



Financial Sector Performance and System Stability

During the eight months ending August 2021, the financial system remained resilient amidst challenging domestic and global macroeconomic conditions. The banking sector exhibited expansion in terms of key indicators with adequate levels of capital. The LFCs sector performance remained moderate with a marginal increase of total assets and credit portfolio. Domestic money market liquidity, which remained in a persistently surplus level during the first half of 2021, declined considerably by mid July 2021 and turned to a negative position by mid-August 2021. Domestic forex market came under pressure with continuous foreign currency debt service payment requirements compared to limited inflows due to effects of the COVID-19 pandemic. The CSE recorded an impressive performance amidst significant volatilities. Despite the continuous net foreign outflow, CSE recorded a significant improvement in terms of price indices, market capitalisation and daily turnover driven by domestic investors. The financial infrastructure ensured a smooth functioning of the financial sector, in spite of the heightened uncertainties due to the pandemic.

8.2. Financial Institutions

Banking Sector

The banking sector displayed signs of expansion in terms of key indicators during the eight months ending August 2021 amidst restrained economic activities in the local and the global economy due to the COVID-19 pandemic. Despite continuous stress faced by the sector in terms of foreign currency liquidity, the banking sector continued to operate with adequate levels of capital, statutory liquid assets ratios and provision coverage ratios during the eight months ending August 2021. Further, capital ratios are expected to improve with retention of profits and raising of new capital to meet the increased minimum capital requirements. However, liquidity of banks needs to be monitored closely as a portion of the credit portfolio is under moratorium. As subdued economic activities in the global and domestic economy due to the COVID-19 pandemic hampered economic growth, the banking sector needs to be cautious of the direct and indirect impacts of the economic slowdown, together with the impact of the debt moratorium.



Banking sector performance improved, despite setbacks from macroeconomic conditions during the eight months ending August 2021...

The assets growth of the banking sector improved during the eight months ending August 2021 when compared with the corresponding period of 2020. Total assets of the banking sector expanded by 12.1% (Rs. 1.8 tn) to Rs. 16.4 tn during the eight months ending August 2021 compared to a growth of 10.5% (Rs. 1.3 tn) during the eight months ending August 2020.

Y-o-y credit growth which declined to 5.6% as at end 2019, increased to 11.9% as at end 2020 and further picked up during the eight months ending August 2021 and reached to 18.0% by end August 2021. Total loans and advances reported an increase of Rs. 1.3 tn (14.8%) during the eight months ending August 2021 and recorded Rs. 10.4 tn as at end August 2021 when compared to an increase of Rs. 725.6 bn (8.9%) during the corresponding period of 2020.

A decrease in growth of investments was observed during the period under consideration. Investments of the banking sector increased by Rs. 253.9 bn (6.0%) during the eight months ending August 2021 but were lower than the growth of investments recorded during the corresponding period of last year which amounted to Rs. 598.3 bn (19.8%).

The banking sector expansion was largely funded through deposits which contributed towards 75.8% of the total assets as at end August 2021. The deposit base of the banking sector grew by Rs. 1.3 tn (12.0%) mainly due to the growth of rupee deposits. The total borrowings of the banking sector increased by Rs. 285.8 bn (16.9%) during the eight months ending August 2021 mainly due to increased rupee borrowings.

Asset quality of the sector measured in terms of non NPL ratio showed a decline and remained manageable. NPLs increased by Rs. 46.9 bn (10.5%) to Rs. 494.9 bn as at end August 2021 from Rs. 448.1 bn as at end 2020. However, with a higher growth in credit, NPL ratio decreased to 4.7% by end August 2021 from 4.9% recorded at end December 2020. Although there is a potential for NPLs to increase upon cessation of moratoria, it is noted that banks had already absorbed a considerable portion of the potential impact of moratoria through impairment.

The banking sector operated with an adequate liquidity buffer above the minimum regulatory requirement of 20%. The Statutory Liquid Asset Ratios of DBU and OBU were at 36.1% and 32.6%, respectively.

The net long position of foreign currency exposure of the banking sector decreased to a short position of USD 84.8 mn as at end June 2021 compared to a long position of USD 33.7 mn as at end June 2020 due to the greater increase in foreign currency liabilities compared to the increase in foreign currency assets. The banking sector reported a short foreign currency position of Rupee equivalent of Rs. 17.2 bn as at end June 2021 in comparison to a long position of Rupee equivalent of Rs. 6.3 bn as at end June 2020. A net gain of Rs. 18.8 bn on foreign currency revaluation was recorded during the first half of 2021 compared to Rs. 12.8 bn during the corresponding period in 2020.

The sector recorded a low capital gain on investments. Capital gain on Treasury bonds during the eight months ending August 2021 was Rs. 4.5 bn and was lower than the gain of Rs. 7.7 bn reported during the

