Monthly Economic Update (MEU)

July 2025

Economic Intelligence Unit
The Ceylon Chamber of Commerce

Highlights

Sri Lankan Economy

CBSL Keeps Policy Rate Unchanged

The CBSL decided to keep the Overnight Policy Rate (OPR) unchanged at 7.75%. This decision was made after a thorough assessment of domestic and global economic conditions. The Board believes that maintaining the current policy stance will guide inflation toward the 5% target while also supporting economic growth.

IMF Approves 4th Review of Sri Lanka's USD 2.9 Bn Bailout

Sri Lanka secured an additional USD 347 million from the IMF, raising total disbursements to USD 1.74 billion. Strong program performance is reflected in a 1.6% primary surplus, improved reserves (USD 6.2 billion), and inflation control. Key reforms include VAT-led revenue gains, electricity tariff hikes to stabilize the CEB, and expanded Aswesuma transfers. Debt restructuring is nearing completion, and financial sector stability is improving. However, risks remain, requiring agile policies and continued structural reforms to boost exports, attract FDI, and enhance public sector efficiency.

New US Tariff on Sri Lanka signals Trade Tensions and Need Policy Response

On July 17, 2025, U.S. President Donald Trump imposed a 30% tariff on all imports from Sri Lanka, effective August 1, as part of a broader trade move targeting several countries. Although lower than the earlier proposed 44%, the tariff significantly affects key Sri Lankan exports like apparel, seafood, rubber, and processed foods, threatening competitiveness and jobs, especially among SMEs. Rising domestic energy costs further weaken Sri Lanka's export position. Trump justified the tariff citing trade imbalances and offered tariff relief if firms shift production to the U.S. Without strategic policy action, Sri Lanka risks long-term export market losses.

Sri Lanka Retains Lower- Middle-Income Status in World Bank's 2026 Classification

The World Bank's FY2026 update classifies Sri Lanka as a lower-middle-income country, with a GNI per capita between $1,136 and $4,465. This status reflects a fragile recovery marked by inflation, currency depreciation, and ongoing reforms. The classification influences Sri Lanka's access to concessional financing and development aid, serving as a benchmark for progress. Regionally, most South Asian countries, including Sri Lanka, have moved from low- to lower-middle-income status since 1987. To reach upper-middle-income status, Sri Lanka must boost productivity, diversify exports, invest in human capital, and strengthen infrastructure, requiring sustained reform and inclusive growth strategies to ensure long-term resilience.

Global Economy

Global Trade Rebounds Amid Rising Digital Market Concentration

Global trade rebounded by $300 billion in early 2025, led by price increases and strong demand in developed economies. Yet, rising digital market concentration poses risks, with the top five digital multinationals now controlling 48% of global digital sales, up from 21% in 2017. This dominance threatens competition and equitable access, especially for developing nations. UNCTAD urges countries like Sri Lanka to invest in digital infrastructure, promote fair competition, and engage in global digital governance to harness inclusive growth from the evolving digital economy.

UK's Growing Role in Trade with Asia and Developing Economies

The UK has introduced two key trade initiatives: a free trade agreement with India and reforms to the Developing Countries Trading Scheme (DCTS). The UK-India FTA removes most tariffs and aims to boost bilateral trade to $120 billion by 2030. Meanwhile, DCTS reforms simplify rules and expand tariff-free access for over 65 developing countries, including Sri Lanka. Notably, relaxed rules of origin will benefit Sri Lanka's apparel exports. These policies offer export growth opportunities but require countries to meet UK standards and enhance supply chain efficiency.

Dashboard

Y-o-Y changes, otherwise specified

Economic Growth

4.8% Q1-2025

5.1% (Q1-2024)

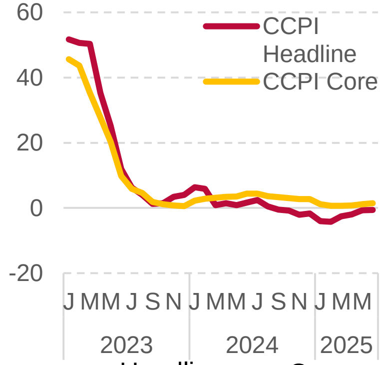
Movement of Purchasing Managers' Index- June 2025

