

12. Money and Interest Rates

The rate of monetary expansion remained moderate despite a substantial increase in domestic credit, due to the reduction in net foreign assets of the banking system. Government borrowing and tightened monetary policy caused a rise in interest rates.

Money Growth

- ▲ Monetary growth (M_{2b}) in 2000 has been stable, at around 13 per cent. Although the growth of domestic credit has expanded to all sectors, *i.e.*, government, public corporations, and private sector, the decline in the net foreign assets of the banking system dampened the growth of money.
- ▲ The moderate growth in money avoided creating additional demand pull pressure on inflation.

Money Growth and Inflation

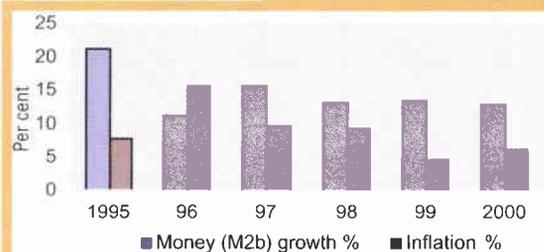


Chart 12.1

Monetary Policy

- ▲ Monetary policy focussed on stabilising the money and foreign exchange markets while providing adequate liquidity to facilitate economic activity. Monetary policy was tightened, particularly in the second half, to provide market stability by raising the Central Bank's interest rates.
- ▲ In order to promote foreign currency deposits and reduce intermediation costs of banks the statutory reserve requirement on foreign currency deposits was removed.

Changes in Central Bank Rates

Date	Repurchase Rate(%)	Reverse Repurchase Rate(%)	Bank Rate(%)
31-Dec-99	9.25	13.48	16.00
5-Jan-00	9.00		
21-Jan-00	9.00	13.30	
9-May-00	9.25		
12-May-00		13.25	
19-May-00		14.00	
8-Jun-00	9.50	15.00	
26-Jul-00	11.00		
31-Aug-00	11.75		
19-Sep-00		15.50	
26-Sep-00	12.50		
29-Sep-00	13.00	16.00	
2-Oct-00			18.00
8-Nov-00	15.00	18.00	20.00
21-Nov-00	17.00	20.00	25.00

Source: Central Bank of Sri Lanka

Table 12.1

Credit to Private Sector from Commercial Banks

- ▲ Credit expansion to the private sector from the commercial banks increased from 11 per cent in 1999 to 12 per cent in 2000. Total credit extended to the private sector by commercial banks increased by Rs. 38 billion.
- ▲ The sectors which recorded high growth in credit, were services, commercial, industry and housing and property development.

▲ Credit to government from the banking system increased significantly due to a resource shortfall resulting from delays in the privatisation process, increased defence expenditure and reduced foreign financing.

▲ Credit to public corporations from commercial banks increased in 2000 due mainly to high oil prices requiring higher recourse to bank borrowing.

Credit to Private Sector

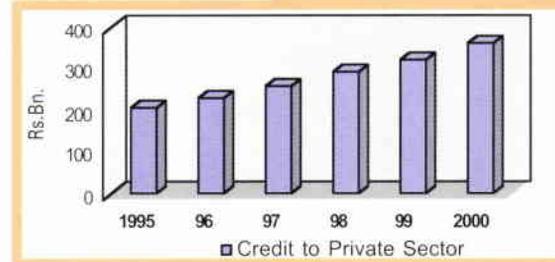


Chart 12.2

Credit from Long-Term Lending Institutions

▲ In addition to credit from commercial banks, investors were also able to obtain substantial amounts of credit from the long-term lending institutions, the National Development Bank (NDB) and the DFCC Bank.

Credit to Private Sector from NDB & DFCC Bank (Rs. million)

	1997	1998	1999	2000
NDB	22,782	30,553	35,557	35,667
DFCC	16,696	19,332	21,523	22,567
Total	39,478	49,885	57,080	58,234

Source: NDB and DFCC Bank

Table 12.2

▲ Total credit extended by the two long-term lending institutions increased by 14 per cent in 1999 and a further 2 per cent in 2000.

