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இலங்கை மத்திய வங்கி
CENTRAL BANK OF SRI LANKA

CENTRAL BANK'S **POLICY AGENDA** for 2025 and Beyond



STABILITY FOR PROSPERITY
1950-2025

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Preamble

*Sri Lanka has made a significant recovery after enduring its worst economic crisis in history. Macroeconomic stability that was restored through decisive policy action and collective resolve has laid the foundation for a stronger, more resilient economy. Leveraging on the stability achieved, the country is making notable progress by continuing with the economic reform agenda, strengthening its economic buffers, institutions and governance, and building overall resilience for potential headwinds. Significant progress was made on the fronts of debt restructuring as well as the Extended Fund Facility (EFF) arrangement with the International Monetary Fund (IMF). Faster-than-expected recovery in domestic economic activity was supported by renewed business and consumer confidence. General price levels have adjusted down following a period of high inflation, enabling the continuation of the eased monetary policy stance. External buffers have been built, supported by improved foreign exchange inflows amidst the flexible exchange rate regime. A notable improvement in the fiscal sector performance was witnessed along with efforts to enhance support extended to the poor and vulnerable. Financial system stability was reinforced through the strengthening of the regulatory framework and improved risk management and monitoring. These achievements are outcomes of the continued commitment and perseverance and the sacrifices made by all stakeholders of the economy, including the general public, in pursuing the economic reform agenda. More importantly, these measures have helped restore investor confidence and set the platform for the long-term transformation of the economy. While broad-based stability has been achieved, the focus, going forward, would be on fostering sustained growth, which requires driving innovation, enhancing productivity, maintaining a strong commitment to implementing structural reforms, and encouraging greater stakeholder collaboration without compromising hard-earned stability. The Central Bank, in keeping with its mandate as stipulated in the Central Bank of Sri Lanka Act, will commit to maintaining domestic price stability and securing financial system stability, thereby playing a leading role in creating an enabling environment for all stakeholders of the economy to thrive. As the Central Bank celebrates its 75th anniversary, the focus and efforts will be increasingly directed towards maintaining **STABILITY FOR PROSPERITY**.*

1. Economic and Financial Sector Performance in 2024

During 2024, the Sri Lankan economy achieved significant strides in restoring macroeconomic stability and maintaining the stability of its financial system. The Extended Fund Facility arrangement with the International Monetary Fund (IMF-EFF) continued, supporting the stabilisation of economic conditions. While marking a major milestone in the country's journey of economic recovery, **the Government completed its debt restructuring process successfully, except for a small portion, by end 2024,** paving the way for the normalisation of relations with creditors and external partners. Following these developments, **the sovereign rating of the country was upgraded** by two leading rating agencies, thereby notably reducing the country's risk premium.

Inflation declined steadily throughout 2024 and eventually reached deflationary levels towards the latter part of the year. There was a temporary acceleration in headline inflation in early 2024 due to the increase in Value Added Tax (VAT) and the removal of VAT exemptions from several items in the consumer basket. However, inflation decelerated thereafter, reaching levels below the target of 5%, driven by the higher-than-predicted downward revisions to the energy prices, stronger currency as well as the decline in food prices. Consequently, in September 2024, headline inflation reached deflationary levels for the first time in nine years. Meanwhile, core inflation, which mainly reflects the demand pressures in the economy, also reached lower positive levels.

With the notable deceleration of headline inflation and subsequent deflation, the inflation target was breached from the lower margin for two consecutive quarters in the second and third quarters of 2024. Such inflation target-miss continued in the final quarter of 2024 as well. Accordingly, as agreed under the Monetary Policy Framework Agreement (MPFA), the Central Bank submitted a report to the Hon. Minister of Finance to be submitted to the Parliament. The report includes the reasons for the deviation of inflation from the target, the remedial actions taken, and an estimate of the time period within which the inflation target could be achieved. This report will also be made available to the public,

marking a significant milestone in further enhancing the Central Bank's accountability to the Parliament and the general public.

Continuing the recovery observed since the second half of 2023, the Sri Lankan economy rebounded strongly in 2024, initially benefiting from the base effect, but also supported by accommodative monetary policy and a low-inflation environment. During the first three quarters of 2024, the economy is estimated to have grown notably by 5.2% with key economic sectors recording expansions. Building on the momentum in economic activity, leading economic indicators of industry and service sectors reflect a continuation of the expansion in output in the last quarter of 2024 as well. Accordingly, real GDP is projected to have grown by around 5.0% in 2024, registering the highest annual growth since 2017. This higher-than-expected growth also provides evidence that deflation in recent months was not due to demand factors but mainly due to supply-side factors, including administrative price adjustments.

Supported by the benign inflation environment and gradual restoration of macroeconomic stability, monetary policy of the Central Bank was increasingly accommodative throughout the year 2024. Accordingly, the Central Bank eased monetary policy on three occasions during the year, effecting considerable downward adjustments in market interest rates, thereby enabling a greater transmission of such policy easing to the broader economy. Domestic money market liquidity remained broadly at surplus levels during 2024, and short-term money market rates were maintained in line with the monetary policy stance supported by well-calibrated market operations. The low interest rate environment, coupled with adequate levels of market liquidity, supported the economy to progress through its recovery phase. Accordingly, these enabling conditions encouraged consumer spending and promoted investments that laid the basis for the economic recovery.