Manufacturing PMI	51.9
Services PMI	61.9
Construction PMI (May)	59.7

All three indices recorded an expansion indicating the overall ourlook of three sectors remain positive in the next 3 months

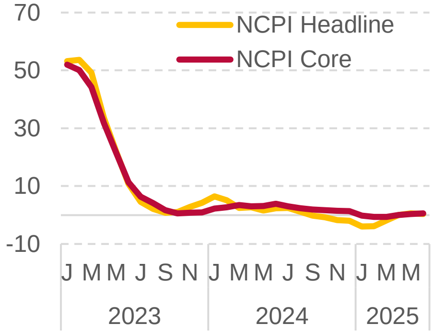
Inflation

CCPI Inflation (%)-*Base 2021*



Jun 2025 Headline **-0.6%** Core **1.5%**

NCPI Inflation (%)-*Base 2021*



May 2025 Headline **0.6%** Core **0.3%**

External Sector

Merchandise Trade
May 2025

Trade Deficit USD 473mn

Exports USD 1,035mn
2.3% y-o-y growth

Imports USD 1,507mn
7.3% y-o-y growth

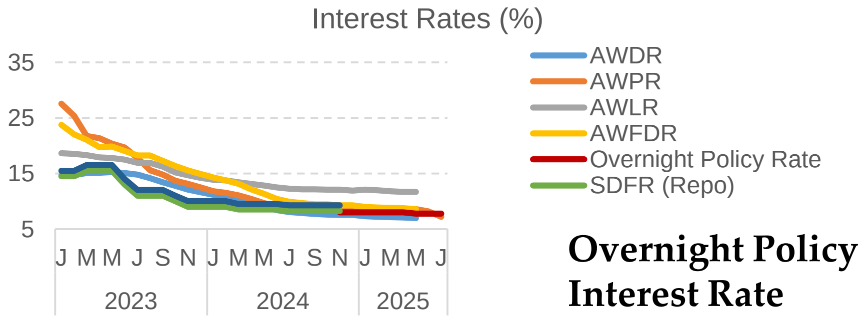
Services Trade USD 227mn
6.4.% y-o-y contraction

Tourist Arrivals 132,241
May 2025 19% y-o-y growth

Tourism Earnings
USD 169.5mn
7% y-o-y growth

Workers' Remittances
USD 645.7mn
18% y-o-y growth

Interest Rates



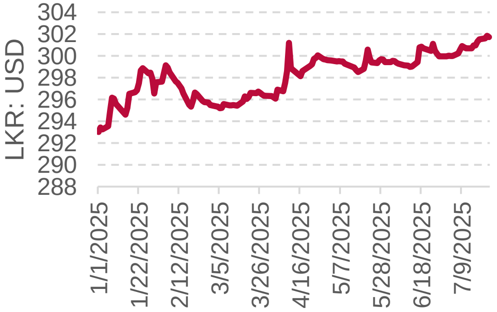
Growth in Credit to Private Sector

May 2025

16.1%

Overnight Policy Interest Rate (OPR): 7.75%

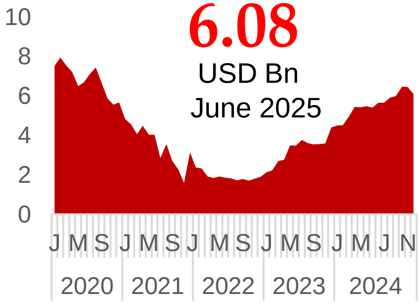
Exchange Rate



Depreciation of LKR thus far 2025

3%

Official Reserves



6.08
USD Bn
June 2025

KEY INSIGHTS
Sri Lankan Economy

IMF Approves 4th Review of Sri Lanka's USD 2.9 Bn Bailout

On completion of the Fourth Review by the IMF Executive Board, Sri Lanka has been granted access to an additional USD 347 million, bringing total purchases to USD 1.74 billion. The approval follows new and modified quantitative targets and structural benchmarks until June 2026. Program performance remains strong, with end-March 2025 fiscal and monetary targets mostly met. Key achievements include strong revenue performance, a 1.6% of GDP primary surplus, and inflation control, aided by low energy prices. Importantly, gross official reserves climbed to USD 6.2 billion by April 2025, driven by robust tourism and remittances. Fiscal consolidation continues on a revenue-led path, with VAT and external trade taxes performing well. However, arrears data was revised upward, leading to a breach of expenditure arrears targets. The government is committed to clearing these by 2027, aided by improved public financial management systems.