Table 8.1
Banking Sector - Selected Indicators

Item	End Aug 2019	End Aug 2020 (c)	End Dec 2020	End Aug 2021 (a)	y-o-y Change (%)	
					Aug 2020 (c)	Aug 2021 (a)
Total Assets (Rs. bn)	12,072	13,834	14,666	16,446	14.6	18.9
Loans & Advances (Rs. bn)	7,796	8,848	9,092	10,440	13.5	18.0
Investments (Rs. bn)	2,952	3,625	4,228	4,482	22.8	23.6
Deposits (Rs. bn)	8,836	10,344	11,141	12,473	17.1	20.6
Borrowings (Rs. bn)	1,621	1,737	1,692	1,978	7.1	13.9
Capital Funds (Rs. bn)	1,096	1,206	1,254	1,401	10.0	16.2
Tier 1 Capital Adequacy Ratio (%) (b)	13.5	13.2	13.6	13.0		
Total Capital Adequacy Ratio (%) (b)	16.7	16.5	17.1	16.3		
Gross Non-performing Loans Ratio (%)	4.9	5.4	4.9	4.7		
Net Non-performing Loans Ratio (%)	3.1	3.1	2.4	2.2		
Return on Assets (Before Tax) (%)	1.5	1.3	1.4	1.8		
Return on Equity (After Tax) (%)	10.8	10.6	11.4	15.9		
Statutory Liquid Assets Ratio (DBU) (%)	31.2	38.6	37.3	36.1		
Liquid Assets to Total Assets (%)	29.3	34.6	33.7	31.4		

(a) Provisional

(b) As at end of June

(c) Revised

Source: Central Bank of Sri Lanka

corresponding period in 2020. This was largely due to comparatively lower funds being directed to Government securities due to higher credit growth.

Profits of the sector increased during the period under consideration. Profit before tax of the banking sector was Rs. 178.7 bn for the eight months ending August 2021, which was an increase of Rs. 66.9 bn compared to the profits of Rs. 111.8 bn during the corresponding period of 2020. Increase in profit was mainly due to the increase in net interest income (Rs. 73.4 bn), non interest income (Rs. 23.5 bn) and lower loan loss provisions (Rs. 11.3 bn). ROA before tax and ROE increased to 1.8% and 15.9%, respectively, at end August 2021 from 1.3% and 10.6%, respectively, at end August 2020.

The banking sector maintained adequate capital during the first half of 2021 in order to absorb any adverse shocks. By end June 2021, the banking sector operated with a Tier 1 capital ratio of 13.0% and a total capital ratio of 16.3%, well above the Basel III requirements.

The branch network expanded further during the first half of 2021 facilitating financial inclusion in the country. Accordingly, 137 ATMs were installed and 02 branches opened, while 10 ATMs and 01 branch were closed during the first half of 2021.

Supervisory activities are ongoing through the establishment of close monitoring groups, obtaining daily 'Early Warning Indicators Statement' to assess the impact of key risks on earnings, liquidity and capital of licensed banks, and perusing other periodic reports to

capture details of stress testing computations, foreign currency borrowings, loan impairment schedules in terms of Sri Lanka Financial Reporting Standards 9, moratoria/concessions relating to COVID-19. Further, a Remote-based Examination methodology has been adopted to overcome the limitation for conducting On-site Examinations while shifting to virtual platforms for meetings/discussions with senior officials of banks and continuing paperless correspondence via safe data sharing solutions.

Licensed Finance Companies Sector

The LFCs sector performance remained moderate during the eight months ending August 2021 with a marginal increase of total assets and credit portfolio. Total asset base of the sector increased by Rs. 9.5 bn (0.7%) during the eight months ending August 2021 and stood at Rs. 1,377.4 bn at end August 2021. Loans and advances portfolio, which represents a major part of total assets, marginally increased by Rs. 29.1 bn (2.9%) during the eight months ending August 2021.

While the sector recorded an increase in deposits and capital a decline in borrowings was observed during the eight months ending August 2021. Total borrowings of the sector showed a decline of Rs. 32.5 bn (10.4%). The deposit base of the sector stood at Rs. 765.9 bn, which increased by Rs. 17.3 bn (2.3%). Overall capital position improved notably with increased capital of Rs. 22.5 bn (11.0%) due to enhanced minimum capital requirements and profits recorded by several large LFCs. Liquidity position of the sector remained satisfactory.



Performance of the LFC sector was moderate during the eight months ending August 2021 owing to adverse macroeconomic conditions...

The sector recorded a PAT of Rs. 33.0 bn during the eight months ending August 2021, compared with a PAT of Rs. 2.2 bn recorded during the corresponding period. Increased net interest income and non-interest income by Rs. 15.2 bn and Rs. 12.8 bn, respectively, and decreased provisioning by Rs. 16.6 bn, contributed to the increased profitability. While the industry recorded an overall increase in profits, 10 LFCs recorded losses during the period under consideration.

Asset quality of the sector marginally increased. Gross NPL ratio reduced to 12.5% by end August 2021 compared with the ratio of 13.9% by end December 2020, mainly due to decrease in NPLs by Rs. 11.9 bn (7.6%) and increase in loans and advances portfolio by Rs. 31.6 bn (2.8%). Net NPL ratio and provision coverage ratio stood at 3.2% and 64.5%, respectively, compared to the ratios of 4.2% and 58.9%, recorded at end December 2020. However, NPLs of the sector maybe higher since credit facilities under moratorium are not subject to classification and impairment.

The Central Bank conducted statutory examinations (on-site supervision) and continuous surveillance (off-site supervision) of the LFCs, while the regulatory function involved issuance of prudential regulations, granting regulatory approvals, and investigating into companies carrying on finance business without authority. Apart from these major functions, capacity building of the sector, facilitating court proceedings and attending to public complaints were also conducted.