2024 had been crucial for monetary policymaking as the Central Bank shifted to a single policy interest rate mechanism from its dual policy interest rate system. As announced in the Annual Policy Statement for 2024, the Central Bank introduced

the “**Overnight Policy Rate (OPR)**” as the **primary tool of monetary policy** in November 2024, which signals the monetary policy stance of the Central Bank.

Supported by the eased monetary conditions, credit extended to the private sector expanded notably in 2024, while credit obtained by the public sector contracted, freeing up financial resources for private-sector investment.

The Central Bank facilitated the increased demand for currency by providing adequate currency notes and coins to the banking system. This ensured that transactions could be carried out unhindered amidst the recovery in domestic economic activity. During 2024, the public adoption of digital payments also continued to increase rapidly. Further, customers' payments to government institutions through online payment platforms have also recorded a notable expansion in 2024.

The external sector continued its positive momentum in 2024 building on renewed resilience in the sector. The Balance of Payments position strengthened, and the current account is estimated to have recorded a surplus in 2024 as well, a record of two consecutive years of surpluses in Sri Lanka’s recent history. Remarkably, the Central Bank purchased the **highest-ever annual amount of foreign exchange from the domestic foreign exchange market in 2024, exceeding US dollars 2.8 billion (net).** Gross official reserves increased to around **US dollars 6.1 billion by the end of 2024** compared to US dollars 4.4 billion at end 2023. As mandated by the Central Bank Act, the flexible exchange rate policy was continued in 2024, complementing the Flexible Inflation Targeting (FIT) framework. The Sri Lanka rupee recorded an appreciation and demonstrated greater stability in 2024 as well, driven by net forex inflows and improved market sentiments.

The financial system remained resilient and showed greater stability in 2024. With the gradual dissipation of spillover effects of the economic crisis on the financial sector, the soundness of the banking sector improved during the year. Gross loans and receivables (credit) of the banking sector continued to grow, while the default risk of the sector declined during the year as reflected by the reduction in the non-performing loan (NPL) ratio. Further, the Liquidity Coverage Ratios

(LCRs) of the sector remained well above the minimum regulatory requirements. During 2024, the Return on Equity (ROE) of the banking sector also improved considerably. The Capital Adequacy Ratio (CAR) of the banking sector improved during 2024 reflecting the higher growth recorded in regulatory capital than the Risk Weighted Assets. Meanwhile, the Finance Companies sector also recorded a steep recovery in total loans and advances, while profitability indicators improved in 2024. Financial markets operated with low stress as macrofinancial conditions and the confidence of market participants continued to improve.

The Central Bank continued to strengthen the regulatory framework of the financial sector with a view to ensuring the safety and soundness of financial institutions. The legal and regulatory framework of Licensed Banks was strengthened through **the Banking (Amendment) Act** and the issuing of necessary Directions to licensed banks to facilitate the effective implementation of the amendments. Accordingly, Banking Act Directions on, *inter alia*, large exposure, corporate governance, liquidity ratios, related party transactions, and offshore banking business were issued to Licensed Banks. Further, the Central Bank developed the **Bank Recapitalisation Strategy** in line with the roadmap for the restructuring and recapitalisation of nine large domestic banks with a view to strengthening financial system stability through an adequately capitalised banking system. **Depositor-wise Data Collection System** was also initiated to cover all Licensed Banks and Licensed Finance Companies (LFCs) to enhance the effectiveness and efficiency of the compensation payment mechanism under the Sri Lanka Deposit Insurance Scheme (SLDIS), ensuring accurate, timely and streamlined management of depositor information.

The Central Bank achieved significant milestones in 2024 in strengthening the resolution framework under the Banking (Special Provisions) Act (BSPA). These achievements spanned key areas, such as resolution policy formulation, issuing a Direction to licensed banks on data templates for resolution planning, resolution trigger establishment for licensed banks and operationalisation of the **Financial**

Stability Fund (FSF). In October 2024, FSF was established with an initial allocation of Rs. 500 million by the Government.

Meanwhile, regulations on financial consumer protection were fully operationalised effective August 2024, marking a significant milestone in the Central Bank's efforts to enhance financial consumer protection. During 2024, the responsibilities to handle prohibited financial schemes related cases were transferred to a dedicated department, with full operationalisation of financial consumer protection regulations.

During the year, the restrictions on investments made outside Sri Lanka by resident Sri Lankans and capital transfers by emigrants were significantly relaxed. These restrictions were in place since 2020. Similarly, the rules relating to the repatriation of export proceeds to Sri Lanka and their conversion into Sri Lanka rupees were relaxed.

The Central Bank continued to enhance the national payment infrastructure further by way of integrating into regional and country payment networks during 2024. Further, with a view to ensuring that Sri Lanka's payment infrastructure is compliant with international standards, the ISO 20022 implementation project completed its first phase in 2024 by introducing a new Real Time Gross Settlement (RTGS) System. In addition, the Central Bank played an active role in developing the government digital payment platform (GDPP), which is an initiative aimed at improving citizen-government interactions and streamlining payment processes for various government services in Sri Lanka.

