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Press Release

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Monetary Policy Review: No. 4 – 2018

The Central Bank of Sri Lanka maintains policy interest rates at current levels

The Monetary Board of the Central Bank of Sri Lanka, at its meeting held on 05 July 2018, decided to maintain policy interest rates at their current levels. Accordingly, the Standing Deposit Facility Rate (SDFR) and Standing Lending Facility Rate (SLFR) remain at 7.25 per cent and 8.50 per cent, respectively. The Board's decision is consistent with stabilising inflation at mid-single digit levels in the medium term, thereby contributing to a favourable growth outlook for the Sri Lankan economy.

Inflation to stabilise at mid-single digit levels despite temporary supply side pressures

Headline inflation, as measured by the Colombo Consumer Price Index (CCPI) and the National Consumer Price Index (NCPI), remained at low single digit levels, in spite of the transient acceleration mainly arising from the upward revisions to prices of domestic petroleum products and other administratively determined prices. Core inflation also remained subdued, and inflation expectations remain favourable. Although pressures on domestic food supplies during the off-season could exert some upward pressure on prices in the short term, inflation is expected to remain at the desired mid-single digit levels during the remainder of the year and over the medium term, underpinned by firmly anchored inflation expectations and appropriate policy adjustments.

Economic growth remained subdued in the first quarter of 2018

According to the provisional estimates released by the Department of Census and Statistics (DCS), the Sri Lankan economy grew by 3.2 per cent, year-on-year, in the first quarter of 2018, compared to the revised annual growth rate of 3.3 per cent in 2017. Economic growth during the first quarter of 2018 was mainly driven by the Services and Agriculture related activities while the Industry related activities recorded a moderate growth. It is envisaged that the government's continued commitment to the implementation of structural reforms will help the economy to attain its potential over the medium term, amidst fiscal consolidation. The sustained recovery in the global economy is likely to support domestic economic growth, while the prevalence of a low inflation environment and an appropriately valued flexible exchange rate are also expected to facilitate higher growth.

Interest rates remain high both in nominal and real terms, while growth in money supply decelerated

Short term interest rates increased recently responding to the prevailing deficit liquidity conditions in the domestic money market. Yields of short term government securities displayed mixed movements in the recent past, while other market interest rates appear to have stabilised at elevated levels. While appropriate open market operations will address short term liquidity concerns, it is expected that nominal and real interest rates would gradually adjust downwards in line with the neutral policy stance of the Central Bank and the prevailing low inflation environment.

Meanwhile, the year-on-year growth of broad money supply (M_{2b}) decelerated in May 2018. The growth of credit extended to the private sector by commercial banks too decelerated in the months of April and May 2018, following the festive season-led credit expansion observed in March 2018.

External sector performance buoyed by strong foreign exchange reserve position

The moderation of earnings from exports alongside the increase in import expenditure resulted in an expansion of the trade deficit over the first four months of 2018. The recent growth in imports was largely driven by the importation of personal vehicles and gold, and the latter is expected to have been addressed by the imposition of the customs duty on gold imports. Earnings from tourism and workers' remittances continued their positive growth momentum so far during the year. Tightening global financial conditions prompted some outflows from the rupee denominated government securities market and the secondary market of the Colombo Stock Exchange (CSE), although primary market inflows resulted in a net overall inflow to the CSE so far during the year. Amidst these

developments, the Central Bank recorded a net foreign exchange absorption of US dollars 141 million from the domestic market in the first half of 2018. With the successful issuance of the International Sovereign Bond (ISB) in April 2018, the receipt of the fifth tranche of the Extended Fund Facility with the International Monetary Fund (IMF-EFF), receipts from the divestiture of the Hambantota port and foreign exchange purchases of the Central Bank from the domestic market in early 2018, the gross official reserve position is estimated to have improved to around US dollars 9.2 billion by end June 2018, compared to US dollars 8.0 billion at end 2017. So far during the year, the Sri Lankan rupee has depreciated against the US dollar by 3.6 per cent. Much of this depreciation was recorded since late April, reflecting the broad based strengthening of the US dollar in the international market. The Central Bank intervened in the domestic foreign exchange market to address speculative behaviour in the foreign exchange market and the unwarranted volatility in the exchange rate.

Unchanged monetary policy stance to sustain inflation at mid-single digit levels

Based on the recent developments and outlook for key macroeconomic variables, the Monetary Board of the Central Bank was of the view that the continuation of the current monetary policy stance is appropriate. The Central Bank will remain vigilant on global market developments and possible spillover effects, while continuing to closely monitor domestic real economic activity.