Table 8.2
Key Performance Indicators of the LFCs Sector

KPIs	%	
	End Dec 2020	End Aug 2021
Gross NPL Ratio	13.9	12.5
Net NPL Ratio	4.2	3.2
Tier 1 Capital Adequacy Ratio	13.9	15.2
Total Capital Adequacy Ratio	15.1	16.7
Net Interest Margin	6.9	8.1
Return on Assets	1.6	3.2
Return on Equity	5.2	12.4
Cost to Income Ratio	90.3	80.3

Source: Central Bank of Sri Lanka

Specialised Leasing Companies

Total assets of the sector stood at Rs. 34.6 bn by end August 2021, which increased marginally by Rs. 0.9 bn (2.6%) during the eight months ending August 2021. Loans and Advances stood at Rs. 28.2 bn, which contracted by Rs. 1.4 bn (4.8%). Total capital stood at Rs. 18.2 bn by end August 2021, which increased by Rs. 3.1 bn (20.2%). The sector recorded a PAT of Rs. 0.8 bn during the eight months ending August 2021, compared with a PAT of Rs. 0.7 bn during the corresponding period of 2020. Gross and Net NPL ratios stood at 15.0% and 4.7%, respectively, and provision coverage ratio at 68.9% by end August 2021, compared with the ratios of 13.6%, 5.3% and 61.3%, by end December 2020.

Primary Dealer Companies

The PDCs sector displayed signs of contraction in terms of key indicators during the eight months ending August 2021. Total assets of PDCs industry stood at Rs. 61.6 bn, which decreased by 29.3%, and the total portfolio of government securities held by PDCs stood at Rs. 49.0 bn, which decreased by 38.8% during the eight months ending August 2021. All active PDCs maintained their core capital above the minimum requirement of Rs. 1.0 bn by end August 2021. The RWCAR of the PDCs was above the minimum RWCAR of 10% and stood at 43.0% by end August 2021. PDCs recorded a loss after tax of Rs. 95.2 mn over the eight months period, compared with a profit of Rs. 4.7 bn recorded in the corresponding period of 2020.

Licensed Microfinance Companies

The total assets of LMFCs stood at Rs. 7.5 bn by end August 2021, of which 70% comprised loans and advances. Accordingly, gross loans and advances of LMFCs were at Rs. 5.9 bn indicating a marginal increase of 4.0% during the period under consideration. The NPL ratio of LMFCs increased to 10.2% by end August 2021, compared to 8.7% by end December 2020. The sector reported a loss of Rs. 166 mn during the eight months ending August 2021.

Insurance Sector

The insurance sector recorded a mixed performance during the first half of 2021. The life insurance sub-sector registered a significant y-o-y increase in terms

of total assets and GWP while the general insurance subsector recorded a y-o-y decline in total assets and GWP at end June 2021. The total assets and the GWP of the insurance sector grew by 7.9% and 10.7% y-o-y respectively. However, profit before tax of the sector decelerated and recorded Rs. 14.5 bn during the first half of 2021 compared to Rs. 18.2 bn recorded during the corresponding period of 2020.

Unit Trusts

Performance of the unit trusts sector indicated a significant improvement at end June 2021 compared to the corresponding period of 2020. The net asset value of the industry surged by 95.7% y-o-y to Rs. 222.0 bn, and the number of unit holders increased by 16.2% to 55,651 at end June 2021. Investments of the sector recorded a significant growth of 94.8% y-o-y to Rs. 222.7 bn. The unit trusts sector invested 10.6% in government securities as a percentage of net asset value at end June 2021 compared to 7.5% at end June 2020.

Stockbroker Companies

Stockbroker companies recorded an improvement in its overall performance as at end June 2021 mainly due to the expansion of market activities in the CSE during the first half of 2021, compared to the corresponding period of 2020. The average turnover of stockbrokers increased by 250.6% to Rs. 1,553.0 mn while the profit before tax of the sector increased to Rs. 910.0 mn by 476.0% during the first half of 2021.

Superannuation Funds

The EPF is the largest superannuation fund in Sri Lanka which operated with an asset base of Rs. 3.1 tn as at end August 2021. The total number of member accounts of EPF reached 19.8 mn in December 2020.

Total member contributions during the eight months ending August 2021 increased by 2.3% to Rs. 101.8 bn whereas refund payments decreased by 2.3% to Rs. 72.1 bn. In comparison, total member contributions and refund payments were Rs. 99.5 bn and Rs. 73.8 bn, respectively, in the corresponding period of 2020. Accordingly, the net contribution during the period under review stood at Rs. 29.7 bn.

Total investment of EPF stood at Rs. 3,037.9 bn. The investment portfolio mainly consists of investments in government securities which represented 93.7% of total investments. The estimated gross investment income of the Fund during the eight months ending August 2021 is Rs. 211.2 bn, which is an increase of 22.4% compared to Rs. 172.5 bn recorded in the corresponding period of 2020.

Meanwhile, total assets of the ETF grew by 9.8%, y-o-y, and reported Rs. 398.2 bn at end June 2021. Total member contributions during the first six months of 2021 increased by 8.3% to Rs. 14.3 bn while refund payments increased by 25.3% to Rs. 10.4 bn. In comparison, total member contributions and refund payments were Rs. 13.2 bn and Rs. 8.3 bn, respectively, in the corresponding period of 2020. Investments made by the fund recorded a healthy growth of 9.9% y-o-y at end June 2021 and government securities consisted of 83.4% of the total investments.

There were 117 privately managed APFs with 72,083 employees at end June 2021. The total assets of APFs stood at Rs. 169.6 bn while APFs have made investments of Rs. 144.7 bn at end June 2021. Total assets of the PSPF increased by 12.8% y-o-y to Rs. 80.9 bn at end June 2021. Total investments made by the PSPF stood at Rs. 77.6 bn at end June 2021 and the rate of return on member balances was 8.0% during the period under consideration.

