Monthly Economic Update (MEU)

January 2025

Economic Intelligence Unit
The Ceylon Chamber of Commerce

Highlights

Sri Lankan Economy

CBSL Maintains it's Policy Rate at the Current Level

The Monetary Policy Board of the Central Bank of Sri Lanka (CBSL) decided to maintain the Overnight Policy Rate (OPR) at 8.00% during its meeting on 28 January 2025, after assessing domestic and global macroeconomic trends. The decision aims to guide inflation toward the 5% target while supporting economic growth.

Inflation remained Negative for the Fourth Consecutive Month and Expected to Remain Negative in the Near Term

Headline inflation, measured by the year-on-year change in the Colombo Consumer Price Index, remained negative for the fourth consecutive month in December 2024, driven by lower electricity tariffs and fuel prices amid weak demand. Projections indicate a deeper-than-expected deflation due to the significant electricity tariff reduction in January 2025. Inflation is expected to turn positive by mid-2025 and gradually move toward the 5% target with appropriate policy measures. Core inflation, currently at low positive levels, is projected to decline further before rising later in the year.

GDP Grows by 5.2% in First Nine Months of 2024

Sri Lanka's GDP grew by 5.2% in the first nine months of 2024, marking a strong recovery from previous economic challenges, though largely influenced by a low statistical base. The economy benefited from lower inflation, declining interest rates, and increased trade activity, particularly in exports and imports, which boosted key sectors like apparel and construction. Additionally, higher tourism earnings, remittance inflows, and improved hydroelectric power generation contributed to economic stability and growth. As per the CBSL, this robust economic growth is likely to have continued, resulting in higher growth for 2024 than initially projected.

Market Lending Rates Continued to Decline, Credit to Private Sector Improves

Market lending interest rates continued to decline following the recent monetary policy easing, with short-term money market rates adjusting downward and the Average Weighted Call Money Rate (AWCMR) aligning with the OPR. Lower rates, along with economic recovery, have accelerated private sector credit growth, a trend expected to continue. Meanwhile, government securities yields have also fallen, reflecting improved fiscal performance and reduced sovereign risk premia.

Sri Lanka's Credit Rating Improve following Soverign Bond Restructuring

Sri Lanka completed its International Sovereign Bond restructuring on 20th December 2024, leading to a Fitch Ratings upgrade of its Long-Term Foreign-Currency IDR to 'CCC+' from 'RD'. Moody's also upgraded Sri Lanka's rating from Ca to Caa1, marking the most significant long-term foreign currency issuer rating improvement among recent sovereign defaults. However, S&P maintained Sri Lanka's rating at selective default (SD) due to the unresolved USD 175 million SriLankan Airlines bond, which remains in default.

External Sector Strengthens Amid Debt Restructuring and Reserve Growth

The external sector remained strong despite a wider trade deficit in 2024, driven by higher import growth outpacing exports. Increased earnings from tourism and workers' remittances supported the external current account, while the Sri Lankan rupee appreciated by 10.7% in 2024 before depreciating by 2.0% in early 2025. The successful completion of external debt restructuring, except for a small portion, improved the country's external outlook. Gross Official Reserves reached USD 6.1 billion by end-2024, including the renewed three-year bilateral currency swap with the People's Bank of China.

Global Economy

IMF Revises Global Growth Outlook Amid Mixed Economic Trends

The IMF's January World Economic Outlook projects global growth to rise from 3.2% in 2024 to 3.3% in 2026, with a slight upward revision for 2025 due to stronger U.S. performance offsetting weaker growth in Asia and Europe. While the U.S. expanded by 2.7%, China's slowdown, weak euro area manufacturing, and Japan's mild contraction contributed to lower-than-expected global GDP growth in Q3 2024. Inflation continues to ease unevenly, with energy prices expected to decline and monetary policies adjusting at different rates, while downside risks remain due to policy uncertainty and trade tensions.

