

## SRI LANKA

FINANCIAL SECTOR QUARTERLY UPDATEFOURTH QUARTER 2005

## • Highlights •

**Performance of the Commercial Banking Sector<sup>1</sup>:** At the end of the 3<sup>rd</sup> quarter of 2005, out of the total assets in the commercial banking sector, the two state commercial banks (SCBs) accounted for 42% while the private domestic banks (PDBs) had increased their share up to 43%. In terms of deposits, the PDBs led with 44%, closely followed by the SCBs with 43.2%. In terms of advances, the PDBs recorded 48.5% while the SCBs followed with 38%, indicating that the PDBs have been more aggressive in the supply side. The PDBs, during the period under review, recorded an increase of 10.2% in terms of assets, 6.0% in terms of deposits and 12.7% in terms of advances. The four major private banks (HNB, Commercial Bank, Seylan and Sampath) continued to dominate the PDB category accounting for 85% of the assets, 90% of the deposits and 85% of the loans granted. The Non Performing Loans (NPLs), as a percentage of total advances in the commercial banking sector, declined from 9.6% in the 2<sup>nd</sup> quarter to 8.4% in the 3<sup>rd</sup> quarter. The decline was reflected in all categories and the level of NPLs in the state commercial banks declined from 12.0% to 10.2%. The banks continue to make high provisions for the NPLs and the Tsunami has not impacted too adversely on the banks' performance.

After the elections in November 2005, Fitch Rating International assigned BB minus Sovereign Rating for Sri Lanka. The Central Bank arranged a syndicated loan of US\$ 100.0 million through CitiGroup for the Government to ameliorate the pressure on the balance of payment due to the increasing fuel bill. The 3 year loan will carry an interest rate of LIBOR plus 95 basis points. The Government issued Rs. 22 billion worth of 3 year inflation indexed tradable bonds for the two state banks to clear the over drafts for petroleum bills. The Central Bank announced that it financed 8,278 loans amounting to Rs 3.8 billion for micro enterprises and SMEs affected by Tsunami. The government made a public announcement of reviving the Pramuka bank, a failed bank which will send negative signals to the market. The Government also has announced setting up an Agricultural bank and a state insurance company.

**Performance of the Licensed Specialized Banks (LSB) :** At the end of the 3<sup>rd</sup> quarter 2005, out of the total assets of the LSBs, the National Savings Bank (NSB) led with 69% followed by DFCC Bank (15%), Regional Development Banks (7%) and the State Mortgage & Investment Bank (SMIB) (3%). In terms of their lending operations, DFCC led with 32% followed by NSB (30%), RDB (16%) and SMIB (9%). NPLs, as a percentage of total advances of the LSBs, declined from 11.0% in the 2<sup>nd</sup> quarter to 10% in the 3<sup>rd</sup> quarter. The SMIB (a state housing bank) continues at a relatively high level of NPLs recording 34%. The DFCC has brought down their NPLs to 10% from 13% the 2<sup>nd</sup> quarter.

**Interest Rates :** During the 4<sup>th</sup> quarter of 2005, the average prime lending rate has further increased from 11.8% in September to 12.2% in December. The CBSL increased the repo rate to 8.75% and reverse repo rate to 10.25%<sup>2</sup> as a monetary policy measure to curb the inflationary tendencies in the market. The short term Treasury Bill rates have increased from 9.8 % in September to 10.4% in December. The offer rates, in the interbank money market, have followed the market trends and escalated from 10.3-10.5% - 10.9% - 11.5%. The Central Bank adjusted the policy rates in December for the fourth time this year as a further mopping up operation of excess liquidity in the system. The Central Bank has been relatively aggressive in open market operations which helped in containing monetary expansion to some extent. Broad money supply

<sup>1</sup> The changes noted in the percentages of both commercial banks and specialized banks is mainly due to the NDB bank being transferred to the commercial category.

<sup>2</sup> Active open market operations which commenced in March, 2003 continued.

has been increasing due to the rapid credit expansion for the private sector and the state sector. Despite losses incurred by the Petroleum Corporation, it is reported that the exposure to the banking sector had been contained by issuing tradable bonds.

**Exchange Rate Movements:**<sup>3</sup> The Rupee movements against all major currencies reflected a marginal appreciation except for the dollar. The rupee depreciated against the Dollar by 0.8% while appreciating against Euro by 0.7%, SDR by 0.7%, Sterling Pound by 1.3% and Japanese Yen by 3.3%. The trade deficit widened marginally but it has been offset by private remittances, official inflows for the Government and the savings from debt relief recording a further improvement with a surplus increasing to US\$ 400 million in the Balance of Payment. The gross official reserves amounted to Rs. 2.6 billion to cover 3.5 months of imports while the total reserves increased to Rs. 4.1 billion covering 5.5 months of imports.