Aimed at restoring fiscal sustainability, fiscal sector performance continued to improve in 2024 supported by consolidation measures in line with the IMF-EFF arrangement. These policy reforms have been reflected in government finances in 2024, with a notable increase in tax revenue collection and broad-based improvements in key fiscal indicators, including achieving a sizeable primary surplus. Additionally, the continuation of structural reforms, including cost-reflective pricing mechanisms for major utilities, have largely supported reducing the burden of state-owned business enterprises on the fiscal balances and the

banking sector. Improved fiscal performance along with reduced risk premia in an environment of declining market interest rates helped notably reduce yields on government securities, thereby reducing the interest cost to the Government. Further, fiscal consolidation measures complemented the Central Bank's efforts to ease monetary policy, which highlights the importance of fiscal prudence for monetary policymaking.

Policies for 2025 and Beyond

2. Policies Supporting Price Stability

Key Highlights

- *Monetary policy focus to be on maintaining inflation around 5% while ensuring that the economy remains on track towards achieving sustained growth*
- *Inflation to return to positive territory toward mid-2025*
- *Expansionary momentum of private sector credit to continue, supporting economic activity*
- *Excessive loan interest rates on selected products are to be reduced in collaboration with financial institutions*
- *Need for introducing innovative solutions to promote savings*
- *Further improvements to forward-looking and data-driven monetary policy formulation are envisaged*
- *Monetary policy operations to be carried out to steer the short-term market interest rates in line with OPR*
- *The liquidity forecasting framework is to be enhanced*
- *The SRR framework will be optimised*
- *An OMO auction schedule to be announced*
- *Efforts to rebuild external buffers to continue*
- *A benchmark spot exchange rate to be introduced to guide markets and the public*
- *Communication strategy to be focused on reaching the grassroots level*

With normalcy being restored and stability attained through the implementation of much-needed sound macroeconomic policies, including monetary policy, the Central Bank's focus going forward will be **on stabilising inflation around the target of 5%**, consistent with the FIT framework, while ensuring that the economy remains on track towards achieving sustained growth over the medium term, thereby ensuring the prosperity of the nation.

The deflationary environment resulting from the one-off effects of supply-side price adjustments will continue in early 2025 as per the current projections of the Central Bank. However, inflation is projected to converge to the target during the latter half of the year with the dissipation of the effects of such supply-side factors and accommodative conditions created by relaxed monetary policy. Until then, the Central Bank will continue to submit comprehensive reports to the Parliament as required under the Central Bank of Sri Lanka Act (CBA), providing reasoning for missing the inflation target, despite it being on the downside, **with the aim of ensuring transparency and accountability of the actions of the Central Bank.** Following the high inflation episode from late 2021 to early 2023, it is believed that this temporary period of deflation would provide some respite to the general public by dampening the cost of living to some extent.

The broad-based recovery of credit to the private sector observed in 2024 is expected to continue in the period ahead as well, supported by the prevailing accommodative monetary policy stance and improving business and investor sentiment. This is expected to enhance the productive capacity of the economy, thereby supporting domestic economic expansion. That said, the Central Bank will continue to closely monitor developments in credit and related dynamics to ensure the timely identification and mitigation of potential risks and vulnerabilities in maintaining domestic price stability. Timely monetary policy intervention will prevent excessive swings in interest rates, setting the platform for the economy to navigate through challenging economic circumstances, while facilitating the economy to reach its potential.

The recovery in credit to the private sector has been supported by the noteworthy reduction in market lending interest rates. However, the Central Bank observes some excessive, outlier rates of interest on facilities extended to Micro, Small and Medium Scale Enterprises (MSMEs) as well as marginal borrowers and certain credit products, which are not consistent with the prevailing relaxed monetary policy stance. Moreover, risks associated with lending are on the decline while the credit appetite of banks and financial institutions is improving given the overall

stability and recovery witnessed in the economy. Therefore, with a view to making low interest rate credit accessible, the Central Bank will closely work with banks and other financial institutions **to reduce the excessive interest rates still prevalent in the market.**

While low interest rates have helped revive credit and contributed to improving the overall business sentiment, they could also disproportionately hurt savers. However, unlike during the high inflation episode, real returns on deposits have been positive, with inflation successfully being reined into low levels. Interest rates have their cycles, and the Central Bank will manoeuvre interest rates to ensure that inflation is kept low and stable with a view to promoting overall public welfare. Amidst these developments, to ensure that domestic savings are promoted in a low interest rate environment, **the financial industry is encouraged to introduce innovative solutions and products to promote savings in the context of the rapidly ageing population,** while also embedding elements of liquidity and safety to compensate for interest rate volatilities during business cycles. Moreover, the culture of saving at an earlier stage of life should be nurtured, which will not only promote long-term savings but will also ensure greater financial security for a better life after retirement.

The Central Bank follows a forward-looking, data-driven approach to monetary policy formulation, which is an integral feature of policymaking under the FIT framework. **Continuous efforts will be made to improve existing models used to generate macroeconomic forecasts, while the evaluation of alternative models and frameworks to complement the same will continue in parallel.** Additionally, **enhancing policy research and nurturing a strong research culture within the institution will remain key priorities.** These efforts on improving technical capacity are expected to better support the monetary policy decision-making process via high quality analyses and, better data collection and forecasting capabilities aided by modern technology. Moreover, the Central Bank will broaden its spectrum of data used for policy analysis by **exploring new sources of high-**

frequency data to enhance short-term forecasting, while the coverage of the surveys conducted by the Central Bank will be further improved.

