8

FINANCIAL SECTOR PERFORMANCE AND SYSTEM STABILITY

Performance of the financial sector moderated during the first eight months of 2019 in an environment of subdued economic activities. Investor sentiment stemming from political uncertainty and the Easter Sunday attack added further stress on financial institutions. Growth in total assets reduced significantly for both Banking sector and Licensed Finance Companies and Specialised Leasing Companies (LFCs and SLCs) sector. Banking sector's credit growth decelerated while the LFCs and SLCs sector recorded a negative credit growth compared to the same period in the previous year. Further, non-performing loans increased to high levels in both sectors, but remained manageable. The profitability of both the banking sector and LFCs and SLCs sector decelerated compared to the corresponding period of the previous years. However, the banking sector complied with enhanced capital requirements under Basel III and maintained most of the prudential indicators well above the minimum regulatory requirements. Meanwhile, necessary prudential actions were taken by the Central Bank to revive certain weak finance companies and to cease the operations of insolvent companies to maintain long-term stability of the financial sector. The total assets of the insurance sector registered a healthy growth while other financial institutions such as primary dealers, unit trusts and superannuation funds were able to maintain their performance, at former levels. Policy rate changes, reduction of the Statutory Reserve Ratio, appropriate open market operations, introduction of the Liquidity Support Facility and outright purchase of Treasury bonds helped maintain Weighted Average Call Money Rate (AWCMR) around the middle of the Standing Rate Corridor (SRC) with a downward adjustment. The dismal performance observed in the Colombo Stock Exchange during 2018 continued during the first nine months of 2019 as well. Yield rates of the primary market issuances of Treasury bills and Treasury bonds in the domestic market reverted from its increasing trend noted during early part of the year to decline towards latter part of the first half of 2019. The exchange rate which significantly depreciated in 2018, appreciated during the first nine months of 2019 though a slight increase in the pressure on the exchange rate was observed following the Easter Sunday attacks and during the month of August, due to the repatriation of foreign investments from the government securities market. However, modest forex intervention by the Central Bank eased this pressure on the exchange rate. In addition, the value of the Sri Lankan rupee against the US dollar was maintained with the support of receipts of the sixth tranche of the Extended Fund Facility (EFF) from the International Monetary Fund (IMF) and International Sovereign Bond (ISB) issuances in March and June 2019, and net customer inflows to the domestic forex market.

Developments in Financial Institutions

Banking Sector

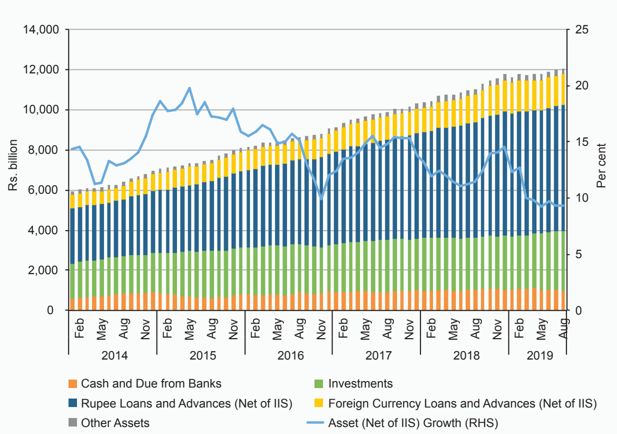
- **The banking sector recorded a moderation of its growth momentum during the first eight months of 2019**. However, the sector maintained capital and liquidity well above the regulatory minimum requirements, thereby ensuring the resilience of the sector. The asset base of the banking sector which comprised credit and investment portfolios, was largely funded through deposits and continued to grow albeit at a slower pace compared to the previous year. Deterioration in asset quality was reflected by an increase in NPLs resulting from adverse business environment due to unfavourable weather conditions, political uncertainty and the Easter Sunday attack in April 2019. Several measures were taken by the Central Bank with the aim of reversing the decelerating growth in credit. Among these measures, the reduction in the SRR enabled banks to invest additional funds in revenue generating activities and also supported in improving rupee liquidity in the domestic money market. The reduction in policy interest rates also facilitated banks to reduce their cost of funds. The profitability of the sector deteriorated during the first eight months mainly due to higher operating costs, increase in loan loss provisions and taxes. However, implementation of the Basel III framework would further enhance the resilience of the banking sector. The bank branch and ATM network expanded further with new branches, ATMs and digital banking units being added to the system thereby increasing financial inclusion in the country.

- **The growth in assets of the banking sector moderated during the first eight months of 2019 when compared with the same period of last year.** Total assets of the sector expanded by 2.4 per cent (Rs. 277.8 billion) to Rs. 12.1 trillion in the first eight months of 2019 compared to a growth of 7.3 per cent (Rs. 747.5 billion) in the corresponding period of 2018. The increase in assets during the first eight months of 2019 was mainly contributed by the increase in investments while the moderation in loans and advances hindered the expansion of the asset base of the banking sector. The asset base of the banking sector was funded primarily through deposits (Rs. 8.8 trillion) and borrowings (Rs. 1.6 trillion). Year-on-year growth in assets, which increased up to 14.6 per cent as at end 2018 from 13.8 per cent as at end 2017, gradually declined and reached 9.3 per cent at end August 2019.

- **Year-on-year credit growth which reached 19.6 per cent as at end 2018 moderated in 2019 owing to lower demand for credit due to the adverse business environment that prevailed**

Figure 8.1

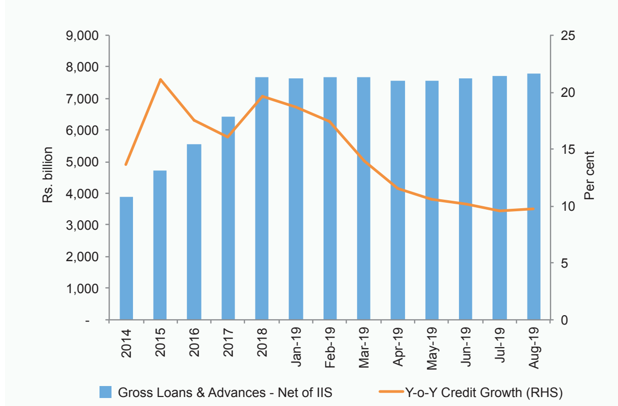
Total Assets of the Banking Sector



Source: Central Bank of Sri Lanka

Figure 8.2

Loans and Advances of the Banking Sector



Source: Central Bank of Sri Lanka

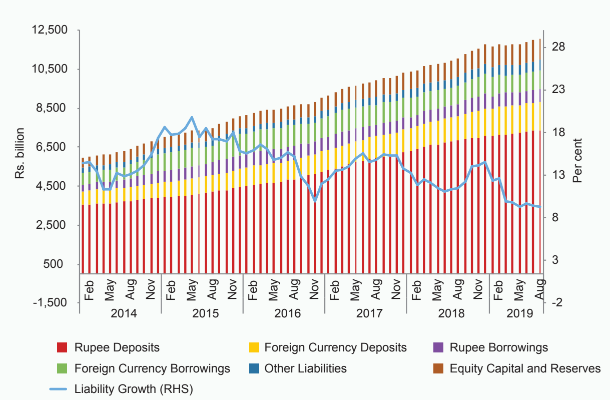
in the first eight months of 2019 and dipped to 9.7 per cent as at end August 2019. Total loans and advances reported an increase of Rs. 102.7 billion (1.3 per cent) during the first eight months of 2019 to reach Rs. 7.8 trillion at end August 2019 when compared to a significant growth of Rs. 673.5 billion (10.5 per cent) in the same period of year 2018. Credit growth in 2019 was driven by the increase in rupee loans, which exceeded the total increase in loans and reported a growth of 1.9 per cent during the period. Growth in loans and advances was driven by increased lending by banks to the Central Government and State-Owned Enterprises while lending to the private sector decelerated during this period. In terms of products, except for overdrafts which decreased by Rs. 64.1 billion, all other main loan products reported an increase during the period. At end June 2019, banking sector credit was mainly extended to the consumption (18.4 per cent), construction (15.4 per cent), wholesale & retail trade (15.2 per cent), manufacturing (11.0 per cent), infrastructure developments (8.6 per cent) and agriculture, forestry & fishing (8.2 per cent) sectors. Meanwhile, out of the main sectors, credit granted to construction, financial services and tourism reported a decline during the first half of 2019, while credit granted to other main sectors increased.

- **Funds were largely directed to investments resulting from lower demand for credit**. Increase in investments during the first eight months of 2019 was Rs. 254.3 billion (9.4 per cent) compared to that of Rs. 31.4 billion (1.2 per cent) during the corresponding period of 2018.

- **The banking sector expansion was largely funded through deposits which contributed towards 73.2 per cent of the total assets as at end August 2019.** The deposit base of the banking sector grew by Rs. 343.9 billion with 4.0 per cent growth during the first eight months of 2019 and primarily consisted of rupee deposits. The caps on deposit interest rates on banks was imposed in consultation with banks in April 2019, which was subsequently removed in September 2019, was aimed at reducing the cost of funds of banks and assisting them to reduce lending interest rates. Meanwhile, a notable decrease in share of demand deposits was observed during this period with a shift in deposits from demand to term deposits and short term savings, particularly in 3-month term deposits. The share of current and savings deposits as a percentage of total deposits (CASA Ratio) declined to 30.9 per cent as at end August 2019, compared to 32.7 per cent during the corresponding period in 2018. Borrowings declined by Rs. 142.0 billion showing a negative growth of 8.1 per cent during the first eight months of 2019 when compared with the decline of Rs. 58.9 billion (3.7 per cent negative growth) in the corresponding period of 2018. Total borrowings declined mainly due to the decline in rupee borrowings by 11.9 per cent (Rs. 88.1 billion). Meanwhile, FCY borrowings decreased by 4.2 per cent (US dollar 235.2 million) during the first 8 months of 2019 mainly due to settlement of borrowings through off-shore banking units.

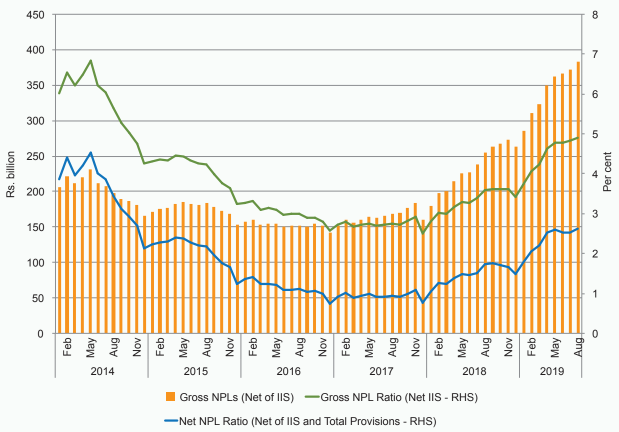
- **Asset quality showed a deterioration, but remained manageable**. NPLs increased by Rs. 119.9 billion (45.6 per cent) to Rs. 383.1

Figure 8.3
Sources of Funding of the Banking Sector



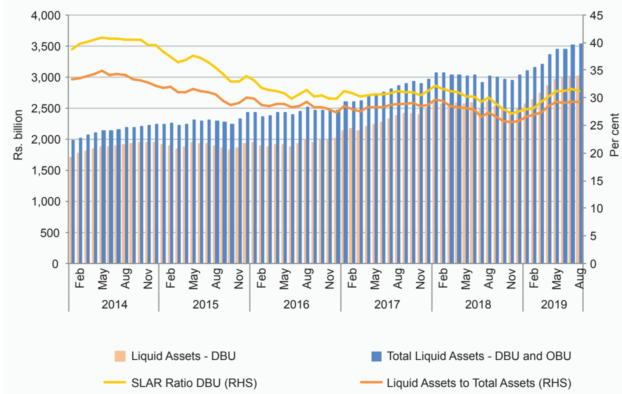
Source: Central Bank of Sri Lanka

Figure 8.4
Non-performing Loans of the Banking Sector



Source: Central Bank of Sri Lanka

Figure 8.5
Liquidity Position of the Banking Sector



Source: Central Bank of Sri Lanka

billion as at end August 2019 from Rs. 263.1 billion as at end 2018, resulting in increasing the NPL ratio to 4.9 per cent by end August 2019 from 3.4 per cent as at end December 2018. A rise in NPLs was observed across all economic sectors in the first half of 2019. The NPL ratio of the agriculture sector increased significantly mainly due to the impact of the drought that prevailed during the first quarter of 2019, while tourism sector NPLs also increased significantly mainly due to the impact of the Easter Sunday attack. However, the lower increase in provisions compared to the increase in NPLs resulted in a deterioration in specific and total provision coverage ratios. The lower increase in provisions was due to the new NPLs being classified under categories which require lower provisions and availability of underlying security.