Dashboard

Y-o-Y changes, otherwise specified

Economic Growth

5.5% in Q3-2024

1.6% (Q3-2023)

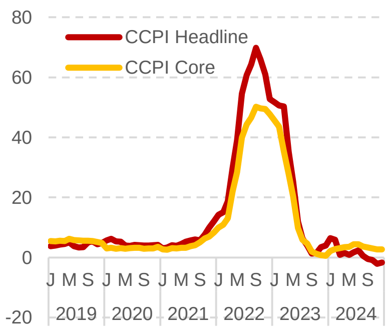
Movement of Purchasing Managers' Index-Dec 2024

Manufacturing PMI	57.2
Services PMI	71.1
Construction PMI (Nov)	51.4

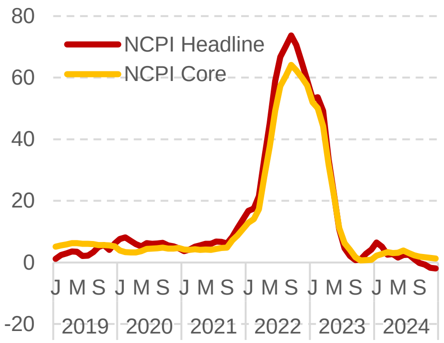
All three indices recorded an expansion

Inflation

CCPI Inflation (%)-*Base 2021*



NCPI Inflation (%)-*Base 2021*

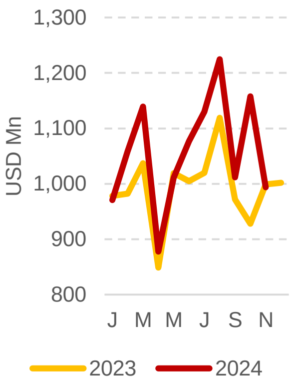


	Headline	Core
Dec 2024 (CCPI)	-1.7%	2.7%
Dec 2024 (NCPI)	-2.0%	1.3%

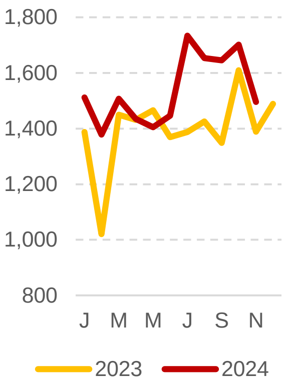
External Sector

Merchandise Trade

Exports



Imports



Trade Deficit

Dec 2024

64%

Services Account Balance

Nov 2024

7.7%

Tourism

Dec 2024

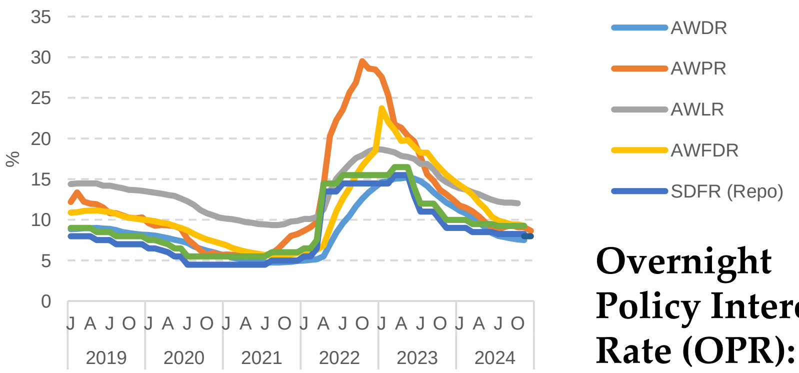
Arrivals **18%**

Earnings **34%**

Workers' Remittances

Dec 2024 **8%**

Interest Rates



Growth in Credit to Private Sector

Nov 2024

9.7%

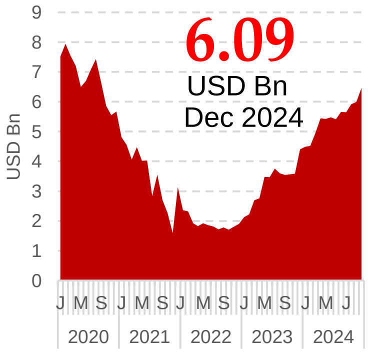
Overnight Policy Interest Rate (OPR): 8%