**Inflation:** The increasing trend in inflation has been arrested during the 4<sup>th</sup> quarter. In the 4<sup>th</sup> quarter of 2005, Point-to Point Index declined from 10.5% in September to 8.0% in December while the Monthly Moving Average Index declined from 12.7% to 11.6%. The impact of the fuel prices were off set by favorable prices in vegetables and other food products. Paddy cultivation and plantation sector recorded better output while the Tsunami affected fisheries sector too has recovered substantially. The adverse impact of the Tsunami on some of the economic sub-sectors is declining gradually. Inflation has moderated due to the improved supply conditions and active monetary policy measures adopted. However, the fuel, gas and electricity prices have not been adequately adjusted which is causing heavy losses to these enterprises.

**Capital Market Movements**<sup>4</sup> : With the election of a new president backed by a more socialist coalition, the stock market has been rather volatile. After the election, even though the ceasefire officially continues, the sporadic attacks on the government forces and the civilians have escalated substantially with few retaliatory actions taken by the forces. The new president has also announced his commitment to a negotiated settlement; however the reaction from the LTTE has not been encouraging. A new budget was presented in December but was not too different from the previous budget in November.

The capital market performance has been mixed and volatile. The ASPI has dipped down from 2,434 in September to 1,922 in December and Milanka and MBSL indices recorded a significant decline of 24.0% and 17.0% respectively. The investors are still not confident of the conflict situation and the volatility in the market has been quite significant during the past two months. Monthly turnover ranged from Rs. 5.0 billion (US \$ 49.0 million) to Rs. 13.5 billion (US \$ 132.4 million) during the quarter. Foreign investor transactions recorded a net inflow of Rs. 1.1 billion (US \$. 10.8 million) during the 4<sup>th</sup> quarter of 2005. Market capitalization declined from Rs.735.0 billion to Rs. 584.0 billion. The Colombo Stock Exchange established a new debt exchange (DEX) to improve the accessibility of government securities to the public.

*Report, Graphic design and concept: Sriyani Hulugalle  
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January 15, 2006*

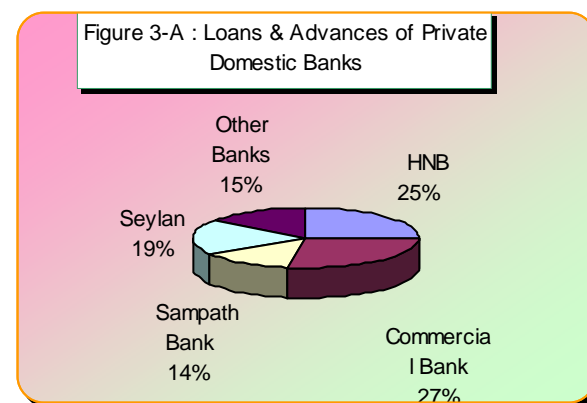
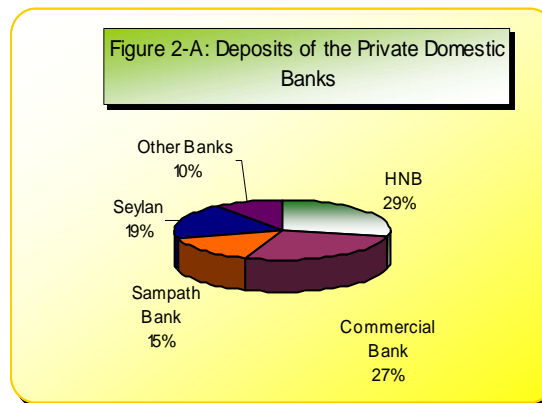
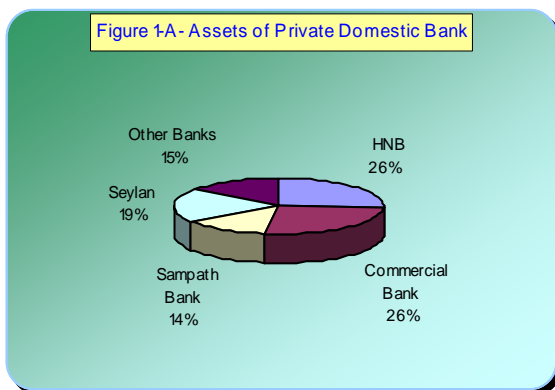
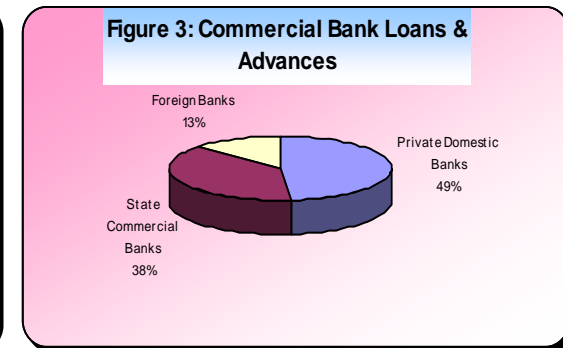
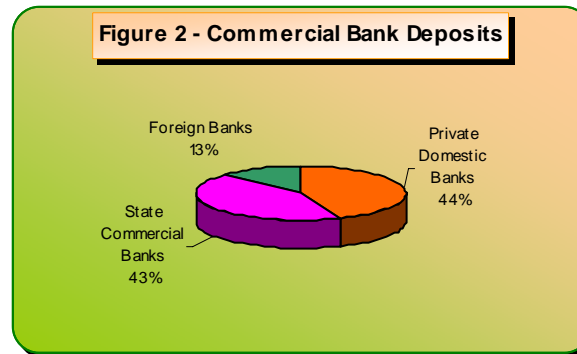
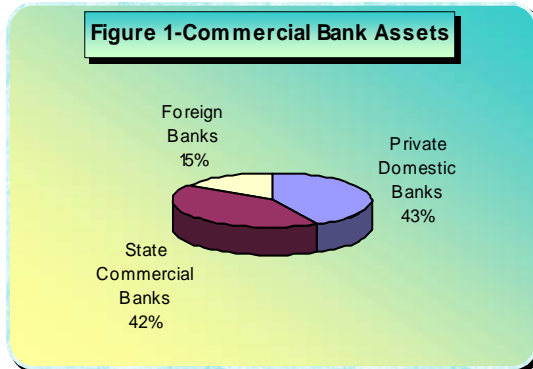
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<sup>3</sup> The Central Bank floated the Rupee in January 2003.

