

Pre-Policy Analysis

25TH SEPTEMBER 2017

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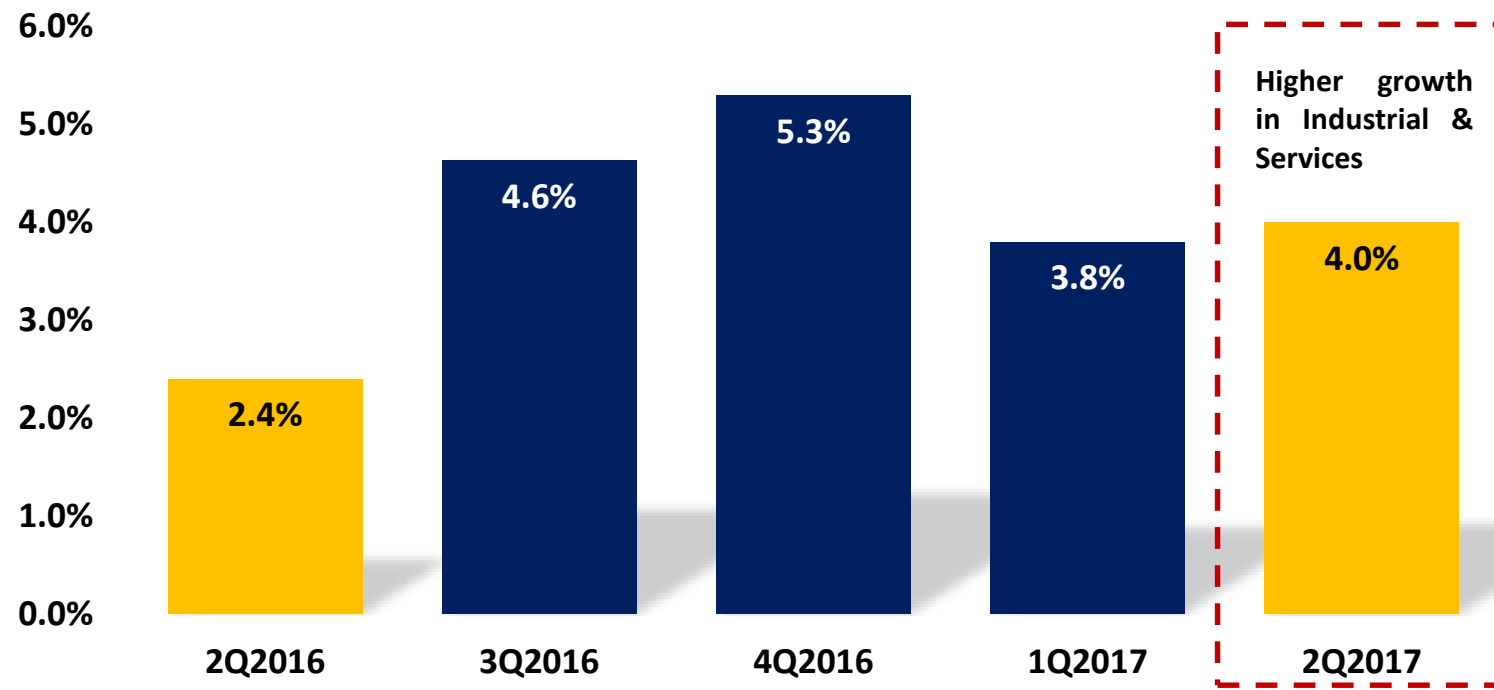
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GDP Growth