Table 8.3
Employees' Provident Fund - Selected Indicators

Item	End Aug 2020	End Aug 2021 (a)	Change (%)
Total Contributions (Rs. bn) (b)	99.5	101.8	2.3
Total Refunds (Rs. bn) (b)	73.8	72.1	- 2.3
Total Assets (Rs. bn)	2,714.4	3,062.0	12.8
Total Investment Portfolio (Rs. bn)	2,711.9	3,037.9	12.0
o/w, Government Securities (%)	93.7	93.7	-
Gross Income (Rs. bn) (b)	172.5	211.2	22.4

(a) Provisional
(b) During the eight months ending August of the respective year

Source: Central Bank of Sri Lanka

Table 8.4
Employees' Trust Fund - Selected Indicators

Item	End Jun 2020	End Jun 2021 (a)	Change (%)
Total Contributions (Rs. bn) (b)	13.2	14.3	8.3
Total Refunds (Rs. bn) (b)	8.3	10.4	25.3
Total Assets (Rs. bn)	362.7	398.2	9.8
Total Investment Portfolio (Rs. bn)	343.1	377.0	9.9
o/w, Government Securities (%)	80.3	83.4	3.9
Gross Income (Rs. bn) (b)	16.9	17.1	1.4

(a) Provisional
(b) During the period

Source: Employees' Trust Fund Board

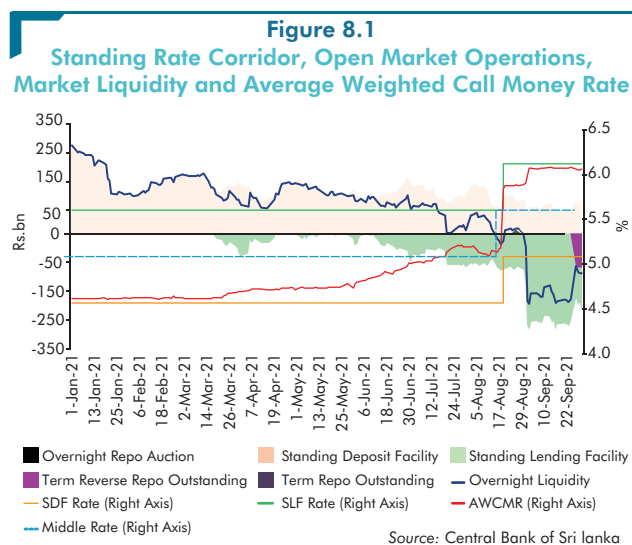
8.3 Financial Markets

Domestic Money Market

Liquidity in the domestic money market, which remained in a persistently surplus level during 2020 and in the first half of 2021, declined considerably by mid July 2021 and turned to a negative position by mid-August 2021. Liquidity surplus declined mainly due to the impact of foreign loan repayments, currency withdrawals as well as maturities of Treasury bills and foreign currency swap transactions of the Central Bank. With the increase of the SRR by 2.00 pps to 4.00% with effect from the reserve maintenance period commencing 01 September 2021, about Rs. 170 bn worth of liquidity was

Rupee liquidity in the domestic money market, which prevailed in surplus levels by the beginning of 2021, declined by mid-July and turned into a deficit by mid August 2021...

absorbed from the market. Accordingly, liquidity surplus which was at Rs. 206.7 bn by end 2020, recorded a deficit of Rs. 119.6 bn by end September 2021. As guided by the monetary policy stance, a deficit was maintained in the overnight liquidity through monetary operations. However, a one-off term reverse repo auction was conducted by the Central Bank in late September 2021 to ease liquidity stress in certain banks. Further, as liquidity position improved to some extent



due to the Central Bank transactions with the Government, the Central Bank conducted repo auctions since early October 2021 to absorb liquidity. The AWCMR the operating target of the monetary policy framework, which was maintained at the lower bound of the SRC in 2020, adjusted towards the upper bound of the SRC with declining trend in market liquidity in 2021 and the upward adjustment in policy interest rates in August 2021. The AWRR also moved in line with the AWCMR during this period. As at end September 2021, AWCMR and AWRR stood at 5.94% and 5.93%, respectively.

Domestic Foreign Exchange Market

The Sri Lanka rupee depreciated against US dollar by 6.8% during the period from January to September 2021. The LKR/USD exchange rate, which hovered around Rs. 186 levels at the beginning of the year, came under pressure during the first four months with the increased demand in the foreign exchange market mainly due to high import expenditure and continuous foreign currency debt service payment requirements compared to the limited supply caused by the effects of the COVID-19 pandemic such as the delay in the revival of tourism industry and difficulties in tapping international capital markets. However, as this sharp depreciation pressure was largely abated by the supply of foreign exchange liquidity by the Central Bank, and by policy directions and guidance provided by the Central Bank and the Government, the exchange rate hovered around Rs. 200-203 against the USD since then, except for some intermittent sharp movements, especially towards the end of August 2021. Meanwhile, during the period from January to September 2021, the Sri Lanka rupee appreciated against the Japanese yen, but depreciated against the pound sterling, the Australian dollar, euro, and the Indian rupee.