<sup>4</sup> The investor sentiments have been strengthened since the cease fire since 2002

**Table 1: Market Structure of the Commercial Banking System  
As at the end of 3rd Quarter 2005**

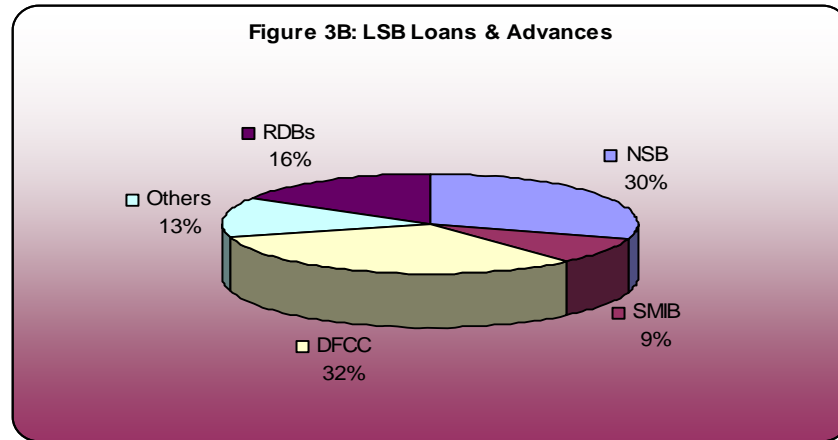
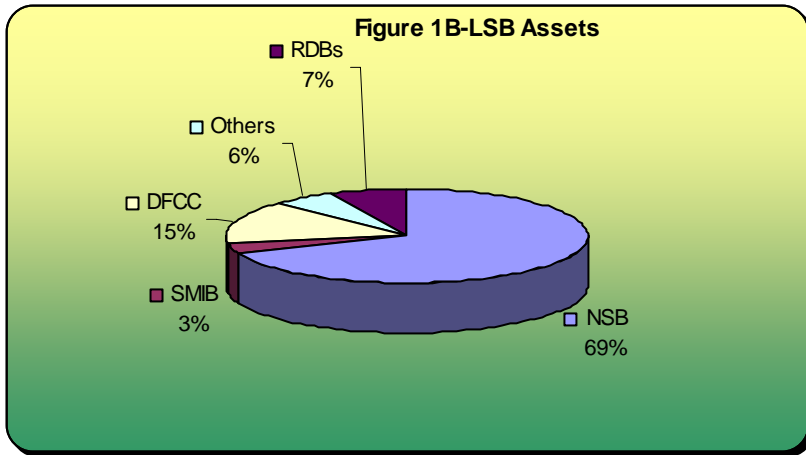
**Licensed Commercial Banks**



Note : Only in the case of Table 1, data relate to Quarter 3, 2005. Data reflect Domestic and Foreign Currency Banking Unit transactions.

