

MONTHLY ECONOMIC UPDATE

March 2023

EIU



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KEY INSIGHTS

IMF Board Approved a 48-month EFF of about USD 2.9 Bn to Support Sri Lanka's economic policies and reforms

Sri Lankan Economy Contracted by 7.8% in 2022, IMF is expecting a 3% contraction in 2023.

Global Goods Trade Barometer Declines further, hinting at Q4 Trade Slump: WTO

SRI LANKAN ECONOMY

Sri Lanka received the Board Approval for the IMF-EFF: The Executive Board of the International Monetary Fund (IMF) approved a 48-month Extended Fund Facility (EFF) of SDR 2.286 Bn (about USD 2.9 Bn) to support Sri Lanka's economic policies and reforms. The first disbursement of USD 333 Mn was received.

LKR Appreciated in March: In the lead up to the IMF Board approval, improvement in dollar liquidity and sentiment saw a sharp appreciation of the LKR against the USD. The LKR recorded an appreciation of 13% against the USD, thus far in 2023.

CBSL Policy Rates Increased: The CBSL has decided on a further tightening of the Monetary Policy by increasing policy rates by 100 basis points to 15.5% and 16.5% for SDFR and SLFR respectively.

Economy contracted by 7.8% in 2022: The economy declined in all four quarters of 2022, with a higher contraction in each consecutive quarter resulting in a 7.8% annual contraction in 2022.

Trade Deficit Narrowed in January: Export earnings declined and import expenditure remained subdued in January 2023, and as a result the trade deficit narrowed by 52.3% on a Y-o-Y basis.

Strong growth in remittances inflows: In February 2023, inflow of workers' remittances registered a record level increase of 99% on a Y-O-Y basis.

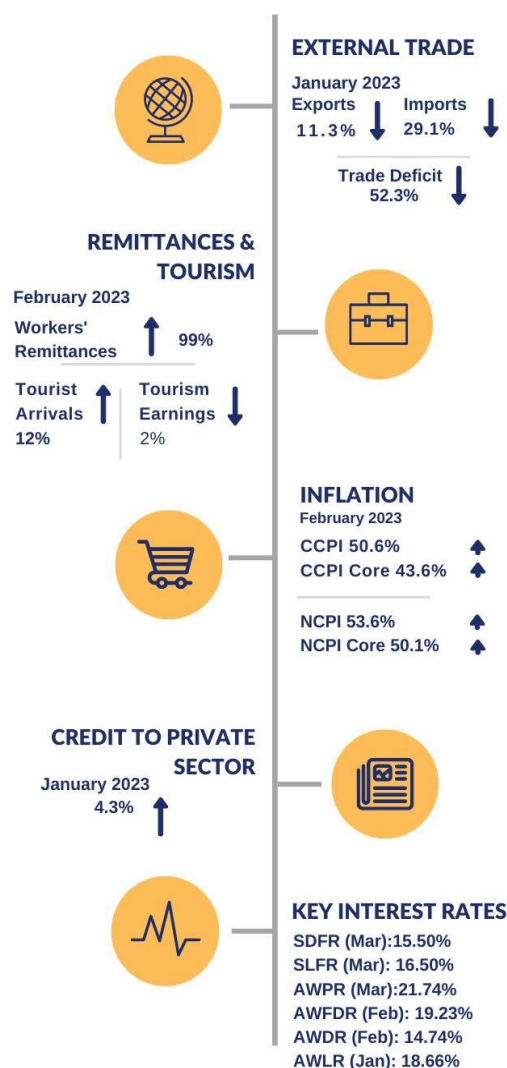
GLOBAL ECONOMY

The DCTS was introduced by the UK Government: The Developing Country Trading Scheme (DCTS) was introduced by the UK Government, which they are expecting to implement in early 2023. The scheme contributes to developing countries' integration into the global economy, creating stronger trade with developing countries, boosting the economy and supporting jobs in those countries.

Global Goods Trade Barometer Declines Further: As per the latest Global Goods Trade Barometer, the World merchandise trade growth appears to have lost momentum in the 4Q of 2022 and is likely to remain weak in the first quarter, says the World Trade Organization.