During the year up to end September 2021, the Central Bank had been a net seller in the domestic foreign exchange market. Although the Central Bank took measures to absorb foreign exchange to support gross official reserves of the country through non borrowed sources by mandating Licensed Banks to sell a certain portion of export proceeds and workers remittances converting into Sri Lankan rupees, the liquidity situation in the domestic foreign exchange market necessitated the Central Bank to supply USD

since August 2021, aiming at financing essential imports of the country. Accordingly, during the period from January to end September 2021, the Central Bank absorbed USD 331.8 mn and supplied USD 342.6 mn, resulting in a net sale of USD 10.7 mn.

Domestic forex market faced adversities primarily due to foreign currency debt service payments and the limited foreign currency inflows, urging the involvement of the Central Bank in the market...

During the nine months ending September 2021, trading volumes in the domestic FX market declined substantially. Accordingly, the daily average trading volumes in the inter bank FX market declined by 34.7% to USD 51.8 mn during the period under consideration, compared to USD 79.4 mn recorded in the same period in 2020.

Government Securities Market

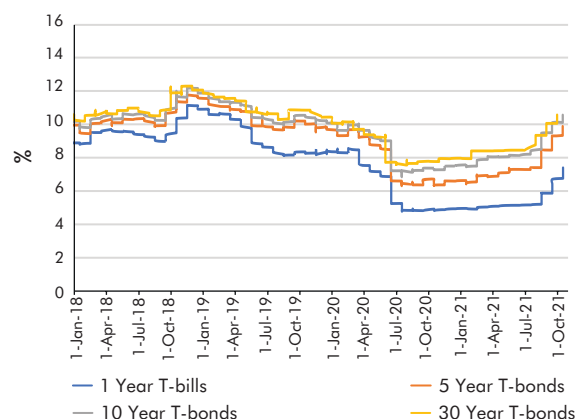
Historically low yield rates observed across Treasury bills and Treasury bonds market since mid-2020 continued into early 2021, but started adjusting upward there onwards. Due to the conducive overall market liquidity conditions, issuance arrangements in line with resource availability and supportive monetary policy stance that prevailed since mid-2020 and announcement of maximum yield rate of acceptance for primary market and the secondary market yield rates for government securities continued its low yield structure into the early part of 2021. The yield rates exhibited upward adjustment, albeit moderately, based on yield rate guidance until August 2021. The monetary policy decisions in mid-August 2021 and the decision to move away from announcement of maximum yield rate of acceptance for primary auctions of Treasury bills and bonds in an environment of substantive financing requirement of the Government allowed upward adjustment in yield rates of government securities since early September 2021. Accordingly, by end September 2021, the secondary market yield rates of 91-day,

182-day and 364-day Treasury bills increased by 185 bps, 186 bps and 174 bps, respectively, compared to the rates prevailed at end 2020. Meanwhile, the market yield rates of actively traded Treasury bonds with maturities ranging from 2 to 8 years increased in the range of 181 to 285 bps during the period of January to September 2021.

Primary and secondary market yields on government securities increased with increased borrowing requirement and tightening monetary conditions...

Meanwhile, in accommodating the substantive funding requirements of the Government in the midst of the prolonged COVID-19 pandemic while adhering to effectiveness and transparency of the primary issuance process of government securities, several arrangements were initiated and continued in line with Government policy directions in government securities market. Accordingly, measures were taken to publish the maximum yield rate for acceptance only for 364 day maturity and accommodating acceptance for 91 day and 182 day maturities within the announced yield rate for 364 day maturity at Treasury bill auctions with effect from 03 February 2021, while continuing to publish the maximum yield rate for acceptance for all Treasury bond maturities. Subsequently, the

Figure 8.2
Movements of Secondary Market Yield Curve of Government Securities



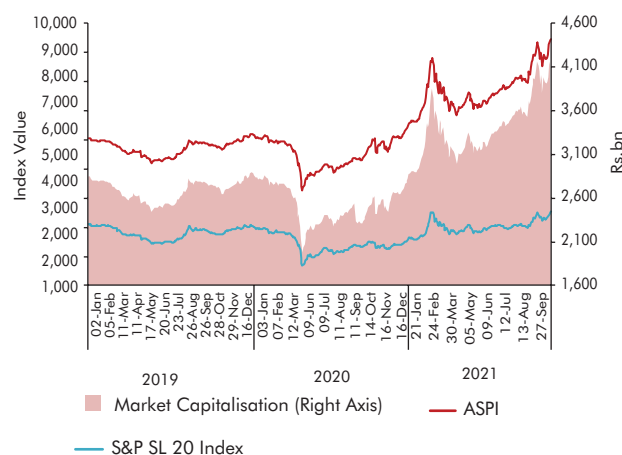
Source: Central Bank of Sri Lanka

government securities issuances were accommodated without pre-announcing the maximum yield rate for both Treasury bills and Treasury bonds auctions with effect from 22 September 2021, to ensure increased financing requirements are facilitated through effective market subscriptions. Further, With respect to Treasury bond auctions, the minimum acceptance at Phase I to execute Phase III was increased from 70% to 80% of the offered amount to further ensure the establishment of market cleared price/yield together with restricting the execution of Phase III of the Treasury bond issuances only for those with remaining maturity of 5 years or below, effective from 23 September 2021. In addition to the above developments, a new web based issuance system for Treasury bills is envisaged to be implemented by end 2021. To further facilitate the Treasury's cash flow management and to raise funds at opportune times and at favourable terms, a 'Direct Issuance Window' for Treasury bonds was introduced since August 2021, to raise up to 20% of the amount offered post auction, from any Treasury bond series with the offered amount fully accepted at Phase I.