Source : CBSL Bank Supervision Department and individual commercial banks.

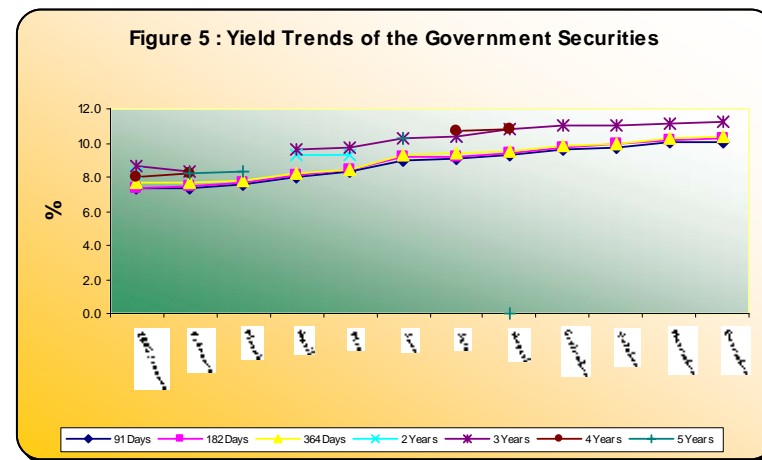
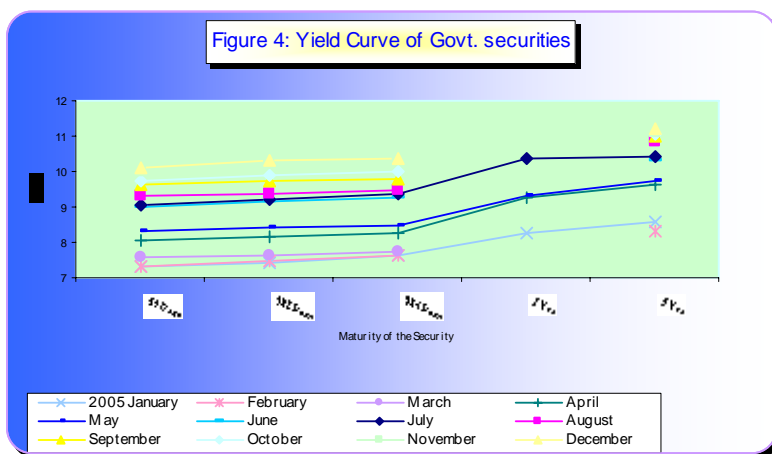
**Licensed Specialized Banks**