Exchange Rate

Depreciation of LKR thus far 2025

2.1%

Official Reserves



6.09 USD Bn

Dec 2024

KEY INSIGHTS
Sri Lankan Economy

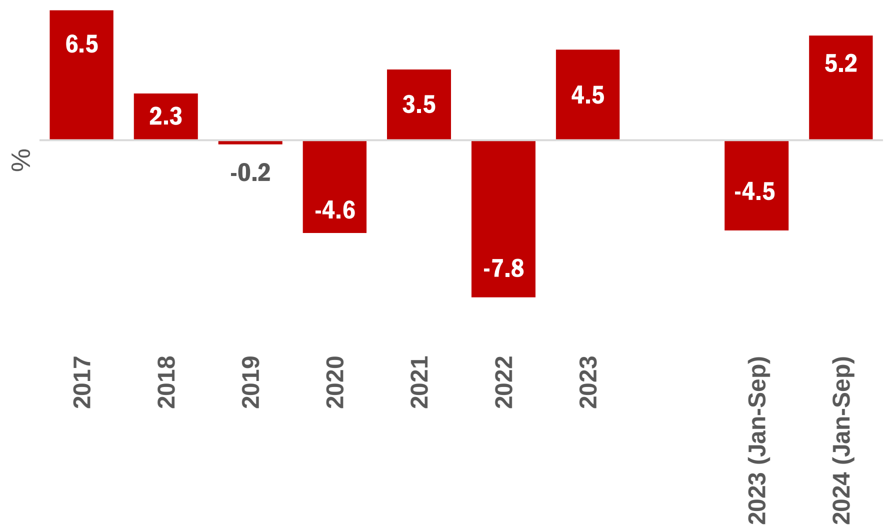
Sri Lanka's GDP Grows by 5.2% in First Nine Months of 2024

Sri Lanka's Gross Domestic Product (GDP) demonstrated substantial growth in the first nine months of 2024, expanding by 5.2% compared to the same period in 2023. This marks a notable rebound from the economic difficulties of the previous years. However, it's essential to recognize that this growth follows consecutive quarters of economic contraction due to the impact of the pandemic and subsequent financial crisis. Therefore, much of the growth is attributed to the lower statistical base used for these calculations, which had been significantly eroded by earlier declines.

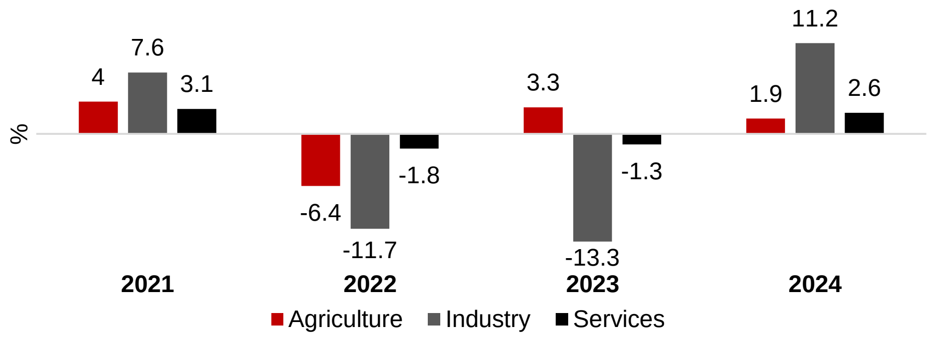
In the first half of 2024, Sri Lanka's economy benefited from lower inflation, and a sharp decline in interest rates was noticed towards the end of the third quarter of 2024, which eased the domestic credit supply especially to the private sector. A noteworthy increase in export and import quantities were identified, which facilitated most of the economic activities by providing forward and backward linkages to prosper. More importantly, increase in imports of investment goods as well as intermediate goods such as textile and textile articles and cement mainly facilitated to the recorded high growth in apparel industry and construction industry respectively. Moreover, increased earnings from Tourism and Workers' Remittances inflows strengthened the country's foreign currency stance with the simultaneous uplift in country's rupee value in the foreign currency market. From the domestic front, the increased water stocks in reservoirs further increased the hydro electricity generation and relatively high production of eggs and poultry supported animal production activity to report a remarkable positive growth rate.