Electricity pricing reforms were restored in June 2025 after an earlier tariff cut led to operating losses at the CEB. A 15% tariff hike is expected to stabilize the utility's finances. The authorities also recommended maintaining automatic tariff adjustments and amending regulations to ensure transparent, cost-reflective pricing. Social protection reforms have advanced, with expanded Aswesuma transfers and steps toward a national social protection strategy. Financial sector resilience is supported by capital adequacy across banks, with declining NPLs.

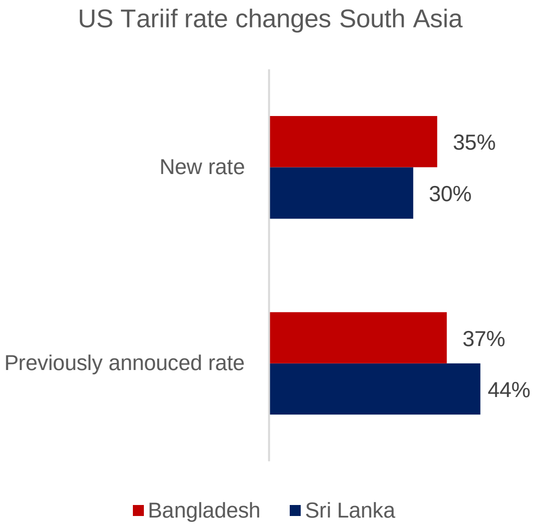
Debt sustainability remains a key priority, with Sri Lanka nearing completion of external debt restructuring. The establishment of the Public Debt Management Office strengthens institutional capacity for prudent borrowing and risk management. IMF notes that the programme risks remain elevated due to potential global trade shocks. The IMF stresses the need for policy agility and coordinated responses to protect program gains. Structural reforms to boost exports, attract FDI, and improve public sector efficiency remain central to Sri Lanka's medium-term recovery.

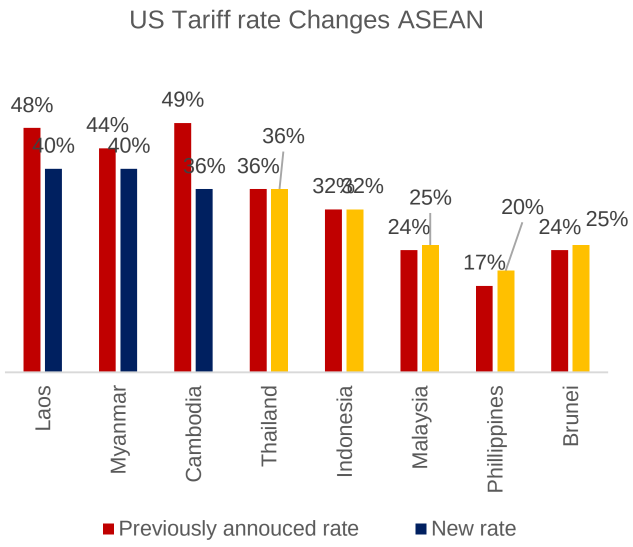
Quantitative performance criteria		
	End March Target	**Actual**
Central government primary balance (floor)	**Rs. 80 billion**	**Rs. 397 billion**
Net credit to the government of the CBSL (ceiling)	**Rs. 2,560 billion**	**Rs. 2,508 billion**
Programme net Official International Reserves (floor)	**(USD 645 million)**	**USD 285 million**
Stock of expenditure arrears of the central government (ceiling)	**Rs. 0**	**Rs. 138 billion**
Central government tax revenue (floor)	**Rs. 800 billion**	**Rs. 986 billion**
CBSL purchases of government securities in the primary market	**Rs. 0**	**Rs. 0**
Headline Inflation	**5% ± 3%**	**-3.6%**
Social Spending by central government (floor)	**Rs. 53 billion**	**Rs. 53 billion**
Treasury guarantees (ceiling)	**Rs. 2,100 billion**	**Rs. 1,452 billion**
Treasury FX guarantees (ceiling)	**Rs. 1,275 billion**	**Rs. 912 billion**