2.1. Implementation of Monetary Policy

Monetary policy operations will be carried out with the aim of steering the short-term market interest rates in line with the Central Bank's monetary policy stance as announced through the Overnight Policy Rate (OPR). As already witnessed, with the introduction of the OPR under the single policy interest rate mechanism and simultaneous monetary policy easing, the short-term market interest rates, particularly the Average Weighted Call Money Rate (AWCMR), remained well aligned with the OPR. Several further measures have been planned for 2025 to enhance the effectiveness of monetary policy implementation.

The Central Bank will continue to manage liquidity in the domestic money market to steer the short-term interest rates in line with its monetary policy stance. Domestic money market liquidity is likely to increase gradually in 2025 with the expected buildup of foreign reserves, and **the Central Bank will stand ready to manage liquidity, through appropriate monetary operations**. Meanwhile, the Central Bank will explore ways to gradually phase out its holding of restructured bonds, a legacy of the Central Bank's financial support to the Government during the crisis.

The Central Bank is in the process of reviewing the current Statutory Reserve Requirement (SRR) Framework in line with the FIT framework and international best practices. Required changes will be implemented following stakeholder consultations to optimise the SRR framework for the benefit of effective monetary policy implementation and the overall financial system.

Further, the Central Bank plans **to transition to a more market-friendly system for Open Market Operations (OMOs) in 2025**, with a view to effectively implementing the monetary policy under the single policy interest rate mechanism and to adapt to evolving domestic and global developments. Accordingly, **an OMO auction schedule is expected to be announced this year** to create certainty on liquidity management among market participants. In addition, the Central

Bank will **enhance the liquidity forecasting framework and explore alternative approaches to manage money market liquidity in line with the Flexible Inflation Targeting framework.**

Further, during 2025, the Central Bank expects to **review and streamline the eligible counterparties of monetary policy operations** for the purpose of improving the effectiveness of OMOs and Standing Facilities.

Additionally, in keeping with the statutory requirement and the past practice, the following **monetary policy advance release calendar** for the year 2025 is hereby published.

Monetary Policy Advance Release Calendar - 2025

CYCLE NO.	MONETARY POLICY BOARD MEETING	MONETARY POLICY ANNOUNCEMENT
1	28 January	29 January <i>Monetary Policy Report - 15 February</i>
2	25 March	26 March
3	27 May	28 May
4	22 July	23 July <i>Monetary Policy Report - 15 August</i>
5	23 September	24 September
6	25 November	26 November

2.2. Maintaining External Sector Stability

The near completion of the Government's external debt restructuring, coupled with the significant progress made under the IMF-EFF programme, has created a solid foundation for boosting investor confidence and ensuring the stability of the external sector. In this regard, the Central Bank will closely observe the developments and risks on the external front to advocate appropriate policies promptly.

Sri Lanka has been able to record a current account surplus continuously for two years, in 2023 and 2024. However, as economic activity picks up, the external current account is likely to record a deficit in 2025. Sri Lanka needs to **maintain the external current account at sustainable levels over the medium term**. A gradual recovery in import expenditure is expected, particularly in the context of the planned relaxation of vehicle import restrictions in 2025 by the Government. Furthermore, the external current account will be supported by inflows from the services trade and workers' remittances, which together are expected to reach historically high levels.

The journey towards ensuring long-term stability in the external sector will be essentially built upon the **ongoing IMF-EFF programme** to ensure the implementation of reforms and promote overall macroeconomic stability. The Central Bank will continue to strive towards the key commitment of **rebuilding external buffers** under the programme by purchasing forex from the foreign exchange market. Such buildup of external buffers needs to be facilitated by sufficient foreign exchange inflows to the country by way of enhanced earnings from merchandise and services exports, workers' remittances, and foreign direct investment. Further, with the objective of expanding reserve management activities, the Central Bank intends to capitalise market opportunities through various diversification strategies across the markets, such as **establishing a new investment tranche with advanced portfolio management strategies**. Due attention will be given to strengthening risk mitigating aspects to ensure the safety of invested foreign reserves.

Aligning with its mandate, the Central Bank is committed to **maintaining a market-determined and flexible exchange rate to serve as a buffer against external shocks**, with interventions aimed at building up reserves and mitigating excessive volatility in the exchange rate. The Central Bank strives to foster a deeper, transparent and more liquid foreign exchange market and develop adequate systems for managing exchange rate risks, which includes the introduction of a **benchmark spot exchange rate as a reflective rate to guide participants in the domestic foreign exchange markets as well as the general public**.

The Central Bank successfully operationalised the **International Transactions Reporting System (ITRS)** in 2023 and started publishing monthly statistics on trade in services, based on ITRS data from January 2024. This would enhance the accuracy and coverage of external sector statistics, thereby facilitating policy formulation to harness the potential of the country. The Central Bank plans to use ITRS to improve the data quality and coverage of the financial account of the BOP, facilitating policy analysis and planning related to foreign exchange flows.