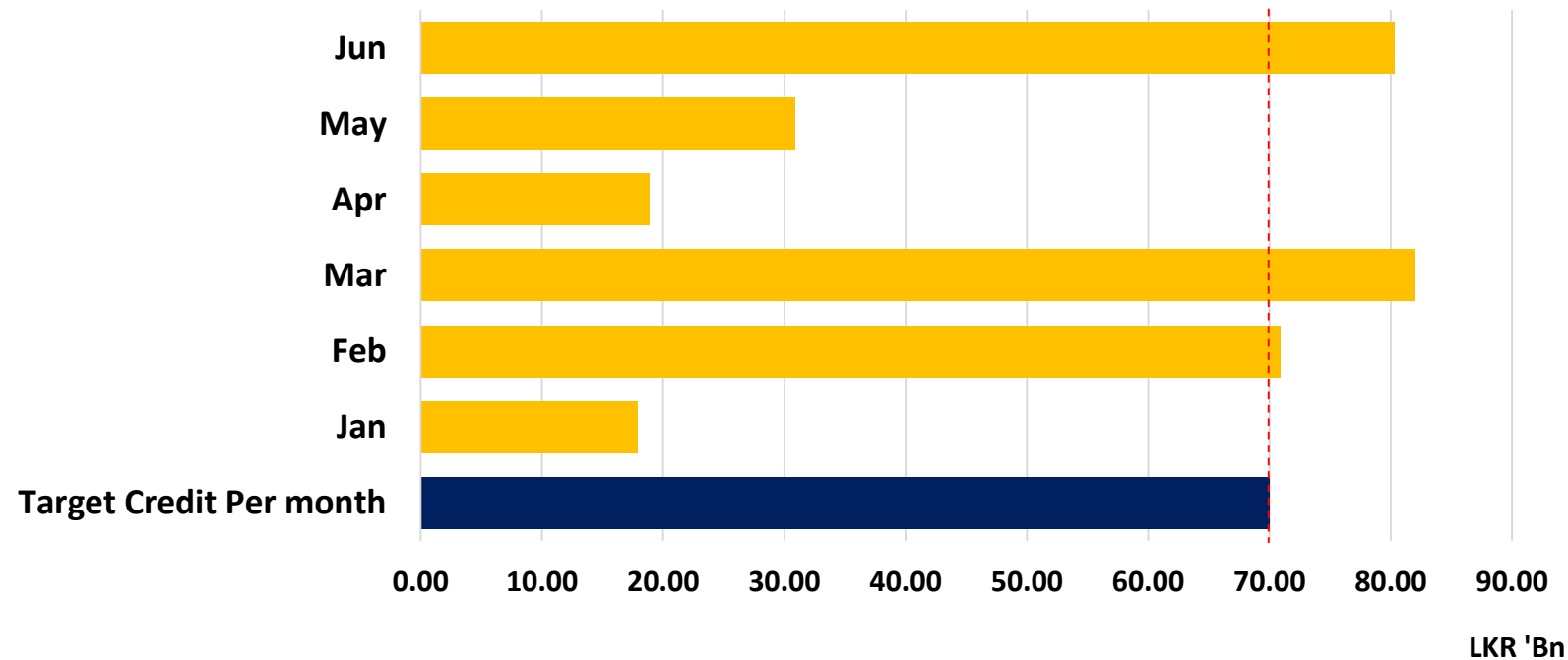
GDP growth for 2Q 2017 was better than expected, grew by 4.0%YoY in the 2Q2017 with the industrial and the services activities recorded higher growth rates of 5.2%YoY and 4.5%YoY respectively.



Source: CBSL

CREDIT GROWTH

FC Research upgrades private sector credit growth for 2017E to 16% from 14% amidst a possible pickup towards year end. In spite of a high private sector credit figure in June 2017 we believe overall credit is likely to continue to remain under check.



INFLATION

CCPI based headline inflation, accelerated on a YOY basis to 6.0% in Aug 2017 from 4.8% in Jul 2017, and CCPI based core inflation also accelerated to 5.0% in Aug 2017 from 4.9% in Jul 2017.

NCPI based inflation also decelerated on a YOY basis to 8.4% in April 2017 from 8.6% in March 2017.

FC Research forecast Sep 2017 CCPI headline inflation to be at 6.3% and CCPI core inflation at 6.5%