Stock Market

The CSE recorded an impressive performance during the nine months ending September 2021 amidst significant volatilities observed. ASPI and S&P SL20 index recorded y-t-d growth of 39.6% and 34.0% respectively, at end September 2021. The market capitalisation stood at Rs. 4,215.6 bn as at end September 2021 recording a 42.4% y-t-d growth. Average daily turnover during the nine months ending September 2021 significantly increased to Rs. 4.5 bn from Rs. 1.5 bn recorded during the corresponding period of 2020. However, performance in the stock market was driven by domestic investments. Foreign contribution

Figure 8.3
Movements of Share Market Indicators



to the total turnover remained at a noticeably low level and market recorded Rs. 44.9 bn (USD 226.2 mn) outflows during the nine months ending September 2021.

During the nine months ending September 2021, significant improvements were observed related to market infrastructure of CSE. Enactment of the Securities and Exchange Commission of Sri Lanka Act, No. 19 of 2021 implementation of the second stage of digitalisation, implementation of DVP mechanism at CSE and taking initial steps to allow local companies to raise dollar denominated debt and equity at CSE were some of the major developments occurred during the period.

Corporate Debt Securities Market

The corporate bond market recorded a significant growth during the nine months ending September 2021. Thirteen institutions issued debentures during

Table 8.5
Equity Market - Selected Indicators

Item	End 2019	2020 Sep	End 2020	2021 Sep
All Share Price Index (1985=100)	6,129.2	5,984.8	6,774.2	9,459.9
Y-t-d change (%)	1.3	- 2.4	10.5	39.6
S&P SL 20 Index (2004=1,000)	2,937.0	2,463.3	2,638.1	3,534.8
Y-t-d change (%)	- 6.3	- 16.1	- 10.2	34.0
Market Capitalisation (Rs. bn)	2,851.3	2,595.8	2,960.6	4,215.6
As a (%) of GDP (a)	19.0	17.3	19.8	28.2
Market Price Earning Ratio	10.8	10.1	11.2	11.5
Average Daily Turnover (Rs. mn)	711.2	1,481.6	1,899.0	4,455.0
Net Cumulative Foreign Purchases (Rs. bn)	- 11,735.3	- 39,856.6	- 51,091.0	- 44,862.0
Number of Companies Listed	289	285	283	287

(a) Based on GDP for 2020 (Rs. 14,973 bn)

Source: Colombo Stock Exchange

the period under consideration raising Rs. 76.3 bn compared to Rs. 16.4 bn raised by six institutions during the corresponding period of 2020. The fixed interest rates of debentures ranged from 8.00–12.00% during the period under review compared to the interest rates of 9.50–13.25% observed during the corresponding period of 2020. However, the CP market continued to be relatively less active in the first six months of 2021 similar to previous year. The interest rates on CPs declined further to a range of 6.25% to 11.5% in first half of 2021 from a range of 11.50% to 15.75% recorded in June 2020. Further, SEC together with CSE implemented a new Over the Counter platform to conduct repo transactions on debt securities during the year.

8.4 Developments in the Financial Infrastructure

Payment and Settlement Systems

During 2021, the Central Bank took several measures aiming to promote digital payments and developed national payment infrastructure in Sri Lanka including but not limited to increasing the maximum transaction limit of JustPay to Rs. 50,000, reducing the CEFTS transaction fee from Rs. 50 to

The national payment infrastructure continued to facilitate economic activities of the country through effectively catering to the payment and settlement needs of individuals and institutions while addressing the risks faced by stakeholders of the digital payment ecosystem in a prudent manner...

Rs. 30 per transaction, extending the reduced maximum Merchant Discount Rate charge of 0.5% for LANKAQR initiated transactions and several awareness campaigns to educate public on using digital payment products safely. A substantial growth was observed in LANKAQR based transactions due to continuous campaigns and promotions conducted by both the Central Bank and the FIs, which further increased the number of issuers of the LANKAQR codes and registered merchants to 17 and 255,874, respectively, during the first six months of 2021. Volumes and values of all modes of digital transactions

Table 8.6
Transactions through Payment Systems During the First Six Months

Payment System	2020		2021 (a)		Growth %	
	Volume ('000)	Value (Rs. bn)	Volume ('000)	Value (Rs. bn)	Volume	Value
Large Value Payment Systems						
RTGS System	192.0	61,505.0	202.9	93,672.4	5.7	52.3
Retail Value Payment Systems						
Main Cheque Clearing System	15,822.2	3,450.5	16,838.6	4,015.3	6.4	16.4
Sri Lanka Interbank Payment System (SLIPS)	17,905.9	1,045.9	19,952.4	1,331.6	11.4	27.3
Credit Cards	20,519.5	101.8	23,349.0	126.2	13.8	24.0
Debit Cards	31,269.9	87.1	48,411.9	137.8	54.8	58.2
Internet Banking	24,643.2	1,958.2	49,179.8	2,750.5	99.6	40.5
Phone Banking (b)	11,871.8	232.7	16,390.6	263.2	38.1	13.1
Total	122,224.5	68,381.2	174,325.2	102,297.0	42.6	49.6

(a) Provisional

(b) Mobile Banking & Tele Banking

Source: Central Bank of Sri Lanka

Table 8.7
LANKAQR Transactions During the First Six Months (a)

Description	2020		2021	
	Volume	Value ('000)	Volume	Value ('000)
LANKAQR Transactions	131	844	590,660	1,017,222
Merchant Registrations (As at end period)	28,832	-	255,874	-

(a) Provisional

Source: Central Bank of Sri Lanka

grew significantly, especially transactions conducted via Internet, Credit Cards and LANKAQR. Further, with the approval from the Central Bank, LankaClear (Pvt) Ltd, together with relevant stakeholders such as Sri Lanka Transport Board, the National Transport Commission are planning to launch the National Transit Card. The proposal to the development of Proof of Concept for the deployment and testing of the Blockchain Technology based Shared KYC facility initiated by the Central Bank was successfully completed to explore the potential of Blockchain Technology to enable innovations in many financial services.

