



# MONTHLY ECONOMIC UPDATE | March

Economy at a glance for March 2021

## Economic activity picks up, ends 1Q stronger.

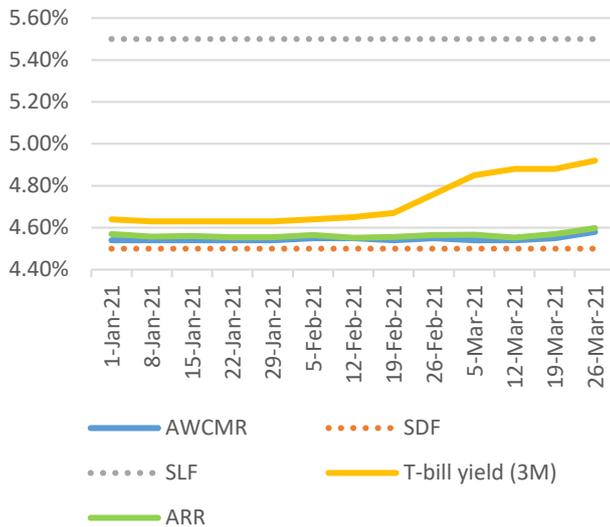
### Highlights

- Call and repo rates started to move up from mid-March while the call volumes exceeded the precrisis levels mainly due to substantial decline in excess liquidity by about LKR 70 Bn due to forex payments (equivalent to about LKR 180 Bn drain on money supply) by the CBSL.
- T-bill yields, which were already on an upward trajectory, saw further (~13-16 bps) increase.
- Reserve money expanded recording the strongest year-on-year expansion since April last year.
- Yields on the near-dated SLISBs plunged (10-20 pps) in March after the market parsed the news on confirmation of USD 1.5 Bn swap with China.
- Increasing yields in US treasury market and weakening rupee dimmed the attractiveness of local treasuries which triggered foreigners to sell over USD 6 Mn treasuries.
- Rupee faced gradual depreciation throughout the month amid selling pressure in the interbank spot market.
- Inflation rose to 4.1% as a result of broad base increase in both food and non-food inflation.
- The CSE continued to remain bearish for the second straight month with market closing with a drop of 4.75% in the ASPI and a drop of 3.93% in the S&P20.
- PMI for manufacturing recorded the highest index value since June last year indicating stronger recovery in March.

## Interest Rates

### Short-term rates

Figure 1: Treasury bill yield and money market rates



Notes: AWCMR- Average Weighted Call Money Rate, SDFR- Standing Deposit Facility Rate, SLFR- Standing Lending Facility Rate, T-bill yields are for the secondary market, ARR – simple average of daily repo rates  
Source: CBSL

Call and repo rates started to move up from mid-March while the call volumes exceeded the precrisis levels. This was mainly due to substantial decline in excess liquidity by about LKR 70 Bn due to forex payments (equivalent to about LKR 180 Bn drain on money supply) by the CBSL. T-bill yields, which were already on an upward trajectory, saw further (~13-to-16 bps) increase during the said period. Meanwhile, the CBSL relaxed the yield caps on 12M T-bills by 2bps.

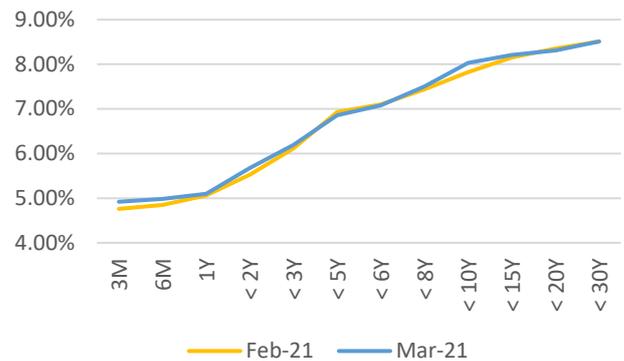
As usual, there were no auction based open market operations during the month. The demand for treasuries in the primary auctions gradually declined (the ratio between amount offered to bids received declined to 1.2 from 2.5). As a result, the market was only able to absorb offered treasury stock partially in all primary auctions during March except in the first auction. The CBSL intervened and absorbed around LKR 40 Bn from the primary market to take up the shortfall. Furthermore, it

<sup>1</sup> AWPR is calculated based on the submissions made by the commercial banks to the CBSL on the rates offered to customers who borrowed more than LKR 10 Mn for less than three months.  
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helped to moderate the effect of falling liquidity level. In contrast, the activity levels in the secondary T-bills market remained elevated recording modest volumes with respect to February.

