

PART II

PART II

ACCOUNTS AND OPERATIONS OF THE CENTRAL BANK OF SRI LANKA

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1. ACCOUNTS AND FINANCE

Activity Report of the Monetary Board Advisory Audit Committee during and relating to the Financial Year 2018

1. Introduction

Monetary Board Advisory Audit Committee (AAC) is a subcommittee appointed by the Monetary Board. The AAC advises the Monetary Board on policies and matters relating to the financial reporting, internal controls, risk management systems, compliance, whistleblowing, fraud, internal audit, external audit and any other matter assigned by the Monetary Board. The AAC reports its performance and recommendations to the Monetary Board on a quarterly basis and as and when necessary.

2. Composition of AAC

The AAC is chaired by an appointed member of the Monetary Board and comprised of two other external audit professionals. The composition of the AAC as at 31.12.2018 was as follows:

- | | | |
|--------------------------|---|----------|
| i. Mr. A N Fonseka | - | Chairman |
| ii. Mr. H M A Jayasinghe | - | Member |
| iii. Mrs. A I Mohotti | - | Member |

The Secretary to the Monetary Board is the Secretary to the AAC and the Director of the Internal Audit Department is the Assistant Secretary to the AAC. The Internal Audit Department (IAD) provides secretarial facilitation to the AAC. The Audit Superintendent from the National Audit Office in charge of the external audit of the Central Bank of Sri Lanka (CBSL), the Chief Accountant and the Compliance Officer of the CBSL attend the AAC meetings as observers. Heads of Department of the CBSL are invited by the Chairman of the AAC as and when necessary for discussion. The engagement partner of KPMG, being the Audit Firm appointed by the Auditor General to carry out the external audit also attends when the financial statements of the CBSL are discussed.

AAC is required to meet at least six (06) times a year or as may be decided by the Chairman of the AAC or as directed by the Monetary Board. Meetings of the AAC are convened by the Secretary to the Committee. A quorum for a meeting is two (02) including the Chairman.

3. Activities carried out during and relating to the financial year 2018

The AAC held eight (08) meetings in 2018 and major activities carried out are indicated below.

a) Financial reporting and external Audit:

AAC reviewed,

- i. the Report of the Auditor General on the Financial Statements of the CBSL for the year 2016,
- ii. the Interim Issues Memorandum on the audit of Financial Statements of the CBSL for the period ended 30.09.2017, Management Letter for the year 2017, the responses of the management thereto and the recommendations of the External Auditor,
- iii. the Audit Plan of KPMG for the year 2018,
- iv. the Interim Issues Memorandum on the audit of Financial Statements of the CBSL for the period ended 31.12.2018 and
- v. the Financial Statements of the CBSL for the year 2018.

b) Internal controls and risk management systems:

AAC,

- i. reviewed and advised on internal controls and risk management systems of the CBSL.
- ii. reviewed the implementation progress of the AAC recommendations by the respective Heads of Department.

c) Internal Audit:

AAC,

- i. reviewed the progress of the implementation of the internal audit plan of 2018.
- ii. reviewed the implementation status of the recommendations made by IAD through Audits.
- iii. reviewed the internal audit plan for 2019.
- iv. reviewed and amended the audit results communication methodology.
- v. reviewed the staff requirement of IAD.

Central Bank of Sri Lanka

Management Statement

For the period ended 31 December 2018

Accountability and the Financial Performance of the Central Bank of Sri Lanka in relation to the Objectives

The Central Bank was established as the authority responsible for the administration, supervision and regulation of the monetary, financial and payment systems of Sri Lanka under the Monetary Law Act. In accordance with this Act, the Bank is charged with the responsibility of securing the core objectives of economic and price stability and financial system stability.

The basis of accountability for the Central Bank and the success of its operations therefore would be the effectiveness of its policies and operations leading towards the achievement of its core objectives and not necessarily its profitability. These statutory objectives are the fundamental features that distinguish the Central Bank from any other entity, private or public. Accordingly, profitability related approach, if adopted by the Central Bank, could result in the Bank pursuing profits while compromising its core objectives, since it has the unique ability to create its own profits through its monetary policy activities, which could influence interest rates and exchange rates. It therefore

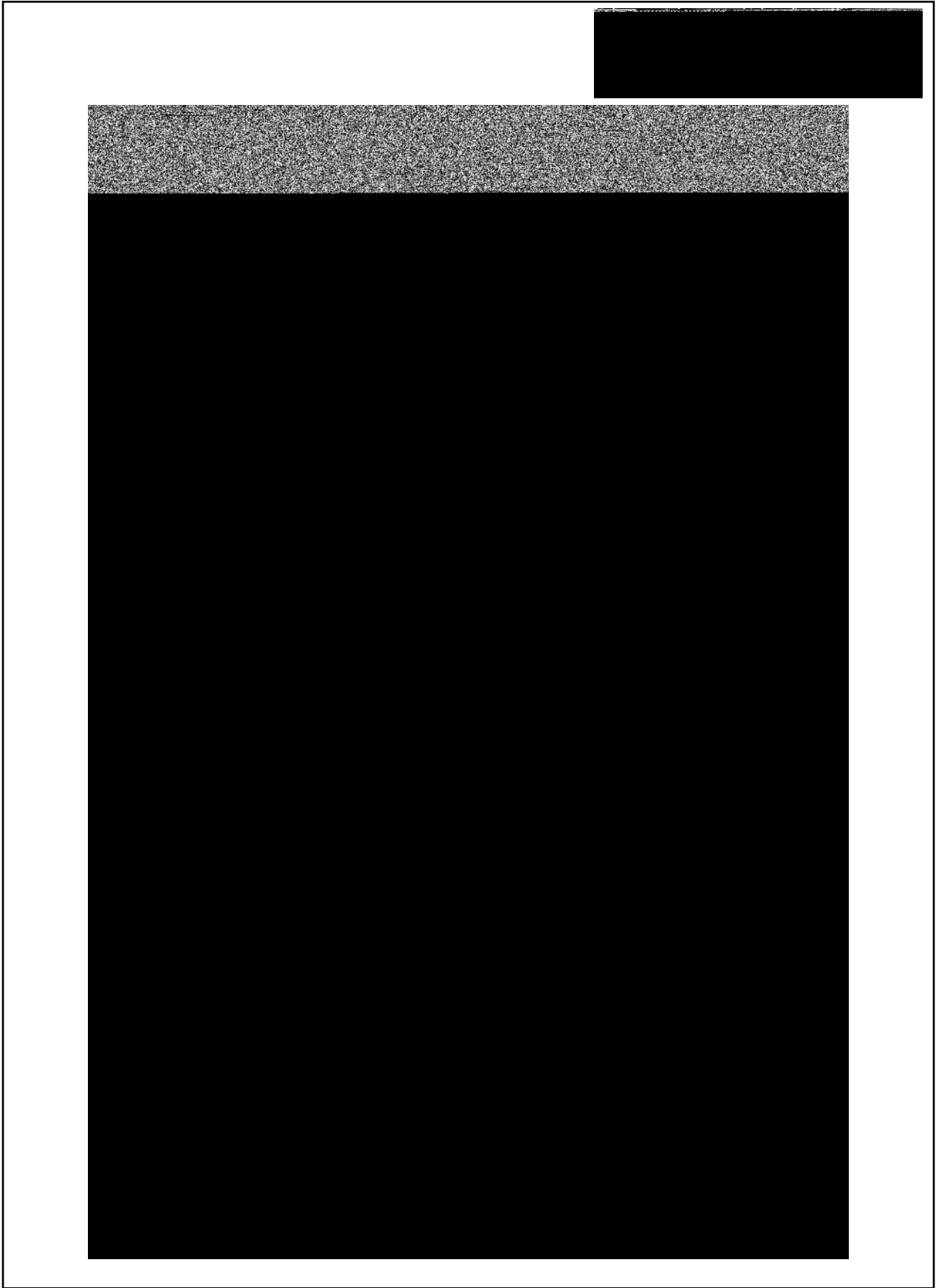
follows that the Central Bank's objectives of economic and price stability and financial system stability need to be distinguished and detached from the pure profitability objective which should essentially be incidental or academic only.

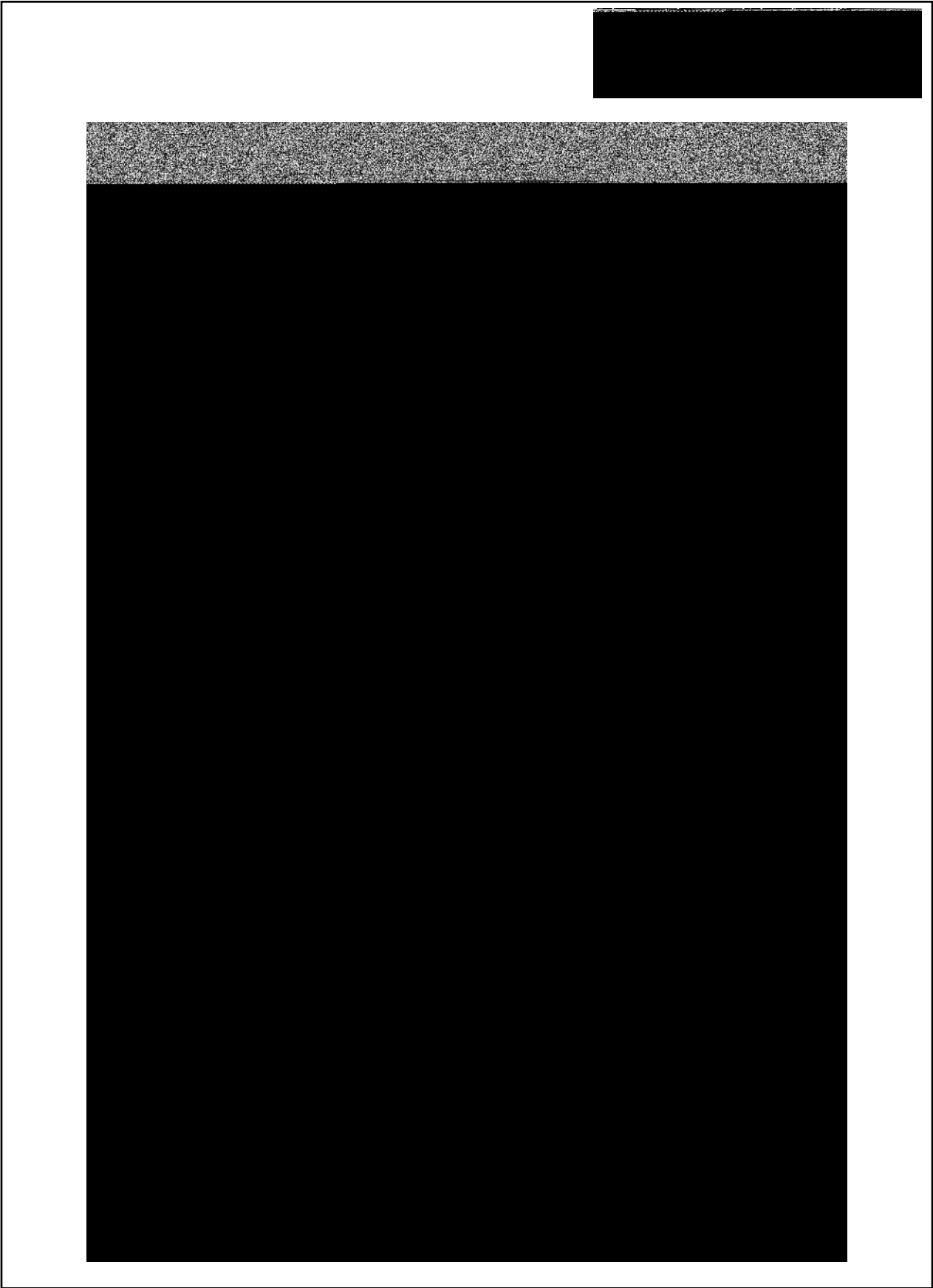
In this background, the Central Bank's financial statements record gains and/or deficits in the implementation of its monetary policy operations, exchange rate management, issuing of currency, etc. at the values as realized and hence, the financial performance as reported in these statements needs to be interpreted and understood in that context.

The Bank is subject to an external audit by the Auditor General under the Monetary Law Act sections 42 & 43. The Auditor General in turn has obtained the services of a firm of Chartered Accountants, M/s KPMG, to carry out an audit under International Standards of Auditing to ensure compliance with the International Financial Reporting Standards.

BAF/H/CBSL/1/18/1

03 April 2019





Central Bank of Sri Lanka

Statement of Financial Position

As at 31 December

Assets**Foreign Currency Financial Assets**

| | Note | 2018 Rs. 000 | 2017 Rs. 000 |
|--|------|-----------------|-----------------|
| Cash & Cash Equivalents | 9 | 372,175,176 | 459,827,641 |
| Securities at Fair Value through Profit or Loss | 10 | 37,467,239 | 45,264,376 |
| Securities at Fair Value through Other Comprehensive Income/Available for Sale | 10 | 694,876,394 | 566,228,935 |
| Derivative Financial Instruments | 11 | 750 | 4,940,455 |
| IMF Related Assets | 12 | 147,427,452 | 126,842,946 |
| Other Receivables | | 961,284 | 3,665,700 |

Total Foreign Currency Financial Assets**Local Currency Financial Assets**

| | | | |
|--|----|-------------|-------------|
| Sri Lanka Government Securities | 13 | 45,031,157 | 9,704,962 |
| Securities Purchased under Resale Agreements | 14 | 229,454,409 | 22,375,124 |
| Provisional Advances to Government | 15 | 198,632,571 | 199,800,871 |
| Loans to Banks | 16 | 95,963 | 223,702 |
| Equity Investments in Financial and Other Institutions | 17 | 1,381,879 | 41,095 |
| Other Assets | 18 | 14,783,305 | 12,882,470 |

Total Local Currency Financial Assets**Total Financial Assets****Foreign Currency Non-Financial Assets**

| | | | |
|------|----|-------------|-------------|
| Gold | 19 | 149,683,439 | 126,583,727 |
|------|----|-------------|-------------|

Non-Financial Assets

| | | | |
|-----------------------------------|----|------------|------------|
| Inventories | 20 | 6,568,935 | 6,875,533 |
| Other Receivables and Prepayments | | 1,914,087 | 1,534,848 |
| Property, Plant and Equipment | 21 | 16,955,854 | 17,960,517 |
| Intangible Assets | 22 | 30,437 | 80,623 |

Total Non-Financial Assets**Total Assets****Liabilities and Equity****Foreign Currency Financial Liabilities**

| | | | |
|----------------------------------|----|-------------|-------------|
| Banks and Financial Institutions | 23 | 19,301,160 | 8,239,544 |
| Derivative Financial Instruments | 11 | 14,056,460 | 4,648,449 |
| Asian Clearing Union | 24 | 79,158,977 | 90,981,712 |
| International Monetary Fund | 25 | 416,988,246 | 318,995,269 |
| Others | 26 | 134,730,933 | 64,095,889 |

Total Foreign Currency Financial Liabilities**Local Currency Financial Liabilities**

| | | | |
|--|----|-------------|-------------|
| Deposits of Banks and Financial Institutions | 27 | 320,106,183 | 341,712,198 |
| Deposits of Government and Governmental Entities | 28 | 348,718 | 324,517 |
| Securities Sold Under Repurchase Agreements | 29 | 28,311,221 | 40,655,278 |
| Balances of Employee Benefit Plans | 30 | 18,333 | 4,547 |
| Currency in Circulation | 31 | 640,942,510 | 598,053,901 |
| Other Payables | 32 | 12,606,431 | 8,887,156 |

Total Local Currency Financial Liabilities**Total Financial Liabilities****Other Liabilities**

| | | | |
|---|----|------------|---------|
| Deferred Grants | 33 | 11 | 45 |
| Pension and Other Post Employment Benefit Plans | 34 | 12,016,804 | 671,061 |
| Miscellaneous Liabilities and Accruals | 35 | 85,945 | 211,720 |

Total Other Liabilities**Total Liabilities****Equity**

| | | | |
|---------------|----|-------------|------------|
| Capital Funds | | 50,000,000 | 50,000,000 |
| Reserves | 36 | 188,768,399 | 77,352,239 |

Total Equity**Total Liabilities and Equity**

| | | | |
|--|--|---------------|---------------|
| | | 1,742,287,579 | 1,451,798,277 |
| | | 489,379,284 | 245,028,224 |
| | | 1,742,287,579 | 1,451,798,277 |
| | | 1,917,440,331 | 1,604,833,525 |
| | | 1,917,440,331 | 1,604,833,525 |

The accounting policies and notes on pages 11 through 70 form an integral part of the Financial Statements.

The Governor and the Chief Accountant of the Central Bank of Sri Lanka authorised these Financial Statements for issue on 29th March 2019 for and signed on behalf of the Monetary Board.

Dr. Indrajit Coomaraswamy – Governor

U.L. Muthugala - Chief Accountant

Central Bank of Sri Lanka

Statement of Income

| For the year ended 31 December | Note | 2018 Rs. 000 | 2017 Rs. 000 |
|---|------|---------------------|---------------------|
| Operating Income : | | | |
| Income from Foreign Currency Financial Assets | | | |
| Interest Income | 38 | 25,556,932 | 22,914,716 |
| Gain/(Loss) from Unrealized Price Revaluations | 39 | (18,259,956) | 24,000,475 |
| Gain/(Loss) from Realized Price Changes | | (4,092,390) | 2,772,209 |
| Total Income from Foreign Currency Financial Assets | | 3,204,586 | 49,687,400 |
| Expenses on Foreign Currency Financial Liabilities | | | |
| Interest Expense | 40 | (5,350,155) | (2,963,231) |
| Expected Credit Losses on Foreign Currency Financial Assets | 41 | (19,121) | - |
| Total Expenses on Foreign Currency Financial Liabilities | | (5,369,276) | (2,963,231) |
| Net Foreign Exchange Revaluation Gain/(Loss) | | 146,854,048 | (3,808,147) |
| Foreign Currency Investment Income | | 144,689,358 | 42,916,022 |
| Income from Local Currency Financial Assets | | | |
| Interest Income | 38 | 8,956,322 | 18,501,748 |
| Gain from Realised Price Changes | | 117,771 | 267,180 |
| Interest Expense | 40 | (2,880,220) | (2,676,116) |
| Expected Credit Losses on Local Currency Financial Assets | 41 | (10,966) | - |
| Total Income from Local Currency Financial Assets | | 6,182,907 | 16,092,812 |
| Other Income | 42 | 1,692,994 | 1,602,664 |
| Total Net Operating Income | | 152,565,259 | 60,611,498 |
| Operating Expenses: | | | |
| Personnel Expenses: | 43 | | |
| — Salaries and Wages | | (5,409,137) | (4,112,349) |
| — Defined Contribution Plan Costs | | (1,536,049) | (610,489) |
| — Contribution to Post Employment Benefit Plan Costs | | (205,147) | (744,356) |
| | | (7,150,333) | (5,467,194) |
| Depreciation & Amortization | | (498,189) | (518,716) |
| Cost of Inventory (Cost of new currency issue) | | (3,999,000) | (2,850,823) |
| Administration and Other Expenses | 44 | (1,850,083) | (1,305,649) |
| Impairment Charges on Assets | | (20,650) | (274,773) |
| Total Operating Expenses | | (13,518,255) | (10,417,155) |
| Profit Before Tax | | 139,047,004 | 50,194,343 |
| Tax | 45 | (1,119,286) | (1,837,976) |
| Profit for the Year | | 137,927,718 | 48,356,367 |

Figures in brackets indicate deductions

The accounting policies and notes on pages 11 through 70 form an integral part of the Financial Statements.

Central Bank of Sri Lanka

Statement of Other Comprehensive Income

As at 31 December

| | 2018 Rs. 000 | 2017 Rs. 000 |
|--|--------------------|-------------------|
| Profit for the Year | 137,927,718 | 48,356,367 |
| Other Comprehensive Income (OCI) | | |
| Items that are or may be re-classified subsequently to Profit/(Loss) | | |
| Net Fair Value Loss on Securities at Fair Value through Other Comprehensive Income/ Available for Sale | (877,778) | (6,843,970) |
| Net Fair Value Gain on Government Securities at Fair Value through Other Comprehensive Income | 5,259 | - |
| Expected Credit Losses on FVOCI Investments | (1,939) | - |
| Items that will not be re-classified subsequently to Profit/(Loss) | | |
| Post-Employment Benefit Plan Cost Recognized in Other Comprehensive Income | (11,823,458) | 1,741,622 |
| Net Fair Value Gain on Equity Investments at Fair Value through Other Comprehensive Income | 122,747 | - |
| Total Comprehensive Income | 125,352,549 | 43,254,019 |

Figures in brackets indicate deductions

The accounting policies and notes on pages 11 through 70 form an integral part of the Financial Statements.

Central Bank of Sri Lanka

Statement of Changes In Equity

For the year ended 31 December

| | Contributed Capital Rs. 000 | Revaluation Reserve Rs. 000 | Other Reserves (Note 36) Rs. 000 | Retained Earnings Rs. 000 | Total Rs. 000 |
|---|-----------------------------------|-----------------------------------|---|---------------------------------|--------------------|
| Balance as at 1 January 2017 | 50,000,000 | 9,022,907 | 30,530,509 | (3,910,215) | 85,643,201 |
| Net Profit for the year | - | - | - | 48,356,367 | 48,356,367 |
| Transfer to RTGS Sinking Fund | - | - | 273,918 | (273,918) | - |
| Post Employment Benefit Plans cost recognized in Other Comprehensive Income | - | - | - | 1,741,622 | 1,741,622 |
| Transfer of Net Foreign Exchange Revaluation Loss (IRR) | - | - | (3,808,147) | 3,808,147 | - |
| Transfer to CBSL Specific Reserve | - | - | - | (166,388) | (166,388) |
| Net Fair Value Loss on Available for Sale Securities | - | - | (6,843,970) | - | (6,843,970) |
| Transfer of Funds from Retained Earnings to Market Revaluation Reserve | - | - | 14,028,792 | (14,028,792) | - |
| Transfer to General Reserve | - | - | 7,462,613 | (7,462,613) | - |
| Profit appropriation for the year 2016 - Recovery of outstanding GOSL obligations from 2016 profit | - | - | - | (1,378,272) | (1,378,272) |
| Transfer of Funds to CBSL Employees and Pensioners Distress Relief Fund | - | - | - | (321) | (321) |
| Transfer to Reserve for funding purposes of Post-Employment Benefits | - | - | 689,025 | (689,025) | - |
| Balance as at 31 December 2017 | 50,000,000 | 9,022,907 | 42,332,740 | 25,996,592 | 127,352,239 |
| Transition Adjustment on IFRS 9 Reclassification Impact | - | - | 1,287,347 | - | 1,287,347 |
| Transition Adjustment for Expected Credit Losses on FVOCI Investments | - | - | 65,588 | (117,160) | (51,572) |
| Adjusted Balance as at 1 January 2018 | 50,000,000 | 9,022,907 | 43,685,675 | 25,879,432 | 128,588,014 |
| Net Profit for the year | - | - | - | 137,927,718 | 137,927,718 |
| Transfer to RTGS Sinking Fund | - | - | 291,983 | (291,983) | - |
| Post Employment Benefit Plans cost recognized in Other Comprehensive Income | - | - | - | (11,823,458) | (11,823,458) |
| Transfer of Net Foreign Exchange Revaluation Gain (IRR) | - | - | 146,854,048 | (146,854,048) | - |
| Transfer of funds to Technical Advancement Reserve | - | - | 2,000,000 | (2,000,000) | - |
| Transfer to CBSL Specific Reserve | - | - | - | (171,843) | (171,843) |
| Net Fair Value Loss on Fair Value through Other Comprehensive Income | - | - | (877,778) | - | (877,778) |
| Transfer of Funds from Retained Earnings to Market Revaluation Reserve | - | - | 24,337,841 | (24,337,841) | - |
| Transfer of Funds to General Reserve | - | - | 5,013,869 | (5,013,869) | - |
| Profit appropriation for the year 2017 - Recovery of outstanding GOSL obligations from 2017 profit | - | - | - | (15,000,000) | (15,000,000) |
| Transfer of Funds to CBSL Employees and Pensioners Distress Relief Fund | - | - | - | (321) | (321) |
| Transfer to Reserve for funding purposes of Post-Employment Benefits | - | - | 5,372,178 | (5,372,178) | - |
| Disposal Gain on Equity Investments Classified at Fair Value through Other Comprehensive Income | - | - | (16,289) | 16,289 | - |
| Gain on Market Valuation of Government Securities Classified at Fair Value through Other Comprehensive Income | - | - | 5,259 | - | 5,259 |
| Gain on Market Revaluation of Equity Investments Classified at Fair Value through Other Comprehensive Income | - | - | 122,747 | - | 122,747 |
| Expected Credit Losses on FVOCI Investments | - | - | (1,939) | - | (1,939) |
| Transfer to Retained Earnings | - | - | (21,154,178) | 21,154,178 | - |
| Balance as at 31 December 2018 | 50,000,000 | 9,022,907 | 205,633,416 | (25,887,924) | 238,768,399 |

Figures in brackets indicate deductions

The accounting policies and notes on pages 11 through 70 form an integral part of the Financial Statements.

Central Bank of Sri Lanka

Statement of Cash Flows

For the year ended 31 December

Cash Flows from Operating Activities

Receipts:

Interest Received - Foreign Currency
Interest Received - Local Currency - Others
Liquidity Management and Trading Income
Realised Exchange Loss
Other Income Received

Disbursements:

Interest Paid - Foreign Currency
Interest Paid - Local Currency
Payments to Employees
Payments to Suppliers
Tax Paid

Net Cash Flows used in Operating Activities

Cash Flows from Investing Activities

Receipts:

Net Increase in Other Local Currency Financial Assets
Disposal/Redemption of Investments in Financial & Other Institutes
Principal Recoveries from Loans and Advances to Other Institutions
Disposal/Redemption of Investments in Debentures
Proceeds on disposal of Property, Plant and Equipment
Net Decrease in Securities Purchased under Resale Agreements

Disbursements:

Net Increase in Foreign Currency Securities
Net Increase/(Decrease) in Other Foreign Currency Financial Assets
Net Increase/(Decrease) in Other Foreign Currency Financial Liabilities
Net Decrease in Other Local Deposits and Payables
Purchase of Property, Plant and Equipment net of Grants
Purchase of Intangible Assets
Net Decrease in Gold Inventory
Loans and Advances Granted to Other Institutions

Net Cash Flows generated from/(used in) Investing Activities

Cash Flows from Financing Activities

Receipts :

Issue of Circulating Currency
Withdrawal of Circulating Currency
Net Issue of Circulating Currency

Disbursements:

Net Issues/(Withdrawals) of Circulating Currency on Government Transactions
Net Issues/(Withdrawals) of Circulating Currency on Transactions with Banks and Financial Institutions
Net Issues/(Withdrawals) of Circulating Currency

Net Increase/(Decrease) in Circulating Currency

Disbursements:

Repayment of Foreign Currency Term Liabilities
Payments to Other Funds
Payments to Pension Fund
Transfer of Profits to Consolidated Fund

Net Cash Flows from Financing Activities

Net Increase/(Decrease) in Cash and Cash Equivalents

Exchange Rate Effect on Cash and Cash Equivalents
Cash and Cash Equivalents at the Beginning of the Year

Cash and Cash Equivalents as at 31 December

| Note | 2018 Rs. 000 | 2017 Rs. 000 |
|------|-----------------|-----------------|
| | 25,346,571 | 24,380,250 |
| | 821,348 | 843,143 |
| | (3,974,618) | 2,772,208 |
| | (9,065,597) | (14,514,115) |
| | 1,605,833 | 1,607,790 |
| | 14,733,537 | 15,089,276 |
| | 4,855,646 | 2,740,357 |
| | 2,368,605 | 2,679,274 |
| | 6,765,420 | 5,245,612 |
| | 3,380,162 | 4,823,628 |
| | 1,100,219 | 902,864 |
| | 18,470,052 | 16,391,735 |
| 46 | (3,736,515) | (1,302,459) |
| | (2,487,565) | (1,524,155) |
| | 19,789 | - |
| | 127,584 | 487,927 |
| | 15,178 | - |
| | 10,284 | 3,088 |
| | (12,340,173) | (29,394,318) |
| | (14,654,903) | (30,427,458) |
| | 5,592,252 | 211,673,611 |
| | (263,842) | 355,012 |
| | (34,064,176) | 60,818,636 |
| | (14,311) | (155) |
| | 104,362 | 265,725 |
| | 25,484 | 7,432 |
| | (19,060,015) | - |
| | - | 369,684 |
| | (47,680,246) | 273,489,945 |
| | 33,025,343 | (303,917,403) |
| | 796,515,572 | 628,828,164 |
| | (753,626,964) | (583,552,128) |
| | 42,888,608 | 45,276,036 |
| 47 | 233,216,924 | (220,649,290) |
| 48 | 23,010,511 | (38,460,908) |
| | 256,227,435 | (259,110,198) |
| | (213,338,827) | 304,386,234 |
| | (39,813,671) | (28,666,576) |
| | 321 | 321 |
| | - | 261,625 |
| | 14,227,097 | - |
| | (25,586,253) | (28,404,630) |
| | (187,752,574) | 332,790,864 |
| | (158,463,746) | 27,571,002 |
| | 70,882,845 | 8,472,902 |
| | 459,827,641 | 423,783,737 |
| 9 | 372,246,740 | 459,827,641 |

Figures in brackets indicate deductions

The accounting policies and notes on pages 11 through 70 form an integral part of the Financial Statements.

Central Bank of Sri Lanka

Notes to the Financial Statements

For the year ended 31 December 2018

1. REPORTING ENTITY AND STATUTORY BASE

The Central Bank of Sri Lanka ("Bank" or "CBSL") is an institution established under the Monetary Law Act No. 58 of 1949 of Sri Lanka as amended ("MLA"), as the authority responsible for the administration, supervision and regulation of monetary, financial and payment system of Sri Lanka. The Bank is domiciled in the Democratic Socialist Republic of Sri Lanka and situated at No: 30, Janadhipathi Mawatha, Colombo 01.

These financial statements were authorised for issue by the Governor and Chief Accountant for and on behalf of the Monetary Board on 29th March 2019.

1.1 Principal Activities

The Monetary Board of the CBSL is, in addition to determining the policies or measures authorized to be adopted or taken under Monetary Law Act No. 58 of 1949 of Sri Lanka as amended, vested with the powers, duties and functions of the CBSL and are generally responsible for the management, operations and administration of the Bank. The Bank is primarily responsible for the administration, supervision, regulation of monetary, financial and payment system of Sri Lanka and also acts as the fiscal agent of the Government. The activities of the bank mainly include:

- Implementing monetary and exchange rate policies.
- Issuing of currency.
- Facilitating free competition and stability in the financial system.
- Licensing and supervision of defined financial institutions.
- Organization and management of the inter-bank settlement system and promotion of the smooth functioning of the payment system.
- Providing loans and advances to the Government, bank and financial institutions under various facilities.
- Acting as a depository of the Government under specific arrangements with Government and agencies acting on behalf of the Government.

The activities carried out in order to achieve its objective of economic, price and financial system stability with a view to encouraging and promoting the development of the productive resources of Sri Lanka can be broadly segregated into foreign currency and local currency activities. Results of these activities are taken to Operating Activities in the context of the Statement of Income.

2. BASIS OF PRESENTATION OF FINANCIAL STATEMENTS

2.1 Statement of Compliance

These financial statements of the Bank for the year ended 31 December 2018 have been prepared in accordance with International Financial Reporting Standards (IFRS).

This is the first set of the Financial Statements presented after the first time adoption of IFRS 9 – "Financial Instruments" and IFRS 15 – "Revenue from Contracts with Customers". Changes to significant accounting policies are described in Note 4.

2.2 Basis of Measurement

The financial statements are prepared on the historical cost basis, except for the following,

- Gold is measured at fair value through profit or loss (FVTPL).
- Derivative financial instruments and non-derivative financial instruments held at fair value through profit or loss (FVTPL) and fair value through other comprehensive income (FVOCI) are measured at fair value.
- Land and buildings are measured at cost at the time of acquisition and subsequently at revalued amounts less accumulated depreciation and impairment losses.
- Liability for defined benefit obligations is measured as the present value of the defined benefit obligation less the fair value of the plan assets.

2.3 Reporting Format

The Bank presents financial assets and financial liabilities, and their associated income and expense streams, by distinguishing between foreign currency and local currency operations. In the Statement of Financial Position, assets and liabilities are presented broadly in order of liquidity within such distinguished categories. The Bank considers that this reporting approach provides appropriate reporting of the Bank's activities which are more fully described in Note 7.

2.4 Functional and Presentation Currency

The Financial Statements are presented in Sri Lankan Rupees (LKR), which is the Bank's functional currency. Financial information presented in Sri Lankan Rupees has been rounded to the nearest thousand. There was no change in the Bank's presentation and functional currency during the year under review.

2.5 Materiality and Aggregation

Each material class of similar item is presented separately in the Financial Statements. Items of dissimilar nature or function are presented separately unless they are immaterial.

2.6 Offsetting

Financial assets and liabilities are offset and the net amount presented in Statement of Financial Position when, and only when, the Bank has a legal right to set off the recognized amounts and it intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.

2.7 Comparative Information

The comparative information is reclassified whenever necessary to conform with the current year's presentation.

3. USE OF ESTIMATES AND JUDGMENTS

The preparation of the Bank's financial statements requires management to make judgements, estimates and assumptions that affect the reported amount of revenues, expenses, assets and liabilities, and the accompanying disclosures, as well as the disclosure of contingent liabilities.

Uncertainty about these assumptions and estimates could result in outcomes that require a material adjustment to the carrying amount of assets or liabilities affected in future periods.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to estimates are recognized prospectively. Information about judgements made in applying accounting policies that have the most significant effects on the amounts recognized in the financial statements are described in the following notes.

3.1 Classification and Impairment of Financial Assets (Applicable from 1 January 2018)

The Bank used judgements when assessing the business model within which the assets are held and whether the contractual terms of the financial assets are Solely Payment of Principal and Interest (SPPI) on the principal amount of the outstanding. The Bank also used judgements when establishing the criteria for determining whether credit risk on the financial assets has increased significantly since initial recognition, determining methodology for incorporating forward looking information into measurement of Expected Credit Losses (ECL) and selection and approval of models to measure ECL.

3.2 Pensions and Other Post Employment Benefit Plans

The cost of defined benefit plans is determined using an actuarial valuation. The actuarial valuation involves

making assumptions about discount rates, future compensation increases, mortality rates and future pension increases. Due to the long-term nature of these plans, such estimates are subject to significant uncertainty. Assumptions used in the actuarial valuation are disclosed in Note 34 to the Financial Statements.

3.3 Fair Value of Financial Instruments

Where the fair values of financial assets and financial liabilities recorded on the Statement of Financial Position cannot be derived from active markets, they are determined using a variety of valuation techniques that include the use of mathematical models. The inputs to these models are derived from observable market data where possible, but if this is not available, judgment is required to establish fair values. The judgments include considerations of liquidity and model inputs such as volatility for longer-dated derivatives.

4. CHANGES TO SIGNIFICANT ACCOUNTING POLICIES

There were no changes to the accounting policies and accounting policies adopted are consistent with those of the previous financial year, except for the IFRS 9 and IFRS 15 related policies mentioned in detail below.

4.1 IFRS 9 Financial Instruments

The financial statements of the Bank have been prepared based on the new accounting policies and methods which have been revised in line with the requirements of the IFRS 9 - Financial Instruments. The Bank complied with IAS 39, Financial Instruments: Recognition and Measurement up to 31 December 2017, in the preparation of its annual Financial Statements.

Changes to Classification and Measurement

IFRS 9 requires all financial assets, except equity instruments and derivatives, to be assessed based on a combination of the entity's business model for managing the assets and the instruments' contractual cash flow characteristics. The IAS 39 measurement categories of financial assets (fair value through profit or loss (FVTPL), available for sale (AFS), held to maturity, loans and receivables) have been replaced by:

- Financial Assets at amortized cost
- Debt Securities at Fair Value through Other Comprehensive Income (FVOCI), with gains or losses recycling through Statement of Income on derecognition
- Equity instruments at FVOCI, with no recycling of gains or losses through Statement of Income on derecognition
- Financial assets at fair value through profit or loss (FVTPL)

The accounting for financial liabilities remains largely the same as it was under IAS 39. The Bank's classification of its financial assets and liabilities and quantitative impact of applying IFRS 9 as at 1 January 2018 is disclosed in Note 8.

Changes to the Impairment Calculation

The adoption of IFRS 9 has changed the Bank's accounting for impairments on financial assets by replacing the incurred loss approach of IAS 39 with a forward-looking expected credit loss (ECL) approach. Detailed explanation of how the Bank has applied the impairment requirements of IFRS 9 is disclosed in Note 5.3.4

Transition

Changes in accounting policies resulting from the adoption of IFRS 9 have been applied retrospectively, except as described below:

- The Bank has not restated the comparative information for 2017 for financial instruments in the scope of IFRS 9. Therefore, the comparative information for 2017 is reported under IAS 39 and is not comparable to the information presented for 2018. Differences arising from the adoption of IFRS 9 have been recognized directly in retained earnings as of 1 January 2018 and are disclosed in Note 8 to these financial statements.
- The following assessments have been made on the basis of the facts and circumstances that existed at the date of initial application.
 - The determination of the business model within which a financial asset is held.
 - The designation of certain investments made in equity instruments as per the Section 105 A of the Monetary Law Act which are not held for trading as at FVOCI.

4.2 IFRS 15 – Revenue from Contracts with Customers

IFRS 15 establishes a comprehensive framework for determining, how much and when revenue is recognized. It replaced IAS 18 – "Revenue", IAS 11 – "Construction Contracts" and related interpretations. However, the timing or amount of the Bank's fee and commission income from contracts with customers was not impacted by the adoption of IFRS 15. Accordingly, there was no impact on adoption of the said standard.

5. SIGNIFICANT ACCOUNTING POLICIES

The accounting policies have been applied consistently by the Bank, except for the changes in accounting policies described in Note 4.

5.1 Foreign Currency Translations and Balances

Transactions in foreign currencies are translated to Sri Lankan Rupees at the rate of exchange prevailing at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated to Sri Lankan Rupees at the rate of exchange prevailing at the reporting date. The foreign currency translation gain or loss on monetary items are taken to the Statement of Income. For the purposes of retranslation, as at the reporting date, the following Sri Lankan Rupee exchange rates for major currencies were used:

| Currency | 2018 Rs. | 2017 Rs. |
|--------------------------------|-------------|-------------|
| 1 Australian Dollar | 128.8113 | 119.3796 |
| 1 Canadian Dollar | 134.0153 | 121.8598 |
| 1 Euro | 209.5593 | 183.1353 |
| 1 Japanese Yen | 1.6661 | 1.3580 |
| 1 Special Drawing Rights (SDR) | 253.5111 | 217.1608 |
| 1 Sterling Pound | 233.0792 | 206.5221 |
| 1 United States Dollar | 182.7499 | 152.8548 |
| 1 Chinese Yuan (Offshore) | 26.5988 | 23.4847 |

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction.

5.2 Fair Value Measurement

The Bank measures financial instruments, such as, foreign securities, derivatives and non-financial assets such as Gold, at fair value at each reporting date. The fair values of financial instruments measured at amortised cost are disclosed in Note 53.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either:

- In the principal market for the asset or liability, or
- In the absence of a principal market, in the most advantageous market for the asset or liability

The principal or the most advantageous market must be accessible by the Bank.

The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest. A fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

The Bank uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximizing the use of relevant observable inputs and minimizing the use of unobservable inputs.

All assets and liabilities for which fair value is measured or disclosed in the financial statements are categorised within the fair value hierarchy, described as follows, based on the lowest level input that is significant to the fair value measurement as a whole:

- Level 1 — Quoted (unadjusted) market prices in active markets for identical assets or liabilities
- Level 2 — Valuation techniques for which the lowest level input that is significant to the fair value measurement is directly or indirectly observable.
- Level 3 — Valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable.

For assets and liabilities that are recognised in the financial statements on a recurring basis, the Bank determines whether transfers have occurred between Levels in the hierarchy by re-assessing categorisation (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period.

5.3 Financial Assets and Financial Liabilities

The Bank presents financial assets and liabilities, and the associated income and expense streams, by distinguishing between foreign currency and local currency activities. Foreign currency activities mainly arise from the Bank's foreign reserves management function. Local currency activities mainly reflect the assets and liabilities associated with monetary policy implementation, issuing currency and banking activities.

The separate reporting of these activities is considered to provide a better presentation of the Bank's financial position, financial performance and risk profile. The Bank considers that the combined reporting of foreign and local currency activities would weaken the informational value of the financial statements.

5.3.1 Recognition and Initial Measurement

All financial assets and liabilities are initially recognised at cost, being the fair value of the consideration given and including acquisition charges associated with the investment. Subsequent measurement bases for individual line items of financial assets after initial recognition are described after the policies applicable from 01 January 2018. All regular way purchases and sales of financial assets and liabilities are recognised on the trade date respectively. Regular way purchases or sales are purchases

or sales of financial assets that require delivery of assets within the time frame generally established by regulation or convention in the market place.

5.3.2 (A) Classification

Policy applicable from 1 January 2018

Financial Assets

On initial recognition, Bank classifies the financial assets as measured at;

- Amortized Cost
- Fair Value through Other Comprehensive Income (FVOCI)
- Fair Value through Profit or Loss (FVTPL)

A financial asset is measured at amortized cost if it meets both of the following conditions and is not designated as at FVTPL

- The asset is held within a business model whose objective is to hold assets to collect contractual cash flows; and
- The contractual terms of the financial asset give rise on specified dates to cashflows that are Solely Payment of Principle and Interest.

A financial asset is measured at FVOCI only if it meets both of the following conditions and is not designated as at FVTPL.

- The asset is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets; and
- The contractual terms of the financial asset give rise on specified dates to cashflows that are Solely Payment of Principle and Interest.

On initial recognition of an equity investment that is not held for trading, the Bank may irrevocably elect to present subsequent changes in fair value in OCI. All other financial assets are classified as measured at FVTPL.

Business Model Assessment

The Bank makes an assessment of the objective of a business model in which an asset is held at a portfolio level because this best reflects the way the business is managed and information is provided to management. The information considered includes but not limited to:

- How the performance of the business model and the financial assets held within that business model are evaluated and reported to the entity's key management personnel.
- The risks that affect the performance of the business model (and the financial assets held within that business model) and, in particular, the way those risks are managed.

