

Monthly Economic Update (MEU)

June 2023

**Economic Intelligence Unit
The Ceylon Chamber of Commerce**



**The
Ceylon
Chamber of
Commerce**

EIU

Highlights

Sri Lankan Economy

Economy Shrinks 11.5% in Q1-2023

During the Q1-2023, Sri Lankan economy recorded a y-o-y contraction of 11.5% and this downturn was mainly driven by accelerated inflation, the rising cost of components, restrictions on imports and lower earnings from apparel exports. The agriculture sector recorded a growth, while industry and services sectors contracting significantly.

CBSL Relaxed Monetary Stance for the first time in 3 years

CBSL relaxed its Monetary Policy stance in line with the faster than expected slowing of inflation and accordingly, the SLFR and SDFR were reduced to 14% and 13% respectively. This marks the first time of monetary policy easing since last three years.

Statistics show Decline in Food Insecurity

Estimated number of people in food insecurity has declined to 3.9 million in May 2023, from 6.2 million recorded during the same period of last year. This reduction can be attributed to the improved food consumption and decrease the share of expenditure allocated for food.

External Sector Improves

Trade deficit continued to remain modest in April 2023 on a Y-o-Y basis. Remittances and earnings from tourism improved notably, and foreign holdings in government securities continued to increase. LKR appreciated against the USD by 18.3% thus far in 2023.

Global Economy

World Bank (WB) Predicts a Slowdown in Growth

WB projects a deceleration in global growth to 2.1% in 2023, down from 3.1% in 2022. While global economic activity demonstrated resilience earlier this year, it is anticipated to fade, leading to an overall slowdown in 2023. Advanced Economies and EMDEs are projected to grow by 0.7% and 4% respectively, in 2023.

Goods Barometer Improves; suggests a Turning point for Trade

The latest reading of the Goods Trade Barometer of the WTO, suggests that global goods trade remained depressed during the Q1-2023, but forward looking indicators point to a possible turnaround in the Q2.

Dashboard

Y-o-Y changes, otherwise specified

Economic Growth

-11.5% in Q1-2023

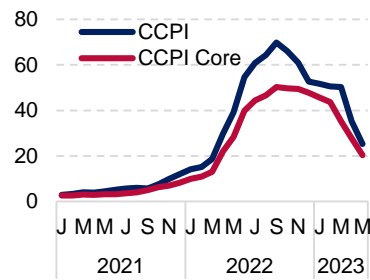
Movement of Purchasing Managers' Index-May 2023

Manufacturing PMI **46.2**
Services PMI **53.5**

Services activities expanded,
Manufacturing activities contracted.

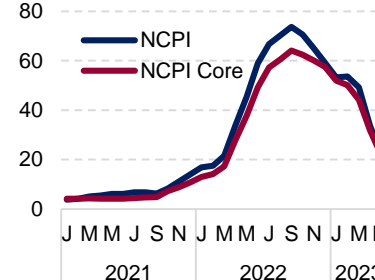
Inflation

CCPI Inflation (%) - Base 2021



May. 2023
Headline **25.2%**
Core **20.3%**

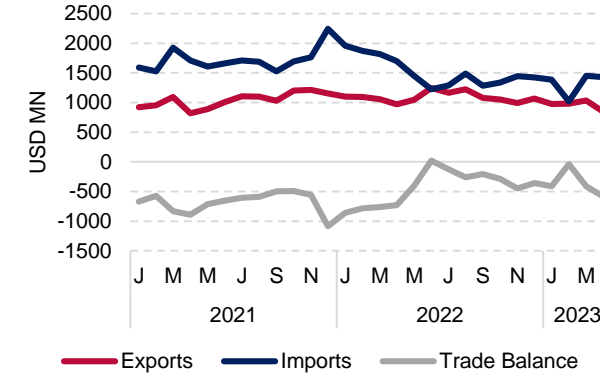
NCPI Inflation (%) - Base 2021



May. 2023
Headline **22.1%**
Core **21.6%**

External Sector

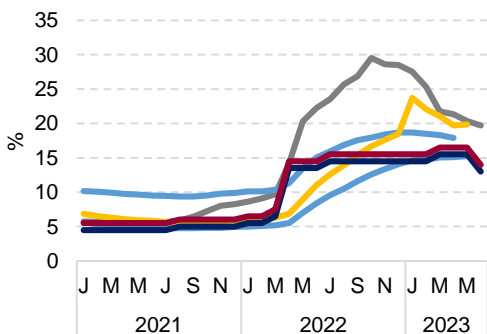
Merchandise Trade



Tourism

Apr. 2023	May. 2023
Exports 12.6% ↓	Arrivals 176% ↑
Imports 15.8% ↓	Earnings 142% ↑
Trade Deficit 20% ↓	Workers' Remittances 58% ↑

Interest Rates



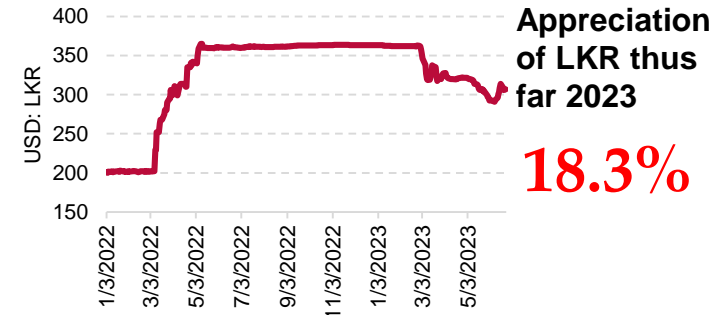
AWDR
AWPR
AWLR
AWFDR
SDFR (Repo)
SLFR (Rev.Repo)