3. Policies Aimed at Financial System Stability

Key Highlights

- *Exercise regulatory oversight on bank recapitalisation strategy to ensure compliance with minimum capital requirements for all banks*
- *A framework for market-driven consolidation of licensed banks to ensure strong and resilient banks with adequate capital*
- *Further strengthening the regulatory framework under the Banking (Amendment) Act*
- *Coordinate with Colombo Port City Economic Commission to facilitate the conduct of offshore banking business*
- *Implementing phase II of the Masterplan for the Consolidation of Finance Companies*
- *Introducing amendments to Finance Business Act and Finance Leasing Act*
- *Announcements of capital buffers of Domestic Systemically Important Banks and identifying Systemically Important Finance Companies*
- *Launching the Sustainable Finance Roadmap for Sri Lanka - Version 2.0*
- *Strengthen oversight of banking sector credit through the use of appropriate macroprudential tools*
- *Revision of the Payment and Settlement Systems Act along with several subsidiary legislations*
- *Operationalise the Government Digital Payment Platform (GDPP)*
- *Broadening the market conduct supervision in compliance with Financial Consumer Protection Regulations*
- *Display key financial information enabling consumers to make informed decisions*

3.1. Banking Sector Policies

With a view to securing financial system stability and strengthening the operational resilience of the banking sector, the Central Bank expects to implement an array of policy measures spanning from the near term to medium term. In line with the roadmap for the restructuring and recapitalisation of nine large domestic

banks, the **Central Bank has developed the Bank Recapitalisation Strategy** to strengthen the financial system stability through an adequately capitalised banking system. Under this strategy, these banks have submitted Board-approved recapitalisation plans and the progress of the implementation of these plans would be monitored semi-annually, with **ongoing oversight to ensure compliance with minimum capital requirements for all banks**. Further, to ensure that the financial system comprises strong and resilient banks with adequate capital, a framework for **market-driven consolidation of licensed banks** is to be established and consolidation is expected to be facilitated on a case-by-case basis.

The implementation of the Directions issued under **the Banking (Amendment) Act** covering areas such as large exposures, corporate governance, liquidity ratios, related party transactions, and offshore banking business will be monitored in 2025. Existing regulations will also be reviewed in line with **market developments and international best practices** to ensure the regulatory framework is further strengthened.

The Central Bank, with the coordination of the Colombo Port City Economic Commission will **facilitate the conduct of offshore banking business** through required regulatory and supervisory functions.

Further, resilience of the financial system would also be strengthened through **enhanced crisis management and resolution measures**. The Central Bank would continue to coordinate and assist the functioning of the Financial Sector Crisis Management Committee on an ongoing basis. The effectiveness of risk-based supervision would be enhanced by improving the supervisory infrastructure and the continuous surveillance of banks will be intensified.

The Central Bank would further **strengthen the conduct of risk-based Anti-Money Laundering (AML) and Countering the Financing of Terrorism (CFT) examinations of banks** in terms of the Financial Transactions Reporting Act (FTRA) and the recommendations of the Financial Action Task Force (FATF).

3.2. Non-Bank Financial Institutions Sector Policies

The Central Bank remains committed to safeguarding the non-bank financial institutions sector by **strengthening the regulatory environment** alongside the **implementation of the Masterplan for the Consolidation of Finance Companies**, which was initially announced in 2020. The Masterplan aims to create a strong and stable non-bank financial institutions sector and consists of two phases. **Under Phase I, eight amalgamation transactions were successfully completed.**

The revised **Phase II of the Masterplan was announced in December 2024**, with an execution period spanning three years, from March 2025 to March 2028. **Phase II of the Masterplan focuses on enhancing the resilience of finance companies that intend to continue on a stand-alone basis.** The progress of these finance companies in meeting the benchmarks established under Phase II would be monitored to ensure successful implementation.

To strengthen regulatory oversight, enhance risk management, and promote the stability of the non-bank financial institutions sector, **amendments would be made to the Finance Business Act, No. 42 of 2011, and Finance Leasing Act, No. 56 of 2000** in line with the developments in the non-bank financial institutions sector. To broaden the regulatory framework and thereby improve the risk management and stability of the sector, rules and regulations are to be issued. In addition, automation would be embraced to improve the effectiveness of the supervisory process, while enhancing public disclosures to raise awareness of the performance of finance companies.

3.3. Macroprudential Policies

The Central Bank, as the macroprudential authority of Sri Lanka, published the macroprudential policy framework as a step towards ensuring financial system stability, through enhanced communication on the Bank's macroprudential approach.

The Central Bank is strengthening its macroprudential approach through enhanced systemic risk surveillance. In this regard, stress testing and analysis frameworks were further improved to better estimate the sensitivity to various

macro-financial stress scenarios, thus strengthening the monitoring of developments and risks in the financial system. **The Central Bank envisages extending its stress testing frameworks to the Finance Companies Sector in 2025.**

Furthermore, the **reassessment of Domestic Systemically Important Banks (DSIBs)** with the required capital buffers has been completed. The announcement of the DSIBs, along with corresponding DSIB capital buffers is expected in 2025. Moving forward, the Central Bank will focus on **identifying Systemically Important Finance Companies** to strengthen financial sector resilience and oversight.

