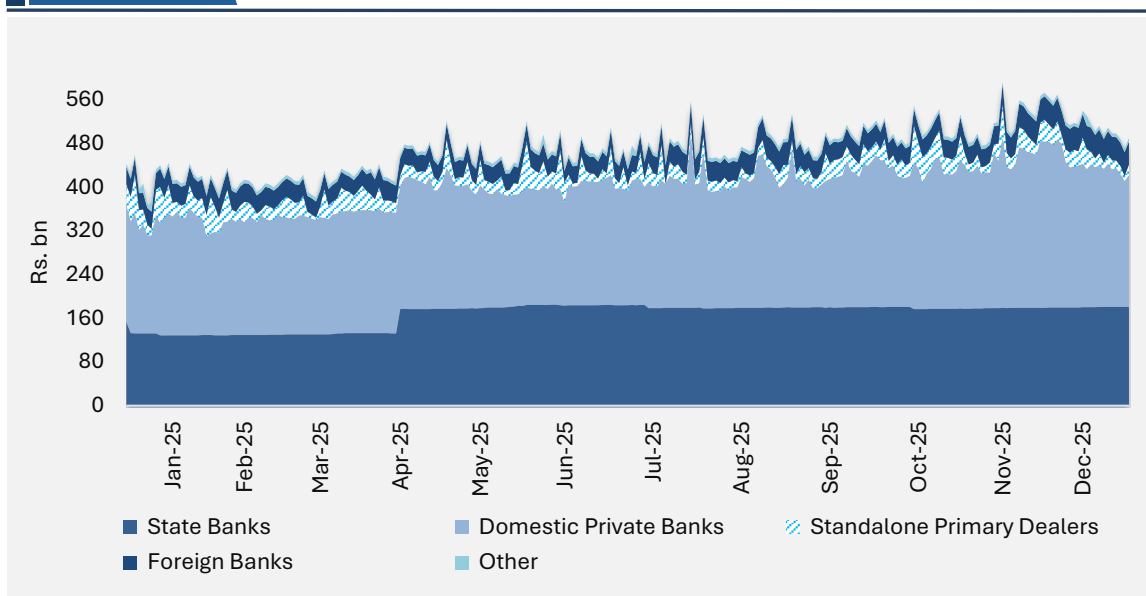
Source: Central Bank of Sri Lanka

Intra-Day Liquidity Facility

- The Central Bank made available intra-day funding through the Intra-day Liquidity Facility (ILF) to eligible participants to ensure smooth and efficient operation of the Real Time Gross Settlement (RTGS) system. The total value and the average daily value of ILF drawn during the year 2025 amounted to Rs.111,788.0 billion, and Rs. 467.7 billion, respectively, compared to Rs.101,812.6 billion and Rs. 420.7 billion, respectively, reported during 2024.