SDFR:13.0%
SLFR:14.0%

Growth in Credit to Private Sector

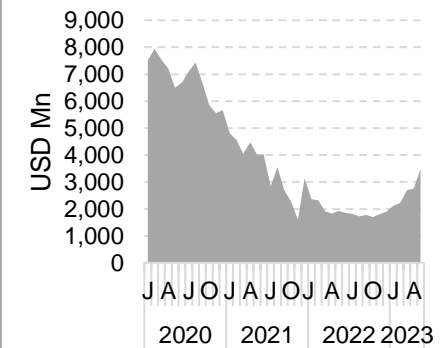
Apr. 2023
8.3% ↓

Exchange Rate



Appreciation of LKR thus far 2023
18.3%

Reserves



KEY INSIGHTS

Sri Lankan Economy

Economy Shrinks 11.5% in Q1 2023

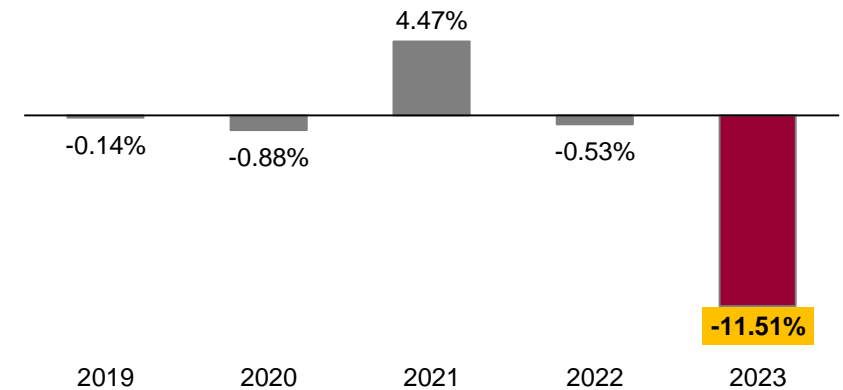
During the Q1-2023, Sri Lankan economy recorded a **y-o-y contraction of 11.5%** and this downturn was mainly **driven by accelerated inflation, the rising cost of components, restrictions on imports and lower earnings from apparel exports.**

The major economic activities - Agriculture, Industry, and Services - contributed 8%, 28.7%, and 58.2% respectively to the current price GDP, while "Taxes less subsidies on products" accounted for 5.1% of GDP in Q1 2023.

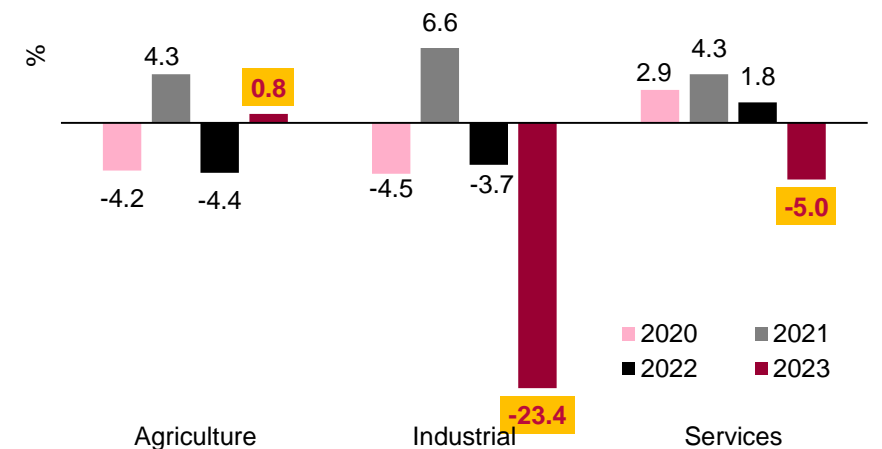
The economic background of the country did not encourage the investments during this period due to the high interest rates. Hence, most of public and private construction works were halted due to the increase of input prices in the construction sector while restrictions imposed on imports by the government have made an adverse effect on the manufacturing industry sector and services sectors. Additionally, high input prices led to a decline in manufacturing and certain agricultural activities.

The agriculture sector expanded by 0.8% compared to Q1 2022, driven by growth in rice and cereal production, as well as fresh water fishing and aquaculture. However, the forestry & logging and animal production segments lagged behind. **The industry sector declined by 23.4%** which was mainly attributed to negative growth in the areas of construction, mining and the manufacture of basic metal, fabricated metal products, machinery and furniture. **Services declined by 5%** driven by downturns of insurance and financial service activities. Further declines were seen in the programming, broadcasting and in the real estate activities.