**Table 2: Open Market Operations (Quarter 4, 2005)**

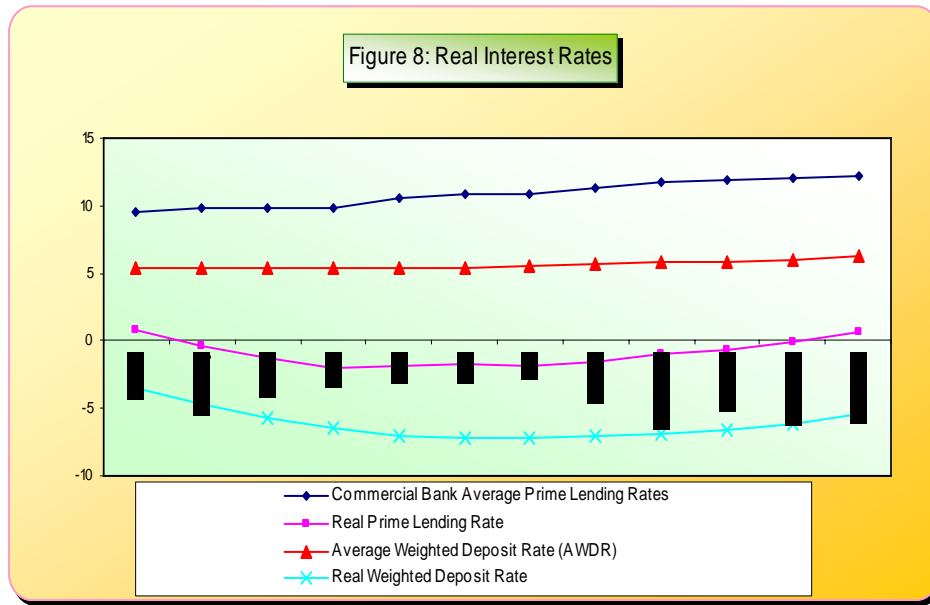
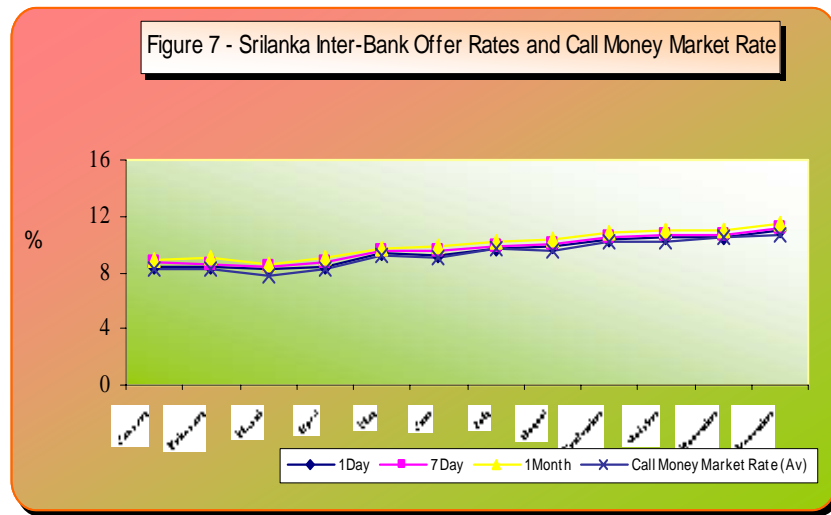
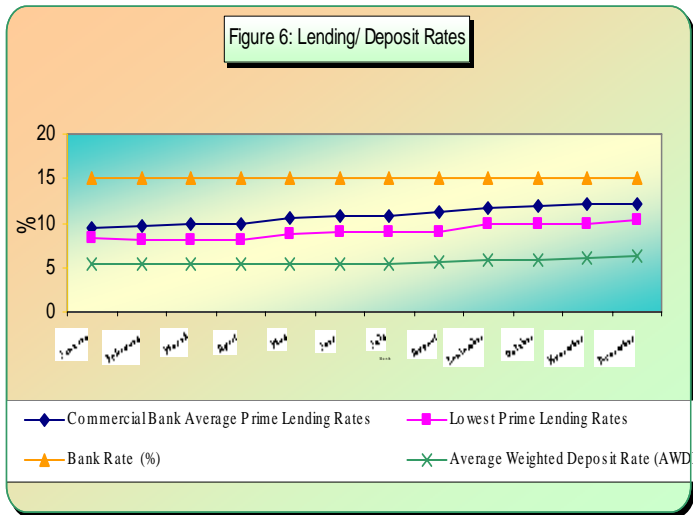
Month	Treasury Bills						Treasury Bonds										
	91 Days		182 Days		364 Days		2 Years		3 Years		4 Years		5 Years		6 Years		
	Volume	Av. Yield %	Volume	Av. Yield	Volume	Av. Yield	Volume	Av. Yield	Volume	Av. Yield	Volume	Av. Yield	Volume	Av. Yield	Volume	Av. Yield	
Rs. Mn	%	Rs. Mn	%	Rs. Mn	%	Rs. Mn	%	Rs. Mn	%	Rs. Mn	%	Rs. Mn	%	Rs. Mn	%	Rs. Mn	%
2005 January	2,464	7.34	1576	7.40	1,257	7.65	2,000	8.24	2,000	8.60	1,000	7.95					
February	1,464	7.34	2259	7.50	1,652	7.65			630	8.29	1,500	8.26	1,500	8.19			
March	5,216	7.56	1700	7.65	941	7.76							900 <sup>1</sup>	8.35	900 <sup>2</sup>	8.45	
April	3,300	8.05	455	8.15	1,093	8.25	430	9.25	400	9.62							
May	3,084	8.30	1021	8.42	1,273	8.48	750	9.30	2,800	9.73						1100 <sup>5</sup>	9.82
June	7,011	9.01	205	9.16	362	9.25			550 <sup>3</sup>	10.32			1380 <sup>4</sup>	10.31			
July	5,972	9.03	319	9.19	681	9.36	100	10.39	600 <sup>6</sup>	10.42	1,500	10.74					
August	5,994	9.34	315	9.39	2,622	9.48			1,250	10.83	850	10.85	1,000	10.65	600 <sup>7</sup>	10.87	
September	7,410	9.62	405	9.76	1,371	9.80			2,000	11.02					600 <sup>8</sup>	11.05	
October	7,902	9.74	340	9.91	1,680	9.98			560	11.04					510 <sup>11</sup>	11.08	
November	5,628	10.02	372	10.21	1,253	10.29			950	11.12			1000 <sup>9</sup>	10.69			
December	6,352	10.10	347	10.32	1,923	10.37			950	11.22					1000 <sup>10</sup>		10