Figure 07

Usage of Intraday Liquidity Facility by Participatory Institutions - 2025



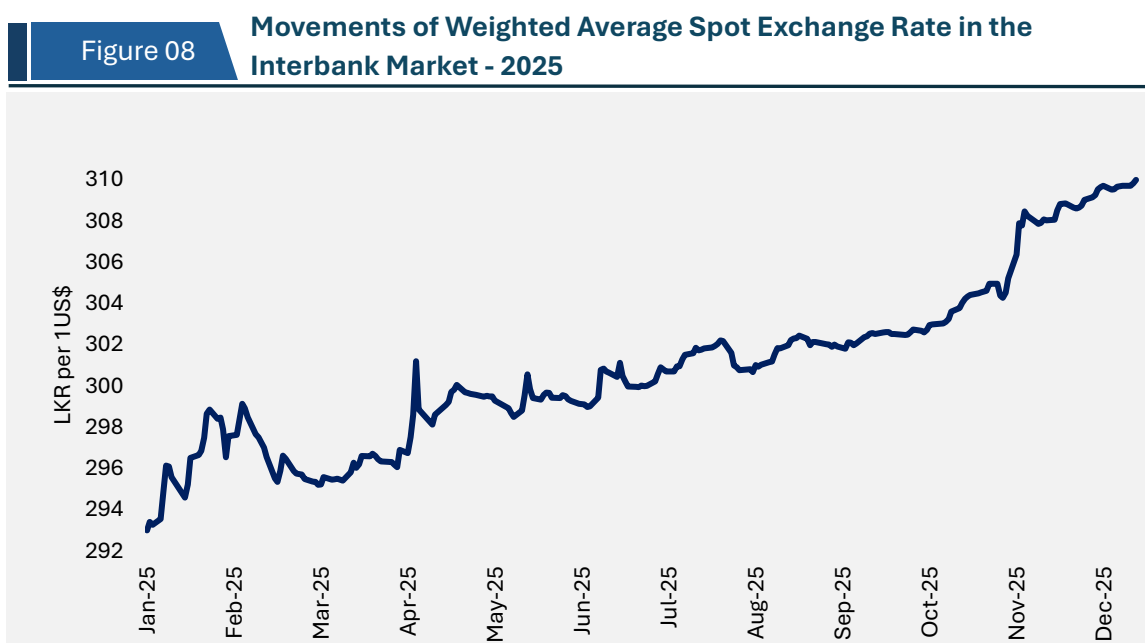
Source: Central Bank of Sri Lanka

Movements in the Exchange Rate

- The Sri Lanka rupee recorded a modest depreciation against the US dollar over the year 2025. During the second half of 2025, the Sri Lanka rupee depreciated by 3.1 per cent against the US dollar compared to 2.5 per cent depreciation recorded in the first half of 2025. Accordingly, throughout the year, the Sri Lanka rupee depreciated by 5.6 per cent against the US dollar from Rs. 292.58 by end December 2024 to Rs. 309.99 by end December 2025 compared to the 10.7 per cent appreciation recorded in 2024. This depreciation in 2025 reflected the impact of external developments, and geopolitical factors, alongside domestic foreign exchange market dynamics mainly driven by import related demand, amidst notable rise in motor vehicle imports.
- The year began with improved market confidence following the significant progress in Sri Lanka's debt restructuring process in late 2024. However, the exchange rate experienced depreciation pressure in early 2025, amidst speculations surrounding the announcement of relaxation of motor vehicle import restrictions. During the first half of 2025, the movement in the exchange

rate was affected owing to capital outflows, seasonal dividend payments, and rising import demand. Moreover, the exchange rate movements were further affected by the announcement of reciprocal tariffs by the United States Government and geopolitical tensions.

- At the beginning of the second half of 2025, depreciation pressures emerged due to import related foreign exchange demand and speculation amidst the recovery in the domestic economic activity. The materialisation of sizeable outflows related to motor vehicle imports, as well as dividend and infrastructure project related outflows imposed some pressure on the exchange rate during the second half of 2025. In addition, economic activities were temporarily disrupted during the latter part of the year due to extreme weather conditions arising from *Cyclone Ditwah*, which also influenced the dynamics of the domestic foreign exchange market. However, foreign exchange inflows due to increased workers' remittances and export proceed conversions helped to curtail these pressures, resulting a modest overall depreciation of the Sri Lanka rupee, while enabling foreign exchange purchases of the Central Bank.



Source: Central Bank of Sri Lanka

Domestic Foreign Exchange Market Operations of the Central Bank

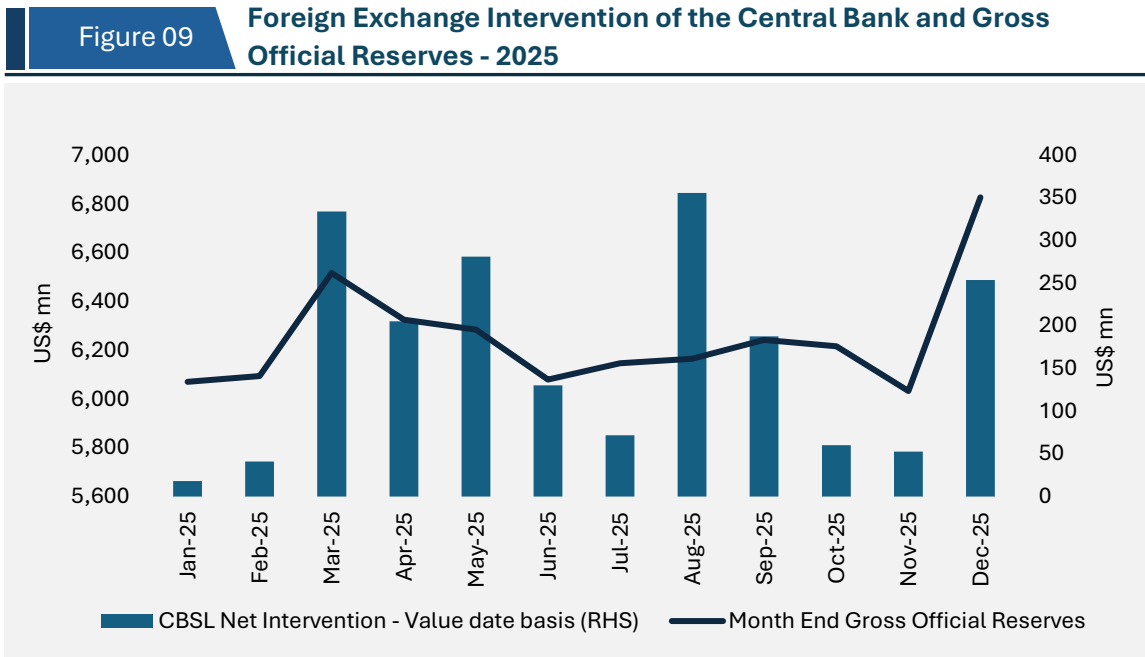
- Throughout the year, the Central Bank continued to closely monitor developments in the domestic foreign exchange market and intervened, as required. The Central Bank interventions mainly focused on building up foreign reserves and strengthen the external sector buffers, which is also a key requirement under the current Extended Fund Facility (EFF) programme with the International Monetary Fund (IMF). The Central Bank also intervened in the market at times of excessive volatility with limited supply of foreign exchange. Accordingly, during the second half of the year, the Central Bank purchased US dollars 1,027.0 million on value date basis compared to US dollars 1,073.4 million purchased during the first half of the year, while supplying only a marginal volume of US dollars 44.7 million to the market compared to US dollars 63.3 million supplied during the first half of the year, resulting in net purchases of US dollars 982.3 million on value date basis compared to net purchases of US dollars 1,010.1 million recorded during the first half of the year. Accordingly, over the year 2025, the Central Bank absorbed US dollars 2,100.4 million on value date basis, while supplying US dollars 108.0 million to the market, resulting in net purchases of US dollars 1,992.4 million on value date basis, thereby boosting the foreign reserves of the Country.
- During the second half of the year, the Central Bank entered into new buy-sell swap transactions with Licensed Banks amounting to US dollars 1,177.0 million on value date basis, compared to US dollars 868.0 million recorded during the first half of the year. During the same period, existing buy-sell swap transactions amounting to US dollars 770.0 million were rolled over, compared to US dollars 550.0 million in the first half of 2025 with the Licensed Banks, on value date basis. Meanwhile, buy-sell swap transactions amounting to US dollars 938.5 million