The Central Bank is planning to promote issuing of payment cards under the National Card Scheme and monitor the progress of FIs adopting the "LANKAQR" specification. Further, the Central Bank will continue to monitor and supervise the operations of mobile phone-based e-money systems to ensure security and effectiveness of services provided by the e-money system operators, including the recently granted service improvements such as depositing funds to the accounts of FIs via e-money wallets. Further, the Central Bank has taken several measures to educate on secure usage of digital payment instruments to protect the public from financial frauds and scams.

Regulation and Supervision of Foreign Exchange

Regulations, Directions and Orders issued under the Foreign Exchange Act, No. 12 of 2017 (FEA) were revised and issued during the year to address varied concerns of the stakeholders and to improve clarity of same, whilst further facilitating foreign exchange transactions of the country.

To improve market liquidity and thereby to support stabilisation of the prevailing exchange rates, Rules were issued under the Monetary Law Act, No. 58 of 1949 requiring every exporter of goods to mandatorily repatriate export proceeds within a stipulated period of 180 days from the date of exportation and to convert a portion of such proceeds into Sri Lanka Rupees. These Rules were initially issued in early February 2021 and four other Rules were issued thereafter considering the domestic foreign exchange market conditions.

Meantime, to preserve the foreign exchange reserves of the country and to avoid abrupt outflows

from the market, an order was issued under Section 22 of the FEA imposing limitations/ suspensions on remittances in respect of outward capital transactions including repatriation of funds under migration allowance. In order to encourage inflow and retention of foreign exchange within the country, regulations were issued under FEA permitting Special Deposit Accounts to be rolled over with 6 and 12 month tenures up to a maximum of 24 months from the initial placement of such deposits.

Furthermore, considering the anticipated positive economic benefits in terms of foreign exchange remittances/ inflows boosting further investments of the country, at large, Regulations applicable for carrying out capital transactions in Sri Lanka by persons resident outside Sri Lanka were amended, permitting listing and trading of foreign currency denominated shares and debt securities issued by local companies on the CSE. Additionally, new Regulations were also issued under the FEA, facilitating companies incorporated in Sri Lanka (excluding companies engaged in finance business) to purchase International Sovereign Bonds in the secondary market by utilising their foreign borrowings.

Anti-Money Laundering and Countering the Financing of Terrorism

Amidst the global COVID-19 pandemic, the FIU continued to carry out its functions to strengthen AML/CFT regime of the country while ensuring compliance of reporting institutions with the AML/CFT requirements through effective supervision and enforcement actions. Although the ability to conduct on-site supervision was restricted during the nine months ending September 2021 due to the restrictions caused by the COVID-19 pandemic, thematic studies and off-site monitoring were conducted on FIs as well as designated non-finance businesses and professions to ensure their compliance. During the nine months ending September 2021, the FIU imposed penalties totaling Rs. 10.5 mn on nine FIs for non compliances under the provisions of the Financial Transactions Reporting Act, No. 06 of 2006 and Customer Due Diligence Rules.

With a view to strengthening institutional compliance with AML/CFT related laws, rules and regulations, the FIU continued to provide guidance to

the reporting institutions and conducted programmes to enhance stakeholders' awareness on AML CFT measures and obligations. Accordingly, during the nine months ending September 2021, FIU issued 3 guidelines for FIs on "Enhancing STR Reporting Quality", "CCTV Operations for AML CFT Purposes" and "Guideline on suspension of Transactions". In addition, the FIU issued 4 circulars to reporting institutions on the trends observed in recent times.

During 2021, FIU initiated actions to update the NRA on ML/TF in line with Recommendation 1 of the Financial Action Task Force with technical assistance from the World Bank. The first NRA for Sri Lanka was conducted in 2014 and the ML/TF risk level of the country at that time has been assessed as Medium. The 2021 NRA consists of 13 modules including 4 new modules, which have not been assessed in 2014. Around 120 officials from more than 60 public and private institutions are allocated to these modules to identify and assess the ML/TF risks in each sector. This exercise is expected to be completed in the first half of 2022, and based on its results, the National AML/CFT Policy of Sri Lanka will be revisited.

Resolution and Enforcement

The Central Bank continued the compensation payments to the depositors of six licence cancelled/business suspending finance companies, under SLDILSS. In the meantime, the Monetary Board of the Central Bank decided to increase the amount of maximum compensation payable under SLDILSS was increased from Rs. 600,000 to Rs. 1,100,000. Accordingly, compensation payments at the increased maximum compensation payable amount of Rs. 1,100,000 was commenced under SLDILSS from 9 April 2021.

With a view to further streamline the operational procedures of SLDILSS and to strengthen the regulatory framework applicable to SLDILSS, new Regulations were issued under Sri Lanka Deposit Insurance and Liquidity Support Scheme Regulation, No. 02 of 2021 with effect from 06 August 2021, after repealing and replacing the preceding SLDILSS Regulations No. 1 of 2020, as amended by subsequent Regulations.