In the Agriculture sector, a modest growth of 1.9% was recorded, with substantial gains in "Growing of cereals" (29.2%) and "Animal Production" (11.6%). However, severe contractions were noted in "Plant propagation" (-18%) and "Growing of rubber" (-11.9%), reflecting uneven performance within the sector. The industry sector posted robust growth of 11.2%, driven by the "Construction" and " Manufacture of basic metals and fabricated metal products" industries, which surged by 17.8% and 27.2%, respectively. The Services sector saw a 2.6% increase, supported by a 27.7% surge in "Accommodation, food, and beverage serving activities," benefiting from the resurgence of tourism. "Insurance, reinsurance, and pension funding" also posted strong growth of 13.1%.

Annual Growth of Real GDP



Sectoral Growth First Nine Months



Data Source: DCS

KEY INSIGHTS
Sri Lankan Economy

Rating Agencies Upgrade Sri Lanka from Restricted Default Status

On 20th December 2024, Sri Lanka successfully concluded the settlement of its International Sovereign Bond (ISB) restructuring, marking a critical milestone in the country's path toward economic stabilization. In recognition of this achievement, Fitch Ratings upgraded Sri Lanka's Long-Term Foreign-Currency Issuer Default Rating (IDR) to 'CCC+' from 'RD' (Restricted Default). Fitch also raised the Local-Currency IDR to 'CCC+' from 'CCC-', aligning it with the Long-Term Foreign-Currency IDR. This adjustment reflects a reduced risk of further defaults on local-currency debt, supported by the completion of the ISB restructuring and an improved outlook for key macroeconomic indicators, including inflation and foreign exchange reserves. Whilst Sri Lanka's issuer rating was upgraded by Fitch, other recent sovereign debt restructurings Zambia and Ghana have not yet received a long-term foreign currency issuer rating upgrade as at end 2024.

On 23rd December 2024, Moody's followed suit, upgrading Sri Lanka's rating from Ca to Caa1. This represents the most significant long-term foreign currency issuer rating upgrade among Moody's recent adjustments for nations emerging from sovereign default in 2024. Moody's also raised Sri Lanka's local and foreign currency country ceilings, upgrading the local currency ceiling to B1 from Caa1 and the foreign currency ceiling to B3 from Ca. These changes reflect a more favorable assessment of Sri Lanka's economic resilience and ability to manage its debt obligations. This rating upgrade by Moody is the highest long term foreign currency issuer rating upgrade among Moody's recent upgrades from sovereign default in 2024.

However, Standard & Poor's (S&P) maintained Sri Lanka's sovereign rating at selective default (SD). Under S&P's assessment criteria, a rating upgrade is precluded if any foreign currency-denominated commercial debt remains unresolved. This restriction applies to the USD 175 million government-guaranteed bond issued by Sri Lankan Airlines, which has yet to be restructured and remains in default. The government continues to work on restructuring this bond, and its resolution is likely to influence future upgrades from S&P.

Rating Agency	Rating	Last Update	Action
Fitch Ratings	CCC+	20 Dec 2024	Rating upgrade
Moody's Investors Service	Caa1	23 Dec 2024	Rating upgrade
Standard & Poor's	SD	25 Apr 2022	Rating downgrade

"The restructuring under Fitch's baseline assumptions lowers general government debt/GDP to about 90% by 2028, while Fitch forecasts the interest/revenue ratio to decline to 42%, still well above the 'CCC' median of 16%. This is, however, a large drop from the 67% in 2021, prior to the sovereign default.

- Fitch Ratings

"We could raise the long-term local currency rating on Sri Lanka if we perceive that the sustainability of the government's large local currency debt stock has improved further.

Our post-restructuring ratings tend to be in the 'CCC' or low 'B' categories, depending on the sovereign's new debt structure and capacity to support its debt."