- The frequency, volume and timing of sales in prior periods, the reasons for such sales and its expectations about future sales activity. However, information about sales activity is not considered in isolation, but as part of an overall assessment of how the Bank's stated objective for managing the financial assets is achieved and how cash flows are realized.

Financial assets that are held for trading or managed and whose performance is evaluated on a fair value basis are measured at FVTPL because they are neither held to collect contractual cash flows nor held both to collect contractual cash flows and to sell financial assets.

Assessment of whether Contractual Cash Flows are Solely Payments of Principal and Interest

The Bank assesses the contractual terms of Financial Assets to identify whether they meet the SPPI test. For the purpose of this assessment, 'Principal' is defined as the fair value of the financial asset at initial recognition and "Interest" is defined as consideration for the time value of money and for the credit risk associated with the principal amount outstanding during a particular period of time and for other basic lending risks and costs.

The most significant elements of interest within a lending arrangement are typically the consideration for the time value of money and credit risk. To make the SPPI assessment, the Bank applies judgement and considers relevant factors such as the currency in which the financial asset is denominated, and the period for which the interest rate is set.

In contrast, contractual terms that introduce a more than the minimum exposure to risks or volatility in the contractual cash flows that are unrelated to a basic lending arrangement do not give rise to contractual cash flows that are solely payments of principal and interest on the amount outstanding. In such cases, the financial asset is required to be measured at FVTPL.

Reclassifications

Financial assets are not reclassified subsequent to their initial recognition, except in the period after the Bank changes its business model for managing financial assets.

5.3.2 (B) Classification

Policy applicable before 1 January 2018

Financial Assets

The Bank classified financial assets in one of the following categories under IAS 39,

- Loans and Receivables
- Held to Maturity
- Available for Sale or

- At fair value through profit or loss and within the category as,

- Held for Trading or
- Designated at fair value through profit or loss.

Financial Liabilities

The Bank classifies its financial liabilities, as measured at amortized cost.

5.3.3 Derecognition

Financial Assets

Bank derecognizes a financial asset when the contractual rights to the cash flows from the financial asset expire or it transfers the rights to receive the contractual cash flows in a transaction in which substantially all of the risks and rewards of ownership of the financial asset are transferred or in which the Bank neither transfers nor retains substantially all of the risks and rewards of ownership and it does not retain control of the financial asset.

On derecognition of a financial asset, the difference between the carrying amount of the asset (or the carrying amount allocated to the portion of the asset derecognised) and the sum of (i) the consideration received (including any new asset obtained less any new liability assumed) and (ii) any cumulative gain or loss that had been recognised in OCI is recognised in profit or loss.

From 1 January 2018 any cumulative gain/loss recognised in OCI in respect of equity investment securities designated as at FVOCI is not recognised in profit or loss on derecognition of such securities. Any interest in transferred financial assets that qualify for derecognition that is created or retained by the Bank is recognised as a separate asset or liability.

The Bank enters into transactions whereby it transfers assets recognized on its Statement of Financial Position, but retains either all or substantially all of the risks and rewards of the transferred assets or a portion of them. In such cases, the transferred assets are not derecognized. Examples of such transactions are securities lending and sale and repurchase transactions. In transactions in which the Bank neither retains nor transfers substantially all of the risks and rewards of ownership of a financial asset and it retains control over the asset, the Bank continues to recognize the asset to the extent of its continuing involvement, determined by the extent to which it is exposed to changes in the value of the transferred asset.

Financial Liabilities

The Bank derecognizes a financial liability when its contractual obligations are discharged or cancelled, or expired.

5.3.4 (A) Impairment of Financial Assets (Policy applicable from 1 January 2018)

The Bank recognises loss allowances for ECL on the following financial instruments that are not measured at FVTPL:

- Financial Assets at Fair Value through Other Comprehensive Income
- Financial Assets at Amortized Cost
- Credit guarantee contracts of Regional Development Department

No impairment loss is recognized on equity investments.

The Bank measures loss allowances at an amount equal to 12 months ECL for investments which are in investment grade (rated Baa3/BBB- and above). Majority of the investments of the bank which are classified as Fair Value through Other Comprehensive Income and Amortized cost are above Baa3/BBB- rate. Financial instruments for which a 12-month ECL is recognised are referred to as 'Stage 1 financial instruments'.

Life time ECL is calculated for those instruments which are below the investment grade at initial recognition or whose credit risk deteriorates below Baa3/BBB- or when a doubling of the probability of default has occurred after initial recognition. Financial instruments for which a lifetime ECL is recognised but which are not credit-impaired are referred to as 'Stage 2 financial instruments'. Life time ECL would also be computed for credit impaired assets which would be referred to as 'Stage 3 financial instruments'.

Measurement of ECL

The mechanism of the ECL calculations are outlined below with the key elements.

Probability of Default (PD): The Probability of Default is an estimate of the likelihood of default over a given time horizon. A default may only happen at a certain time over the assessed period, if the facility has not been previously derecognized and is still in the portfolio. The bank uses specific equity PD's of issuers/counterparties from Bloomberg for all its foreign investments at FVOCI and amortized cost and in the absence of equity PDs, the PD's applicable to the rating of the specific issuer/counterparty from the Bloomberg common PD table at a given reporting date.

Exposure at Default: The Exposure at Default is an estimate of the exposure at a future default date, taking into account expected changes in the exposure after the reporting date, including repayments of principal and interest, whether scheduled by contract or otherwise, expected draw downs on committed facilities and accrued interest from missed payments.

Loss Given Default (LGD): The Loss Given Default is an estimate of the loss arising in the case where a default occurs at a given time. It is based on the difference between the contractual cash flows due and those that the lender would expect to receive, including from the realisation of any collateral. The Bank has an approved internal policy in applying the LGD for different types of financial assets based on their risk exposure to the bank.

Economic Factor Adjustment: Bank uses the Economic Factor Adjustment for the conversion of Through the Cycle PD to Point in Time PD and the Bank mainly uses GDP data as the main economic factor in stimulating the PD.

Assessing the Significant Increase in Credit Risk (SICR)

Bank will consider that the financial instruments have significant increase in credit risk (SICR) when doubling of PD has occurred from initial recognition and any rating downgrade below BBB- after initial recognition. This is based on the observation that all ratings downgrades from an investment grade rating to a non-investment grade rating, including the marginal one notch downgrade from Baa3 to Ba1, results in a two-fold or greater increase of PD.

Credit-impaired financial assets

At each reporting date, the Bank assesses whether financial assets carried at amortized cost, at FVOCI, and credit guarantees, are credit-impaired (referred to as 'Stage 3 financial assets'). A financial asset is 'credit-impaired' when one or more events that have a detrimental impact on the estimated future cash flows of the financial asset have occurred. Evidence that a financial asset is credit-impaired includes the following observable data:

- significant financial difficulty of the borrower or issuer;
- a breach of contract such as a default or past due event;
- it is becoming probable that the borrower will enter bankruptcy or other financial reorganization

Presentation of allowance for ECL in the Statement of Financial Position

Loss allowances for ECL are presented in the Statement of Financial Position as follows:

- Financial assets measured at amortised cost: as a deduction from the gross carrying amount of the assets.
- Investments measured at FVOCI: no loss allowance is recognised in the Statement of Financial Position because the carrying amount of these assets is their fair value. However, the loss allowance is disclosed and is recognised in Other Comprehensive Income.
- Credit guarantee contracts: generally, as a provision.

Write-off

Loans and debt securities are written off (either partially or in full) when there is no reasonable expectation of recovering a financial asset in its entirety or a portion thereof. This is generally the case when the Bank determines that the borrower does not have assets or sources of income that could generate sufficient cash flows to repay the amounts subject to the write-off. This assessment is carried out at the individual asset level. Recoveries of amounts previously written off are included in 'impairment losses on financial instruments' in the Statement of Income and OCI.

5.3.4 (B) Impairment of Financial Assets (Policy applicable before 1 January 2018)

The Bank assessed at each reporting date whether a financial asset is impaired. If there was objective evidence that an impairment loss on loans and receivables carried at amortized cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate (i.e. the effective interest rate computed at initial recognition). The carrying amount of the asset shall be reduced either directly or through use of an allowance account. The amount of the loss shall be recognized in the Statement of Income.

The Bank first assessed whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. If it is determined that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, the asset is included in a group of financial assets with similar credit risk characteristics and that group of financial assets is collectively assessed for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognized are not included in a collective assessment of impairment.

If, in a subsequent period, the amount of the impairment loss decreased and the decrease can be related objectively to an event occurring after the impairment was recognized, the previously recognized impairment loss was reversed. Any subsequent reversal of an impairment loss was recognized in the Statement of Income, to the extent that the carrying value of the asset did not exceed its amortized cost at the reversal date.

If an Available for Sale asset was impaired, an amount comprising the difference between its cost (net of any principal payment and amortization) and its current fair value, less any impairment loss previously recognized in the Statement of Income, was transferred from equity to the Statement of Income. Reversals in respect of equity

instruments classified as available for sale were not recognized in profit. Reversals of impairment losses on debt instruments were reversed through the Statement of Income, if the increase in fair value of the instrument can be objectively related to an event occurring after the impairment loss was recognized in Statement of Income.

5.4 Financial Assets at Fair Value through Profit or Loss

Financial assets classified as held for trading are included in the category "securities at fair value through profit or loss". Upon initial recognition, attributable transaction costs are recognized in the Statement of Income as incurred. These securities are subsequently valued at quoted market prices. Changes in market values are recognised as an increase or decrease in the value of the securities in the Statement of Financial Position while resulting gains and losses are recognised in the Statement of Income.

Where the security is still owned, the gain or loss is reported as "Gain/(Loss) from Unrealised Price Revaluations". Where the gain or loss has been realised (through selling the security), it is reported as "Gain/(Loss) from realised Price Revaluations".

5.5 Financial Assets at Fair Value through Other Comprehensive Income

Investments at Fair Value through Other Comprehensive Income are non-derivative investments that are designated as Fair Value through other Comprehensive Income or are not classified as another category of financial assets. Investments at Fair Value through other Comprehensive Income comprise equity securities and debt securities.

Foreign and Local Currency debt securities at Fair Value through Other Comprehensive Income are subsequently valued at quoted market prices. Changes in market value are recognised as an increase or decrease in the value of the Investments at Fair Value through Other Comprehensive Income in the Statement of Financial Position.

The equity investments at Fair Value through Other Comprehensive Income are subsequently valued based on the Net Assets of the respective institutions due to the non-availability of quoted prices.

Gains and losses arising from changes in the market value of Foreign and Local Currency debt securities and Equity Investments at Fair Value through Other Comprehensive Income are recognised directly in equity (Other Comprehensive Income) which is shown under Other Reserves in the Statement of Financial Position until the investment is sold, collected or otherwise disposed of, or until the investment is determined to be impaired, at which time the cumulative gain or loss previously reported as equity is included in Statement of Income with the exception of fair value changes in equity investments which will not be recycled to Statement of Income upon

derecognition.

Interest income is recognised in Statement of Income using the effective interest method.

5.6 Instruments held at Amortized Cost

The items classified as Loans and Receivables and Held to Maturity instruments under IAS 39 are classified as Amortized Cost instruments under IFRS 9 and include loans given to banks/government and investments with fixed or determinable payments and fixed maturity that the bank has the positive intent and ability to hold to maturity. These instruments are subsequently measured at amortized cost using the effective interest method.

5.7 Derivative Instruments

The Bank uses derivatives such as cross currency swaps, currency options, forward foreign exchange contracts, for risk management purposes and not for speculative purposes. Derivatives are recorded at fair value and carried as assets when their fair value is positive and as liabilities when their fair value is negative. Changes in the fair value of derivatives are included in 'Gain/(Loss) from Unrealized Price Revaluations'.

When the transaction price differs from the fair value of other observable current market transactions in the same instrument, or based on a valuation technique whose variables include only data from observable markets, the bank immediately recognises the difference between the transaction price and fair value (a Day 1 difference) in 'Gain/(Loss) from Unrealized Price Revaluations'. In cases where fair value is determined using data which is not observable, the difference between the transaction price and model value is only recognised in the Statement of Income when inputs become observable, or when the instrument is derecognised.

5.8 International Monetary Fund (IMF) Related Balances

The Bank transacts with the International Monetary Fund (IMF) in its own right rather than as the depository of the Government of Sri Lanka. All transactions by the bank with the IMF have been included in these financial statements on that basis.

The bank records the quota with the IMF as an asset and the amount payable to the IMF for quota is recorded as a liability of the bank. The cumulative allocation of SDRs by the IMF is treated as a liability. All the IMF related assets and liabilities are recognized at amortised cost using the effective interest method. Exchange gains and losses arising on revaluation of IMF assets and liabilities at the exchange rate applying at reporting date as published by the IMF are recognised in the Statement of Income.

All other charges and interest pertaining to balances with the IMF are recorded immediately in the Statement of

Income.

5.9 Cash and Cash Equivalents

Cash and cash equivalents comprise cash at foreign banks and financial institutions, short-term deposits and highly liquid financial assets with original maturities of less than three months, which are subject to insignificant risk of changes in their fair value, and are used by the Bank in the management of its short-term commitments. Cash and cash equivalents are carried at amortized cost in the Statement of Financial Position.

As a part of local currency activities CBSL generates certain income and incurs expenses, which do not involve in movement of cash. Those activities result in certain assets and liabilities and mainly comprise of the transactions with the Government of Sri Lanka (GOSL) and transactions with domestic banks and financial institutions. Transactions with GOSL include the purchase of Treasury bills and bonds that are issued by the Government as a monetary policy mechanism. Such purchases, disposals or interest thereon are reflected as mere book entries in the records of CBSL. These are disclosed separately in Note 47 and Note 48 to the Financial Statements.

As the sole statutory authority, CBSL issues currency to the public in line with Monetary Law Act. Currency issued by CBSL represents a claim on the bank in favor of the holder. This is a liability on the part of the CBSL while it is an item of cash in the hands of the holder. Movement in circulation currency is included as part of financing activities in line with prevailing industry practices among those central banks which present cash flow statements.

CBSL through the cash/pay order process disburses cash in the form of notes and coins or cheques drawn on CBSL, to various drawees including suppliers and employees for goods and services obtained, which is either added to the currency in circulation liability or deposits by banks and financial institutions. Such forms of utilization of currency for the purposes of CBSL's payments form part of cash outflows of CBSL.

For the purposes of the Statement of Cash Flows, cash and cash equivalents consist of cash and cash equivalents as defined above, net of cash/pay order outflows.

5.10 Repurchase and Reverse-Repurchase Transactions

Securities sold under agreements to repurchase continue to be recorded as assets in the Statement of Financial Position. The obligation to repurchase (Securities Sold under Agreements to Repurchase) is recognised as a liability. The difference between the sale and repurchase price in repurchase transactions and the purchase price and sale price in reverse-repurchase transactions represents an expense and income respectively and recognised in the Statement of Income.

Securities held under reverse-repurchase agreements are recorded as an asset in the Statement of Financial Position (Securities Purchased under Resale Agreements). Both repurchase and reverse-repurchase transactions are reported at amortized cost inclusive of any accrued income or expense.

5.11 Standing Deposit and Lending Facilities

With effect from 1 February 2014, Standing Deposit Facility (former Standing Repurchase (Repo) Facility) was converted in to a 'clean deposit' with no allocation of collateral. Hence, participating institutions invest their excess funds in the Standing Deposit Facility as a clean deposit on daily basis at standing deposit facility rate.

The procedures of Standing Lending Facility (Formerly Standing Reverse Repurchase (Reverse Repo) Facility) are identical to the Standing Reverse Repurchase Facility and the both are recognized at amortized cost in the Statement of Financial Position.

5.12 CBSL Securities

The Bank issues CBSL Securities from time to time under its Monetary Policy operations to absorb excess liquidity in the market.

The securities issued are recorded as a liability. The difference between the issue price and the face value is recorded as an expense in the Statement of Income.

5.13 Sri Lanka Government Securities

Sri Lanka Government Securities consists of Treasury bills purchased from GOSL. Investments in Sri Lanka Government Securities is recorded in the Statement of Financial Position at Fair Value through Other Comprehensive Income.

5.14 Provisional Advances to Government

Advances to Government represents direct provisional advances made to GOSL under Section 89 of the Monetary Law Act No.58 of 1949 of Sri Lanka, as amended. These advances are subsequently measured at amortized cost.

5.15 Loans to Other Institutions

Loans granted to Other Institutions are recognized and carried at amortized cost.

5.16 Securities Borrowings and Securities Lending

Bank borrows Government Securities from time to time under its Monetary Policy operations from major institutional investors. The borrowed securities are used by the bank for repurchase operations to absorb excess liquidity in the market.

The securities borrowings is an unconditional blanket guarantee from the Bank for return of securities, payment

of agreed fee and on compensation at market rate (as per the market rates communicated to the primary market participants by the Public Debt Department of the Bank) in events of any failure in delivery.

The market values of the securities borrowed and not used for the repurchase operations at a particular time are recorded as a contingent liability. The commission paid is expensed on accrual basis.

Transfer of securities to counterparties under lending transactions is only reflected on the Statement of Financial Position if the risks and rewards of ownership are also transferred.

5.17 Staff Loans

Bank employees are entitled to loan facilities under concessionary interest rates. These loans which were granted from 2008 onwards are fair valued as per IFRS 9 using discounted cash flows.

Discount rate - The rate compiled by the Economic Research Department of CBSL (ERD) based on the long term inflation target on USD –Commercial Interest Reference Rate (CIRR) plus 1 per cent added for the risk premium as agreed by the Audit Committee of the Bank is used as the discount rate and it varies with the period of the loans.

The difference between the present value of the staff loan as at the end of a year and beginning of the year have been amortized yearly to record the expense incurred by the Bank in providing these loans at concessionary rates and equivalent amount is recorded as other income to record the income that would have been earned by the bank if these loans were granted at market rates.

Assumptions used for computation of fair valuation

- The date of staff loan granted is considered as 1 January.
- There were no amendments or early settlements.

5.18 Gold

Section 67 (1) of the Monetary Law Act which specifies the composition of the International Reserve indicates that gold may be held by the CBSL as part of this Reserve. Section 67 (2), Monetary Board is required to endeavor to hold at least a nuclear reserve in gold or currencies freely convertible by the Central Bank, whether directly or indirectly, in to gold as per the MLA. As this gold is part of the International Reserve and not used as a commodity which is traded during the normal course of business, gold is fair valued and the gains or losses are transferred to the Statement of Income. Prior to appropriation of profits, the unrealised gains from gold are transferred to

the relevant reserve account.

5.19 Inventories

5.19.1 Currency Inventory

Inventories of the Bank include new currencies that are not yet issued to the circulation. Cost related to production and design of new currency notes and coins are initially recognized at cost. Cost of new currency notes and coins which are issued to the circulation is determined on a weighted average basis and at the time of issue it is charged to Statement of Income. Allowance is made for slow moving inventories.

5.19.2 Other Inventories

Other inventories are carried at lower of cost and net realisable value. Cost is determined on a weighted average basis.

5.20 Property, Plant and Equipment

Property, Plant and Equipment excluding land & building are stated at cost, less accumulated depreciation and accumulated impairment in value. Such cost includes the cost of replacing part of such Property, Plant and Equipment when that cost is incurred if the recognition criteria are met. Land and buildings are measured at revalued amount, being their fair value at the date of revaluation, less any subsequent accumulated depreciation and subsequent accumulated impairment losses.

Except for the freehold land, depreciation is calculated on a straight-line method over the following estimated useful lives.

| Class of Asset | Useful Life |
|--------------------------------------|---|
| Buildings on Freehold Lands | Over 50 Years |
| Buildings on Lease hold lands | Lower of 50 years or over the lease hold period |
| Plant & Plant Integrals | 20 Years |
| Furniture & Equipment | 10 Years |
| Motor Vehicles | 5 Years |
| Motor Vehicles acquired 2014 onwards | 10 Years |
| Computer Hardware | 4 Years |
| Others | 3 Years |

The carrying values of Property, Plant and Equipment are reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable.

Policy for revaluation of Land & Building of the Bank is at least once in five years or at any shorter interval when a significant valuation adjustment becomes evident. Any revaluation surplus is credited to the Revaluation Reserve included in the equity section of the Statement of Financial

Position, except to the extent that it reverses a revaluation decrease of the same asset previously recognized in Statement of Income, in which case the increase is recognized in Statement of Income. A revaluation deficit is recognized in Statement of Income, except that a deficit directly offsetting a previous surplus on the same asset is directly offset against the surplus in the Revaluation Reserve. Upon disposal, any revaluation surplus relating to the particular asset being sold is transferred to retained earnings.

An item of Property, Plant and Equipment is de-recognized upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss arising on de-recognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in the Statement of Income in the year the asset is de-recognized. The asset's residual values, useful lives and methods are reviewed, and adjusted if appropriate, regularly.

Capital work-in-progress is stated at cost. These are expenses of a capital nature directly incurred in the construction of buildings, major plant and machinery and system development, awaiting capitalisation.

5.21 Intangible Assets

Computer software not integral to computer hardware are shown as intangible assets and recognized at cost. Following initial recognition these intangible assets are carried at cost less any accumulated amortization and accumulated impairment.

Subsequent expenditure on software assets is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is expensed as incurred.

Amortisation is recognised in the Statement of Income on a straight-line basis over the useful life of 4 years, from the date that it is available for use since this most closely reflects the expected pattern of consumption of the future economic benefits embodied in the asset.

5.22 Other Assets

Other assets are carried at expected realisable values.

5.23 Impairment of Non-Financial Assets

The Bank assesses at each end of reporting period if events or changes in circumstances indicate that the carrying value may be impaired, whether there is an indication that a non-financial asset may be impaired. If any such indication exists, the bank makes an estimate of the asset's recoverable amount. Where the carrying amount of an asset exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount. Impairment losses are recognized in the Statement of Income.

5.24 Provisions

Provisions are recognised when the Bank has a present obligation (legal or constructive) as a result of a past event and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Where the Bank expects a provision to be reimbursed, the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain.

5.25 Currency in Circulation

Currency issued by the Bank represents a claim on the bank in favour of the holder. The liability for Currency in Circulation is recorded at face value in the Statement of Financial Position.

5.26 Pension and Other Post Employment Benefit Plans

Pension and other Post Employment Benefit Plans operated by the bank are disclosed in Note 34.

5.27 Defined Benefit Plans

A defined benefit plan is a post employment benefit plan other than a defined contribution plan. Bank operates defined benefit schemes for Pension, Widows' and Orphans' Pensions (W&OP), Widowers' and Orphans' Pensions (WR&OP), Retirement Gratuity and Post Employment Medical Benefits. The Bank and eligible beneficiaries make contributions, to separately administered funds in respect of the first three schemes.

The cost of providing benefits under the defined benefit plans is determined separately for each plan using the projected unit credit actuarial valuation method. The Bank's obligation in respect of defined benefit plan is calculated separately for each plan by estimating the amount of future benefit that employees have earned in return for their service in the current and prior periods; that benefit is discounted to determine its present value. Any unrecognised past service costs and the fair value of any plan assets are deducted. The discount rate is the yield at the valuation date on Government Bonds that have maturity dates approximating to the average remaining years of service. All principal actuarial assumptions disclosed in Note 34 are revised only when a full actuarial valuation is performed.

5.28 Defined Contribution Plans

Employees are eligible for Employees' Provident Fund Contributions and Employees' Trust Fund Contributions in line with respective statutes and regulations. The bank contributes 24% and 3% of employees' gross emoluments to Employees' Provident Fund and Employees' Trust Fund respectively which are separately administered defined contribution plans.

Obligations for contributions to defined contribution plans are recognized as expense in the Statement of Income as and when they are due.

5.29 Grants

Grants recognised at their fair value (where there is a reasonable assurance that the grant will be received and all attaching conditions, if any, will be complied with) are shown under equity. When the grant relates to an expense item it is recognised in the Statement of Income over the periods necessary to match them to the expenses it is intended to compensate on a systematic basis. Where the grant relates to an asset, the fair value is credited to a deferred government grant account and is released to the Statement of Income over the expected useful life of the relevant asset on a systematic basis consistent with the depreciation policy of the related asset.

5.30 Contingent Liabilities and Commitments

Contingent liabilities are possible obligations whose existence will be confirmed only by uncertain future events or present obligations where the transfer of economic benefit is not probable or cannot be reliably measured. All guarantees of indebtedness, forward foreign exchange transactions and other commitments, which are not recognized in Statement of Financial Position, are shown under respective headings disclosed as Contingent Liabilities and Capital Commitments items. Where applicable, such amounts are measured at best estimates.

STATEMENT OF INCOME AND OTHER COMPREHENSIVE INCOME

5.31 Revenue and Expenses

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Bank and the revenue can be reliably measured. Expenses are recognised in the Statement of Income on the basis of a direct association between the cost incurred and the earning of specific items of income. All expenditure incurred in the running of the business and in maintaining the property, plant & equipment in a state of efficiency has been charged to income in arriving at the result for the year.

The following specific recognition criteria must also be met before revenue and expenses are recognised:

5.31.1 Interest Income and Expenses

Interest income and expenses are recognised in the Statement of Income for all interest bearing instruments on an accrual basis using the effective yield method based on the actual purchase price unless collectability is in doubt. Interest income includes coupons earned on fixed income investments and securities and accrued discount and premium on Treasury bills and other discounted instruments. Interest income is suspended when loans become doubtful of collection. Such income is excluded from interest income until received.

5.31.2 Dividends

Dividend income is recognised when the shareholder's right to receive the payment is established.

5.31.3 Miscellaneous Income and Expenses

Miscellaneous income and expenses are recognised on an accrual basis.

Net gains and losses of a revenue nature on the disposal of Property, Plant & Equipment have been accounted for in the Statement of Income, having deducted from proceeds on disposal, the carrying amount of the assets and related selling expenses.

Gains and losses arising from incidental activities to the main revenue generating activities and those arising from a group of similar transactions which are not material, are aggregated, reported and presented on a net basis.

5.31.4 Personnel Expenses

Personnel Expenses include the full cost of all staff benefits. Salaries and related expenses due at year-end are included in other local payables.

5.31.5 Operating Leases

All the lease rentals on the operating leases are recognised in Statement of Income on a straight line basis over the term of the lease.

5.31.6 Income Tax Expense

The income of the bank is exempted from tax under section 118 of the Monetary Law Act No. 58 of 1949 as amended and as per section 7b (xvi) of Inland Revenue (Amendment) Act No. 10 of 2006 and section 9(1) of Inland Revenue Act No. 24 of 2017. In terms of the Economic Service Charge (amendment) Act No. 07 of 2017, CBSL is liable for ESC commencing from 1 April 2017. However, unrealized gain on exchange rate and unrealized marked to market gain on foreign currency financial assets are exempted from ESC with effect from October 2018 as per the ESC (amendment) Act No. 33 of 2018. Further, the bank is exempted from Value Added Tax on supply of financial services as per Value Added Tax (Amendment) Act No.17 of 2013.

5.32 Events Occurring after the Reporting Date

All material subsequent events after the reporting date have been considered and where appropriate adjustments or disclosures have been made in the respective notes to the financial statements.

STATEMENT OF CASH FLOWS

The cash flow statement has been prepared by using the "Direct Method" of preparing of cash flow statement in accordance with the IAS 7 - Statement of Cash Flow.

For the purposes of the Statement of Cash Flows, cash and cash equivalents consist of cash and cash equivalents as defined above, net of cash/pay order outflows.

6. NEW ACCOUNTING STANDARDS ISSUED BUT NOT EFFECTIVE AS AT REPORTING DATE

The following standards and related interpretations issued, but not yet effective which is applicable to the Bank, up to the date of issuance of the Bank's financial statements is disclosed below. The Bank intends to adopt the following standard, when it becomes effective.

6.1 IFRS 16 Leases

The IASB issued the new standard for accounting for leases - IFRS 16 Leases in January 2016. The new standard does not significantly change the accounting for leases for lessors. However, it does require lessees to recognise most leases on their balance sheets as lease liabilities, with the corresponding right of use assets. Lessees must apply a single model for all recognised leases, but will have the option not to recognise 'short-term' leases and leases of 'low-value' assets. Generally, the profit or loss recognition pattern for recognised leases will be similar to today's finance lease accounting, with interest and depreciation expense recognised separately in the Statement of Income.

IFRS 16 is effective for annual periods beginning on or after 1 January 2019. Early application is permitted provided the new revenue standard, IFRS 15, is applied on the same date. Lessees must adopt IFRS 16 using either a full retrospective or a modified retrospective approach.

The Bank does not anticipate early adopting IFRS 16 and is currently evaluating its impact.

7 NATURE AND EXTENT OF ACTIVITIES

7.1 Foreign Currency Activities

Foreign currency activities result mainly from the CBSL's holdings of foreign currency assets under its foreign reserves management function. The foreign reserves management portfolio comprises foreign currency assets held for foreign exchange intervention purposes and other foreign currency assets held for trading purposes.

The foreign currency assets are held in various currencies. The majorities are denominated in United States Dollars, Australian Dollars, Euros, Sterling Pounds, Japanese Yen and New Zealand Dollars. The financial instruments held within these foreign currency portfolios consist mainly of sovereign securities, securities held under reverse-repurchase transactions or balances held with other central banks, commercial banks and custodial institutions.

The Bank also holds, from time to time, foreign currency assets and liabilities that arise from international market operations.

7.2 Local Currency Activities

Local currency activities arise as follows:

- (i) Liquidity management operations: Liquidity management largely involves the CBSL offsetting the daily net flows to or from government or market by

advancing funds to or withdrawing funds from the banking system. Most of this business is undertaken through daily open market operations.

- (ii) Holding an investment portfolio comprising Sri Lanka government securities to support the liability for currency in circulation. The bank's policy is to hold these investments for monetary operations and not for trading.

7.3 Trust and Custodial Activities

Amounts administered by the CBSL under custodial and administration arrangements are not included in these

financial statements, as they do not form part of elements of financial statements of the Bank.

8. TRANSITION DISCLOSURES

The following disclosure set out the impact of adopting IFRS 9 on the Statement of Financial Position, retained earnings and other reserves including the effect of expected credit losses.

8.1 Reconciliation between the Carrying Amounts under IAS 39 to the Balances Reported under IFRS 9 as at 1 January 2018

| Assets/Liabilities | Note | IAS 39 | | Reclassification (Rs. 000) | Re-measurement (Rs. 000) | IFRS 9 | |
|---|-------|----------|---------------------|-------------------------------|-----------------------------|----------|---------------------|
| | | Category | Amount (Rs. 000) | | | Category | Amount (Rs. 000) |
| Cash & Cash Equivalents | | HTM | 459,827,641 | - | - | AC | 459,827,641 |
| Less: Expected Credit Losses | 8.1.1 | | - | - | (50,505) | | (50,505) |
| | | | | | | | 459,777,136 |
| Securities at Fair Value through Profit or Loss | | FVTPL | 45,264,376 | - | - | FVTPL | 45,264,376 |
| Securities at Fair Value through Other Comprehensive Income | | | - | - | - | FVOCI | 566,228,935 |
| Available for Sale Investments | | AFS | 566,228,935 | - | - | | - |
| Derivative Financial Instruments | | FVTPL | 4,940,455 | - | - | FVTPL | 4,940,455 |
| IMF Related Assets | | HTM | 126,842,946 | - | - | AC | 126,842,946 |
| Less: Expected Credit Losses | 8.1.1 | | - | - | (3) | | (3) |
| | | | | | | | 126,842,943 |
| Other Receivables | | L&R | 3,665,700 | - | - | AC | 3,665,700 |
| Sri Lanka Government Securities (Treasury Bill Holding) | 8.1.2 | HTM | 9,704,962 | 9,704,962 | 49,521 | FVOCI | 9,754,483 |
| Securities Purchased Under Resale Agreements | | HTM | 22,375,124 | - | - | AC | 22,375,124 |
| Provisional Advances to Government | | L&R | 199,800,871 | - | - | AC | 199,800,871 |
| Loans to Banks | | L&R | 223,702 | - | - | AC | 223,702 |
| Less: Expected Credit Losses | 8.1.1 | | - | - | (642) | | (642) |
| | | | | | | | 223,060 |
| Equity Investments in Financial and Other Institutions | | | - | - | 1,237,826 | FVOCI | 1,278,921 |
| Equity Investments in Financial and Other Institutions | 8.1.3 | AFS | 41,095 | - | - | | - |
| Other Assets | | HTM | 12,882,470 | - | - | AC | 12,882,470 |
| Less: Expected Credit Losses | 8.1.1 | | - | - | (8) | | (8) |
| | | | | | | | 12,882,462 |
| Reserves | | | 77,352,239 | - | 1,235,775 | | 78,588,014 |

8.1.1. The adoption of IFRS 9 has changed the impairment model of the Bank where by all assets classified as Amortized Cost and FVOCI are subject to expected credit losses.

8.1.2. The Treasury Bill holding of the Bank which is held for open market operations was under the Held to Maturity category under IAS 39. This has been reclassified as FVOCI through the

transition to IFRS 9 due to the business model of the Treasury Bill holding.

8.1.3. Bank has certain equity investments in financial and other institutions which were classified as Available for Sale investments under IAS 39. This has been reclassified as FVOCI from the transition to IFRS 9.

8.2 The Impact of Transition to IFRS 9 on Retained Earnings and Other Reserves

| | Other Reserves Rs. 000 | Retained Earnings Rs. 000 |
|---|---------------------------|------------------------------|
| Closing Balance under IAS 39 as at 31 December 2017 | 42,332,740 | 25,996,592 |
| Transition Adjustment on Reclassifications under IFRS 9 (Note 8.2.1) | 1,287,347 | - |
| Transition Adjustment on Expected Credit Losses under IFRS 9 (Note 8.2.2) | 65,588 | (117,160) |
| Opening Balance under IFRS 9 as at 1 January 2018 | 43,685,675 | 25,879,432 |

8.2.1. Reconciliation of the Carrying Values under IAS 39 and IFRS 9 due to Reclassification

| Category | Carrying Value Under IAS 39 Rs. 000 | Re-measurement Rs. 000 | Carrying Value under IFRS 9 Rs. 000 |
|--|--|---------------------------|--|
| CBSL Treasury Bill Holding | 9,704,962 | 49,521 | 9,754,483 |
| Equity Investments in Financial and Other Institutions | 41,095 | 1,237,826 | 1,278,921 |
| | <u>9,746,057</u> | <u>1,287,347</u> | <u>11,033,404</u> |

8.2.2. Reconciliation of the Aggregate Opening Impairment Allowances under IAS 39 to the Expected Credit Loss Provision under IFRS 9

| | Impairment under IAS 39 as at 31 December 2017 Rs. 000 | Re-measurement Rs. 000 | Impairment under IFRS 9 as at 1 January 2018 Rs. 000 |
|---|---|---------------------------|---|
| Cash & Cash Equivalents | - | 50,505 | 50,505 |
| Securities at Fair Value through Other Comprehensive Income | - | 65,588 | 65,588 |
| IMF Related Assets | - | 3 | 3 |
| Loans to Banks | - | 642 | 642 |
| Other Assets | 151,674 | 8 | 151,682 |
| Contingent Liability - Credit Guarantee Scheme | 12,600 | 414 | 13,014 |
| | <u>164,274</u> | <u>117,160</u> | <u>281,434</u> |

9. CASH AND CASH EQUIVALENTS

| | 2018 Rs. 000 | 2017 Rs. 000 |
|---|--------------------|--------------------|
| Cash Balances with Banks | 117,035,257 | 16,518,603 |
| Time Deposits with Banks | 92,862,673 | 269,193,626 |
| Overnight Placements | 162,300,186 | 173,979,333 |
| Interest Receivable on Cash and Cash Equivalents | 48,624 | 136,079 |
| Cash and Cash Equivalents for Cash Flow Purpose | 372,246,740 | 459,827,641 |
| Less: Expected Credit Losses on Cash and Cash Equivalents (Note 9.1) | (71,564) | - |
| Total | 372,175,176 | 459,827,641 |

9.1 Movement in Expected Credit Losses on Cash and Cash Equivalents

Stage 1

| | |
|--|---------------|
| Balance as at 1 January | - |
| Adjustment on Initial Application of IFRS 9 (Note 8.2.2) | 50,505 |
| Adjusted Balance as at 1 January | 50,505 |
| Charge during the Year | 21,059 |
| Balance as at 31 December | 71,564 |

10. INVESTMENTS IN FOREIGN SECURITIES

| | 2018 Rs. 000 | 2017 Rs. 000 |
|---|--------------------|--------------------|
| Securities at Fair Value through Profit or Loss | | |
| -Investment in Foreign Securities (Note 10.1) | 37,467,239 | 29,988,753 |
| -Gold (Un-Allocated) | - | 15,275,623 |
| | <u>37,467,239</u> | <u>45,264,376</u> |
| Securities at Fair Value through Other Comprehensive Income/ Available for Sale | | |
| -Investment in Foreign Securities | 694,876,394 | 566,228,935 |
| | <u>694,876,394</u> | <u>566,228,935</u> |
| Total Investment in Foreign Securities | 732,343,633 | 611,493,311 |
| Expected Credit Loss on Securities at Fair Value through Other Comprehensive Income (Note 10.2) | 63,649 | - |

10.1 Investment in foreign securities classified as securities at fair value through profit or loss includes the investments made by the Bank during 2016 in the Reserve Advisory Management Program (RAMP) managed by the World Bank. The value of the investment with RAMP as at 31st December 2018 was Rs. 37,467.24 Mn (2017 - Rs. 29,988.75 Mn).

10.2 Movement in Expected Credit Losses on Securities at Fair Value through Other Comprehensive Income

| | 2018 Rs. 000 |
|--|-----------------|
| Stage 1 | |
| Balance as at 1 January | - |
| Adjustment on Initial Application of IFRS 9 (Note 8.2.2) | 65,588 |
| Adjusted Balance as at 1 January | 65,588 |
| Reversal during the Year | (1,939) |
| Balance as at 31 December | 63,649 |

11. DERIVATIVE FINANCIAL INSTRUMENTS

11.1 The table below shows the fair values of derivative financial instruments, recorded as assets or liabilities, together with their notional

amounts. The notional amount, recorded gross, is the amount of derivative's underlying asset, reference rate or index and is the basis upon which changes in the value of derivatives are measured. The notional amounts indicate the volume of transactions outstanding at period end and are indicative of neither the market risk nor the credit risk.

| | 2018 | | | 2017 | | |
|---|------------|-------------------|--------------------|------------------|------------------|--------------------|
| | Assets | Liabilities | Notional Amount | Assets | Liabilities | Notional Amount |
| | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 |
| Currency SWAPS | - | 13,590,145 | 203,257,715 | 4,939,919 | 3,403,868 | 228,553,847 |
| Forward Forex | 750 | - | 548,250 | 536 | - | 132,773 |
| Embedded Derivatives - Currency Options | - | 466,315 | 5,299,747 | - | 1,244,581 | 13,374,795 |
| Total | 750 | 14,056,460 | 209,105,712 | 4,940,455 | 4,648,449 | 242,061,415 |

11.2 The above derivatives consisting of Currency Swaps, Currency Options and Foreign Exchange Forward Contracts were used for the purpose of managing market and liquidity risks in international reserves held by the Bank in line with the statutory objectives of maintenance of international reserves. In addition, the Bank entered into Swap transactions with Licensed Commercial Banks (LCBs), Licensed Specialized Banks (LSBs) and Foreign Central Banks in order to maintain international stability of the Sri Lankan Rupee, to strengthen the financial system of the country and to encourage those Banks to bring foreign funds.

11.3 Derivatives are financial contracts that derive their value in response to changes in interest rates, financial instruments prices, commodity prices, foreign exchange rates, credit risk and indices.

11.4 A significant part of derivatives portfolio of the Bank consists of currency swaps entered into as a strategy to manage the short term liquidity requirements. In a currency swap, the Bank pays/ receives a specified amount of a currency on an agreed date in exchange of another currency at agreed rates.

11.5 From Foreign Exchange Forward contracts, the Bank gets the obligation to buy or sell specific amount of foreign currency on an agreed future date at an agreed rate.

11.6 The Bank's exposure to derivative contracts is closely monitored as part of the overall risk management of the Bank to ensure expected benefits from such derivatives are crystalized to the Bank.

12. IMF RELATED ASSETS

| | 2018 Rs. 000 | 2017 Rs. 000 |
|---|--------------------|--------------------|
| Holding of Special Drawing Rights (Note 12.1) | 217,126 | 677,131 |
| IMF Quota (Note 12.2) | 146,732,242 | 125,996,456 |
| Deposits with IMF (Note 12.3) | 199,965 | 164,565 |
| Prepaid Charges - IMF Loans | 268,456 | - |
| Interest Receivable on IMF Quota | 9,667 | 4,794 |
| Less: Expected Credit Losses on IMF Related Assets (Note 12.4) | (4) | - |
| | 147,427,452 | 126,842,946 |

12.1 Holding of Special Drawing Rights

Holding of Special Drawing Rights (SDR) is potentially a claim on the freely usable currencies of IMF members in which holders of SDRs can exchange their SDRs for these currencies. The SDRs value as a reserve asset derives from the commitments of members to hold and accept SDRs, and to honor various obligations connected with the operation of the SDR system. The IMF ensures that the SDRs claim on freely usable currencies is being honored in two ways: by designating IMF members with a strong external position to purchase SDRs from members with weak external positions, and through the arrangement of voluntary exchanges between participating members in a managed market. The amount shown above represents the total holding of the Bank as at the respective reporting dates.

12.2 IMF Quota

The IMF Quotas (capital subscriptions) are the primary source of IMF resources received from its member countries. Each country's quota is determined broadly on the basis of the relative economic size of the country. Upon joining the IMF, a country must pay 25 per cent of its quota in widely accepted foreign currencies or SDRs, and the remaining 75 per cent in its own currency. The IMF quota represents an asset of the Bank as it transacts with the IMF on its own account on behalf of the Government as per Articles of the IMF.

The IMF, based on the General Quota Review Agreement, decided to increase the quotas of each of the IMF's 189 members in January 2016. As a result, Sri Lanka's IMF quota increased to SDR 578.80 Mn on 17 February 2016 from the previous quota amount of SDR 413.40 Mn.

The amounts payable in respect of the IMF Quota is shown under the heading Quota Liability in Note 25. A member's quota determines that country's financial and organizational relationship with IMF, including:

(i) **Subscriptions:** A member's subscription to IMF resources is equal to its quota and determines the maximum amount of financial resources the member is obliged to provide to the IMF. A member must pay its subscription in full; up to 25 per cent must be paid in reserve assets specified by the IMF (SDRs or usable currencies), and the rest in the member's own currency.