- **The banking sector operated with an adequate liquidity buffer above the minimum regulatory requirement.** As at end August 2019, the Statutory Liquid Assets Ratios (SLAR) of the Domestic Banking Unit (DBU) and the Off-shore Banking Unit (OBU) were at 31.2 per cent and 45.7 per cent, respectively, which is well above the minimum statutory requirement of 20 per cent, while the ratio of liquid assets to total assets stood at 29.3 per cent at the end of August 2019. The loans to deposits ratio slightly increased to 88.2 per cent at end August 2019 from 87.8 per cent as at end August 2018. The Rupee and All Currency Liquidity Coverage Ratios of the banking industry stood at 202.8 per cent and 169.5 per cent, respectively, as at end August 2019 well above the regulatory minimum of 100 per cent. The net stable funding ratio was at 131.4 per cent as at end June 2019.

- **The net foreign currency exposure of the banking sector decreased by end June 2019, compared to end December 2018, with the higher decrease in assets denominated in foreign currency compared to the decrease in liabilities denominated in foreign currency.** During the first half of 2019, on-balance sheet assets denominated in foreign currency decreased mainly due to decrease in loans, while on-balance sheet foreign currency liabilities decreased mainly due to decrease in borrowings. The net foreign currency exposure as a percentage of banks' regulatory capital and on-balance sheet foreign currency assets stood at 0.7 per cent and 0.5 per cent, respectively, as at end June 2019. The banking sector reported a long foreign currency position of US dollar 41.9 million as at end June 2019 in comparison to a long position of US dollar 63.7 million as at end December 2018. There was a net gain of Rs. 7.3 billion on foreign currency revaluation during the first eight months of 2019.

Table 8.1

Banking Sector - Selected Indicators

Item	End Aug 2017	End Aug 2018	End Dec 2018	End Aug 2019 (a)	Y-O-Y Change (%)	
					Aug 2018	Aug 2019 (a)
Total Assets (Rs.billion)	9,901.5	11,039.9	11,794.0	12,071.8	11.5	9.3
Loans & Advances (Rs.billion)	6,140.2	7,104.4	7,693.4	7,796.0	15.7	9.7
Investments (Rs.billion)	2,588.4	2,608.1	2,697.4	2,951.7	0.8	13.2
Deposits (Rs.billion)	7,063.5	8,088.6	8,492.4	8,836.3	14.5	9.2
Borrowings (Rs.billion)	1,604.2	1,548.2	1,763.4	1,621.4	-3.5	4.7
Capital Funds (Rs.billion)	823.2	958.9	1,030.4	1,095.7	16.5	14.3
Tier 1 Capital Adequacy Ratio (%) (b)	12.3	12.8	13.1	13.3		
Total Capital Adequacy Ratio (%) (b)	15.1	16.0	16.2	16.5		
Gross Non-performing Loans Ratio (%)	2.8	3.6	3.4	4.9		
Net Non-performing Loans Ratio (%)	0.9	1.7	1.5	2.6		
Return on Assets (Before Tax) (%)	2.0	1.9	1.8	1.5		
Return on Equity (After Tax) (%)	17.6	14.6	13.2	10.8		
Statutory Liquid Assets Ratio (DBU) (%)	31.2	30.0	27.6	31.2		
Liquid Assets to Total Assets (%)	29.0	27.4	25.7	29.3		

(a) Provisional
(b) As at end June

Source: Central Bank of Sri Lanka

- **The gradual downward movement in market interest rates during the first eight months of 2019 resulted in an increase in capital gains on Treasury bonds to Rs. 3.4 billion compared to Rs. 1.8 billion reported during the corresponding period in 2018.** This was due to the increase in investments in Government securities during the first eight months of 2019 compared to the corresponding period in 2018. Equity risk of the banking sector was minimal as exposure to the equity market of banks' trading portfolio was Rs.15.8 billion and was only 0.1 per cent and 2.4 per cent, respectively, of total assets and investments held for trading of the banking sector as at end August 2019.

- **Subdued business activities, decreased lending, deterioration of assets quality thereby increasing provisioning and increased taxes resulted in a decline in profits during 2019.** Profits after tax of the banking sector was Rs. 125.9 billion for the year 2018 and Rs. 74.8 billion for the first eight months of 2019, which decreased by Rs. 12.2 billion when compared to the profits of Rs. 87.0 billion during the corresponding period of 2018. Despite the increase in net interest income, profits decreased during this period when compared with the corresponding period of last year due to increases in non-interest expenses (Rs. 14.9 billion) and loan loss provisions (Rs. 13.7 billion). There was a notable decrease in

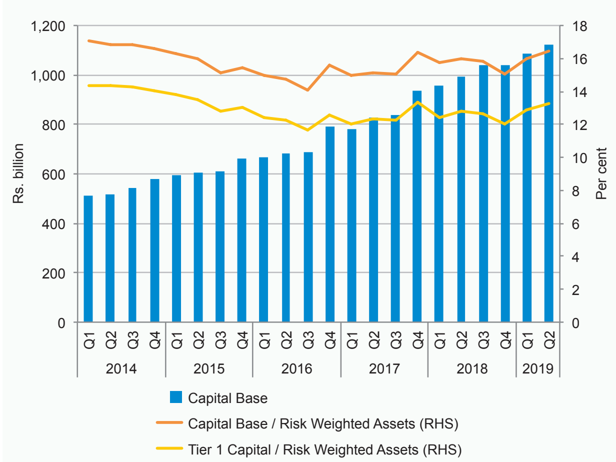
Figure 8.6

ROA and ROE of the Banking Sector

Source: Central Bank of Sri Lanka

Figure 8.7

Capital Adequacy of the Banking Sector



Source: Central Bank of Sri Lanka

foreign exchange income of Rs. 3.8 billion during this period which was partially set-off by the gains in trading/investment securities of Rs. 3.4 billion during first eight months of 2019 compared to the corresponding period of 2018 resulting in a marginal decrease in non-interest income.

- **Decrease in profits was reflected in profitability ratios**. Return on Assets (ROA) before tax and Return on Equity (ROE) had dropped to 1.5 per cent and 10.8 per cent, respectively, in August 2019 from 1.9 per cent and 14.6 per cent, respectively, in August 2018. Further, the net interest margin (NIM) decreased slightly to 3.6 per cent from 3.7 per cent during this period. Increase in operating cost had resulted in the deterioration of the efficiency ratio to 51.6 per cent in August 2019 from 48.5 per cent in August 2018.

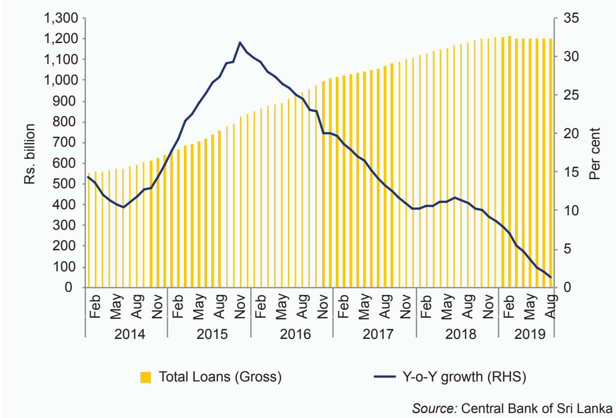
- **The banking sector maintained adequate capital during the first half of 2019 in order to absorb any adverse shocks.** By end June 2019, the banking sector operated with a common equity ratio of 13.3 per cent and a total capital ratio of 16.5 per cent, well above the Basel III requirements. However, in the medium term, banks may face challenges in raising funds to meet the enhanced capital requirements for business growth. Leverage ratio of the banking sector was at 6.9 per cent as at end June 2019.

- **The branch network expanded further during the first half of 2019 improving access to finance.** Accordingly, 332 automated teller machines (ATMs) were installed and there were 13 new branches opened during the first half of 2019, while 9 ATMs were closed.

LFCs and SLCs Sector

- **The LFCs and SLCs sector performance deteriorated during the first eight months of year 2019 with negative credit growth, with a decline in profitability and an increase in non-performing loans.** The slowdown in the sector was mainly due to subdued economic activities that prevailed in the first half of year 2019 which was aggravated by the Easter Sunday attack. However, key prudential indicators of the sector, including capital and liquidity levels, continued to be positive and remained above the minimum requirement, except for a few distressed/high-risk LFCs. The Central Bank continued to monitor key prudential measures with the consideration of reviving the companies with weak financial positions. Accordingly, necessary actions have been taken to cease or limit finance business operations of high-risk LFCs to safeguard the interest of depositors and other creditors to ensure the long-term stability of the financial sector. As at end August 2019, there were 43 LFCs[1] and 4 SLCs with 1,418 branches and 638 other outlets[2].

Figure 8.8
Total Loans and Advances of LFCs and SLCs Sector



Source: Central Bank of Sri Lanka

- **The growth in assets of the sector deteriorated during the first eight months of 2019 when compared to the corresponding period of 2018.** Total assets of the sector grew only by 0.8 per cent (Rs.11 billion) to Rs. 1,442.4 billion compared to the growth of 3.8 per cent reported in the corresponding period of 2018. Deterioration of assets was mainly due to negative credit growth which subdued the growth of other assets including liquid assets and the investment portfolio.

1 Licence of TKS Finance Limited was cancelled on 19 September 2019.
2 Other outlets mean service centers, pawning centers, collection centers which do not mobilize public deposits.

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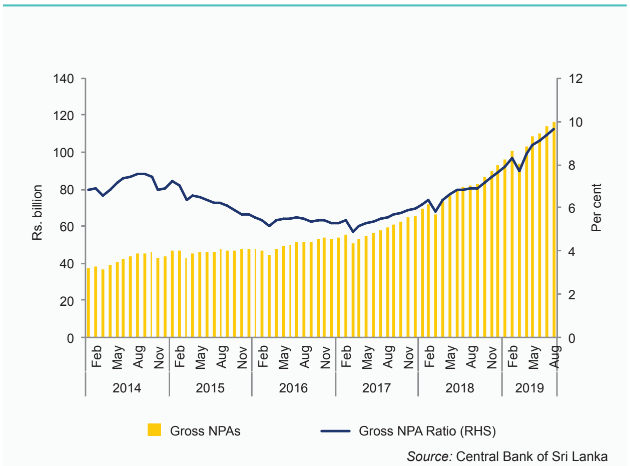
- **Credit growth subdued during the period mainly due to economic slowdown, deterioration of investor sentiments and high real interest rates that prevailed in the economy.** A negative credit growth of 1.9 per cent was recorded during the first eight months of 2019, compared with a credit growth of 6.4 per cent recorded in the corresponding period of 2018.