Source: Economic Research Department, Central Bank of Sri Lanka

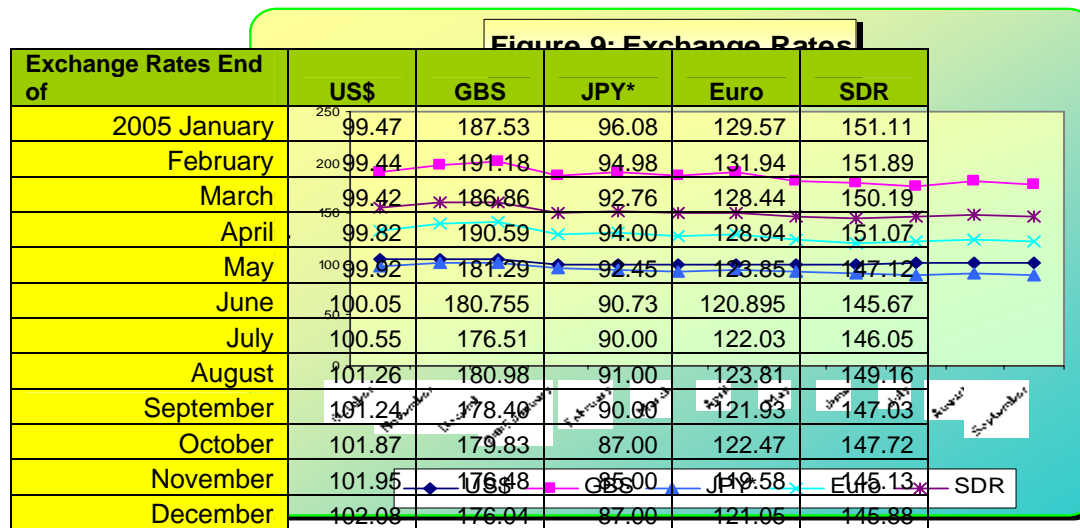


**Table 3 – Interest Rates**

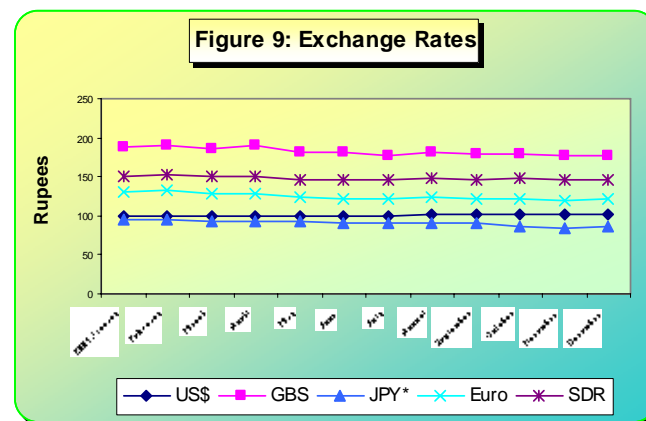
	January	February	March	April	May	June	July	August	September	October	November	December
<b>Lending Rates (%)</b>												
Commercial Bank Average Prime Lending Rates	9.53	9.76	9.88	9.89	10.52	10.88	10.83	11.30	11.76	11.85	12.03	12.24
Lowest Prime Lending Rates	8.25	8.20	8.20	8.00	8.75	9.00	9.00	9.00	10.00	9.80	10.00	10.40
<b>Sri Lanka Inter Bank Offer Rate (SLIBOR) (%)</b>												
1 Day	8.46	8.42	8.23	8.47	9.37	9.22	9.76	9.81	10.31	10.54	10.56	10.93
7 Day	8.66	8.62	8.35	8.68	9.53	9.5	9.93	9.97	10.50	10.69	10.73	11.09
1 Month	8.95	9.02	8.61	9.04	9.77	9.93	10.26	10.34	10.85	10.98	11.00	11.50
Call Money Market Rate (Av) (%)	8.30	8.25	7.77	8.2	9.25	8.97	9.63	9.49	10.14	10.21	10.43	10.73
Central Bank Repurchase Rate (%)	7.50	7.50	7.50	7.50	7.75	8.25	8.25	8.25	8.5	8.50	8.50	8.75
CB Reverse Repurchase Rate (%)	9.00	9.00	9.00	9.00	9.25	9.75	9.75	9.75	10.00	10.00	10.00	10.25
Bank Rate (%)	15.00	15.00	15.00	15.00	15.00	15.00	15.00	15.00	15.00	15.00	15.00	15.00
<b>Savings Rates (%)</b>												
Commercial Bank Savings Deposits	3.00-9.00	3.00-7.5	3.00-8.0	3.00-8.0	3.00-8.0	3.00-8.0	3.00-8.0	3.00-9.0	3.00-10.25	3.00-10.25	N/A	N/A
Commercial Bank 1 Yr. Fixed Deposits	5.50-9.75	5.50-9.75	5.00-9.75	5.65-9.75	5.50-9.75	5.50-9.75	5.50-10.00	5.50-10.50	5.50-11.00	5.50-11.00	N/A	N/A
National Savings Bank Savings Deposits	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0	5.0
National Savings Bank 1 yr. Fixed Deposits	8.00	7.5	7.5	7.5	8.0	8.0	9.0	9.0	9.0	9.0	9.0	9.0
Average Weighted Deposit Rate (AWDR)	5.35	5.43	5.42	5.43	5.43	5.45	5.5	5.73	5.84	5.86	5.96	6.24