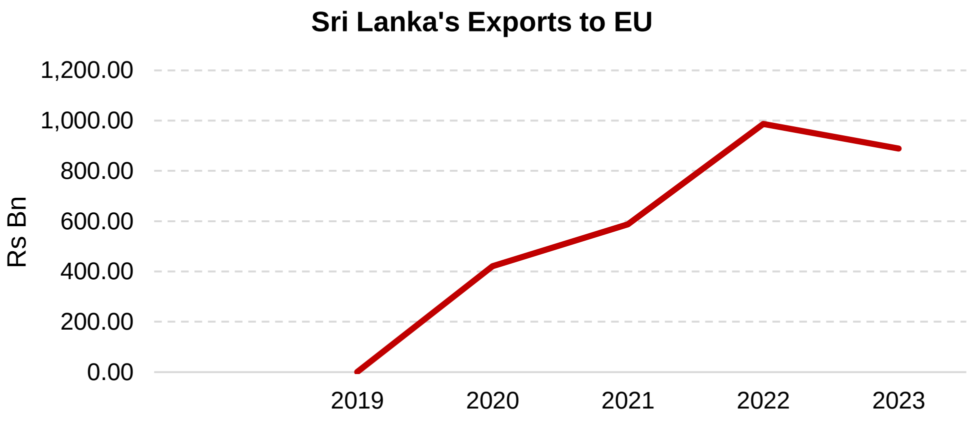
- Standards and Poor's

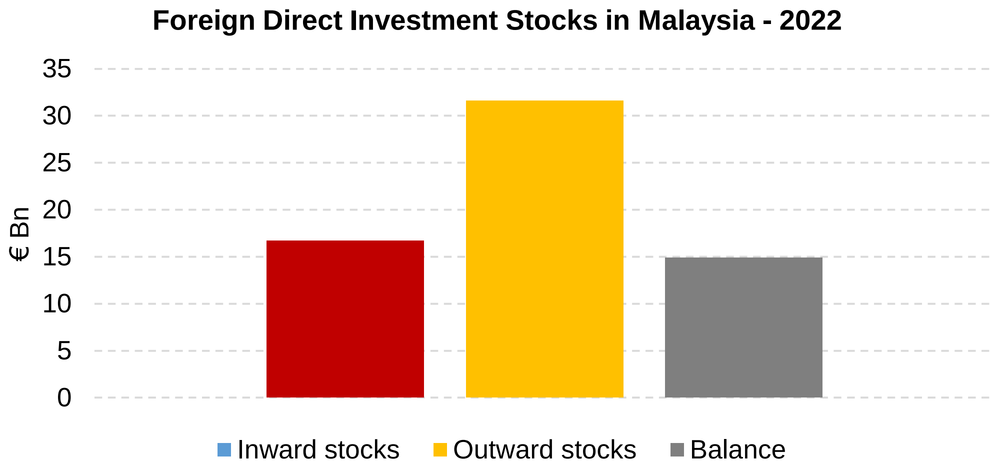
Data Source: Fitch, Moody's, Standard and Poor's

KEY INSIGHTS
Global Economy

EU-Malaysia FTA Resumption

On January 20, 2025, the European Union (EU) and Malaysia resumed negotiations for a comprehensive and modern Free Trade Agreement (FTA). In 2023, Malaysia was the EU's third-largest trading partner in ASEAN, contributing 12% to the region's GDP. This agreement could increase Malaysia's access to the EU market, supporting growth in exports like machinery, electronics, and palm oil products. In 2023, trade between the EU and Malaysia was concentrated in industrial goods, with machinery and appliances accounting for 62% of EU imports and 46% of EU exports. Other key imports from Malaysia included fats, oils, and chemical products, while chemical products dominated EU exports to Malaysia. This development could indirectly impact Sri Lanka, a major beneficiary of the EU's Generalized Scheme of Preferences Plus (GSP+) program, which provides duty-free access on 66% of tariff lines. In 2023, Sri Lanka's exports to the EU, its second-largest trading partner, were led by textiles and rubber products. Sri Lanka's trade with Malaysia remains modest, with key exports including milling industry products and apparel, while imports are dominated by mineral fuels and machinery. Strengthened EU-Malaysia trade ties may affect Sri Lanka, particularly in sectors like rubber, machinery, and apparel. Malaysia's liberalization policies have attracted significant EU Foreign Direct Investment (FDI), which reached €31.6 billion in 2022. Sri Lanka, however, faces challenges such as regulatory delays and infrastructure gaps that hinder FDI in services. Unlike Malaysia, which is part of agreements like the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP), Sri Lanka has limited participation in global trade frameworks. To improve competitiveness, Sri Lanka needs structural reforms in its investment climate. Simplifying regulatory procedures, upgrading infrastructure, and investing in workforce skills are necessary measures to attract FDI. Sri Lanka should also begin negotiations for comprehensive FTAs with partners such as the EU, India, and Singapore to improve access to international markets and expand its trade portfolio beyond apparel.