(ii) **Voting power:** The quota defines a member's voting power in IMF decisions. IMF member's votes are comprised of basic votes plus one additional vote for each SDR 100,000 of quota. The 2008 reform fixed the number of basic vote at 5.50 per cent of total votes.

(iii) **Access to financing:** The amount of financing a member can obtain from the IMF (access limits) is based on its quota. Under Stand-By and Extended Arrangements, for instance, a member can currently borrow up to 145 per cent of its quota annually and 435 per cent cumulatively. Access to finance may be higher in exceptional circumstances.

(iv) **SDR allocations:** Members' shares of SDR allocations are established in proportion to their quotas.

12.3 Deposits with IMF – PRGF – HIPC Trust Deposit

The PRGF – HIPC (Poverty Reduction and Growth Facility for the Heavily Indebted Poor Countries) Trust Deposit was made under the agreement between the GOSL and the IMF on 21 April 2000 by transferring SDR 788,783 from Sri Lanka's deposit in the post SCA-2 (Special Contingent Account) administered account with the IMF. This account was created under the guidance of the IMF by transferring the balance held in SCA-2 against Sri Lanka when it was decided to wind up SCA-2 by the IMF. The IMF requested the countries that had balances in the Post SCA-2 account to consider providing the balances in that account to the PRGF/HIPC Trust either as outright grant or as a means of providing a subsidy for PRGF/HIPC Loan. Accordingly GOSL agreed to transfer the funds from Post SCA –2 accounts to PRGF/HIPC Trust account, not as an outright grant, but as an interest free deposit until 2018. This was later extended until 2024.

12.4 Movement in Expected Credit Losses on IMF Related Assets

| | 2018 Rs. 000 |
|--|-----------------|
| Stage 1 | |
| Balance as at 1 January | - |
| Adjustment on Initial Application of IFRS 9 (Note 8.2.2) | 3 |
| Adjusted Balance as at 1 January | 3 |
| Charge for the Year | 1 |
| Balance as at 31 December | 4 |

13. SRI LANKA GOVERNMENT SECURITIES

Portfolio of government securities is acquired and maintained as per Section 90 (2) of the Monetary Law Act for the purpose of open market operations to be carried out in the conduct of the monetary policy.

| | 2018 Rs. 000 | 2017 Rs.000 |
|---------------------|-------------------|------------------|
| Treasury Bills | 43,443,802 | 9,704,962 |
| Treasury Bonds | 1,542,796 | - |
| Interest Receivable | 44,559 | - |
| | 45,031,157 | 9,704,962 |

14. SECURITIES PURCHASED UNDER RESALE AGREEMENTS

| | 2018 Rs. 000 | 2017 Rs.000 |
|---|--------------------|-------------------|
| Securities Purchased under Resale Agreements | 229,333,000 | 22,359,000 |
| Interest Receivable on Securities Purchased under Resale Agreements | 121,409 | 16,124 |
| | 229,454,409 | 22,375,124 |

15. PROVISIONAL ADVANCES TO GOVERNMENT

These represent advances granted to the Government of Sri Lanka (GOSL) under Section 89 of the Monetary Law Act subject to the conditions stated in provision of advances to finance expenditures authorised to be incurred out of the Consolidated Fund.

16. LOANS TO BANKS

These are the loans granted in terms of Part IIIA of Chapter V of the Monetary Law Act to facilitate lending for productive purposes.

| | 2018 Rs. 000 | 2017 Rs. 000 |
|---|-----------------|-----------------|
| Medium & Long Term Credit Scheme | | |
| - Related Parties | 26,951 | 29,146 |
| Provincial Development Credit Loan Scheme | | |
| - Related Parties | - | 28,254 |
| Saubaghyia Loan Scheme | | |
| - Related Parties | 13,122 | 49,539 |
| - Others | 8,345 | 14,211 |
| Resumption of Economic Activities in the East | | |
| - Related Parties | 12,358 | 41,382 |
| - Others | 16,403 | 35,492 |
| Repair of Damaged Houses North & East | | |
| - Related Parties | 18,830 | 24,330 |
| Awakening North Loan Scheme (RF Phase II) | | |
| - Related Parties | 108 | 1,348 |
| Less: | | |
| Provision for Impairment (Note 16.1) | (154) | - |
| Net Receivable | 95,963 | 223,702 |

16.1 Movement in Provision for Impairment

| | 2018 Rs. 000 | 2017 Rs. 000 |
|--|-----------------|-----------------|
| As at 1 January | - | 27,302 |
| Reversal during the Year | - | (27,302) |
| Expected Credit Losses on Loans to Banks (Note 16.2) | 154 | - |
| As at 31 December | 154 | - |

16.2 Movement in Expected Credit Losses on Loans to Banks

| | 2018 | | |
|--|--------------------|--------------------|------------------|
| | Stage 1 Rs. 000 | Stage 2 Rs. 000 | Total Rs. 000 |
| Balance as at 1 January | - | - | - |
| Adjustment on Initial Application of IFRS 9 (Note 8.2.2) | 26 | 616 | 642 |
| Adjusted Balance as at 1 January | 26 | 616 | 642 |
| Reversal during the Year | (11) | (477) | (488) |
| Balance as at 31 December | 15 | 139 | 154 |

17. EQUITY INVESTMENTS IN FINANCIAL AND OTHER INSTITUTIONS

These investments are made in terms of Section 105 A of the Monetary Law Act. Under this Section, the Bank is empowered to acquire and hold shares in any company which, in the opinion of the Monetary Board, was formed for the advancement and promotion of human resources and technological development in the Banking and financial sector or to facilitate clearance of transactions among commercial Banks operating in Sri Lanka.

17.1 Investment position

| Company | Nature of the Business | 2018 | | 2017 | |
|--|---------------------------------|---------------|------------------------|---------------|------------------------|
| | | No. of Shares | Carrying Value Rs. 000 | No. of Shares | Carrying Value Rs. 000 |
| Lanka Clear (Private) Limited | Automated Clearing | 2,950,000 | 417,128 | 2,950,000 | 29,500 |
| Fitch Ratings Lanka Limited | Credit Rating | - | - | 3,500,000 | 3,500 |
| Lanka Financial Services Bureau Limited | Automated Fund Transfers | 225,000 | 1,396 | 225,000 | 2,250 |
| Credit Information Bureau of Sri Lanka Limited | Provision of Credit Information | 48,244 | 963,355 | 48,244 | 5,845 |
| | | | 1,381,879 | | 41,095 |

17.2 The equity investments were carried at fair value as at 31 December 2018 based on Net Assets per Share basis as per the latest available unaudited financial statements of those companies at the time of preparation of the Bank's financial statements. Accordingly, the Net Asset per Share companies as at the following dates were used.

Lanka Clear (Private) Limited - 30 November 2018

Lanka Financial Services Bureau Limited - 31 October 2018

Credit Information Bureau of Sri Lanka Limited - 31 December 2018

18. OTHER ASSETS

| | 2018 Rs. 000 | 2017 Rs. 000 |
|---|-------------------|-------------------|
| Financial Assets | | |
| Investment of Internal Funds | 7,955,537 | 6,730,548 |
| Less: Provision for Impairment of Assets (Note 18.1) | (163,144) | (151,674) |
| Net Investment of Internal Funds | 7,792,393 | 6,578,874 |
| Staff Loans at Amortized Cost | 5,780,754 | 5,036,028 |
| Receivable from Treasury and Other Ministries | 18,785 | 54,490 |
| Other Receivables | 126,086 | 143,276 |
| | 13,718,018 | 11,812,668 |
| Non Financial Assets | | |
| Deferred asset on Staff Loan | 1,065,287 | 1,069,802 |
| | 14,783,305 | 12,882,470 |

18.1 Movement in Provision for Impairment of Assets

| | 2018 | | | 2017 |
|--|--------------------|--------------------|------------------|----------------|
| | Stage 1 Rs. 000 | Stage 3 Rs. 000 | Total Rs. 000 | Rs. 000 |
| Balance as at 1 January | - | 151,674 | 151,674 | 139,131 |
| Adjustment on Initial Application of IFRS 9 (Note 8.2.2) | 8 | - | 8 | - |
| Adjusted Balance as at 1 January | 8 | 151,674 | 151,682 | 139,131 |
| Charge during the Year | 84 | 11,378 | 11,462 | 12,543 |
| Balance as at 31 December | 92 | 163,052 | 163,144 | 151,674 |

19. GOLD

This is the value of physical gold held as required under Section 67 (1) and Section 67(2) of the Monetary Law Act (MLA) as part of the International Reserve of the Bank. As per Section 67(2) of MLA, Monetary Board is required to endeavor to hold at least a nuclear reserve in gold or currencies freely convertible by the Bank, whether directly or indirectly, in to gold as per the MLA.

20. INVENTORIES

| | 2018 Rs. 000 | 2017 Rs. 000 |
|---|------------------|------------------|
| Notes for Circulation | 2,495,222 | 4,442,014 |
| Coins for Circulation | 2,194,055 | 1,850,723 |
| Coins in Transit from the Supplier | 613,432 | - |
| Notes in Transit from the Supplier | 1,253,694 | 568,716 |
| | 6,556,403 | 6,861,453 |
| Less: Provision for Slow Moving Items | (45,000) | (45,000) |
| | 6,511,403 | 6,816,453 |
| Stationery and Sundry Inventory | 57,318 | 58,881 |
| Medical Center Stock | 214 | 199 |
| Total Inventories at Lower of Cost or Net Realizable Value | 6,568,935 | 6,875,533 |

In 2018, inventories of Rs. 3,999.00 Mn (2017 Rs. 2,850.82 Mn) were recognized as an expense during the year and included in "Cost of Inventory (Cost of new currency issue)".

21. PROPERTY, PLANT AND EQUIPMENT

| Cost | Land and Buildings Rs.000 | Plant & Plant Integrals Rs.000 | Furniture & Equipment Rs.000 | Vehicles Rs.000 | Computers Rs.000 | Others Rs.000 | Construction In progress Rs.000 | 2018 Total Rs.000 | 2017 Total Rs.000 |
|-------------------------------------|------------------------------|-----------------------------------|---------------------------------|--------------------|---------------------|------------------|------------------------------------|----------------------|----------------------|
| As at 1 January | 16,743,200 | 1,567,670 | 1,305,057 | 614,563 | 843,365 | 55,436 | 28,206 | 21,157,497 | 20,920,014 |
| Additions during the year | - | 10,272 | 17,537 | - | 64,328 | 1,303 | 11,074 | 104,514 | 267,129 |
| Disposals during the year | (734,278) | (1,278) | (11,672) | (13,300) | (12,143) | - | - | (772,671) | (29,646) |
| Transfers/Write off during the year | 106 | - | 450 | - | - | - | (22,958) | (22,402) | - |
| As at 31 December | 16,009,028 | 1,576,664 | 1,311,372 | 601,263 | 895,550 | 56,739 | 16,322 | 20,466,938 | 21,157,497 |

| Depreciation | Land and Buildings Rs.000 | Plant & Plant Integrals Rs.000 | Furniture & Equipment Rs.000 | Vehicles Rs.000 | Computers Rs.000 | Others Rs.000 | Construction In progress Rs.000 | 2018 Total Rs.000 | 2017 Total Rs.000 |
|---------------------------|------------------------------|-----------------------------------|---------------------------------|--------------------|---------------------|------------------|------------------------------------|----------------------|----------------------|
| As at 1 January | 251,534 | 860,947 | 863,095 | 410,441 | 774,790 | 36,173 | - | 3,196,980 | 2,787,624 |
| Depreciation for the year | 195,031 | 78,357 | 80,725 | 25,923 | 40,289 | 1,126 | - | 421,451 | 434,558 |
| Disposals during the year | (70,478) | (663) | (10,866) | (13,300) | (12,040) | - | - | (107,347) | (25,202) |
| As at 31 December | 376,087 | 938,641 | 932,954 | 423,064 | 803,039 | 37,299 | - | 3,511,084 | 3,196,980 |
| Net Book Value | 15,632,941 | 638,023 | 378,418 | 178,199 | 92,511 | 19,440 | 16,322 | 16,955,854 | 17,960,517 |

The carrying values of Land and Buildings are recorded at fair value. The latest independent valuation was performed as at 31 December 2016 by FM Valuers, which was recorded as at 31 December 2016.

The properties of the bank at New York and Brazil were sold to the Ministry of Foreign Affairs at cost in May 2018.

During the financial year, the Bank has acquired property, plant and equipment by means of cash with an aggregated cost of Rs. 104.18 Mn (2017 - Rs. 265.73 Mn).

The value of the fully depreciated assets which are still in use as at 31 December 2018 was Rs. 1,611.38 Mn. (2017 - Rs. 1,598.17 Mn).

During the financial year, the Bank has charged Rs. 22.40 Mn to the Statement of Income from Construction in progress.

| Information on Valuations of Freehold Land and Buildings and Buildings on Leasehold Land of the Bank | | | | | | | |
|--|--|---------------------------------|---------------------------------|---------------------------------------|--------------------------------|-------------------|----------------|
| Property | Name of the chartered valuation surveyor | Valuation approach | Estimated price per perch (Rs.) | Estimated price per square foot (Rs.) | Estimated rent per month (Rs.) | Outgoing expenses | Years Purchase |
| Land & Building | | | | | | | |
| Head Office - Colombo 01 | A. A. M. Fathihu | Market Approach & Cost Approach | 12,500,000 | 9,000 - 15,000 | - | - | - |
| Whiteaways Building - Colombo 01 | -do- | Income Approach | 13,500,000 | - | 6,000,000 | 40% | 16.66 |
| Lloyds Building - Colombo 01 | -do- | Income Approach | 13,500,000 | - | 6,750,000 | 40% | 16.66 |
| Central Point Building - Colombo 01 | -do- | Income Approach | 14,000,000 | - | 7,500,000 | 35% | 16.66 |
| Centre for Banking Studies - Rajagiriya | -do- | Market Approach & Cost Approach | 2,500,000 - 3,500,000 | 2,500 - 9,500 | - | - | - |
| Bank House - Colombo 07 | -do- | Market Approach & Cost Approach | 7,500,000 | 3,500 - 8,500 | - | - | - |
| Regional Office - Matara | -do- | Market Approach & Cost Approach | 1,500,000 - 3,000,000 | 4,000 - 7,500 | - | - | - |
| Regional Office - Matale | -do- | Market Approach & Cost Approach | 100,000 - 500,000 | 2,500 - 7,500 | - | - | - |
| Holiday Home - Nuwara Eliya | -do- | Market Approach & Cost Approach | 1,000,000 | 2,000 - 7,000 | - | - | - |
| Holiday Home - Kataragama | -do- | Market Approach & Cost Approach | 200,000 | 4,500 - 10,000 | - | - | - |
| Building on Leasehold Land | | | | | | | |
| Regional Office - Anuradhapura | A. A. M. Fathihu | Cost Approach | - | 3,500 - 7,500 | - | - | - |
| Holiday Home - Anuradhapura | -do- | Cost Approach | - | 5,500 | - | - | - |
| Regional Office - Kilinochchi | -do- | Cost Approach | - | 1,500 - 7,000 | - | - | - |
| Holiday Home - Somawathiya | -do- | Cost Approach | - | 10,000 | - | - | - |
| Composition of Land and Buildings | | | | | | | |
| | Carrying Value 2018 Rs. 000 | Carrying Value 2017 Rs. 000 | | | | | |
| Freehold Land | 8,930,375 | 8,976,339 | | | | | |
| Buildings on Freehold Land | 6,449,206 | 7,250,954 | | | | | |
| Buildings on Leasehold Land | 253,360 | 264,373 | | | | | |
| | <u>15,632,941</u> | <u>16,491,666</u> | | | | | |
| The carrying amount of revalued Land and Buildings that would have been included in the financial statements had they been carried at cost less depreciation is Rs. 7,796.82 Mn (2017 - Rs. 8,607.88 Mn). | | | | | | | |
| 22. INTANGIBLE ASSETS | | | | | | | |
| | 2018 Rs. 000 | 2017 Rs. 000 | | | | | |
| Computer Software: | | | | | | | |
| Cost: | | | | | | | |
| As at 1 January | 957,204 | 949,772 | | | | | |
| Additions during the year | 25,484 | 7,432 | | | | | |
| As at 31 December | <u>982,688</u> | <u>957,204</u> | | | | | |
| Amortization: | | | | | | | |
| As at 1 January | 876,581 | 793,452 | | | | | |
| Amortization Charge for the Year | 75,670 | 83,129 | | | | | |
| As at 31 December | <u>952,251</u> | <u>876,581</u> | | | | | |
| Net Book Value: | | | | | | | |
| As at 31 December | <u>30,437</u> | <u>80,623</u> | | | | | |
| The Bank has acquired intangible assets by means of cash with an aggregated cost of Rs. 25.48 Mn during the year (2017 - Rs. 7.43 Mn). | | | | | | | |
| The value of fully amortized intangible assets which are still in use as at 31 December 2018 was Rs. 927.38 Mn. (2017 - Rs. 636.58 Mn). | | | | | | | |
| 23. BANKS AND FINANCIAL INSTITUTIONS | | | | | | | |
| | 2018 Rs. 000 | 2017 Rs. 000 | | | | | |
| Payable to Foreign Banks | 16,864,115 | 8,237,633 | | | | | |
| Payable to Other Foreign Financial Institutions | 2,437,045 | 1,911 | | | | | |
| | <u>19,301,160</u> | <u>8,239,544</u> | | | | | |
| 24. ASIAN CLEARING UNION | | | | | | | |
| The Asian Clearing Union (ACU) was established in 1974 at the initiative of the United Nations Economic and Social Commission for Asia and the Pacific (ESCAP) as a mechanism to settle, on a multilateral basis of payments for intra-regional transactions among participating Central Banks. The participants of ACU are Sri Lanka, Bangladesh, Iran, Nepal, Pakistan, India, Bhutan, Myanmar and Maldives. Net settlement position of each ACU participant is calculated based on the daily outstanding balance held over the two months period and settlement will take place within four working days of the following month. Interest rate was spread between 1.45% and 2.28% during the year (2017 - 0.63% and 1.28%). | | | | | | | |

25. INTERNATIONAL MONETARY FUND

| | 2018 Rs. 000 | 2017 Rs. 000 |
|--------------------------------------|-----------------|-----------------|
| Interest Bearing Loans | 181,318,765 | 116,996,460 |
| Allocation of Special Drawing Rights | 100,253,563 | 86,086,013 |
| Other Amounts Payable to IMF | 67,352,253 | 57,467,696 |
| Quota Liability | 68,063,665 | 58,445,100 |
| | 235,669,481 | 201,998,809 |
| | 416,988,246 | 318,995,269 |

25.1 Interest bearing Loans consist of the Extended Fund Facility (EFF) obtained from the IMF.

25.2 Extended Fund Facility (EFF) is a three year facility provided by the IMF to support the Balance of Payments and Government's economic reform agenda. The IMF approved the EFF fund facility of SDR 1.10 Bn (approximately USD 1.50 Bn) in June 2016. This amount is equivalent to 185 per cent of the country's current quota with the IMF. The first tranche under the EFF amounting to SDR 119.89 Mn (approximately USD 168.10 Mn) was made available in June 2016. The second tranche to the value of SDR 119.89 Mn (approximately USD 162.56 Mn), third tranche to the value of SDR 119.89 Mn (approximately USD 167.2 Mn), fourth tranche to the value of SDR 177.77 Mn (approximately USD 251.4 Mn) and the fifth tranche to the value of SDR 177.77 Mn (approximately USD 252 Mn) were disbursed in June 2016, July 2017, December 2017 and June 2018, respectively. With the disbursement of the fifth tranche, a total of USD 1,014 Mn has been received so far by Sri Lanka on account of EFF. The remaining amount is expected to be disbursed in two more tranches over a period of one year. The interest rate applicable on the EFF comprise of the basic rate of charge, which is equivalent to the SDR interest rate (currently stands at 0.05 per cent per annum) plus 100 basis points.

| | Effective interest rate % | Maturity | 2018 Rs. 000 | 2017 Rs. 000 |
|-------------------------------------|---------------------------|----------|--------------------|--------------------|
| Extended Fund Facility | 1.103 | 2028 | 181,318,765 | 116,996,460 |
| Total Interest bearing loans | | | 181,318,765 | 116,996,460 |

25.3 The Special Drawing Right (SDR) is a reserve asset created by the IMF in order to meet a long-term global need to supplement existing reserve assets. SDRs are allocated to member countries in proportion to their IMF quotas. SDR allocations can only be made to countries that participate in the IMF's SDR Department (an accounting unit within the IMF). The IMF created

SDRs to supplement existing official reserve assets such as gold holdings, foreign exchange and reserve positions in the IMF. Under certain conditions, which are set in the Articles of Agreement signed on behalf of the Government of Sri Lanka by the Bank, the IMF may allocate SDRs to members in proportion to their IMF quotas. An allocation of SDRs by the IMF provides each member with a costless asset on which interest is neither earned nor paid. The Articles of Agreement also allow for cancellations of SDRs, but to date, this provision has not been used. Increases in Allocation of SDR represents increases in holding of SDR as described in Note 12. Members of IMF are obligated to pay to the IMF an amount equal to its net cumulative allocation and any other amounts that may be due and payable because of its participation in the Special Drawing Rights Department at the point of termination or liquidation of IMF's SDR Department.

25.4 Other Amounts Payable to IMF represent amounts owed by the Bank to IMF on account of operational and administrative transactions.

25.5 Quota Liability The amounts payable in respect of the IMF Quota as described in Note 12.2.

26. OTHERS

| | 2018 Rs. 000 | 2017 Rs. 000 |
|--|--------------------|-------------------|
| Moragahakanda Development Project Loan under Escrow Agreement (Note 26.1) | 1,577,068 | 2,056,009 |
| DST - PRP III under Escrow Agreement (Note 26.2) | 5,968,519 | 7,588,467 |
| DST - PRP III Phase II under Escrow Agreement (Note 26.3) | 6,242,573 | 8,094,403 |
| DST Special Dollar A/C - Small & Medium Enterprises (SME) and Green Energy Global Loan (Note 26.4) | - | 109,808 |
| DST Special Dollar A/C - Ambatale Water Supply Improvement Project (Note 26.5) | - | 189,196 |
| DST - NORAD Waso Asia Project of the University of Peradeniya (Note 26.6) | - | 10,664 |
| DST's Dollar Account - Hambantota Port (Note 26.7) | 91,374,950 | 44,648,475 |
| DST Special Dollar A/C 2 (Note 26.8) | 29,493,915 | - |
| Other Foreign Liabilities | 73,908 | 1,398,867 |
| | 134,730,933 | 64,095,889 |

26.1 Moragahakanda Development Project Loan under Escrow Agreement

This Loan Agreement was signed between China Development Bank and the Government of Sri Lanka on 28 June 2012 for USD 214.20 Mn. The purpose of this loan agreement is to provide facility for financing the construction of a hydroelectric power station in Moragahakanda. This Project has

been implemented by the Ministry of Irrigation and Water Resources Management. The Bank opened an account in its books of account, as the Banker to this agreement, according to the instructions of the Department of External Resources for the purpose of receiving and disbursing the loan. During the year 2018, USD 4.82 Mn was disbursed and the balance as at 31st December 2018 is USD 8.63 Mn.

26.2 Priority Road Project III under Escrow Agreement

This Facility Agreement was signed between the China Development Bank and the Government of Sri Lanka on 11 March 2014 for USD 300 Mn. The purpose of this loan is to finance the cost of improvement and rehabilitation of Priority Road Project III-Phase I. As per the Facility Agreement, the Bank has been appointed as the Banker to the Government of Sri Lanka. Accordingly, an account has been opened in its books of account for the sole purpose of depositing the loan and disbursing such received monies to the Road Project. During the year 2018, USD 16.99 Mn was disbursed and the remaining balance as at 31 December 2018 is USD 32.66 Mn.

26.3 Priority Road Project III Phase II under Escrow Agreement

The Phase II of this agreement was received on 24 November 2014 for USD 100 Mn. During the year 2018, USD 18.80 Mn was disbursed and the remaining balance as at 31 December 2018 is USD 34.16 Mn.

26.4 SME and Green Energy Global Loan

This is a Finance Contract between the Democratic Socialist Republic of Sri Lanka and European Investment Bank signed on 13 November 2013. As per the Facility Agreement, the Bank has been appointed as the Banker to the Government of Sri Lanka. Accordingly, an account has been opened in its books of account for depositing the loan proceeds and disbursing such received money to the project.

The second tranche of the above SME and Green Energy Global Loan was received in Euro on 09 July 2015. Accordingly, an account has been opened in the books of account of the CBSL for depositing the loan and disbursing such received money to the project.

During the year 2018, USD 0.71 Mn was disbursed and there was no outstanding balance as at 31 December 2018.

26.5 DST Special Dollar Account - Ambatale Water Supply Improvement Project

This Credit Facility Agreement was signed between Agence Francaise de Development and the Democratic Socialist Republic of Sri Lanka on 29 September 2014. The Bank has opened an account in its books of account, as the Banker to this agreement, according to the the instructions of the Department of Treasury Operations for the purpose of receiving and disbursing the loan. USD 5.0 Mn was received to the above account on 14 September 2015.

During the year 2018, USD 1.24 Mn was disbursed and there was no outstanding balance as at 31 December 2018.

26.6 NORAD Waso Asia Project of the University of Peradeniya

The Central Bank of Sri Lanka is maintaining USD Account NORAD Waso Asia Project of the University of Peradeniya on behalf of University of Peradeniya to receive funds from NORAD for the Capacity Building Project since 2016. University of Peradeniya withdraws the funds in USD or LKR by submitting the withdrawal applications through Treasury Operation Department. During the year 2018, USD 0.16 Mn was received to the account and two transfers totalling USD 0.23 Mn was transferred to DST. There was no outstanding balance as at 31 December 2018.

26.7 DST's Dollar A/C - Hambantota Port

This is a special dollar account maintained on behalf of the Treasury Operations Department crediting the proceeds from China Merchant Port Holdings Co. Ltd, received for handing over the operations of Hambantota Port subsequent to the agreement signed between Sri Lanka Ports Authority and the China Merchant Port Holdings Co. Ltd. Initial proceeds of USD 292.1 Mn was received on 22 December 2017. Second and third proceeds of USD 97.37 Mn and USD 584.19 Mn were received on 24 January 2018 and 25 June 2018 respectively. The remaining balance as at 31 December 2018 was USD 500.00 Mn.

26.8 DST Special Dollar A/C 2

This is a dollar account maintained on behalf of the Treasury Operations Department in order to credit the proceeds received on behalf of Treasury in USD. During the year 2018, the proceeds of SLDB, FCBU Loans and Term Financing Facility have been credited and utilized for repayment of loans on behalf of government. The remaining balance as at 31 December 2018 is USD 161.39 Mn.

27. DEPOSITS OF BANKS AND FINANCIAL INSTITUTIONS

These are the deposits maintained by LCBs for the purpose of meeting Statutory Reserve Requirement under section 93 of the Monetary Law Act and deposits maintained by LCBs, Primary Dealers and the Employee Provident Fund as participants of Real Time Gross Settlement System (RTGS) for honoring payments under the RTGS operated by the Bank as per the provisions of the Monetary Law Act. Under the scheme, an interest free intra-day liquidity facility, fully collateralized by Government Securities is available to participants to meet payment obligations within the day to facilitate smooth functioning of the settlement system. Although these deposits are classified as related parties (i.e., State owned Banks and institutions) and others for the purpose of accounting disclosure requirements, such deposits are maintained in terms of relevant statutory provisions and not because of specific business relationship of the Bank with those state institutions.

| | 2018 Rs. 000 | 2017 Rs. 000 |
|---|---------------------------|---------------------------|
| Deposits by Banks : | | |
| - Related Parties | 192,367,084 | 215,901,806 |
| - Others | 127,555,665 | 125,805,585 |
| | <u>319,922,749</u> | <u>341,707,391</u> |
| Deposits by Financial Institutions : | | |
| - Related Parties | 177 | 94 |
| - Others | 183,257 | 4,713 |
| | <u>183,434</u> | <u>4,807</u> |
| Total Deposits by Banks and Other Financial Institutions | <u>320,106,183</u> | <u>341,712,198</u> |

28. DEPOSITS OF GOVERNMENT AND GOVERNMENTAL ENTITIES

| | 2018 Rs. 000 | 2017 Rs. 000 |
|-------------------------------|-----------------------|-----------------------|
| Government Deposits | 167,537 | 167,492 |
| Government Agencies and Funds | 181,181 | 157,025 |
| | <u>348,718</u> | <u>324,517</u> |

These are the deposits maintained in terms of Section 106 (1) of the Monetary Law Act since the Bank is the official depository of the Government and/or government agencies or institutions.

29. SECURITIES SOLD UNDER REPURCHASE AGREEMENTS

| | 2018 Rs. 000 | 2017 Rs. 000 |
|---|--------------------------|--------------------------|
| Securities sold under Repurchase Agreements | - | 6,503,884 |
| Standing Deposit Facility | 28,311,221 | 34,151,394 |
| | <u>28,311,221</u> | <u>40,655,278</u> |

Repurchase agreements are undertaken for Open Market Operations (OMO) to regulate liquidity in the money market under Sections 90 and 91 of Monetary Law Act as part of conduct of the monetary policy. These repurchase agreements were engaged only in Government securities on over-night basis or term basis depending on the market liquidity management policies of the Bank, decided from time to time.

30. BALANCES OF EMPLOYEE BENEFIT PLANS

The Bank as a part of normal activities provides current account facilities for its Employee Benefit Plans. The amounts held in credit of these separately administered current accounts and inter entity accounts of Employee Benefit Plans of the Bank, are as follows:

| | 2018 Rs. 000 | 2017 Rs. 000 |
|---|----------------------|---------------------|
| Balances in CBSL Provident Fund, Pension Schemes and Widows'/Widowers' & Orphans' Pension Schemes | 18,333 | 4,547 |
| | <u>18,333</u> | <u>4,547</u> |

31. CURRENCY IN CIRCULATION

The Bank as the sole currency issuing authority in Sri Lanka continued to perform the function of issuing legal tender currency. The amount of currency issued by the Bank and in circulation at respective reporting dates are as follows:

| Denomination Coins: | 2018 Rs. 000 | 2017 Rs. 000 |
|------------------------|--------------------------|--------------------------|
| 1 cent | 3,631 | 3,631 |
| 2 cent | 5,707 | 5,707 |
| 5 cent | 23,260 | 23,258 |
| 10 cent | 39,232 | 39,229 |
| 25 cent | 121,046 | 121,039 |
| 50 cent | 185,247 | 185,590 |
| 1 rupee | 929,905 | 898,148 |
| 2 rupee | 1,414,466 | 1,357,849 |
| 5 rupee | 4,408,327 | 4,102,486 |
| 10 rupee | 6,101,195 | 5,402,312 |
| Commemorative coins | 590,240 | 587,075 |
| | <u>13,822,256</u> | <u>12,726,324</u> |

Notes:

| | | |
|--------------------------------------|---------------------------|---------------------------|
| 1 rupee | 4,981 | 4,981 |
| 2 rupee | 26,694 | 26,696 |
| 5 rupee | 37,192 | 37,193 |
| 10 rupee | 1,271,474 | 1,340,240 |
| 20 rupee | 5,607,149 | 5,758,265 |
| 50 rupee | 5,456,882 | 5,561,352 |
| 100 rupee | 22,612,502 | 21,599,562 |
| 200 rupee | 128,307 | 130,040 |
| 500 rupee | 40,093,478 | 38,153,548 |
| 1000 rupee | 136,787,726 | 141,832,264 |
| 2000 rupee | 5,331,902 | 10,526,029 |
| 5000 rupee | 409,761,967 | 360,357,407 |
| | <u>627,120,254</u> | <u>585,327,577</u> |
| Total Currency in Circulation | <u>640,942,510</u> | <u>598,053,901</u> |

32. OTHER PAYABLES

| | 2018 | 2017 |
|---|-------------------|------------------|
| | Rs. 000 | Rs. 000 |
| Domestic Interest Payable | - | 1,676 |
| Provision and Charges | 1,706,541 | 396,531 |
| Deposits by RDD | 2,082,061 | 2,306,897 |
| Liability against Abandoned Properties Received (Note 32.1) | 6,188,502 | 5,083,171 |
| Other Payables | 2,629,327 | 1,098,881 |
| | 12,606,431 | 8,887,156 |

32.1 Payable in respect of Abandoned Properties represents the amounts collected from the Licensed Banks under the Banking Act Direction No.05 of 2009 - Identifying, Reporting, Transferring & Maintaining Abandoned Property of Licensed Commercial Banks. In the event of any further claims on Abandoned Properties, Bank is liable to pay deposits so collected with interest. Hence, the total deposit collected with the interest calculated on weighted average Treasury Bill interest rate is recorded as a liability of the Bank.

33. DEFERRED GRANTS

| | 2018 | 2017 |
|------------------------------|-----------|-----------|
| | Rs. 000 | Rs. 000 |
| As at 1 January | 45 | 80 |
| Amortization during the year | (34) | (35) |
| As at 31 December | 11 | 45 |

Deferred grant is amortized over the period that matches with the depreciation policy of such assets. This includes the assets received by the Bank without any consideration. The fair value of the assets have been credited to a deferred grant account and taken to other income over the useful life of the relevant asset consistent with the depreciation policy of the related asset.

34. PENSION AND OTHER POST EMPLOYMENT BENEFIT PLANS

The Bank operates seven defined benefit plans which cover all eligible employees. Under the Employees' Retirement Pension Scheme (old), employees who joined the Bank prior to 1 January 1998 and complete 10 years of service become eligible to the scheme. The employees who have joined the Bank after 1 January 1998 and complete 10 years of service become eligible for the new pension scheme. These pension schemes are non-contributory pension schemes where the cost of benefits is wholly borne by the Bank. The Widows' and Orphans' Pension Scheme for male employees and Widowers' and Orphans' Pension Scheme for female employees are open to employees of the Bank who had joined prior to 1 January 1998 whereas the new Widows' and Orphans and Widowers' and Orphans' Pension Scheme

is open for employees of the Bank who joined after 1 January 1998. Eligible employees under the Widows' and Orphans Pension Scheme (old) and Widowers' and Orphans' Pension Scheme (old) plans who were recruited before 1 August 1994 contribute 5% of the monthly basic salary & employees who were recruited on or after 1 August 1994 contribute 10% of the monthly basic salary whereas the eligible employees under the new Widows' and Orphans and Widowers' and Orphans' Pension Scheme contribute 5.5% of the monthly basic salary.

The Bank also provides gratuity benefits to employees who have completed five years of service in the Bank and who are not eligible for a monthly pension payment under the Employees' Retirement Pension Schemes. In order to meet this liability, a provision is carried forward in the Statement of Financial Position, equivalent to the liability calculated using the actuarial valuation.

The Bank has a Post-Employment Medical Benefit Scheme which provides reimbursement of certain medical expenses incurred by retired employees on account of themselves or their spouses and by widows/widowers.

The Bank employed an Independent Actuary M/s K. A. Pandit, Consultant & Actuary (Mumbai) to re-assess the defined benefit obligations and the current service costs attributable to the Employees' Retirement Pension Schemes, Widows' and Orphans' Pension Scheme, Widowers' and Orphans' Pension Scheme, Gratuity Scheme and Medical Benefit Scheme during the year. The bank employed the same Independent Actuary to assess the defined benefit obligations of the new Widows' and Orphans' and Widowers' and Orphans' Pension scheme for the first time during the year.

Funds of the Employee Retirement Pension Schemes, Widows' and Orphans' Pension Scheme, Widowers' and Orphans' Pension Scheme are managed separately and separate books are maintained. However, Gratuity Scheme and Medical Benefit Scheme are not separated from the books of accounts of the Bank. Further, investments and investment income are recorded separately for these funds in the Bank books and the income earned from the investments are transferred back to these funds and reinvested without being distributed.

The total present value of all benefit obligations of Rs. 48,245.66 Mn (2017 – Rs. 38,392.29 Mn) exceeds the total fair value of plan assets of Rs. 38,884.03 Mn (2017 – Rs. 40,816.60 Mn) at the end of the reporting period resulting in a deficit of Rs. 9,361.63 Mn (2017 – surplus of Rs. 2,424.31 Mn).