were allowed to mature during the second half of the year, compared to US dollars 503.5 million that matured in the first half of 2025. As a result, the outstanding amount of buy-sell swap transactions increased from US dollars 1,318.3 million at end-2024 to US dollars 1,921.3 million by the end-2025, on value date basis. These swap transactions helped banks to manage their liquidity position and cash flows, in both the foreign exchange market and the domestic money market.

- With the Central Bank's net purchases of foreign exchange from the domestic foreign exchange market amounting to US dollars 2.0 billion, along with swap transactions, foreign reserves increased in 2025. As a result, the Gross Official Reserves (GOR) of the Country increased to US dollars 6.8 billion (including People's Bank of China (PBoC) swap facility equivalent to US dollars 1.4 billion) by the end of 2025, which is the highest level of GOR recorded in the post crisis period.

Activities in the Domestic Foreign Exchange Market

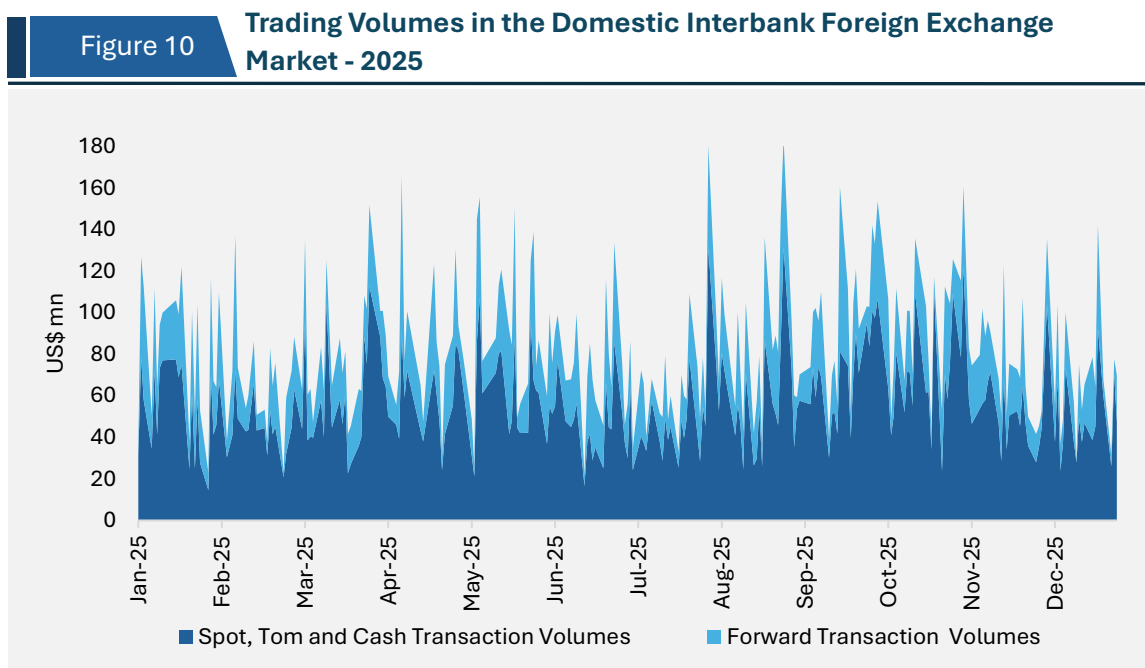
- During 2025, the domestic interbank foreign exchange market recorded a marked improvement in activity, reflecting enhanced market confidence and participation compared to 2024. In the first half of 2025, the average daily trading volume increased by 17.3 per cent to US dollars 81.5 million from US dollars 69.5 million in the corresponding period of 2024, while in the second half of 2025, the average daily trading volume rose sharply by 25.3 per cent to US dollars 82.3 million from US dollars 65.7 million in the corresponding period of 2024. Overall, the average daily trading volume during 2025 amounted to US dollars 81.9 million, compared to US dollars 67.5 million recorded in 2024.