Accordingly, the Monetary Board decided to maintain the Standing Deposit Facility Rate (SDFR) and the Standing Lending Facility Rate (SLFR) of the Central Bank at their current levels.

Monetary Policy Decision: Policy rates unchanged

Standing Deposit Facility Rate (SDFR)	7.25%
Standing Lending Facility Rate (SLFR)	8.50%
Statutory Reserve Ratio (SRR)	7.50%

INFORMATION NOTE:

A press conference with Governor Dr. Indrajit Coomaraswamy will be held today (06 July 2018) at 12 noon at the John Exter International Conference Hall (JEICH) of the Central Bank of Sri Lanka.

The release of the next regular statement on monetary policy will be on 03 August 2018.

Data Annexure:

Table 01: Real GDP Growth (Provisional)

Economic Activities	Year - on - Year % Change						
	2016	2017					2018
	Annual	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Annual	First Quarter
Agriculture	-3.8	-4.4	-3.1	-3.0	7.1	-0.8	4.8
Industries	5.8	3.7	5.6	5.3	4.1	4.6	0.9
Services	4.7	4.3	2.7	2.8	3.2	3.2	4.4
GDP	4.5	3.4	3.0	3.2	3.5	3.3	3.2

Source: Department of Census and Statistics

Table 02: Inflation

Month		Dec 17	Jan 18	Feb 18	Mar 18	Apr 18	May 18	Jun 18
Headline Inflation (Year on year % change)	CCPI (2013=100)	7.1	5.8	4.5	4.2	3.8	4.0	4.4
	NCPI (2013=100)	7.3	5.4	3.2	2.8	1.6	2.1	-
Core Inflation (Year on year % change)	CCPI (2013=100)	4.3	3.5	3.5	3.4	3.5	3.2	3.4
	NCPI (2013=100)	2.7	2.1	2.0	1.9	1.9	1.7	-

Source: Department of Census and Statistics

Table 03: Monetary Sector Developments (Provisional)

Indicator	Outstanding Amount (Rs. billion)					Year - on - Year % Change				
	Jan 18	Feb 18	Mar 18	Apr 18	May 18	Jan 18	Feb 18	Mar 18	Apr 18	May 18
Reserve Money	930	938	997	1,000	973	12.3	10.7	11.8	12.9	13.2
Broad Money (M _{2b})	6,378	6,451	6,607	6,692	6,671	16.8	16.2	16.4	16.8	15.0
Net Foreign Assets (NFA)	128	116	106	119	74	138.9	131.3	128.6	135.0	123.4
Net Domestic Assets (NDA)	6,251	6,335	6,500	6,572	6,597	8.0	7.0	7.5	8.2	7.8
Net Credit to the Government (NCG)	2,221	2,246	2,278	2,322	2,324	5.1	2.4	2.9	5.3	3.8
Credit to Public Corporations (a)	528	546	557	581	608	-1.5	-1.4	-2.6	0.8	4.8
Credit to the Private Sector (a)	4,842	4,900	5,022	5,044	5,073	15.2	14.6	15.3	15.3	15.1
Broad Money (M ₄)	7,900	7,979	8,112	8,218	8,207	17.7	17.1	16.7	16.8	15.1

(a) Revised

Source: Central Bank of Sri Lanka

Table 04: Interest Rates

Interest Rate (%)	End Dec 17	End Mar 18	End Apr 18	End May 18	End Jun 18	As at 5 Jul 18
Policy Rates of the Central Bank						
Standing Deposit Facility Rate	7.25	7.25	7.25	7.25	7.25	7.25
Standing Lending Facility Rate	8.75	8.75	8.50	8.50	8.50	8.50
Weighted Average Call Money Rate (AWCMR)	8.15	8.41	7.86	7.93	8.50	8.48
Treasury bill yields (Primary market)						
91-day	7.69	8.17	8.10	8.34	8.32	8.35
182-day	8.30	-	-	8.93	8.85	8.85
364-day	8.90	9.69	9.59	9.62	9.39	9.43
Lending Rates						
Average Weighted Prime Lending Rate (Weekly)	11.55	11.55	11.21	11.42	11.33	-
Average Weighted Lending Rate (AWLR)	13.88	14.04	14.13	14.06	-	-
Average Weighted New Lending Rate (AWNLR)	14.31	14.25	14.29	14.15	-	-
Deposit Rates						
Average Weighted Deposit Rate (AWDR)	9.07	9.00	8.98	8.91	8.92	-
Average Weighted Fixed Deposit Rate (AWFDR)	11.48	11.41	11.38	11.23	11.26	-
Average Weighted New Deposit Rate (AWNDR)	10.06	10.33	10.75	10.67	-	-

Source: Central Bank of Sri Lanka