As at 31 December 2018

| Benefit (Asset)/Liability | Employee Retirement Pension Scheme | Employee Retirement Pension Scheme - New | Widows' and Orphans' Pension Scheme | Widowers' and Orphans' Pension Scheme | Widows' and Orphans' and Widowers' Pension Scheme - New | Gratuity Scheme | Medical Benefit Scheme | Total |
|---------------------------------------|------------------------------------|--|-------------------------------------|---------------------------------------|---|-----------------|------------------------|------------------|
| | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 |
| Present Value of Benefit Obligation | 35,971,523 | 1,055,695 | 6,241,591 | 1,199,154 | 718,088 | 290,932 | 2,768,680 | 48,245,663 |
| Fair Value of Plan Assets/Investments | (26,120,425) | (3,519,332) | (5,337,743) | (2,177,286) | (52,204) | (243,167) | (1,433,872) | (38,884,029) |
| Net Benefit (Asset)/Liability | 9,851,098 | (2,463,637) | 903,848 | (978,132) | 665,884 | 47,765 | 1,334,808 | 9,361,634 |

The balance shown under Pension and Other Post Employment Benefit Plans in Statement of Financial Position differs from the net liability as per the actuary due to the following reasons:

- The net asset position of the and Widowers' and Orphans' Pension Scheme is not reflected in the accounts due to the remote possibility of distributing any residual balance of the fund to the bank.
- For both gratuity and medical benefit schemes, the accounts represent the gross liability position and not the net liability as per actuary, since the Bank does not keep relevant assets in a separate fund (internally maintained).

| | 2018 Rs. 000 | 2017 Rs. 000 |
|--|-------------------|-----------------|
| Employee Retirement Pension Scheme | 9,851,097 | 892,685 |
| Employee Retirement Pension Scheme-New | (2,463,637) | (2,533,060) |
| Widows' and Orphans' Pension Scheme | 903,848 | - |
| Widowers' and Orphans' Pension Scheme | - | - |
| Widows' and Orphans' and Widowers' and Orphans' Pension Scheme - New | 665,884 | - |
| Gratuity Scheme | 290,932 | 153,167 |
| Medical Benefit Scheme | 2,768,680 | 2,158,269 |
| | 12,016,804 | 671,061 |

| Movement in the Benefit Liability/(Asset) | Employee Retirement Pension Scheme | Employee Retirement Pension Scheme - New | Widows' and Orphans' Pension Scheme | Widowers' and Orphans' Pension Scheme | Widows' and Orphans' and Widowers' Pension Scheme - New | Gratuity Scheme | Medical Benefit Scheme | Total |
|---|------------------------------------|--|-------------------------------------|---------------------------------------|---|-----------------|------------------------|------------------|
| | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 |
| As at 1 January 2018 | 892,685 | (2,533,060) | (424,605) | (1,279,273) | - | (22,218) | 942,158 | (2,424,313) |
| Benefit Expense | 283,821 | (294,427) | (88,343) | (176,350) | 665,884 | 14,991 | 145,554 | 551,130 |
| Amount recognized in Other Comprehensive Income | 9,059,635 | 567,448 | 1,416,796 | 477,491 | - | 54,992 | 247,096 | 11,823,458 |
| Contribution Paid | (385,044) | (203,598) | - | - | - | - | - | (588,642) |
| As at 31 December 2018 | 9,851,097 | (2,463,637) | 903,848 | (978,132) | 665,884 | 47,765 | 1,334,808 | 9,361,633 |

| Movement in the Present Value of Projected Benefit Obligations | Employee Retirement Pension Scheme | Employee Retirement Pension Scheme - New | Widows' and Orphans' Pension Scheme | Widowers' and Orphans' Pension Scheme | Widows' and Orphans' and Widowers' Pension Scheme - New | Gratuity Scheme | Medical Benefit Scheme | Total |
|---|---|---|--|--|--|------------------------|-------------------------------|-------------------|
| | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 |
| As at 1 January 2018 | 29,232,145 | 718,032 | 5,218,411 | 912,262 | - | 153,167 | 2,158,269 | 38,392,286 |
| Interest Cost | 3,800,179 | 93,344 | 678,393 | 118,594 | - | 19,912 | 280,575 | 4,990,997 |
| Current Service Cost | 167,772 | 34,871 | - | - | - | 17,879 | 30,481 | 251,003 |
| Past Service Cost | - | - | - | - | 718,088 | - | - | 718,088 |
| Benefit Paid From the Fund | (2,365,843) | (966) | (479,098) | (30,040) | - | (5,570) | (218,416) | (3,099,933) |
| Actuarial Losses on Obligations | 5,137,270 | 210,414 | 823,885 | 198,338 | - | 105,544 | 517,771 | 6,993,222 |
| As at 31 December 2018 | 35,971,523 | 1,055,695 | 6,241,591 | 1,199,154 | 718,088 | 290,932 | 2,768,680 | 48,245,663 |
| Movement in Fair Value of Plan Assets/ Investments | Employee Retirement Pension Scheme | Employee Retirement Pension Scheme - New | Widows' and Orphans' Pension Scheme | Widowers' and Orphans' Pension Scheme | Widows' and Orphans' and Widowers' Pension Scheme - New | Gratuity Scheme | Medical Benefit Scheme | Total |
| | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 |
| As at 1 January 2018 | 28,339,459 | 3,251,092 | 5,643,016 | 2,191,535 | - | 175,385 | 1,216,111 | 40,816,598 |
| Interest Income | 3,684,130 | 422,642 | 733,592 | 284,900 | 14,346 | 22,800 | 158,094 | 5,320,504 |
| Contributions by the Employer | 385,044 | 203,598 | - | - | - | - | - | 588,642 |
| Contributions by the Employees | - | - | 33,144 | 10,044 | 37,858 | - | 7,408 | 88,454 |
| Benefit Paid from the Fund | (2,365,843) | (966) | (479,098) | (30,040) | - | (5,570) | (218,416) | (3,099,933) |
| Return on Plan Assets, excluding Interest Income | (3,922,365) | (357,034) | (592,911) | (279,153) | - | 50,552 | 270,675 | (4,830,236) |
| As at 31 December 2018 | 26,120,425 | 3,519,332 | 5,337,743 | 2,177,286 | 52,204 | 243,167 | 1,433,872 | 38,884,029 |
| There are uncollateralized investments under Pension, Widows' and Orphans' fund, Widowers' and Orphans' fund, Gratuity and Medical Benefit Scheme fund worth of Rs. 522.23 Mn for which 100% provision has been made and thus not included in the value of plan assets. Even without the value of such investments, the Bank has a net asset position under its pension liability as per actuarial valuation. | | | | | | | | |
| Expenses Recognised in Other Comprehensive Income (OCI) for the Year Ended 31 December 2018 | Employee Retirement Pension Scheme | Employee Retirement Pension Scheme - New | Widows' and Orphans' Pension Scheme | Widowers' and Orphans' Pension Scheme | Widows' and Orphans' and Widowers' Pension Scheme - New | Gratuity Scheme | Medical Benefit Scheme | Total |
| | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 |
| Actuarial (Gains)/Losses on Obligations for the Period | | | | | | | | |
| Due to Change in Financial Assumptions | 3,809,336 | 200,760 | 638,640 | 156,561 | - | 76,750 | 460,701 | 5,342,748 |
| Due to Experience | 1,327,934 | 9,654 | 185,245 | 41,777 | - | 28,794 | 57,070 | 1,650,474 |
| Return on Plan Assets, excluding Interest Income | 3,922,365 | 357,034 | 592,911 | 279,153 | - | (50,552) | (270,675) | 4,830,236 |
| Net (Income)/Expense For the Period Recognized in OCI | 9,059,635 | 567,448 | 1,416,796 | 477,491 | - | 54,992 | 247,096 | 11,823,458 |
| Benefit Expense for the Year Ended of December 2018 | Employee Retirement Pension Scheme | Employee Retirement Pension Scheme-New | Widows' and Orphans' Pension Scheme | Widowers' and Orphans' Pension Scheme | Widows' and Orphans' and Widowers' Pension Scheme - New | Gratuity Scheme | Medical Benefit Scheme | Total |
| | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 |
| Interest Cost on Benefit Obligation | 3,800,179 | 93,344 | 678,393 | 118,594 | - | 19,912 | 280,575 | 4,990,997 |
| Interest Income on Plan assets | (3,684,130) | (422,642) | (733,592) | (284,900) | (14,346) | (22,800) | (158,094) | (5,320,504) |
| Current Service Cost | 167,772 | 34,871 | - | - | - | 17,879 | 30,481 | 251,003 |
| Past Service Cost | - | - | - | - | 718,088 | - | - | 718,088 |
| Contributions by the Employees | - | - | (33,144) | (10,044) | (37,858) | - | (7,408) | (88,454) |
| Benefit Expense | 283,821 | (294,427) | (88,343) | (176,350) | 665,884 | 14,991 | 145,554 | 551,130 |

| Composition of the Plan Assets | Employee Retirement Pension Scheme | Employee Retirement Pension Scheme-New | Widows' and Orphans' Pension Scheme | Widowers' and Orphans' Pension Scheme | Widows' and Orphans' and Widowers' Pension Scheme - New | Gratuity Scheme | Medical Benefit Scheme | Total |
|---|------------------------------------|---|-------------------------------------|---------------------------------------|---|------------------------|------------------------|-------------------|
| | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 |
| Investment in Government Securities | 18,951,019 | 3,138,194 | 3,665,611 | 1,682,559 | 43,131 | 214,815 | 1,150,734 | 28,846,063 |
| Investment in Reverse Repo | 219,425 | 21,471 | 44,950 | 26,096 | 3,883 | - | 4,013 | 319,838 |
| Investment in Debentures | 761,114 | 43,004 | 449,408 | 20,335 | - | 6,633 | - | 1,280,494 |
| Investment in Fixed Deposits | 6,173,983 | 315,885 | 1,176,978 | 448,149 | 4,848 | 21,719 | 279,125 | 8,420,687 |
| Balances Remaining in Current Accounts | 14,884 | 778 | 796 | 147 | 342 | - | - | 16,947 |
| Total Plan Assets as at 31 December 2018 | 26,120,425 | 3,519,332 | 5,337,743 | 2,177,286 | 52,204 | 243,167 | 1,433,872 | 38,884,029 |
| As at 31 December 2017 | | | | | | | | |
| Benefit (Asset)/Liability | Employee Retirement Pension Scheme | Employee Retirement Pension Scheme-New | Widows' and Orphans' Pension Scheme | Widowers' and Orphans' Pension Scheme | Gratuity Scheme | Medical Benefit Scheme | Total | |
| | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 |
| Present Value of Benefit Obligation | 29,232,145 | 718,032 | 5,218,411 | 912,262 | 153,167 | 2,158,269 | 38,392,286 | |
| Fair Value of Plan Assets/Investments | (28,339,460) | (3,251,092) | (5,643,016) | (2,191,535) | (175,385) | (1,216,111) | (40,816,599) | |
| Net Benefit (Asset)/Liability | 892,685 | (2,533,060) | (424,605) | (1,279,273) | (22,218) | 942,158 | (2,424,313) | |
| | | | | | | | | |
| Movement in the Benefit Liability/ (Asset) | Employee Retirement Pension Scheme | Employee Retirement Pension Scheme-New | Widows' and Orphans' Pension Scheme | Widowers' and Orphans' Pension Scheme | Gratuity Scheme | Medical Benefit Scheme | Total | |
| | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 |
| As at 1 January 2017 | 2,076,018 | (1,834,772) | (187,705) | (1,002,453) | (20,646) | 889,590 | (79,968) | |
| Benefit Expense | 480,203 | (208,897) | (24,402) | (130,319) | 12,698 | 144,685 | 273,968 | |
| Amount recognized in Other Comprehensive Income | (1,017,607) | (308,404) | (180,379) | (136,612) | (14,270) | (84,350) | (1,741,622) | |
| Contribution Paid | (645,929) | (180,987) | (32,119) | (9,889) | - | (7,767) | (876,691) | |
| As at 31 December 2017 | 892,685 | (2,533,060) | (424,605) | (1,279,273) | (22,218) | 942,158 | (2,424,313) | |
| | | | | | | | | |
| Benefit Expense for the Year Ended 31 December 2017 | Employee Retirement Pension Scheme | Employee Retirement Pension Scheme-New | Widows' and Orphans' Pension Scheme | Widowers' and Orphans' Pension Scheme | Gratuity Scheme | Medical Benefit Scheme | Total | |
| | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 |
| Net Interest Cost | 269,882 | (238,520) | (24,402) | (130,319) | (2,684) | 115,647 | (10,396) | |
| Current Service Cost | 210,321 | 29,623 | - | - | 15,382 | 29,038 | 284,364 | |
| Benefit Expense | 480,203 | (208,897) | (24,402) | (130,319) | 12,698 | 144,685 | 273,968 | |
| | | | | | | | | |
| Changes in Fair Value of Plan Assets/ Investments | Employee Retirement Pension Scheme | Employee Retirement Pension Scheme -New | Widows' and Orphans' Pension Scheme | Widowers' and Orphans' Pension Scheme | Gratuity Scheme | Medical Benefit Scheme | Total | |
| | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 |
| As at 1 January 2017 | 25,408,311 | 2,444,748 | 5,144,789 | 1,828,245 | 152,419 | 1,166,543 | 36,145,055 | |
| Actual Return on Plan Assets/ Investments | 4,375,497 | 627,231 | 849,631 | 375,242 | 37,653 | 253,174 | 6,518,428 | |
| Contribution Received | 645,929 | 180,987 | 32,119 | 9,889 | - | 7,767 | 876,691 | |
| Benefits Paid | (2,090,277) | (1,874) | (383,523) | (21,842) | (14,687) | (211,373) | (2,723,576) | |
| As at 31 December 2017 | 28,339,460 | 3,251,092 | 5,643,016 | 2,191,534 | 175,385 | 1,216,111 | 40,816,598 | |

The principal assumptions used in determining Employee Benefit Obligations for all the plans are shown below:

| | 2018 | 2017 |
|---|----------|----------|
| Discount Rate | 12.00% | 13.00% |
| Expected Rate of Return on Assets | 12.00% | 13.00% |
| Future Salary Increases - Medical Benefit Scheme | 8.50% | 8.50% |
| Rate of Salary Increases - Gratuity, W & OP, WR & OP, Old Pension Schemes | 11.50% | 8.50% |
| Rate of Salary Increase - Pension New, W & OP and WR & OP New | 6.50% | 6.50% |
| Future Pension Increases | 7.50% | 7.50% |
| Attrition Rate | 2.00% | 2.00% |
| Medical Cost Inflation Rate | 4.50% | 3.00% |
| Average Remaining years of Service | | |
| CBSL Pension | 26 Years | 27 Years |
| CBSL Pension - New | 38 Years | 41 Years |
| W & OP Pension Scheme | 26 Years | 27 Years |
| WR & OP Pension Scheme | 26 Years | 27 Years |
| W & OP and WR & OP Pension Scheme - New | 38 Years | - |
| Gratuity Scheme | 19 Years | 20 Years |
| CBSL Medical Benefit Scheme | 26 Years | 32 Years |
| Retirement Age | 60 Years | 60 Years |

Sensitivity Analysis at 0.5%
(As at 31 December 2018)

| | Employee Retirement Pension Scheme | Employee Retirement Pension Scheme-New | Widows' and Orphans' Pension Scheme | Widowers' and Orphans' Pension Scheme | Widows' and Orphans' and Widowers' Pension Scheme - New | Gratuity Scheme | Medical Benefit Scheme |
|--|------------------------------------|--|-------------------------------------|---------------------------------------|---|-----------------|------------------------|
| | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 |
| Projected benefit obligation on current assumptions | 35,971,523 | 1,055,695 | 6,241,591 | 1,199,154 | 718,088 | 290,932 | 2,768,680 |
| Effect of "+" change in discount rate | (1,508,089) | (106,827) | (298,931) | (68,243) | (79,520) | (11,697) | (105,627) |
| Effect of "-" change in discount rate | 1,628,425 | 121,759 | 326,649 | 74,734 | 92,308 | 12,548 | 114,320 |
| Effect of "+" change in attrition rate | - | - | - | - | - | 55,973 | 15,155 |
| Effect of "-" change in attrition rate | - | - | - | - | - | (61,945) | (16,016) |
| Effect of "+" change in salary escalation rate | 188,526 | 87,724 | 14,634 | 5,647 | 55,034 | 12,548 | - |
| Effect of "-" change in salary escalation rate | (183,845) | (80,157) | (14,279) | (5,510) | (50,354) | (11,799) | - |
| Effect of "+" change in Medical Cost Inflation | - | - | - | - | - | - | 115,653 |
| Effect of "-" change in Medical Cost Inflation | - | - | - | - | - | - | (106,871) |
| Effect of "+" change in Rate of Pension Escalation | 1,486,502 | - | 322,830 | 71,348 | - | - | - |
| Effect of "-" change in Rate of Pension Escalation | (1,393,434) | - | (298,617) | (65,954) | - | - | - |

35. MISCELLANEOUS LIABILITIES AND ACCRUALS

Miscellaneous liabilities and accruals include the balances payable in the accounts payable, contract retention, deposits taken as refundable tender deposits and the penalties payable by the Department of Foreign Exchange of Central Bank of Sri Lanka.

36. EQUITY

Nature of Equity Items

36.1 Capital Funds

Contributed Capital - The capital account represents the capital of the Bank in accordance with section 6 of the Monetary Law Act (MLA). As per the section 6 of the MLA (Amendment) Act No. 15 of 2014, the capital of the Bank has been increased to Rs. 50.0 Bn. Accordingly, the Bank has increased its capital up to Rs. 50.0 Bn by capitalizing the Bank's reserves with the concurrence of Minister of Finance in September 2014.

36.2 Fixed Asset Revaluation Reserve – This reserve is made up of the revaluation surpluses of Property, Plant and Equipment as per IAS 16.

36.3 Other Reserves comprise the following;

- International Revaluation Reserve (IRR)** : International Revaluation Reserve is a reserve established in accordance with section 41 of the Monetary Law Act which requires that any unrealised gain or loss arising from the revaluation of net assets and liabilities of CBSL in gold or foreign currency shall not be considered in computing the net profit of the Bank, instead such profit or loss should be transferred to the IRR.
- Market Revaluation Reserve (MRR)**: Market Revaluation Reserve was set up as per the Monetary Board decision of 30 January 2003, to transfer the price valuation gains from marking to market the foreign assets, in order to meet any adverse effects

of volatilities in the international markets leading to adverse movements in market prices of the foreign financial assets. The Monetary Board has decided to build up this reserve to a maximum of 10% of the gross foreign reserves of the Bank.

Further, as per the Monetary Board decision MB/DG (W)/7/1/2016 dated 29 February 2016 on proposed amendments to the Profit Distribution Policy of the Bank, where Monetary Board deems necessary, transfer may be made from the MRR to Retained Earnings, in the case of negative Retained Earnings due to significant unrealized marked to market losses.

Accordingly, an amount of Rs.19.43 Bn has been transferred to Retained Earnings from MRR in view of improving the negative Retained Earnings of the Bank.

Considering the marked to market gains recorded in 2017, an amount of Rs. 24.34 Bn was transferred to MRR from Retained Earnings in 2018 as per the Monetary Board decision BP MB/F/8/34/2018 dated 26 February 2018.

- iii). **Other Reserves** : Other reserves include General Reserve, Building Reserve and Credit Guarantee Reserve. General Reserve includes the amounts set aside from the retained earnings by the Monetary Board.
- iv). **Net Fair Value Gain/(Loss) on Securities at Fair Value through Other Comprehensive Income**: Unrealized gains and losses on the revaluation of securities and unit investments designated as Fair Value through Other Comprehensive Income are transferred to this reserve.
- v). **RTGS Sinking Fund** : This fund is built up with the charges collected from the participants for the use of the RTGS system.
- vi). **Pension Fund Reserve** : This reserve is made up by transferring an additional Rs.3.0 Bn from 2007 profits to be used to meet any shortfalls in the pension fund given the vulnerability of the income generating capacity of the Bank to external risks. Another Rs. 1.0 Bn have been transferred to this reserve from 2011 profits. During June 2015, Rs. 2.0 Bn has been transferred from Pension Fund Reserve to New Pension Liability Account to implement the new pension scheme as per Board Paper No: MB/HR/11/12/2015.

vii). **Technical Advancement Reserve** : This reserve is built up from 2007 profits specifically to be used for technical advancement requirements, modification or upgrading of the IT systems currently used by the Bank i.e., General Ledger, RTGS, Treasury Management System and Scriptless Securities Settlement System. During March 2018, an additional Rs. 2.0 Bn was transferred from 2017 profits to this reserve.

viii). **Provincial Development Credit Scheme** : During 2010, the Bank has commenced a refinance credit scheme for medium & long term development purposes for provinces by creating a fund from the profits, amounting to Rs. 2.90 Bn. Such loans are granted through Bank of Ceylon & People's Bank.

ix). **Special Credit Guarantee Scheme Reserve** : This reserve was set up in the year 2014 by transferring Rs. 2.0 Bn from Medium and Long Term Credit Fund, of which Rs. 1.0 Bn is allocated to support restructure of Saubaghyia Loan Scheme, Awakening North Loan Scheme (phase II), Resumption of Economic Activities in the East (phase II) and Repair of Damaged Houses in North and East operated by Regional Development Department of the Bank. The balance of Rs. 1.0 Bn is allocated to implement a special credit guarantee scheme to support lending to Small and Medium Enterprises by Commercial Banks.

x). **Reserve for Funding purpose of Post Employment Benefit Plans** : As per Monetary Board decision MB/F/39/20/2016 dated 16 December 2016, it is proposed to allocate 50 per cent of the benefit expenses of the actuary of a given year (starting from 2016) to a separate reserve, if there are adequate distributable profits with a view to compensate the possible negative impact to the equity attributed to actuarial losses and benefit expenses. Accordingly, CBSL has transferred an amount of Rs. 0.37 Bn in 2017. An additional amount of Rs. 5.0 Bn was transferred in anticipation of the possible impact to the equity of the bank from the Actuarial valuation of the guaranteed return of the Employee Provident Fund. No transfer had taken place for the year 2018 as the Bank does not have any distributable profits in 2018.

The movements in the other reserves are as follows:

| | Medium and Long Term Credit Reserve | Market Revaluation Reserve | Other Reserves | Special Credit Guarantee Scheme Reserve | RTGS Sinking Fund | IRR | Net Fair Value Gain/(Loss) on FVOCI Securities | Pension Fund Reserve | Technical Advancement Reserve | Provincial Development Credit Scheme Fund | Reserve for Funding purposes of Post Employment Benefit Plans | Total |
|--|-------------------------------------|----------------------------|----------------|---|-------------------|-------------|--|----------------------|-------------------------------|---|---|--------------|
| | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 |
| Balance as at 31 December 2017 | 1,925,000 | 14,028,792 | 10,952,533 | 2,000,000 | 1,826,818 | 8,573,729 | (3,563,157) | 2,000,000 | 1,000,000 | 2,900,000 | 689,025 | 42,332,740 |
| Transition Adjustment on IFRS 9 Reclassification Impact | - | - | - | - | - | - | 1,287,347 | - | - | - | - | 1,287,347 |
| Transition Adjustment for Expected Credit Losses on FVOCI Investments | - | - | - | - | - | - | 65,588 | - | - | - | - | 65,588 |
| Adjusted Balance as at 1 January 2018 | 1,925,000 | 14,028,792 | 10,952,533 | 2,000,000 | 1,826,818 | 8,573,729 | (2,210,222) | 2,000,000 | 1,000,000 | 2,900,000 | 689,025 | 43,685,675 |
| Transfer to RTGS Sinking Fund | - | - | - | - | 291,983 | - | - | - | - | - | - | 291,983 |
| Transfer of Profits to General Reserve | - | - | 5,013,869 | - | - | - | - | - | - | - | - | 5,013,869 |
| Transfer of Net Foreign Exchange Revaluation Gain | - | - | - | - | - | 146,854,048 | - | - | - | - | - | 146,854,048 |
| Net Fair Value Loss on Securities at Fair Value through Other Comprehensive Income | - | - | - | - | - | - | (877,778) | - | - | - | - | (877,778) |
| Transfer of Funds to Market Revaluation Reserve | - | 24,337,841 | - | - | - | - | - | - | - | - | - | 24,337,841 |
| Transfer to Reserve for funding purposes of Post-Employment Benefit | - | - | - | - | - | - | - | - | - | - | 5,372,178 | 5,372,178 |
| Transfer of Funds to Technical Advancement Reserve | - | - | - | - | - | - | - | - | 2,000,000 | - | - | 2,000,000 |
| Market Valuation Reserve - Government Securities Classified at Fair Value through Other Comprehensive Income | - | - | - | - | - | - | 5,259 | - | - | - | - | 5,259 |
| Market Valuation Reserve - Equity Investments Classified at Fair Value through Other Comprehensive Income | - | - | - | - | - | - | 122,747 | - | - | - | - | 122,747 |
| Expected Credit Losses on FVOCI Investments | - | - | - | - | - | - | (1,939) | - | - | - | - | (1,939) |
| Transfer of Funds to Retained Earnings | - | (19,426,472) | - | - | - | - | (16,289) | - | - | - | (1,727,706) | (21,170,467) |
| Balance as at 31 December 2018 | 1,925,000 | 18,940,161 | 15,966,402 | 2,000,000 | 2,118,801 | 155,427,777 | (2,978,222) | 2,000,000 | 3,000,000 | 2,900,000 | 4,333,497 | 205,633,416 |

37. PROFIT DISTRIBUTION

In terms of the Monetary Law Act and Monetary Board approved Profit Distribution Policy of CBSL (effective from 2018), the following adjustments are made to the net profit for the year in order to arrive at the distributable profit.

- Remove the exchange gains. Remove the exchange losses until the accumulated exchange gains are sufficient to absorb the losses. Charge any additional exchange losses (as per the Profit Distribution policy of CBSL).
- Remove gains from Unrealized Price Revaluations (unrealized "marked to market" gains) but charge

losses from Unrealized Price Revaluations (unrealized "marked to market" losses) (As per the Profit Distribution Policy of CBSL)

- Any other transfers to reserves as per Sec.38 of MLA and any other adjustments arising from Sec. 39 of MLA as decided by the Monetary Board.

Further, any other adjustment as required by accounting standards and management decisions are adjusted in arriving at the distributable profit.

Based on the above adjustments, the distributable loss for the year ended 31 December 2018 is as follows:

| Item | 2018 Rs. 000 |
|--|---------------------|
| Profit for the year | 137,927,718 |
| Less: | |
| Transfer of exchange gains to IRR in accordance with the MLA | 146,854,048 |
| Transfer of "marked to market" gain on foreign assets to Market Revaluation Reserve (MRR) | 1,166,516 |
| Other accounting adjustments | 463,842 |
| Transfer to Other Comprehensive Income (As per IAS 19 : Employee Benefits) | 11,823,458 |
| Add: | |
| Transfer from Reserve for funding purpose of Post Employment Benefit Plans to Retained Earnings | 1,727,706 |
| Distributable Loss as per MLA, Profit Distribution Policy of the Bank and other adjustments - Realised Loss | (20,652,440) |

38. INTEREST INCOME FROM FINANCIAL ASSETS

| | 2018 Rs. 000 | 2017 Rs. 000 |
|---|-------------------|-------------------|
| Interest Income from Foreign Currency Financial Assets | | |
| Cash and Short Term Deposits | 3,889,162 | 2,760,599 |
| Financial Assets | 13,588,824 | 6,170,100 |
| Derivatives | 8,078,946 | 13,984,017 |
| Total Interest Income from Foreign Currency Financial Assets | 25,556,932 | 22,914,716 |
| Interest Income from Local Currency Financial Assets | | |
| Sri Lanka Government Securities | 7,941,274 | 17,656,195 |
| Other Loans and Advances | 1,015,048 | 845,553 |
| Total Interest Income from Local Currency Financial Assets | 8,956,322 | 18,501,748 |
| Total Interest Income from Financial Assets | 34,513,254 | 41,416,464 |

39. GAIN/(LOSS) FROM UNREALIZED PRICE REVALUATIONS

| | 2018 Rs. 000 | 2017 Rs. 000 |
|---|---------------------|-------------------|
| Foreign Securities | 214,157 | (61,814) |
| Gold | (4,103,042) | 13,949,169 |
| Forex & Currency SWAPS | (14,882,288) | 9,702,099 |
| Currency Options | 511,217 | 411,021 |
| Total Gain/(Loss) from Unrealized Price Revaluations | (18,259,956) | 24,000,475 |

40. INTEREST EXPENSE ON FINANCIAL LIABILITIES

| | 2018 Rs. 000 | 2017 Rs. 000 |
|---|------------------|------------------|
| Interest Expense on Foreign Currency Financial Liabilities | | |
| Asian Clearing Union | 991,982 | 467,828 |
| IMF Related Liabilities | 3,862,093 | 1,900,742 |
| Derivatives | 486,325 | 210,877 |
| Other Foreign Payable | 9,755 | 383,784 |
| Total Interest Expense on Foreign Currency Financial Liabilities | 5,350,155 | 2,963,231 |
| Interest Expense on Local Currency Financial Liabilities | | |
| Securities Sold Under Repurchase Agreements | 925,379 | 1,023,720 |
| Standing Deposit Facility | 1,409,287 | 1,195,866 |
| Bond Borrowing | 15,882 | 1,716 |
| Abandoned Property | 529,672 | 454,814 |
| Total Interest Expense on Local Currency Financial Liabilities | 2,880,220 | 2,676,116 |
| Total Interest Expense on Financial Liabilities | 8,230,375 | 5,639,347 |

The Bank has a net sterilization gain of Rs. 10,041.78 Mn (2017 - Rs. 12,977.01 Mn) in its activities to inject the liquidity to the market due to the deficit liquidity position. The sterilization cost is composed of the interest expenses incurred on securities sold under agreement to repurchase, interest expense on Bond Borrowing and interest expense on Standing Deposit Facility netted off with interest income earned on the securities purchased under agreement to resale (Reverse Repurchase) included under interest income from Sri Lanka Government Securities and USD/LKR Derivative gain included in the Derivative gain under interest income from foreign currency financial assets, as discussed below:

| | 2018 Rs. 000 | 2017 Rs. 000 |
|--|-------------------|-------------------|
| Interest expenses incurred on securities sold under agreement to repurchase | 925,379 | 1,023,720 |
| Interest expense on Bond Borrowing | 15,882 | 1,716 |
| Interest expense on Standing Deposit Facility | 1,409,287 | 1,195,866 |
| Less: | | |
| Interest income earned on the securities purchased under agreement to resale | 4,313,387 | 1,214,298 |
| USD / LKR Derivative Gain | 8,078,946 | 13,984,017 |
| | 10,041,785 | 12,977,013 |

41. EXPECTED CREDIT LOSSES ON FINANCIAL ASSETS

| | 2018 Rs. 000 | 2017 Rs. 000 |
|--|-----------------|-----------------|
| Foreign Currency Financial Assets | | |
| Financial Assets at Amortized Cost | | |
| Cash & Cash Equivalents (Note 9.1) | (21,059) | - |
| IMF Related Assets (Note 12.4) | (1) | - |
| Securities at Fair Value through Other Comprehensive Income (Note 10.2) | 1,939 | - |
| Total Expected Credit Loss Reversals on Foreign Currency Financial Assets | (19,121) | - |
| Local Currency Financial Assets | | |
| Financial Assets at Amortized Cost | | |
| Loans to Banks (Note 16.2) | 488 | - |
| Other Assets (Note 18.1) | (11,462) | - |
| Credit Guarantee of RDD | 8 | - |
| Total Expected Credit Loss Reversals on Local Currency Financial Assets | (10,966) | - |
| Total Expected Credit Loss Reversals on Financial Assets | (30,087) | - |

42. OTHER INCOME

| | 2018 Rs. 000 | 2017 Rs. 000 |
|--|------------------|------------------|
| Dividend Income - Related Party | 126,111 | 104,601 |
| - Others | - | 2,540 |
| Gain/(Loss) on Disposal of Property, Plant & Equipment | 79,373 | (732) |
| Amortization of Deferred Grant | 34 | 34 |
| Licensing Fees of Financial Institutions | 580,950 | 555,975 |
| Rent Income | 402,429 | 485,515 |
| Charges collected from RTGS Participants | 123,361 | 119,606 |
| Miscellaneous Income | 380,736 | 335,125 |
| Total Other Income | 1,692,994 | 1,602,664 |

43. PERSONNEL EXPENSES

| | 2018 Rs. 000 | 2017 Rs. 000 |
|--|------------------|------------------|
| Wages and Salaries | 5,409,137 | 4,112,349 |
| Defined Contribution Plan Costs | 1,536,049 | 610,489 |
| Post Employee Defined Benefit Plan Costs | 205,147 | 744,356 |
| Total Personnel Expenses | 7,150,333 | 5,467,194 |

44. ADMINISTRATION AND OTHER EXPENSES

| | 2018 Rs. 000 | 2017 Rs. 000 |
|--|------------------|------------------|
| Repairs and Maintenance | 831,201 | 796,595 |
| Operating Expenses for Reuters, Bloomberg, SWIFT etc. | 162,735 | 122,260 |
| Travelling | 131,033 | 114,217 |
| Rental Expenses | 3,004 | 3,325 |
| Printing | 36,412 | 27,728 |
| Audit Fees | 11,199 | 10,412 |
| Remuneration to Members of the Monetary Board | 4,510 | 4,463 |
| Interest Subsidy on CBSL Provident Fund | 85,383 | - |
| Advertising Cost | 104,930 | 36,045 |
| Consultancy, Communication, Advisory and Professional Fees | 102,718 | 87,020 |
| Miscellaneous Expenses | 376,958 | 103,584 |
| Total Administration and Other Expenses | 1,850,083 | 1,305,649 |

45. TAX

The Bank is not liable for the income tax as per section 7b (xvi) of Inland Revenue (Amendment) Act No. 10 of 2006 and section 9 (1) of Inland Revenue Act No. 24 of 2017.

The Withholding Tax paid by the Bank till 31 March 2018 and Economic Service Charge paid by the bank is treated as the final tax paid to the Inland Revenue Department (IRD) as the requirement to pay withholding tax on government securities was removed with effect from 1 April 2018 by the Inland Revenue Act No. 24 of 2017.

During the year 2018, Bank paid a total tax of Rs. 1,119.29 Mn (2017 - Rs. 1,837.98 Mn) in relation to withholding tax of Rs. 268.08 mn (2017 - Rs. 1,837.98 Mn) and Economic Service Charge of Rs. 851.21 Mn (2017 - nil).

**46. RECONCILIATION OF OPERATING PROFIT
WITH OPERATING CASH FLOWS**

| | 2018 Rs. 000 | 2017 Rs. 000 |
|---|--------------------|--------------------|
| Reported Profit from Operating Activities | 137,927,718 | 48,356,367 |
| Add / (Less) Non-Cash Items | | |
| Depreciation & Amortization | 498,189 | 518,716 |
| Interest Received – Local Currency – Investment Portfolio | (7,941,272) | (17,911,409) |
| Bad Debts written Back | - | (27,302) |
| Net Provision for Defined Employee Benefit Plans | 390,483 | 236,269 |
| Gross Unrealised Foreign Exchange Gain | (149,861,582) | (9,595,724) |
| Profit on Sale of Property, Plant and Equipment | (79,381) | - |
| Provisions and Accruals | 2,288,287 | 489,509 |
| Expected Credit Loss Provision on Financial Assets | 30,086 | - |
| Deferred Grants | (34) | (34) |
| Amortization of PRGF Deposit | (7,747) | (6,804) |
| Write off of Construction in Progress | 22,402 | - |
| Amortization Expense of Fixed Income Securities | 109,525 | 883,659 |
| Add/ (Less) Movements in Other Working Capital Items | | |
| (Increase)/Decrease in Inventories | 306,597 | (760,672) |
| Decrease in Interest Receivable | 2,558,796 | 579,464 |
| Increase /(Decrease) in Miscellaneous Liabilities | (21,325) | 906,181 |
| Increase in Interest Payable | 1,075,371 | 219,716 |
| Increase in Other Receivable | (3,234,520) | (79,675) |
| Add /(Less) Investing and Financing Activities | | |
| Net Unrealised Market Value Changes | 12,201,892 | (25,110,720) |
| Net Cash Flows from Operating Activities | (3,736,515) | (1,302,459) |

**47. NET ISSUES/(WITHDRAWALS) OF CIRCULATION
CURRENCY ON GOVERNMENT TRANSACTIONS**

| | 2018 Rs. 000 | 2017 Rs. 000 |
|--|--------------------|----------------------|
| Purchases/(Sales) of Sri Lanka Government Securities | 241,803,062 | (315,960,919) |
| Interest Received – Local Currency – Sri Lanka Government Securities | (7,393,636) | (21,308,838) |
| Increase /(Decrease) in Advances to GOSL | (1,168,300) | 116,494,100 |
| (Increase) /Decrease in Balances with Government and Government Entities | (24,202) | 126,367 |
| | 233,216,924 | (220,649,290) |

**48. NET ISSUES/(WITHDRAWALS) OF CIRCULATION
CURRENCY ON BANK AND FINANCIAL
INSTITUTIONS TRANSACTIONS**

| | 2018 Rs. 000 | 2017 Rs. 000 |
|---|-------------------|---------------------|
| (Increase)/Decrease in Deposits by Banks and Financial Institutions | 23,010,511 | (38,460,908) |
| | 23,010,511 | (38,460,908) |

49. CONCENTRATIONS OF FUNDING

The Bank's significant end-of-year concentrations of funding were as follows:

| 49.1 Balance as at 31 December 2018 | Sri Lanka Government | Sri Lanka Public | Sri Lanka Commercial Banks | Supranational Financial Institutions | Other | Total |
|---|---------------------------------|-----------------------------|---|---|-------------------|----------------------|
| | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 |
| Foreign Currency Financial Liabilities | | | | | | |
| Banks and Financial Institutions | - | - | - | 811,552 | 18,489,608 | 19,301,160 |
| Derivative Financial Instruments | - | - | 12,156,003 | - | 1,900,457 | 14,056,460 |
| Asian Clearing Union | - | - | - | 79,158,977 | - | 79,158,977 |
| IMF | - | - | - | 416,988,246 | - | 416,988,246 |
| Other | 134,657,025 | - | - | 68,817 | 5,091 | 134,730,933 |
| Total Foreign Currency Financial Liabilities | 134,657,025 | - | 12,156,003 | 497,027,592 | 20,395,156 | 664,235,776 |
| Local Currency Financial Liabilities | | | | | | |
| Deposits of Banks and Financial Institutions | - | - | 319,922,749 | - | 183,434 | 320,106,183 |
| Deposits of Government and Government Entities | 348,681 | 37 | - | - | - | 348,718 |
| Securities Sold Under Repurchase Agreements | - | - | 16,741,679 | - | 11,569,542 | 28,311,221 |
| Balances of Employee Benefit Plans | - | - | - | - | 18,333 | 18,333 |
| Currency in Circulation | - | 640,942,510 | - | - | - | 640,942,510 |
| Other Payables | 103,736 | - | 2,082,061 | - | 10,420,634 | 12,606,431 |
| Total Local Currency Financial Liabilities | 452,417 | 640,942,547 | 338,746,489 | - | 22,191,943 | 1,002,333,396 |
| Total Financial Liabilities | 135,109,442 | 640,942,547 | 350,902,492 | 497,027,592 | 42,587,099 | 1,666,569,172 |
| Other Liabilities | | | | | | |
| Deferred Grants | - | - | - | - | 11 | 11 |
| Pension and Other Post Employment Benefit Plans | - | - | - | - | 12,016,804 | 12,016,804 |
| Miscellaneous Liabilities and Accruals | 2,562 | - | - | - | 83,383 | 85,945 |
| Total Other Liabilities | 2,562 | - | - | - | 12,100,198 | 12,102,760 |
| Total Liabilities | 135,112,004 | 640,942,547 | 350,902,492 | 497,027,592 | 54,687,297 | 1,678,671,932 |
| 49.2 Balance as at 31 December 2017 | | | | | | |
| Foreign Currency Financial Liabilities | | | | | | |
| Banks and Financial Institutions | - | - | - | - | 8,239,544 | 8,239,544 |
| Derivative Financial Instruments | - | - | 4,648,449 | - | - | 4,648,449 |
| Asian Clearing Union | - | - | - | 90,981,712 | - | 90,981,712 |
| IMF | - | - | - | 318,995,269 | - | 318,995,269 |
| Other | 62,497,163 | - | 1,193,019 | 200,757 | 204,950 | 64,095,889 |
| Total Foreign Currency Financial Liabilities | 62,497,163 | - | 5,841,468 | 410,177,738 | 8,444,494 | 486,960,863 |
| Local Currency Financial Liabilities | | | | | | |
| Deposits of Banks and Financial Institutions | - | - | 341,707,391 | - | 4,807 | 341,712,198 |
| Deposits of Government and Government Entities | 324,515 | 2 | - | - | - | 324,517 |
| Securities Sold Under Repurchase Agreements | - | - | 40,655,278 | - | - | 40,655,278 |
| Balances of Employee Benefit Plans | - | - | - | - | 4,547 | 4,547 |
| Currency in Circulation | - | 598,053,901 | - | - | - | 598,053,901 |
| Other Payable | 45,734 | - | 2,306,897 | - | 6,534,525 | 8,887,156 |
| Total Local Currency Financial Liabilities | 370,249 | 598,053,903 | 384,669,566 | - | 6,543,879 | 989,637,597 |
| Total Financial Liabilities | 62,867,412 | 598,053,903 | 390,511,034 | 410,177,738 | 14,988,373 | 1,476,598,460 |
| Other Liabilities | | | | | | |
| Deferred Grants | - | - | - | - | 45 | 45 |
| Pension and Other Post Employment Benefit Plans | - | - | - | - | 671,061 | 671,061 |
| Miscellaneous Liabilities and Accruals | 82,328 | - | - | - | 129,392 | 211,720 |
| Total Other Liabilities | 82,328 | - | - | - | 800,498 | 882,826 |
| Total Liabilities | 62,949,740 | 598,053,903 | 390,511,034 | 410,177,738 | 15,788,871 | 1,477,481,286 |

50. RISK MANAGEMENT

In pursuing Central Bank of Sri Lanka's (CBSL) policy objectives, it faces various risks, both financial and non-financial in nature. Since the materialization of any of these risks could have a severe impact on the financial position and the reputation of CBSL, a properly designed risk management framework is vital for CBSL. Recognizing the strategic importance of an integrated approach to risk management, led to the creation of a separate Risk Management Department (RMD) at CBSL in 2015 to overcome the conventional management of viewing risk in silos. Accordingly, risk management was recognized as a key strategic priority of the CBSL for 2018-2020 and the Bank is in the process of implementing an Enterprise-wide Risk Management (ERM) Framework for CBSL. This framework is intended to promote a culture of informed risk-taking at all levels of the Bank.

The Risk Governance Framework which was approved by the Monetary Board in July 2018 comprises both a Risk Governance Structure and a Risk Management Structure and covers both, financial and non-financial risks confronted by the Bank.

The Risk Governance Structure consists of the Monetary Board (MB), and two Board sub-committees, the Board Risk Oversight Committee (BROC) and the Monetary Board Advisory Audit Committee (MBAAC). The MB holds the ultimate responsibility for the overall risk management function of the Bank and sets the "Tone at the Top". Further, MB is responsible for setting the Risk Appetite and Risk Tolerance level for CBSL and approving the risk management/compliance framework.

The BROC was set up in August 2018 and is chaired by Mr. Chrishantha Perera, independent member of the Monetary Board and comprises external experts (Mr. Ravi Abeyesuriya, Director HNB Assurance from 01.08.2018 to 05.10.2018 and Mr. Priyan Fernando, Chairman Brandix and Senior Advisor, Boston Consulting Group from 05.10.2018 onwards). The BROC oversees CBSL's overall Risk Management and Compliance Functions via a formal delegation from the MB, and is responsible for laying the broad strategy and policies for the Bank's risk management and compliance functions. The BROC also assists the MB to ensure a dedicated focus on risk management and compliance at the Bank.

The Risk Management Structure that has been put in place follows the Three Lines of Defense model. In the first line of defense, operational departments are expected to identify, assess, control and mitigate risks and implement internal policies and procedures to ensure that activities carried out are consistent with the Bank's goals and objectives. The Risk Management Department assists in monitoring the implementation of effective risk management practices by operational management and independently reports risk related issues to the Risk Governance Structure creating a link between the Risk Management and Risk Governance Structures. The third line of defense, Internal Audit provides assurance on the effectiveness of governance, risk management and internal controls, including the manner in which the first and second lines of defense achieve risk management and control objectives. Each of these three 'lines' plays a distinct role within the Bank's risk governance framework.

In addition to facilitating non-financial risk management of all the departments under the three lines of defense model, RMD is also responsible for the financial risk management of the fund management activities of the International Reserves (IR), and the Internal Investment Funds (IIF) of CBSL, as well as the Employees' Provident Fund (EPF) which is carried out as an agency function for the Government. RMD revised the Investment Policy Statements (IPS) and Investment Guidelines (IG) for the EPF and IIF and set up Investment Oversight Committees (IOCs) to oversee these fund management activities. RMD also independently monitored market and credit risks pertaining to these fund management activities and reported risks emanating from them to the management. Market and credit risk indicators were presented at the monthly meetings of the Foreign Reserves Management Committee, where observations, from a risk perspective, on investment strategies and global market developments, were conveyed to the Committee. Similar meetings were convened for the IOCs of the EPF and IIF on a monthly basis, where risks and compliance issues pertaining to their investments were discussed.

In line with the new framework, RMD prepared a Risk Management Policy Statement (RMPS) for the CBSL, setting out the policies for implementation of risk management across CBSL. In this process, CBSL follows accepted standards and guidelines for managing risks, while assigning risk ownership and management among different stakeholders with clear accountability.

A survey was conducted amongst the Monetary Board and management of CBSL to determine the top bank-wide non-financial risks impacting the CBSL. The survey results would be used to develop a Risk Taxonomy for CBSL, which would help prioritize the bank-wide non-financial risk categories affecting CBSL and enable the management to concentrate on key risk categories that impact the institution.

Recognizing the importance of creating a risk culture within the bank, RMD conducted several risk awareness programs for CBSL staff throughout the year at various fora, with the involvement of RMD staff and external resource personnel.

With a view to strengthen the operational risk management function, RMD would secure technical assistance from the World Bank's Operational Risk Team to enhance risk governance and develop a risk management framework for the CBSL.

Going forward, RMD will continue to strive to create an environment to ensure that emerging risks that will have a material impact on

the CBSL, and any risk-taken beyond the risk appetite of the CBSL, would be recognized, escalated and addressed in a timely manner.

RMD will work with the operational departments to develop Risk Registers in a phased-out manner. Risk registers would enable the measurement of risk in a more consistent and uniform manner across all the operations in the bank. It would also provide risk information to the management to enable timely assessment and treatment of risks.

RMD will implement an Incident Reporting Mechanism in early 2019, to facilitate reporting of risk incidents affecting the CBSL to the management and to ensure that appropriate actions are implemented to address the causes of such incidents. This on-line Incident Reporting System, would be accessible to staff at all levels. This would facilitate the development of a central repository of risk events within the CBSL to serve as a basis for analyzing and assessing risk incidents, tracking progress on the implementation of corrective actions, identifying possible trends and areas of vulnerabilities and improving risk reduction measures.

With respect to financial risk management, RMD will further strengthen the risk management framework of the fund management activities and is in the process of reviewing the investment policies and guidelines for each of the funds managed by CBSL. RMD's focus would be on revisiting the credit risk policies and guidelines with a view to improving the credit risk management framework of the fund management activities of CBSL, covering CBSL's counterparties, issuers and custodians. In the meantime, RMD would continue to monitor credit and market risks pertaining to investments on an ongoing basis to ensure they are within the stipulated limits specified by the Monetary Board approved Strategic Asset Allocation (SAA), IPS and IG and highlight risks to the management at all times.

