CREDIT SUPPLY SURVEY

(Trends in 1st Quarter 2023 & Outlook for 2nd Quarter 2023)

STATISTICS DEPARTMENT
CENTRAL BANK OF SRI LANKA

Survey concluded on 04.05.2023

The Credit Supply Survey covers all Licensed Commercial Banks (LCBs) and Licensed Specialised Banks (LSBs), from which information on all lending categories are obtained.

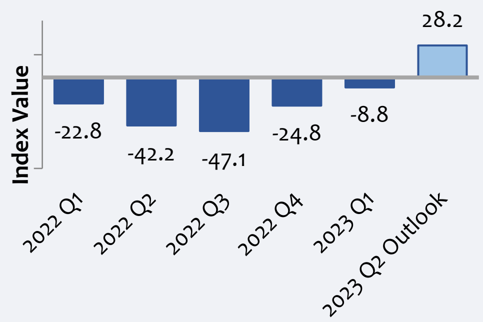
Indices are calculated as 'Diffusion Indices', that take values between -100 and 100, by weighting responses of the licensed banks using exposure of each bank to Total Gross Loan Portfolio of the banking sector.

Key to Interpretation

- ***Index value > 0 : increase***
- ***Index value < 0 : decrease***
- ***Index value = 0 : unchanged***

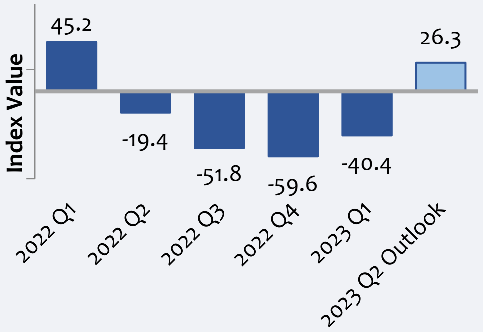
On quarter-on-quarter (Q-o-Q) basis

Willingness to Lend



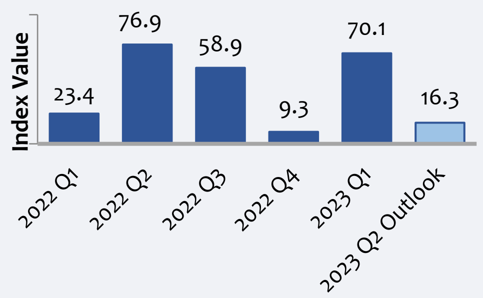
- The overall willingness to lend among banks continued to decline during 2023 Q1. However, the pace of this reduction was much slower when compared to the previous quarters.
- At the same time, the overall willingness to lend is anticipated to increase during 2023 Q2.
- This anticipated increase in 2023 Q2 as well as the slower pace of reduction in willingness to lend during 2023 Q1 is mainly attributed to the expected recovery in economic conditions.

Demand for Loans



- The overall demand for loans declined during 2023 Q1, though at a slower pace compared to the previous quarter.
- High interest rates and subdued economic conditions mainly contributed towards this decline.
- Demand is expected to gather pace during 2023 Q2 with expectations on policy rate reductions.

Non-Performing Loans (NPLs)



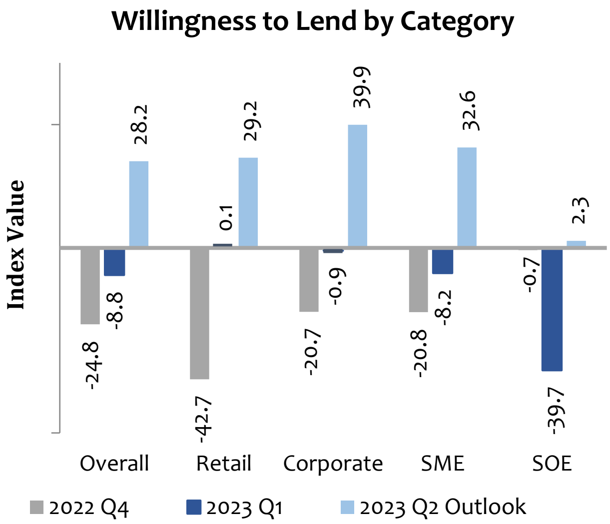
- The overall number of NPLs increased during 2023 Q1, with a significantly higher pace over the previous quarter.
- The prolonged stress in the market as well as the ending of moratoriums have contributed towards this increase.
- The level of NPL is expected to increase during 2023 Q2 as well, though at a much slower pace.

Rejected Loan Applications

- The overall number of rejected loan applications increased during 2023 Q1, yet at a slower pace compared to the past few quarters.
- Lower credit appetite by banks given the volatile economic conditions that prevailed during the quarter mainly led this continued increase of loan application rejections.
- During 2023 Q2, rejected loan applications are expected to decrease given the expected revival of certain sectors with the favorable economic outlook.