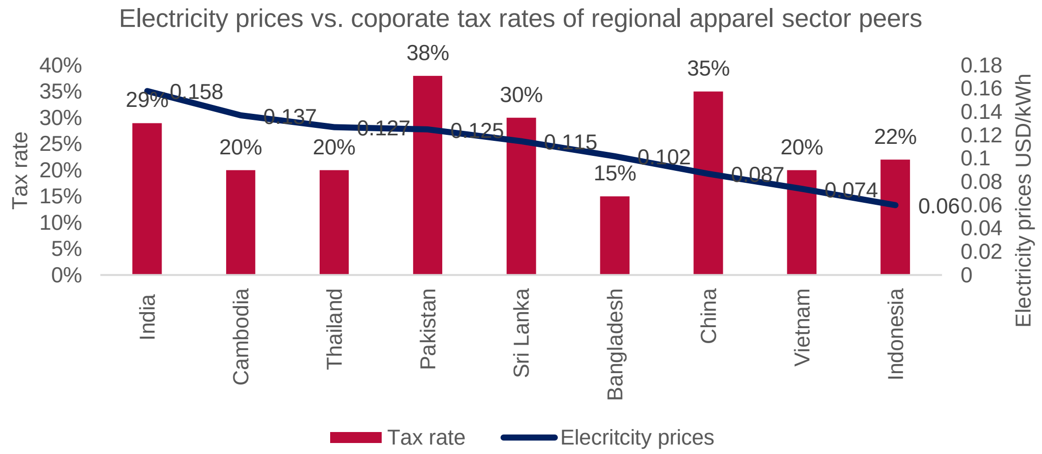
Data Source: IMF

New U.S. Tariff on Sri Lanka Signals Trade Tensions and Need for Policy Response

On July 17, 2025, U.S. President Donald Trump announced a new 30% tariff on all imports from Sri Lanka, effective August 1, 2025. This move is part of a broader trade action affecting seven countries, including Algeria, Libya, Iraq, Brunei, and the Philippines. The tariff is a reduction from the earlier 44% floated in April, but it remains well above the Most Favoured Nation (MFN) rate for key products such as apparel. However, other sectors are also exposed. Exports of seafood, rubber products, plastics, processed foods, and even select industrial goods like auto components and chemicals now face sharp cost increases. These sectors, many of which previously benefited from low or near-zero duties, now risk losing competitiveness. Small and medium exporters are especially vulnerable, with risks of job losses and reduced foreign exchange earnings. Sri Lankan exports may also become less competitive due to rising domestic production costs. In addition to the new U.S. import tariff, local manufacturers already face higher electricity tariffs compared to regional apparel-exporting peers. These elevated energy costs, combined with increased external taxes, continue to erode Sri Lanka's price advantage, making its products more expensive in global markets. In a statement shared on Trump's social media platform, the tariff was justified as a response to what he described as a long-standing trade imbalance and non-reciprocal barriers in Sri Lanka. Trump also warned that any retaliation from Sri Lanka through tariff hikes would be met with an equal increase in U.S. levies. He offered a pathway for relief, suggesting that Sri Lankan firms could avoid the tariffs by relocating production to the United States. This move comes amid a broader recalibration of U.S. trade policy, which appears to be balancing geopolitical interests with efforts to diversify supply chains. While some ASEAN nations such as Cambodia, Laos, and Myanmar received tariff reductions, others like Malaysia and Brunei faced modest increases. For Sri Lanka, the 30% blanket tariff poses serious risks to export competitiveness, especially in sectors such as apparel that heavily depend on the U.S. market. Though the cut from 44% offers some short-term relief, Sri Lanka remains at a disadvantage compared to countries like the Philippines (20%) and Bangladesh (35%). Without a clear policy response, Sri Lanka risks long-term displacement in global markets especially in industries where pricing and reliability determine supplier choices.







Data Sources: Whitehouse, First Capital Research

KEY INSIGHTS
Sri Lankan Economy

Sri Lanka Retains Lower- Middle-Income Status in World Bank's 2026 Classification

The World Bank's annual update for fiscal year 2026 reaffirms Sri Lanka's status as a lower-middle-income economy, based on its Gross National Income (GNI) per capita, calculated using the Atlas method. This method smooths exchange rate fluctuations to provide a more stable and comparable measure of economic capacity across countries.