50.1 Credit Risk

(a) Concentrations of credit Exposure by geographical area

The Bank's significant end-of-year concentrations of credit exposure by geographical area (based on the entity's country of ownership) were as follows:

| | 2018 Rs. 000 | 2017 Rs. 000 |
|-------------------------------|----------------------|----------------------|
| Sri Lanka | 489,380,034 | 249,968,143 |
| USA | 665,241,791 | 643,710,289 |
| Japan | 95,625,902 | 18,253,104 |
| Britain | 9,869,079 | 28,946,605 |
| Europe | 118,939,171 | 94,190,661 |
| Supranational | 266,277,984 | 273,831,693 |
| Other | 96,953,618 | 142,897,782 |
| Total Financial Assets | 1,742,287,579 | 1,451,798,277 |

(b) Concentrations of Credit Exposure by Institutions

The Bank's significant end-of-year concentrations of credit exposure by Institution type were as follows:

| | 2018 Rs. 000 | 2017 Rs. 000 |
|---|----------------------|----------------------|
| Governments | 1,340,399,127 | 958,345,205 |
| Supranational Financial Institutions | 266,277,984 | 273,831,693 |
| Foreign Banks and Financial Institutions | 121,789,777 | 201,640,454 |
| Banks & Financial Institutions in Sri Lanka | 1,353,647 | 10,308,545 |
| Other | 12,467,044 | 7,672,380 |
| Total Financial Assets | 1,742,287,579 | 1,451,798,277 |

(c) Credit Exposure by Credit Rating

The following table represents the credit ratings of respective financial assets or issuers, based on the ratings of Standard and Poor's and Fitch Ratings. Under Standard & Poor's ratings and Fitch Ratings, AAA is the highest quality rating possible and indicates the lowest expectations of credit risk. It is assigned only in the case of exceptionally strong capacity for timely payment of financial commitment. AA is very high quality grade, indicating very low expectation of credit risk, and A is an upper medium grade, indicating a low expectation of credit risk; BBB is the lowest investment grade rating, indicating that there is currently a low expectation of credit risk and exhibits adequate protection parameters, ratings lower than AAA can be modified by + or - signs to indicate relative standing within the major categories. NR indicates that Standard and Poor's or Fitch Rating have not rated the entity.

Credit Exposure by Credit Rating**Cash & Cash Equivalents**

Federal Reserve Bank - USA/Reserve Bank of Australia/Bank for International Settlements/Bank of Japan/Deutsche Bundesbank/Bank of England/Sveriges Riksbank/Bank of Canada/Reserve Bank of New Zealand

| Credit Rating | 2018 Rs.000 | % | 2017 Rs.000 | % |
|--|----------------------|---------------|----------------------|---------------|
| | 327,240,508 | 18.78% | 310,350,210 | 21.38% |
| AAA | - | 0.00% | 50,158,566 | 3.45% |
| AA | 79,844 | 0.00% | 772,746 | 0.05% |
| AA- | 15,894,101 | 0.91% | 81,500,623 | 5.61% |
| A+ | 28,154,296 | 1.62% | 3,032,823 | 0.21% |
| A | 544,841 | 0.03% | 13,741,004 | 0.95% |
| A- | 51,131 | 0.00% | 84,841 | 0.01% |
| BBB- | 1,572 | 0.00% | 1,505 | 0.00% |
| NR | 208,883 | 0.01% | 185,323 | 0.01% |
| | 372,175,176 | 21.36% | 459,827,641 | 31.67% |
| Securities at Fair Value through Other Comprehensive Income/ Available for Sale | | | | |
| AAA | 137,844,494 | 7.91% | 62,060,643 | 4.27% |
| AA+ | 508,501,483 | 29.19% | 464,672,544 | 32.01% |
| AA | 3,892,615 | 0.22% | 1,862,308 | 0.13% |
| AA- | 26,115,880 | 1.50% | 13,360,972 | 0.92% |
| A+ | 13,325,830 | 0.76% | 21,867,283 | 1.51% |
| A | 196,616 | 0.01% | 298,956 | 0.02% |
| BBB+ | 134,539 | 0.01% | - | 0.00% |
| NR | 4,864,937 | 0.28% | 2,106,229 | 0.15% |
| | 694,876,394 | 39.88% | 566,228,935 | 39.00% |
| Securities at Fair Value through Profit or Loss | | | | |
| AAA | 26,605,392 | 1.53% | 23,517,574 | 1.62% |
| AA+ | 2,335,172 | 0.13% | 1,393,767 | 0.10% |
| AA | 4,861,898 | 0.28% | 3,593,798 | 0.25% |
| AA- | 1,385,016 | 0.08% | 1,174,551 | 0.08% |
| A+ | 367,606 | 0.02% | 309,062 | 0.02% |
| A | - | 0.00% | 15,275,623 | 1.05% |
| A- | (596,292) | -0.03% | - | 0.00% |
| BBB+ | 671,554 | 0.04% | - | 0.00% |
| NR | 1,836,893 | 0.11% | - | 0.00% |
| | 37,467,239 | 2.15% | 45,264,376 | 3.12% |
| Derivative Financial Instruments | | | | |
| Locally Rated | | | | |
| AAA | - | 0.00% | 979,560 | 0.07% |
| AA | - | 0.00% | 2,749,069 | 0.19% |
| AA- | 750 | 0.00% | 481,327 | 0.03% |
| A+ | - | 0.00% | 66,030 | 0.00% |
| A | - | 0.00% | 64,099 | 0.00% |
| A- | - | 0.00% | 387,706 | 0.03% |
| B | - | 0.00% | 24,265 | 0.00% |
| NR | - | 0.00% | 188,399 | 0.01% |
| | 750 | 0.00% | 4,940,455 | 0.33% |
| IMF Related Assets | | | | |
| | 147,427,452 | 8.46% | 126,842,946 | 8.74% |
| | 147,427,452 | 8.46% | 126,842,946 | 8.74% |
| Other Receivables | | | | |
| Locally Rated | | | | |
| AA+ | - | 0.00% | 3,072,381 | 0.21% |
| NR | 961,284 | 0.06% | - | 0.00% |
| NR | - | 0.00% | 593,319 | 0.04% |
| | 961,284 | 0.06% | 3,665,700 | 0.25% |
| Total Foreign Currency Financial Assets | 1,252,908,295 | 71.91% | 1,206,770,053 | 83.12% |

| | Credit Rating | 2018 Rs.000 | % | 2017 Rs.000 | % |
|---|---------------|----------------------|----------------|----------------------|----------------|
| Local Currency Financial Assets | | | | | |
| Sri Lanka Government Securities | B+ | - | 0.00% | 9,704,962 | 0.67% |
| | B | 45,031,157 | 2.58% | - | 0.00% |
| Securities Purchased under Agreements to Re-sell | B+ | - | 0.00% | 22,375,124 | 1.54% |
| | B | 229,454,409 | 13.17% | - | 0.00% |
| Provisional Advances to Government | B+ | - | 0.00% | 199,800,871 | 13.76% |
| | B | 198,632,571 | 11.40% | - | 0.00% |
| Loans to Banks | AA+ | 39,448 | 0.00% | 96,025 | 0.01% |
| | AA | - | 0.00% | 2,056 | 0.00% |
| | AA- | 1,233 | 0.00% | 2,493 | 0.00% |
| | A+ | 6,904 | 0.00% | 8,218 | 0.00% |
| | A- | 2,816 | 0.00% | 14,624 | 0.00% |
| | BBB | - | 0.00% | 1,449 | 0.00% |
| | BBB- | 523 | 0.00% | - | 0.00% |
| | BB+ | 17,704 | 0.00% | 39,692 | 0.00% |
| | B | - | 0.00% | 2,140 | 0.00% |
| | NR | 27,335 | 0.00% | 57,006 | 0.00% |
| Equity Investments in Financial and Other Institutions | NR | 1,381,879 | 0.08% | 41,095 | 0.00% |
| Other Assets | AAA | 198,899 | 0.01% | 135,457 | 0.01% |
| | AA+ | 996,102 | 0.06% | 919,142 | 0.06% |
| | AA | 55,313 | 0.00% | - | 0.00% |
| | A | 6,620 | 0.00% | 6,746 | 0.00% |
| | B+ | - | 0.00% | 5,443,809 | 0.37% |
| | B | 6,458,108 | 0.37% | - | 0.00% |
| | NR | 7,068,263 | 0.41% | 6,377,316 | 0.44% |
| Total Local Currency Financial Assets | | 489,379,284 | 28.09% | 245,028,224 | 16.88% |
| Total Financial Assets | | 1,742,287,579 | 100.00% | 1,451,798,277 | 100.00% |
| (d) Summary by Major Credit Category | | | | | |
| Foreign Currency Financial Assets | | | | | |
| Federal Reserve Bank - USA/Reserve Bank of Australia/Bank for International Settlements/ Bank of Japan/ Deutsche Bundesbank/Bank of England/ Sveriges Riks Bank/Bank of Canada/Reserve Bank of New Zealand IMF Related Assets | | 327,240,508 | 18.78% | 310,350,210 | 21.38% |
| | | 147,427,452 | 8.46% | 126,838,152 | 8.74% |
| | AAA | 164,449,886 | 9.44% | 135,741,577 | 9.35% |
| | AA+/- | 563,066,009 | 32.32% | 571,403,690 | 39.36% |
| | A+/- | 42,044,028 | 2.41% | 54,609,592 | 3.76% |
| | BBB+/- | 807,665 | 0.05% | 1,505 | 0.00% |
| | NR | 7,871,997 | 0.45% | 2,291,553 | 0.16% |
| Locally Rated | AAA | - | 0.00% | 979,560 | 0.07% |
| | AA | - | 0.00% | 2,749,069 | 0.19% |
| | AA- | 750 | 0.00% | 481,327 | 0.03% |
| | A+/- | - | 0.00% | 517,835 | 0.04% |
| | B | - | 0.00% | 24,265 | 0.00% |
| | NR | - | 0.00% | 781,718 | 0.05% |
| Total Foreign Currency Financial Assets | | 1,252,908,295 | 71.91% | 1,206,770,053 | 83.12% |
| Local Currency Financial Assets | AAA | 198,899 | 0.01% | 135,457 | 0.01% |
| | AA+ | 1,035,550 | 0.06% | 1,015,167 | 0.07% |
| | AA | 55,313 | 0.00% | 2,056 | 0.00% |
| | AA- | 1,233 | 0.00% | 2,493 | 0.00% |
| | A+ | 6,904 | 0.00% | 8,218 | 0.00% |
| | A | 6,620 | 0.00% | 6,746 | 0.00% |
| | A- | 2,816 | 0.00% | 14,624 | 0.00% |
| | BBB | - | 0.00% | 1,449 | 0.00% |
| | BBB- | 523 | 0.00% | - | 0.00% |
| | BB+ | 17,704 | 0.00% | 39,692 | 0.00% |
| | B+ | - | 0.00% | 237,324,767 | 16.35% |
| | B | 479,576,245 | 27.53% | 2,140 | 0.00% |
| | NR | 8,477,477 | 0.49% | 6,475,417 | 0.45% |
| Total Local Currency Financial Assets | | 489,379,284 | 28.09% | 245,028,224 | 16.88% |
| Total Financial Assets | | 1,742,287,579 | 100.00% | 1,451,798,277 | 100.00% |

50.2 Interest Rate Risk

(a) Foreign Currency Interest Rate Sensitivity

Interest rate risk is the risk of loss arising from the changes in interest rates.

The interest rate sensitivity of the Fixed Income Securities portfolio, except the investment in Reserve Advisory Management Program (RAMP), is measured by the potential gain or loss that could incur due to a change in interest rate by 10 basis points. The interest rate sensitivity of the fixed income securities portfolio held under RAMP is measured by the potential gain or loss that could incur due to a change in interest by 1 basis point. Sensitivity of the risk exposure of the segmented Fixed Income Securities Portfolio is given below:

| Portfolio Segment | Potential Loss (USD Mn) | |
|---|-------------------------|------|
| | 2018 | 2017 |
| Fair Value through Other Comprehensive Income/ Available for Sale | 7.86 | 7.55 |
| RAMP | 0.03 | 0.03 |

RMD manages the interest rate risk of the foreign assets portfolio by employing the following strategies:

- i) While the interest rate sensitivity measures the effect of a change in interest rates on the foreign assets portfolio, the Bank uses Modified Duration (MD) as a measurement of interest rate risk which considers interest rates as well as the duration of an investment. The MD measures the change in price of a security for a 1% change in the interest rates (yield). A higher MD indicates a higher risk. Hence, the Bank sets an appropriate MD from time to time considering the developments in the financial markets, portfolio characteristics and the risk appetite of the bond portfolio. The MDs of the foreign assets portfolio are tabulated below:

Modified Duration

| Investment Segment | Modified Duration | |
|--|-------------------|------|
| | 2018 | 2017 |
| Capital Market (Fixed Income Securities) | 2.08 | 2.02 |
| RAMP | 1.41 | 1.39 |

- ii) Since the MD does not account for large changes in prices, another measure used for management of interest rate risk of the foreign reserves portfolio is convexity. Convexity measures the extent of deviation in bond price-yield curve from a straight line representing duration. It allows improving the duration approximation for bond price changes. Convexity is a change in Duration for a change in yield. It measures the predictive error of Modified Duration. In other words, it is the second derivative of a security's price with respect to its yield.

Convexity of the segmented Fixed Income Securities portfolio

| Portfolio Segment | Potential Loss (USD Mn) | |
|---|-------------------------|------|
| | 2018 | 2017 |
| Fair Value through Other Comprehensive Income/ Available for Sale | 0.07 | 0.07 |
| RAMP | 0.04 | 0.04 |

iii) Value at Risk (VaR)

VaR summarizes in a single number the downside risk of the portfolio, under normal market conditions, from financial market movements. Therefore, VaR is the maximum loss over a target horizon such that there is a low, pre-specified probability that the actual loss will be larger. VaR gives a number, in terms of money, which can be aggregated across risks and positions. The Bank uses Monte Carlo method to calculate VaR number for 10 days period at 99% confidence interval for its fixed income securities portfolio except for the investment in RAMP. The VaR of the fixed income securities portfolio held under RAMP is measured using the Monte Carlo method for one month period at 99 % confidence interval.

| Portfolio Segment | Value at Risk (VaR) (USD) Mn | |
|---|------------------------------|-------|
| | 2018 | 2017 |
| Fair Value through Other Comprehensive Income/ Available for Sale | 19.94 | 22.98 |
| RAMP | 0.78 | 0.64 |

iv) Trading & Open Position Limits

Bank assigns specific dealer limits on intra-day and overnight position limits for individual dealers by way of "Dealing Authority".

Interest rate risk measures related to the investments in the Reserve Advisory Management Program (RAMP) is reported to the Foreign Reserve Management Committee on a regular basis.

(b) Local Currency Interest Rate Sensitivity

The local Treasury Bill portfolio is recorded in the Statement of Financial Position of the Bank at Fair Value through Other Comprehensive Income as per the Business Model assessment under IFRS 9. This portfolio is not an investment portfolio, as the Bank does not purchase Treasury Bills with the intention of earning an interest income. The Bank purchases or sells Treasury Bills to inject rupee liquidity into the domestic market or to absorb liquidity from the market in the course of carrying out its monetary policy operations in relation to one of its core objectives, maintaining economic and price stability. Hence, the volume of Treasury Bills in the Bank's portfolio is determined by its monetary policy operations. In addition, the basic interest rates in the rupee market, the Repo rate and the Reverse Repo rate are policy rates determined by the Bank in the course of implementing its monetary policy. Moreover, the Bank's actions in injecting rupee liquidity or absorbing liquidity from the market have a significant impact on general rupee market interest rates. Thus, changes in the interest income earned from the Treasury Bill portfolio, which arise from changes in the volume of the Bank's Treasury Bill portfolio, as well as changes in interest rates, are primarily a consequence of the Bank's monetary policy actions, rather than due to investment decisions. Therefore, the Bank does not consider interest rate sensitivities arising from local currency assets.

(c) Assets and liabilities will mature or re-price within the following Periods

| Foreign Currency Interest Rate Sensitivity Gap: | Weighted Avg. Int. Rate % | 2018 Total Rs. 000 | 6 Months or Less Rs. 000 | 6 to 12 Months Rs. 000 | 1 to 2 Years Rs. 000 | 2 to 5 Years Rs. 000 | Over 5 Years Rs. 000 |
|---|---------------------------|----------------------|--------------------------|------------------------|----------------------|----------------------|----------------------|
| Interest Sensitive Foreign Currency Financial Assets | | | | | | | |
| Cash & Cash equivalents | 1.9645 | 372,175,176 | 372,175,176 | - | - | - | - |
| Securities at Fair Value through Profit or Loss and Fair Value through Other Comprehensive Income | 2.4936 | 732,343,633 | 121,625,585 | 51,601,808 | 223,725,010 | 329,351,259 | 6,039,971 |
| IMF Related Assets | 1.0991 | 12,348,975 | 12,348,975 | - | - | - | - |
| Total Interest Sensitive Foreign Currency Financial Assets | | 1,116,867,784 | 506,149,736 | 51,601,808 | 223,725,010 | 329,351,259 | 6,039,971 |
| Non Interest Sensitive Foreign Currency Financial Assets | | | | | | | |
| IMF Related Assets | | 135,078,477 | 9,667 | - | - | 199,961 | 134,868,849 |
| Derivative Financial Instruments | | 750 | 750 | - | - | - | - |
| Other Receivables | | 961,284 | 961,284 | - | - | - | - |
| Total non Interest Sensitive Foreign Currency Financial Assets | | 136,040,511 | 971,701 | - | - | 199,961 | 134,868,849 |
| Total Foreign Currency Financial Assets | | 1,252,908,295 | 507,121,437 | 51,601,808 | 223,725,010 | 329,551,220 | 140,908,820 |
| Interest Sensitive Foreign Currency Financial Liabilities | | | | | | | |
| IMF | 2.1080 | 181,318,765 | - | - | - | 99,568,098 | 81,750,667 |
| Asian Clearing Union | 2.2345 | 79,158,977 | 79,158,977 | - | - | - | - |
| Total Interest Sensitive Foreign Currency Financial Liabilities | | 260,477,742 | 79,158,977 | - | - | 99,568,098 | 81,750,667 |
| Non Interest Sensitive Foreign Currency Financial Liabilities | | | | | | | |
| Banks and Financial Institutions | | 19,301,160 | 19,301,160 | - | - | - | - |
| Derivative Financial Instruments | | 14,056,460 | 11,736,595 | 1,853,550 | - | 466,315 | - |
| IMF | | 235,669,481 | - | - | - | - | 235,669,481 |
| Other Foreign Liabilities | | 134,730,933 | 134,730,933 | - | - | - | - |
| Total non Interest Sensitive Foreign Currency Financial Liabilities | | 403,758,034 | 165,768,688 | 1,853,550 | - | 466,315 | 235,669,481 |
| Total Foreign Currency Financial Liabilities | | 664,235,776 | 244,927,665 | 1,853,550 | - | 100,034,413 | 317,420,148 |
| Foreign Currency Interest Rate Sensitivity Gap | | 856,390,042 | 426,990,759 | 51,601,808 | 223,725,010 | 229,783,161 | (75,710,696) |

| | Weighted Avg. Int. Rate % | 2018 Total Rs. 000 | 6 Months or Less Rs. 000 | 6 to 12 Months Rs. 000 | 1 to 2 Years Rs. 000 | 2 to 5 Years Rs. 000 | Over 5 Years Rs. 000 |
|---|---------------------------------|--------------------------|--------------------------------|------------------------------|----------------------------|----------------------------|----------------------------|
| Interest Sensitive Local Currency Financial Assets | | | | | | | |
| Sri Lanka Government Securities | 12.8451 | 45,031,157 | 43,443,802 | 407,078 | - | 886,336 | 293,941 |
| Securities Purchased under Resale Agreements | 8.9950 | 229,454,409 | 229,454,409 | - | - | - | - |
| Loans to Banks | 7.7395 | 95,963 | 65,057 | 16,347 | 3,571 | 9,499 | 1,489 |
| Other Assets - Staff Loans | 4.2160 | 6,846,041 | 269,780 | 275,058 | 563,545 | 1,810,962 | 3,926,696 |
| - Others | 9.7553 | 7,792,394 | 470,308 | 1,012,421 | 1,417,860 | 1,105,413 | 3,786,392 |
| Total Interest Sensitive Local Currency Financial Assets | | 289,219,964 | 273,703,356 | 1,710,904 | 1,984,976 | 3,812,210 | 8,008,518 |
| Non Interest Sensitive Local Currency Financial Assets | | | | | | | |
| Provisional Advances to Government | | 198,632,571 | 198,632,571 | - | - | - | - |
| Other Assets - Others | | 144,870 | 144,870 | - | - | - | - |
| Investment in Equity Securities - Fair Value through Other Comprehensive Income | | 1,381,879 | - | - | - | - | 1,381,879 |
| Total Non Interest Sensitive Local Currency Financial Assets | | 200,159,320 | 198,777,441 | - | - | - | 1,381,879 |
| Total Local Currency Financial Assets | | 489,379,284 | 472,480,797 | 1,710,904 | 1,984,976 | 3,812,210 | 9,390,397 |
| Interest Sensitive Local Currency Financial Liabilities | | | | | | | |
| Standing Deposit Facility | 8.0000 | 28,311,221 | 28,311,221 | - | - | - | - |
| Total Interest Sensitive Local Currency Financial Liabilities | | 28,311,221 | 28,311,221 | - | - | - | - |
| Non Interest Sensitive Local Currency Financial Liabilities | | | | | | | |
| Deposits of Banks and Financial Institutions | | 320,106,183 | 320,106,183 | - | - | - | - |
| Deposits of Government and Government Entities | | 348,718 | 348,718 | - | - | - | - |
| Balances of Employee Benefit Plans | | 18,333 | 18,333 | - | - | - | - |
| Currency in Circulation | | 640,942,510 | 640,942,510 | - | - | - | - |
| Other Payables | | 12,606,431 | 12,606,431 | - | - | - | - |
| Total Non Interest Sensitive Local Currency Financial Liabilities | | 974,022,175 | 974,022,175 | - | - | - | - |
| Total Local Currency Financial Liabilities | | 1,002,333,396 | 1,002,333,396 | - | - | - | - |
| Local Currency Interest Rate Sensitivity Gap | | 260,908,743 | 245,392,135 | 1,710,904 | 1,984,976 | 3,812,210 | 8,008,518 |

Comparative figures as at 31 December 2017 were as follows:

| Foreign Currency Interest Rate Sensitivity Gap: | Weighted Avg. Int. Rate % | 2017 Total Rs. 000 | 6 Months or Less Rs. 000 | 6 to 12 Months Rs. 000 | 1 to 2 Years Rs. 000 | 2 to 5 Years Rs. 000 | Over 5 Years Rs. 000 |
|--|---------------------------|----------------------|--------------------------|------------------------|----------------------|----------------------|----------------------|
| Interest Sensitive Foreign Currency Financial Assets | | | | | | | |
| Cash & Cash equivalents | 1.5150 | 459,827,641 | 459,827,641 | - | - | - | - |
| Securities at Fair Value through Profit or Loss and Available for Sale Investments | 1.9158 | 596,217,687 | 87,922,743 | 76,479,327 | 118,516,346 | 313,299,271 | - |
| IMF Related assets | 0.5392 | 11,094,542 | 11,094,542 | - | - | - | - |
| Total Interest Sensitive Foreign Currency Financial Assets | | <u>1,067,139,870</u> | <u>558,844,926</u> | <u>76,479,327</u> | <u>118,516,346</u> | <u>313,299,271</u> | <u>-</u> |
| Non Interest Sensitive Foreign Currency Financial Assets | | | | | | | |
| IMF Related assets | | 115,748,404 | 4,794 | 164,564 | - | - | 115,579,046 |
| Derivative Financial Instruments | | 4,940,455 | 4,536,892 | 403,563 | - | - | - |
| Other Receivables | | 3,665,700 | 3,665,700 | - | - | - | - |
| Securities at Fair Value through Profit or Loss | | 15,275,624 | 15,275,624 | - | - | - | - |
| Total Non Interest Sensitive Foreign Currency Financial Assets | | <u>139,630,183</u> | <u>23,483,010</u> | <u>568,127</u> | <u>-</u> | <u>-</u> | <u>115,579,046</u> |
| Total Foreign Currency Financial Assets | | <u>1,206,770,053</u> | <u>582,327,936</u> | <u>77,047,454</u> | <u>118,516,346</u> | <u>313,299,271</u> | <u>115,579,046</u> |
| Interest Sensitive Foreign Currency Financial Liabilities | | | | | | | |
| IMF | 1.5480 | 116,996,460 | - | - | - | 49,873,486 | 67,122,974 |
| Asian Clearing Union | 1.2800 | 90,981,712 | 90,981,712 | - | - | - | - |
| Total Interest Sensitive Foreign Currency Financial Liabilities | | <u>207,978,172</u> | <u>90,981,712</u> | <u>-</u> | <u>-</u> | <u>49,873,486</u> | <u>67,122,974</u> |
| Non Interest Sensitive Foreign Currency Financial Liabilities | | | | | | | |
| Banks and Financial Institutions | | 8,239,544 | 8,239,544 | - | - | - | - |
| Derivative Financial Instruments | | 4,648,449 | 1,048,241 | 2,355,626 | 448,134 | 796,448 | - |
| IMF | | 201,998,809 | 329,937 | - | - | - | 201,668,872 |
| Other Foreign Liabilities | | 64,095,889 | 62,902,870 | - | - | - | 1,193,019 |
| Total Non Interest Sensitive Foreign Currency Financial Liabilities | | <u>278,982,691</u> | <u>72,520,592</u> | <u>2,355,626</u> | <u>448,134</u> | <u>796,448</u> | <u>202,861,891</u> |
| Total Foreign Currency Financial Liabilities | | <u>486,960,863</u> | <u>163,502,304</u> | <u>2,355,626</u> | <u>448,134</u> | <u>50,669,934</u> | <u>269,984,865</u> |
| Foreign Currency Interest Rate Sensitivity Gap | | <u>859,161,698</u> | <u>467,863,214</u> | <u>76,479,327</u> | <u>118,516,346</u> | <u>263,425,785</u> | <u>(67,122,974)</u> |

| | Weighted Avg. Int. Rate % | 2017 Total Rs. 000 | 6 Months or Less Rs. 000 | 6 to 12 Months Rs. 000 | 1 to 2 Years Rs. 000 | 2 to 5 Years Rs. 000 | Over 5 Years Rs. 000 |
|--|---------------------------------|--------------------------|--------------------------------|------------------------------|----------------------------|----------------------------|----------------------------|
| Interest Sensitive Local Currency Financial Assets | | | | | | | |
| Sri Lanka Government Securities | 8.9863 | 9,704,962 | 9,704,962 | - | - | - | - |
| Securities Purchased under Agreements to Re-sell | 8.7500 | 22,375,124 | 22,375,124 | - | - | - | - |
| Loans to Banks | 8.0891 | 223,702 | 110,409 | 44,126 | 54,599 | 10,049 | 4,519 |
| Other Assets - Staff Loans | 3.9834 | 6,105,830 | 231,580 | 238,514 | 486,331 | 1,543,517 | 3,605,888 |
| - Others | 10.2520 | 6,579,629 | 593,501 | 622,037 | 1,142,843 | 1,870,103 | 2,351,145 |
| Total Interest Sensitive Local Currency Financial Assets | | 44,989,247 | 33,015,576 | 904,677 | 1,683,773 | 3,423,669 | 5,961,552 |
| Non Interest Sensitive Local Currency Financial Assets | | | | | | | |
| Provisional Advances to Government | | 199,800,871 | 199,800,871 | - | - | - | - |
| Other Assets - Others | | 197,011 | 197,011 | - | - | - | - |
| Investment in Equity Securities - Available for Sale | | 41,095 | - | - | - | - | 41,095 |
| Total Non Interest Sensitive Local Currency Financial Assets | | 200,038,977 | 199,997,882 | - | - | - | 41,095 |
| Total Local Currency Financial Assets | | 245,028,224 | 233,013,458 | 904,677 | 1,683,773 | 3,423,669 | 6,002,647 |
| Interest Sensitive Local Currency Financial Liabilities | | | | | | | |
| Securities sold under Repurchase Agreements | 7.2500 | 6,503,884 | 6,503,884 | - | - | - | - |
| Standing Deposit Facility | 7.2500 | 34,151,394 | 34,151,394 | - | - | - | - |
| Total Interest Sensitive Local Currency Financial Liabilities | | 40,655,278 | 40,655,278 | - | - | - | - |
| Non Interest Sensitive Local Currency Financial Liabilities | | | | | | | |
| Deposits of Banks and Financial Institutions | | 341,712,198 | 341,712,198 | - | - | - | - |
| Deposits of Government and Government Entities | | 324,517 | 324,517 | - | - | - | - |
| Balances of Employee Benefit Plans | | 4,547 | 4,547 | - | - | - | - |
| Currency in Circulation | | 598,053,901 | 598,053,901 | - | - | - | - |
| Other Payables | | 8,887,156 | 8,887,156 | - | - | - | - |
| Total Non Interest Sensitive Local Currency Financial Liabilities | | 948,982,319 | 948,982,319 | - | - | - | - |
| Total Local Currency Financial Liabilities | | 989,637,597 | 989,637,597 | - | - | - | - |
| Local Currency Interest Rate Sensitivity Gap | | 4,333,969 | (7,639,702) | 904,677 | 1,683,773 | 3,423,669 | 5,961,552 |

50.3 Foreign Currency Risk

Foreign currency activities result mainly from the Bank's holding of foreign currency assets under its foreign reserve management function. Volatility of the foreign exchange markets may expose the Bank to exchange risk. The Monetary Board and Foreign Reserves Management Committee (FRMC) have set percentage holdings of different currencies in its International Reserves. In

deciding on the currency allocation, public debt repayment requirements are given due consideration. Accordingly, the Bank holds most major currencies such as US Dollars, Sterling Pounds, Japanese Yen, Euro, Australian Dollars and New Zealand Dollars. Compliance with limits established for foreign currency positions are monitored.

Net Exposure to Foreign Currencies

As at 31 December 2018, the net exposure of the Central Bank of Sri Lanka to major currencies were as follows:

| As at 31 December 2018 | Currency | | | | | | | | | Total All Currencies |
|---|-----------------------|--------------|---------------|----------------|---------------|--------------------|------------------|---------------------|------------------|----------------------|
| | United States Dollars | Euro | Japanese Yen | Sterling Pound | SDR | Australian Dollars | Canadian Dollars | New Zealand Dollars | Other Currencies | |
| | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 |
| Foreign Currency Financial Assets | | | | | | | | | | |
| Cash & Cash Equivalents | 567,599,621 | (74,694,623) | (152,407,729) | 92,299,209 | - | 130,349,501 | (132,506) | (10,045,385) | (180,721,348) | 372,246,740 |
| Securities at Fair Value through Profit or Loss and Fair Value through Other Comprehensive Income | 658,211,280 | - | 5,303,481 | 6,251,413 | - | 32,289,309 | - | 17,069,668 | 13,218,482 | 732,343,633 |
| Derivative Financial Instruments | - | - | - | - | - | - | - | - | 750 | 750 |
| IMF Related Assets | - | - | - | - | 147,427,456 | - | - | - | - | 147,427,456 |
| Other Receivables | 961,284 | - | - | - | - | - | - | - | - | 961,284 |
| Total Foreign Currency Financial Assets | 1,226,772,185 | (74,694,623) | (147,104,248) | 98,550,622 | 147,427,456 | 162,638,810 | (132,506) | 7,024,283 | (167,502,116) | 1,252,979,863 |
| Proportion | 97.91% | -5.96% | -11.74% | 7.87% | 11.77% | 12.98% | -0.01% | 0.56% | -13.37% | 100% |
| Foreign Currency Financial Liabilities | | | | | | | | | | |
| Banks and Financial Institutions | 19,299,921 | 444 | 1 | 57 | - | 737 | - | - | - | 19,301,160 |
| Derivative Financial Instruments | - | - | 1,900,457 | - | - | - | - | - | 12,156,003 | 14,056,460 |
| Asian Clearing Union | 79,158,977 | - | - | - | - | - | - | - | - | 79,158,977 |
| IMF | 811,552 | - | - | - | 416,176,694 | - | - | - | - | 416,988,246 |
| Other | 43,282,075 | - | - | - | - | - | - | - | 91,448,858 | 134,730,933 |
| Total Foreign Currency Financial Liabilities | 142,552,525 | 444 | 1,900,458 | 57 | 416,176,694 | 737 | - | - | 103,604,861 | 664,235,776 |
| Proportion | 21.46% | 0.00% | 0.29% | 0.00% | 62.65% | 0.00% | 0.00% | 0.00% | 15.60% | 100% |
| Net Foreign Currency Exposure | 1,084,219,660 | (74,695,067) | (149,004,706) | 98,550,565 | (268,749,238) | 162,638,073 | (132,506) | 7,024,283 | (271,106,977) | 588,744,087 |

Cash and Cash Equivalents include the foreign transactions entered into for buying and selling of various currencies of which the trade dates have been occurred in the current financial year and value dates to be fallen in the next financial year. Those transactions were as follows:

| As at 31 December 2018 | Sri Lanka Rupees Rs. 000 | United States Dollars Rs. 000 | Euro Rs. 000 | Sterling Pound Rs. 000 | Japanese Yen Rs. 000 | Australian Dollars Rs. 000 |
|--------------------------------------|--------------------------|-------------------------------|--------------|------------------------|----------------------|----------------------------|
| Purchases | 123,164,315 | 71,072,884 | - | - | - | - |
| Sales | - | (132,733,080) | - | - | (72,973,340) | - |
| FX Forward Contra Account - Near Leg | - | - | - | - | - | - |
| Forward contra account | 11,469,221 | - | - | - | - | - |

As at 31 December 2017, the net exposure of the Central Bank of Sri Lanka to major currencies were as follows:

| As at 31 December 2017 | Currency | | | | | | | | | |
|--|----------------------------------|---------------------|-------------------------|---------------------------|----------------------|-------------------------------|-----------------------------|--------------------------------|-----------------------------|---------------------------------|
| | United States Dollars Rs. 000 | Euro Rs. 000 | Japanese Yen Rs. 000 | Sterling Pound Rs. 000 | SDR Rs. 000 | Australian Dollars Rs. 000 | Canadian Dollars Rs. 000 | New Zealand Dollars Rs. 000 | Other Currencies Rs. 000 | Total All Currencies Rs. 000 |
| Foreign Currency Financial Assets | | | | | | | | | | |
| Cash & Cash Equivalents | 133,266,127 | (50,974,866) | (58,292,654) | 92,771,973 | - | 124,864,455 | 390,378 | (6,412,537) | 224,214,765 | 459,827,641 |
| Securities at Fair Value through Profit or Loss and Available for Sale | 532,783,747 | 3,676,937 | 6,297,818 | 5,302,523 | - | 34,445,694 | - | 11,011,941 | 17,974,651 | 611,493,311 |
| Investments | | | | | | | | | | |
| Derivative Financial Instruments | 536 | - | - | - | - | - | - | - | 4,939,919 | 4,940,455 |
| IMF Related Assets | - | - | - | - | 126,842,946 | - | - | - | - | 126,842,946 |
| Other Foreign Receivables | 3,665,700 | - | - | - | - | - | - | - | - | 3,665,700 |
| Total Foreign Currency Financial Assets | 669,716,110 | (47,297,929) | (51,994,836) | 98,074,496 | 126,842,946 | 159,310,149 | 390,378 | 4,599,404 | 247,129,335 | 1,206,770,053 |
| Proportion | 55.50% | -3.92% | -4.31% | 8.13% | 10.51% | 13.20% | 0.03% | 0.38% | 20.48% | 100% |
| Foreign Currency Financial Liabilities | | | | | | | | | | |
| Banks and Financial Institutions | 8,237,608 | 12 | - | - | - | - | - | - | 1,924 | 8,239,544 |
| Derivative Financial Instruments | - | - | - | - | - | - | - | - | 4,648,449 | 4,648,449 |
| Asian Clearing Union | 90,981,712 | - | - | - | - | - | - | - | - | 90,981,712 |
| IMF | - | - | - | - | 318,995,269 | - | - | - | - | 318,995,269 |
| Other | 19,241,566 | - | - | - | - | - | - | - | 44,854,323 | 64,095,889 |
| Total Foreign Currency Financial Liabilities | 118,460,886 | 12 | - | - | 318,995,269 | - | - | - | 49,504,696 | 486,960,863 |
| Proportion | 24.33% | 0.00% | 0.00% | 0.00% | 65.50% | 0.00% | 0.00% | 0.00% | 10.17% | 100% |
| Net Foreign Currency Exposure | 551,255,224 | (47,297,941) | (51,994,836) | 98,074,496 | (192,152,323) | 159,310,149 | 390,378 | 4,599,404 | 197,624,639 | 719,809,190 |

Cash and Cash Equivalents include the foreign transactions entered into for buying and selling of various currencies of which the trade dates have been occurred in the current financial year and value dates to be fallen in the next financial year. Those transactions were as follows:

| As at 31 December 2017 | Sri Lanka Rupees Rs. 000 | United States Dollars Rs. 000 | Euro Rs. 000 | Sterling Pound Rs. 000 | Japanese Yen Rs. 000 | Australian Dollars Rs. 000 |
|--------------------------------------|-----------------------------|----------------------------------|-----------------|---------------------------|-------------------------|-------------------------------|
| Purchases | 260,379,629 | (18,113,664) | 131,788 | (62,622) | (4,876) | (6,352,618) |
| Sales | (24,459,676) | (231,780,079) | 5,375,438 | 19,321,868 | 4,876 | 30,444 |
| FX Forward Contra Account - Near Leg | (1,667) | - | - | - | - | - |
| Forward contra account | (4,468,841) | - | - | - | - | - |

50.4 Contractual maturities of un-discounted cash flows of Financial Assets and Liabilities

As at 31 December 2018, Contractual maturities of un-discounted cash flows of Financial Assets and Liabilities are as follows,

| As at 31 December 2018 | Less than 6 months | 6 Months -1 Yr | 1-2 Yrs | 2-5 Yrs | Over 5 Yrs | Total |
|---|-----------------------|-------------------|--------------------|--------------------|----------------------|----------------------|
| | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 |
| Foreign Currency Financial Assets | | | | | | |
| Cash & Cash Equivalents | 372,175,176 | - | - | - | - | 372,175,176 |
| Securities at Fair Value through Profit or Loss | 38,478,059 | - | - | - | - | 38,478,059 |
| Securities at Fair Value through Other Comprehensive Income | 86,972,038 | 58,347,392 | 236,273,635 | 341,808,636 | 9,636,712 | 733,038,413 |
| IMF Related Assets | 12,358,642 | - | - | 199,961 | 134,868,849 | 147,427,452 |
| Other Receivables | 961,284 | - | - | - | - | 961,284 |
| Total un-discounted Foreign Financial Assets | 510,945,199 | 58,347,392 | 236,273,635 | 342,008,597 | 144,505,561 | 1,292,080,384 |
| Local Currency Financial Assets | | | | | | |
| Sri Lanka Government Securities | 42,861,171 | 1,928,480 | 128,960 | 1,150,405 | 384,130 | 46,453,146 |
| Securities Purchased under Resale Agreements to | 229,504,446 | - | - | - | - | 229,504,446 |
| Provisional Advances to Government | 198,632,571 | - | - | - | - | 198,632,571 |
| Loans to Banks | 66,536 | 17,009 | 4,119 | 10,333 | 1,520 | 99,517 |
| Equity Investments in Financial and Other Institutions | - | - | - | - | 1,381,879 | 1,381,879 |
| Other Assets | 14,716,611 | 1,729,014 | 2,777,236 | 4,487,198 | 11,525,061 | 35,235,120 |
| Total un-discounted Local Financial Assets | 485,781,335 | 3,674,503 | 2,910,315 | 5,647,936 | 13,292,590 | 511,306,679 |
| Total un-discounted Financial Assets | 996,726,534 | 62,021,895 | 239,183,950 | 347,656,533 | 157,798,151 | 1,803,387,063 |
| Foreign Financial Liabilities | | | | | | |
| Banks and Financial Institutions | 19,301,160 | - | - | - | - | 19,301,160 |
| Asian Clearing Union | 79,158,977 | - | - | - | - | 79,158,977 |
| IMF | 2,429,189 | 2,481,530 | 7,459,381 | 80,131,608 | 363,326,740 | 455,828,448 |
| Other | 134,730,933 | - | - | - | - | 134,730,933 |
| Total un-discounted Foreign Financial Liabilities | 235,620,259 | 2,481,530 | 7,459,381 | 80,131,608 | 363,326,740 | 689,019,518 |
| Local Currency Financial Liabilities | | | | | | |
| Deposits of Banks and Financial Institutions | 320,106,183 | - | - | - | - | 320,106,183 |
| Deposits of Government and Governmental Entities | 348,718 | - | - | - | - | 348,718 |
| Securities Sold Under Repurchase Agreements | 28,311,221 | - | - | - | - | 28,311,221 |
| Balances of Employee Benefit Plans | 18,333 | - | - | - | - | 18,333 |
| Currency in Circulation | 640,942,510 | - | - | - | - | 640,942,510 |
| Other Payables | 12,606,431 | - | - | - | - | 12,606,431 |
| Total un-discounted Local Financial Liabilities | 1,002,333,396 | - | - | - | - | 1,002,333,396 |
| Total un-discounted Financial Liabilities | 1,237,953,655 | 2,481,530 | 7,459,381 | 80,131,608 | 363,326,740 | 1,691,352,914 |
| Net un-discounted Financial Assets/ (Liabilities) | (241,227,121) | 59,540,365 | 231,724,569 | 267,524,925 | (205,528,589) | 112,034,149 |

| As at 31 December 2018 | Less than 6 months | 6 Months -1 Yr |
|----------------------------------|-----------------------|-------------------|
| | Rs. 000 | Rs. 000 |
| Derivative Financial Assets | 103,671,375 | 18,943,940 |
| Derivative Financial Liabilities | 114,165,546 | 19,919,739 |

Foreign Currency Conversions

All future cash flows related to Foreign Currency Financial Assets & Liabilities are converted to reporting currency using the rate of exchange prevailing at the reporting date.