Despite the limitations arising from the COVID-19 pandemic situation, the Central Bank continuously educated the general public on the risks of investing

in prohibited schemes by using various communication channels such as participating in radio/video programmes, publishing newspaper advertisements and public notices and conducting awareness sessions through social media platforms. The Central Bank also conducted seminars on combating prohibited schemes. Investigations into prohibited schemes were conducted in collaboration with the Police and Attorney General's Department. Investigations based on the complaints received from the general public and various other parties are also in progress.

In order to strengthen the resolution of problematic financial institutions, it has also been planned to complete the development of a Resolution Framework for Licensed Banks and LFCs regulated and supervised by the Central Bank, within the existing legal framework. The Central Bank anticipates developing a depositor-wise data collection system for all MIs of SLDILSS with the purpose of increasing the quality and the accuracy of the data reporting and minimising the risk associated with data security. Accordingly, it is intended to mandate recording of unique identification number of each depositor by all MIs.

Development Finance and Access to Finance

The Central Bank continued to coordinate, facilitate, and implement various refinance, interest subsidy and credit guarantee schemes, and provided a range of credit supplementary services during the nine months ending September 2021. The Central Bank disbursed a total of Rs. 15,229 mn amongst 50,238 beneficiaries through PFIs under 7 subsidised refinance loan schemes and 2 interest subsidy and credit guarantee schemes during the nine months ending September 2021.

The Central Bank actively engaged in implementing extraordinary policy measures to provide concessions to businesses and individuals affected by the COVID-19 pandemic. Accordingly, further concessions were provided for the beneficiaries of Saubagya COVID-19 Renaissance Facility, including the borrowers in the tourism sector by extending repayment period up to 36 months from 24 months, while extending the grace period up to 30 September 2021 for the beneficiaries who request these concessions. In addition, guidelines were issued to extend the grace period/debt moratorium for

several loan schemes. A Credit Guarantee Scheme for the loans to Rice Mill owners, and Credit Guarantee and Interest Subsidy Scheme for Dairy Farming Development and Micro Small Medium Enterprises Development will be implemented. Further, the Central Bank implemented the Domestic Agriculture Development Programme – Pilot Phase through selected three value chains (dairy, vegetable, spices), which will support in designing the main Domestic Agriculture Development programme to be implemented with the support of Government through ten agriculture value chains island-wide as a national programme.

The Central Bank successfully launched the NFIS of Sri Lanka in March 2021 and several actions are being taken to operationalise the implementation of the NFIS to identify and promote financial inclusion across the country. Further, a new project has been introduced by the Central Bank to increase the quality of life of the people by introducing green initiatives and encouraging to use those initiatives to consume natural resources efficiently, minimise environmental degradation, and enhance green production while promoting “Go Green” attitude in domestic communities.

During the nine months ending September 2021, the Central Bank conducted eight Training of Trainers programmes, 18 Radio and TV programmes and more than 200 awareness programmes to promote financial literacy and financial inclusiveness, targeting those who have been excluded from the formal financial sector. Amidst the constraints associated with the COVID-19 pandemic, most of the above programmes were carried out online, utilising the newly developed online oriented educational materials.

Financial Consumer Relations

The Central Bank processed more than 8,000 complaints and inquiries relating to entities under the purview of Central Bank and answered more than 60,000 telephone calls received from the general public through its Contact Centre from August 2020. Out of the complaints received so far, most of the complaints were from COVID-19 affected businesses and individuals with respect to debt moratoria, rescheduling of loans, high interest rates, repossession of assets and early settlement of credit facilities.

Abbreviations and Acronyms

AML/CFT	: Anti-Money Laundering and Countering the Financing of Terrorism	ML/TF	: Money Laundering/Terrorist Financing
APFs	: Approved Provident Funds	mn	: Million
ASPI	: All Share Price Index	NFIS	: National Financial Inclusion Strategy
ATMs	: Automated Teller Machine	NPLs	: Non Performing Loans
AWCMR	: Average Weighted Call Money Rate	NRA	: National Risk Assessment
AWRR	: Average Weighted Repo Rate	OBU	: Offshore Banking Unit
bn	: Billion	PAT	: Profit after Tax
CEFTS	: Common Electronic Fund Transfer Switch	PDCs	: Primary Dealer Companies
CPs	: Commercial Papers	PFI	: Participating Financial Institutions
CSE	: Colombo Stock Exchange	PPS	: Percentage Points
DBU	: Domestic Banking Unit	PSPF	: Public Service Provident Fund
DVP	: Delivery Vs. Payment	RTGS	: Real Time Gross Settlement
EPF	: Employees' Provident Fund	ROA	: Return on Assets
ETF	: Employees' Trust Fund	RTGS	: Real time Growth Settlement
FEA	: Foreign Exchange Act No. 12 of 2017	RWCAR	: Risk Weighted Capital Adequacy Ratio
FIs	: Financial Institutions	SEC	: Securities and Exchange Commission
FIU	: Financial Intelligence Unit	SLCs	: Specialised Leasing Companies
GWP	: Gross Written Premium	SLDILSS	: Sri Lanka Deposit Insurance and Liquidity Support Scheme
KYC	: Know Your Customer	SLIPS	: Sri Lanka Interbank Payment System
LBs	: Licensed Banks	SRC	: Standing Rate Corridor
LCBs	: Licensed Commercial Banks	SRR	: Statutory Reserve Ratio
LFCs	: Licensed Finance Companies	tn	: Trillion
MI	: Member Institutions	y-o-y	: year on year
		y-t-d	: year to date