For 2026, the World Bank defines income groups as follows:

- Low-income: GNI per capita of $1,135 or less
- Lower-middle-income: $1,136 to $4,465
- Upper-middle-income: $4,466 to $13,845
- High-income: $13,846 or more

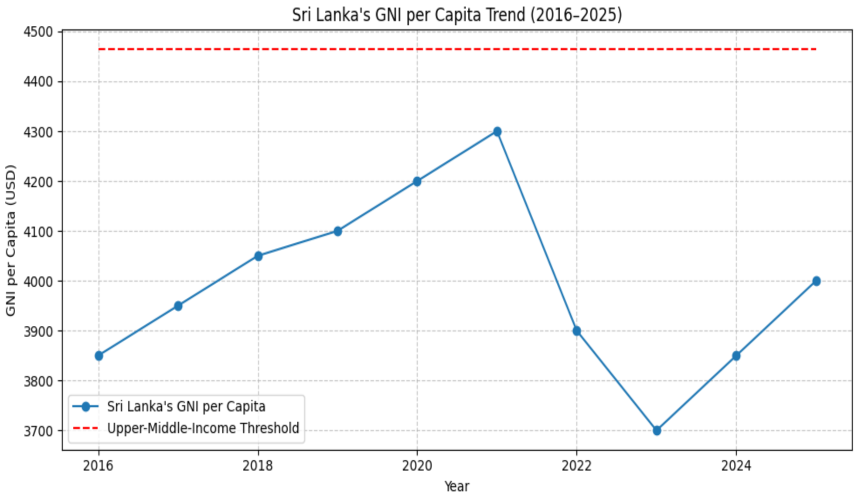
Sri Lanka's continued placement in the lower-middle-income bracket reflects a complex and uneven recovery path. While the country has made progress in macroeconomic stabilization, its GNI per capita remains below the threshold required to transition into the upper-middle-income category. Key factors influencing this outcome include persistent inflation, currency depreciation, and the ongoing implementation of structural reforms aimed at fiscal consolidation and economic resilience.

This classification has far-reaching implications. It affects Sri Lanka's eligibility for concessional financing, access to development aid, and its positioning in global economic forums. Moreover, it serves as a benchmark for policymakers to evaluate progress and refine strategies for inclusive and sustainable growth.

Regionally, South Asia has undergone a significant transformation. In 1987, all countries in the region were classified as low-income. By 2024, only 13% remained in that category, with most including Sri Lanka now in the lower-middle-income group. This shift underscores the region's broader development momentum, but also highlights the need for continued reform and investment.

To advance toward upper-middle-income status, Sri Lanka must prioritize boosting productivity across sectors, diversifying exports to reduce external vulnerabilities, strengthening human capital through education and health investments and enhancing digital and physical infrastructure to support innovation and competitiveness

Achieving this transition will require sustained policy commitment, strategic investments, and inclusive growth strategies that empower all segments of society. As global economic dynamics evolve, Sri Lanka's ability to adapt and innovate will be key to unlocking long-term prosperity.



Data Source: World bank

KEY INSIGHTS
Global Economy

Global Trade Rebounds Amid Rising Digital Market Concentration

In the first half of 2025, global trade experienced a notable recovery, expanding by approximately $300 billion, driven largely by price increases and strong performance in developed economies. The United States saw a 14% surge in imports, while the European Union's exports rose by 6%, reversing recent trends that had favored developing nations.

However, this rebound masks a growing concern: the increasing concentration of digital markets. According to UNCTAD, the top five multinational digital enterprises now command 48% of global digital sales, up from 21% in 2017. These firms spanning cloud services, e-commerce, AI, and digital advertising are reshaping global commerce through aggressive platform expansion, data monopolization, and vertical integration.

This consolidation raises serious risks for competition, innovation, and equitable access. Seven of the world's ten most valuable companies are now digital giants, and their dominance threatens to marginalize startups, MSMEs, and developing economies that lack robust digital infrastructure. For countries like Sri Lanka, which are working to expand their digital trade footprint, the challenge lies in accessing global platforms on fair and inclusive terms.