Data Source: European Commission

KEY INSIGHTS
Global Economy

IMF World Economic Outlook: January 2025 Update

The International Monetary Fund's (IMF) January World Economic Outlook (WEO) updates global growth estimates. Growth is projected to rise from 3.2% in 2024 to 3.3% in 2026, with the 2025 forecast revised up by 0.1 percentage points due to stronger U.S. projections offsetting weaker growth in other major economies. Slower growth from 2022 to 2023 was driven by advanced economies. Global GDP growth in Q3 2024 was 0.1 percentage points below October forecasts, reflecting weaker-than-expected data from Asia and Europe. China's growth slowed to 4.7% due to delayed property market stabilization and low consumer confidence. India faced sharper-than-expected industrial slowdown, while the euro area, particularly Germany, struggled with weak manufacturing and exports. Japan experienced mild contraction due to supply disruptions. In contrast, the U.S. economy expanded by 2.7% year-over-year, supported by strong consumption.

Global disinflation persists but progress is uneven, with core inflation slightly above 2%. While wage growth moderates, services price inflation remains elevated, particularly in the U.S. and euro area, with pockets of high inflation in parts of Europe and Latin America. Energy prices are projected to decline by 2.6% in 2025, driven by weak Chinese demand and strong non-OPEC+ supply. Nonfuel commodity prices are expected to rise by 2.5%, reflecting bad weather affecting food production. Major central banks' monetary policies will ease at varying rates, while fiscal tightening is anticipated in advanced economies and some emerging markets.

Growth in the U.S. is forecast at 2.7% in 2025 before normalizing in 2026. The euro area's growth is revised to 1.0% in 2025, rising to 1.4% in 2026 amid improved financial conditions. China's growth is projected at 4.6% in 2025, stabilizing at 4.5% in 2026, while India remains strong at 6.5% annually. Global risks remain tilted to the downside, with heightened policy uncertainty and potential trade tensions posing challenges across economies.

IMF World Economic Growth Projections

	2024	2025	2026
Advanced economies	1.7	1.9	1.8
United States	2.8	2.7	2.1
United Kingdom	0.9	1.6	1.5
Japan	-0.2	1.1	0.8
Canada	1.3	2.0	2.0
Germany	-0.2	0.3	1.1
France	1.1	0.8	1.1
Italy	0.6	0.7	0.9
EMDEs	4.2	4.2	4.3
China	4.8	4.6	4.5
India	6.5	6.5	6.5
Russia	3.8	1.4	1.2
Brazil	3.7	2.2	2.2
Mexico	1.8	1.4	2.0
Saudi Arabia	1.4	3.3	4.1

Data Source: IMF

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.

Divergence and Challenges in Global Financial Markets amid Policy Shifts

Global financial markets are witnessing growing divergence in monetary policies and mounting uncertainties as the world adjusts to evolving economic dynamics. The IMF's January 2025 update highlights significant differences in the projected policy rate trajectories between the U.S. and other major advanced and emerging market economies. This divergence reflects varying growth outlooks, inflation pressures, and domestic challenges. While the U.S. Federal Reserve maintains a relatively tighter monetary stance, weaker growth in the euro area and key emerging markets has spurred expectations of accelerated monetary easing in those regions.

Medium- and long-term bond yields in the U.S. have risen, driven by persistent inflation risks and labor market adjustments. Meanwhile, yields in other advanced economies and emerging markets have generally declined, reflecting a more cautious outlook on growth. This disparity has bolstered the U.S. dollar, which has appreciated against major currencies, including the euro, amid geopolitical tensions and trade policy uncertainties. Emerging market currencies have faced additional depreciation pressures due to domestic fiscal concerns, resulting in net capital outflows and heightened vulnerability. Global financial conditions, though broadly accommodative, have tightened slightly since October 2024, especially for emerging markets. U.S. equity markets reached record highs in Q4 2024, underpinned by expectations of deregulation and tax cuts, which have brightened growth prospects. However, rising long-term rates have tempered some of these gains. In contrast, emerging markets have experienced tighter financial conditions, as risk assets remain more sensitive to geopolitical risks, trade uncertainties, and currency volatility.