Growth in Q1 Real GDP (Y-o-Y)



Q1 Year on Year Sectorial Growth



KEY INSIGHTS

Sri Lankan Economy

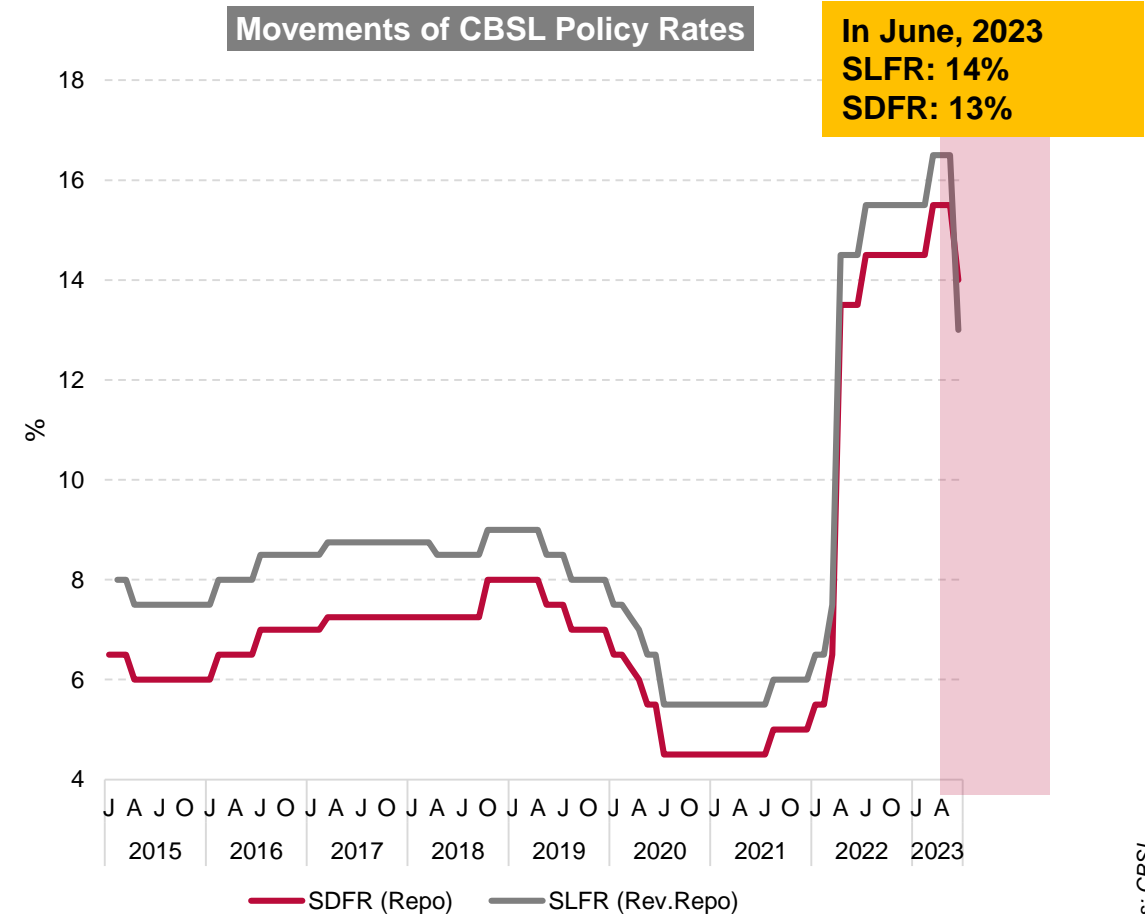
CBSL Relaxed Monetary Policy Stance in June 2023, for the first time in 3 years

The Central Bank of Sri Lanka (CBSL) relaxed its Monetary Policy stance in line with the faster than expected slowing of inflation. Accordingly, **the SLFR and SDFR were reduced by 250 basis points to 14% and 13% respectively, with effect from 1st June 2023. This marks the first time of monetary policy easing since last three years.**

As per the latest projections of the CBSL, headline inflation based on Colombo Consumer Price Index (CCPI), is forecasted to reach single digit levels in early Q3-2023, and stabilize around mid-single digit levels over the medium term.

The relaxation of the monetary policy is expected to accelerate the normalization of the interest rate structure in the period ahead and broad base the recovery of activity in the economy and ease pressure in the financial markets, thereby steering the economy towards a rebound phase, the CBSL stated in its latest Monetary Policy Review.

CBSL further stated that, faster deceleration of inflation and lower probability of excessive demand pressures during economic rebound phase create space for a gradual policy relaxation in the period ahead.