UNCTAD emphasizes the need for coordinated policy responses. The European Union and ASEAN have proposed stricter antitrust regulations and enhanced digital market oversight. Meanwhile, UNCTAD urges developing nations to invest in digital infrastructure, foster local platforms, and engage in international digital governance frameworks.

For Sri Lanka, this moment presents both a challenge and an opportunity. By strengthening domestic digital capabilities, ensuring fair competition, and aligning with global standards, the country can better position itself to benefit from the digital economy. Proactive policy engagement and regional collaboration will be essential to navigate risks and unlock inclusive growth.

As digitalization continues to reshape global trade, ensuring a balanced and equitable digital ecosystem will be key to sustaining long-term development and resilience.

United States import growth strong in Q1 2025; European Union exports lead major economies

GOODS (Q1 2025)	Imports growth		Exports growth	
	Quarterly	Annual	Quarterly	Annual
Brazil	7%	13%	1%	-2%
China	-4%	-1%	1%	6%
India	-8%	6%	-4%	0%
Japan	2%	-1%	1%	0%
Republic of Korea	-4%	1%	-5%	6%
Russian Federation	-11%*	1%*	-9%*	1%*
South Africa	0%	-1%	-5%	1%
United States	14%	12%	3%	3%
European Union	3%	1%	6%	3%

Source: UNCTAD calculations based on national statistics.
Note: Quarterly growth rates are relative to the previous quarter. The annual growth is calculated using a trade-weighted average over four quarters. Data is seasonally adjusted. Data excludes intra-European Union trade. *denotes estimates.

Q1 2025 services trade growth was mixed for major economies

SERVICES (Q1 2025)	Imports growth		Exports growth	
	Quarterly	Annual	Quarterly	Annual
Brazil	-1%	14%	-2%	5%
China	2%	11%	-4%	18%
India	-9%	11%	2%	15%
Japan	4%	7%	-3%	9%
Republic of Korea	0%	6%	0%	10%
Russian Federation	-4%*	6%*	-1%*	3%*
South Africa[1]	4%	6%	2%	12%
United States	2%	10%	0%	8%
European Union	3%	6%	0%	6%

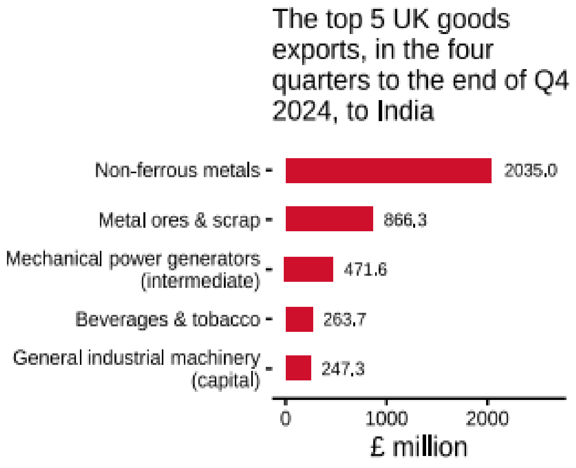
Source: UNCTAD calculations based on national statistics.
Note: Quarterly growth rates are relative to the previous quarter. The annual growth is calculated using a trade-weighted average over four quarters. Data is seasonally adjusted. Data excludes intra-European Union trade. *denotes estimates. [1]data is for Q4 2024.