The intervention data for 2025 are presented on value date basis

Source: Central Bank of Sri Lanka

- Further, in line with the overall increase in activity in the domestic foreign exchange market, the average daily volume of foreign exchange transactions in all Spot, Tom and Cash tenors during the second half of 2025 was US dollars 57.5 million, compared to the average daily volume of US dollars 54.2 million

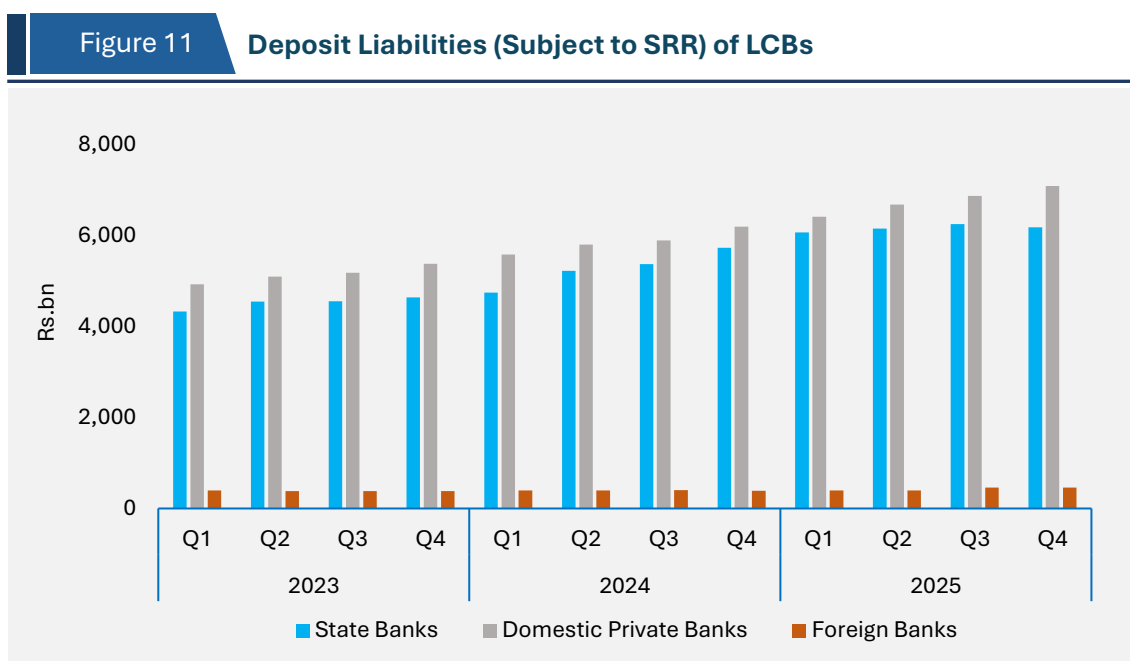


Source: Central Bank of Sri Lanka

during the first half of the year. For the entire year, the average daily volume of these transactions rose to US dollars 55.9 million, compared to US dollars 46.8 million in 2024.

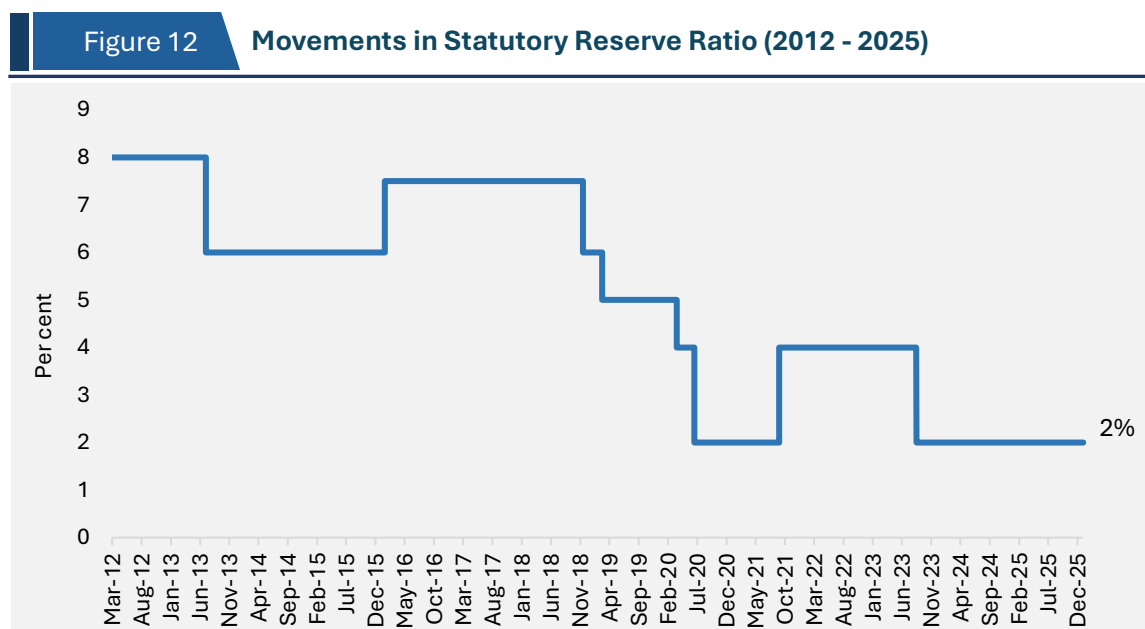
Movements in Deposit Liabilities of Licensed Commercial Banks and Statutory Reserve Requirement