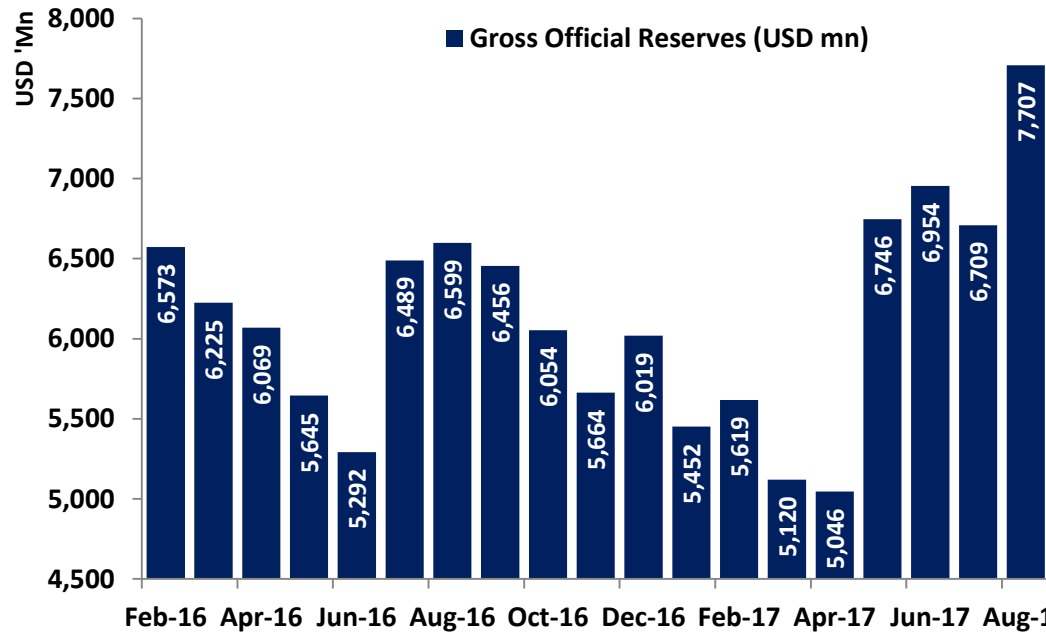
FC Research View

We believe inflation will be upward pressure toward October and beyond with the floods in May 2017 affecting the supply in the current growing season. As a result there could be possible supply side shortages towards October and beyond but may continue to remain around the 6.0% mark throughout the year.

Official Reserves

Sri Lanka's forex reserves rose to USD 7.7Bn in Aug 2017 from USD 6.7Bn in July, helped by USD 550Mn syndicated loan and dollar purchases by the CBSL. The CBSL had net purchased USD 975Mn from currency markets so far this year.

FC Research View: FC Research believe Foreign Reserves are now at comfortable levels



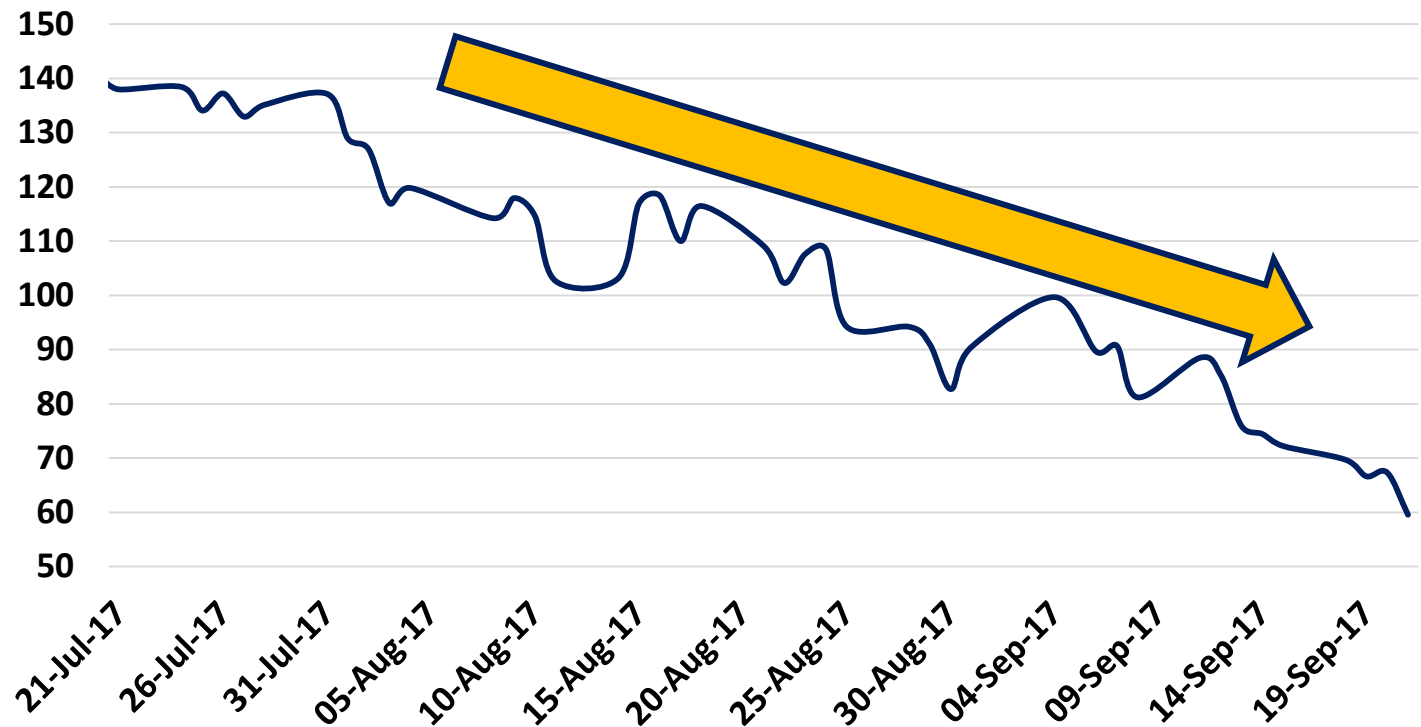
Source: CBSL

Central Bank purchases and sales (USD Mn)