KEY INSIGHTS

Sri Lankan Economy

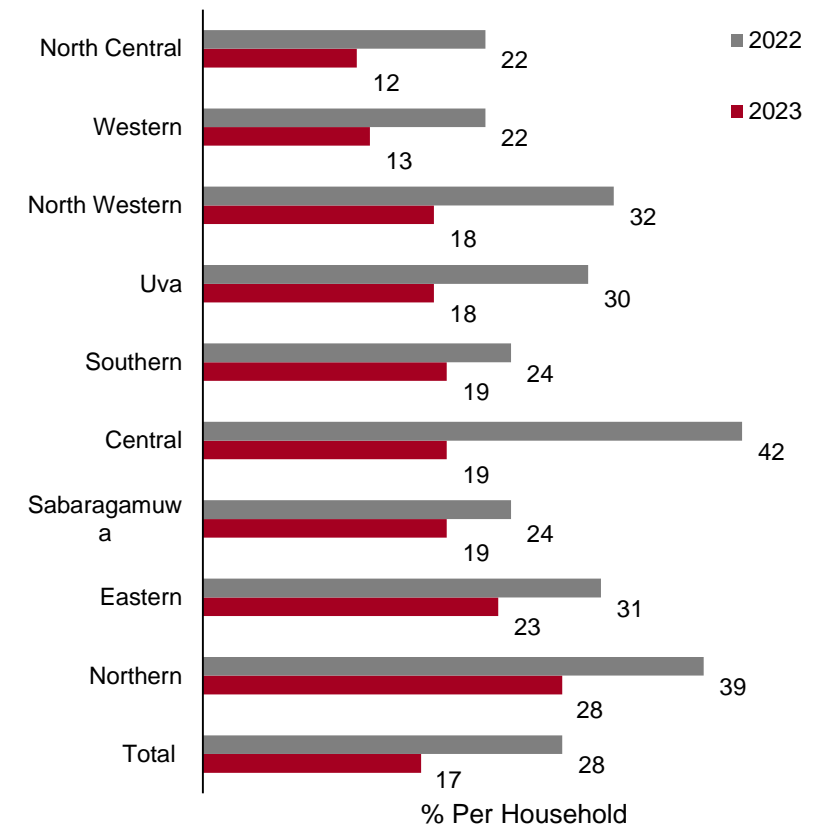
Statistics show a Decline in Food Insecurity

About 3.9 million people (17% of the population) are estimated to be moderately food insecure, and 10,000 people are classified as severely food insecure. This marks an improvement compared to May 2022 when approximately 6.2 million people were moderately food insecure, and 66,000 people were severely food insecure. The reduction in food insecurity can be attributed to improved food consumption and a decrease in the share of expenditures allocated to food. This seasonal effect, which is influenced by the harvest period, impacted market prices and farmers' income, thus contributing to the overall positive trend.

Challenges persist in specific sectors and demographics. The Estate sector, experiences the highest level of acute food insecurity (42%) compared to urban and rural sectors. Similarly, households relying on social protection schemes like Samurdhi and disability benefits face affordability issues regarding food and healthy diets. Additionally, high levels of food insecurity are found among households' dependent on unskilled wage labor, both in agriculture and non-agriculture sectors, as well as fishing communities.

Household characteristics such as gender and education play a vital role in determining food insecurity. Female-headed households have higher rates of food insecurity (23%) compared to male-headed households (16%). Based on the focus group discussions with female-headed households, this disparity was attributed to women being paid low wages compared to men and, therefore, faced problems with regular access to adequate and diverse food. Furthermore, they spent considerable amount of time caring for children, which limited their ability to work and to earn a stable income. Households headed by individuals with no education show the highest rates of food insecurity (34%). In contrast, households where the head has completed secondary school education or higher experience significantly lower rates of food insecurity (11.8%).

Acute food insecurity trend by province



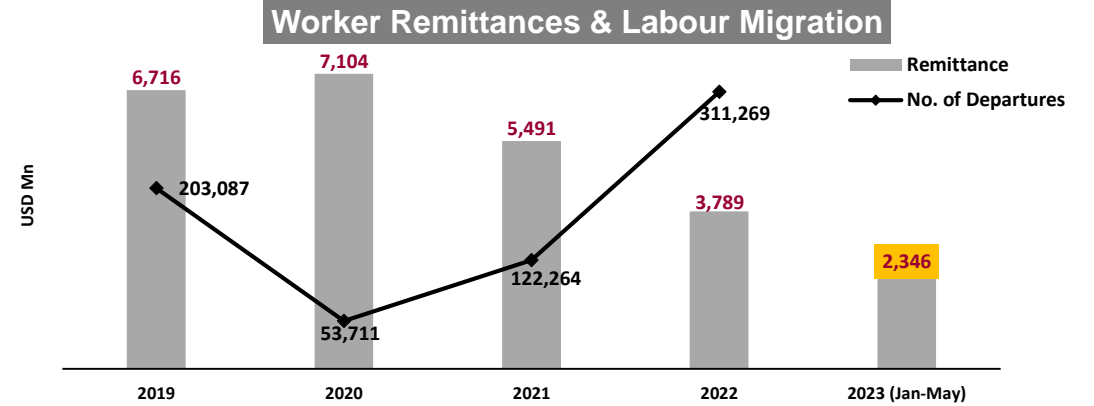
KEY INSIGHTS

Sri Lankan Economy

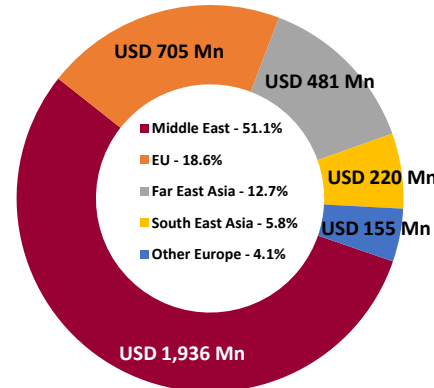
Surge in Labor Migration in 2022 Fuels Rebound in Worker Remittances in 2023

Despite showing a relative improvement in the latter half of 2022 compared to the previous year, **worker remittances reached a year-end total of USD 3,789 million, marking the lowest level since 2009**. This represents a significant drop of 31% from the remittances recorded in 2021, which totaled USD 5,491 million. The regions serving as sources of worker remittances were primarily concentrated in Middle Eastern countries, with the European Union and Far East Asian countries following suit. Nevertheless, there has been a notable increase in remittances, which continues to strengthen in 2023. This positive trend comes as a result of the authorities' successful efforts in restoring stability to the domestic foreign exchange. The cumulative workers' remittances for the first five months of 2023 surged by an impressive 75.7% year-on-year, reaching a total of USD 2,346 million.