- Rupee deposit liabilities of LCBs which are liable to maintain the Statutory Reserve Requirement (SRR), increased in 2025 compared to 2024, mainly driven by deposits of domestic private banks and foreign banks. In absolute terms, rupee deposit liabilities increased from Rs. 12,323.8 billion at end 2024 to Rs. 13,234.3 billion by end June 2025, and further to Rs. 13,734.1 billion by end 2025. This increase was largely attributable to the growth in deposits of domestic private banks and foreign banks, which mirrored the rising private-sector credit flows.



Source: Central Bank of Sri Lanka

- The growth in rupee deposit liabilities moderated during 2025, despite the elevation in the first quarter. Accordingly, deposit liability growth decelerated from 18.4 per cent at end 2024 to 15.9 per cent by mid-2025, and further to 11.4 per cent by end-2025, primarily reflecting the base effect.



Source: Central Bank of Sri Lanka

- In line with the accommodative monetary policy stance, SRR, the proportion of rupee cash reserves that the LCBs are required to maintain in their settlement accounts with the Central Bank, remained unchanged at 2.0 per cent throughout 2025. With the increase in deposit liabilities, required reserves increased in absolute terms.

Table 1: Changes in Components of Required Reserve Calculation

Category to SRR	Value (Rs. billion)	
	End December 2024 (SRR 2%)	End December 2025 (SRR 2%)
1. Total Rupee Deposit Liabilities	12,323.8	13,734.1
1.1. Demand Deposits	815.8	949.8
1.2 Time & Savings Deposits	11,463.8	12,719.5
1.3 Other Deposits	44.2	64.7
2. Total Required Reserves (a)	187.3	225.5

(a) After adjusting for vault cash concession

Introduction

The Statutory Reserve Requirement (SRR), which serves as a monetary policy instrument, is predominantly used for changing credit creation ability of Licensed Commercial Banks (LCBs) and money supply. The SRR has been an effective tool of the monetary policy framework for a long period, while supporting liquidity management in the banking system. However, its usage as a regular monetary policy tool has gradually declined, reflecting the bias of central banks towards the market-based monetary policy tools such as Policy Interest Rates and Open Market Operations (OMOs). Accordingly, the Central Bank of Sri Lanka (the Central Bank) currently utilises the SRR primarily to manage persistent liquidity conditions, rather than a regular monetary policy instrument.

Given the SRR's usefulness as an important monetary policy tool and a liquidity management instrument, a thorough review of its design or operational features was required. The evolving economic environment and ongoing changes in the banking and financial sectors, necessitated a reassessment of the SRR framework help to raise its effectiveness, relevance, and consistency. Moreover, developments in payment and settlement systems, advances in banks' cash management supported by technology, and lessons learned from market disruptions, particularly during the COVID-19 pandemic, have highlighted the need for a comprehensive review of the SRR framework in Sri Lanka. In this context, the Central Bank conducted a comprehensive review of the SRR framework in 2024/2025 period in line with changing economic environment and evolving banking and financial sector dynamics, with a view to strengthening the SRR framework and operational practices in line with international best practices.

The Current SRR Framework and Key Considerations

The reserve requirement (RR) refers to the proportion of reserves that financial institutions, as defined by a central bank, are required to hold as cash deposits (reserve assets) with the central bank. RRs are commonly designed to serve either monetary or prudential policy objectives, and in some cases, central banks use them to pursue a combination of objectives, including prudential regulation, monetary control, and liquidity management. In Sri Lanka, the SRR represents the proportion of deposit liabilities that the LCBs are required to maintain as cash deposits with the Central Bank as per provisions of the Central Bank of Sri Lanka Act (CBA) No. 16 of 2023. At present, all demand, time, and savings deposits of LCBs denominated in Sri Lankan rupee are subject to the SRR and LCBs are required to maintain such statutory reserves over two Reserve Maintenance Periods (RMPs) in a calendar month. This framework allows some degree of flexibility through reserve averaging, a daily

minimum balance requirement, and recognition of vault cash as an eligible reserve asset.