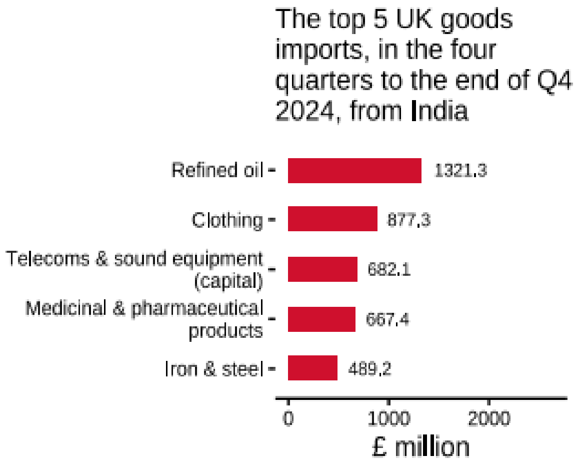
Data Source: UNCTAD

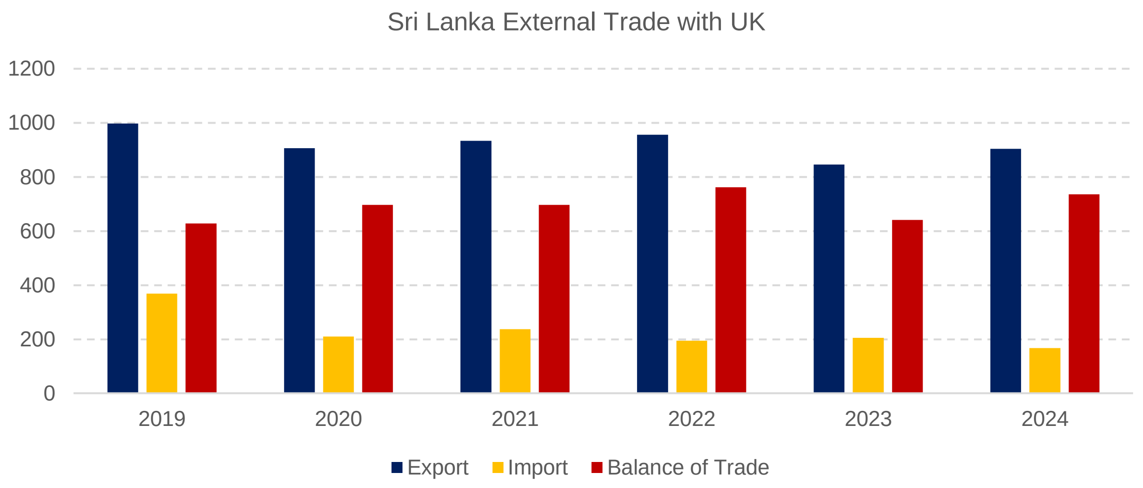
KEY INSIGHTS
Global Economy

UK’s Growing Role in Trade with Asia and Developing Economies

The United Kingdom has recently implemented two significant trade policy initiatives affecting developing and emerging economies: the free trade agreement (FTA) with India and reforms to the Developing Countries Trading Scheme (DCTS). The UK-India FTA, signed during Indian Prime Minister Narendra Modi’s visit to London in July 2025, removes tariffs on nearly all Indian exports to the UK and reduces tariffs on the majority of UK exports to India. The agreement covers sectors including textiles, electric vehicles, pharmaceuticals, and alcoholic beverages. It aims to increase bilateral trade from current levels to $120 billion by 2030, reflecting the UK’s post-Brexit strategy to expand trade partnerships beyond Europe. Concurrently, the UK government has revised the DCTS to simplify trade rules and broaden tariff-free access for products from developing countries such as Sri Lanka, Nigeria, and the Philippines. One key reform is the relaxation of rules of origin, which now allows exporters to use components sourced from multiple countries in Asia and Africa without losing tariff-free status in the UK. This change is especially relevant for Sri Lanka’s apparel sector, which depends on imported inputs, as the new rules will take effect starting early 2026. The scheme covers over 65 countries and thousands of products, aiming to lower trade costs, improve market access, and support economic development. Together, these policies aim to strengthen trade relationships, enhance supply chain resilience, and promote economic growth. For countries like Sri Lanka, the combined effect of the UK-India FTA and DCTS reforms presents an opportunity to increase exports, diversify markets, and attract foreign investment. However, fully realizing these benefits requires meeting UK import standards, streamlining customs procedures, and investing in efficient supply chains. These evolving UK trade policies offer significant opportunities but also demand proactive engagement and adaptation from developing economies.







Data Sources: Department for Business and Trade-UK, Sri Lanka Customs

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.