Interest Rates

▲ Interest rates in 2000 declined until May but rose in the second half of the year. The increase was mainly due to increased government borrowing, a reduction of liquidity resulting from a significant deficit in the balance of payments and tightening of the monetary policy by the Central Bank to contain pressure on the exchange rate.

Interest Rates

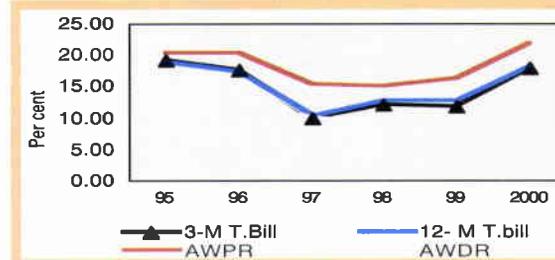


Chart 12.3

▲ It is expected that rates will decline during 2001 with improved stability in the foreign exchange market and a reduction in public sector demand for domestic financial resources.

The banking sector continued to expand. Increasing competition led banks to offer more facilities to their customers.

Deposit Mobilisation

- ▲ Deposits mobilised by commercial banks (14 per cent) and the National Savings Bank (13 per cent) further expanded. With the rise in interest rates, real interest rates increased significantly towards the latter part of the year, encouraging savings.

Foreign Currency Deposits

- ▲ There are four foreign currency deposit schemes now in operation. The Non Resident Foreign Currency Scheme (NRFC) was introduced in 1978 and subsequently, three other deposit schemes, viz, the Resident Non-National Foreign Currency Scheme (RNNFC-1980), Resident Foreign Currency Deposit scheme (RFC -1991) and Exporters Foreign Currency Deposit Scheme (EFCD-1994) were introduced.

- ▲ Total foreign currency deposits in domestic banking units as at end 2000 were US Dollars 1,074 million.

- ▲ Following the increases in interest rates in international markets in 2000, commercial banks have adjusted their interest rates upwards for foreign currency deposits during the second half of 2000 offering attractive rates to depositors.

Foreign Currency Deposit Rates (%)

Month/Year	Savings Deposits for US\$	Fixed Deposits-1yr for US\$	US Fed Fund Rate	LIBOR 6 m for US\$
1999 Dec	2.50-5.25	5.00-6.13	5.50	6.13
2000 Jan	2.50-5.25	5.00-6.00	5.50	6.00
Feb	2.50-5.50	5.00-6.18	5.75	6.29
Mar	2.50-5.50	5.00-6.15	6.00	6.33
Apr	2.50-5.50	5.00-6.40	6.50	6.53
May	2.50-5.50	5.00-6.34	6.50	7.11
Jun	2.50-5.70	5.00-6.50	6.50	7.00
Nov	2.50-5.75	6.00-6.75	6.50	6.64
Dec	2.50-5.90	6.00-6.90	6.50	6.20
2001 Jan	2.50-6.25	5.75-7.00	6.00	5.48

Table 13.1

Sources: Bank of Ceylon, People's Bank, Hatton National Bank, Hongkong & Shanghai Banking Corporation Ltd, Sampath Bank, Seylan Bank

Banking Facilities

- ▲ With the expansion of banks, the banking density, which is the number of bank branches per 10,000 people, now stands at 0.56.

- ▲ The ATM network of the commercial banks expanded as banks increased the automation of their activities and provided more facilities to customers.

- ▲ The use of credit cards, a great convenience to customers, is increasing.

- ▲ At present, several domestic commercial banks and foreign commercial banks issue credit cards that can be used both locally and internationally.

Commercial Paper

- ▲ Commercial paper has become a significant source of funds for corporate sector and gained in popularity in the recent past.