**Table 4: Exchange Rate Movements**



Note: Rupees per 100 JPY; From January 2002, all 12 members of the Euro Currency Area replaced their national currencies with the Euro.  
 Source: Economic Research Department, Central Bank of Sri Lanka

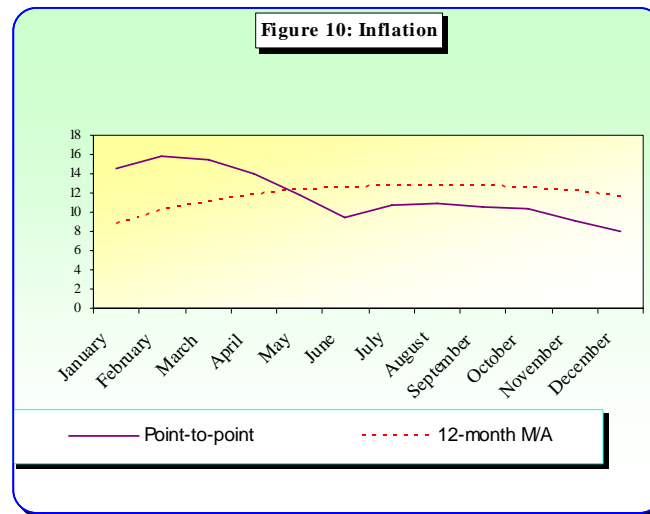




**Table 5 : Consumer Prices Indices 2004**

	January	February	March	April	May	June	July	August	September	October	November	December
<b>Colombo Consumers' Price</b> ( 1952=100)												
All items	3986.7	4004.8	3956.3	3958.5	4021.5	4019.1	4073.0	4032.1	4072.4	4082.3	4172.9	4286.6
<b>Growth Rate %</b>												
Month-to-month	0.4	0.5	-1.2	0.1	1.6	-0.1	1.3	-1.0	1.0	0.2	2.2	2.7
Point-to-point	14.6	15.9	15.5	14.0	11.8	9.4	10.8	10.9	10.5	10.4	9.1	8.0
12-month M/A	8.8	10.1	11.1	11.9	12.4	12.6	12.7	12.8	12.7	12.5	12.1	11.6
<b>Greater Colombo Consumers' Price Index</b> (1989 = 100)												
All items	375.5	374.7	370.5	372.5	373.9	377.2	374.8	372.3	374.1	375.2	383.1	-
<b>Growth Rate %</b>												
Point-to-point	15.7	15.4	14.9	13.5	11.5	11.5	9.8	9.1	6.6	6.0	4.8	-
12-month M/A	8.6	9.8	11.0	11.8	12.4	13.0	13.2	13.2	12.7	12.0	11.1	-