	Purchase	Sales
Jan-17	64.66	204.50
Feb-17	145.09	297.25
Mar-17	192.23	13.00
Apr-17	257.92	-
May-17	183.47	35.00
Jun-17	136.00	-
Jul-17	344.75	-
Aug-17	200.00	-

CBSL HOLDINGS

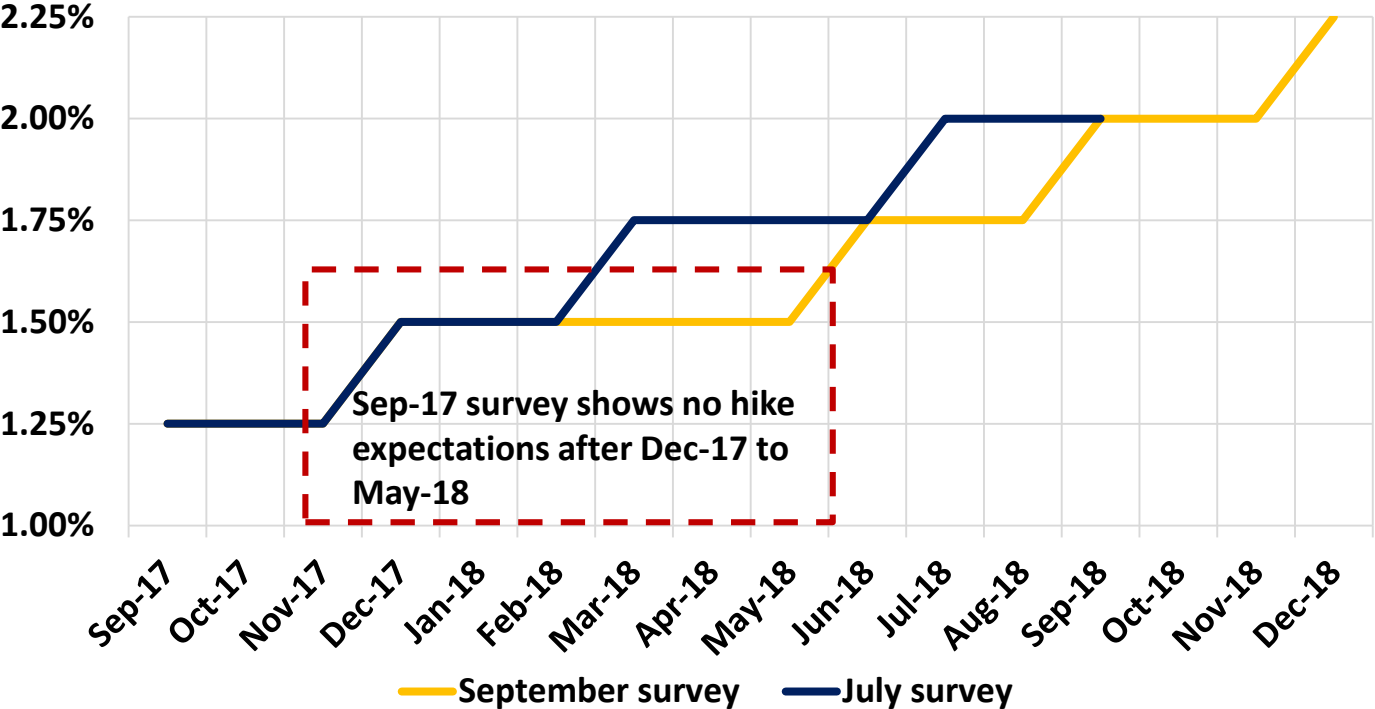
During last two months CBSL bought down its holding in Government Securities from LKR 138Bn to below LKR60Bn as at 21st Sep 2017.



Source: CBSL

Fed Rate Hike Expectations

Economists said the Fed will still pencil in three hikes for 2018, but with the first of those not projected until June, versus March in the Fed's previous set of forecasts. Sep-17 survey shows Fed expects to raise policy rates in Dec-17 and no further hikes are expected after Dec-17 until after May-18.



Source: Bloomberg surveys

Expected Monetary Policy Stance

FC Research believes that considering the current economic conditions with better than expected GDP growth level and the considerable improvement in the Economic Health the **current monetary policy is appropriate and no change is required**

Expected Monetary Policy Stance by CBSL	Probability	Current Policy Rates	
Raising Policy Rates by 50bps	0%	Standing Deposit Facility Rate (SDFR)	7.25%
Raising Policy Rates by 25bps	10%	Standing Lending Facility Rate (SLFR)	8.75%
Policy Rates to remain unchanged	90%	Statutory Reserve Ratio (SRR)	7.50%
Cutting Policy Rates by 25bps	0%		
Cutting Policy Rates by 50bps	0%		

We expect the CBSL to keep Statutory Reserve Ratio (SRR) unchanged at 7.50%

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