Upliftment of Rural Income

- ▲ Several policy measures have been taken in the past few years to increase the income generating activities in the rural sector.
- ▲ Promotion of people-based micro finance organisations: Samurdhi Bank Societies and Isuru Development Societies.
- ▲ Encouragement of private sector to set-up development banks and savings banks: the Sanasa Development Bank, Pramuka Savings and Development Bank and the Ceylinco Development Bank.
- ▲ Reorganisation of district based Regional Rural Development Banks at a provincial level as Regional Development Banks.
- ▲ Establishment of a 'Forward Sales Contract System' to stabilise the prices of agricultural produce.
- ▲ Further encouragement to enhance the credit facilities to the rural sector by providing interest subsidies.

Credit Facilities

▲ New Comprehensive Rural Credit Scheme

This is an islandwide scheme which provides short-term cultivation loans for paddy and other subsidiary food crops. An interest subsidy is given by the Government. A sum of Rs. 294 million was granted under this scheme as at end 2000.

▲ The Second Perennial Crops Development Project

The Second Perennial Crops Development Project operates with assistance from the ADB and is designed to support the development and commercialisation of the perennial crop sector by providing credit facilities and support services.

▲ Surathura Scheme

The Self-employment Promotion through Micro-Enterprise Credit (Surathura Scheme) operates with the participation of three lending institutions to increase income and improve living standards of unemployed youth by promoting self-employment. Under Phase II of this project which commenced in 1998, loans amounting to Rs. 907 million have been extended as at end 2000.

Banking Facilities

	1997	1998	1999	2000
Number of commercial bank branches per 10,000 people	0.54	0.55	0.55	0.56
ATM machines	197	270	316	355
Credit Cards (No.)	52,882	85,964	161,079	205,297

Source: Central Bank of Sri Lanka

Table 13.2

Commercial Paper

(Rs.mn)

	1997	1998	1999	2000
Total Issues	11,240	16,557	16,203	14,145
Outstanding	3,517	4,386	5,056	3,963

Source: Central Bank of Sri Lanka

Table 13.3

Employees' Provident Fund

- ▲ Total contributions received by the Employees' Provident Fund (EPF) increased significantly. Total contributions increased by 24 per cent in 2000 which includes payments of arrears as compared to 14 per cent in 1999. The number of employers who contributed to the fund increased by 2 per cent.
- ▲ Total investments of the EPF increased from Rs. 186 billion as at end 1999 to Rs. 215 billion at end 2000.
- ▲ Total refunds by the EPF during the year amounted to Rs. 11 billion, recording an increase of 37 per cent over the previous year.

The Employees' Trust Fund

- ▲ The Employees' Trust Fund (ETF) is an employer's contributory fund. The ETF can invest in private sector instruments such as equity.
- ▲ As at end 2000, total investments of ETF amounted to Rs. 29 billion. Altogether, 35,280 employers are contributing to the ETF

Share Market

- ▲ Share market activities continued to be depressed in 2000. In spite of healthy earnings in several listed companies, uncertainty due to the security situation, lack of liquidity and lack of foreign participation were mainly responsible for the continued decline in stock market activities.
- ▲ A declining trend was observed in both the share indices and market turnover.
- ▲ The share market is expected to recover in 2001 and foreign investors have been already net buyers.

Other Credit Schemes in operation

Credit Scheme	Mission
Small Farmers and the Landless Credit Project	Establish a cost effective and sustainable micro-credit delivery system to generate employment and improve savings habits
Kegalle District IRDP (Revolving Fund) Project	Uplift the standard of living of the people in the project area by promoting income generating activities
Tea Development Project	Increase tea smallholders' income on a sustainable basis and improve the natural environment in the project area.
Southern Province Rural Development Project	Improve the quality of life of the people in the Southern Province
North-Western Province Water Resources Development Project	Improve economic, social and nutritional well-being of the people living in the area.
North-Central Province: Participatory Rural Development Project	Poverty alleviation, improve food security nutrition and increase employment opportunities for low-income families
Food and Nutrition Promotion Credit Scheme	Increase food production and improve food processing techniques of the country.
Skills Development Project	Improve the quality and relevant skill training programmes to build a high quality work force
Japan U-Ko Micro-finance Project	Establish a cost-effective and sustainable micro-credit delivery system to generate employment and improve savings habits.

Source: Central Bank of Sri Lanka