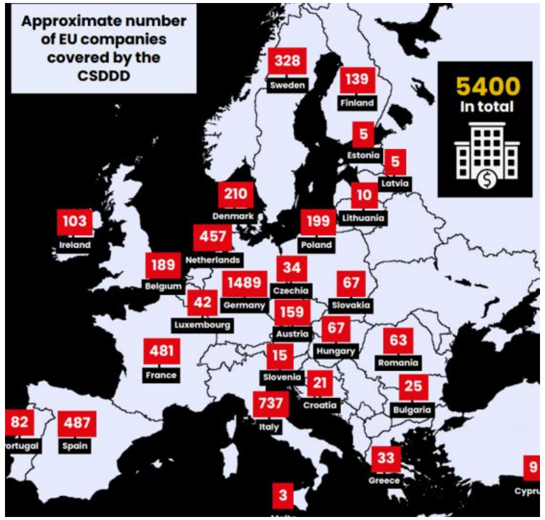
The Looming Reach of EU Sustainability Due Diligence

As global trade becomes increasingly intertwined with environmental and social governance (ESG) imperatives, regulatory frameworks are evolving to ensure that companies act responsibly, not just individually but across their entire value chain. One such development is the European Union's Corporate Sustainability Due Diligence Directive (CSDDD), which introduces binding rules for companies to identify, prevent, mitigate, and account for adverse impacts on human rights and the environment, both within their operations and through their supply chains. CSDDD has been in effect since 25 July 2024, and the EU member states must transpose the Directive into national law by 26 July 2026.

The CSDDD is based on the idea that corporate responsibility extends beyond financial performance. It requires companies to embed sustainability in their core decision-making and to demonstrate accountability for their value chains. This includes identifying risks such as child labour, unsafe working conditions, deforestation, biodiversity loss, and pollution. The directive complements the EU's Green Deal and aligns with international standards such as the UN Guiding Principles on Business and Human Rights and the OECD Guidelines for Multinational Enterprises. The benefits of the directive, though demanding, are significant. For the EU, it ensures that companies operating within its borders contribute to sustainable development goals and uphold ethical business practices globally. For suppliers and business partners outside the EU, including those in Sri Lanka, it presents an opportunity to align with global sustainability benchmarks, strengthen competitiveness, and enhance their appeal to ESG-conscious investors and consumers. In the long term, this can build resilience, improve risk management, and open preferential access to sustainable finance and procurement opportunities.

Under the new rules, companies will have specific obligations. These include conducting due diligence to identify and assess actual or potential adverse impacts, taking appropriate measures to prevent or mitigate them, establishing grievance mechanisms, and publishing annual reports on due diligence practices. Importantly, companies will be held liable for harms that result from non-compliance if reasonable due diligence could have prevented them. Enforcement will involve supervisory authorities in each member state, with sanctions including fines of up to 5% of global turnover and public naming. The CSDDD will apply to EU-based companies with more than 1,000 employees and a global turnover exceeding €450 million, as well as to non-EU companies meeting the same revenue threshold from operations within the EU. This marks a revision from the original proposal, which had lower thresholds, but it still casts a wide net over global supply chains. While the directive primarily targets large firms, its reach extends to thousands of suppliers, subcontractors, and service providers, including many in developing and middle-income countries such as Sri Lanka.

For Sri Lankan businesses, particularly those in sectors such as apparel, tea, rubber, ICT, and manufacturing, the implications are profound as they export to or are linked with European markets. This marks a pivotal moment to assess readiness, risk exposure, and long-term strategy. The apparel industry, which accounts for over 40% of Sri Lanka's export earnings and is heavily dependent on EU markets, is particularly exposed. Apparel industry leaders have already called for urgent, collective action to prepare for the upcoming requirements. This includes strengthening traceability, improving environmental and social compliance, and adopting digital tools for transparency. SMEs within these supply chains may face the greatest challenge.



While they are not directly covered by the EU rules, they will be expected to demonstrate compliance by the European buyers they supply. This includes maintaining documentation, conducting risk assessments, and responding to audits that can be resource-intensive for smaller firms without robust ESG systems. The risk is that non-compliance, or even the perception of weak due diligence, could lead to order cancellations, reputational damage, or exclusion from EU supply chains.

However, with risk comes opportunity. For Sri Lanka, aligning with the CSDDD can enhance its profile as a responsible sourcing destination at a time when buyers are re-evaluating global supply chains for resilience and ethical standards. The country's reputation for high labour standards, relatively low carbon intensity in the power mix, and an established social compliance framework provide a strong foundation to build on. Initiatives such as Higg Index adoption, OEKO-TEX certification, and ethical labour practices can serve as steppingstones.

Data Sources: European Commision, Climate Action Network, Daily FT

EIU

Economic Intelligence Unit of The Ceylon Chamber of Commerce

The Ceylon Chamber of Commerce

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