MACROECONOMIC SNAPSHOT

Y-O-Y CHANGES



Data Sources: Central Bank, Sri Lanka
Department of Census and Statistics, Sri Lanka
Tourism Development Authority, Sri Lanka

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FURTHER INSIGHTS- SRI LANKAN ECONOMY

Sri Lanka Received the IMF Executive Board Approval for the EFF Arrangement

The Executive Board of the International Monetary Fund (IMF) approved a 48-month Extended Fund Facility (EFF) of SDR 2.286 Bn (about USD 2.9 Bn) to support Sri Lanka's economic policies and reforms.

As the country was struggling with its worst financial crisis, Sri Lanka defaulted in its debt in April 2022, for the first time in history. Thereafter, a Sri Lankan delegation had a technical discussion with the IMF and on 1st of September 2022, the IMF staff reached a staff-level agreement on an EFF with Sri Lanka.

The Government had to implement some difficult steps in lead-up to securing the EFF, such as cost-reflective tariff for utilities, changes in tax regime, legislation of the new Central Bank Act and the move towards a flexible exchange rate. By early March 2023, Sri Lanka received IMF-compatible financing assurance from its official creditors, including Paris Club members, India and China. As a result of all these efforts, on 20th March 2023, Sri Lanka received the IMF board-level approval.

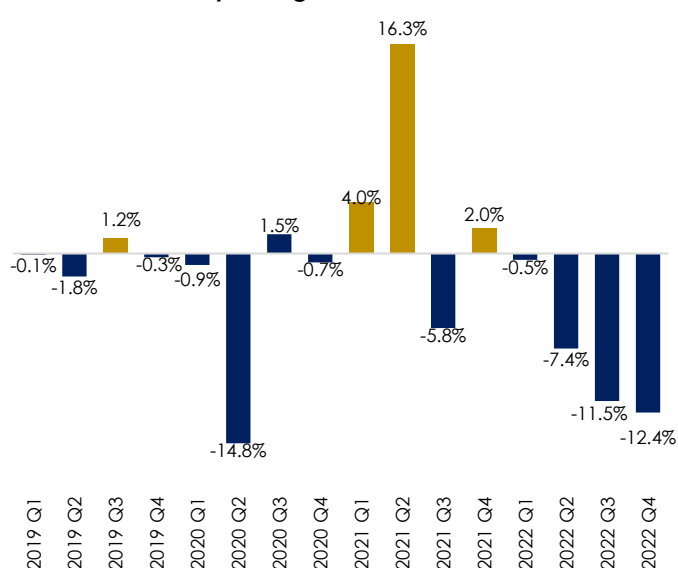
The objectives of the EFF-supported program are to restore macroeconomic stability and debt sustainability, safeguarding financial stability, and stepping up structural reforms to unlock Sri Lanka's growth potential.

Interested to read more on this? Please see the attached supplement.

Economy Contracted by 7.8% in 2022 compared to 2021

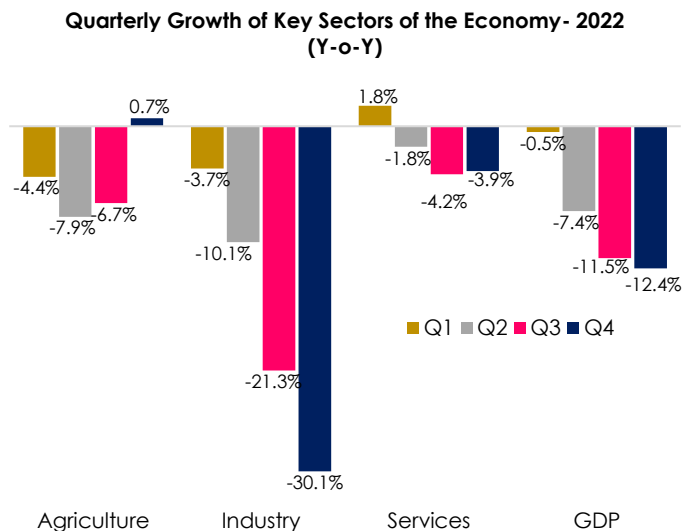
The Sri Lankan economy recorded a negative growth of 7.8% for the year 2022 in comparison to the value recorded in 2021. In real terms, GDP of the country for 2022 has declined to Rs. 12,017 Bn from Rs. 13,037 Bn recorded in 2021. The gradual recovery observed in economic activities post the COVID 19 pandemic was reversed by the deepening economic crisis and the rising of youth and social unrest related impacts. In addition, frequent power disruptions, fuel shortages, unavailability or shortage of raw material, foreign exchange crisis and supply chain disruptions drove the economy to a record level contraction. In terms of economic activities, the contraction of the economy was mainly contributed by the declining of construction activities and manufacturing of food and beverages.