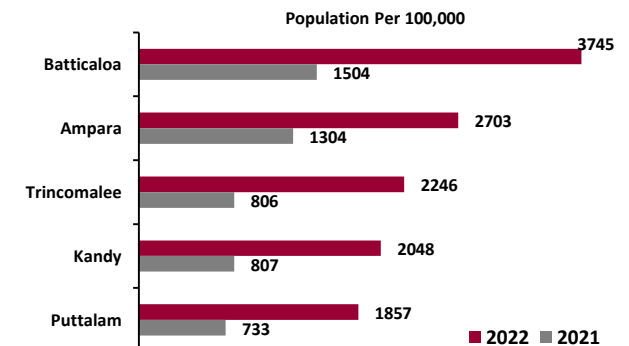
Labour migration showed a substantial increase, with the total number of departures reaching 311,269 in 2022, highest since 2014, reflecting a staggering year-on-year increase of 155%. Kuwait emerged as the prominent destination country for migrant workers in 2022, followed by Qatar, Saudi Arabia, and the United Arab Emirates. Nearly 60% of the overall participation in foreign employment is concentrated within the semi-skilled and low-skilled workforce. When examining its gender breakdown, it is evident that female participation is predominantly concentrated in semi-skilled roles, while male participation is more prevalent in skilled occupations. Additionally, a significant proportion of male migrant workers fall within the age group of 25 to 29 years, whereas most female workers are concentrated in the age group of 40 to 44 years. Notably, Batticaloa reported the highest percentage of migration in relation to the population of each district, both in 2021 and 2022.



Top 5 Regions for Remittance Inflows in 2022



Top 5 Districts - Departures For Foreign Employment



KEY INSIGHTS

Global Economy

World Bank Predicts a Slowdown in Growth

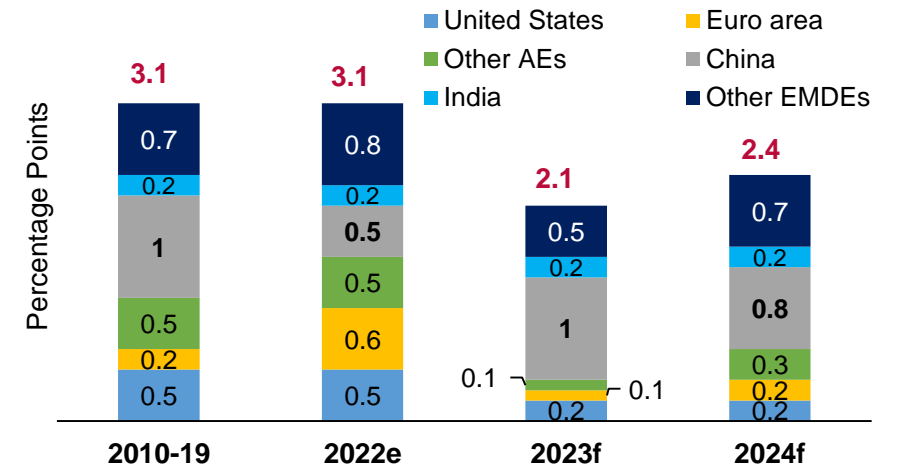
The latest Global Economic Prospects report by the World Bank (WB), published this month, projects a **deceleration in global growth to 2.1% in 2023, down from 3.1% in 2022**. While global economic activity demonstrated resilience earlier this year, it is anticipated to fade, leading to an overall slowdown in 2023.

Advanced economies (AEs) are expected to exhibit a deceleration, with China playing a prominent role in anchoring global growth. This growth slowdown can primarily be attributed to persistent global inflationary pressures, which, despite easing, remain elevated. Additionally, the lagged and ongoing effects of monetary tightening and recent banking stress are contributing factors.

In particular, the report **forecasts that AEs growth will slow to a 0.7% in 2023**. Growth in AEs is anticipated to modestly accelerate to 1.2% in 2024, driven by the euro area's recovery, which is supported by reforms and investments funded by the Recovery and Resilience Facility.

Regarding **Emerging Markets and Developing Economies (EMDEs)**, a **slight uptick in GDP growth to 4%** (up 0.6% from WB projections made in January 2023), although excluding China, growth is anticipated to decline to 2.9% in 2023. However, in 2024, growth in EMDEs, excluding China, is expected to pick up modestly to 3.4%. This recovery is attributed to the diminishing effects of monetary tightening and several larger EMDEs emerge from domestic strains, including natural disasters, power shortages, and political turbulence.