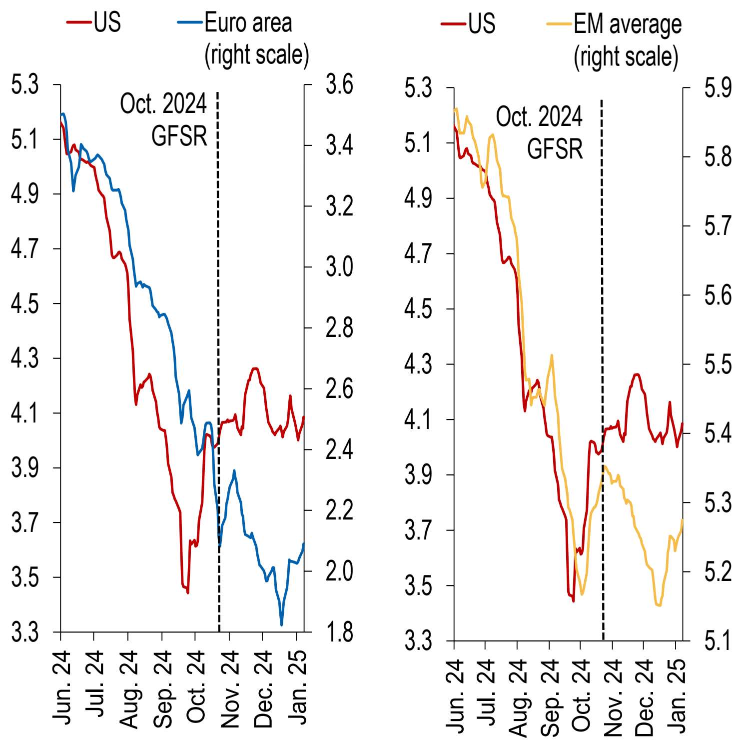
The divergence in financial conditions is creating challenges for policymakers. Advanced economies are contending with inflationary pressures and the risk of financial market overheating, while emerging markets face constraints from external financing pressures and domestic fiscal vulnerabilities. For economies heavily reliant on external financing or with weaker fiscal fundamentals, the potential for sharp adjustments in financial conditions poses a significant risk. Energy markets add another layer of complexity, with geopolitical risks contributing to supply disruptions. Non-OPEC+ countries have increased oil production, but weaker demand from China and elevated gas prices due to colder-than-expected weather and supply outages have introduced further volatility. These trends have broader implications for inflation and trade balances, particularly in energy-importing economies.

Looking ahead, market participants are closely monitoring tariff policies and geopolitical developments, which remain key drivers of global financial stability. The possibility of escalating trade tensions or protectionist measures poses a significant risk to the global economy, potentially distorting trade flows, reducing investment efficiency, and disrupting supply chains. Such developments could amplify volatility in financial markets, particularly in economies already grappling with macroeconomic imbalances. Monetary policy paths are expected to diverge further. The U.S. Federal Reserve's relatively hawkish stance contrasts with the more dovish expectations in the euro area and emerging markets. In the euro area, weak manufacturing momentum and heightened policy uncertainty have led to downward revisions in growth forecasts, while domestic demand remains subdued. Emerging markets face additional challenges, including geopolitical uncertainties and fiscal pressures, which are dampening growth prospects.