- **Asset quality of the sector deteriorated during the period under consideration.** Gross NPL ratio increased to 9.6 per cent from 7.7 per cent reported in December 2018, showing signs of deterioration in the asset quality mainly due to slow down in economic activities. However, the provision coverage ratio slightly increased to 58.0 per cent from the reported level of 57.0 per cent in December 2018. The net NPL ratio remained manageable at 3.1 per cent due to high provisioning for loan losses and high provision coverage ratio. It is expected that NPL will further increase with the uncertain political situation and slowdown in economic activities.

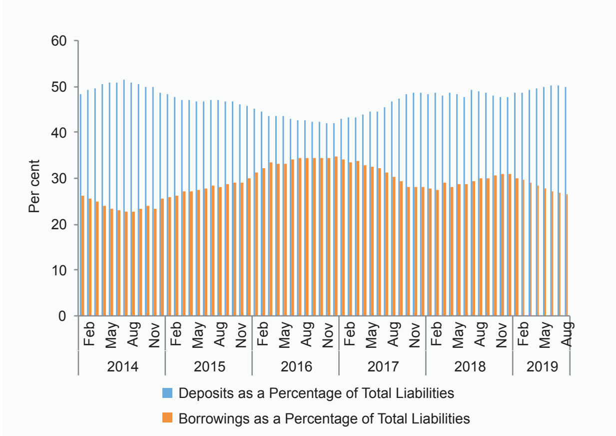
- **The sector expansion was largely funded through deposits.** Deposits dominates the funding mix with a share of 53.0 per cent, and this has increased when compared to the share of 50.1 per cent recorded at end December

Figure 8.9
Non-performing Accommodations of LFCs and SLCs Sector



Source: Central Bank of Sri Lanka

Figure 8.10
Total Deposits and Borrowings of LFCs and SLCs Sector

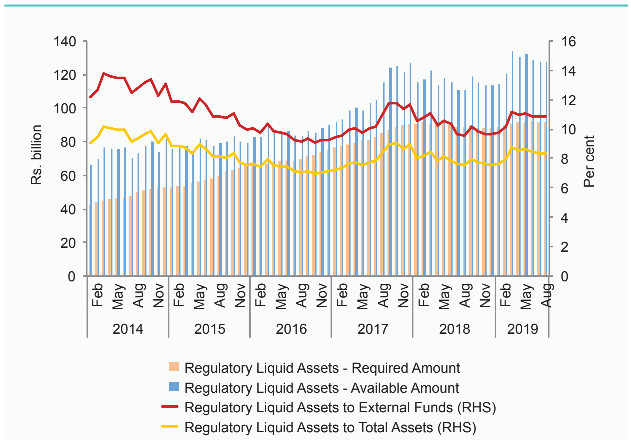


Source: Central Bank of Sri Lanka

2018. Deposits recorded a growth of 6.7 per cent (Rs. 48 billion) during the first eight months of 2019, compared to growth of 4.6 per cent recorded in the corresponding period of 2018. Borrowings of the sector showed a negative growth of 12.3 per cent (Rs. 57 billion), compared to the growth of 11.3 per cent (Rs. 45 billion) recorded in the corresponding period of 2018.

- **The overall liquidity position of LFCs and SLCs recorded a surplus.** The overall statutory liquid assets available in the sector at end August 2019 showed a surplus of Rs. 35.8 billion as against the stipulated minimum requirement of Rs. 91.7 billion. The liquidity ratio (liquid assets

Figure 8.11
Total Liquid Assets and Liquidity Ratio of LFCs and SLCs Sector



Source: Central Bank of Sri Lanka

Table 8.2
LFCs and SLCs Sector - Selected Indicators

Item	End Aug 2017	End Aug 2018 (a)	End Dec 2018	End Aug 2019 (b)	Y-O-Y Change (%)	
					Aug 2018 (a)	Aug 2019 (b)
Total Assets - Gross (Rs.billion)	1,363.7	1,469.6	1,503.5	1,531.2	7.8	4.2
Total Assets - Net (Rs.billion)	1,306.8	1,406.4	1,431.3	1,442.4	7.6	2.6
Loans & Advances - Gross (Rs.billion)	1,067.0	1,184.6	1,205.0	1,200.3	11.0	1.3
Loans & Advances - Net (Rs.billion)	1,020.2	1,125.1	1,137.0	1,115.2	10.3	-0.9
Deposits (Rs.billion)	635.6	718.0	716.8	764.6	13.0	6.5
Borrowings (Rs.billion)	413.2	440.7	463.8	406.9	6.6	-7.7
Capital Funds (Rs.billion)	164.1	184.1	181.6	204.8	12.2	11.2
Tier 1 Capital Adequacy Ratio (%)	12.6	9.8	9.8	11.2		
Total Capital Adequacy Ratio (%)	13.3	11.1	11.1	12.6		
Gross Non-performing Accommodations Ratio (%)	5.5	6.9	7.7	9.6		
Net Non-performing Accommodations Ratio (%)	1.3	2.2	2.4	3.1		
Return on Assets (Before Tax) (%) - Annualised	3.0	2.8	2.7	1.6		
Return on Equity (After Tax) (%) - Annualised	14.9	12.9	11.4	4.3		
Liquid Assets to Total Assets (%)	8.5	7.5	7.5	8.3		

(a) Revised
(b) Provisional

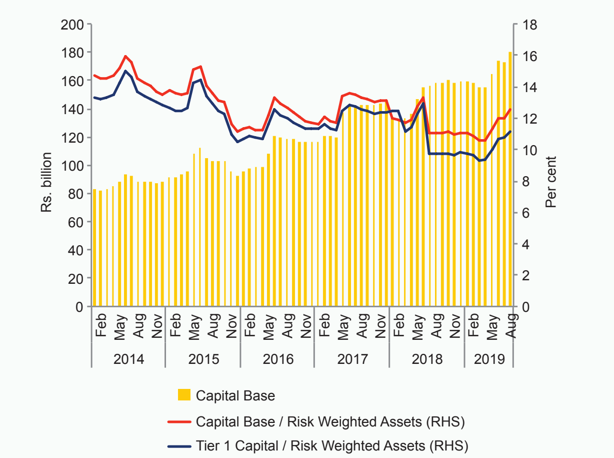
Source: Central Bank of Sri Lanka

on deposits and borrowings) increased to 10.9 per cent compared to the ratio of 9.6 per cent recorded at end December 2018. The increase in the ratio is attributed to the increase in available liquid assets by 12.3 per cent.

- **Capital levels of the sector improved due to the enhancement of regulatory capital requirements.** The total regulatory capital levels improved by Rs. 20.7 billion by end August 2019 compared to Rs. 159.9 billion recorded at end December 2018. The sector core capital and total risk weighted capital ratios increased to 11.2 per cent and 12.6 per cent, respectively, by end August 2019 from the reported level of 9.8 per cent and 11.1 per cent in December 2018. However, there are a few LFCs including distressed LFCs which do not comply with the stipulated minimum capital requirements.

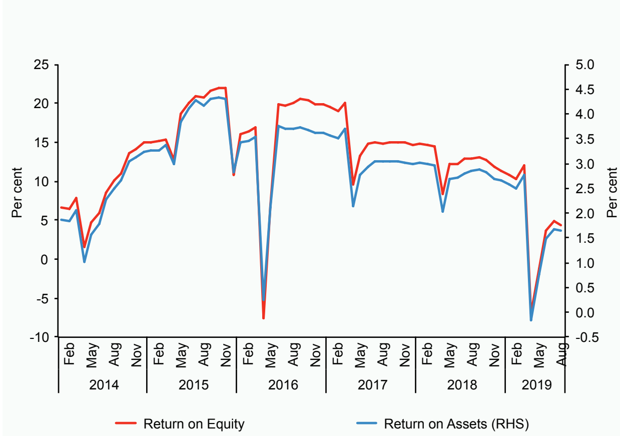
- **Profitability declined mainly due to rising NPLs**. Profits of the LFCs and SLCs sector was Rs. 9.8 billion for the first eight months of 2019 compared to the profit of Rs. 15.5 billion in the corresponding period of 2018. The sector profits for the period decreased mainly due to reduced NIM, increased operating expenses and higher loan loss provisions. NIM decreased as interest expenses increased by 5.2 per cent (Rs. 3 billion), while interest income increased only by

Figure 8.12
Capital Position of LFCs and SLCs Sector



Source: Central Bank of Sri Lanka

Figure 8.13
ROA and ROE of LFCs and SLCs Sector



Source: Central Bank of Sri Lanka

0.5 per cent (Rs. 0.6 billion). The annualized ROA and ROE ratios were at 1.6 per cent and 4.3 per cent, respectively, for the eight months period ending August 2019, compared to 2.8 per cent and 12.9 per cent in the corresponding period of 2018.

- **Several regulatory actions were initiated including imposing deposit, lending and borrowing restrictions on weak LFCs.** The Central Bank appointed a management panel to manage the business affairs of a distressed company. The Central Bank also facilitated another distressed finance company for repaying part of its deposits through the disposal of subsidiaries and other investment properties. Further, a part of the deposits of one distressed company was repaid using the funds generated by the company.

Primary Dealer Companies

- **Total assets and total portfolio of the Primary Dealer Companies (PDCs) decreased during the first eight months of 2019.** Total assets of PDC industry decreased by 4.5 per cent to Rs.79.8 billion and the total portfolio of government securities held by PDCs decreased by 4.0 per cent to Rs. 73.7 billion during the first eight months of the year. This decline was mainly caused by the decrease in the Investment portfolio. Borrowings under repo agreements also unveiled a decline by 7.1 per cent to Rs. 63.8 billion by the end of August 2019 in comparison to that of end August 2018.

- **Profitability of PDCs measured in terms of the ROA and ROE stood at 6.9 per cent and 33.1 per cent, respectively, during the first eight months of 2019.** Overall, PDCs recorded a profit of Rs. 3.7 billion over the eight months period ended August 2019 compared to the profit of Rs. 1.4 billion corresponding to that of the same period of 2018. PDCs recorded total gains (realised and unrealised) of Rs. 3.1 billion for the eight months ended August 2019, which has increased significantly compared to the Rs. 0.9 billion recorded in the corresponding period in 2018. The downward trend in the yield curve affect to increase the profitability of PDCs significantly during the first eight months of 2019.

- **All PDCs maintained their core capital above the minimum requirement of Rs. 1,000 million at the end of August 2019.** The Risk Weighted Capital Adequacy Ratio (RWCAR) of the PDCs was above the minimum RWCAR of 10.0 per cent and the ratio increased to 23.0 per cent by end August 2019 from 21.3 per cent at the end August 2018.