As at 31 December 2017, Contractual maturities of un-discounted cash flows of Financial Assets and Liabilities are as follows,

| As at 31 December 2017 | Less than 6 months | 6 Months -1 Yr | 1-2 Yrs | 2-5 Yrs | Over 5 Yrs | Total |
|--|-----------------------|--------------------|--------------------|--------------------|----------------------|----------------------|
| | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 |
| Foreign Currency Financial Assets | | | | | | |
| Cash & Cash Equivalents | 459,827,641 | - | - | - | - | 459,827,641 |
| Securities at Fair Value through Profit or Loss | 21,369,496 | 4,465,690 | 13,178,459 | 8,851,636 | - | 47,865,281 |
| Available for Sale Investments | 46,372,253 | 94,705,246 | 126,493,457 | 322,848,221 | - | 590,419,177 |
| IMF Related Assets | 11,099,336 | - | - | 164,565 | 115,579,046 | 126,842,947 |
| Other Receivables | 3,665,700 | - | - | - | - | 3,665,700 |
| Total un-discounted Foreign Financial Assets | 542,334,426 | 99,170,936 | 139,671,916 | 331,864,422 | 115,579,046 | 1,228,620,746 |
| Local Currency Financial Assets | | | | | | |
| Sri Lanka Government Securities | 9,907,506 | - | - | - | - | 9,907,506 |
| Securities Purchased under Resale Agreements | 22,380,499 | - | - | - | - | 22,380,499 |
| Provisional Advances to Government | 199,800,871 | - | - | - | - | 199,800,871 |
| Loans to Banks | 114,827 | 46,409 | 56,593 | 11,274 | 4,697 | 233,800 |
| Equity Investments in Financial and Other Institutions | - | - | - | - | 41,095 | 41,095 |
| Other Assets | 14,901,062 | 1,189,827 | 2,713,417 | 4,296,510 | 8,129,740 | 31,230,555 |
| Total un-discounted Local Financial Assets | 247,104,765 | 1,236,235 | 2,770,010 | 4,307,784 | 8,175,531 | 263,594,325 |
| Total un-discounted Financial Assets | 789,439,191 | 100,407,171 | 142,441,927 | 336,172,205 | 123,754,577 | 1,492,215,071 |
| Foreign Financial Liabilities | | | | | | |
| Banks and Financial Institutions | 8,239,544 | - | - | - | - | 8,239,544 |
| Asian Clearing Union | 90,981,712 | - | - | - | - | 90,981,712 |
| IMF | 1,254,051 | 1,348,974 | 2,678,505 | 38,063,211 | 298,604,658 | 341,949,399 |
| Other | 62,902,870 | - | - | - | 1,193,019 | 64,095,889 |
| Total un-discounted Foreign Financial Liabilities | 163,378,177 | 1,348,974 | 2,678,505 | 38,063,211 | 299,797,677 | 505,266,544 |
| Local Currency Financial Liabilities | | | | | | |
| Deposits of Banks and Financial Institutions | 341,712,198 | - | - | - | - | 341,712,198 |
| Deposits of Government and Government Entities | 324,517 | - | - | - | - | 324,517 |
| Securities Sold Under Repurchase Agreements | 40,663 | - | - | - | - | 40,663 |
| Balances of Employee Benefit Plans | 4,547 | - | - | - | - | 4,547 |
| Currency in Circulation | 598,053,901 | - | - | - | - | 598,053,901 |
| Other Payables | 9,189,166 | - | - | - | - | 9,189,166 |
| Total un-discounted Local Financial Liabilities | 949,324,992 | - | - | - | - | 949,324,992 |
| Total un-discounted Financial Liabilities | 1,112,703,169 | 1,348,974 | 2,678,505 | 38,063,211 | 299,797,677 | 1,454,591,536 |
| Net un-discounted Financial Assets/ (Liabilities) | (323,263,978) | 99,058,197 | 139,763,422 | 298,108,994 | (176,043,100) | 37,623,535 |
| As at 31 December 2017 | | | | | | |
| Derivative Financial Assets | 178,883,331 | 57,169,395 | | | | |
| Derivative Financial Liabilities | 171,988,417 | 56,697,667 | | | | |

50.5 Liquidity Risk

Liquidity risk is the difficulty that an entity will encounter in raising funds at short notice to meet commitments associated with financial instruments. Liquidity risk is also the risk that an entity will have to sell a financial asset quickly at much less than its fair value

a) Liquidity is a key consideration in determining the composition of the Bank's foreign currency assets. This reflects the potential requirement to liquidate foreign reserves for intervention purposes and to settle other commitments such as public debt and IMF Loan repayments when the need arises. The Bank has adopted the following measures aimed at ensuring quick access to funds:

- Liquid asset ratios based on the liquidity characteristics of securities held
- Limits on maximum proportion of reserves that may be held in one currency and with one counterparty

b) In order to reduce the level of liquidity risk arising out of the local currency activities, particularly open market operations, the Bank uses highly liquid marketable instruments such as Treasury Bills and Treasury Bonds as collateral. It manages the daily liquidity position of the banking system by way of infusing into or withdrawal from the system, using instruments such as repo / reverse repo, CBSL securities and USD /LKR Swaps.

51. MATURITY ANALYSIS OF ASSETS & LIABILITIES

As at 31 December 2018

| | Less than 12 months Rs. 000 | Over 12 months Rs. 000 | Total Rs. 000 |
|---|-----------------------------------|------------------------------|----------------------|
| Assets | | | |
| Cash & Cash Equivalents | 372,175,176 | - | 372,175,176 |
| Securities at Fair Value through Profit or Loss | 9,975,116 | 27,492,123 | 37,467,239 |
| Securities at Fair Value through Other Comprehensive Income | 80,991,450 | 613,884,944 | 694,876,394 |
| Derivative Financial Instruments | 750 | - | 750 |
| IMF Related Assets | 12,358,642 | 135,068,810 | 147,427,452 |
| Other Foreign Receivables | 961,284 | - | 961,284 |
| Sri Lanka Government Securities | 43,874,997 | 1,156,160 | 45,031,157 |
| Securities Purchased under Resale Agreements | 229,454,409 | - | 229,454,409 |
| Provisional Advances to Government | 198,632,571 | - | 198,632,571 |
| Loans to Banks | 81,396 | 14,567 | 95,963 |
| Equity Investments in Financial and Other Institutions | - | 1,381,879 | 1,381,879 |
| Other Assets | 2,513,732 | 12,269,573 | 14,783,305 |
| Gold | - | 149,683,439 | 149,683,439 |
| Inventories | - | 6,568,935 | 6,568,935 |
| Other Receivables and Prepayments | 1,789,376 | 124,712 | 1,914,088 |
| Property, Plant and Equipment | - | 16,955,853 | 16,955,853 |
| Intangible Assets | - | 30,437 | 30,437 |
| Total Assets | 952,808,899 | 964,631,432 | 1,917,440,331 |
| Liabilities | | | |
| Banks and Financial Institutions | 19,301,160 | - | 19,301,160 |
| Derivative Financial Instruments | 14,056,460 | - | 14,056,460 |
| Asian Clearing Union | 79,158,977 | - | 79,158,977 |
| IMF | - | 416,988,246 | 416,988,246 |
| Other | 134,730,933 | - | 134,730,933 |
| Deposits by Banks and Financial Institutions | 320,106,183 | - | 320,106,183 |
| Balances with Government and Government Entities | 348,718 | - | 348,718 |
| Securities Sold Under Agreement to Repurchase | 28,311,221 | - | 28,311,221 |
| Balances with Employee Benefit Plans | 18,333 | - | 18,333 |
| Currency in Circulation | 640,942,510 | - | 640,942,510 |
| Other Payables | 12,606,431 | - | 12,606,431 |
| Deferred Grants | 6 | 5 | 11 |
| Pension and Other Post Employment Benefit Plans | - | 12,016,804 | 12,016,804 |
| Miscellaneous Liabilities and Accruals | 49,224 | 36,721 | 85,945 |
| Total Liabilities | 1,249,630,156 | 429,041,776 | 1,678,671,932 |
| Net | (296,821,257) | 535,589,656 | 238,768,399 |

| As at 31 December 2017 | Less than 12 months | Over 12 months | Total |
|--|------------------------|--------------------|----------------------|
| | Rs. 000 | Rs. 000 | Rs. 000 |
| Assets | | | |
| Cash & Cash Equivalents | 459,827,641 | - | 459,827,641 |
| Securities at Fair Value through Profit or Loss | 23,416,953 | 21,847,423 | 45,264,376 |
| Available for Sale Investments | 134,413,318 | 431,815,617 | 566,228,935 |
| Derivative Financial Instruments | 4,940,455 | - | 4,940,455 |
| IMF Related Assets | 11,099,336 | 115,743,610 | 126,842,946 |
| Other Foreign Receivables | 3,665,700 | - | 3,665,700 |
| Sri Lanka Government Securities | 9,704,962 | - | 9,704,962 |
| Securities Purchased under Resale Agreements | 22,375,124 | - | 22,375,124 |
| Provisional Advances to Government | 199,800,871 | - | 199,800,871 |
| Loans to Banks | 154,536 | 69,166 | 223,702 |
| Equity Investments in Financial and Other Institutions | - | 41,095 | 41,095 |
| Other Assets | 2,180,722 | 10,701,748 | 12,882,470 |
| Gold | - | 126,583,727 | 126,583,727 |
| Inventories | - | 6,875,533 | 6,875,533 |
| Other Receivables and Prepayments | 1,369,157 | 165,691 | 1,534,848 |
| Property, Plant and Equipment | - | 17,960,517 | 17,960,517 |
| Intangible Assets | - | 80,623 | 80,623 |
| Total Assets | 872,948,775 | 731,884,750 | 1,604,833,525 |
| Liabilities | | | |
| Banks and Financial Institutions | 8,239,544 | - | 8,239,544 |
| Derivative Financial Instruments | 4,648,449 | - | 4,648,449 |
| Asian Clearing Union | 90,981,712 | - | 90,981,712 |
| IMF | - | 318,995,269 | 318,995,269 |
| Other | 62,902,870 | 1,193,019 | 64,095,889 |
| Deposits by Banks and Financial Institutions | 341,712,198 | - | 341,712,198 |
| Balances with Government and Government Entities | 324,517 | - | 324,517 |
| Securities Sold Under Agreement to Repurchase | 40,655,278 | - | 40,655,278 |
| Balances with Employee Benefit Plans | 4,547 | - | 4,547 |
| Currency in Circulation | 598,053,901 | - | 598,053,901 |
| Other Payables | 8,887,156 | - | 8,887,156 |
| Deferred Grants | 34 | 11 | 45 |
| Pension and Other Post Employment Benefit Plans | - | 671,061 | 671,061 |
| Miscellaneous Liabilities and Accruals | 160,398 | 51,322 | 211,720 |
| Total Liabilities | 1,156,900,541 | 320,580,745 | 1,477,481,286 |
| Net | (285,951,766) | 411,304,605 | 127,352,239 |

52.1 Classification of Financial Assets and Financial Liabilities

The following table provides a reconciliation between line items in the Statement of Financial Position and categories of Financial Instruments

| As at 31 December 2018 | Mandatorily at FVTPL | FVOCI - Debt Instruments | FVOCI - Equity Instru- ments | Amortized Cost | Total |
|--|-------------------------|--------------------------------|------------------------------------|----------------------|----------------------|
| | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 |
| Foreign Currency Financial Assets | | | | | |
| Cash & Cash Equivalents | - | - | - | 372,175,176 | 372,175,176 |
| Securities at Fair Value through Profit or Loss | 37,467,239 | - | - | - | 37,467,239 |
| Securities at Fair Value through Other Comprehensive Income | - | 694,876,394 | - | - | 694,876,394 |
| Derivative Financial Instruments | 750 | - | - | - | 750 |
| IMF Related Assets | - | - | - | 147,427,452 | 147,427,452 |
| Other Receivables | - | - | - | 961,284 | 961,284 |
| Total Foreign Currency Financial Assets | 37,467,989 | 694,876,394 | - | 520,563,912 | 1,252,908,295 |
| Local Currency Financial Assets | | | | | |
| Sri Lanka Government Securities | - | 45,031,157 | - | - | 45,031,157 |
| Securities purchased under Resale Agreements | - | - | - | 229,454,409 | 229,454,409 |
| Provisional Advances to Government | - | - | - | 198,632,571 | 198,632,571 |
| Loans to Banks | - | - | - | 95,963 | 95,963 |
| Equity Investments in Financial and Other Institutions | - | - | 1,381,879 | - | 1,381,879 |
| Other Assets | - | - | - | 14,783,305 | 14,783,305 |
| Total Local Currency Financial Assets | - | 45,031,157 | 1,381,879 | 442,966,248 | 489,379,284 |
| Foreign Currency Financial Liabilities | | | | | |
| Banks and Financial Institutions | - | - | - | 19,301,160 | 19,301,160 |
| Derivative Financial Instrument | 14,056,460 | - | - | - | 14,056,460 |
| Asian Clearing Union | - | - | - | 79,158,977 | 79,158,977 |
| IMF | - | - | - | 416,988,246 | 416,988,246 |
| Other | - | - | - | 134,730,933 | 134,730,933 |
| Total Foreign Currency Financial Liabilities | 14,056,460 | - | - | 650,179,316 | 664,235,776 |
| Local Currency Financial Liabilities | | | | | |
| Deposits of Banks and Financial Institutions | - | - | - | 320,106,183 | 320,106,183 |
| Deposits of Government and Government Entities | - | - | - | 348,718 | 348,718 |
| Securities Sold Under Repurchase Agreements | - | - | - | 28,311,221 | 28,311,221 |
| Balances of Employee Benefit Plans | - | - | - | 18,333 | 18,333 |
| Currency in Circulation | - | - | - | 640,942,510 | 640,942,510 |
| Other Payables | - | - | - | 12,606,431 | 12,606,431 |
| Total Local Currency Financial Liabilities | - | - | - | 1,002,333,396 | 1,002,333,396 |

| As at 31 December 2017 | Trading | Available for Sale | Loans & Receivables | Held to Maturity | Total |
|--|-------------------|-----------------------|------------------------|---------------------|----------------------|
| | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 | Rs. 000 |
| Foreign Currency Financial Assets | | | | | |
| Cash & Cash Equivalents | - | - | - | 459,827,641 | 459,827,641 |
| Securities at Fair Value through Profit or Loss | 45,264,376 | - | - | - | 45,264,376 |
| Securities at Available for Sale | - | 566,228,935 | - | - | 566,228,935 |
| Derivative Financial Instruments | 4,940,455 | - | - | - | 4,940,455 |
| IMF Related Assets | - | - | - | 126,842,946 | 126,842,946 |
| Other Receivables | - | - | 3,665,700 | - | 3,665,700 |
| Total Foreign Currency Financial Assets | 50,204,831 | 566,228,935 | 3,665,700 | 586,670,587 | 1,206,770,053 |
| Local Currency Financial Assets | | | | | |
| Sri Lanka Government Securities | - | - | - | 9,704,962 | 9,704,962 |
| Securities purchased under Resale Agreements | - | - | - | 22,375,124 | 22,375,124 |
| Provisional Advances to Government | - | - | 199,800,871 | - | 199,800,871 |
| Loans to Banks | - | - | 223,702 | - | 223,702 |
| Equity Investments in Financial and Other Institutions | - | - | - | 41,095 | 41,095 |
| Other Assets | - | - | - | 12,882,470 | 12,882,470 |
| Total Local Currency Financial Assets | - | - | 200,024,573 | 45,003,651 | 245,028,224 |
| Foreign Currency Financial Liabilities | | | | | |
| Banks and Financial Institutions | - | - | - | 8,239,544 | 8,239,544 |
| Derivative Financial Instruments | 4,648,449 | - | - | - | 4,648,449 |
| Asian Clearing Union | - | - | - | 90,981,712 | 90,981,712 |
| IMF | - | - | - | 318,995,269 | 318,995,269 |
| Others | - | - | - | 64,095,889 | 64,095,889 |
| Total Foreign Currency Financial Liabilities | 4,648,449 | - | - | 482,312,414 | 486,960,863 |
| Local Currency Financial Liabilities | | | | | |
| Deposits of Banks and Financial Institutions | - | - | - | 341,712,198 | 341,712,198 |
| Deposits of Government and Government Entities | - | - | - | 324,517 | 324,517 |
| Securities Sold Under Repurchase Agreements | - | - | - | 40,655,278 | 40,655,278 |
| Balances of Employee Benefit Plans | - | - | - | 4,547 | 4,547 |
| Currency in Circulation | - | - | - | 598,053,901 | 598,053,901 |
| Other Payables | - | - | - | 8,887,156 | 8,887,156 |
| Total Local Currency Financial Liabilities | - | - | - | 989,637,597 | 989,637,597 |

53. FAIR VALUE DISCLOSURES

53.1 Fair Value of Assets and Liabilities

'Fair Value' is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal or, in its absence, the most advantageous market to which the Bank has access at that date. The fair value of a liability reflects its non-performance risk

The determination of fair value for financial assets and liabilities for which there is no observable market price requires the use of valuation techniques as described in accounting policy Note 5.2 For financial instruments that trade infrequently and have little price transparency, fair value is less objective, and requires varying degrees

of judgement depending on liquidity, concentration, uncertainty of market factors, pricing assumptions and other risks affecting the specific instrument. The fair value hierarchy of financial instruments is given below:

Level 1: Fair value measurements using quoted prices (unadjusted) in active markets for identical assets or liabilities;

Level 2: Fair value measurements using inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and

Level 3: Fair value measurements using inputs for the asset or liability that are not based on observable market data (i.e. unobservable inputs).

The following table shows an analysis of assets and liabilities recorded at fair value hierarchy:

| 31 December 2018 | Level 1 Rs. 000 | Level 2 Rs. 000 | Level 3 Rs. 000 | Total Rs. 000 |
|--|----------------------------|----------------------------|----------------------------|--------------------------|
| Financial Assets | | | | |
| Securities at Fair Value through Profit or Loss | 37,467,239 | - | - | 37,467,239 |
| Securities at Fair Value through Other Comprehensive Income | 694,876,394 | - | - | 694,876,394 |
| Derivatives | - | 750 | - | 750 |
| | <u>732,343,633</u> | <u>750</u> | <u>-</u> | <u>732,344,383</u> |
| Foreign Currency Non-Financial Assets | | | | |
| Gold | 149,683,439 | - | - | 149,683,439 |
| | <u>149,683,439</u> | <u>-</u> | <u>-</u> | <u>149,683,439</u> |
| Local Currency Financial Assets | | | | |
| Sri Lanka Government Securities | 44,986,598 | - | - | 44,986,598 |
| Equity Investments in Financial and Other Institutions | - | - | 1,381,879 | 1,381,879 |
| | <u>44,986,598</u> | <u>-</u> | <u>1,381,879</u> | <u>46,368,477</u> |
| Other Non-Financial Assets | | | | |
| Land | - | - | 8,930,375 | 8,930,375 |
| Building | - | - | 6,702,567 | 6,702,567 |
| | <u>-</u> | <u>-</u> | <u>15,632,942</u> | <u>15,632,942</u> |
| Financial Liabilities | | | | |
| Embedded Derivatives - Currency Options | - | - | 466,315 | 466,315 |
| Derivatives | - | 13,590,145 | - | 13,590,145 |
| | <u>-</u> | <u>13,590,145</u> | <u>466,315</u> | <u>14,056,460</u> |
| 31 December 2017 | Level 1 Rs. 000 | Level 2 Rs. 000 | Level 3 Rs. 000 | Total Rs. 000 |
| Financial Assets | | | | |
| Securities at Fair Value through Profit or Loss | 45,264,376 | - | - | 45,264,376 |
| Available for Sale Investments | 566,228,935 | - | - | 566,228,935 |
| Derivatives | - | 4,940,455 | - | 4,940,455 |
| | <u>611,493,311</u> | <u>4,940,455</u> | <u>-</u> | <u>616,433,766</u> |
| Foreign Currency Non-Financial Assets | | | | |
| Gold | 126,583,727 | - | - | 126,583,727 |
| | <u>126,583,727</u> | <u>-</u> | <u>-</u> | <u>126,583,727</u> |
| Local Currency Financial Assets | | | | |
| Sri Lanka Government Securities | 9,754,483 | - | - | 9,754,483 |
| | <u>9,754,483</u> | <u>-</u> | <u>-</u> | <u>9,754,483</u> |
| Other Non-Financial Assets | | | | |
| Land | - | - | 8,976,339 | 8,976,339 |
| Building | - | - | 7,515,327 | 7,515,327 |
| | <u>-</u> | <u>-</u> | <u>16,491,666</u> | <u>16,491,666</u> |
| Financial Liabilities | | | | |
| Embedded Derivatives - Currency Options | - | - | 1,244,581 | 1,244,581 |
| Derivatives | - | 3,403,868 | - | 3,403,868 |
| | <u>-</u> | <u>3,403,868</u> | <u>1,244,581</u> | <u>4,648,449</u> |
| Equity Investments in Financial and Other Institutions | | | | |
| Fair value of the equity investments were calculated using the Net Assets per Share valuation technique. | | | | |
| Significant unobservable input used | | | | |
| Net Asset Value per Share (NAVPS) | | | | |
| Sensitivity Analysis | | | | |
| A 10% increase in the NAVPS would increase the fair value by 10%. | | | | |
| | | | 2018 Rs. 000 | 2017 Rs. 000 |
| Balance as at 1 January | | | 41,095 | 41,095 |
| Fair Value Gain Recognised in the Other Comprehensive Income | | | 1,360,573 | - |
| Disposals during the Year | | | (19,789) | - |
| Balance as at 31 December | | | <u>1,381,879</u> | <u>41,095</u> |

Land & Buildings**Valuation Method**

Land is valued using market approach with direct comparison method, whereby assets are compared to recent sales with no added or nominal added improvement value, making adjustments for points of difference to derive the fair value.

Depreciated Current Replacement Cost (DRC) method is used in valuing all the buildings except Central Point, White Aways and Lloyds Building, considering that the assets controlled by the public sector entities that provide service to the community are not traded on an open liquid market.

Income approach is used to value the other buildings which values the property based on estimated future income, profits or cash flow that are converted (discounted) to a single current amount.

Under the Market Approach, estimated fair value would get increased/(decreased) if;

- Price per perch would get higher/(lower)
- Price per square foot would get higher/(lower)
- Depreciation rate for building would get lower/(higher)

Under Income Approach, estimated fair value would get increased/(decreased) if;

- Gross annual rentals would get higher/(lower)
- Years purchase would get higher/(lower)

Derivatives

Derivative valuation models use forward prices (calculated by extrapolating the forward points available in the market) and discount rates calculated based on zero coupon yield curves of the respective currencies as of the valuation date. If the instrument that is valued contains a margin, adjustments are made to the forward prices and/or the interest rates to represent the impact of the margin rate.

Embedded Derivatives - Currency Options

Fair Value of the Embedded Derivative Products was calculated using Black- Scholes model

| | 2018 Rs.000 | 2017 Rs.000 |
|---|----------------|----------------|
| Balance as at 1 January | 1,244,582 | 5,911,813 |
| Fair Value Loss recognised in the Statement of Income | (778,266) | (4,667,231) |
| Balance as at 31 December | 466,316 | 1,244,582 |

Significant unobservable inputs used

Discount Rate 10%

Volatility 4%

| Sensitivity Analysis | Discount Rate | | Volatility | |
|---|---------------|---------------|--------------|--------------|
| | 9% Rs.000 | 11% Rs.000 | 3% Rs.000 | 5% Rs.000 |
| Embedded Derivatives - Currency Options | 475,893 | 457,048 | 466,305 | 466,578 |

Deferred Asset on Embedded Derivatives

Balance as at 1 January

Premium Amortised during the year

Balance as at 31 December

| 2018 Rs.000 | 2017 Rs. 000 |
|----------------|-----------------|
| 369,455 | 4,625,665 |
| (267,049) | (4,256,210) |
| 102,406 | 369,455 |

53.2 Repurchase and Resale Agreements

The reported value of repurchase and resale agreements is considered to approximate their fair value due to short term nature of the agreements. The carrying value of the provided Standing Deposit Facility as at 31 December 2018 was Rs. 28,311.22 Mn (2017 - Rs. 34,151.39 Mn) and the carrying value of Sri Lanka Government Securities purchased under resale agreements as at 31 December 2018 was Rs. 229,454.41 Mn (2017 - Rs. 22,375.12 Mn). There was no outstanding Sri Lanka Government Securities sold under repurchase agreements as at 31 December 2018 (2017 - Rs. 6,503.88 Mn).

53.3 Currency in Circulation

The fair value of Currency in Circulation is considered to be its face value as reported in the Financial Statements.

53.4 Deposits

The carrying value of deposits are considered to approximate their fair value as they are payable on demand.

53.5 Determination of Fair Value and Fair Value Hierarchy

Set out below is a comparison, by class, of the carrying value and fair value of Bank's financial assets and liabilities other than those with carrying values that are reasonable approximation of fair value.

| | Carrying Amount | | Fair Value | |
|--|-----------------|-----------------|-----------------|-----------------|
| | 2018 Rs. 000 | 2017 Rs. 000 | 2018 Rs. 000 | 2017 Rs. 000 |
| Foreign Currency Financial Assets | | | | |
| Foreign Currency Trading/Securities at Fair Value through Other Comprehensive Income/Available for Sale Securities | 732,343,633 | 611,493,311 | 732,343,633 | 611,493,311 |
| Derivative Financial Instruments | 750 | 4,940,455 | 750 | 4,940,455 |
| Local Currency Financial Assets | | | | |
| Sri Lanka Government Securities | 45,031,157 | 32,080,086 | 45,031,157 | 32,129,607 |
| Loans to Banks | 95,963 | 223,702 | 92,601 | 214,077 |
| Other Assets | 14,783,305 | 12,882,470 | 12,947,767 | 9,702,999 |
| Foreign Currency Non Financial Assets | | | | |
| Allocated Gold | 149,683,439 | 126,583,727 | 149,683,439 | 126,583,727 |
| Foreign Currency Financial Liabilities | | | | |
| Derivative Financial Instruments | 14,056,460 | 4,648,449 | 14,056,460 | 4,648,449 |

54. COMPARATIVE INFORMATION

| As reported previously: | 2017 Rs. 000 |
|--|-------------------------|
| Foreign Currency Financial Assets | |
| IMF Related Assets | 126,838,152 |
| Other Receivables | 3,670,494 |
| Local Currency Financial Assets | |
| Sri Lanka Government Securities | 32,080,086 |
| Foreign Currency Financial Liabilities | |
| Banks and Financial Institutions | 8,683,033 |
| Asian Clearing Union | 90,868,160 |
| IMF | 318,665,332 |
| Income form Local Currency Financial Assets | |
| Interest Income | 18,768,928 |

| Current Presentation: | Note | 2018 Rs. 000 | 2017 Rs. 000 |
|--|-------------|-------------------------|-------------------------|
| Foreign Currency Financial Assets | | | |
| IMF Related Assets | 54.1 | 147,427,452 | 126,842,946 |
| Other Receivables | | 961,284 | 3,665,700 |
| Local Currency Financial Assets | | | |
| Sri Lanka Government Securities | 54.2 | 45,031,157 | 9,704,962 |
| Securities Purchased under Resale Agreements | | 229,454,409 | 22,375,124 |
| Foreign Currency Financial Liabilities | | | |
| Banks and Financial Institutions | 54.3 | 19,301,160 | 8,239,544 |
| Asian Clearing Union | | 79,158,977 | 90,981,712 |
| IMF | | 416,988,246 | 318,995,269 |
| Income form Local Currency Financial Assets | | | |
| Interest Income | 54.4 | 8,956,322 | 18,501,748 |
| Gain from Realised price changes | | 117,771 | 267,180 |

54.1 Interest receivable on the IMF Quota amounting to Rs. 4.79 Mn which was classified under Other Receivables in 2017 have now been included under IMF Related Assets for better presentation.

54.2 Outstanding balance of the reverse repurchase transactions and the Standing Lending Facility transactions amounting to Rs. 22,375.12 Mn which was classified under Sri Lanka Government Securities in 2017 have now been disclosed under Securities Purchased under Agreements to Re-sell.

54.3 Interest payables relating to IMF liabilities and ACU liabilities amounting to Rs. 329.94 Mn and Rs. 113.55 Mn respectively that was presented under Banks and Financial Institutions in 2017 have now been disclosed under liabilities of IMF and the Asian Clearing Union.

54.4 The realised gain on secondary sale of Sri Lanka Government Securities amounting to Rs. 267.18 Mn that was presented under Interest Income from local Currency Financial Assets have new been disclosed under Gain from Realised Price changes.

55. RELATED PARTIES**55.1 Transactions with State and State Controlled Entities**

In the normal course of its operations, the Bank enters into transactions with related parties. Related parties include the Government of Sri Lanka (State as the ultimate owner of the CBSL), various government departments, and State controlled entities. Particulars of transactions, and arrangements entered into by the Bank with the State and State controlled entities which are individually significant and for other transactions that are collectively, but not individually, significant as per IAS 24 -Amended Related Party Disclosures are as follows:

| Nature of the Transaction | 2018 Rs. 000 | 2017 Rs. 000 |
|--|-----------------|-----------------|
| Transactions: | | |
| Outright purchases of Government Securities | 20,458,308 | - |
| Outright sales of Government Securities | 58,674,669 | 74,237,317 |
| CBSL and Government Securities Purchased/Sold under Agreement to Repurchase/Sales | 4,800,410,194 | 4,311,989,631 |
| Interest income/expenses on CBSL and Government Securities Purchased/Sold under Agreement to Repurchase/Sales | 2,426,510 | 1,210,183 |
| Funds received on behalf of Government (Note 26.1 - 26.9) | 1,188,003,197 | 44,676,985 |
| Funds disbursed on behalf of Government (Note 26.1 - 26.9) | 1,144,407,670 | 17,346,423 |
| Cost of Printing currency notes, for the year ended 31 December (Note 55.1.3) | 1,605,463 | 1,906,625 |
| Payments for Goods, Services and Taxes, during the year ended 31 December (Note 55.1.4) | 2,234,657 | 2,744,815 |
| Gross Foreign Exchange Transactions during the period (Note 55.1.6) | | |
| Sales | 89,011,978 | 5,337,500 |
| Purchases | 25,078,570 | 85,719,851 |
| USD/LKR Derivatives | 221,347,285 | 751,569,889 |
| Funds Received in respect of Abandoned Property, during the year | 118,989 | 123,394 |
| Rent Income | 395,682 | 412,206 |
| Other Transactions (Note 55.1.10) | 1,392,785 | 996,174 |
| Balances: | | |
| Sri Lanka Government Securities held by CBSL (Note 55.1.7) | 45,031,157 | 9,704,962 |
| Provisional Advances to Government, (Note 15) | 198,632,571 | 199,800,871 |
| Loans given under Susahana Phase I and II, Provincial Development Credit Scheme, Saubaghyia Loan Scheme, Awakening North Loan Scheme (phase II), Resumption of Economic Activities in the East (phase II) and Repair of Damaged Houses in North and East | - | 28,254 |
| Government Securities held for specific purposes | 7,524,488 | 6,443,984 |
| RTGS Balances with Banks and Financial Institutions (Note 27) | 192,367,084 | 215,901,806 |
| Nostro Balance with BOC London | 209,155 | 185,324 |
| Receivable from Treasury and other Ministries | - | 54,490 |
| Payable to Treasury and other Ministries (Note 26) | 134,657,025 | 62,576,551 |
| Current Account Balances with Government and Government Entities as at 31 December | (141,802) | 84,833 |
| Abandoned Property balances | 2,571,814 | 2,257,579 |
| Other Balances (Note 55.1.10) | 212,877 | 599,623 |

55.1.1 Empowered by the sections 28-33 of the MLA the Bank Supervision Department of the Bank carries out regulatory and supervisory functions of the banks licensed by the Monetary Board of CBSL. As at 31 December 2018, 06 Licensed Commercial Banks and 01 Licensed Specialised Bank which had been funded by the Government or has a significant influence which are classified as related parties of the Central Bank of Sri Lanka.

The Department of Supervision of Non-Bank Financial Institutions of the Bank carries out its regulatory and supervisory functions in respect of Non-Bank Financial Institutions. Accordingly, related entities of state controlled or Government funded Non-Bank Financial Institutions are under the supervision of this department.

55.1.2 As per Section 113 of the MLA, the Monetary Board and the Bank are vested with the function of public debt management. Accordingly, as the agent of the Government, Public Debt Department (PDD) of the bank issues securities to the domestic market to meet the budgetary requirements and services both foreign and domestic debt. The PDD deals with public debt management and debt market development. It manages the Government debt to ensure that financing needs of the Government and its payment obligations are met.

55.1.3 The Bank has the sole right and authority to issue currency in Sri Lanka as per section 49 of the MLA. Accordingly, the Currency Department of the Bank functions as the sole issuing authority of the legal tender in Sri Lanka. Printing of the currency notes is carried out by De La Rue Lanka Currency and Security Print (Pvt) Ltd., of which 40% shareholding is owned by the Government.

55.1.4 In carrying out the normal operations, the Bank enters into transactions to obtain various goods and services with Government entities or entities in which Government has significant influence or control.

55.1.5 The Bank commonly acts as trustees and in other fiduciary capacities that result in the holding or placing of assets and liabilities on behalf of Government, trusts, retirement benefit plans and other institutions, as explained in Note 58.

55.1.6 In accordance with the provisions of the MLA, International Operations Department of the Bank monitors the development in the domestic foreign exchange market and overnight net foreign exchange open positions of commercial banks. In monitoring the domestic foreign exchange market developments, the Bank is on both

sides of the market to moderate the excessive volatility in the exchange rate of Sri Lankan Rupee. The amounts of purchases and sales of foreign exchange represents results of such monitoring activities.

55.1.7 The Domestic Operations Department of the Bank performs its direct functions of implementing the Bank's monetary policy mainly through open market operations as per sections 90-92 of the MLA No. 58 of 1949 (amended) and enforcing Statutory Reserve Requirement as per sections 93-98 of MLA and functions as the banker to both commercial banks where Government has shareholdings and certain other financial institutions and Governmental entities. The aggregate balances arising from this function as at 31 December 2018 are given in Notes 28 and 29. Interest earned on the Government securities is given in Note 38.

55.1.8 The Bank also has custodial arrangements with one State-controlled bank, for which no charges were levied.

55.1.9 As per the circular issued by Director of Bank Supervision, the banks that do not maintain the minimum advance limit of 10% to agriculture, contribute the shortfall to Refinance Fund operated by RDD of the bank. As at 31 December 2018, no loans were outstanding under the specified refinance scheme (as at 31 December 2017, Rs. 6.83 Mn loans were outstanding under the refinance scheme from People's Bank - Rs. 2.46 Mn, Bank of Ceylon - Rs. 1.88 Mn, Pradeshiya Sanwardana Bank - Rs. 0.63 Mn and Lankaputhra Development Bank - Rs. 1.86 Mn) for which RDD has received an interest of Rs. 99.36 Mn (as at 31 December 2017 Rs. 99.19 Mn).

55.1.10 Other Balances and transactions include the transactions carried out with the Government, Government departments and state controlled entities that are not individually significant.

55.2 Transactions with Key Management Personnel

Key Management Personnel of the Bank are the members of the Monetary Board that includes Governor, Deputy Governors and Assistant Governors. Particulars of transactions with Key Management Personnel were as follows:

55.3 Compensations to the Key Management Personnel

| | 2018 Rs. 000 | 2017 Rs. 000 |
|------------------------------|-----------------|-----------------|
| Short Term Employee Benefits | 161,833 | 123,072 |

In addition to above compensation, the Bank also provides non cash benefits to Key Management Personnel in terms of the employment contracts with them.

55.4 Other Transactions with Key Management Personnel

| | 2018 Rs. 000 | 2017 Rs. 000 |
|-----------------------------------|-----------------|-----------------|
| Loans to Key Management Personnel | 71,459 | 73,141 |

All the loans are adequately secured and carry interest rates ranging from 2% - 7% depending on the loan category and are repayable monthly.

55.5 Transactions with Post-Employment Benefit Plans

| | 2018 Rs. 000 | 2017 Rs. 000 |
|--------------------------------|-----------------|-----------------|
| Contributions paid and payable | 82,798 | 69,573 |

The Bank contributed various amounts to Pension and Other Post Retirement Plans as disclosed in Note 34 and paid Rs. 718.71 Mn (2017 – Rs. 542.58 Mn) to Employees Provident Fund. In the normal course of business, the Bank provides banking and financial services to its post employment plans. Amounts of balances with such plans are given in Note 30.

56. CONTINGENT LIABILITIES AND COMMITMENTS

56.1 Financial Guarantee Contracts

The Bank acting as an agent of the Government or its agencies and institutions, provides guarantees to various parties on the strength of counter guarantees issued to Bank by the General Treasury. There were no such outstanding guarantees as at 31 December 2018.

56.2 Credit Guarantees

The Regional Development Department (RDD) of the Bank performs the functions of providing refinance out of loan proceeds from external lines of credit to participating financial institutions for financing small and medium enterprises, issuing credit guarantees on loans to such enterprises, collecting guarantee premia, administering credit guarantee funds and undertaking post credit inspection and follow up action to ensure proper utilization of loan funds with a view of preventing defaults. During the year, RDD continued to provide refinance facilities under which the Bank provided guarantees against losses arising to a participating credit institution, which grants credit under this arrangement. This is not a guarantee on default by recipient of loans but against loss, which means that participating credit institutions should submit claims only in respect of amounts in loss after having pursued recovery action. The amount of contingent liabilities arising out of this arrangement are given below.

Local commercial banks - in respect of credit guarantees.

| | Outstanding Guarantee Amount | |
|-------------------------|------------------------------|-----------------|
| | 2018 Rs. 000 | 2017 Rs. 000 |
| Related Parties | 784 | 1,798 |
| Total Credit Guarantees | 784 | 1,798 |

The Bank has recorded an expected credit loss of Rs. 0.40 Mn as at the year ended 31 December 2018 (Rs. 0.41 Mn as at 1 January 2018) in respect of the credit guarantees on local commercial banks.

56.3 Fiduciary Activities

The Bank carries out fiduciary activities under the provisions of the MLA. Acting in such capacity results in holding or placing of funds on behalf of various parties. However, the Bank does not expect any liability to arise on account of such activities.

56.4 Legal Claims

There were number of legal proceedings outstanding against the Bank as at 31 December 2018 and no provision has been made as the Bank is of the opinion that it is unlikely that any significant loss will arise.

56.5 Commitments

- As at 31 December 2018, the Bank has capital commitments amounting to Rs. 577.99 Mn, in respect of the acquisition of Property, Plant and Equipment.
- As at 31 December 2018, outstanding forward exchange transactions are as follows:

| Forward exchange contracts | | 2018 '000 | 2017 '000 |
|----------------------------|-----|--------------|--------------|
| | | | |
| Forward Exchange Sales | USD | 726,310 | 1,850,735 |
| | EUR | - | 2 |
| Forward Exchange Purchases | USD | 388,908 | 5,000 |
| | EUR | - | 400 |

57. TRANSFERS OF FINANCIAL ASSETS

In the ordinary course of business, the Bank enters into transactions that result in the transfer of financial assets, primarily both foreign and local currency denominated debt securities. In accordance with the accounting policy set out in Note 5.3.3, the transferred financial assets continue to be recognised in their entirety or to the extent of the Bank's continuing involvement or are derecognised in their entirety.

The Bank transfers financial assets that are not derecognised in their entirety or for which the Bank has continuing involvement primarily through the following transactions:

Securities Sold under Agreements to Repurchase
Securities Lending
Securities Pledged

57.1 Transferred Financial Assets that are not derecognized in their Entirety**a. Securities Sold under Agreements to Repurchase**

Securities sold under agreements to repurchase transactions are performed as part of the Monetary Policy operations of the Bank and continues to be recognized in their entirety under "Sri Lanka Government Securities" in the Statement of Financial Position because it retains substantially all of the risks and rewards of ownership. The cash consideration to be paid and the interest accrued there on are recognized under Securities sold under repurchase agreements in the local financial liabilities of the Statement of Financial Position.

b. Securities Lending

Securities lending describes the established market practice by which, for a fee, securities are transferred temporarily from one party (the lender, i.e. CBSL), to another (the borrower); the borrower is obliged to return them either on demand or at the end of any agreed term. Currently a selected Clearing House (CH) functions as the custodian for the supranational bonds and bonds issued by different issuers. CBSL has signed an agreement which enable CH to lend at their wish depending on the demand for those bonds. Since the lending does not involve CBSL and CH lends them directly to the borrowers, the process is called auto bond lending. At the end of each month, custodian will send fee income for auto bond lending, if any for the bonds which they lent under auto bond lending programme. The Bank continues to recognize the securities in their entirety in the Statement of Financial Position because it retains substantially all of the risks and rewards of ownership. These securities are presented in the Statement of Financial Position as "Securities at Fair Value through Other Comprehensive Income".

c. Securities Pledged

In order to facilitate the securities settlement process, securities amounting to AUD 35.0 Mn were pledged by CBSL to Euroclear and obtained a credit facility of USD 30.0 Mn until 30 January 2017. The pledged securities are held in a separate account at Euroclear.

Following a review of the activity in CBSL accounts and with reference to the General Conditions Governing Extensions of Credit to participants in the Euroclear

System, Bank's credit facility was decreased to USD 20.0 Mn with effect from 31 January 2017.

Bank conducts these transactions under the terms that are usually based on the "Collateral Agreement Governing Secured Borrowings by Participants in the Euroclear System" and "General Conditions Governing Extensions of Credit to Participants in the Euroclear System" guidelines.

The Bank continues to recognise the securities in their entirety in the Statement of Financial Position because it retains substantially all of the risks and rewards of ownership and these securities are presented in the Statement of Financial Position as "Securities at Fair Value through Other Comprehensive Income".

The following table sets out the carrying amounts and fair values of all financial assets transferred that are not derecognized in their entirety and associated liabilities.

| | 2018 | 2017 | |
|---|---------------------------|-------------------------|---|
| | Financial Assets at FVOCI | Financial Assets at AFS | Financial Liabilities at Amortized Cost |
| | Rs. 000 | Rs. 000 | Rs. 000 |
| Assets | | | |
| Securities Sold under Agreement to Repurchase | - | 6,366,710 | - |
| Securities Lending | 3,714 | 2,466 | - |
| Securities Pledged | 4,841,397 | 4,583,944 | - |
| Carrying Amount of Assets | 4,845,111 | 10,953,120 | - |
| Associated Liabilities | | | |
| Securities Sold under Agreement to Repurchase | - | - | 6,503,884 |
| Carrying Amount of Associated Liability | - | - | 6,503,884 |

58. TRUST AND CUSTODIAL ACTIVITIES

The bank commonly acts as trustees and in other fiduciary capacities that result in the holding or placing of assets and liabilities on behalf of the GOSL, trusts, retirement benefit plans and other institutions. The significant trust activities performed by the Bank are as follows:

58.1 The bank handles disbursements and repayments of various foreign loans and grants under foreign funded development projects and credit schemes on behalf of the GOSL. It also collects counterparty funds under various foreign loans and grants on behalf of the GOSL and invests such funds in Treasury bills on requests made by donor agencies.

58.2 The bank is the custodian of the Employees Provident Fund (EPF). In terms of the statute, the functions of the Monetary Board consist of receiving contributions, surcharges, income from investments,

maintaining proper accounts of registered members of EPF, investing surplus funds and payment of benefits to the members.