While these features have been introduced to ease operational constraints, financial market developments suggest that further refinements to the SRR framework could enhance short-term liquidity management of banks and improve the precision of liquidity forecasting.

Strengthening the Reserve Requirement Framework in Sri Lanka

The review of the SRR framework of Sri Lanka is based on several key operational elements, including the design of the RMP, eligibility of vault cash as a reserve asset, level of the appropriate daily minimum reserve requirement, and the structure of penalties for non-compliance. These elements have been reviewed by the Central Bank with a view to improving liquidity management, reducing interest rate volatility, and strengthening the effectiveness of monetary policy implementation.

(i) Calendar-Based RMPs and Interest Rate Volatility

Under the existing SRR framework, RMPs commence on the 1st and 16th day of each month and the second RMP is typically concluded at the end of the calendar month or sometimes during weekends. These periods are often associated with heightened liquidity demand arising from government salary payments, tax payments, and increased currency withdrawals, etc. Evidence from daily net liquidity conditions and the movements in overnight call money rates indicates that liquidity pressures and interest rate volatility tend to increase toward the end of such calendar based RMPs. These pressures frequently lead to increased demand for liquidity, which sometimes lead to mixed policy signals. Experience of other central banks suggests that aligning RMPs with monetary operations is more effective to address such concerns. Many emerging market economies, including India and Thailand operate RMPs based on monetary operations rather than fixed calendar dates. Such arrangements help maintaining smoother liquidity conditions and reduce end-of-period stress on interest rates. In this context, Sri Lanka's RMPs are expected to be reorganized into two-week periods commencing mid-week, from Wednesday to Tuesday, while publishing the RMP calendar in advance. This would help to ease end-of-period liquidity pressures and moderate overnight interest rate volatility, thereby improving the effectiveness of market operations. The proposed RMP structure would also enhance accuracy of liquidity forecasting of the Central Bank and support efficient liquidity management, as OMOs would be conducted during reserve maintenance period as appropriate, supplemented by fine-tuning operations to address any unexpected liquidity needs.

(ii) Vault Cash Concession in the Context of Reserve Assets

Vault cash, or till cash, represents physical currency held by banks to meet daily transaction needs. Under the current SRR framework, LCBs are permitted to treat a limited portion of vault cash as part of their required reserves. While this concession has supported banks in meeting their daily cash requirements, particularly for large banks with extensive branch networks, evidence indicates that

vault cash holdings are highly seasonal and are increasing significantly during festive periods. Such volatility directly contributes to fluctuations in effective reserve holdings and interest rates, thereby complicating liquidity monitoring and diminishing the effectiveness of the SRR as a monetary policy instrument.

Most emerging market central banks exclude vault cash from eligible reserve assets, which is consistent with the statistical standards of the International Monetary Fund (IMF). In Sri Lanka, improvements in cash management of banks and real-time monitoring, supported by advances in information technology, have greatly reduced banks' reliance on this concession. Accordingly, the Central Bank plans to implement a phased removal of the vault cash concession, while allowing a smooth transition for LCBs.

(iii) Reinstating Daily Minimum Reserve Requirements

Under the current reserve averaging framework, LCBs are allowed to reduce their daily minimum reserve requirement up to 20 per cent of the required reserve. This temporary concession, which is a reduction from 90 percent to 20 per cent, was introduced in 2020 in response to heightened liquidity pressures during the COVID-19 pandemic. While this relaxation was appropriate during periods of acute liquidity stress, a review of recent SRR data suggests that it may no longer be necessary.

An analysis of daily reserve holdings indicates that LCBs consistently maintain reserve balances well above the prevailing minimum requirement. Accordingly, increasing the daily minimum reserve requirement gradually to the previous level, would not constitute a binding constraint on banks. At the same time, this adjustment would improve accuracy of liquidity forecasting and strengthen reserve maintenance practices among LCBs.

(iv) Current Penalty Structure and International Best Practices

At present, the penalty structure of SRR non-compliance is not explicitly linked to monetary policy signals and it may result in costs to LCBs that are disproportionate to the policy stance. In many emerging market economies, penalty rates for reserve shortfalls are explicitly linked to the policy interest rates. Accordingly, linking the penalty rate to the Overnight Policy Rate (OPR), plus a margin would introduce transparency and proportionality into the SRR framework. This approach would ensure that penalties are appropriately calibrated to encourage compliance, remain sufficiently punitive without placing an undue burden on banks, and are aligned with international best practices.

Implications of Introducing Changes to SRR Framework for Monetary Policy Implementation

Taken together, the proposed reforms to be implemented by the Central Bank represent a comprehensive recalibration of Sri Lanka's SRR framework, consistent with the Central Bank's policy objectives and international best practices. Such measures are expected to reduce short-term

liquidity and interest rate volatility, enhance accuracy of liquidity forecasting, and improve the effectiveness of OMOs and policy signaling. Collectively, these improvements will support smoother monetary transmission and strengthen the effectiveness of monetary operations in achieving price stability. At the same time, these reforms are aligned with international standards of monetary policy implementation and are broadly consistent with banking sector practices in liquidity and cash management.