Quarterly GDP growth rates 2019- 2022



Considering on quarterly growth performance, the economy declined in all quarters of 2022, with a higher contraction in each consecutive quarter. The quarterly economic growth rate had worsened from -0.5% in Q1 to -12.4% in Q4 at a Y-o-Y basis.

The growth projections for Sri Lanka are pessimistic as The World Bank, IMF and ADB expect a growth of -4.2%, -3% and -3.3% respectively in 2023.



Q1-2022: Services was the only sector that showed a growth with a marginal growth of 1.8%, while the Agriculture and Industry sectors had contracted by 4.4% & 3.7% respectively.

Q2: All three sectors had shown negative growth with the Industry sector contracting the most by 10.1%, followed by the Agriculture sector with a 7.9% contraction.

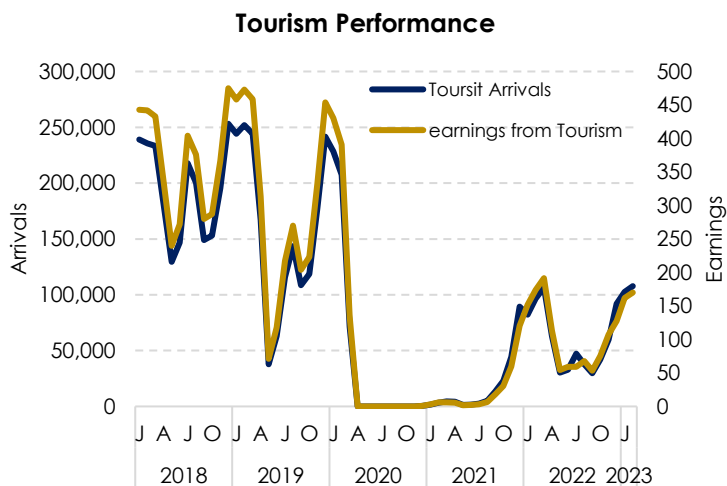
Q3: The trend worsened with Industry sector declining by 21.3% and services sector declining by 4.2%. Agriculture sector also had declined in Q3 by 6.7%.

Q4: The Industry sector had declined for the 4th consecutive quarter, with highest contraction in the fourth quarter of 30.1%. Services had also experienced a decline of 3.9%. Agriculture is the only sector which showed positive growth of 0.7%.

Tourism shows the much-needed Recovery

Sri Lanka's tourism industry is showing signs of a much-needed recovery thus far in 2023, with an increase in tourist arrivals compared to the previous year. According to the Sri Lanka Tourism Development Authority, the country has seen a significant rise in the number of arrivals in recent months, indicating that the industry is slowly bouncing back from the setbacks of the past. This positive trend is a welcome relief for Sri Lanka's tourism sector, which was severely impacted by the COVID-19 pandemic and the resulting travel restrictions.

The first two months of the year have been positive for Sri Lanka's tourism industry, with the top five countries that generated the most international tourism being the Russian Federation, India, the United Kingdom, Germany, and France. The Russian Federation maintained its position as the leading source of tourists, accounting for a significant percentage of total arrivals in both January and February. Arrivals from China has increased from 835 in January to 1,535 in February. China was one of the top sources of tourists pre- COVID.