A targeted policy approach through the use of appropriate macroprudential tools will strengthen oversight of banking sector credit. This will improve risk management among lending institutions and ensure financial system stability.

As the macroprudential authority of the country, the Central Bank **extends its macroprudential approach to financial sector participants outside the bank's regulatory purview through the Financial System Oversight Committee (FSOC)**, which brings all financial sector regulators under one umbrella.

The Central Bank has taken a wide range of policy measures to ensure financial stability, and further policies are underway covering multiple aspects of the financial system. As the economy recovers and the credit cycle moves into the expansionary phase, vulnerabilities may arise due to increased risk-taking and heightened exuberance. As such, the Central Bank will diligently monitor systemic risks and promptly implement appropriate macroprudential and microprudential policy measures to address any emerging risks to ensure continued financial system stability.

3.4. Initiatives under Sustainable Finance

As an important initiative, **the Sustainable Finance Roadmap for Sri Lanka - Version 2.0** is to be launched in 2025 in line with evolving global and domestic conditions and to be operationalised with a view to providing a timely guide for the expansion in sustainable finance activities in the country. To support the implementation of the Roadmap, the Central Bank would continue **capacity-building activities**, including programmes on the **Sri Lanka Green Finance Taxonomy**, to equip stakeholders with

the necessary knowledge and tools to integrate sustainable practices in line with the Roadmap. The existing regulatory framework for sustainable financing activities would also be reviewed based on the updated Basel Core Principles, with necessary actions taken to address any identified gaps.

3.5. Payment and Settlement Systems

Maintaining a stable and efficient payment system is pivotal in ensuring a sound financial system. **In this regard, initiatives are planned to improve relevant legislation and payment infrastructure, and increase public trust in digital payments.** As digital payments grow faster, the Central Bank has initiated a multipronged three-year comprehensive plan to enhance the legal and institutional structure of the payments landscape. This approach begins with enhancing the legal framework that governs the oversight, supervision and regulation of payment and settlement systems as well as facilitating payment innovations and development of the digital payments market in Sri Lanka. Accordingly, the Central Bank is in the process of **revising the Payment and Settlement Systems Act.** Several subsidiary legislations such as the Guidelines on Minimum Compliance Standard for Payment related Mobile Applications, will be revised in 2025 to facilitate the rapid expansion of retail digital payments.

The Central Bank launched a new **Real-Time Gross Settlement (RTGS) system in 2024, fully compliant with ISO 20022 standards for domestic payment transactions.** The Bank plans to extend this standard to all cross-border transactions, aligning with international timelines.

The Common Electronic Fund Transfer Switch (CEFTS) would be further extended to reach more points of access, especially targeting government payments. In 2025, **the Government Digital Payment Platform (GDPP),** which enables government institutions without digitalised databases to receive real-time payments from the public through internet banking portals/mobile payment apps will be operationalised, following successful pilot testing in 2024.

Further, the Central Bank aims to **review the access regime to interbank payment systems as well as the licensing regime for payment services. The Merchant Discount Rate (MDR) for LANKAQR was restored to 1%, up from 0.5% from 1 January 2025,** encouraging financial institutions and FinTechs to promote adoption actively.

Moreover, recognising the vulnerabilities associated with digital payments, the Central Bank is committed to **safeguarding public trust by monitoring fraud patterns and issuing necessary guidance.** As a part of this, the Central Bank issued a **Circular to safeguard the Current and Savings Accounts of customers from unauthorised access through Payment Apps in 2024 with effect from March 2025.** This would add to the existing regulations relating to payment app security. To bridge the gap in digital payment adoption, the Central Bank will conduct **nationwide public awareness programmes** on digital payment services, their benefits, associated security features and possible threats, such as fraud and scams, through mass media.

3.6. Improving Financial Consumer Relations

Strengthening Financial Consumer Protection is one of the key priorities as the Central Bank aims to foster a more transparent and consumer-centric sustainable financial system. A series of strategic initiatives are planned for 2025 and beyond in this regard, in order to enhance the trust of financial consumers in the financial system.

The scope of **market conduct supervision is expected to be broadened** by increasing the frequency and depth of on-site examinations of market conduct. This aims to ensure greater compliance with Financial Consumer Protection Regulations and to address emerging financial consumer risks.

In order to **address critical financial consumer risks and dissatisfaction and to set clear guidelines to prevent unfair practices and ensure compliance,** Directions focusing on issues such as fees and charges, penalties, and the imposition of interest on future obligations are to be issued.

In an attempt to enhance transparency, it is planned to **display key financial information** such as interest rates, fees, and charges of all Financial Service Providers on the Central Bank's official website, enabling consumers to make informed decisions.

4. Other Policies and Functions of the Central Bank

Key Highlights

- *Efforts to enhance and promote financial inclusion by broadening the related policy frameworks*
- *Facilitate the smooth transfer of the public debt management function to the Public Debt Management Office*
- *Conduct a comprehensive review of existing foreign exchange regulations considering the evolving needs of the market*
- *Undertake efforts to strengthen the Anti-Money Laundering and Countering the Financing of Terrorism (AML/CFT) framework and regulations*
- *EPF to enhance operational efficiency through digitalisation*
- *Diversify EPF's investment portfolio to provide secure and stable returns for its members*

The Central Bank has the responsibility of promoting financial inclusion. It also carries out several agency functions for the Government. Some key policies to be implemented in the period ahead in these areas are summarised in this section.