### Long-term rates

Figure 2: Yield curve of treasuries

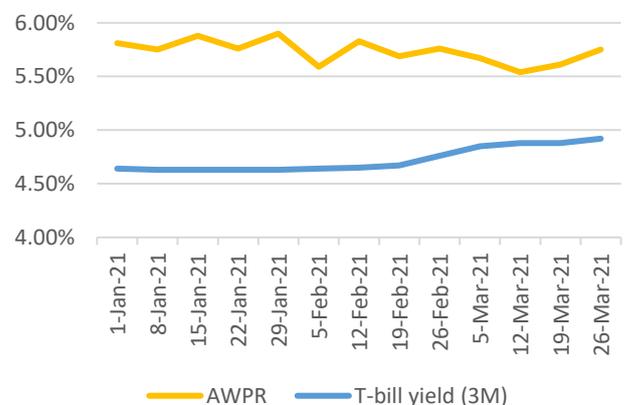


Notes: Yields are based on the weekly average prevailed at the last week of the month, Shorter end – less than 2Y, mid/intermediate tenor – 2 to 10Y, longer tenor – above 10Y, Source: CBSL

Compared to T-bills, investors showed better appetite for fresh bond issues during March and was able to absorb most of the offered.

Movements in the secondary market bond yields were mixed with some mid-tenor maturities increasing by 10-to-20 bps.

Figure 3: AWPR<sup>1</sup> and 3M T-bill yield



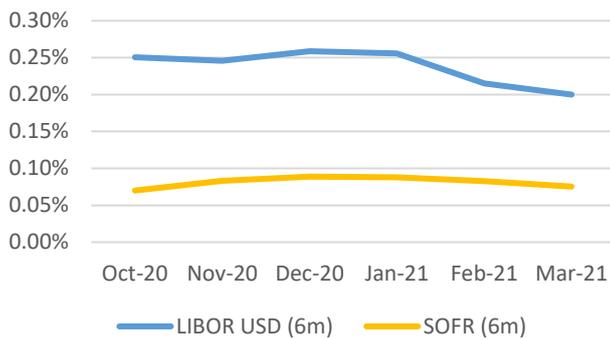
Note: T-bill yield for secondary market  
Source: CBSL

Dip in the liquidity levels drove the AWPR higher in the second half of the month back to 5.75%.

Credit growth in February exceeded our expectations. Reserve money expanded in March recording the strongest year-on-year expansion since April last year. The expansion is on account of growth in both currency in circulation and deposits held by the commercial banks with the Central Bank. Generally, currency in circulation expands ahead of festive seasons. In addition, manufacturing, plantations, and trading businesses operate above average capacity during March, which may increase their working capital intensity leading to a temporary spike in borrowings. Therefore, we expect a relatively stronger credit expansion in March.

### International rates

Figure 4: Month open international lending rates



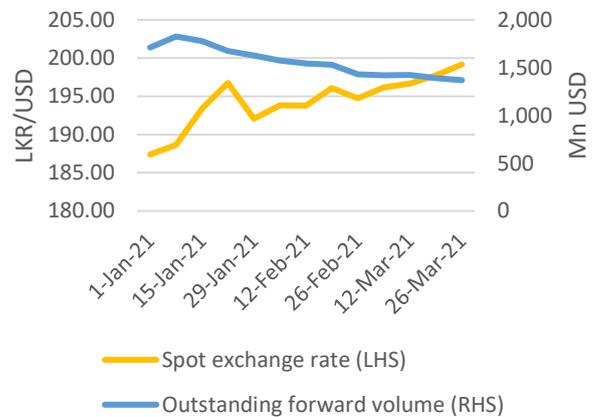
Notes: The SOFR Averages are compounded averages of the SOFR over rolling 180-calendar day periods.  
Source: New York Federal Reserve and global-rates.com

US treasury yields continued to move up despite reassurances from Fed before moderating towards the end of March. Europe’s slow recovery sparked concerns among investors. Market seemed to believe that inflation would pick up faster than what the Fed has forecasted. The testimonies of Powell and Yellen to the Senate Banking Committee helped to sooth yields.

Yields on the near-dated SLISBs plunged (10-to-20 pps) in March after the market parsed the news on confirmation of USD 1.5 Bn swap with China [1].