Table 8.3
Primary Dealer Companies - Selected Indicators

Item	End Aug 2017	End Aug 2018	End Dec 2018	End Aug 2019 (a)	Y-O-Y Change (%)	
					Aug 2018	Aug 2019 (a)
Total Assets (Rs. billion)	**67.6**	**73.9**	**83.6**	**79.8**	**9.2**	**8.0**
Total Portfolio (Rs. billion)	50.6	67.3	76.7	73.7	33.0	9.4
Total Capital (Rs. billion)	22.7	11.9	11.5	14.4	-47.4	20.6
Profit before Tax (Rs. billion)	**2.4**	**1.3**	**-0.01**	**3.7**	**-43.5**	**180.2**
Risk Weighted Capital Adequacy Ratio (%)	58.8	22.3	21.3	23.0	-36.4	0.7
Return on Assets (%)	4.8	2.8	-0.02	6.9	-2.0	4.1
Return on Equity (%)	14.2	13.9	2.0	33.1	-0.3	19.2
Leverage Times	**1.9**	**5.1**	**6.0**	**4.4**	**165.4**	**-12.5**
Operating Expenses to Total Income (%)	12.1	11.6	12.8	7.0	-0.5	-4.6
Total Cost to Total Income (%)	24.0	31.8	103.0	13.4	7.8	-18.3
Duration of Assets and Liabilities (years)	2.4	2.5	2.4	2.5	3.9	2.7

(a) Provisional
Note: 1. Excludes financials of Entrust Securities PLC
2. Excludes financials of Perpetual Treasuries PLC for 2018 and 2019

Source: Central Bank of Sri Lanka

Table 8.4
Insurance Sector - Selected Indicators

Item	End Jun 2017	End Jun 2018	End Dec 2018	End Jun 2019 (a)	Y-O-Y Change (%)	
					Jun 2018	Jun 2019 (a)
Total Assets (Rs. billion)	**533.1**	**581.8**	**606.6**	**654.0**	**9.1**	**12.4**
Total Income (Rs. billion) (b)	**96.6**	**108.1**	**221.2**	**119.0**	**11.8**	**10.2**
Gross Written Premium Income (Rs. billion) (b)	76.2	85.8	176.2	93.6	12.6	9.2
Investment Income (Rs. billion) (b)	20.5	22.3	45.0	25.4	8.9	13.8
Profit Before Tax (Rs. billion) (b)	**4.7**	**21.7**	**29.5**	**12.5**	**364.7**	**-42.4**
Capital Adequacy Ratio (CAR) (%)						
Long-term Insurance	358.0	310.3	312.0	293.0		
General Insurance	117.0	179.5	204.0	193.0		
Retention Ratio (%)						
Long-term Insurance	95.9	96.0	95.8	96.1		
General Insurance	78.5	76.1	77.9	75.7		
Claims Ratio (%)						
Long-term Insurance	36.9	44.2	46.2	47.5		
General Insurance	63.9	63.7	63.7	63.2		
Combined Operating Ratio (%)						
Long-term Insurance	86.2	98.0	101.0	98.4		
General Insurance	102.9	101.4	102.9	103.5		
Return on Assets (ROA) (%)						
Long-term Insurance	1.8	8.5	4.9	10.8		
General Insurance	8.9	5.1	5.4	4.6		
Return on Equity (ROE) (%)-General Insurance	**18.8**	**10.4**	**11.2**	**9.6**		
Underwriting Ratio (%) - General Insurance	**17.1**	**18.0**	**18.1**	**17.8**		

(a) Provisional
(b) During the period

Source: Insurance Regulatory Commission of Sri Lanka

- **Risk profile of the PDCs improved.** As the proportion of trading portfolio to total portfolio marginally increased from 77.7 per cent at end August 2018 to 79.0 per cent at end August 2019, the exposure of the industry to the market risk remain stable during the first eight months of 2019. In view of the large proportion of risk free government securities holdings of PDCs and also the ability of PDCs to use such government securities as collateral for obtaining funds to bridge unforeseen liquidity gaps, the liquidity risk profile of PDCs remained low. Further, most of the PDCs had stand-by contingency funding arrangements to bridge liquidity gaps, if materialised.

Insurance Sector

- **The overall performance of the insurance sector improved with total assets showing a healthy growth.** The total assets of the insurance sector grew by 12.4 per cent at end June 2019 as against 9.1 per cent reported during the corresponding period of 2018. The growth of the Gross Written Premium (GWP) was 9.2 per cent at end June 2019 which was a deceleration from 12.6 per cent reported at end June 2018. The GWP of the long-term insurance sector increased by 9.9 per cent at end June 2019, while the general insurance sector grew by 8.6 per cent. When considering the sub-sectors of the general insurance sector, health insurance has indicated the highest growth of GWP which was 31.2 per cent, followed by fire insurance at 28.3 per cent, marine insurance at 4.5 per cent and motor insurance at 3.1 per cent. Compared to the corresponding period of year 2018, fire insurance, health insurance and marine insurance have recorded higher growth in GWP, whereas, growth in motor insurance has decelerated.

- **The insurance sector profits declined during the period under consideration**. The total profit of the sector declined by 42.4 per cent at end June 2019 compared to June 2018 mainly due to the base effect. Profits sharply declined by 51.6 per cent in the long-term insurance sector whereas the general insurance sector profits have declined only by 5.4 per cent. The

Table 8.5
Unit Trust Sector - Selected Indicators

Item	End Jun 2017	End Jun 2018	End Dec 2018	End Jun 2019 (a)	Y-O-Y Change (%)	
					Jun 2018	Jun 2019 (a)
Total Assets (Rs.billion)	104.3	64.8	64.3	75.5	-37.9	16.5
Net Asset Value - NAV (Rs.billion)	103.3	64.6	64.2	75.2	-37.4	16.4
Investments (Rs.billion)	102.3	64.8	64.3	75.3	-36.7	16.3
Equity	14.4	11.1	9.5	8.0	-22.8	-27.4
Government Securities	42.8	5.3	2.5	4.0	-87.6	-24.4
Other (e.g.,Commercial Papers, Debentures, Trust Certificates & Bank Deposits)	45.2	48.4	52.4	63.3	7.1	30.8
Investments in Equity as a % of NAV	13.9	17.2	14.7	10.7		
Investments in Government Securities as a % of NAV	41.0	8.2	3.8	5.3		
Other Investments as a % of NAV	43.8	74.9	81.5	84.1		
Total No. of Unit Holders	40,651	41,200	42,093	44,224		
No. of Units in Issue (billion)	6.7	2.0	3.4	3.6		
No. of Unit Trusts	76	79	75	75		

(a) Provisional

Source: Securities and Exchange Commission
Unit Trust Association of Sri Lanka

long-term insurance sector profits in June 2018 was unusually high due to a one off surplus transfer made by two insurance companies during the year which was created as a result of change in valuation method of life policy holder liabilities, to comply with regulations issued by the Insurance Regulatory Commission of Sri Lanka. Contribution of the long-term insurance sector to the overall profit of the insurance sector was 67.1 per cent.

Unit Trust Sector

- **Performance of the unit trust sector indicated an overall improvement during the period under consideration.** The total number of unit holders increased to 44,224 by end June 2019 from 41,200 in end June 2018, even though the number of Unit Trusts in operation declined by 4 by end June 2019. The net asset value has increased by 16.4 per cent from a decline reported during the last year. Investments on equity have declined by 27.4 per cent during the period under consideration, while investment in other securities increased by 30.8 per cent.

Stock Broker Companies Sector

- **The stock broker companies sector indicated a decline in its overall performance in line with dismal performance of the equity market.** The income of the stock broker companies substantially declined by 37.7 per cent to Rs. 239.6 million at end June 2019 due to a drop in average daily turnover compared to the corresponding period of the previous year. Subsequent to the decline in income, the loss position of the stock broker companies sector has worsened to Rs. 184.1 million at end June 2019 from the loss of Rs. 57.9 million reported at end June 2018. Net capital level of the sector has decreased by 8.4 per cent during the period under consideration.

Table 8.6
Stock Broker Companies Sector - Selected Indicators

Item	End Jun 2017	End Jun 2018	End Dec 2018	End Jun 2019 (a)	Y-O-Y Change (%)	
					Jun 2018	Jun 2019 (a)
Total Assets (Rs. billion)	12.8	10.5	8.7	7.5	-18.4	-27.9
Total Liabilities (Rs. billion)	7.3	5.0	3.3	2.5	-31.7	-49.5
Net Capital (Rs. billion)	5.6	5.5	5.3	5.0	-1.0	-8.4
Income (Rs. million) (b)	447.2	384.6	502.0	239.6	-14.0	-37.7
Net Profit/(Loss) Before Tax (Rs. million) (b)	35.3	-57.9	1.9	-184.1	-263.8	-218.2

(a) Provisional
(b) During the period

Source: Securities and Exchange Commission of Sri Lanka

Superannuation Funds

- **The Employees' Provident Fund (EPF) is the largest superannuation fund in Sri Lanka with an asset base of over Rs. 2.4 trillion as at end June 2019.** The total number of member accounts of EPF reached 18.7 million mark in December 2018, recording an increase of 3.9 per cent when compared with the previous year.

- **Total member contributions during the first six months of 2019 increased by 10.3 per cent to Rs. 78.3 billion while refund payments increased by 27.0 per cent to Rs. 64.0 billion when compared with the corresponding period of the previous year.** Accordingly, the net contribution received (net of contributions received and refunds paid) during the period under review stood at Rs. 14.3 billion.

- **During the 12 months period ending 30 June 2019, total assets of EPF increased by 10.8 per cent to Rs. 2,428 billion whereas the total investment of EPF also grew by 14.9 per cent to Rs. 2,425 billion.** The investment of EPF consists of 94.0 per cent in government securities, 2.6 per cent in equity market, and 2.5 per cent in corporate debt, trust certificates and reverse repo and 0.9 per cent in fixed deposits. The Fund estimated a gross investment income of Rs. 115.0 billion during the first half of 2019, which is an increase of 2.8 per cent compared with the corresponding period of 2018.

- **The Employees' Trust Fund (ETF) expanded in terms of both assets and net contributions at end June 2019.** The total assets grew by 11.1 per cent by end June 2019 compared to the end June 2018 and stood at Rs. 327.7 billion. The net contributions of the ETF increased to Rs. 3.2 billion by 10.3 per cent during the period under consideration. The investment portfolio of the ETF is concentrated in government securities, which accounted for 77.8 per cent of the total portfolio by end June 2019. Investments in equity and corporate debt securities accounted for 3.5 per cent and 1.1 per cent, respectively, of the total investments.

- **The Public Service Provident Fund (PSPF) contracted in terms of assets while showing an expansion in terms of the number of members and net contributions at end June 2019.** The active members of the fund increased to 230,414 at end June 2019 compared to 228,700 recorded at end June 2018. Total assets declined by 2.4 per cent and stood at Rs. 62.7 billion while investments of the PSPF declined by 6.2 per cent to Rs. 58.8 billion in 2019. However, the net contribution increased to Rs. 240.3 million by end June 2019, compared to Rs. 50.9 million by end June 2018. The investments in government securities accounted for 44.0 per cent of total investments. The rate of return on member balances was 12.6 per cent for the first half of 2019.