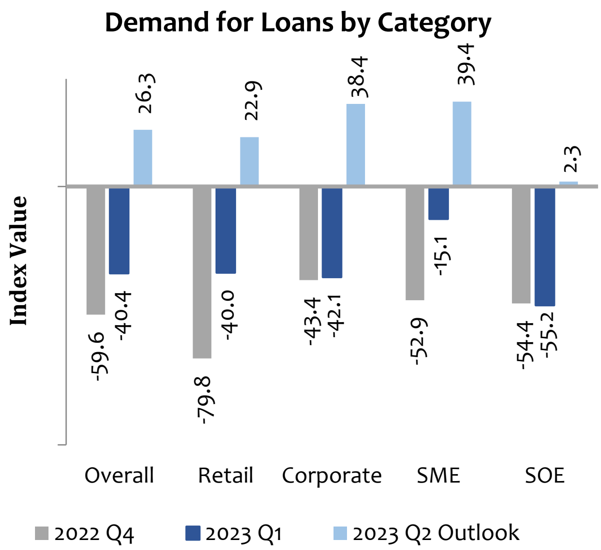
DETAILED REPORT

Willingness to Lend



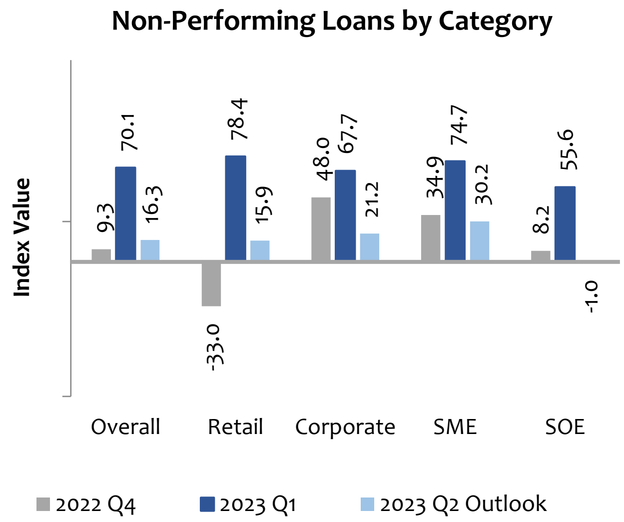
- The overall willingness to lend among banks continued to decline during 2023 Q1, mainly driven by the decline in willingness to lend to SOE and SME sectors. Meanwhile, the willingness among banks to lend to retail and corporate sectors remained broadly unchanged during 2023 Q1.
- The overall willingness continued to decline during 2023 Q1 mainly due to factors such as restrained repayment capacity of customers due to decline in disposable income because of higher inflation, higher taxes and high interest rates.
- The willingness to lend is anticipated to increase during 2023 Q2 to all sectors; retail, corporate, SME and SOE, the highest being corporate sector and lowest being SOE.
- The expected increase in willingness to lend is mainly driven by improvements in the general economic conditions in the country. The improved ability to access market financing, improved liquidity positions, and overall positive market sentiments have also contributed towards this increase.

Demand for Loans



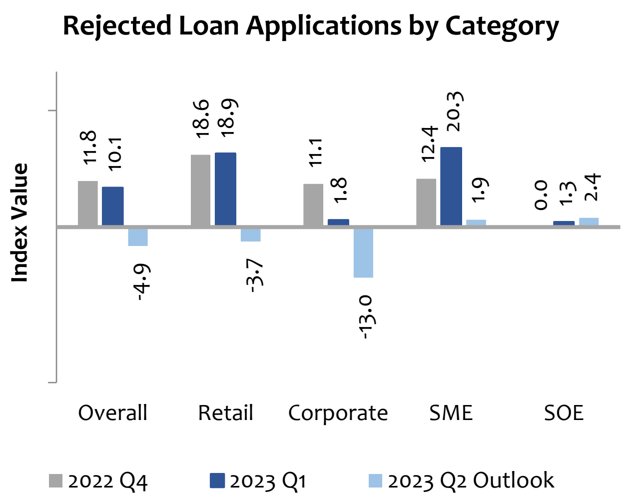
- The overall demand for loans continued to decrease during 2023 Q1, contributed by declines in all sectors, where the decrease was comparatively lower in the SME sector.
- The overall decrease can be attributed to the high interest cost and subdued activity levels that prevailed during the quarter.
- When considering the outlook for 2023 Q2, demand from all sectors is expected to increase where the highest increase is expected from the SME and corporate sectors.
- Factors such as revival of business activity with improvements in general economic activity driven by easing of inflation and higher credit appetite of borrowers due to expectations on lower interest rates are expected to fuel demand for loans. Further, new investments, diversifications, and expansions of businesses that are expected from the corporate sector will have a positive impact on demand for loans in the period ahead.

Non-Performing Loans



- NPLs of the banking industry continued to increase during 2023 Q1 at a higher pace compared to 2022 Q4, driven by all four sectors.
- Inability to repay loans as a result of ending of moratoriums and also due to additional burdens of new taxes have led to increased NPL across all sectors.
- NPLs are expected to increase at a much slower rate during 2023 Q2 when compared to 2023 Q1.
- Stabilization of the economy as well as the introduction of new repayment plans for customers with restructurings and rescheduling of loans will ease some pressure off leading to a slower increase of NPLs during 2023 Q2.

Rejected Loan Applications



- In line with the trend observed in the willingness to lend, the overall number of rejected loan applications increased during 2023 Q1, at a slower pace compared to the previous quarters.
- This increase was observed across all four sectors, where the highest increase was from the SME sector.
- Industry specific risks, increased overdue position of customers and poor repayment capacity contributed towards this increase.
- Moreover, forex and rupee liquidity constraints faced by banks impacted their credit appetite leading to more strict credit approval processes.
- At the same time, the overall number of rejected loan applications are expected to decrease in 2023 Q2 led by retail and corporate sectors.
- Easing of forex and rupee liquidity constraints faced by banks, as well as the favorable economic outlook led by anticipated revival of certain sectors would encourage banks to enhance lending avenues during 2023 Q2.