## External Sector

Figure 5: Exchange rate and outstanding forward volume



Source: CBSL

In February, merchandise exports showed a 3.7%(Y/Y) decline, in line with our early predictions. However, imports retreated (-2.5% Y/Y) stronger than what we have predicted leading to a slightly wider trade deficit (USD 572 Mn) than initially envisaged. Worker remittances grew 9.9%(Y/Y) broadly in line with our expectations.

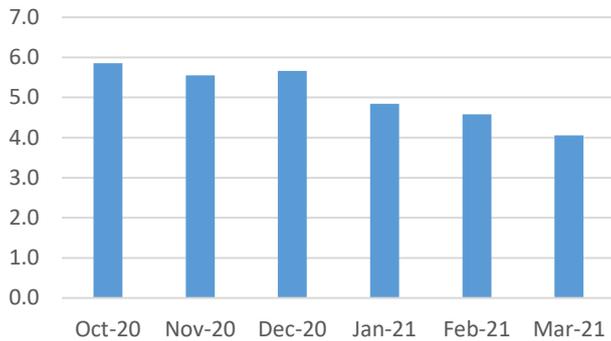
Increasing yields in US treasury market and weakening rupee dimmed the attractiveness of local treasuries which triggered foreigners to sell over USD 6 Mn treasuries. In the local equities market also foreigners were bearish and sold around USD 21 Mn worth shares.

Reserves slid to just over USD 4 Bn in March. Official data shows total forex loan payments due for March to be around USD 910 Mn. In addition, the settlement related to the repo facility (USD 500 Mn) with Fed fell in March<sup>2</sup>. The CBSL bought over USD 75 Mn from the domestic forex market during March.

Rupee faced gradual depreciation throughout the month amid selling pressure in the interbank spot market. Imports typically pick up in March in anticipation of consumer demand during the festive season which increases demand for dollar. Activity level in the forward market continued to decline for the said period.

<sup>2</sup> Settlement of the repo would not affect the overall reserve position.  
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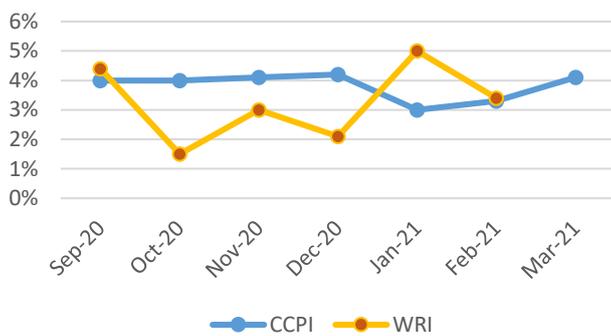
Figure 6: Gross official reserves (Mn USD)



Source: CBSL

## Prices & Wages

Figure 7: CCPI and Nominal Wage Rate Index of the informal private sector (Y/Y)



Notes: WRI (100=2012), CCPI (100=2013)

Source: CBSL

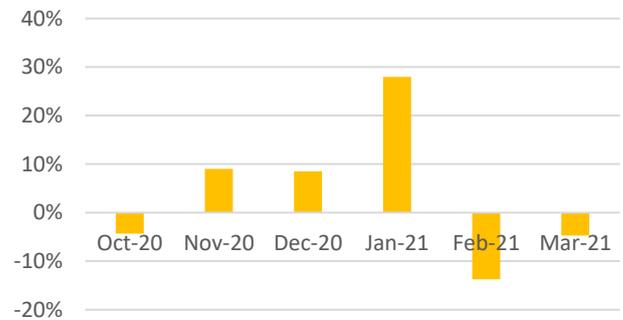
Wage growth declined a little bit but stayed on par with the inflation level in February. Recovery of wages is mainly due to the recovery of the services sector.

Inflation rose to 4.1% as a result of broad base increase in both food and non-food inflation. Notable increases in transports, clothing, footwear, restaurant, and hotels contributed to increase in non-food inflation.

## Equities

### Domestic Market

Figure 8: ASPI (M/M)



Source: CSE

The CSE continued to remain bearish for the second straight month with market closing with a 4.75% fall in the ASPI and a 3.93% fall in the S&P20. Foreign investors moved away due to the upbeat global equity markets. Almost all GICS sectors recorded losses. The market exhibited a steeper drop during the first week with heavy selling pressure causing the market to lose over LKR 200 Bn. By the end of the second week continuous dips in the market resulted in the stocks plunging by another 5.4%. However, towards the end of the month the investors regained confidence ending with a positive note. In this context, market PBV (price-to-book-value) decreased from 1.22 to 1.12 favouring buyers.