Table 8.7
Superannuation Funds - Selected Indicators

Item	Employees' Provident Fund (EPF)			Employees' Trust Fund (ETF)		
	End Jun 2018	End Jun 2019 (a)	Change (%)	End Jun 2018	End Jun 2019 (a)	Change (%)
Total Contributions (Rs. billion) (b)	71.0	78.3	10.3	12.3	13.4	8.9
Total Refunds (Rs. billion) (b)	50.4	64.0	27.0	9.4	10.2	8.7
Total Assets (Rs. billion)	2,191	2,428	10.8	295.0	327.7	11.1
Total Investment Portfolio (Rs. billion)	2,111	2,425	14.9	277.9	308.3	10.9
o/w, Government Securities (%)	91.6	94.0	2.4	75.0	77.8	3.7
Gross Income (Rs. billion) (b)	112.2	115.3	2.8	14.5	15.9	9.9

(a) Provisional
(b) During the period

Sources: Central Bank of Sri Lanka
Employees' Trust Fund Board

- **The number of Approved Private Provident Funds (APPFs) further declined to 123 at end June 2019 due to closure of entities registered with such funds, compared to 127 funds remained at end June 2018.** Accordingly, the total number of members of the APPFs declined to 134,465 in June 2019 from 169,201 recorded at end June 2018. Total assets of APPFs declined by 2.9 per cent to Rs. 174.5 billion by end June 2019 compared to end 2018.

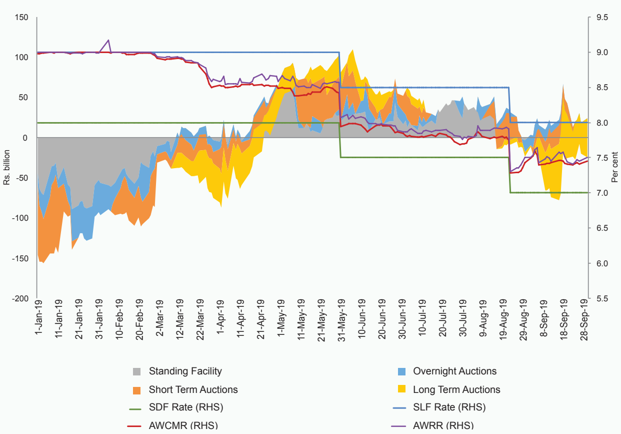
Developments in Financial Markets

Domestic Money Market

- **The Average Weighted Call Money Rate (AWCMR), which remained closer to the upper bound of the Standing Rate Corridor (SRC) during the first three months of the year, declined following the monetary policy relaxing measures amidst active Open Market Operations (OMOs) aimed at steering the AWCMR towards the middle rate of the SRC.** During the latter part of 2018 and early 2019, AWCMR was maintained at the upper bound of the SRC in view of external sector concerns. Despite releasing liquidity of around Rs. 60 billion to the domestic money market following the downward revision of the Statutory Reserve Ratio (SRR) by hundred basis points to 5.00 per cent from 6.00 per cent with effect from 01 March 2019, the AWCMR remained at the upper bound of the SRC. With the improvement of the external sector environment, the AWCMR was allowed to move towards the middle of the SRC, supported by favourable liquidity conditions in the money market since mid-April 2019. Following the reduction in the Standing Deposit Facility Rate (SDFR) and the Standing Lending Facility Rate (SLFR) by 50 basis points to 7.50 per cent and 8.50 per cent, respectively, in May 2019, the AWCMR declined below the middle of the SRC. An upward pressure in the AWCMR was observed since August 2019, in spite of the liquidity surplus in the domestic money market. The asymmetric liquidity distribution among Licensed Commercial Banks (LCBs) and the limited participation of the foreign LCBs in the call money market led to an increase in the interest rate in the call money market. In response to the OMOs of the Central Bank which were conducted with the view to maintain the short term interest rates in line with the monetary policy stance, the AWCMR indicated some downward adjustment towards the lower bound of the SRC. At the same time with the reduction of the SDFR and the SLFR by 50 basis points to 7.00 per cent and 8.00 per cent, respectively, in August 2019 the AWCMR indicated a significant downward adjustment. Thus, being guided by the monetary policy stance of the Central Bank, the AWCMR was allowed to move towards the middle rate of the SRC through appropriate OMOs. The introduction of the Liquidity Support Facility (LSF) to the Standalone Primary Dealers (SPDs) by the Central Bank since early September 2019 also helped the Central Bank to steer the AWCMR and hence improve the signaling mechanism of OMOs. The Average Weighted Repo Rate (AWRR) also followed a similar trend of AWCMR. With the introduction of the LSF the gap between AWCMR and AWRR was reduced. AWCMR and AWRR stood at 7.45 per cent and 7.50 per cent, respectively, by end September 2019.

- **During the first nine months of 2019, liquidity in the domestic money market indicated mixed movements.** Liquidity management operations were carried out by the Central Bank to maintain the AWCMR within the policy rate corridor in consistence with the monetary policy stance, while avoiding large fluctuations in AWCMR through maintaining adequate liquidity in the domestic money market. Accordingly, during first three months of 2019, the Central Bank actively engaged in OMOs by conducting overnight, short-term and long-term reverse repo auctions to inject liquidity, while conducting outright purchase of Treasury bill auctions to inject liquidity to the domestic money market on a permanent basis. In addition, the Central Bank reduced the SRR by hundred basis points to 5.00 per cent with

Figure 8.14
Standing Rate Corridor, AWCMR and Market Liquidity



Source: Central Bank of Sri Lanka

effect from 01 March 2019 to ease the pressure on liquidity in the domestic money market, in addition to the SRR reduction in November 2018. The liquidity position remained at deficit levels until mid-April 2019 mainly due to foreign exchange related transactions carried out by the Central Bank as well as currency withdrawals for the festive season in April. Subsequently, liquidity deficit turned into a surplus level from mid-April 2019 mainly due to a conversion of sovereign bond proceeds, foreign currency purchases by the Central Bank and currency deposits after the festive season. Liquidity injections through the SRR reductions along with appropriate OMOs, led to a gradual decline in the AWCMR. The surplus liquidity in the domestic money market was absorbed by the Central Bank through overnight, short term and long-term repo auctions since May 2019. Although the market was in surplus levels, liquidity was mainly concentrated among certain banks, particularly foreign LCBs. Considering the asymmetric distribution of liquidity in the domestic money market the Central Bank conducted overnight and short-term reverse repo auctions with a view to induce a downward adjustment in the AWCMR despite the surplus liquidity position in the domestic money market. By end August 2019, with the maturing of Swaps and Treasury bills held by the Central Bank, liquidity in the domestic money market turned into negative levels. As a result, the Central Bank conducted overnight, short-term and long-term reverse repo auctions while conducting outright auctions for Treasury bills to inject liquidity to the market on a permanent basis. In addition, considering anticipated movements in the liquidity condition in the domestic money market, the Central Bank conducted auctions for outright purchase of Treasury bonds to inject liquidity into the domestic money market on a permanent basis since mid-September 2019. In September 2019, the Central Bank injected around Rs. 8.4 billion to the domestic money market through outright purchase of Treasury bond auctions. In addition, conversion of International Sovereign Bond (ISB) proceeds in to domestic currency contributed to increase the liquidity level of the domestic money market in September 2019. Under LSF, the Central Bank has provided about Rs.17 billion in September 2019 to support short-term funding needs of SPDs. By end September 2019, market liquidity stood at a surplus of around Rs.23 billion.

Domestic Foreign Exchange Market

- **During the first nine months of 2019, the Sri Lankan rupee marginally appreciated against the US dollar by 0.44 per cent from Rs. 182.75 at end December 2018 to Rs. 181.94 at end September 2019.** The positive impact of the policy measures taken in late 2018 to curtail imports, the easing of external pressure and the increased conversions of export proceeds and worker remittances resulted in the exchange rate appreciating at a higher pace during the first half of 2019. Despite the slight increase in the pressure on the exchange rate following the Easter Sunday attacks and the decline in inflows on account of tourism observed in the aftermath of the attacks, the receipts of the delayed sixth tranche of the Extended Fund Facility (EFF) from the International Monetary Fund (IMF) in May 2019, and the International Sovereign Bond (ISB) issuance in June 2019 supported to uphold the value of Sri Lanka rupee against the US dollar. Accordingly, the Sri Lankan rupee appreciated by 3.53 per cent in the first half of 2019. However, this situation turned around during the month of

Figure 8.15
Movement of Rupee per US dollar

Source: Central Bank of Sri Lanka

August, mainly due to the repatriation of foreign investments from the government securities market, which continued till September 2019. Further, the gradual increase in import demand for vehicles following the easing of the policy measures that were imposed in 2018 and the high demand for foreign currency to import oil resulted in the exchange rate to depreciate by 2.98 per cent in the third quarter of 2019. Accordingly, the rupee appreciated by 0.44 per cent in the first nine months of 2019. Meanwhile, in the first nine months of 2019, Sri Lankan rupee appreciated against the Indian rupee as well as other major currencies such as Australian dollar, sterling pound and euro, while depreciating against the Japanese yen.

- **The Central Bank was a net buyer in the domestic foreign exchange market during the first nine months of 2019.** Continuous purchases of US dollars from the market despite moderate sales during periods of excessive volatility in the exchange rate, enabled the Central Bank to build up the foreign reserves of the country. Accordingly, during the first nine months of 2019, the Central Bank absorbed US dollars 469.7 million and supplied US dollars 184.9 million resulting in a net purchase of US dollars 284.8 million.

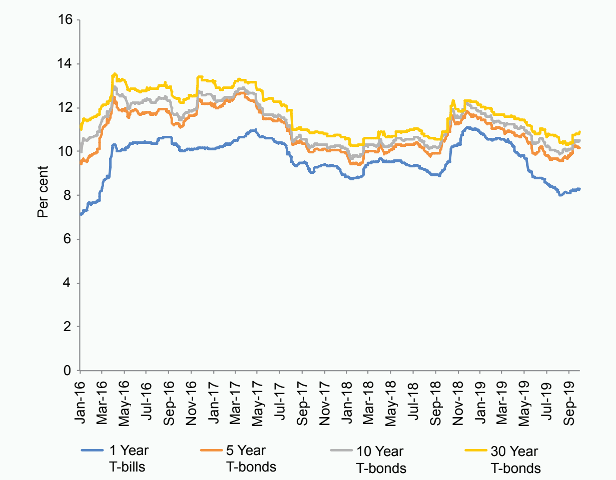
- **During the first nine months of 2019, trading volumes in the domestic foreign exchange interbank market increased by 13.6 per cent compared with the corresponding period in 2018.** The total volume of inter-bank foreign exchange transactions amounted to US dollars 14.9 billion during this period compared to US dollars 13.1 billion in the corresponding period of 2018. In line with this, the daily average volumes in the inter-bank foreign exchange market increased to US dollars 82 million during the reference period in 2019, from US dollar 73 million in the corresponding period of 2018. Meanwhile, the total volume of forward transactions for the period up to end September 2019 increased to US dollars 6.1 billion compared to US dollar 5.0 billion during the period under review in 2018.

Government Securities Market

- **During the first half of 2019, a majority of borrowings of the Government was sourced from the foreign currency markets.** Capitalizing on the conducive opportunities which prevailed in international capital markets, the Government of Sri Lanka issued International Sovereign Bonds (ISBs) amounting to US dollars 4.4 billion and Sri Lanka Development Bonds (SLDBs) amounting to US dollars 345.2 million during the first half of 2019. These issuances were also intended to offset any possibilities of crowding out the available investible funds in the domestic market. Meanwhile, the yield rates of the primary market issuances of Treasury bills and Treasury bonds in the domestic market reverted from its increasing trend noted during the early part of the year to decline towards the latter part of the first half of 2019, in line with the availability of ISB proceeds and the monetary policy stance of the Central Bank.