4.1. Financial Inclusion

With the enactment of the Central Bank Act, the primary focus of the regional development role of the Central Bank has evolved to promote financial inclusion. This shift signifies a broader recognition of the importance of establishing a more inclusive and sustainable financial system.

A post-implementation analysis will be conducted in early 2025 to assess the overall impact of the financial inclusion strategies and regulations implemented from 2021 to 2024 under Phase-I of the National Financial Inclusion Strategy (NFIS). This will be followed by **a national-level demand-side financial inclusion survey. In 2025, it is expected to develop Phase-II of the NFIS.** The new Phase will consider specific interventions for expanding the usage and quality of formal financial services to disproportionately excluded population segments of the country.

Further, the Central Bank expects to expand the scope of the existing financial inclusion policy framework by **integrating Inclusive Green Finance (IGF) as one of the NFIS pillars and by widening the financial consumer protection pillar** into financial consumer protection and market conduct supervision.

4.2. Public Debt Management

From its inception, public debt management has been one of the key agency functions carried out by the Central Bank. After nearly 75 years of the Central Bank handling this responsibility, the Public Debt Management Act was enacted in 2024 to create a separate office dedicated to managing all aspects of public debt under the Ministry of Finance. This will help eliminate the longstanding issue of conflict of interest of conducting monetary policy and managing the public debt by the same institution. **The Central Bank would facilitate in transferring the public debt management function to the dedicated institution called the Public Debt Management Office (PDMO).** PDMO is expected to be operationalised by the end of this year.

4.3. Foreign Exchange Management

The Central Bank carries out the foreign exchange management function on behalf of the Government. Following the rebounding activity in the domestic foreign exchange market, **a thorough and detailed review will be initiated to reassess the existing regulations, orders and directions issued under the Foreign Exchange Act.** This review aims to evaluate the evolving dynamics within the domestic foreign exchange market, address the changing needs and concerns of stakeholders, and enhance the overall regulatory framework. Export Proceeds Monitoring System, which was introduced in 2022, will be further developed to ensure greater efficiency and effectiveness in monitoring and initiating actions against noncompliance. These enhancements aim to foster greater transparency and contribute to the overall stability of the country's foreign exchange reserves. Further, **appropriate policy measures are expected to be implemented with respect to the conduct of the money-changing businesses** to transform the sector into a credible player in financial services.

4.4. Financial Intelligence

Sri Lanka's third Mutual Evaluation on its Anti-Money Laundering and Countering the Financing of Terrorism (AML/CFT) framework, coordinated by the Asia Pacific Group on Money Laundering (APG), is rescheduled to commence in March 2026. This evaluation will assess the country's efforts to combat money laundering and the financing of terrorism. Sri Lanka must ensure compliance with the 40 Recommendations of the Financial Action Task Force (FATF) and demonstrate the effectiveness of its AML/CFT framework under the FATF's 11 Immediate Outcomes.

The high level AML/CFT Task Force, reconstituted in December 2024 will remain operational until the successful completion of the Mutual Evaluation in July 2027. The Cabinet approved 24 institution-specific Action Plans, which were prepared based on FATF criteria and gaps, identified during the previous Mutual Evaluation conducted in 2014/2015 and the National Risk Assessment (NRA) conducted during 2021/2022 on Money Laundering and Terrorist Financing (ML/TF). They are currently being implemented by the relevant stakeholders and implementation progress is continuously reviewed by the AML/CFT Task Force.

The Financial Intelligence Unit (FIU) with its stakeholders and working groups expects to conduct another update to the NRA by Q2 2025. This assessment will consist of an assessment of tax crimes and proliferation financing risks as new areas, in addition to updating the 2021/2022 risk assessment. In order to further strengthen the cooperation between FIU and non-financial institutions and their regulatory authorities, FIU expects to form several working groups. Accordingly, it is planned to form separate working groups including FIU, regulatory bodies, private sector institutions of Designated Non-Finance Businesses and Professions (DNFBPs) sectors and other stakeholders such as sector-specific associations.

Additionally, FIU is in the final stages of drafting amendments to the three key pieces of AML/CFT legislation to strengthen the legal framework in alignment with international standards. The formalisation of the AML/CFT National Coordinating Committee (NCC) will occur through amendments to the FTRA. These legislative amendments are expected to be enacted by Q2 2025, with the review, drafting, and issuance of related Rules and Regulations planned for completion by Q2 2025. Furthermore, FIU will assist in the implementation of amendments to the Companies Act on beneficial ownership requirements and will assist with any other relevant legislative amendments or regulations related to AML/CFT.

In order to enhance intelligence sharing and strengthen international cooperation and compliance with global standards, **FIU aims to increase the number of bilateral Memoranda of Understanding (MOUs), both domestically and with relevant foreign counterparts**, as necessary. FIU will continue to raise awareness among stakeholders regarding the critical importance of effective AML/CFT implementation. Strengthening AML/CFT-related frameworks would provide the country with numerous economic, social, and national security benefits, including enhanced financial system integrity, increased foreign investments, increased access to international financial markets and enhanced support for the promotion of good governance practices.