Contributions to Global Growth



Growth Projections (%)	2023		2024	
	2023	2024	2023	2024
Advanced Economies	0.7	1.2		
United States	1.1	0.8		
Euro Area	0.4	1.3		
Japan	0.8	0.7		
EMDEs	4.0	3.9		
China	5.6	4.6		
India	6.3	6.4		
Russia	-0.2	1.2		
Thailand	3.9	3.6		
Mexico	2.5	1.9		
Saudi Arabia	2.2	3.3		

KEY INSIGHTS

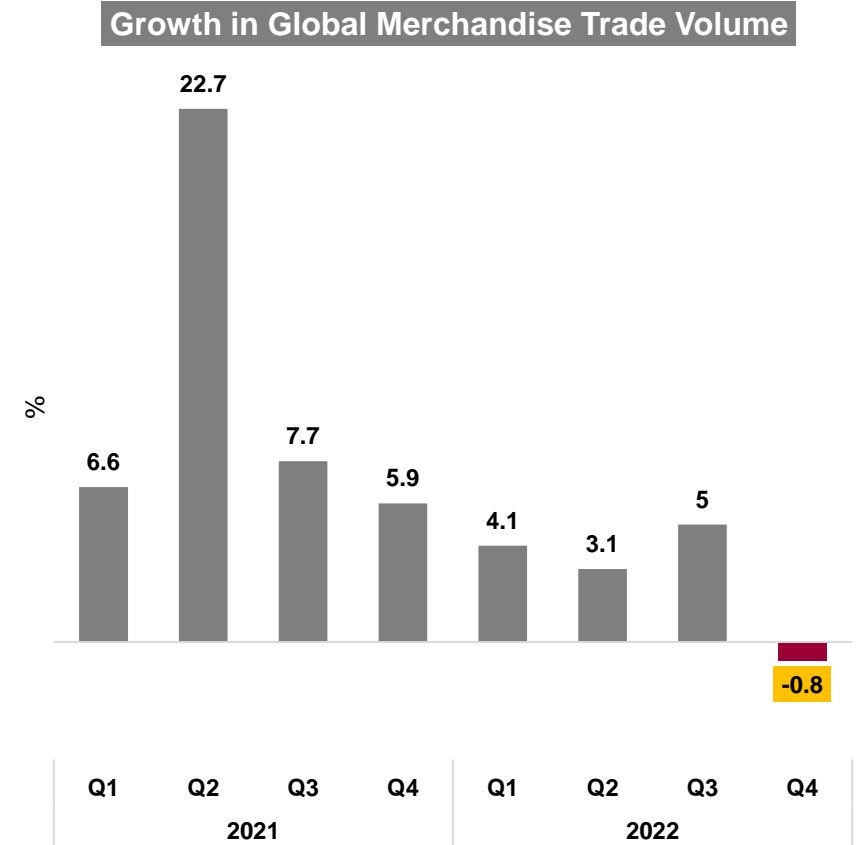
Global Economy

Goods Trade Barometer Improves: A Turning Point for Trade?

The World Trade Organization's goods trade barometer serves as an indicator for global trade, offering real-time information on the trajectory of merchandise trade in relation to recent trends. As of March 2023, the barometer reading stands at 95.6, showing an improvement from its previous value of 92.2 in December 2022. However, it remains below the baseline value of 100, indicating that **merchandise trade continued to be sluggish during the first quarter of 2023, but there are signs of potential improvement in the second quarter.**

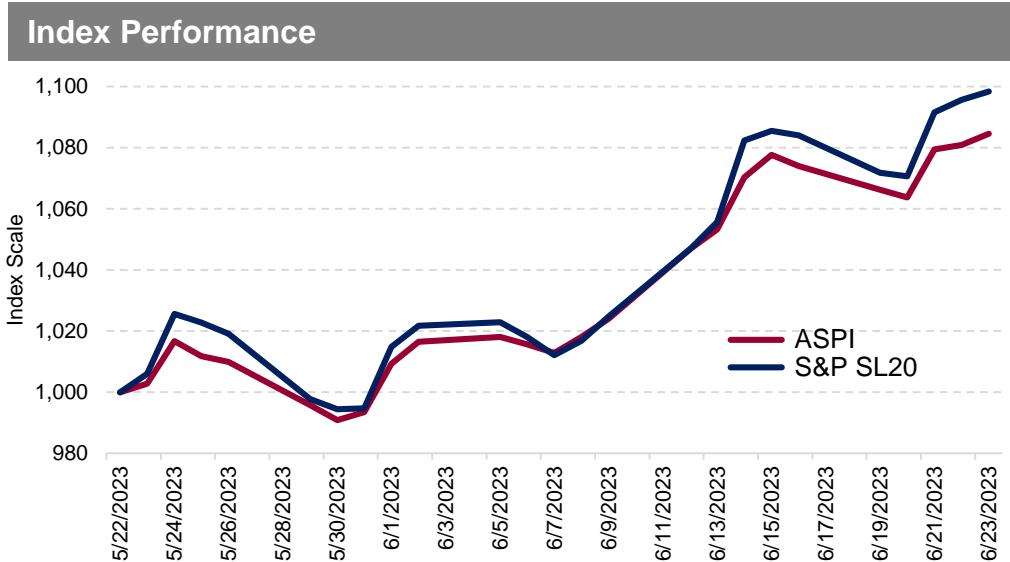
Among the barometer's component indices, the automotive products index (110.8) has surpassed the trend due to strong sales in the United States and Europe. Additionally, the export orders index (102.7), rebounded after a decline triggered by the outbreak of the war in Ukraine. Conversely, indices representing container shipping (89.4), air freight (93.5), and electronic components trade (85.2) continue to exhibit weakness. The raw materials trade index (99.0) remains on track with the overall trend. The mixed signals from these component indices suggest that the path to trade recovery may be challenging.