- **A downward shift was observed in the secondary market yield curve of Government securities by the end of the first half of 2019, in comparison to the corresponding period of 2018.** Secondary market yield rates, which showed an increasing trend during the fourth quarter of 2018 and the early part of 2019, declined

Figure 8.16
Secondary Market Yield Curve of Government Securities



Source: Central Bank of Sri Lanka

gradually since the second half of 2019 reflecting the positive market sentiments associated with the issuance of ISBs amounting to US dollars 2.4 billion and US dollars 2.0 billion in March and June 2019, respectively. Accordingly, by end June 2019, the secondary market yield rates of Treasury bills with maturities of 91-day, 182-day and 364-day declined by 139 basis points, 153 basis points and 227 basis points, respectively, from the rates prevailed at end 2018. Meanwhile, the market yield rates of actively traded Treasury bonds with maturities ranging from 2 to 10 years declined by 34 to 109 basis points during the period under review. The receipt of foreign exchange from ISB issuances coupled with enhanced transparency and predictability in the issuance process of government securities and aligning the issuances of government securities with the debt service payments cycle, contributed positively towards easing the pressure on the interest rates in the domestic market till mid-August 2019. Further, reflecting the combined effect of reducing the threshold of foreign investments in Treasury bills and Treasury bonds from 10.0 per cent to 5.0 per cent of the total outstanding stock with effect from 18 January 2019 and the net foreign outflows from emerging market economies including Sri Lanka, the non-resident holdings of Treasury bills and Treasury bonds declined by 10.1 per cent to Rs. 142.7 billion by end June 2019, from Rs. 158.8 billion recorded at end 2018.

Corporate Debt Securities Market

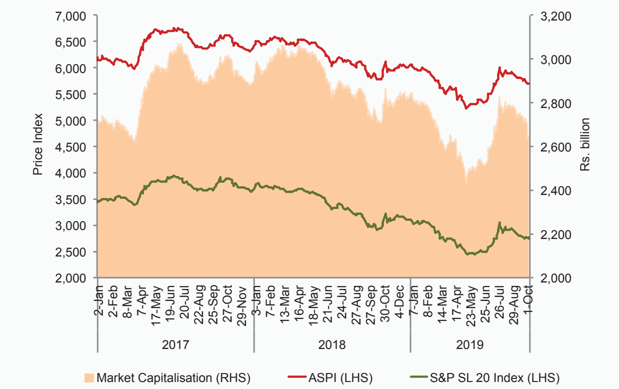
- **Activities of the commercial paper (CPs) market slightly improved during the first eight months of 2019 compared to the corresponding period of 2018.** The value of commercial papers (CPs) issued with the support of banks increased to Rs. 2.4 billion during the first eight months of 2019 in comparison to Rs. 1.7 billion issued during the corresponding period of 2018. The interest rates applicable on CPs issued during the first eight months of 2019 ranged between 14.85 per cent to 16.25 per cent compared to the range of 13.10 per cent to 15.00 per cent recorded in the first eight months of the previous year. CPs with a maturity up to 3 months accounted for 88.7 per cent of the market, while only one issuance with a 12-month maturity period of Rs. 822.9 million worth CPs was recorded during the first eight months of 2019. The total outstanding value of CPs amounted to Rs. 2.2 billion as at end August 2019 compared to Rs. 1.2 billion as at end August 2018.

- **New issuances in the corporate bond market declined during the first nine months of 2019.** During the first nine months of 2019, there were 17 listings of corporate debentures by 9 institutions, compared to 20 listings by 10 institutions during the corresponding period of the previous year. Accordingly, the total funds mobilised through these debentures declined to Rs. 35.6 billion during the first nine months of 2019 compared to Rs. 55.3 billion recorded in the corresponding period of the previous year. This may be due to the negative investor sentiment along with the slowdown of the economy. The interest rate of these debentures ranged from 12.88 - 15.50 per cent during the period under review, compared to the interest rates of 12.00 - 14.75 per cent observed during the first nine months of 2018.

Equity Market

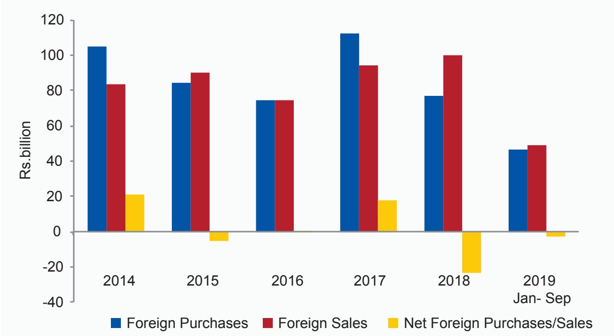
- **The sluggish performance observed in the Colombo Stock Exchange in the latter part of 2018, continued in the first nine months of 2019 as well, with volatile movements in**

Figure 8.17
Movements of Share Price Indices



Source: Colombo Stock Exchange

Figure 8.18
Foreign Participation at the CSE



Source: Colombo Stock Exchange

price indices throughout the period. Reflecting the immediate adverse shock of the Easter attack, both All Share Price Index (ASPI) and S&P Sri Lanka 20 index declined significantly, by 3.6 per cent and 4.4 per cent, respectively, on 23 April 2019. With the lower price earnings ratio of 8.4 times which prevailed in June 2019, the local investors started to invest in stocks at the prevailing lower price and it boosted the performance of the equity market in July 2019. However, this momentum was not continued in August and September 2019.

- **The ASPI and S&P Sri Lanka 20 index decreased by 5.2 per cent and 12.0 per cent, respectively, during the year until end September 2019.** Market capitalisation decreased to Rs. 2,709.2 billion at end September 2019 compared to Rs. 2,839.4 billion at end 2018. Meanwhile, the average daily turnover for the first nine months of 2019 decreased to Rs. 661.0 million compared to Rs. 833.6 million in the previous year. Net cumulative foreign sales were Rs. 2.6 billion at end September 2019 compared to net cumulative foreign sales of Rs. 6.1 billion recorded at end September 2018. Foreign outflows from equity market were largely attributable to the policy uncertainty, negative spill over of the Easter attack and sluggish performance of the corporate sector. However, the market price earnings ratio (PER) increased to 10.2 times at end September 2019 compared to 9.2 times prevailed at the end September 2018. During the period, one Initial Public Offering (IPO) in CSE raised Rs. 0.4 billion

Table 8.8
Equity Market - Selected Indicators

Item	End 2017	2018 Sep	End 2018	2019 Sep
All Share Price Index (1985=100)	6,369.3	5,862.2	6,052.4	5,738.2
Year to date change (%)	2.3	-8.0	-5.0	-5.2
S&P SL 20 Index (2004=1,000)	3,671.7	3,002.0	3,135.2	2,759.2
Year to date change (%)	5.0	-18.2	-14.6	-12.0
Market Capitalisation (Rs. billion)	2,899.3	2,752.9	2,839.5	2,709.2
As a Percentage of GDP (%) (a)	20.1	19.1	19.7	18.7
Market Price Earning Ratio	10.6	9.2	9.7	10.2
Average Daily Turnover (Rs. million)	915.3	787.6	833.6	661.0
Net Cumulative Foreign Purchases (Rs. billion)	17,657.4	-6,118.2	-23,247.5	-2,570.4
Number of Companies Listed	296	297	297	290
Number of Right Issues	15	14	16	14
Amount raised through Right issues (Rs. billion)	50.6	38.1	42.2	30.6
Initial Public Offers	2	2	2	1
Amount raised through IPOs (Rs. billion)	1.0	2.0	2.0	0.4

(a) Based on GDP for 2018 (Rs. 14,450 billion)

Source: Colombo Stock Exchange

8

compared to two IPOs which raised Rs. 2.0 billion during the corresponding period of the year 2018. Further, during the first nine months of 2019, Rs. 30.6 billion was raised through 14 rights issues compared to Rs. 38.1 billion raised through 14 right issues during the corresponding period of year 2018.

Developments in Financial Infrastructure

Payment and Settlement Systems

- **The LankaSettle System which comprises of two closely integrated systems i.e. the Real Time Gross Settlement (RTGS) System and the LankaSecure System, continued to provide a safe and reliable mechanism for the settlement of high value transactions in the country. The RTGS system settles high value time critical customer and interbank transactions.** The daily average volume and value of RTGS transactions were 1,803 and Rs. 519 billion, respectively, during the first nine months of 2019.

- **The Cheque Imaging and Truncation System introduced in 2006 with the objective of increasing the efficiency of cheque clearing by reducing the island-wide cheque realization time to one day (T+1), continued to perform efficiently to settle retail payments.** The daily average volume and value of cheques cleared were 193,979 and Rs. 41 billion, respectively, during the first nine months of 2019.

- **Sri Lanka Interbank Payment System (SLIPS) which provides an online mechanism to facilitate high transaction volumes, continued to operate smoothly during the period under review.** The daily average volume and value of SLIPS transactions were 148,648 and Rs. 9 billion, respectively, during the first nine months of 2019.

- **The Central Bank continued to facilitate the establishment of sub switches of the Common Card and Payment Switch (CCAPS), i.e. Common ATM Switch (CAS), Common Electronic Fund Transfer Switch (CEFTS), Shared ATM Switch (SAS), Common POS Switch (CPS) and Common Mobile Switch (CMobS).** CCAPS is being operated by LankaClear (Pvt.) Ltd. (LCPL) under the brand name of "LankaPay".

- **CAS which facilitates domestic ATM transactions originated from any ATM in the CAS network, started live operations in July 2013.** The daily average volume and value of CAS transactions were 125,891 and Rs. 1.1 billion, respectively, during the first nine months of 2019. In order to enhance the security of card transactions carried through the CAS network, CAS members were instructed to enable EMV (Europay, MasterCard, Visa) technology in ATMs operated by them.

- **CEFTS was implemented in August 2015 which provides a common infrastructure to clear payments effected through multiple payment channels such as ATM, Internet Banking, Mobile Banking, Kiosks and over-the-counter.** The daily average volume and value of CEFTS transactions were 36,875 and Rs. 3.5 billion, respectively, during the first nine months of 2019. Considering the requirement of introducing digital payment mechanisms, the Central Bank granted approval to implement LankaPay Online Payment Platform (LPOPP) based on CEFTS to facilitate real time payments to public and private institutions. LPOPP was launched in July 2017 and initially facilitated real time payments to Sri Lanka Customs. In addition, the Central Bank granted approval to several other institutions to integrate with LPOPP. JustPay, which is another payment mechanism based on CEFTS, was implemented in 2017 targeting low value cash based payments, operated smoothly during the period under review.

- **CPS started live operations in June 2019 which provides switching and clearing facilities for payment card transactions carried out at POS terminals, mainly using payment cards issued by member institutions of CPS under the LankaPay National Card Scheme (NCS).** Three Licensed Commercial Banks (LCB) functioning as Licensed Financial Acquirers joined CPS while one LCB started issuing debit cards under NCS.

- **The National Payments Council (NPC), which is the industry consultative and monitoring committee on payment systems, finalised its Road Map for 2019 - 2021.** The Road Map broadly covers the areas of expanding interbank payment infrastructure, promoting e-payments, standardization and interoperability, innovations for payment systems, strengthening payment system security and public awareness. Further, NPC appointed a committee on FinTech developments to focus on new innovations such as the digital payment platform, the open application programming interface and virtual banking. In addition, NPC appointed a committee on Promoting Digitization of Payments to Enhance Financial Inclusion with the objective of utilizing digitalization to promote financial inclusion.