4.5. Management of the Employees' Provident Fund

The Employees' Provident Fund (EPF) managed by the Central Bank, is the country's largest superannuation fund, with its value surpassing Rs. 4 trillion in 2024.

EPF is implementing several solutions including digitalisation of records and online payments for member contributions to enhance operational efficiency.

Undoubtedly, the introduction of online payment avenues will provide convenience and flexibility to the employers in making their EPF contribution payments and this shift will further streamline processes and reduce administrative burdens. While strengthening the contribution collection procedures with modern solutions, several actions are planned to be executed to

enhance the efficiency in providing the pre and post-retirement benefits to the members. **Moreover, ICT infrastructure is expected to be modernised to re-engineer the existing systems and procedures.** This comprehensive ICT solution will facilitate the automation processes, leading to more effective management of the Fund.

EPF is exploring opportunities to diversify its investment portfolio to achieve a higher risk-adjusted rate of return, while ensuring the safety and long-term sustainability of the Fund. By adopting these measures, the EPF aims to maintain its commitment to providing secure and stable retirement benefits for its members.

4.6. Central Bank's Communication Strategy

The Central Bank understands the importance of transparency and accountability in its activities, as they are essential for enhancing its credibility. The Central Bank's communication strategy for 2025 will also prioritise accessibility and inclusivity to foster public understanding and trust. **The Central Bank aims to ensure that its policy messages reach the grassroots level and are correctly interpreted.** Several steps will be taken to improve the dissemination of statistical data to enhance their accessibility and usability.

The Central Bank will continue to have close dialogue with stakeholders to gauge the pulse of the public and also to gather insights that will help the Central Bank make better-informed decisions.

4.7. Strengthening Internal Efficiency of the Central Bank

The Central Bank is committed to strengthening and institutionalising its human capital governance, expertise, capabilities, disciplines and rigor to manage its talent dynamics to deliver its mandates effectively for the progress of the nation.

Many initiatives are being introduced to enhance the Central Bank's technological capacity aimed at optimising resource utilisation, efficient data management and better decision making, while **cybersecurity aspects will be given increased attention** in the period ahead.

Measures have also been taken to implement a **Risk Appetite Framework (RAF) within the Central Bank** as the next strategic milestone for risk management. The Central Bank is also in the process of **incorporating environment-friendly and sustainable practices** in its day-to-day functions.

5. Fiscal, Monetary and Financial Stability Policy Coordination

The effective coordination between the Central Bank and the Government on fiscal, monetary, and financial stability policies is extremely important for consistent economic policy formulation and in achieving Central Bank's objectives. In pursuing the price stability objective, since inflation is frequently influenced by supply-side factors and impacts of fiscal policy measures, proper policy coordination is essential. This is equally important in pursuing the financial system stability objective. Government policies could affect the financial sector, while Central Bank policies on the financial sector could have a bearing on Government operations.

The Coordination Council established under the Central Bank Act provides for the coordination of fiscal, monetary, and financial stability policies between the Government and the Central Bank. The Coordination Council meets quarterly, where macroeconomic and financial conditions and outlook; and potential gaps relating to fiscal, monetary and financial stability coordination are discussed in detail, alongside deliberations on strategies, and the way forward to address any challenges. Meanwhile, **through the Financial Sector Crisis Management Committee (FCCMC) and the Financial System Oversight Committee (FSOC), the Central Bank coordinates with the Government and other stakeholders** including regulatory bodies, focusing on crisis preparedness and reducing the risk of coordination failures, to maintain a healthy financial system.

In addition, cordial meetings with the Honourable President and Finance Minister, and Deputy Ministers are conducted, as and when needed, on various matters relating to central banking and related economic and financial issues.

Key officials of the Central Bank present before several committees of the Parliament as provided in the Central Bank Act as well as on request, particularly to describe actions of the Central Bank and their impacts, and subjects related to the Central Bank.

Going forward, the continuation of such fiscal-monetary-financial system policy coordination will remain equally important, as the economy is expected to enter a comparatively normal period after several years of crises and uncertainty. Healthy policy coordination is expected to lead to a stable macroeconomic environment, which is an absolute necessity for the stakeholders, including the private sector, to promote productivity and efficiency in the economy, facilitating sustainable and inclusive growth.

6. Concluding Remarks

Today, Sri Lanka stands stronger with restored macroeconomic and financial sector stability, following several difficult years. Notwithstanding Sri Lanka's faster-than-expected recovery compared to the other countries that faced similar situations, sustaining stability in the medium to long run remains conditional on the country's commitments to pursue necessary economic reforms. Achieving a transformative acceleration in growth trajectory is essential to catch up and enhance the growth potential. This would also help enhance the debt-carrying capacity of the country. Building buffers to withstand shocks and accelerating growth without compromising on economic and financial system stability is the essential next step for the country's progress. In this regard, the Central Bank will continue its role in maintaining domestic price stability and safeguarding the financial system stability, while supporting the economy to reach its potential.

Thank you and we wish you all a good year filled with stability and prosperity!