Figure 9: GICS sector performance- March

Sector	Index Points Gain
Insurance	32
Utilities	5
Telecommunication Services	-8
Real Estate	-8
Banks	-10
Food & Staples Retailing	-11
Consumer Services	-11
Automobiles & Components	-12
Retailing	-32
Household & Personal Products	-32
Energy	-36
Food, Beverage & Tobacco	-40
Consumer Durables & Apparel	-46

Healthcare Equipment & Services	-48
Capital Goods	-64
Commercial & Professional Services	-83
Materials	-115
Diversified Financials	-164
Transportation	-301

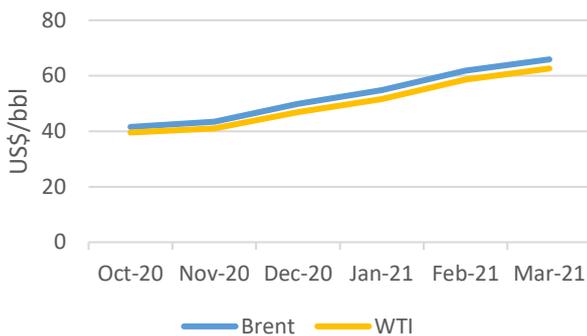
Source: CSE

### Global Markets

US and major European indices were buoyant over recovering economies and reducing infection rates. However, rise in yields drove investors to the treasury market at the expense of equities. In the meanwhile, emerging market indices were mostly positive.

## Commodities

Figure 10: Crude oil price



Source: Bloomberg quoted in CBSL

Brent crude oil averaged around USD 65 a barrel during the month, surpassing February high. The month opened with prices peaking close to USD 70/bbl – highest in over a year. Oil price hikes continued to be mainly influenced by supply restrictions brought about by OPEC+ countries as they continue to rollover production cuts going into April [2].

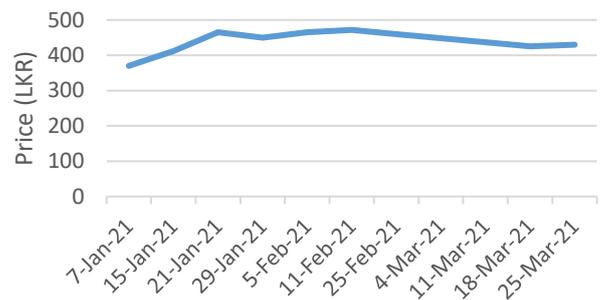
Figure 11: Tea (All Elevations) price and quantity sold at weekly auctions



Source: Forbes & Walker

Tea prices declined in the last two auctions in March. Drop in leaf quality and currency depreciation in middle eastern markets were attributed to the slump [3].

Figure 12: Rubber price weekly auctions

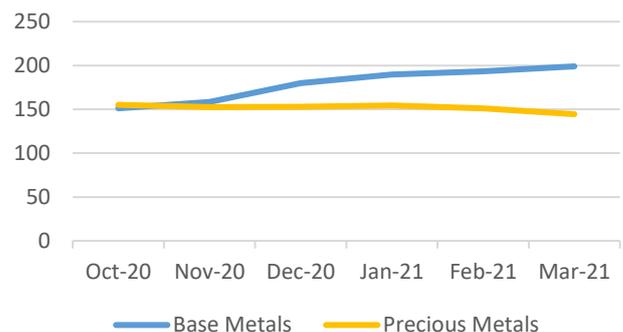


Note: Price of Latex 4X

Source: RRISL

Global rubber prices experienced a fall during the month of March as tire production plummeted but the effect was somewhat offset by soaring crude oil prices.