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FURTHER INSIGHTS- GLOBAL ECONOMY

Brief on the Developing Countries Trading Scheme of the UK

The Government of UK introduced the Developing Countries Trading scheme (DCTS) to improve access to the UK market for developing countries. The DCTS is expected to implement in early 2023. In line with the UK government's new International Development Strategy, the scheme contributes to developing countries' integration into the global economy, creating stronger trade with developing countries, boosting the economy and supporting jobs in those countries. The DCTS aims to support sustainable growth in developing countries through a more generous unilateral offer. This scheme aims to demonstrate the UK's leadership in the use of trade for development. This has led to provisions in the DCTS which reduce tariffs, liberalize rules of origin requirements and simplify the conditions attached to the scheme. The DCTS applies to countries that currently benefit under the UK's Generalized Scheme of Preferences (GSP). The GSP includes 47 countries in the GSP Least Developed Country (LDC) Framework and 18 additional countries or territories classified by the World Bank as low income (LIC) and lower- middle income countries (LMIC) including Sri Lanka. It does not apply to countries classified by the World Bank as upper-middle income for 3 consecutive years, or LICs and LMICs with free trade agreement (FTA) with the UK.

This scheme has three levels of preferences, namely, Comprehensive Preferences for LDCs with 99% duty free access, Enhanced preferences with at least 85% duty free access and Standard Preferences.

According to the Department for International Trade of the UK, there are significant opportunities for Sri Lanka. If preferences were fully utilized, then the DCTS would result in tariff savings of around GBP 69mn a year, making Sri Lanka one of the top five beneficiaries of the scheme. Sri Lanka exports cinnamon, nuts, seeds, underwear, gloves, rubber tyres, cotton fabrics and resins. Imports to the UK from Sri Lanka in these products are comparatively low.

Source: Department for International Trade of the UK

Global Goods Trade Barometer Declines Further, hinting at Q4 Trade Slump

As per the latest reading of the Global Goods Trade Barometer, the World merchandise trade growth appears to have lost momentum in 4Q of 2022 and is likely to remain weak in the first quarter, says the World Trade Organization. The overall barometer index continues to point to weakening trade growth in volume terms after falling to 92.2, down from 96.2 in the previous release of the barometer and well below the baseline value of 100.

All of the barometer's component indices have fallen below trend except for the automotive products index (105.8), which was buoyed by above-trend sales and production figures for the US, Europe and Japan, outweighing declines in China. The export orders index (97.4) remains below trend but rising, hinting at a possible upturn in the near future. On the other hand, indices for container shipping (89.3), electronic components (84.9) and raw materials

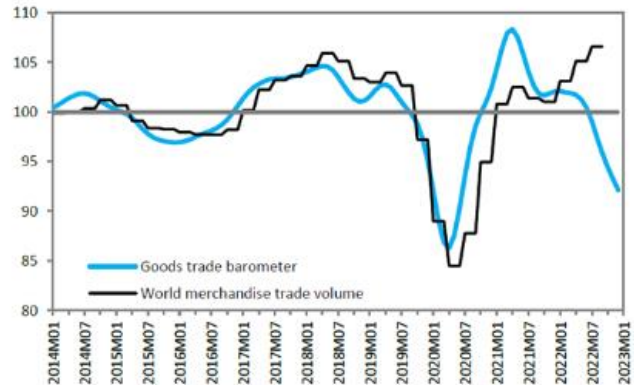
(92.0) are well below trend and declining, suggesting that weakness in trade is broad-based, impacting many sectors.