In Q4 of 2022, the volume of world merchandise trade witnessed a year-on-year decline of 0.8%, following a quarter-on-quarter contraction of 2.4%. Several interconnected factors contributed to this slump, including the ongoing war in Ukraine, persistent high inflation in advanced economies, and tighter monetary policies on a global scale. Although the relaxation of pandemic restrictions in China boosted port traffic in the country, this positive effect was outweighed by reduced throughput in European ports. Preliminary data indicates that trade remained depressed during the first quarter of 2023. However, the increase in export orders suggests a potential turnaround in the second quarter. These findings align with the WTO trade forecast of 1.7% growth in merchandise trade for 2023.



Equity and Debt Market Performance

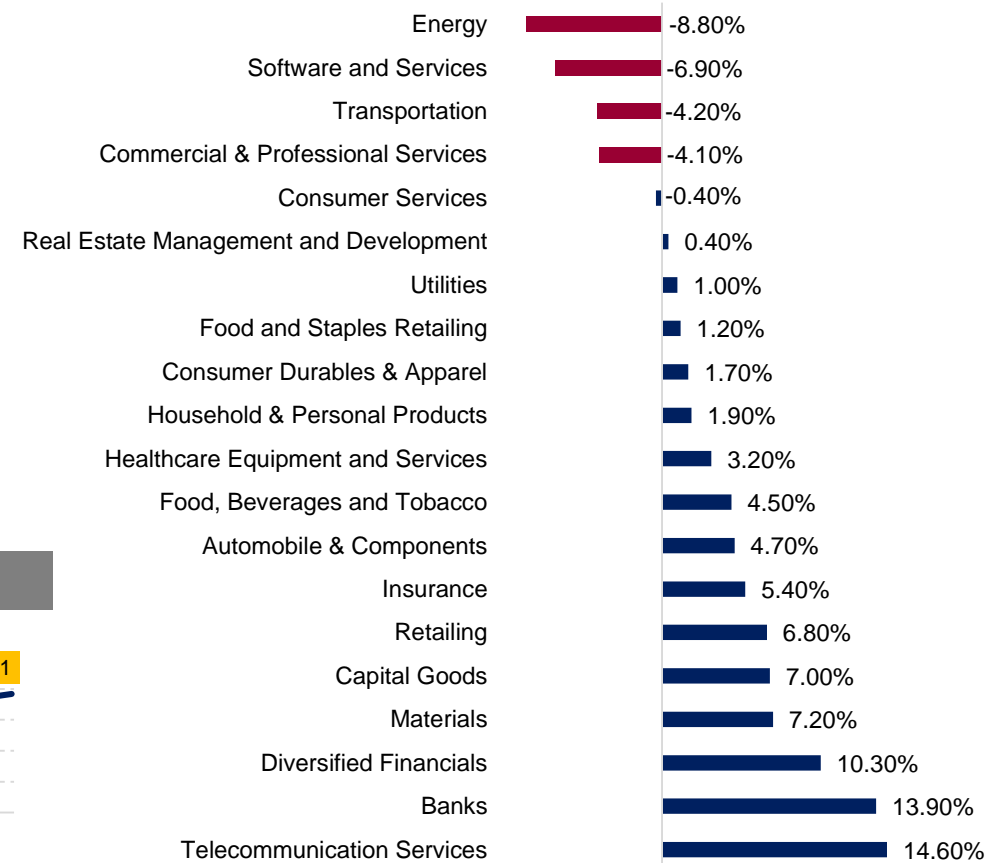
In order to provide our members with a concise update on the equity market performance of the month, the EIU is collaborating with the Colombo Stock Exchange (CSE) to introduce a new section in the MEU. This addition aims to deliver a formal and succinct overview of the equity market's performance.



All Share Price Index (ASPI) is the benchmark index of the Colombo Stock Exchange (CSE). This is based on the float adjusted market capitalization.

S&P Sri Lanka 20 Index (S&P SL20) is the blue-chip index of the CSE and it includes the largest most liquid and profitable 20 companies as index constituents.

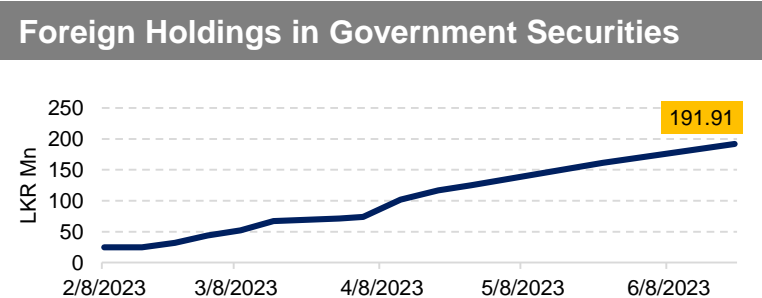
Market Cap Changes of GICS* Industry Groups (22/05/2023-22/05/2023)



Foreign Inflows (Rs Mn) YTD* (23/06/23)

Foreign Inflow	16,343.13
Foreign Outflow	15,833.32
Net Foreign Inflow/(Outflow)	509.79

*YTD: Year to Date



Evolving Landscape

With the aim of keeping our members updated on latest global trends, especially those influencing Sri Lanka, 'Evolving Landscape' section was added to the MEU. This section guide our members in strategic planning, innovation and competitiveness and helping them identify sector-specific opportunities and challenges.