Figure 13: Metal price index (2016=100)



Notes: Base metals index includes Aluminum, Cobalt, Copper, Iron Ore, Molybdenum, Nickel, Tin, Uranium, and Zinc, precious metals index includes Gold, Silver, Palladium, and Platinum

Source: IMF

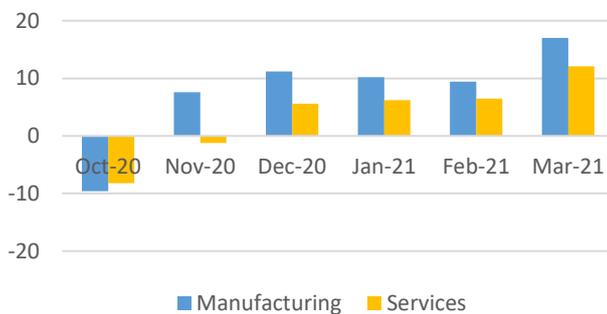
Gold prices in March saw prices reaching its lowest levels since June 2020 continuing from its sharp fall last month as gold struggled to compete with rising treasury yields.

During March copper prices slowly declined from its 9-year peak in February and remained fairly constant throughout the month. Steel prices continued to maintain momentum as it touched a 10-year peak towards the end of March.

Read ICRA Lanka's report on the [implications of rising commodity prices for Sri Lanka](#).

## Real Sector

Figure 14: PMI deviation from point of neutrality (Index points)



Notes- negative values indicate sector is generally contracting on a month-on-month basis while positive values indicate the sector is expanding. The strength of contraction or expansion is manifested by the magnitude of the figure.

Source: CBSL

PMI for manufacturing recorded the highest index value since June last year indicating stronger recovery in March. With the pandemic situation appearing to be under control, consumer spending ahead of the festive season was seen rising helping to boost production and sales. To cater to the demand the businesses were seen scaling their work force up. However, the shipping and logistic related delays were still prevalent causing delays in supplies.

Services sector also experienced a considerable recovery in March. The activity levels rose with gradual return to normalcy of daily lives with pandemic in check. Employment in services too recorded expansion. Overall, businesses seemed to be upbeat about the prospects for next three months.

Read ICRA Lanka's report on [the outlook for Sri Lankan economy - 2021](#).

## Outlook for April

With many markets and businesses winding down operations due to holidays, April is generally considered to be a slow month. Thus, we do not expect major swings in economic indicators for April. However, banks and investors will keep a close tab about the external position of the country. Markets seemed to be alarmed about likelihood of rising inflation and may keep factoring it in treasury yields.

## Rating Actions

Following rating actions were taken by ICRA Lanka during the month of **March**.

Visit <https://www.icralanka.com/ratings/> to read the rating rationales.

Issuer	Issue	Action	Previous Rating	Current Rating
People's Bank	Issuer rating	Assigned	N/A	[SL]AAA (Stable)
People's Bank	Basel III compliant Tier 1 Capital Bond programme (LKR 6000 Mn)	Assigned	N/A	[SL]AA(hyb) (Stable)
Sanasa Life Insurance	Issuer rating	Assigned	N/A	[SL]BBB (Stable)
Sanasa Life Insurance	Senior Unsecured Redeemable Debenture Programme (LKR 200 Mn)	Assigned	N/A	[SL]BBB (Stable)
Softlogic Money Market Fund	MMF	Assigned	N/A	[SL]Amfs
Senfin Money Market Fund	MMF	Assigned	N/A	[SL]A+mfs
Sri Lanka Savings Bank	Issuer rating	Reaffirmed and outlook revised	[SL]BBB- (On Watch)	[SL]BBB- (Stable)

## Abbreviations

ASPI	All Share Price Index
bps	Basis points
pps	Percentage points
CBSL	Central Bank of Sri Lanka
CSD	Census and Statistics Department
CSE	Colombo Stock Exchange
GICS	Global Industry Classification Standard
GoSL	Government of Sri Lanka
SLDB	Sri Lanka Development Bonds
SLISB	Sri Lanka International Sovereign Bonds
SOFR	Secured Overnight Financing Rate
PMI	Purchasing Managers Index
RRISL	Rubber Research Institute of Sri Lanka
YTD	Year-to-date

## Works Cited

- [1] CBSL, "The Central Bank of Sri Lanka enters into a Bilateral Currency Swap Agreement with the People's Bank of China," 22 March 2021. [Online]. Available: <https://www.cbsl.gov.lk/en/node/9944>.
- [2] IEA, "Oil Market Report - March 2021," 2021. [Online]. Available: <https://www.iea.org/reports/oil-market-report-march-2021>.
- [3] S. A. Morrell, "Bad news for tea industry as auction prices slide," The Island, 04 March 2021. [Online]. Available: <https://island.lk/bad-news-for-tea-industry-as-auction-prices-slide/>.

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