Evolving Landscape cont'd

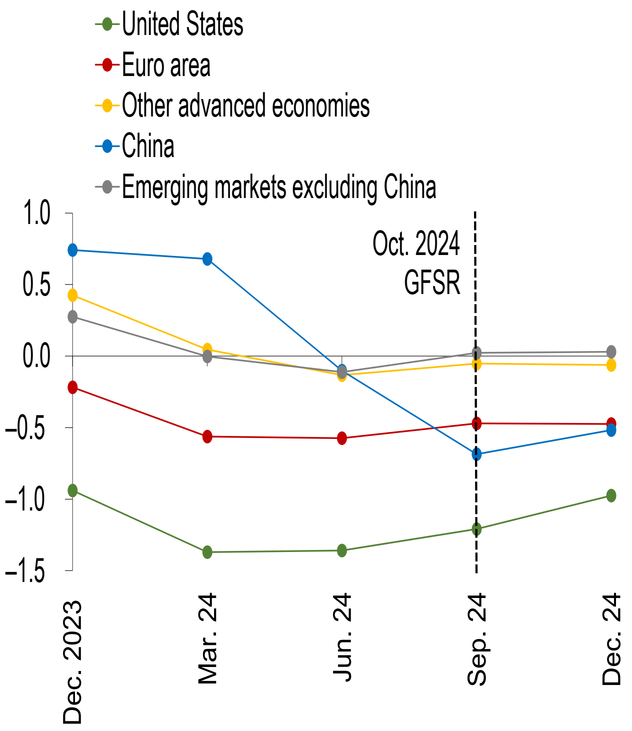
With the aim of keeping our members updated on latest global trends, especially those influencing Sri Lanka, 'Evolving Landscape' section was added to the MEU. This section guide our members in strategic planning, innovation and competitiveness and helping them identify sector-specific opportunities and challenges.

Market-Implied Six-Month-Forward Policy Rate
(Five-day moving average, percentage points)



Sources: Bloomberg Finance L.P.; and IMF staff calculations.
Note: The EM group comprises Chile, China, Colombia, India, Malaysia, Mexico, Poland, South Africa, and Thailand; EM = emerging markets. GFSR = *Global Financial Stability Report.*

Financial Conditions Index
(Number of standard deviations from the mean)



Sources: Bloomberg Finance L.P.; Dealogic; EUROPACE AG/Haver Analytics; national data sources; and IMF staff calculations.
Note: GFSR = *Global Financial Stability Report.*

Despite these challenges, there are pockets of resilience. The U.S. economy continues to demonstrate robust momentum, with strong consumption and labor market conditions supporting growth. However, the elevated valuations of U.S. equities and risk assets highlight potential vulnerabilities. An abrupt shift in investor sentiment could lead to sharp repricing, tightening financial conditions, and exacerbating vulnerabilities in more fragile economies. Policymakers must navigate this complex environment with caution. Advanced economies should prioritize inflation control while avoiding financial market overheating. Emerging markets need to strengthen fiscal frameworks, enhance resilience to external shocks, and attract stable capital inflows. The role of international coordination in addressing systemic risks and promoting financial stability cannot be overstated.

Data Source: IMF

The Ceylon Chamber of Commerce

ECONOMIC REVIEW AND OUTLOOK 2025

Consolidating Stability, Fostering Sustainable Growth

Seminar and Publication Launch

Join us for the Seminar as we cover global and local economic reviews, industry sector analysis and outlook, policy directions and private sector perspectives for 2025

The Forum will also see the launch of 'Outlook 2025' - the annual flagship publication of the Economic Intelligence Unit of the Ceylon Chamber

Members: LKR 2,500 | Non-Members: LKR 3,500
(inclusive of taxes)

7th | February 2025

08:30 AM- 10:30 AM

Ground Floor Auditorium,
The Ceylon Chamber of Commerce

Scan to Register

Keynote Speaker

Dr. P. Nandalal Weerasinghe
Governor of the
Central Bank of Sri Lanka

Opening Remarks

Mr Duminda Hulangamuwa
Chairman
The Ceylon Chamber of Commerce

Moderator

Mr. Sanjaya Ariyawansa
Senior Economist
The Ceylon Chamber of Commerce

Panelists

Mr. Bingumal Thewarathanthri
Chairman Sri Lanka Banks Association
MD/Chief Executive Officer at Standard Chartered

Dr. Chandranath Amarasekara
Assistant Governor at Central Bank of Sri Lanka

Mr. Romesh David
CEO of South Asia Gateway Terminals

Dr. Shruti Lakhtakia
Economist at The World Bank Sri Lanka Office

Ms. Ruvini Fernando
Head of Strategy, Risk and Transactions Services
Deloitte Sri Lanka and Maldives

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