58.3 The bank administered the Deposit Insurance Scheme, which was a voluntary deposit insurance scheme opened to banking institutions licensed by the CBSL and cooperative societies registered under the Cooperative Societies Law No. 5 of 1972, which carry on banking business and with effect from 1 October 2010 funds of this scheme have been transferred to the Sri Lanka Deposit Insurance scheme which was formed as per gazette No. 1673/11 dated 28 September 2010.

58.4 As per the Gazette No. 1673/11 dated 28 September 2010 (as amended), the Bank has established a Mandatory Deposit Insurance Scheme named Sri Lanka Deposit Insurance Scheme with effect from 1 October 2010 as an act of national interest to protect the funds of depositors.

All Licensed Commercial Banks (LCBs), Licensed Specialized Banks (LSBs) and Licensed Finance Companies (LFCs) shall be the members of this Scheme. Accordingly, 76 institutions are members of this Scheme. The deposits to be insured include the demand, time, savings deposit liabilities of the member institutions and value of the shares of shareholders who were initially deposit holders, whose deposits were converted into equity under the directions of the Monetary Board in 2010 and 2011 as part of the business restructuring plans implemented prior to 1 January 2012 and exclude all borrowing instruments and specific exclusions as per section 5.2 of the said gazette notification.

The deposit insurance fund has been created with the transfer of Rs. 350.20 Mn of the investments of Voluntary Deposit Insurance Scheme and Rs. 1,168.31 Mn of investments made out of collections of abandoned property of LCBs. As at 31 December 2018, the fund size is Rs. 53.3 Bn (provisional). Currently, the amount of compensation payable per-depositor per-institution is limited to Rs. 600,000 or its equivalent in the case of foreign currency deposits. The payment of compensation shall not be a liability of the Monetary Board or the Bank and shall be limited to funds available or raised in the deposit insurance fund including any borrowings permitted and contributions received. The Monetary Board and the Bank shall not be responsible for any liability that exceeds the total amount lying to the credit of the fund.

With effect from 22 November 2013, this scheme was renamed as "Sri Lanka Deposit Insurance and Liquidity Support Scheme" and the Deposit Insurance Fund was renamed as "Sri Lanka Deposit Insurance and Liquidity Support Fund".

The Deposit Insurance Unit (DIU) established in the Resolution and Enforcement Department, is responsible for operation & management of the scheme under the instructions and supervision of the Director of Resolution and Enforcement in terms of Directions/Regulations and policies as approved by the Monetary Board from time to time and shall maintain books and accounts distinctly separate from the Financial Statements of the Bank. The Auditor General shall be the Auditor of this Scheme.

- 58.5** The Bank carries out regulatory and supervisory functions in respect of LFCs and attends to related matters under the authority delegated to it by the Monetary Board. While carrying out such functions, with respect to failed LFCs, various actions are taken including the vesting of assets of persons responsible for the unviable and insolvent condition

of such companies, with the Monetary Board as a form of security.

- 58.6** As per the Circular issued by Director Bank Supervision, the banks who do not maintain the minimum advance limit of 10% to agriculture are required to contribute the shortfall to Refinance Fund operated by RDD of the Bank. RDD refinances such amounts collected through Bank of Ceylon, Peoples' Bank, Pradeshiya Sanwardena Bank and Lankaputhra Development Bank to agriculture under Viskam Refinance Scheme. As of 31 December 2018, all such collected funds have been refunded to banks and no loans were outstanding under the refinance scheme (2017 - Rs. 6.83 Mn) and received an interest of Rs. 0.17 Mn for such loans during 2018 (Rs. 1.83 Mn during 2017). Further, Rs. 28.12 Mn (2017 - Rs. 84.72 Mn) of income was earned from the investments.

58.7 On behalf of the Monetary Board of the Bank, RDD acts as the exclusive agent of the GOSL with regard to the projects funded by GOSL and foreign donors. RDD also implements the CBSL funded projects.

Concluded Projects

| Name of the Project | Total Allocation of the Fund (Mn.) | | Purpose of the Loan | Refinance Granted to PFI s (Rs. Mn.) | Salient Features |
|---|------------------------------------|----------|---|--------------------------------------|--|
| Tea Development Project | USD | 24.50 | To increase tea smallholders' income and improve the natural environment in the project areas. | 2,550.90 | Collection of recoveries from Participating Financial Institutions (PFIs) as per scheduled date to be transferred to Deputy Secretary to Treasury (DST). |
| Second Perennial Crop Development Project | SDR | 11.56 | To commercialize the perennial crops sector, increase production, nursery development post harvest handling, processing and marketing. | 1,453.11 | |
| Plantation Sector Reform Project | USD | 40.00 | To support policy and institutional reforms in the plantation sub-sector to increase the productivity and profitability and maintain the competitive advantage of the plantation industry of Sri Lanka. | 5,200.00 | |
| Susahana Finance & Leasing Company | LKR | 352.69 | To provide credit facilities to the resumption of enterprises affected by Tsunami. | 351.06 | |
| Small Business Revival Programme | LKR | 2,656.00 | To provide credit facilities to the resumption of Small and Medium Enterprises (SMEs) affected by Tsunami. | 2,663.40 | |
| Small Business Revival Programme – Revolving Fund | LKR | 150.00 | To provide credit facilities to the resumption of SMEs affected by Tsunami. | 122.72 | |
| Skill Development Project | LKR | 94.31 | To improve quality and relevance of skill training programmes to build high quality workforce and address skill mismatching. | 94.59 | |
| Urban Environment Infrastructure Development Project | USD | 4.00 | To improve environmental facilities, health and sanitary conditions of the people living in urban and semi-urban areas. | 369.15 | |
| Housing Guarantee Low Income Housing Shelter Project | USD | 25.00 | To assist low income community in the country to build houses and renovate and expand their residencies. | 1,362.00 | |
| Urban Development Low Income Housing Project | SDR | 15.10 | To provide capital to support low income households for housing improvement. | 1,915.76 | |
| North Western Province Water Resource Development Project | USD | 1.80 | To improve economic, social and nutritional well-being of the people living in the project areas. | 102.76 | |
| Matale Regional Economic Advancement Project | SDR | 2.00 | Permanent rising and sustaining of income of small entrepreneurs. | 249.06 | |
| Mid Country Perennial Crop Development Project | SDR | 11.56 | To provide credit facilities to the production of perennial crops in the mid country area. | 642.00 | |
| Agriculture Rehabilitation Project | SDR | 17.05 | To rehabilitate persons and property affected by the civil disturbances in the Northern and Eastern provinces and five bordering Districts. | 843.00 | |
| Smallholder Tea Development Project | USD | 12.60 | To develop smallholder tea sector and rehabilitate tea facilities. | 645.93 | |
| Poverty Alleviation Micro Finance Project | YEN | 1,368.00 | To set up an effective credit delivery mechanism for channeling formal credit to income generating activities. | 1,402.45 | |
| Small Farmers Landless Credit Project | USD | 17.40 | To establish a cost effective and sustainable micro credit delivery system to generate employment and improve saving habits among the low income receiving people. | 345.69 | |
| Kegalle Integrated Rural Development Project | SDR | 1.50 | To uplift the standard of living of people in the project areas by promoting income generating activities. | 148.00 | |
| Southern Province Rural Development Project | SDR | 27.90 | To improve the quality of life of the people in the Southern Province. | 564.00 | |
| EIB Contract B | EUR | 10.00 | To reconstruct SMEs directly affected by Tsunami. | 1,553.27 | Collection of recoveries from PFIs as per scheduled date to be transferred to Finance Department (FD). |
| Susahana | LKR | 3,000.00 | To provide credit facilities to resume Micro, Small and Medium Enterprises (MSMEs) affected by Tsunami. | 2,750.00 | |
| Susahana Phase II | LKR | 500.00 | To provide credit facilities to resume MSMEs affected by the Tsunami. | 105.54 | |
| Awakening North | LKR | 2,000.00 | To extend credit to agriculture, livestock, micro and small enterprises in the Northern Province. | 2,000.00 | Collection of recoveries from PFIs as per scheduled date to be transferred to relevant A/Cs of the RDD |
| Resumption of Economic Activities in the Eastern Province | LKR | 1,000.00 | To grant loans to SME sector activities in the Eastern Province. | 1,000.00 | |
| Awakening North - Phase II | LKR | 2,154.25 | To extend credit to agriculture, livestock, micro and small enterprises in the Northern Province. | 2,361.00 | |
| Second Perennial Crops Development Project - Revolving Fund | LKR | 1,200.00 | To provide credit facilities to develop the perennial crops sector in the country. | 1,199.82 | |
| Matale Regional Economic Advancement Project - Revolving Fund | LKR | 77.00 | To raise the income of rural and farm families and to provide funds for medium scale entrepreneurs to create non-farm enterprises and to expand existing projects in the Matale District. | 77.00 | |
| Sabaragamuwa Province Integrated Rural Development Project - Revolving Fund | LKR | 100.00 | To enhance and start new income generating activities in the Sabaragamuwa Province. | 100.00 | |

| | | | | | |
|--|-----|----------|--|----------|---|
| Construction Sector Development Project | EUR | 9.00 | To strengthen the financial and technical capacities of private local businesses to effectively participate in construction and public work in post Tsunami reconstruction. | 1,399.73 | |
| Sabaragamuwa Province Integrated Rural Development Project - Phase II | LKR | 70.00 | To enhance and start new income generating activities in the Sabaragamuwa Province. | 70.00 | |
| Post Tsunami Coastal Rehabilitation Resource Management Project | SDR | 2.09 | To assist communities adversely affected by Tsunami disaster to recover their assets and re-establish the foundation of their usual economic activities, while diversifying into new profitable income generating activities. | 190.77 | |
| Poverty Alleviation Micro Finance Project II (Probodini) | YEN | 2,381.00 | To enhance the living standard of households whose monthly income is less than Rs. 15,000/= in project location. | 3,213.20 | |
| Self Employment Promotion Initiative | LKR | 250.00 | To provide financial assistance to trained youth who passed out from recognized vocational training institutions in the country for establishment of their own self employment projects. | 232.39 | |
| Viskam (Special Loan Scheme for Agriculture Sector Development) | LKR | 1,325.60 | To ensure the availability of credit for investment, diversification and improvement of commercial agri-business in the country. | 881.00 | When the mandatory requirements are fulfilled by contributory banks, funds will be returned |
| Provincial Development Credit Scheme | LKR | 2,900.00 | To provide credit facilities to medium and long term projects in the SME sector in the country. | 2,900.00 | Collection of recoveries from PFIs as per scheduled date to be transferred to FD. |
| Dry Zone Livelihood Support & Partnership Programme | LKR | 252.95 | To provide facilities to income generating activities in Anuradhapura, Moneragala, Kurunegala and Badulla Districts. | 252.95 | |
| Resumption of Economic Activities in the Eastern Province - Phase II | LKR | 1,078.27 | To extend credit to agriculture, livestock, micro and small enterprises in the Eastern Province. | 1,000.00 | |
| Resumption of Economic Activities in the Eastern Province - Phase III | LKR | 1,000.00 | To extend credit to agriculture, livestock, micro and small enterprises in the Eastern Province. | 1,428.47 | |
| Repair of Damaged Houses in the North and East | LKR | 600.00 | To provide credit facilities for repairing the damaged houses that were damaged during the conflict in the Northern and Eastern Provinces. | 600.00 | |
| National Agribusiness Development Programme | USD | 32.90 | To assist smallholder producers and the landless, especially the youth by increasing the income of the beneficiaries in the market / value chain development and providing financing and training for employment. | 113.13 | |
| Small Plantation Entrepreneurship Development Project | SDR | 2.60 | To enhance the living standard of the low income communities in Monaragala, Kandy, Kegalle, and Nuwara-Eliya. | 487.66 | |
| National Agribusiness Development Programme (NADeP) - Microfinance | LKR | 1,049.84 | To improve income level and social conditions of the poor in selected project areas. | 1,049.84 | |
| Value Chain Development Capital Agriculture Loan Scheme under the "Out Grower Farmers Loan scheme" of the National Agribusiness Development Programme (NADeP) | LKR | 135.69 | To increase the production, productivity, quality and value addition of agriculture produce. | 135.69 | |
| Value Chain Development Seasonal Agriculture Loan Scheme under the "Out Grower Farmers Loan scheme" of the National Agribusiness Development Programme (NADeP) | LKR | 302.04 | To increase the production, productivity, quality and value addition of agriculture produce. | 302.04 | |
| Post-Disaster Economic Activity Recovery Loan Scheme (PEARL) | LKR | 134.58 | To support borrowers (individual or group of individuals) in their post disaster recovery efforts of the business/small enterprises affected by recent floods/drought by providing the fund requirements to resume their businesses or income generating activities. | 134.58 | |
| NADeP- "Tharuna Diriya" Youth Empowerment and Employment Programme | LKR | 288.48 | Reach village level poor youth to enhance the skill levels and capacity building by providing credit facilities to small business and other forms of self-employment projects. | 288.48 | |
| Dry Zone Livelihood Support & Partnership Programme - Revolving Fund | LKR | 252.90 | To provide facilities to income generating activities in Anuradhapura, Monaragala, Kurunegala and Badulla Districts. | 252.89 | |
| Small Farmers and Landless Credit Project - Revolving Fund | LKR | 345.69 | To promote the intensification of agricultural production by small farmers and the establishment of small scale non-farming rural enterprises. | 1,564.75 | |
| Poverty Alleviation Micro-finance Project II (Probodini) - Revolving Fund | LKR | 2,764.84 | To improve income levels of the poor and enhance inclusive formal financial services for them by providing credit for income generating activities. | 7,016.86 | |

Ongoing Projects

| Name of the Project | Total Allocation of the Fund (Mn.) | | Purpose of the Loan | Refinance Granted to PFIs (Rs. Mn.) | Salient Features | Warranties & Assurance | Special Conditions |
|---|------------------------------------|-----------|--|-------------------------------------|--|------------------------|--------------------|
| Tea Development Project – Revolving Fund | LKR | 1,100.00 | To provide credit facilities to develop the tea sector in the country. | 964.87 | | | |
| Swashakthi Loan Scheme | LKR | 4,000.00 | To generate employment opportunities via providing financial support for both new and existing entrepreneurs. | 2,522.20 | | | |
| "Aithwela"-Resumption of Economic Activities affected by Disasters (READ) | LKR | 2,000.00 | To provide financial facilities to eligible sub-borrowers to resume any economic activity affected by any disaster as informed by the GOSL. | 1,599.74 | | | |
| Poverty Alleviation Micro-finance Project RF (Probodini) | LKR | 1,031.00 | To assist in setting up an effective credit delivery mechanism for income generating activities conducted by the rural poor who has no access to formal credit. | 4,821.16 | | | |
| "Smallholder Agribusiness Partnership Programme (SAPP) 4P Capital" | USD | 1.10 | | 67.84 | | | |
| "Smallholder Agribusiness Partnership Programme (SAPP) 4P Seasonal" | USD | 2.45 | To contribute to Sri Lanka's smallholders' poverty reduction & competitiveness & increase the income & quality of diet of 57,500 smallholders involved in commercially oriented production & marketing systems, achieving through a process of forming & building capacity of producer groups, organizations & strengthening the network under the partnerships with the private sector. | 254.15 | | | |
| "Smallholder Agribusiness Partnership Programme (SAPP) 4P RF Income Generation" | USD | 6.00 | | 106.42 | | | |
| Saubagya Loan Scheme | LKR | 26,725.60 | To extend credit to MSMEs and disaster affected MSMEs. | 26,725.60 | Collection of recoveries from PFIs as per scheduled date to be transferred to relevant A/Cs of the RDD | | |
| Self Employment Promotion Initiative Phase II (SEPI II) | LKR | 225.00 | To provide financial assistance to trained youth who completed certificate or Diploma in National Vocational Qualification (NVQ) | 352.09 | | | |

59. EVENTS OCCURRING AFTER THE REPORTING DATE

There were no material events occurring subsequent to reporting date that require adjustment or disclosure in the financial statements.

2. BANK SUPERVISION

Bank Supervision Department (BSD) was established under Section 28 of the Monetary Law Act (MLA) for the purpose of continuous supervision and periodic examination of licensed banks in Sri Lanka. Regulations and supervision of licensed banks are governed by the provisions of the Banking Act, No. 30 of 1988 as amended.

The main duties of BSD include formulating and implementing prudential regulations, conducting continuous supervision and periodic statutory examinations of banks, approving the fitness and propriety of Directors, Chief Executive Officers and Key Management Personnel (KMPs) of licensed banks, granting regulatory approvals and taking regulatory actions where necessary with the approval of the Monetary Board, and engaging in awareness and capacity building of the banking sector.

As at the end 2018, the banking sector comprised 26 licensed commercial banks (LCBs) and 7 licensed specialised banks (LSBs) operating under the regulatory and supervisory purview of BSD. In addition, as at end 2018, 3 Representative Offices (ROs) of foreign banks were in operation in Sri Lanka. The list of licensed banks and ROs is provided in Annex II-1.

A summary of the main functions and activities performed by BSD during 2018 is given below:

2.1 Issuance of Prudential Regulations

Prudential regulations issued to licensed banks are provided in Part III of this Report. A summary of the major prudential regulations issued during the year is as follows.

(a) Loan to Value Ratios for Credit Facilities in respect of Motor Vehicles

Licensed banks were required to maintain Loan to Value (LTV) ratios, when granting credit facilities for purchase or utilisation of motor vehicles as a macro-prudential measure to curtail the excessive credit in the banking sector for purchase of motor vehicles. Several amendments to these requirements were introduced from time to time in 2018.

Accordingly, revised LTV ratios were introduced which are applicable for credit facilities in respect of motor vehicles including electric, hybrid and other unregistered vehicles and registered vehicles that have been used in Sri Lanka for more/less than one year after the first registration. Further, measures were taken to curtail imports of motor vehicles and non-essential consumer goods to minimise the adverse impact on the exchange rate by lowering LTV ratios and requesting to refrain from opening of letters of credit for importation of motor vehicles under the scheme for issuance of motor vehicle permits on concessionary terms issued by the Government of Sri Lanka (GOSL).

In addition, licensed banks were informed to refrain from the issuance of Usance Letter of Credit facility for the importation of motor vehicles as proposed by the budget 2018. Nevertheless, exemptions from LTV ratios were granted for identified economic sectors that required importation of vehicles for their core business operations. The applicability of LTV ratio was also waived off for procurement of vehicles for government agencies and concessionary vehicle loan schemes introduced by the government on a need basis.

(b) Off-shore Banking Business Schemes

A Banking Act Order was issued to all LCBs permitting transactions that are allowed under the provisions of the Foreign Exchange Act No. 12 of 2017, in any designated foreign currency, in an account of a non-resident maintained in an off-shore banking unit.

(c) Regulatory Framework for Appointment of Agents

A regulatory framework was introduced on the appointment of agents of licensed banks, including the approval and selection process of agents and sub agents, responsibilities of banks, permitted activities to be performed by agents and sub agents, risk management and oversight, customer protection, compliant measures and relief mechanism. Subsequently, an amendment to the Direction was issued permitting licensed banks to provide inward remittance services to persons other than existing customers.

(d) Strengthening Risk Management of Derivative Transactions

Licensed banks were instructed to adopt more stringent risk management measures for derivative transactions and the Directions issued in this regard cover the areas such as commencement of derivative transactions, board approved policies and procedures, customer awareness, prohibited activities and reporting requirements when engaging in financial derivative transactions. Previous Directions issued in this regard were revoked.

(e) Margin Requirements against Imports on Documents against Acceptance (DA) Terms

Licensed banks were required to take measures to curtail imports of non-essential consumer goods and minimise the adverse impact on the exchange rate, introducing a cash margin requirements of 100 per cent for imports on DA.

(f) Annual Licence Fee of Licensed Commercial Banks and Licensed Specialised Banks

Licensed banks were informed of the increase in annual licence fees of the licensed banks for the calendar years 2019 and 2020, based on the total assets of licensed banks, as at end of the previous year.

(g) Introducing Net Stable Funding Ratio under Basel III Liquidity Standards

With a view to ensuring a stable funding profile in relation to the composition of assets and off-balance sheet activities of banks, licensed banks were required to adopt Net Stable Funding Ratios (NSFR) in accordance with Basel III liquidity standards. Accordingly, licensed banks were required to meet NSFR of 90 per cent by 01 January 2019 and increase it to 100 per cent by 01 July 2019.

(h) Amendments to Directions on Liquidity Coverage Ratio under Basel III Liquidity Standards

Banks were informed of the amended regulatory reporting formats on Liquidity Coverage Ratio under Basel III Liquidity Standards.

(i) Foreign Currency Borrowings by Licensed Banks

Commencing 30 November 2018, licensed banks were required to comply with a new policy on foreign currency borrowings, with a view to further strengthening risk management of foreign currency borrowings by banks. The short and long term limits on foreign currency borrowings were introduced, based on a score that was calculated by considering the bank's external credit rating and capital adequacy ratio, and linked to a certain percentage of total assets. With respect to foreign currency borrowings by off-shore units, licensed banks were informed to engage in the business of foreign currency borrowings and borrowings with residents subject to terms and conditions in Banking Act Direction No. 11 of 2018 on Foreign Currency Borrowings by licensed banks.

(ii) Introducing Leverage Ratio under Basel III for Licensed Banks

Commencing 01 January 2019, licensed banks were required to maintain a minimum leverage ratio of 3 percent in accordance with Basel III leverage ratio framework to act as a credible supplementary measure to the risk based capital requirement.

(k) Adoption of Sri Lanka Accounting Standards – SLFRS 9: Financial Instruments

Guidelines on the adoption of Sri Lankan Accounting Standards – SLFRS 9: Financial Instruments were issued to licensed banks on 31 December 2018 with a view to establishing consistent and prudent practices on the adoption of Sri Lankan Accounting Standards in the banking sector.

2.2 Approvals granted by the Monetary Board

(a) Branches and Other Banking Outlets of Licensed Banks

During the year, 1,557 approvals were processed and 1,519 approvals were granted, while 38 requests were deferred/declined on prudential grounds (Table II-1). Accordingly, by the end 2018, there were 3,572 bank branches, 3,309 Student Savings Units and 4,834 ATMs in operation.

Table II-1
Approvals relating to Branches and Other Banking Outlets

| Types of Approvals | No. of Approvals | |
|---|------------------|--------------|
| | Processed | Granted |
| Opening and Installation | 1,281 | 1,251 |
| Branches | 66 | 50 |
| Automated Teller Machines (ATMs) | 146 | 136 |
| Student Saving Units (SSUs) | 231 | 231 |
| Cash Deposit Machines (CDMs) | 63 | 61 |
| Mobile Banking Units and Vehicles | 560 | 560 |
| Mobile ATMs and CDMs | 8 | 8 |
| Relocation | 149 | 143 |
| Branches | 137 | 131 |
| ATMs | 12 | 12 |
| Closures and cancellations of approvals granted for branches and other service outlets | 25 | 23 |
| Discontinuation and cancellation of approvals granted for ATMs and Others | 102 | 102 |
| Total | 1,557 | 1,519 |

(b) Other Regulatory Approvals

During 2018, a total of 442 regulatory approvals were granted with regard to foreign currency borrowings by licensed banks, inclusion of debentures in Tier 2 capital, acquiring material interest in the share ownership of banks, exceeding maximum amount of accommodation, assessing fitness and propriety for appointment of new/continuing Directors and Officers Performing Executive Functions in licensed banks, disposal of property below market value, meeting the minimum capital requirements, outsourcing arrangements, agency functions, inclusion of revaluation reserves in Tier 2 capital and abandoned property reimbursements.

(c) Regulatory Actions

During 2018, licensed banks have been informed of regulatory actions with regard to non-compliance with the Banking Act and Directions issued thereunder, on 33 instances. Further, the Monetary Board was apprised on banking sector performance on quarterly basis.

2.3 Conduct of Continuous Supervision

- Continuous supervision is an on-going monitoring mechanism on the affairs of individual banks which serves as an early warning system to ascertain the operational efficiency and long term sustainability of the entire banking sector and enables the implementation of corrective measures, where necessary, to ensure the safety of depositors' funds.
- Continuous supervision was conducted based on periodic financial information submitted by banks

through the web based FinNet System. Approximately, 70 statutory returns are submitted monthly/quarterly/annually by each bank through the FinNet system covering financial and prudential information. Revamping of the database maintained in BSD continued in 2018 in order to facilitate better report generation.

- c) In the process of continuous monitoring and supervision of banks, special reports were prepared with respect to sector-wise credit concentration of the banking industry. In addition, banking industry aggregate data were shared with other departments of the CBSL and external government institutions to facilitate preparation of reports. Further, monthly presentations on the banking industry performance were also prepared.
- d) During 2018, approximately 795 customer complaints/requests were handled relating to loan interest rates, rescheduled loans, credit cards, pawning operations, banking malpractices and frauds, unauthorised withdrawal of funds and seeking reduction in Automated Teller Machine (ATM) charges and fees. Further, BSD also facilitated collection and submission of information to the Ministry of Finance and Mass Media, on the reimbursement of interest relating to the special interest scheme for senior citizens, on a quarterly basis.
- e) The progress on addressing supervisory concerns identified during statutory examinations of banks within specified time targets were monitored on a quarterly basis. In addition, 17 meetings were held with licensed banks to discuss regulatory concerns identified by the continuous supervision function.

2.4 Conduct of Periodic Examinations

- (a) BSD conducted 32 examinations during 2018 including 05 that continued from the previous year. Examinations of 27 licensed banks were completed in 2018 through formal discussions with the management of the respective banks and submission of reports to the Monetary Board, while 05 examinations were in the process of completion. Major concerns raised at certain examinations included low capitalization and efficiency, lapses in corporate governance and management, deficiencies in technology risk management and liquidity risk management, under-estimation of non-performing loans and provision for bad and doubtful loans and concerns over treasury operations. In addition, several examinations with limited scope were conducted on areas such as investments in government securities, corporate governance, customer complaints, trade finance transactions, foreign exchange operations and credit facilities granted for purchase of motor vehicles.

- (b) Further, BSD has developed a supervisory rating model for licensed banks viz, Bank Sustainability Rating Indicator (BSRI) which was approved by the Monetary Board to facilitate the risk based supervision framework of licensed banks and to enable early intervention and prompt corrective action through identification of potential risks arising from emerging developments and strategic changes of licensed banks. Accordingly, risk based examinations based on BSRI commenced with effect from 01 January 2019.

2.5 Awareness and Capacity Building of the Banking Sector

(a) Capacity Building

Continuing its contribution towards the building capacity of the banking sector, BSD provided resource persons for various training programs and forums covering areas such as regulatory compliance, corporate governance, new accounting standards, risk management, banking business and laws and regulatory developments pertaining to banking and finance, at the Centre for Banking Studies of the CBSL and other external institutions. BSD also organised a workshop for Board Secretaries of licensed banks on Corporate Governance to improve the conduct of banks.

Capacity building of the staff of BSD was continued in 2018 and officers of BSD participated in local and foreign training programmes including supervisory colleges in the areas of risk based supervision, Basel III standards, corporate governance, culture and ethics, fintech, cyber security, financial innovation, financial reporting standards and sustainable finance.

(b) Meetings with Banks and Other Stakeholders

BSD continued to function as the secretariat for the monthly meetings of bank CEOs chaired by the Governor which are aimed at creating a dialogue between the CBSL and the banking sector on matters relating to the developments in the Sri Lankan economy, the banking sector, and regulatory and supervisory framework. Additionally, a meeting of bank chairpersons was held to apprise on the banking sector performance, developments in the local and global regulatory frameworks and the economy. BSD hosted a Technical Session to further enhance and update the knowledge of Boards of Directors, Chief Executive Officers and other Key Management Personnel of licensed banks with the participation of foreign resource persons covering areas such as culture and conduct of future boards of directors of banks, technology risk resilience, and anti-money laundering compliance challenges. In addition, BSD organised a discussion with Chief Information Officers and Chief Risk Officers of banks on IT risk resilience.

Regular meetings were conducted with the senior management of concerned licensed banks to discuss bank specific matters, to ensure proper oversight and

timely implementation of corrective action, and meetings with the Board appointed committees of banks to ensure the sustainability of the banking sector. Further, BSD facilitated banks to obtain necessary information and clarifications on adoption of new Sri Lanka Financial Reporting Standards by organising meetings with the Institute of Chartered Accountants of Sri Lanka.

BSD organised a meeting of Financial Sector Oversight Committee (FSOC) which comprises heads of core financial sector regulators to facilitate cooperation among member institutions to ensure the efficiency, soundness and safety of the financial system. In addition, a meeting with the panel of auditors of licensed banks was held to discuss the areas to focus on during the forthcoming audits and provision of non-audit services to licensed banks by audit firms.

Annex II - 1

List of Licensed Banks

Licensed Commercial Banks

1. Amana Bank PLC
2. Axis Bank Ltd
3. Bank of Ceylon
4. Bank of China Ltd
5. Cargills Bank Ltd
6. Citibank, N.A.
7. Commercial Bank of Ceylon PLC
8. Deutsche Bank AG
9. DFCC Bank PLC
10. Habib Bank Ltd
11. Hatton National Bank PLC
12. ICICI Bank Ltd
13. Indian Bank
14. Indian Overseas Bank
15. MCB Bank Ltd
16. National Development Bank PLC
17. Nations Trust Bank PLC
18. Pan Asia Banking Corporation PLC
19. People's Bank
20. Public Bank Berhad
21. Sampath Bank PLC
22. Seylan Bank PLC
23. Standard Chartered Bank
24. State Bank of India
25. The Hongkong & Shanghai Banking Corporation Ltd
26. Union Bank of Colombo PLC

Licensed Specialised Banks

27. Housing Development Finance Corporation Bank of Sri Lanka
28. Lankaputhra Development Bank Ltd
29. National Savings Bank
30. Pradeshiya Sanwardhana Bank
31. Sanasa Development Bank PLC
32. State Mortgage & Investment Bank
33. Sri Lanka Savings Bank Ltd

Representative Offices of Foreign Banks

1. Doha Bank QPSC
2. JP Morgan Chase Bank NA
3. MUFG Bank Ltd.

3. CENTRE FOR BANKING STUDIES

Centre for Banking Studies (CBS) is entrusted with the responsibility of developing human capital of the CBSL and financial sector institutions by way of equipping participants with necessary skills and competencies to address the challenges of the fast changing financial landscape.

Accordingly, the focus of CBS during the year 2018 was to design, co-ordinate and conduct required training programmes, seminars and workshops to cater the demand for such services from financial sector institutions, while taking measures to raise standards of CBS to a higher level in terms of quality of training and other facilities provided. Further, special emphasis was given to provide training to the staff of the CBSL in line with the strategic objective of capacity building and support cluster of the CBSL.

CBS offered training programmes covering the areas of commercial banking operations, risk management and compliance, treasury operations, accounting and financial management, credit management, laws and regulations, development banking, research and data analysis, economics, information technology and human resource management in 2018. CBS obtained the services from its resource person panel which comprised of resource persons of CBSL and external experts including foreign experts in financial sector, policy and regulatory areas with high academic/professional qualifications and international exposure.

CBS has successfully conducted 144 programmes during the year which consisted of 53 calendar programmes, 61 special programmes, 18 educational programmes and 12 public lectures in 2018. Further, 18 capacity building programmes were conducted to enhance the competencies of the CBSL staff for which 616 staff members participated. Capacity building programmes included the programmes conducted in collaboration with the SEACEN Research and Training Centre, Reserve Bank Staff College of Reserve Bank of India and Deutsche Bundesbank, Germany. Further, CBS conducted 23 tailor-made training programmes during the year on the requests of local commercial banks, specialized banks, foreign central banks and commercial banks. In view of promoting economic education and financial inclusion, CBS organised 6 public seminars on various topics at CBS and CBSL Head Office and 6 public seminars at regional level.

In addition, CBS continued to co-ordinate the educational television series, "Thakshilawa" and "Ariwootroo", telecast in Sinhala and Tamil media, respectively mainly targeting the Advanced Level students, who study the subject of Economics.

Throughout the year, 7,198 local participants and 226 foreign participants from the Philippines, India, Pakistan, Nepal, Bangladesh, Bhutan, China, the Maldives, Mongolia, Indonesia, Malaysia, Papua New Guinea, Cambodia, Brunei and Thailand have attended CBS Programmes.

CBS also conducted in-depth post evaluation processes, to improve programme modules, the delivery of lectures and other services offered. The Programme Calendar for 2019 was prepared with careful assessment of the present and future training needs of the CBSL and financial sector and CBS strives to maintain high standards in all aspects of its programmes.

4. COMMUNICATIONS

During 2018, the Communications Department (CMD) continued its role of supporting the accomplishment of the mission of the CBSL, i.e., maintaining economic and price stability and financial system stability and the communication of information pertaining to the agency functions and corporate services of the CBSL. In addition to direct communication via speeches, lectures, meetings and seminars, CMD used several media to communicate with its stakeholders i.e. the corporate website CBSL (www.cbsl.gov.lk), publications, newspapers, the television, and even video clips.

4.1 External Communication

In 2018, the annual Open Day programme was conducted in Anuradhapura, at the Regional Office premises and the Public Grounds on 21st and 22nd of September 2018. The CBSL reached out to different target groups including financial sector personnel, public sector officials, teachers, school students and the general public in the area to address various issues faced by these groups, which come within the ambit of the CBSL's operations or policy. The programme also aimed to raise financial literacy and awareness amongst them. The visitors to the event also had the opportunity to access EPF related services, exchange damaged currency notes for new notes, obtain coin requirements and to purchase CBSL's publications at discounted rates. Several seminars for over 350 Advanced level students were also conducted.

CMD launched the revamped corporate website in Sinhala, Tamil and English languages, in collaboration with the Information Technology Department of the CBSL on 28 March 2018. The aim of this revamp was to provide a better browsing experience for web users such as professionals, the public, media, and students to ensure efficient and speedy accessibility to information with user friendly interfaces including mobile browser compatibility. The CBSL was the Gold winner of BestWeb.lk 2018 awards under the special category – Best Tamil Website.

In 2018, CMD issued 438 press releases, including key press releases such as those on the 'Monetary Policy Review' and decisions of the Monetary Board in relation to financial institutions and financial markets. Further, the CBSL held 16 press briefings on various important policy matters relevant to the CBSL during 2018. Meanwhile, 11 Gazette notifications and 87 press notices, including advertisements, were issued to the media in 2018. The CBSL also sent out 488 SMS alerts pertaining to Telegraphic Transfer (exchange) rates, SLIBOR

rates and policy rates. To further facilitate communication with stakeholders, the CMD administers and monitors its corporate social media accounts, namely, Twitter, Facebook and YouTube. Table II-2 below gives a comparison of the performance with respect to the CBSL's social media accounts in 2017 and 2018.

Table II-2
Communication by CBSL through Social Media

| Type of media | 2017 | 2018 |
|--------------------------------|---------|--------|
| YouTube (CBSL video uploads) | 63 | 37 |
| YouTube Views (Cumulative) | 177,454 | 64,996 |
| Facebook Likes (Cumulative) | 18,146 | 23,066 |
| Twitter Followers (Cumulative) | 17,990 | 23,010 |

With a view to promoting knowledge of economics and central banking among school children, CMD organized the initial phase of the "Econ Icon Season IV" TV quiz programme, which is the written examination to select 16 school teams, in Sinhala and Tamil medium, for participating in the TV Quiz. The examination paper based on the syllabus for Economics - General Certificate of Education (Advanced Level), Grade 12 and 13, (implemented from 2017), was prepared during the year. This island-wide examination was held on 22nd January 2019.

CMD also facilitated the Bank's events, amongst which were the Bank's 68th Anniversary Oration on the topic "A Revisit to Central Bank Independence: How to Resolve the Emerging Issues?" delivered by Dr. W A Wijewardena, former Deputy Governor of the CBSL, presentation of the Annual Report 2017, Road Map 2018, the meeting of the Asian Clearing Union Standing Technical Committee, and the 11th Annual International Research Conference.

CMD handled the production of a docudrama on microfinance, in collaboration with the Department of Supervision of Non-Bank Financial Institutions in Sinhala and Tamil media with the objective of educating people about microfinance and was telecast on Rupavahini and Nethra TV channels in August 2018.

CMD participated in the "Colombo International Book Fair" held at the Bandaranaike Memorial International Conference Hall, Colombo, from the 21st to the 30th of September 2018, and the bank's publications were sold/distributed at this event.

CMD handled public grievances directed to the CBSL through the "Tell the President" grievance handling system, and responded to 325 grievances in 2018, in collaboration with the respective Departments of the CBSL.

Since the CMD was also assigned the task of coordinating requests from citizens under the Right to Information (RTI) Act No.12 of 2016 from March 2017, a total of 102 requests and 13 appeals from the public were received and processed for the year 2018, with the assistance of the relevant Departments.

4.2 Internal Communication

To enable the senior management of the CBSL to be well informed with respect to current affairs in the economy, the financial sector and other matters relevant to the CBSL, 6,392 news clips, articles and public opinions extracted from fifteen national newspapers published in three languages were submitted to the senior management. Important press releases issued were also circulated among CBSL staff.

Starting from 2018, the official internal newsletter, "Kavuluwa" (meaning "window") was published only in digital format, with one volume uploaded on the staff internal website, "Mansala".

4.3 Public Awareness

Awareness programmes on diverse topics such as 'Objectives and Functions of the Central Bank' and 'Sri Lanka's Economy' were coordinated by CMD for 15,742 participants as given in Table II-3 below.

Table II-3
Details of Public Awareness Programmes
Conducted in 2018

| Institution | No. of Programmes | No. of Participants |
|---|-------------------|---------------------|
| Schools | 145 | 11,973 |
| Universities | 5 | 200 |
| Sri Lanka Armed Forces and Defense University | 4 | 148 |
| Foreign Delegates (National Defense Colleges) | 3 | 73 |
| Mobile Programmes (held outside CBSL Head Office) | 16 | 3,348 |

Further, CMD assisted two mobile programmes initiated by Regional Offices by providing resource persons and publications. CMD, in collaboration with the Economic Research Department, also successfully conducted an educational programme for journalists during the 2nd quarter of 2018.

CMD's sales of CBSL Publications amounted to Rs. 3.6 million during the year. These sales were made through its sales counters at the Economic History Museum, the CBS Publications Store at Rajagiriya, and sales counters at Regional Offices and at the Colombo International Book Fair. CMD also distributed 6,993 copies of different publications free of charge among school children and Public Libraries throughout the country.

4.4 Tamil Translation Services

CMD provided its Tamil translation services to enable communication by the CBSL in Tamil Language. This included some key publications as well. Hence, CMD accomplished its mission of providing information in all three languages, in compliance with the National Language Policy.

4.5 Photography and Videography Coverage

Over 390 events of the CBSL were captured on camera in 2018 while maintaining high professional standards by delivering all related services including editing, printing of photographs,

preparing albums/CDs, and uploading recordings to the website of the CBSL and Mansala (the Intranet) in a timely manner.

4.6 Printing Press

CMD provided the services of designing, typesetting and printing to meet the printing requirements of the CBSL with high quality standards. In this respect, CBSL's Printing Press completed a total of 221 printing assignments in 2018. These include the periodicals Satahana (10 issues), News Survey (07 issues), Vaippaham (06 issues), and the publication titled "An Introduction to Principles of Economics – II", "Economics and Social Statistics of Sri Lanka – 2018", "A step by step Guide to Doing Business in Sri Lanka (Eighth Edition)", the Socio-Economic Data folder in all three languages and the "Story of Inflation" in Tamil medium. Further, printing of colour posters, handbills, leaflets, letterheads, certificates, visiting cards, various forms etc. and Greeting Cards were undertaken by CMD.

4.7 Library and Information Centre

The Library and Information Centre (LIC) operates with the objective of helping officers of the CBSL to prepare for their professional roles by acquiring knowledge, building awareness, being up-to date with economic developments and by developing balanced personalities.

LIC has a collection of 30,829 books, 19,600 reports, and 2,079 CDs. These include new additions of 229 books, 100 reports, and 144 CDs during the year and over 48,650 journal issues. LIC subscribes to online databases, such as 'ScienceDirect', 'EconLit' and Wiley Online Journals, which provide access to a vast collection of publications on topics relating to economics, management and finance. In addition, LIC subscribed to several other online resources on subjects relevant to central banking, e.g., www.centralbanking.com, www.risk.net and www.ft.com, and continued to provide staff access to these resources. LIC continued the subscription to OpenAthens, which provides CBSL's officers remote access to journal articles. LIC subscribes to 84 foreign journals and 18 local journals in printed form.

LIC continued to compile electronic publications such as the 'Recent Additions' (i.e. new books), 'Current Contents', 'International News Alert', 'Local Press' and notes on economics, banking and finance related reports and disseminated them via the intranet. A selective dissemination of information services was also provided.

Further, LIC continued its services to the banking and economics libraries in Sri Lanka by providing useful information through e-mail and by way of inter-library loans. Further, LIC was an active member of the Global Central Bank, Financial Institutions Library and Information Professionals' Network (CBFA List), which share information resources and experience among the central banks and other international financial institutions across the globe. A digital library service was also maintained, giving access to the CBSL staff through the library's intranet website.

5. CURRENCY

The CBSL has the sole right and authority to issue currency in Sri Lanka which includes both currency notes and coins as stipulated in the MLA No. 58 of 1949. In fulfilling this task, CBSL is entrusted with designing, printing of currency notes, minting of coins and distributing of currency notes and coins. Currency Department (CRD) of CBSL handles functions relating to this statutory responsibility of the Monetary Board. CRD continuously engages in building and maintaining public confidence in the currency by preserving its value and integrity and making available adequate stocks to meet the demand for currency, which is essential for smooth functioning of the economy.

5.1. Currency Printing and Minting

In order to ensure good quality notes in circulation and ensure sufficient stocks to meet the public demand, during 2018, 121 million pieces of currency notes and 311.4 million pieces of coins were printed/minted and received by CRD. A new set of circulation standard coins which are made of stainless steel for the denominations of Rupee 1, Rupees 2, Rupees 5 and Rupees 10 designed and procured in 2016-2017, was issued into circulation on 03 December 2018 through LCBs. This new coin series was designed with the objectives of reducing the cost of minting coins, increasing the durability of coins, giving more portability and providing easy identification by visually impaired people.