Conclusion

An effective SRR framework is critical for the successful implementation of monetary policy in an increasingly dynamic economic and financial environment. This article summarises the proposals under the review of the SRR framework, which aim to enhance the operational efficiency of the monetary policy framework and support greater stability in short-term money market conditions in Sri Lanka, while ensuring alignment with evolving market conditions and international best practices.

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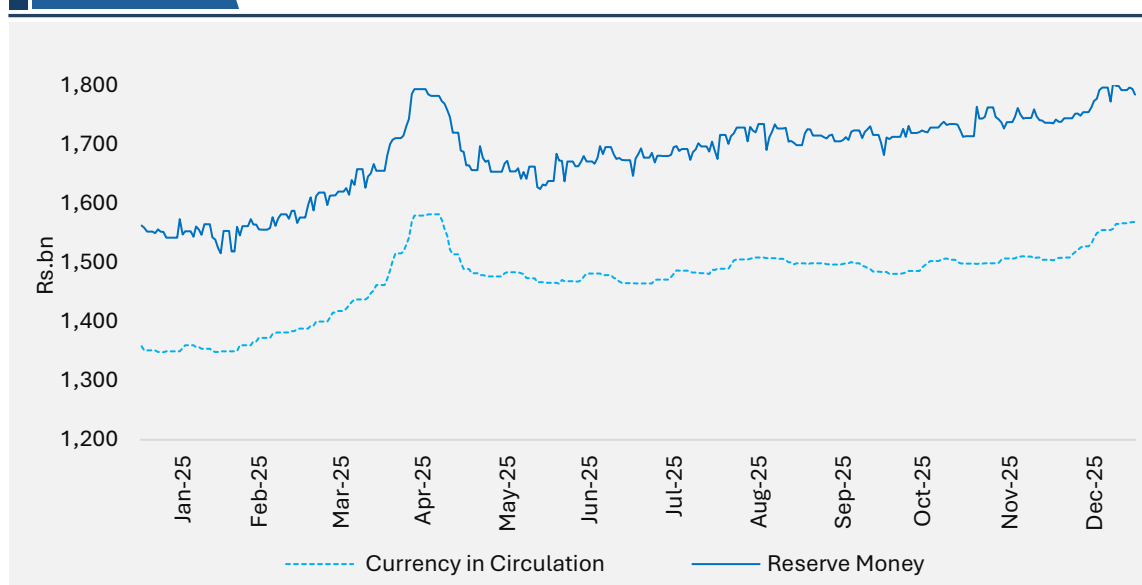
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Movements in Currency in Circulation and Reserve Money

- During 2025, currency in circulation (CIC) increased gradually, with a notable increase in April reflecting seasonal demand. Thereafter, CIC stabilised at higher levels and edged up further toward the end of the year, indicating sustained demand for currency for transactions. The surge in CIC during this period also reflects heightened public preference for holding cash amidst the increase in cash-based transactions, and relatively low opportunity cost of holding currency due to low deposit interest rates.
- The Central Bank released about Rs. 103.8 billion worth of currency into the economy during the second half of 2025, compared to Rs. 106.4 billion in the first half of the year. Out of this amount, about Rs. 64.1 billion worth of currency was withdrawn by LCBs from the Central Bank during month of December 2025, indicating the usual currency withdrawal pattern during the festive season to meet transaction demand.