Generative AI: Impact Across Industries and on Developing Countries

Artificial Intelligence (AI) is a rapidly growing field of technology that has the potential to revolutionize many industries. AI is used to create computer systems that can think and act like humans, allowing them to solve complex problems and automate tasks.

Generative AI: Industry Impacts

Retail and consumer packaged goods companies

Generative AI could enhance the retail and consumer packaged goods sectors, potentially increasing annual revenues by \$400 billion to \$660 billion. This technology enables automation in various areas, including personalized recommendations and faster consumer research. However, quality control and security measures are crucial to mitigate potential risks and ensure reliable output.

Pharmaceuticals and medical products

Generative AI could offer the pharmaceutical and medical-product sectors value equating to \$60 billion to \$110 billion, or 2.6 to 4.5 percent of annual revenues. By automating preliminary screenings and enhancing indication finding, it can expedite drug discovery and improve R&D. However, integration requires considerations for quality checks, generated content explainability, and privacy of medical data.

Banking

Generative AI could potentially add \$200 billion to \$340 billion to annual revenues. It can improve customer satisfaction, decision-making, and fraud monitoring. Examples include AI assistants like Morgan Stanley's, which aid wealth managers. However, integration requires careful consideration of regulatory and data constraints, automation levels, and user expectations.

Work and productivity implications

Generative AI could automate 60-70% of work activities, potentially transforming knowledge work and accelerating automation by nearly a decade. It may significantly impact higher-wage workers and could challenge traditional education credentials as primary skill indicators. If workers can adapt, generative AI might increase global productivity by 0.2 to 3.3% from 2023 to 2040, counteracting slow workforce growth and boosting productivity rates.

Generative AI: Impact Across Industries and on Developing Countries cont'd

AI and Developing Countries

Positive Effects of AI on Developing Nations:

Healthcare: making medical products more affordable and providing remote medical services. AI aids in diagnoses and treatment decisions and enables price comparison of medical products. It also allows healthcare provision in distant areas. An instance is Clinicas de Azucar in Mexico that uses AI for diabetic patient care.

Education: AI facilitates effective study planning and personalizes learning methods for improved results.

Infrastructure and Energy: AI with 3D printing assists in creating affordable housing, while AI services, like Azuri Technologies, optimize energy use.

Agriculture: AI improves weather predictions, crop selection, pesticide use, and irrigation design, boosting productivity, profits, food security, and waste minimization.

Negative Consequences of AI on Developing Nations:

Could exacerbate the income disparity between wealthy and poor nations. The IMF suggests that higher salaries in advanced economies can encourage workforce replacement with new technology, potentially diverting investments from developing nations and decreasing their GDP.

Anticipated to impact job markets, particularly in manufacturing and logistics sectors, traditionally outsourced to developing countries. Automation through robotics could lead to significant job losses.

Access to AI solutions is challenging in the developing world, with regions like Africa, where only 40% of the population uses the internet, potentially being isolated from AI's technological advancements.

According to the 2022 Oxford Insight's Government AI Index, emerging nations considerably trail in national-level AI preparedness, which could amplify AI's possible negative effects.

Datasheet

Latest Available data

External Trade (USD Mn)	Apr-2023	Month Ago	Year Ago
Exports	849	1,037	971
Agricultural Exports	184	216	790
Industrial Exports	661	816	178
Imports	1,431	1,450	1,699
Consumer Goods	262	266	236
Intermediate Goods	985	972	1,197
Investment Goods	180	359	266
Trade Balance	-583	-412	728
Tourist Arrivals ('000)	83,309 (May)	105,498	30,207
Tourism Earnings	132 (May)	167	44
Workers' Remittances	498 (May)	454	304
Inflation (%)	May-2023	Month Ago	
CCPI (2021 base)			
Headline	25.2	35.3	
Core	20.3	27.8	
NCPI (2021 base)			
Headline	22.1	33.6	
Core	21.6	31.8	
Interest Rates (%)		Month Ago	Year Ago
AWPR	19.69 (Jun)	20.34	22.27
AWLR	17.87 (Apr)	18.29	11.31
AWDR	15.23 (May)	15.12	6.99
AWFDR	19.84 (May)	19.72	8.97
SDFR	13.00 (Jun)	15.50	13.50
SLFR	14.00 (Jun)	16.50	14.50
Growth in Credit to Private Sector	-8.3 (Apr)	-5.1	20.3
Fiscal Sector (LKR Bn)		2023 (Jan-Feb)	Year Ago
Revenue and Grants		458.6	311.5
Expenditure and Net Lending		781.5	551.7

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Economic Intelligence Unit
of The Ceylon Chamber
of Commerce

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