Goods trade barometer

Index value, December 2022 = 92.2



Index history, trend = 100



Silicon Valley Bank Collapsed, marking the Second Biggest Bank Failure in the US History

The Silicon Valley Bank (SVB), a bank for US tech startups, collapsed earlier this month, making it the second biggest bank failure in US history. The causes date back to 2018, when the Trump administration rolled back some of the banking regulations on smaller banks (assets with less than USD 250 bn) as means of liberating them from “excessive bureaucracy”. These regulations were placed in 2010 after President Obama signed the Dodd-Frank Act, which was created in the aftermath of the 2008 financial crisis. The SVB which was a relatively smaller bank in 2019 with just over USD 50 mn worth of deposits, had tripled their deposits by the end of 2021, as businesses deposited more during the pandemic. Using this, SVB bought longer-term US treasuries and government backed mortgage securities, increasing its securities portfolio by USD 100 bn. In March 2022, the Federal Reserve had started to raise interest rates in order to combat the rising concerns of inflation. As interest rates continued to rise, the bond prices fell. Soon SVBs investments were USD 17 bn less than their book value. It got worse, as new deposits declined throughout 2022.

In a regulatory filing on March 8th 2023, SVB announced it sold a large number of securities at a loss of USD 1.8 bn in order to cover the decline in deposits. This caused the stock price to fall substantially and a bank run was in action. The next day, people tried to withdraw USD 42 bn in deposits which made it insolvent. The collapse had caused a ripple effect in the banking sector. It caused the third largest bank failure in the US two days later. The Signature bank which had its own problems, experienced a bank run purely contagion from SVB. The First Republic Bank had to be saved by USD 30 bn deposits by 11 other large US banks, in order to boost the confidence of depositors. Further, banks lose billions in value as people lose confidence in the banking industry.

Source: World Trade Organization

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DASHBOARD

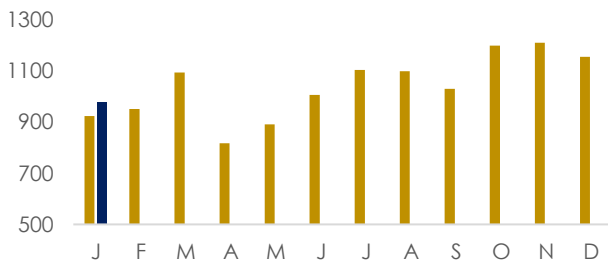
EXTERNAL SECTOR PERFORMANCE-JANUARY 2023

Legend: ■ 2022 ■ 2023

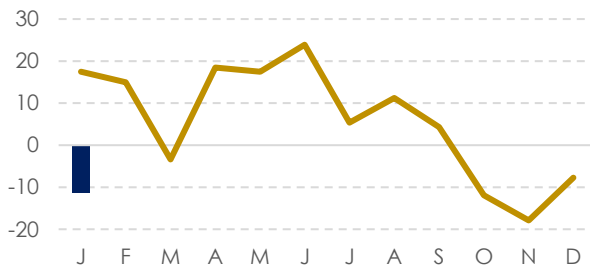
All the numbers are in USD Mn unless otherwise specified.