Source: Census and Statistics Department



**Table 6. Capital Market Information**

Market Assessment	2005-January	February	March	April	May	June	July	August	September	October	November	December
All Share Price Index	1651	1715	1752	1830	1936	1898	2047	2145	2434	2516	2292	1922
Milanka Price Index *1	2267	2330	2392	2575	2694	2681	2734	2804	3209	3321	2944	2451
MBSL Mid Cap *2	3108	3279	3251	3361	3416	3285	3420	3549	3951	4272	3901	3292
<b>Sector Indices</b>												
Banks, Finance & Insurance	2713	2844	3081	3226	3372	3269	3334	3585	4090	4406	4114	3575
Beverage, Food & Tobacco	1546	1615	1612	1672	1740	1732	1830	1913	2406	2476	2245	1890
Chemicals & Pharmaceuticals	2072	2178	2327	2366	2332	2248	2338	2383	2494	2496	2200	1763
Construction	330	367	430	410	408	369	369	356	365	382	329	272
Diversified Holdings	552	569	565	615	663	634	649	702	790	789	720	596
Footwear & Textiles	653	669	673	714	678	692	817	853	949	1079	772	626
Hotels & Travels	1460	1469	1464	1500	1537	1499	1690	1739	1860	1902	1717	1359
Investment Trusts	9053	10150	8763	8932	9211	8831	9042	10099	12416	13239	11908	8382
Land & Property	212	217	252	260	282	253	266	273	339	478	366	293
Manufacturing	904	976	1025	1076	1058	1001	1021	1033	1139	1172	1046	843
Motors	801	934	1154	1247	1282	1364	1350	1527	1932	1992	1860	1517
oil palm	15510	18800	18936	16077	21106	20379	19326	20565	19998	19934	18602	18086
Plantations	223	240	244	258	291	278	298	299	327	342	342	245
Services	5268	5268	5498	5378	6766	6602	6770	6937	9015	9359	9359	6833
Stores & Supplies	7703	6638	6985	7000	6811	7392	8358	9445	9348	12007	12007	10910
Trading	1725	1800	1835	1985	1868	1761	1874	1868	1978	2342	2342	1672
<b>Market Capitalization</b>												
Monthly Market Turnover (Rs. Mns)	6362	8052	13213	8426	10293	4711	7924	12143	13353	13565	11578	4978
Foreign Purchases (Rs. Mns)	1178	1333	1845	1307	1362	1142	3066	3747	3674	3602	3960	1498
Foreign Sales (Rs. Mns)	1556	1363	1405	1980	1157	666	1318	2488	1680	3244	3530	1180
Net Purchases (Rs. Mns)	-378	-30	441	-673	204	476	1748	1259	1994	358	430	318
Market Capitalization (Rs. Billions)	422	439	449	470	497	489	620	650	735	762	696	584

1\* - MILANKA - Covers the largest 25 companies

2\* - MBSL - Covers the next largest 25 companies

Source: Colombo Stock Exchange

Figure 11 Equity Market: Indices

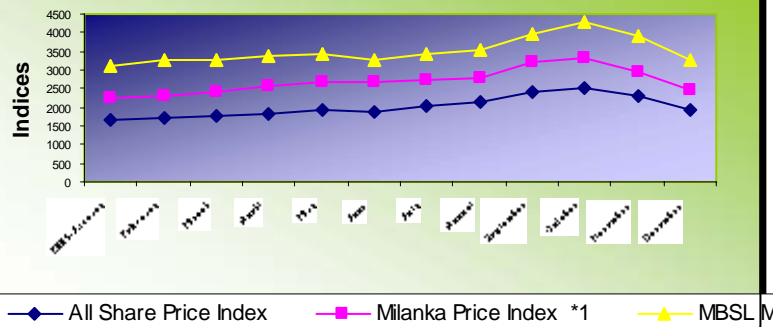


Figure 12: Equity Market - Sector Indices

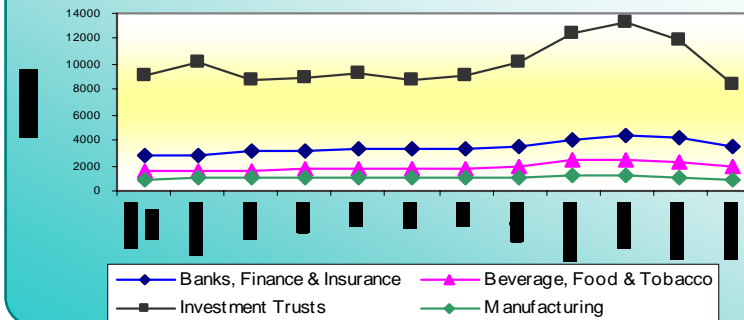


Figure 13: Market Performance