- **PSD issued a National Quick Response (QR) Code specification branded as "LankaQR" to promote customer convenience, safety and ensure interoperability of different payment mechanisms and instruments.** Several financial institutions launched "LankaQR" based payment products during 2019 while several other financial institutions are in the process of developing payment products based on "LankaQR".

Anti-Money Laundering and Countering Financing of Terrorism

- **The Financial Intelligence Unit (FIU) strengthened its multi-pronged strategy to ensure compliance of reporting institutions by effective monitoring and enforcement, onsite and offsite surveillance, raising awareness through seminars and conducting compliance review meetings on Anti-Money Laundering and Countering Financing of Terrorism (AML/CFT).** During the first nine months of the year, 25 risk-based onsite examinations were conducted to assess the financial institutions' (FIs) (i.e. Licensed Commercial Banks, Licensed Specialized Banks, Licensed Finance Companies, Insurance Companies and Stock Brokers) compliance with the Financial Transactions Reporting Act, No. 6 of 2006 (FTRA), Customer Due Diligence (CDD) Rules and other rules and regulations issued. FIU issued 29 warning letters, 4 Show Cause Letters and had 7 follow up discussions with senior management of FIs, and imposed proportionate and dissuasive sanctions against FIs that failed to comply with the AML/CFT requirements, during the period under consideration.

- **The FIU expanded its scope of assessment of institutional compliance to the designated non-finance businesses and professions (DNFBPs), which were recognized as high risk sectors for Money Laundering (ML) and Terrorist Financing (TF), and conducted 24 risk-based supervisions of the DNFBPs (Casinos, Gem and Jewellery and Real Estate Sectors) during the first nine months of the year.** 15 Warning Letters were issued to DNFBPs, informing the deficiencies identified at the onsite examinations and providing a time bound action plan to rectify the deficiencies. Further, during the first nine months of the year, with a view to strengthen the AML/CFT supervision process and institutional compliance, the FIU issued several rules and guidelines, on Suspicious Transactions Reporting, conducting ongoing customer due diligence based on risk-based approach, enhanced due diligence, identification of beneficial ownership and identification of Politically Exposed Persons (PEPs).

- **Since the listing in the Financial Actions Task Force (FATF)[3] Compliance Document "The Grey List" in November 2017, the FIU and Sri Lanka stakeholders have further taken a number of effective steps towards successful completion of the time bound action plan provided to Sri Lanka by the FATF to address the strategic deficiencies identified in AML/CFT activities.** These measures include passing Trusts (Amendment) Act, No. 6 of 2018, Mutual Assistance in Criminal Matters (Amendment) Act, No. 24 of 2018, issuing regulations/ directives/ guidelines on implementing United Nations Security Council Resolutions (UNSCR) on North Korea and Iran, extending the AML/CFT coverage to DNFBPs by issuing CDD Rules, conducting risk based AML/CFT supervision of the DNFBPs sector, taking enforcement actions on non-compliances observed and conducting Island-wide outreach for FIs and DNFBPs on AML/CFT obligations, identifying of beneficial ownership information and implementing of targeted financial sanctions.

- **The FATF assessed Sri Lanka's progress in implementing the Action Plan through Asia Pacific Joint Group (AP/JG).** The AP/JG acknowledged that Sri Lanka has made significant progress and thus, the FATF Plenary held in February 2019, has made the initial determination that Sri Lanka has completed its action plan substantially. Subsequently, an on-site assessment was conducted by the FATF International Cooperation Review Group (ICRG) to verify implementation of the FATF Action Plan, during 16-17 September 2019. The ICRG representatives had face-to-face meetings with all relevant stakeholders, including the private sector and the highest political authorities to ascertain Sri Lanka's political and institutional commitment towards implementation of AML/CFT. Recommendations made by the review team on Sri Lanka's progress were discussed at the FATF Plenary held in October 2019 and all members have endorsed the decision to delist Sri Lanka from the Grey List. It is expected that the delisting by the FATF will have positive economic and financial impact on Sri Lanka.

3 FATF is an independent inter-governmental body that develops and promotes policies to protect the global financial system against money laundering, terrorist financing and the financing of proliferation of weapons of mass destruction.

Legal Reforms Related to the Financial Sector

- **Several legal reforms were continued during the period concerned with the view of facilitating a smooth functioning of the financial system.** During 2019, steps have been taken to amend the Monetary Law Act, No. 58 of 1949. Additionally, arrangements and discussions were in progress to amend the Banking Act, No. 30 of 1988, Finance Business Act, No. 42 of 2011, Payment and Settlement Systems Act, No. 28 of 2005, Registered Stock and Securities Ordinance, No. 7 of 1937, Local Treasury Bills Ordinance, No. 8 of 1923 and the Debt Recovery (Special Provisions) Act, No. 2 of 1990.

Resolution and Enforcement Actions

- **The Central Bank has initiated processes and developed operational procedures on both resolution and enforcement functions.** An Enforcement Committee as well as Operational Procedures on conducting investigations and law enforcement was established. Several investigations were conducted on unauthorized finance businesses and prohibited schemes under the relevant provisions of the Finance Business Act and the Banking Act. Awareness programmes had also been conducted island-wide with a view to improve financial literacy and to educate on the ill-effects of unauthorized finance business and prohibited schemes. Further, a comprehensive Resolution Framework is being developed with technical assistance of a resident consultant from US Treasury.

- **The "RED Claims system" was developed during the year and is being used for compensation payments by the Sri Lanka**

Deposit Insurance and Liquidity Support Scheme (SLDILSS). The Monetary Board cancelled the licences of two finance companies namely Central Investments and Finance PLC (CIFL) and The Standard Credit Finance Limited (TSCFL) during 2018. SLDILSS was able to pay compensation to 2,800 depositors of CIFL and 2,125 depositors of TSCFL amounting to 1,187.58 million and 878.23 million respectively. Compensation payments for the depositors of TKS Finance Ltd. whose licence was cancelled by the Monetary Board in September 2019 will commence in the near future.

Development Finance and Access to Finance

- **The Central Bank continued its development finance activities by implementing several new policy measures to achieve inclusive and balanced economic growth facilitating small and medium scale entrepreneurs in the country and improving financial inclusion.** The Central Bank continued to coordinate, facilitate and implement various refinance, interest subsidy and credit guarantee schemes, funded by the Central Bank, Government, International Donor Agencies and Participating Financial Institutions (PFIs). During the first nine months of 2019, the Central Bank disbursed loans amounting to Rs. 9,910.2 million among 69,103 beneficiaries through the PFIs under 9 refinance loan schemes and 2 interest subsidy schemes. Out of the total amount of disbursements 65.1 per cent was granted through the interest subsidy schemes and the balance 34.9 per cent was granted through refinance loan schemes. The amount of loans disbursed by Government, Central Bank and Donors during the said period accounted for 70.5 per cent, 23.9 per cent and 5.6 per cent of total value of loans disbursed, respectively. The GOSL continued to fund 6 schemes consisting of 5 refinance schemes and 1 interest subsidy scheme by contributing Rs. 6,984.1 million or 70.5 per cent to the total loan disbursements in the first nine months of 2019 serving 63,321 beneficiaries.

Table 8.9
Loan Disbursements by Funding Source

Funding Source	Share (%)			
	2018 Jan - Sep		2019 Jan - Sep	
	No. of Loans	Amount Rs. mn.	No. of Loans	Amount Rs. mn.
Government Funded	93.3	72.2	91.6	70.5
Central Bank Funded	6.7	27.8	4.8	23.9
Donor Funded	0.0	0.0	3.6	5.6

Source: Central Bank of Sri Lanka

- **The New Comprehensive Rural Credit Scheme (NCRCS) which serves as an interest subsidy scheme and a credit guarantee scheme displayed a significant performance during the first nine months of 2019.** The number of loans disbursed under this scheme increased by 9.7 per cent to 55,000 loans and the amount disbursed increased by 12.4 per cent to Rs. 6,415.6 million compared to the corresponding period of the previous year. The Smallholder Agribusiness Partnerships Programme (SAPP) which commenced its lending activities in the fourth quarter of 2018, continued to perform well during the first nine months of 2019. The SAPP, jointly funded by the IFAD and the Government, granted 2,503 loans amounting to Rs.552.6 million during the said period. The credit component of the SAPP was restructured to enhance the operational efficiency and to deliver better service to the beneficiaries. The new credit component of SAPP includes two Public-Private-Producer-Partnership (4P) loan schemes (i.e. 4P Agribusiness and 4P Youth Loan Schemes) and three RF Loan schemes (i.e. RF Agribusiness, RF Youth and RF Income Generation Loan Schemes). The Central Bank continued to fund two principal loan schemes, i.e., “Saubagya – The Prosperity” Loan Scheme (SLS) and the Commercial Scale Dairy Development Loan Scheme (CSDDLS), targeting the Micro Small and Medium Enterprise (MSME) sector and Agriculture & Livestock sector respectively. In addition, the Central Bank disbursed 3,254 loans amounting to Rs. 2,335.2 million among entrepreneurs under the SLS.

Table 8.10

Loan Disbursements by the Government Funded Loan Schemes

Loan Scheme	Loan Disbursements				Growth (%)	
	2018 Jan - Sep		2019 Jan - Sep		2019 Jan - Sep	
	No. of Loans	Amount Rs. mn.	No. of Loans	Amount Rs. mn.	No. of Loans	Amount Rs. mn.
PAMP - RF	9,668.0	482.1	7,852.0	388.3	-18.8	-19.5
PAMP II - RF (a)	3,573.0	336.2	-	-	-100.0	-100.0
Swashakthi	1,608.0	332.9	138.0	44.7	-91.4	-86.6
Athwela (READ)	3,543.0	1,499.7	193.0	78.0	-94.6	-94.8
SEPI – Ph II	216.0	99.8	138.0	57.5	-36.1	-42.4
NCRCS	50,146.0	5,709.0	55,000.0	6,415.6	9.7	12.4
SAPP- Income Generation	-	-	-	-	-	-
Total	**68,754.0**	**8,459.7**	**63,321.0**	**6,984.1**	**-7.9**	**-17.4**

(a) Discontinued in July 2018 *Source:* Central Bank of Sri Lanka

- **Several development finance activities are in the pipeline.** A new Government funded refinance loan scheme for development financing and small and medium scale enterprises is to be introduced to provide the fund requirements for long term development projects, small and medium scale enterprises and working capital requirements of export oriented enterprises. Further, the Central Bank and the Ministry of Finance (MOF) entered into an agreement to implement a Government funded Partial Credit Guarantee Scheme (PCG Scheme) to be operated under the Enterprise Sri Lanka (ESL) Programme. The Smallholder Tea and Rubber Revitalization (STaRR) Interest Subsidy Scheme has been designed to provide concessionary loans to the smallholder farmers involved in tea replanting and rubber new planting activities to establish self-employment or short-term income generating activities until such time the production is generated in new plantations.