EXPORTS

EXPORTS DECLINED BY 11.3% Y-O-Y



Y-o-Y % CHANGE IN EXPORTS



INDUSTRIAL EXPORTS DECLINED BY 12.2% Y-O-Y

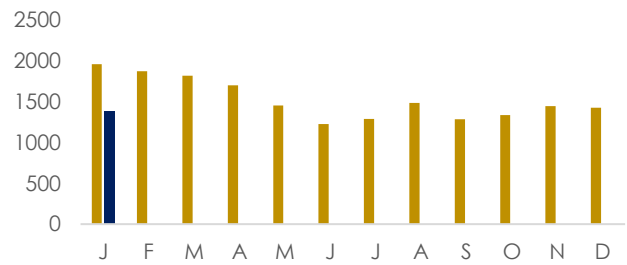


AGRICULTURAL EXPORTS DROPPED UP BY 6.6% Y-O-Y

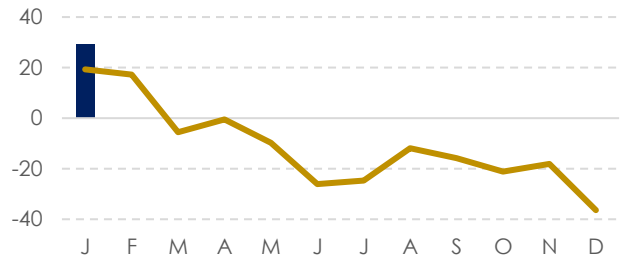


IMPORTS

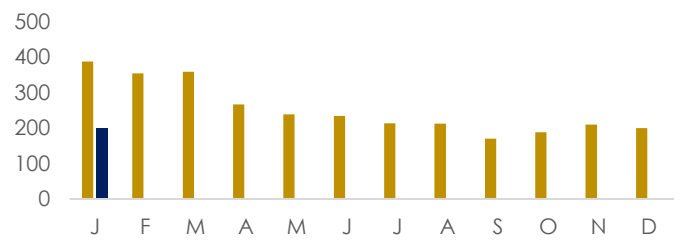
IMPORTS DECLINED BY 29.1% Y-O-Y



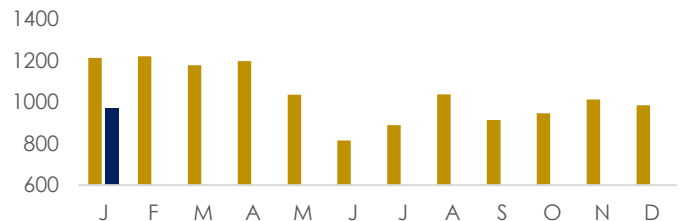
Y-o-Y % CHANGE IN IMPORTS



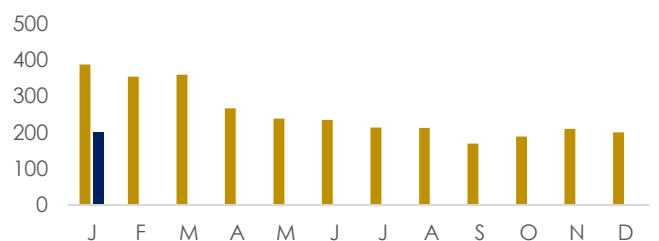
CONSUMER GOODS IMPORTS DROPPED BY 39.3% Y-O-Y



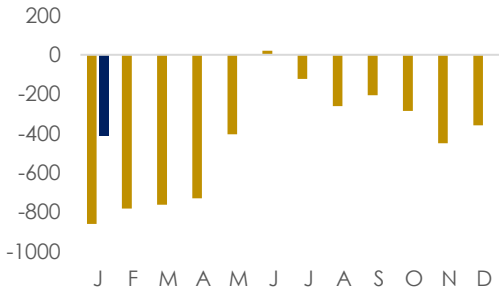
INTERMEDIATE GOODS DECLINED BY 20% Y-o-Y



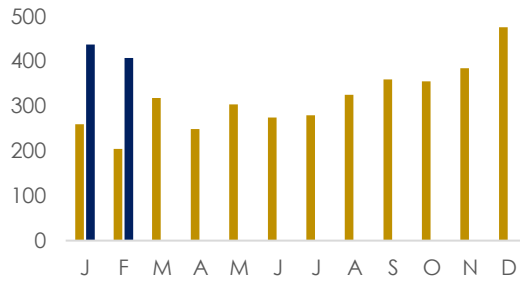
INVESTMENT GOODS DECLINED BY 48.6% Y-o-Y



TRADE DEFICIT NARROWED BY 52.3% Y-o-Y



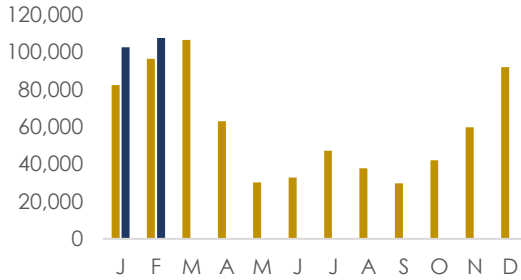
WORKERS' REMITTANCES INCREASED BY 99% Y-o-Y (Feb-2023)