Figure 13

Reserve Money and Currency in Circulation - 2025

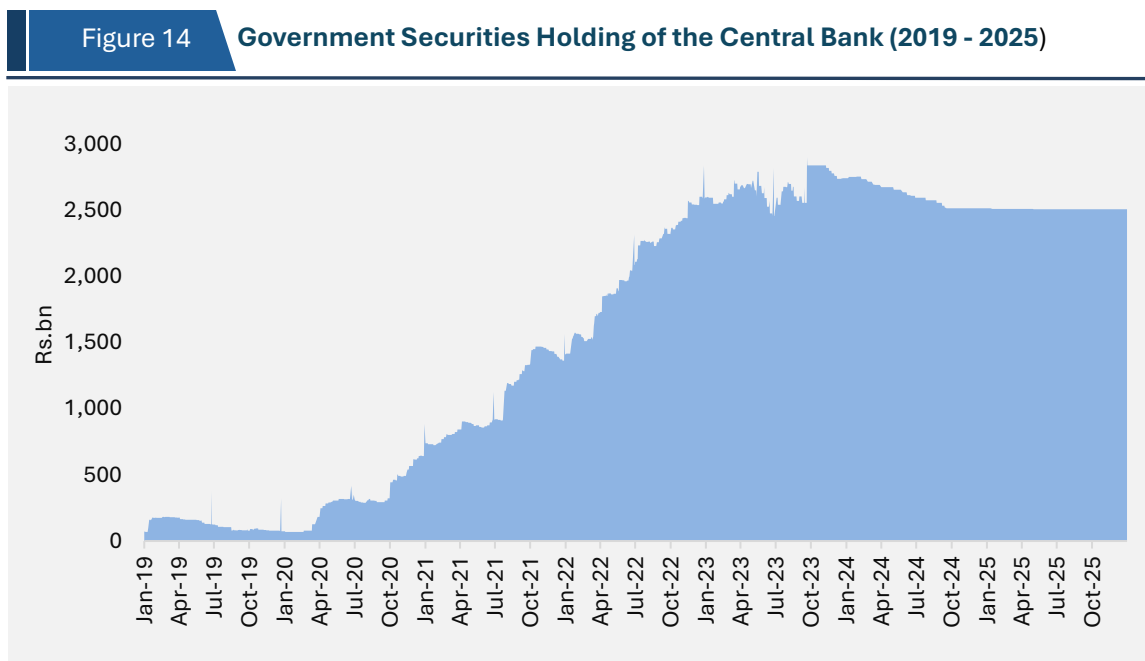


Source: Central Bank of Sri Lanka

- Reserve money, which is the total stock of high-powered money issued by the Central Bank, increased during 2025, with a sharp rise and peak around April, followed by a partial moderation. Thereafter, it remained relatively stable at higher levels and gradually increased toward year-end. Accordingly, reserve money increased to Rs.1,796.5 billion by end December 2025, compared to Rs.1,660.1 billion recorded at end June 2025, and Rs. 1,539.3 billion recorded at end 2024 mainly due to the increase in CIC.

Government Securities Holding of the Central Bank

- The face value of the Central Bank’s holdings of Government Securities, which mainly comprise of restructured Treasury bonds, marginally declined to Rs. 2,508.9 billion by end December 2025 from Rs. 2,515.6 billion at end 2024. This reduction was mainly due to the maturity of Treasury bonds during the year.



Source: Central Bank of Sri Lanka

Selected Indicators of Market Operations and Transactions

Domestic Money Market Operations						
Transactions	Volume (Rs. billion)			Weighted Average Interest Rate		
				(Min-Max) - %		
	2023	2024	2025	2023	2024	2025
Money Market Transactions						
Call Money (Overnight)	2,076.9	3,183.3	7,279.7	9.10 -16.50	7.99 - 9.24	7.68 - 8.04
Repo (Overnight)	3,522.7	8,960.0	13,510.8	9.52 -16.50	8.01 -10.00	7.72 - 8.13
Open Market Operations						
Overnight Basis						
Repo	-	-	-	-	-	-
Reverse Repo	7,484.7	6,006.7	1.9	9.05 - 16.19	8.05 - 9.55	8.14
Liquidity Support Facility	-	-	-	-	-	-
Short-Term Basis						
Repo	-	-	-	-	-	-
Reverse Repo	1,450.3	2,318.1	46.5	10.31-16.50	8.08 -10.00	8.06 - 8.14
Liquidity Support Facility	-	-	-	-	-	-
Long-Term Basis						
Repo	-	-	-	-	-	-
Reverse Repo	1,393.3	279.5	-	10.78- 29.24	8.85 -10.77	-
Liquidity Support Facility	-	-	-	-	-	-
Outright Basis						
Purchase of T-bills	-	-	-	-	-	-
Purchase of T-bonds	8.5	12.0	-	13.70-30.80	13.20-13.73	-
Standing Facility (at Standing Rates)						
Standing Deposit Facility	17,991.0	32,516.8	33,686.7	9.00 ¹	7.50 ¹	7.25 ¹
Standing Lending Facility	26,015.3	1,708.0	1,082.3	10.00 ¹	8.50 ¹	8.25 ¹
Domestic Foreign Exchange Market Operations						
Transactions	Volume (in US dollars million)			Weighted Average USD/LKR Spot Rate		
	2023	2024	2025	2023	2024	2025
Beginning of the Period	-	-	-	363.11	323.99	293.00
End of the Period	-	-	-	323.92	292.58	309.99
Appreciation (+) /Depreciation (-) (%)	-	-	-	12.10	10.71	-5.62
Domestic Foreign Exchange Market Operations						
Spot, Tom and Cash Transactions	9,315.6	11,322.0	13,366.7	-	-	-
Forward Transactions	5,682.6	5,022.4	6,206.4	-	-	-
Total	14,998.2	16,344.4	19,573.1	-	-	-
Central Bank Intervention in the Domestic Foreign Exchange Market²						
Purchases	2,500.3	3,028.6	2,100.4	-	-	-
Sales	825.7	183.0	108.0	-	-	-
Net Purchases	1,674.6	2,845.6	1,992.4	-	-	-
¹ End period rates						
² Value date basis						
Source: Central Bank of Sri Lanka						