Table 8.11

Loan Disbursements by the Central Bank Funded Loan Schemes

Loan Scheme	Loan Disbursements				Growth -%)	
	2018 Jan - Sep		2019 Jan - Sep		2019 Jan - Sep	
	No. of Loans	Amount Rs. mn.	No. of Loans	Amount Rs. mn.	No. of Loans	Amount Rs. mn.
Saubagya	4,627.0	2,996.9	3,254.0	2,335.2	-29.7	-22.1
CSDDLS	275.0	262.7	25.0	38.3	-90.9	-85.4
Total	**4,902.0**	**3,259.6**	**3,279.0**	**2,373.5**	**-33.1**	**-27.2**

Source: Central Bank of Sri Lanka

- **The Central Bank was engaged in developing the National Financial Inclusion Strategy (NFIS) for Sri Lanka with the technical and financial assistance received from the International Finance Corporation (IFC).** Further, Central Bank initiated to conduct a Financial Inclusion Survey (FIS) with the assistance of the IFC. The 3rd consultative mission was successfully conducted during August 2019 to finalize the NFIS, and is expected to be launched the NFIS by the end of 2019. During the first nine months of 2019, the Central Bank conducted 95 programmes for more than 10,500 participants on financial literacy, entrepreneurship development and skill development. There was a wide participation for these programmes and the majority of the participants (70 per cent - 80 per cent) were women.

Expected Developments

- **Capital levels of banks are expected to strengthen further as a result of enhanced capital requirements and other regulatory requirements.** With the enhanced minimum capital levels to be effective from 31 December 2020 and the implementation of Basel III Capital Requirements, banks are expected to meet the enhanced requirement for high quality capital and those which are unable to comply, will be encouraged to consolidate on a voluntary basis or restrictions on banking operations will be imposed. Further, the adoption of the Basel III Leverage Ratio and the new accounting standard "Sri Lanka Financial Reporting Standard 9 on Financial Instruments" (SLFRS 9) will also result in banks to augment their capital level to meet these regulatory requirements. This will improve the ability of the banking sector to absorb shocks arising from financial and economic stresses, reducing the risk of spill-over from the financial sector to the real economy in the coming years.

- **The liquidity positions of banks are expected to be maintained at healthy levels with the adoption of the Liquidity Coverage Ratio (LCR) and the Net Stable Funding Ratio**

(NSFR) under the Basel III Liquidity Standards. Accordingly, the liquidity profiles of banks both in the short-term and long-term horizons will be strengthened through stable funding sources.

- **In line with the prevailing monetary policy direction and the Banking Act Directions issued to enhance credit flows to the economy, the credit growth of the banking sector is expected to pick-up gradually in the near-term.** In the recent past the Central Bank took measures to reduce interest rates in line with erased monetary policy stance. These measures are expected to be an impetus to drive credit growth and support economic activity. At present, a gradual increase in the non-performing loans is observed due to the challenges in the operating environment and banks will need to be cautious of further increase in non-performing loans associated with the increase in credit and ensure that proper risk management mechanisms are in place to mitigate all relevant risks.

- **Macro-economic dynamics will be monitored to identify and address any spill-over risks arising from the real economy to the banking sector.** Accordingly, appropriate macroprudential measures will be introduced, if necessary to pre-empt any future risks to the stability of the banking system arising from any adverse developments. The regulatory and supervisory framework pertaining to licensed banks will be further strengthened in line with the Basel Core Principles on Effective Banking Supervision and other international and regional best practices.

- **The legal and regulatory framework of licensed banks will be further strengthened through new Banking Act**. The key areas proposed to be factored in to the new Banking Act include an overall mandate for supervision and regulation, a differentiated regulatory framework to facilitate proportionality, strengthening corporate governance, consolidated supervision, resolution, imposing monetary penalties/fines, ring-fencing of banks to mitigate contagion risk, strengthening provisions for mergers, acquisitions and consolidation, subsidiarisation of large foreign banks and financial holding company structure for banks.

- **Examination methodology of banks will continue to be enhanced focusing on the efficiency, effectiveness and sustainability of individual banks and the banking sector.** A new supervisory rating model (Bank Sustainability Rating Indicator-BSRI) is being developed by the Central Bank of Sri Lanka with a view to facilitate the risk based supervision framework of licensed banks and to enable early intervention and prompt corrective actions for licensed banks.

- **Considering the need to protect banks from contagion risk, and to ensure the stability and the soundness of the banking sector and the financial system, consolidated supervision of banking groups will also be carried out**. Accordingly, a regulatory framework on consolidated supervision will be formulated and provisions in this regard will also be brought into the Banking Act. Further, in order to strengthen inter-regulatory cooperation and collaboration in this regard, the Central Bank, Securities and Exchange Commission of Sri Lanka and the Insurance Regulatory Commission of Sri Lanka entered into a tri-partite memorandum of understanding on risk-based consolidated supervision where the Central Bank will be the lead regulator.

- **Emergence of FinTech and advanced technologies like Blockchain, while opening up new business opportunities may change business models of banks significantly over time.** These technological developments may lead to an emerging risk for the banking sector. Accordingly, adoption of these new technologies need to be encouraged while ensuring the safety and soundness of the banking system.

- **With the increased risk in cyber security, changes will be introduced to the regulatory and supervisory framework with respect to Cyber-Security, pertaining to banks in line with international standards and best practices.** The proposed regulations will prompt banks to upgrade and strengthen their information systems and related technological platforms enabling banks to cater to resulting information requirements. The Central Bank has also issued a Road Map to banks to mitigate technology risk in the banking sector with a timeline for implementation from 2019 to 2020. Further, a consultation paper on technology risk resilience was also issued to banks for comments and observations and Banking Act Directions will be issued shortly in this regard.

- **The banking sector is expected to facilitate access to banking services throughout the country in order to enhance financial inclusion and support economic activities.** With the increased usage of Information Technology as a service delivery channel, digital initiatives such as mobile/phone banking and internet banking are expected to enhance access to banking services. Adoption of emerging technologies will require banks to take preventive measures to strengthen information security management of all systems related aspects. Large commercial banks will be encouraged to look into avenues of regional expansion, which will lead to an increase in the geographical reach of the banking sector. Hence, close interactions will be maintained with other regional regulators with a view to enhancing information sharing among regulators and cross-border supervision.

- **The Central Bank in consultation with other stakeholders launched a roadmap for promoting sustainable finance in Sri Lanka.** This road map provides a broad direction to financial regulators and financial institutions to effectively manage environmental, social and governance (ESG) risks associated with projects they finance and help increase assistance to businesses that are greener, climate-friendly and socially inclusive. Therefore, it is expected that the banking sector will initiate developing innovative sustainable finance products and services and help create business drivers for sustainable finance. The Central Bank will facilitate such measures to enhance the green economy, where necessary.

- **The resilience of the banking sector is expected to be maintained considering the regulatory efforts to strengthen the capital and liquidity levels of banks, the expected improvements in risk management, information security and corporate governance and the stable macroeconomic fundamentals**.

- **The stability of the LFCs and SLCs sector is expected to be reinforced further in the medium-term horizon with envisaged changes to the existing regulatory framework**. Changes are proposed to the Finance Business Act No.42 of 2011 (FBA) and are to be finalized during the second half of 2020. Further, drafting of the direction on provisioning has been completed to align the classification and measurement of credit facilities in line with SLFRS 9 and to minimize forbearances compared to banks. The regulatory framework will be revisited to strengthen the supervision and regulation of LFCs and SLCs.

- **Capital levels of the sector are expected to strengthen further, with the build-up of capital as a result of the enhanced capital requirements**. The enhanced capital levels of the sector will improve the shock absorbing capacity during periods of stress. Under SLFRS 9, the recognition of expected credit loss as opposed to the incurred credit loss requires increased impairment charges which will be focused on capital augmentation plans to be submitted by LFCs. This would also encourage voluntary consolidation among LFCs in order to meet the minimum capital requirements.

- **A proper resolution framework is to be established for the sector**. Initiatives are currently being taken to resolve distressed finance companies, as per the provisions of the FBA. The process of settling the depositors of the finance companies whose licences were cancelled is being carried through the Sri Lanka Deposit Insurance and Liquidity Support Scheme (SLDILSS). Amendments are proposed to the FBA to facilitate expeditious resolution action in respect of distressed finance companies by the Resolution and Enforcement Department of the Central Bank.

- **Corporate Governance of LFCs is to be strengthened by the introduction of ownership limitations**. One of the reasons for the failure of finance companies is corporate governance issues where the ownership and decision-making is concentrated on one main shareholder or few shareholders linked to the main shareholder. The Central Bank expects to issue directions on the ownership limits for LFCs giving a reasonable time horizon for the implementation. However, concessions will be given for investors who invest in distressed companies for restructuring such companies.

- **It is expectd to revise the existing Direction on Corporate Governance to strengthen good corporate governance practices in LFCs**. Strong corporate governance processes and practices are deemed to be the management framework that facilitates the conduct of the finance business in a responsible and accountable manner so as to promote safety and soundness of the individual companies, thereby leading to the stability of the overall sector. It is expected to issue a more stringent revised direction setting out standards to promote effective operations and management of LFCs.

- **The Central Bank and the Ministry of Finance jointly developed a Medium-Term Debt Management Strategy (MTDS) for the country and published the same in the Central Bank website in April 2019.** This new strategy would facilitate to raise funds required to meet the cash flow needs of the Government in an appropriate composition, to ensure that the Government's financing needs are met at the lowest possible cost with a prudent level of risk.

- **MTDS mainly aims at maintaining foreign currency exposure at the current level, increasing the Average Time to Maturity of external debt portfolio from the current level and reducing the share of debt maturing in one year from the current level.** Additionally, MTDS also plans to reduce the debt stock to GDP ratio gradually to around 71.0 per cent by 2023. The proposed strategy is expected to reduce the Government's need of foreign financing over the medium term while switching instruments from short-term maturities to medium to long-term maturities to contain the foreign currency exposure at the level which was observed in 2018 and to reduce the share of debt maturing in one year to around 15.7 per cent by 2023 from 16.4 per cent recorded at end 2018. Further, it is envisaged to lengthen Average Time to Maturity of the debt stock, while reducing debt servicing costs in the medium term. On the monetary front, the Central Bank expects to maintain inflation at around mid-single digits over the medium term, through prudent conduct of monetary policy, supported by productivity enhancing supply side measures. A combination of these policies together with medium term fiscal consolidation programme of the government will allow the market interest rates to remain at appropriate levels, facilitating for a prudent debt management strategy in the medium term.

- **Meanwhile, a resolution was passed by the Parliament in July 2019 to raise up to Rs. 480 billion for liability management purposes under the Active Liability Management Act, No 8 of 2018 (ALMA), which was enacted by the Parliament in March 2018.** In this regard, the Central Bank is in the process of exploring alternative bond markets including the SAMURAI bond market, to diversify the international capital market issuance base and build up the required buffers in the domestic market thereby smoothening the future debt service obligations under the liability management initiatives.

- **As per the recommendation made by the committee on FinTech developments, a FinTech Regulatory Sandbox will be implemented in order to provide a safe space in a controlled environment for innovators to test their products and services, without the risk of infringing on regulatory requirements.** This process provides innovators with an opportunity to better equip themselves to seek regulatory approval. Further, the Central Bank will be assisting the transport authorities to initiate an electronic ticketing and fare collection system for the transport sector at national level. The Working Committee for Blockchain Technology, appointed as per a recommendation made by the committee to study the Blockchain Technology, recommended to facilitate a shared Know-Your-Customer (KYC) solution based on Blockchain technology. Initially, a Proof of Concept would be developed for a shared KYC solution. In addition, other proposed initiatives of the committee on FinTech developments are expected to be introduced in order to promote the efficiency and security of digital transactions and thereby reduce the usage of physical cash and enable greater financial inclusion. The Central Bank expects to facilitate the development of the financial sector and strengthen the financial system stability by introducing new payment technologies.