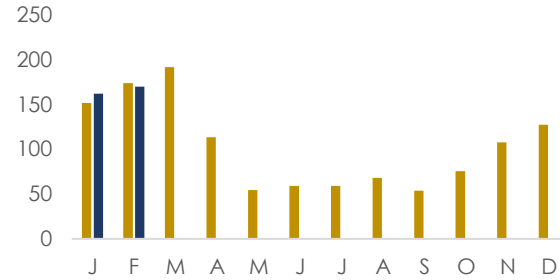
32%

of the total import bill covered by Remittances (Jan 2023)

12% INCREASE IN TOURIST ARRIVALS Y-o-Y (Feb-2023)



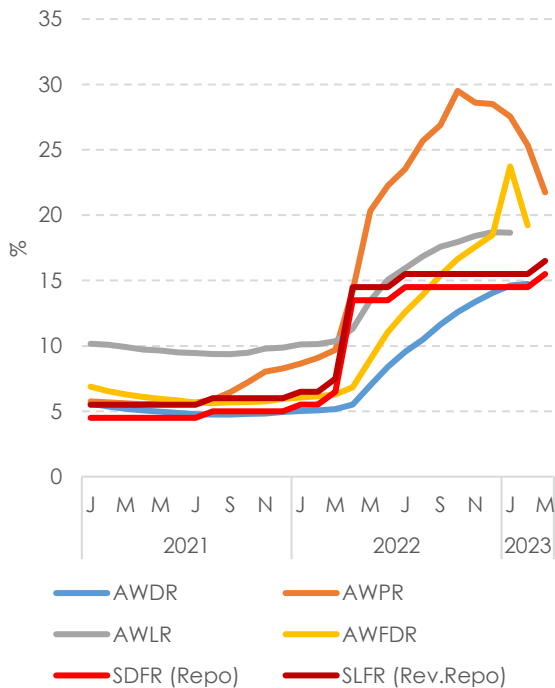
2% DROP IN TOURISM EARNINGS Y-o-Y (Feb-2023)



KEY INTEREST RATE INDICATORS

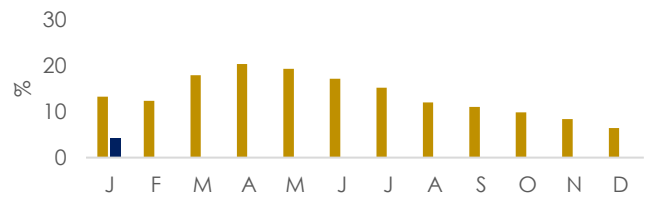
INTEREST RATES

Policy Rates increased to,
 Standing Deposit Facility Rate (SDFR): 15.50%
 Standing Lending Facility Rate (SLFR): 16.50%



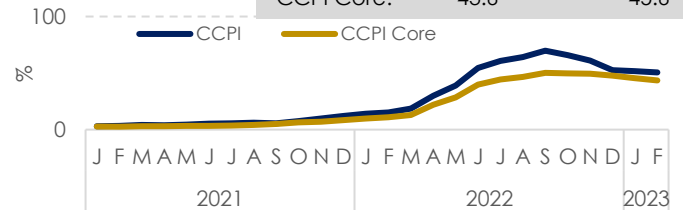
Source: CBSL

PRIVATE SECTOR CREDIT GROWTH



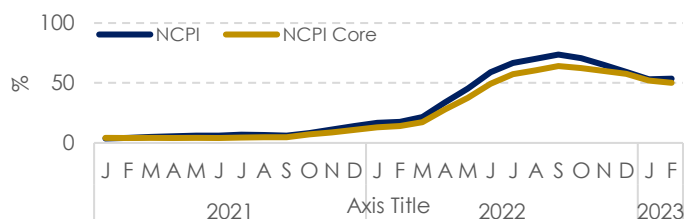
INFLATION: CCPI (BASE 2013) Y-o-Y

	Feb'23	Jan '23
CCPI:	50.6	51.7
CCPI Core:	43.6	45.6



INFLATION: NCPI (BASE 2013) Y-o-Y

	Feb'23	Jan'23
NCPI:	59.2	65.0
NCPI Core:	57.5	60.1



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