5.2. Currency Distribution

(a) Currency in Circulation

Demand for currency notes and coins increased in 2018 in line with the economic growth and inflation in Sri Lankan economy, notwithstanding the continued usage of technology driven non-cash modes of payment. Accordingly, the value of total currency in circulation increased by 7.2 per cent to Rs.640.3 billion as at 31 December 2018, over the previous year, as shown in Table II-4 below.

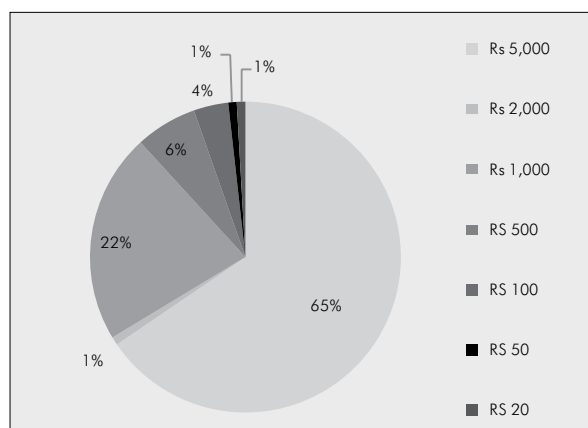
Table II-4
Currency in Circulation (as at end 2018)

| Item | Value (Rs. bn) | | | | | Change (%) | | | | |
|--------------|----------------|--------------|--------------|--------------|--------------|-------------|-------------|-------------|------------|------------|
| | 2014 | 2015 | 2016 | 2017 | 2018 | 2014 | 2015 | 2016 | 2017 | 2018 |
| Notes | 408.8 | 482.0 | 541.5 | 585.3 | 627.1 | 23.0 | 17.9 | 12.3 | 8.1 | 7.1 |
| Coins(a) | 7.5 | 9.1 | 10.7 | 12.1 | 13.2 | 10.3 | 21.3 | 17.6 | 13.1 | 9.1 |
| Total | 416.3 | 491.1 | 552.2 | 597.4 | 640.3 | 22.7 | 18.0 | 12.4 | 8.2 | 7.2 |

(a) The commemorative coins are excluded

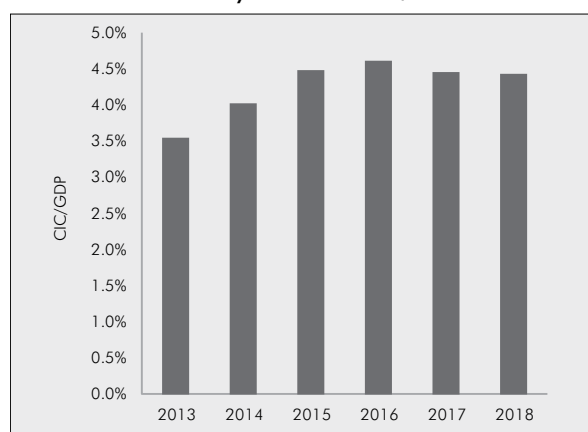
The value of currency notes in circulation increased by 7.1 percent to Rs.627.1 billion in 2018. Among the currency notes, the denominations of Rs.5000 and Rs.1000 together accounted for approximately 87 per cent of the total value of currency notes in circulation as at 31 December 2018, as given in Chart II-1.

Chart II-1
Value of Bank Notes in Circulation



The ratio of currency in circulation to GDP which was 3.54 per cent in 2013 was 4.44 per cent in 2018, demonstrating an increasing demand for currency as an important mode of payment in the country (Chart II-2).

Chart II-2
Currency in Circulation/GDP



(b) Currency issues to Licensed Commercial Banks

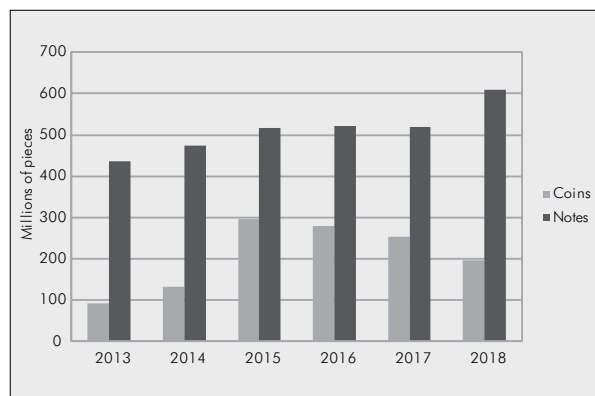
In order to meet the public demand for currency notes and coins, CRD continued to ensure the regular supply of currency notes and coins through LCBs and the special public counter established at the Pettah Branch of Bank of Ceylon to issue coins to the general public. Accordingly, currency notes and coins issued by CRD for circulation of the country during the year 2018, amounted to Rs. 795.4 billion or 610.1 million of pieces and Rs. 1.1 billion or 197.8 million of pieces, respectively (Table II- 5 and Chart II- 3). Demand for coins are in a decreasing trend since 2016 owing to low purchasing power of coins.

Table II-5
Currency Notes and Coins issued to LCBs

| Item | Value (Rs. bn) | | | | |
|-------|----------------|-------|-------|-------|-------|
| | 2014 | 2015 | 2016 | 2017 | 2018 |
| Notes | 431.8 | 503.4 | 594.0 | 628.0 | 795.4 |
| Coins | 0.8 | 1.6 | 1.6 | 1.4 | 1.1 |
| Total | 432.6 | 505.0 | 595.6 | 629.4 | 796.5 |

CRD continued its initiative of island wide coin distribution, to meet the regional level coin requirement. Accordingly, CRD distributed coins through Regional Offices of the CBSL to the regional level branches and Regional Offices of the LCBs.

Chart II-3:
Currency Issues¹ – Number of pieces of Coins and Currency Notes



¹Currency issuances consist both serviceable and new currency notes and coins

(c) Acceptance of Deposits of Currency from LCBs

As a part of currency operations, CRD accepts currency deposits from LCBs, primarily for the maintenance of the statutory reserve requirement imposed by the CBSL as a monetary policy tool. During 2018, CRD accepted both serviceable (fit) and unserviceable (unfit) currency notes including damaged notes from LCBs, as given in Table II- 6. In 2018, currency deposits of LCBs with CRD increased by 29.1 per cent compared to the previous year.

Table II-6:
Currency Deposits by LCBs

| Item | Value (Rs. bn) | | | | Change (%) | | | |
|-------|----------------|-------|-------|-------|------------|------|------|------|
| | 2015 | 2016 | 2017 | 2018 | 2015 | 2016 | 2017 | 2018 |
| Notes | 429.6 | 534.5 | 584.0 | 753.7 | 21.1 | 24.2 | 9.2 | 29.1 |

Note : The value of coins deposited by LCBs with CBSL is not significant

(d) Issue of Commemorative Coins and sales of commemorative collector items

In February 2018, CRD issued a circulation standard commemorative currency note to mark the 70th Independence Day of Sri Lanka with a face value of Rs.1000. In addition, in November 2018, CRD issued a circulation standard commemorative coin with a face value of Rs. 10 to mark the 75th Anniversary of Sri Lanka Signal Corps in recognition of its contribution to the nation. Commemorative collector items were sold through the CBSL Regional Offices and the Economic History Museum in Colombo.

5.3 Clean Note Policy

CRD continued the implementation of the Clean Note Policy during the past several years with the objective of ensuring good quality currency notes in circulation in the country, while withdrawing unfit/unserviceable currency notes from circulation. Accordingly, CRD initiated several actions to strengthen the

Clean Note Policy in 2018, as clean currency notes in circulation reflect a positive image of the country.

During 2018, CRD continued to ensure the regular supply of good quality (fit) currency notes and disposal of unfit currency notes, by destroying 343.8 million pieces of unfit currency notes deposited by LCBs, amounting to a face value of Rs. 252.2 billion². Additionally, CRD re-issued 231.5 million pieces of serviceable currency notes amounting to Rs 467.0 billion in to circulation which was deposited by LCBs.

CRD took measures to strictly enforce the law on willfully mutilation, alteration and defacement of currency notes, considering the increased number of willfully mutilated, altered and/or defaced currency notes among the currency deposits of LCBs on a regular basis.

A sound awareness campaign was conducted to educate the general public to refrain from such practices and informed to exchange such currency notes in their possession by 31 December 2018.

5.4 Assistance Provided to Law Enforcement Authorities

During 2018, CRD continued facilitating law enforcement authorities regarding violation of the provisions of the MLA on counterfeiting of currency as follows:

- Closely co-operated with the Counterfeit Currency Bureau of the Criminal Investigation Department (CID) of the Police and law enforcement authorities pertaining to counterfeiting attempts. Counterfeit notes detected in 2018 amounted to 1,625 pieces. The ratio of counterfeit currency notes in circulation which is measured by pieces per million decreased to 1.6 during 2018 compared to 5 which was in 2017.
- Endorsed and issued 108 certificates in terms of section 59 of the MLA with the signature of the Governor of the CBSL, as conclusive evidence for the imitation of currency note, to facilitate proceedings in courts.
- Attended 15 court cases to give evidence on currency counterfeiting.

5.5 Public Awareness

CRD conducted several public awareness programmes during 2018, targeting the general public, police officers, staff of LCBs and other financial institutions, teachers, students and public officials, to educate them/general public on the history of Sri Lanka currency, security features of Sri Lanka currency notes, good handling practices of currency and on the effective use of coins as follows:

- Conducted 23 seminars/workshops at the Center for Banking Studies, various LCBs, Police stations and national schools, etc.
- Displayed the mobile currency museum at 9 exhibitions around the country.

² The volume of destructed currency notes were considerably high compared to previous years due to strict implementation of the law on wilfully mutilation, alteration and defacement of currency notes.

- (c) Facilitated approximately 10,500 visitors, mainly school children, tourists and general public at the three currency museums of the CBSL and distributed information material and leaflets, highlighting the clean note policy and consequences of counterfeiting currency notes.
- (d) Conducted a discussion program through a leading TV channel on identifying counterfeit notes.

5.6 Approvals for Reproduction of currency notes

In terms of the policy approved by the Monetary Board, six approvals were granted for reproduction of currency notes in 2018.

5.7 System Improvements

CRD initiated actions to ensure the inspection of every single currency note at the end of the production line at the printer, in order to enhance the quality standard of the currency notes issued by the CBSL. As another step closer to automation of currency processing, CRD initiated to revamp the currency processing with the introduction of high-tech machines in order to improve efficiency and effectiveness of currency operations at CRD.

6. DOMESTIC OPERATIONS

6.1 Functions of DOD

As per the MLA, Domestic Operations Department (DOD) carries out several main functions, which include conducting Open Market Operations (OMO), providing standing facilities, regulating statutory reserves of commercial banks, acting as the banker and the official depository of the government, government agencies and other institutions, acting as banker to the commercial banks, providing temporary advances to the government, maintaining settlement accounts for Real Time Gross Settlement (RTGS) participants and providing intraday liquidity facility to RTGS participants.

6.2 Implementation of Monetary Policy

With the objective of maintaining short-term interest rates at a level commensurate with the prevailing monetary policy stance of the CBSL, DOD continued to implement monetary policy. DOD relied mainly on OMO, in signalling and steering Average Weighted Call Money Rate (AWCMR), which serves as the operating target of the enhanced monetary policy framework, towards desired level in a low volatility environment. Meanwhile, standing facilities were provided continuously to market participants to address liquidity needs on overnight basis. Accordingly, monetary policy operating procedure in 2018 continued to evolve in the midst of some changes in the nature and frequency of use of OMOs, policy rates, width of the corridor, the manner of policy signals, enhanced transparency, etc.

To ease the pressure on the foreign exchange market, margin requirement was imposed in September 2018 against Letters of Credit for importation of motor vehicles and non-essential consumer goods. Accordingly, LCBs were required to maintain minimum cash margin of 200 per cent for importation of motor vehicles and 100 per cent for importation of non-essential consumer goods. Further, LCBs were required to maintain minimum reserves of 100 per cent of such margin deposits with effect from 16 October 2018.

Access to real time accurate information on money market transactions is critical to facilitating the price discovery process in the money market. Accordingly, the Central Integrated Market Monitor (CIMM) was introduced with effect from 01 March 2018 to report information on call money, foreign exchange and government security transactions. CIMM also requires LCBs and Primary Dealers (PDs) to report liquidity estimates with high level of accuracy before 08:30 hrs on each working day to estimate daily liquidity in the banking system.

6.2.1 Open Market Operations

(a) Liquidity forecast

DOD estimates overall liquidity in the domestic money market and liquidity distribution among market participants on a daily basis to facilitate the selection of the appropriate OMO action in consistent with the monetary policy stance. To estimate liquidity, the monetary policy actions and autonomous factors which include currency in circulation, foreign exchange transactions of the CBSL, changes in commercial bank reserve positions and transactions of the government with the CBSL are taken into consideration. Based on the estimated liquidity in the money market, along with other factors such as appropriate level of the operating target and liquidity distribution among market participants, DOD uses different types of OMO instruments to conduct monetary policy.

(b) Auctions

(i) Repo Auctions

In 2018, DOD conducted overnight, short term and long term repo auctions on need basis to absorb excess liquidity in the market. Accordingly, overnight repo auctions were conducted to absorb liquidity on overnight basis when the money market liquidity was in surplus. Short-term repo auctions were conducted as a strategy to absorb liquidity up to one week on the same day settlement basis. Long-term repo auctions were conducted with settlement of the next business day to absorb market liquidity for a period beyond seven days when excess liquidity was likely to persist for long periods of time.

Table II-7

| (Rs. Bn) | | | |
|----------------------|----------------|----------------------|-----------------------|
| Type of Repo Auction | No of Auctions | Total Amount offered | Total Amount Accepted |
| Overnight | 103 | 1,724.50 | 1,218.68 |
| Short-term | 57 | 547.00 | 214.95 |
| Long-term | 55 | 429.50 | 96.63 |

(ii) Reverse Repo Auctions

DOD conducted reverse repo auctions on overnight, short term and long term basis to inject liquidity to the market. Intermittent reverse repo auctions, particularly overnight, were held in April, June and July 2018 and continuous auctions were held since mid-September 2018.

Table II-8

| (Rs. Bn) | | | |
|------------------------------|----------------|----------------------|-----------------------|
| Type of Reverse Repo Auction | No of Auctions | Total Amount offered | Total Amount Accepted |
| Overnight | 107 | 2,531.00 | 2,099.10 |
| Short-term | 70 | 1,400.80 | 968.71 |
| Long-term | 31 | 830.00 | 317.91 |

(iii) Outright Auctions

Outright auctions were conducted in 2018 to make a permanent effect in the money market liquidity by transferring the ownership of securities.

Table II-9

| (Rs. Bn) | | | |
|---|-----------------|----------------------|-----------------------|
| Type of Outright Auctions | No. of Auctions | Total Amount Offered | Total Amount Accepted |
| Outright Sale of Treasury bills (to absorb liquidity) | 98 | 241.50 | 63.73 |
| Outright Purchase of Treasury bills (to inject liquidity) | 110 | 475.00 | 40.50 |

To offset the impact of increase in Treasury bill holding of the CBSL as a result of primary market purchase, outright sale of Treasury bill auctions were conducted quite aggressively in the first quarter of 2018. DOD conducted outright sale of Treasury bill amounting to Rs. 56.3 billion as against increase of holding by Rs. 60.0 billion in January 2018.

However, with the emergence of high liquidity deficit in the domestic money market since mid-September 2018, DOD resorted to outright purchase of Treasury bill auctions to inject liquidity on a permanent basis.

6.2.2. Standing Facility

Standing facilities were provided throughout the year at the Standing Deposit Facility Rate (SDFR) and the Standing Lending Facility Rate (SLFR) to Participating Institutions (PIs) by bounding the overnight money market rates within the policy rate corridor. Standing Deposit Facility (SDF) was provided to absorb the excess liquidity from PIs while Standing Lending Facility (SLF) was provided to inject liquidity to PIs, when they

were unable to meet their overnight liquidity requirements fully through the inter-bank money market and OMO auctions. SDF transactions recorded a daily average of Rs. 18.8 billion in 2018, having recorded a total volume of Rs. 4,502.9 billion for the year 2018. The total volume lent under the SLF was Rs. 3,057.5 billion in 2018, with a daily average volume of Rs. 13.4 billion.

6.2.3 Statutory Reserve Ratio (SRR)

The SRR determines the minimum amount of reserves that each commercial bank is required to hold in terms of the regulations of the CBSL, in the reserve account with the CBSL, in proportion to the total rupee deposit liabilities of the respective bank. DOD is responsible for both administering and the maintenance of statutory reserves as per the SRR and monitoring compliance by commercial banks in this regard. SRR applicable to rupee deposit liabilities of commercial banks was reduced by 150 basis points to 6.00 per cent from 7.50 per cent with effect from 16 November 2018.

6.2.4 Bank Rate

The Bank Rate is the rate of interest at which the CBSL provides short term advances to LCBs under Section 87 of the MLA. The Bank Rate remained unchanged at 15 per cent in 2018. However, the CBSL did not lend funds to any LCB at this rate during 2018.

6.3 Banker to Commercial Banks and the Government**6.3.1 Accounts of Financial Institutions**

LCBs and PDs are connected to the monetary system through the settlement accounts with the CBSL. These accounts are maintained at DOD to facilitate clearance of payments and the settlement and for settlement of payments for scripless securities transactions among RTGS participants. Further, LCBs used these accounts for maintenance of bank reserves. Net settlement among LCBs in relation to payment and clearing systems such as Cheque Images and Truncation System (CITS), Sri Lanka Interbank Payment System (SLIPS), Common ATM Switch (CAS) and Common Electronic Fund Transfer Switch (CEFTS) are done via RTGS and such net settlements are facilitated by DOD. By end 2018, DOD maintained accounts for 26 LCBs and 8 PDs, Employees Provident Fund and the Central Depository System.

6.3.2 Government Accounts

Performing the functions relating to the CBSL's role as the banker to the government, DOD continued to maintain the accounts of government departments, agencies and statutory boards, and provided the required banking facilities to them. DOD maintained 64 such accounts as at end 2018 and handled 18,005 transactions amounting to Rs. 17,920.8 billion, during the year, on behalf of the government. More than 90 per cent of transactions were in relation to the Deputy Secretary to the Treasury (DST) Account, the Public Debt Department's Current Account, the Inland Revenue Commissioner's VAT Refund Account and the President's Fund Account.

In terms of Section 89 of the MLA, the CBSL provides provisional advances to the government, free of charge, with a ceiling of 10 per cent of the estimated government revenue approved by the Parliament for a given fiscal year. At the beginning of 2018, provisional advance to the government was increased by Rs. 21.1 billion to Rs. 225.0 billion, based on the government's revenue estimated for the year 2018 and approved by the Parliament, compared to that of Rs. 203.9 billion for the year 2017.

6.4 Provision of Intra-Day Liquidity Facility (ILF)

DOD continued its role towards the smooth and efficient operation of the RTGS system by making available intra-day funding through the intra-day liquidity facility (ILF) to RTGS participants. This facility was provided free of charge against the collateral of Treasury bills and Treasury bonds, which were valued at their current market prices with a sufficient hair cut to absorb any variations in market prices during the day.

The total value and average daily value of ILF drawn during the year amounted to Rs. 13,275 billion and Rs. 55 billion, respectively. This shows an increase in ILF utilisation over that of the previous year which amounted to a total of Rs. 11,430 billion with a daily average of Rs. 47.4 billion.

6.5 Supervision of Authorised Money Brokers

The Money Broking Regulations No. 1 of 2013 was issued under Section 10 (c) of the MLA and came into effect from 15 February 2013, considering the importance of Authorised Money Broking companies (AMBs) in the price discovery process in the money markets and to minimise the possibilities of market disturbances due to the involvement of AMBs. Subsequently, the Money Broking Regulations No. 1 of 2018 was issued with effect from 05 March 2018, repealing the Money Broking Regulations No. 1 of 2013 as amended by Money Broking Regulations No. 01 of 2016. Delegation of regulatory powers on forex market operations to the International Operations Department of the CBSL, introduction of new fit and proper rules for key officers and significant shareholders, inclusion of new sanctions for breaches of regulations and inclusion of reporting requirement of CIMM were included as major new additions.

With a view of further strengthening the market conduct and practices of the AMBs, CBSL took several measures recently to improve money broking industry. DOD introduced an online system to AMBs in 2016 to report details of transactions handled by them and it was further developed into a new system called the CIMM in 2017. At present Pls (LCBs and PDs) and AMBs report their transactions in the call, government securities and foreign exchange markets through the CIMM which came into operation in March 2018. Moreover, to upload financial statements and performance reports of AMBs, an online reporting system was introduced in 2018. CBSL issued a Code of Conduct for AMBs in November 2018 to ensure that operations of AMBs are carried out with high standards of integrity and professionalism in line with the international best practices.

By 2018, nine companies have been issued with "Certificate of Authorisation" under aforementioned regulations, which are designated as "Authorised Money Brokers". During the year 2018, six meetings were held by the DOD with the Boards of Directors of these companies, while DOD conducted 9 on-site examinations.

List of Money Brokers

1. Bartleet Mecklai & Roy (Pvt) Ltd
2. First Alliance Money Brokers (Pvt) Ltd
3. George Steuart Investments (Pvt) Ltd
4. MVS Money Brokers Ltd
5. Central Forex & Money Brokers Ltd
6. Piggot Chapman & Company (Pvt) Ltd
7. SMB Money Brokers (Pvt) Ltd
8. Taprobane Investments (Pvt) Ltd
9. Vishwin Money & Exchange Brokers Ltd

7. ECONOMIC RESEARCH

The Economic Research Department (ERD), which is a member department of the Economic Policy Advisory Cluster, was established with the founding of the CBSL in 1950 under the MLA of 1949. As per Section 25 of the MLA, ERD is responsible for conducting economic research and compilation of information to guide the Monetary Board and the Governor in formulating, implementing and executing policies and providing information to the public in the areas of money and banking and other economic subjects of general interest. With the view of contributing towards maintaining economic and price stability, ERD carried out its major responsibilities by assessing macroeconomic developments on a regular basis and assisting in the formulation of monetary and external sector policies, among others, while improving the existing methodologies and formats in data collection and processing. Performing the CBSL's role as the advisor on economic affairs to the government, ERD provided advice on emerging economic issues and recommendations on measures and policies that should be adopted to ensure greater fiscal-monetary coordination in order to achieve macroeconomic stability. While engaging in policy research, ERD published both statutory and other publications in order to keep the public informed of macroeconomic developments and operations of the CBSL. Moreover, ERD played an important role by establishing and maintaining relationships with foreign counterparts and other international agencies, and disseminating statistics and other macroeconomic information in a timely manner, thereby, improving cooperation and transparency.

7.1 Maintaining Economic and Price Stability

With the aim of achieving economic and price stability as per the mandate of the CBSL, ERD continued to compile, monitor and analyse data related to macroeconomic developments of the country to facilitate proactive and timely monetary policy decisions. Accordingly, as the secretariat of the Monetary Policy Committee (MPC), ERD produced and compiled

comprehensive reports inclusive of forward looking analyses containing economic and monetary statistics supported by model based macroeconomic projections to the MPC, thereby, enabling the MPC to make recommendations to the Monetary Board on required monetary policy decisions. Such inputs were further reinforced by the views and recommendations from the experts of the Monetary Policy Consultative Committee (MPCC), which was re-established in 2017 to enhance the dialogue between the CBSL and representatives of the academia and the private sector, in order to further strengthen the monetary policy decision making process and ERD facilitated the meetings of the MPCC. Moreover, ERD assisted the senior management by preparing the annual policy statement “Road Map 2019 - Monetary and Financial Sector Policies for 2019 and beyond” where the CBSL announced its approach in pursuing monetary policy and financial sector policies in the medium term, thereby, supporting the economy to reach its potential. ERD provided recommendations to the senior management on emerging issues and policy measures required for maintaining macroeconomic stability and the impact of fiscal measures already adopted by the government on various sectors of the economy. Further, ERD provided independent views on various issues of interest and highlighted their economic implications. ERD operated as the lead department on ‘Introduction of an Effective Flexible Inflation Targeting Regime’, which is one of the six bank-wide strategic priorities set for 2018-2020. The preparatory work continued on the adoption of Flexible Inflation Targeting (FIT) as the monetary policy framework including the initiation and the provision of required inputs to amend the MLA. In addition, ERD continued to improve its in-house modelling and forecasting capacity and infrastructure with the technical assistance from the International Monetary Fund (IMF) to develop a comprehensive, model-based Forecasting and Policy Analysis System (FPAS) to enhance the monetary policy decision making process.

7.2 Maintaining External Sector Stability

ERD carried out comprehensive analyses of the external sector by collecting, compiling and analysing statistics related to international trade and external finance, and provided policy advice and recommendations to the MPC and the Monetary Board, on a regular basis. As a part of this process, continuous assessment of the movements in exchange rates was conducted to identify any pressure on the rupee and prepare corrective measures in order to lessen any excessive volatility in the exchange rate.

Meanwhile, as per the provisions of the MLA, ERD continued to assess monetary implications of foreign loans obtained by the government during the year. Further, ERD liaised with the IMF and relevant departments of the Ministries and actively engaged in negotiations on the quantitative performance criteria and indicative targets and structural benchmarks outlined in the Extended Fund Facility (EFF) programme of SDR 1.1 billion (approximately US dollars 1.5 billion). Meanwhile, ERD submitted reports to the government analysing causes

and consequences of the developments in the external sector and the exchange rate and proposed policy measures to be adopted to address external sector vulnerabilities.

ERD undertook several initiatives to improve the compilation and dissemination of external sector statistics, in keeping with internationally accepted data reporting standards. ERD commenced publishing merchandise trade statistics compiled as per Standard International Trade Classification (SITC) Revision 04 on a monthly basis in 2018. ERD continued the publication of Balance of Payments (BOP) statistics and International Investment Position (IIP) statistics in the BPM6 format on a quarterly basis and International Reserve Data Template (RDT) on a monthly basis while making timely submissions related to Quarterly External Debt Statistics (QEDS) to the World Bank and direct investment data for the Coordinated Direct Investment Survey (CDIS) on an annual basis. Further, ERD conducted several surveys during the year to ensure accuracy and timeliness of external sector data. These surveys included the Annual International Investment Survey (AIIS), which was used to collect data on foreign assets and liabilities of the private sector and surveys related to trade in services covering resident and non-resident airlines, shipping lines, telecommunications, construction and insurance sectors. Further, ERD continued to conduct the monthly survey on inward workers’ remittances with commercial banks during the year. Also, ERD laid the groundwork to introduce a new data collection system of International Transactions Reporting System (ITRS), to monitor both cross border and foreign currency transactions that take place through the banking sector.

7.3 Providing Proactive Policy Advice

Continuous provision of proactive policy advice to the Monetary Board, the government and other stakeholders primarily on monetary policy, exchange rate policy and fiscal sector related issues was carried out by ERD in 2018. The *September 15th Report*, the confidential report highlighting the developments in the economy over the first eight months of the year and policy proposals that may be used in the process of preparing the government budget for 2019 was submitted to the Hon. Minister of Finance in compliance with Section 116(1) of the MLA. In addition, ERD provided technical inputs to the National Economic Council (NEC) and provided independent observations on various macroeconomic issues.

ERD coordinated eight MPC meetings during 2018. In addition to serving as a member of the MPC, the Director of Economic Research continued to serve as a member at a number of internal committees, such as the Market Operations Committee (MOC), the Financial System Stability Committee (FSSC), the Domestic Debt Management Committee (DDMC), Foreign Reserve Management Committee (FRMC), the Tender Board for the issuance of Treasury bills, Treasury bonds and Sri Lanka Development Bonds, Steering/Working Committee for Implementing FIT, the Risk Management Committee, the Training Committee, Steering Committee on Implementing a Road Map for Sustainable Finance in Sri Lanka, Steering

Committee for Developing a Policy Framework for Human Resources and Steering Committee cum Tender Board (SCTB) for International Sovereign Bond Issuance by the Government of Sri Lanka in 2018. The senior staff of ERD also served in several internal committees in addition to serving in the MPC as follows: Working Committee for Implementing FIT, Steering Committee on Implementing a Road Map for Sustainable Finance in Sri Lanka, Library Advisory Committee (LAC), Committee on Revamping the Financial Network (FINNET) System and Technical Evaluation Committee on appointing of Joint Lead Managers for the International Sovereign Bond Issuance by the government.

ERD staff continued to provide policy guidance by representing numerous committees and boards of several external institutions including the Hector Kobbekaduwa Agrarian Research and Training Institute (HARTI), National Science Foundation, Sri Lanka Export Credit Insurance Corporation, and several committees appointed by the Ministry of Finance, Ministry of National Policies and Economic Affairs and the Ministry of Power and Energy. Further, the Technical Evaluation Committee on the project of constructing a power plant at Kerawalapitiya, Project Committees on the Rehabilitation on the Northern Part of Elephant Pass Saltern, Restructuring of the Paranthan Chemicals Company Ltd., Restructuring of Lanka Mineral Sands Ltd., Technical Core Committee for National Export Strategy, Family Budget Unit and other national level committees such as National Trade Facilitation Committee (NTFC) and Government Finance Statistics (GFS) Coordinating Committee were also represented by ERD staff during the year.

7.4 Statutory Publications and Dissemination of Data and Information

As per the statutory requirements under the MLA, ERD prepared the Annual Report of the CBSL in all three languages for 2017 and presented to the Hon. Minister of Finance within the stipulated time period with the assistance of other Departments of the CBSL. In addition, *Recent Economic Developments - Highlights of 2018 and Prospects for 2019*, and Monthly Bulletins were also published. Moreover, the September 15th Report was also submitted to the Hon. Minister of Finance, as per the requirements under Section 116(1) of the MLA.

For the twelfth year, ERD prepared the *Road Map 2019 - Monetary and Financial Sector Policies for 2019 and beyond*, the policy statement of the Central Bank, which was announced by the Governor on 02 January 2019. The purpose of the Road Map was to enhance the predictability and transparency of the CBSL's policies which would help stakeholders to design and better calibrate their own plans and strategies for the period ahead.

In addition to the above, ERD continued to disseminate economic and financial information for the benefit of the general public, through daily, weekly and monthly indicators and bulletins published in the media and the data library, which is available on the CBSL website. Apart from the regular monetary policy review and external sector press releases, press statements on emerging matters were also released with

a view to enhancing the awareness of the general public. ERD disseminated statistics covering all sectors of the economy adhering to the requirements of the Special Data Dissemination Statistics (SDDS).

7.5 Engaging in Policy Research and Knowledge Sharing

With a view to fostering the research and analysis on subjects of contemporary importance, officers of ERD undertook a number of research studies during the year. The Research Advisory Panel (RAP), which was set up to facilitate research activities and promote the research culture within the CBSL, continued its activities in 2018 as well. Accordingly, "Research in Economics", a training course on research methodology was completed successfully by the RAP in order to enhance the research skills of officers of the CBSL and external participants, with the assistance of the CBS.

ERD organised the International Research Conference (IRC) in December 2018 for the eleventh consecutive year under the theme of "Inflation Targeting and Central Bank Independence, Accountability and Transparency". The IRC provided a platform to present and discuss theoretical and empirical research and share views among researchers, particularly related to contemporary macroeconomic policy. Accordingly, eight research papers were presented by researchers from Chile, Germany, India, Malta, Thailand, Australia and Sri Lanka, including a researcher from the CBSL. The keynote address was delivered by Prof. Chetan Ghate, Professor of Economics and a member of the Monetary Policy Committee of the Reserve Bank of India while an invited presentation titled "On the Role of the Exchange Rate in an Inflation Targeting Strategy", was delivered by Dr. Hans Genberg, Executive Director of the South East Asian Central Banks (SEACEN) Centre. This year's conference also featured the Dr. D S Wijesinghe Memorial Award presented to the best research paper at the conference.

Further, during the year, ERD published two volumes of Staff Studies, the research journal of the CBSL, which included 7 comprehensive research papers by officers from ERD and other Departments. One research paper published in the Staff Studies titled *An open economy quarterly projection model for Sri Lanka* was co-authored by researchers of the CBSL led by officers from ERD, along with IMF staff, and this paper was also published as an IMF Working Paper. Further, research studies by ERD officers during the year included a chapter titled *Inflation persistence: Evidence from CPI subcategories - The Sri Lankan experience* as part of a SEACEN Research Project, which was later published in early 2019. Further, two research papers were presented by ERD officers at international research conferences held in New Delhi, India. Meanwhile, ERD strengthened the research collaboration with international counterparts during the year by organising events jointly with such institutions.

ERD continued to share the expertise of its staff to improve knowledge on economics, both within and outside the CBSL. The officials of ERD served as resource persons at CBS, educational institutions such as universities, schools and

various other government and private sector institutions. In addition, ERD officers made presentations on central banking and macroeconomic developments to both local and foreign delegations who visited the CBSL. Among those were sessions educating journalists and the staff of the CBSL on FIT. Further, the senior officers of ERD participated at several conferences and seminars organised by outside parties as panelists during the year. Moreover, ERD officers took part in an industry study visit to the Ceylon Petroleum Corporation (CPC) refinery to understand the processes and issues faced by the petroleum sector in Sri Lanka. The senior officers of ERD continued to assist postgraduate aspirants of the CBSL to prepare research proposals and research papers. Meanwhile, several staff members of ERD rendered their services as resource persons at the “Thakshilawa” and “Arivootru” television educational programmes for the benefit of Advanced Level students in Sinhala and Tamil languages, respectively. Further, the officers of ERD facilitated the “Interbank Quiz Competition” of the Institute of Bankers of Sri Lanka (IBSL) and served as examiners, moderators and reviewers for internal and external examinations and publications.

7.6 Maintaining International Relations

On behalf of the CBSL and the government, ERD continued to function as the focal point of contact for multilateral financial organisations, including the IMF, SAARCFINANCE, SEACEN and South East Asia, New Zealand, Australia Central Banks (SEANZA), while also assisting the coordination between the government and other key multilateral development banks and agencies such as the World Bank and Asian Development Bank (ADB). Meanwhile, ERD continued to provide macroeconomic statistics and updates to international organisations such as the IMF, World Bank and international sovereign rating agencies during 2018.

During the year, ERD coordinated and worked closely with IMF staff missions that visited Sri Lanka for the review of the IMF EFF Programme in February 2018 and September 2018. Further, two IMF missions supported the CBSL’s project on monetary law reforms in June and August 2018. Additionally, three IMF Customised Training (CT) missions were coordinated by ERD, two of which were on developing Macroeconomic Diagnostics (MDS) tools for Sri Lanka, the first being conducted in February 2018, followed by a comprehensive follow-up mission in August 2018. The third follow-up CT mission was received in April 2018, which focused on improving the Quarterly Projection Model (QPM) as part of the FPAS of Sri Lanka.

Meanwhile, ERD organised the 54th SEACEN Governors’ Conference / High- Level Seminar and the 38th Meeting of the SEACEN Board of Governors in Colombo from 29 November to 02 December 2018, which was hosted by the CBSL as the chair of the Board of Governors and Executive Committee of the SEACEN Centre. The Conference was attended by Governors and delegates

of 19 member central banks and monetary authorities. The Deputy Managing Director of the IMF, Mr. Mitsuhiro Furusawa attended the Conference as the Keynote Speaker. In addition, ERD was involved in organising the IMF South Asia Regional Training and Technical Assistance Centre’s (SARTTAC) second steering committee meeting in May 2018, which was hosted by the CBSL.

8. EMPLOYEES’ PROVIDENT FUND

The Employees’ Provident Fund (EPF) was established under the Employees’ Provident Fund Act No.15 of 1958 (EPF Act). In terms of the provisions of the EPF Act, the general administration of the Act is vested with the Commissioner of Labour, while all the powers, duties and responsibilities of the fund management are vested with the Monetary Board of the CBSL as the custodian of the Fund. In terms of Section 5 of EPF Act, the Monetary Board has delegated the Employees’ Provident Fund Department of CBSL (EPF Department) to act as the operational arm for performing its duties, exercising its powers and discharging its functions.

8.1 Functions of the Department

The EPF Department is responsible for the collection of member contributions and surcharges, maintenance of general accounts and member accounts (individual accounts), crediting interest to member accounts, payment of benefits to beneficiaries of the Fund, investment of surplus funds and charging the expenditure incurred by the Monetary Board and the Commissioner of Labour in the performance of their duties and functions. The EPF Department continued to engage in the above activities as per the provisions of the EPF Act, while maintaining close collaboration with the Commissioner of Labour. A summary of activities carried out by the EPF Department during the year 2018 is given below.

(a) Receiving contributions and payment of benefits to those entitled

In 2018, total member contribution increased by 8.8 per cent to Rs. 145.0 billion from Rs. 133.3 billion recorded in the previous year, while the total refunds made to the members and their legal heirs amounted to Rs. 108.0 billion (Table II-10). Total refunds indicated a decrease of 8.1 per cent over 2017. Accordingly, the net contribution for 2018 increased to Rs. 37.0 billion compared to Rs. 15.8 billion recorded in 2017.

(b) Maintaining the general account of the Fund and the member accounts

The total value of the Fund increased by 10.8 per cent to Rs. 2,289.4 billion as at end 2018 compared to Rs. 2,066.3 billion as at end 2017, due to the income generated from investments and net contributions (after deducting refunds from contributions) received. Total liability to the members (member balances) stood at Rs. 2,254.2 billion as at end 2018 recording a 11.6 per cent increase from Rs. 2,020.8 billion as at end 2017 (Table II-10).

Table II-10
Selected Key Information of the Fund

| Item | 2017 | 2018(a) | Change (%) |
|---------------------------------------|---------|---------|------------|
| Total value of the Fund (Rs.bn) | 2,066.3 | 2,289.4 | 10.8 |
| Total liability to members (Rs.bn) | 2,020.8 | 2,254.2 | 11.6 |
| Total number of member accounts (mn) | 18.0 | 18.6 | 3.3 |
| Contributing member accounts (mn) | 2.8 | 2.6 | (7.1) |
| Non-contributing member accounts (mn) | 15.3 | 16.0 | 4.6 |
| Total contributions (Rs.bn) | 133.3 | 145.0 | 8.8 |
| Total refunds (Rs. bn) | 117.5 | 108.0 | (8.1) |
| Net contribution (Rs.bn) | 15.8 | 37.0 | 134.2 |
| Number of refunds | 260,989 | 241,190 | (7.6) |

(a) Provisional

Source: EPF Department, Central Bank of Sri Lanka

(c) Investment Activities of the Fund

(i) Investment Portfolio

In 2018, EPF Department continued to invest its funds specially in long term Treasury Bonds and Corporate instruments. The total investment portfolio (book value) of the Fund grew by 15.4 per cent to Rs. 2,298.8 billion as at end 2018 from Rs. 1,992.4 billion recorded as end 2017 (Table II-11). The investment policy of the Fund continued its focus on providing a long-term positive real rate of return to the members while ensuring the safety of the Fund and maintaining a sufficient level of liquidity to meet refund payments and other expenses of the Fund.

Accordingly, as at end 2018, the investment portfolio consisted of 92.2 per cent in government securities, 3.3 per cent in equity, 1.9 per cent in corporate debentures and trust certificates, 1.5 per cent in fixed deposits and the remaining 1.1 per cent in reverse repurchase agreements. The maturity profile of the government securities portfolio together with yield rates as at end 2018 are given in Table II-12.

Table II-11
Investment Portfolio

| Type of Investment | End 2017 | | End 2018 | |
|------------------------|----------------|--------------|----------------|--------------|
| | Amount (Rs.bn) | Share (%) | Amount (Rs.bn) | Share (%) |
| Treasury Bonds & Bills | 1,818.6 | 91.3 | 2,119.2 | 92.2 |
| Equity | 84.3 | 4.2 | 74.9 | 3.3 |
| Corporate Debts | 41.5 | 2.1 | 44.8 | 1.9 |
| Fixed Deposits | 48.0 | 2.4 | 33.6 | 1.5 |
| Reverse Repos | - | - | 26.4 | 1.1 |
| Total | 1,992.4 | 100.0 | 2,298.8 | 100.0 |

Source: EPF Department, Central Bank of Sri Lanka

Table II-12
Maturity Profile of Government Securities Portfolio
(As at end of 2018)

| Maturity | Maturity Value (Rs.mn) | Share (%) | Weighted Average Yield (%) |
|-------------------|------------------------|--------------|----------------------------|
| Less than 1 year | 124,096.4 | 5.8 | 9.90 |
| 1-2 years | 182,944.5 | 8.5 | 11.26 |
| 3-4 years | 269,016.6 | 12.5 | 10.50 |
| More than 5 years | 1,571,118.8 | 73.2 | 11.37 |
| Total | 2,147,176.2 | 100.0 | 11.16 |

Source: EPF Department, Central Bank of Sri Lanka

(ii) Investment Income

During 2018, the total investment income of the Fund amounted to Rs. 222.4 billion, recording a decrease of 0.1 per cent over the previous year (Table II-13). Interest income was the major source of income to the Fund and it grew by 4.47 per cent to Rs.229.4 billion in 2018 from Rs. 219.6 billion in 2017. The dividend income realised from equity portfolio increased by 29.9 per cent to Rs. 3,887.6 million in 2018, compared to Rs. 2,993.6 million earned in 2017. Further, purchase of Treasury Bonds from the secondary market was resumed in 2018. Overall, return on investments of the Fund has recorded 10.4 per cent in 2018 compared to 11.8 per cent recorded in 2017.

Table II-13
Income on Investments

| Source of Income | 2017 | | 2018 | |
|---|------------------|--------------|------------------|--------------|
| | Amount (Rs.mn) | Share (%) | Amount (Rs.mn) | Share (%) |
| Interest with amortization gains | 219,635.3 | 98.7 | 229,446.0 | 103.1 |
| Marked to market gain/ loss from government securities* | 1,640.2 | 0.7 | - | - |
| Marked to market gain/loss from equity | (163.4) | (0.1) | (10,901.3) | (4.9) |
| Capital gains from equity | - | - | 7.2 | - |
| Dividends | 2,993.6 | 1.3 | 3,887.6 | 1.7 |
| Impairment of financial assets | (1,502.1) | (0.7) | 0.6 | - |
| Total | 222,603.7 | 100.0 | 222,440.1 | 100.0 |

Source: EPF Department, Central Bank of Sri Lanka

* Government Securities were reclassified to Amortized Cost Category as per the Accounting Standard, SLFRS 09 - Financial Instruments applied w.e.f. 01.01.2018

(iii) Expenditure

The total operational expenditure of the Fund increased by 11.6 per cent to Rs. 1,505.3 million in 2018 compared to Rs. 1,348.7 million in 2017, and as a

ratio of total gross income, it was increased to 0.68 per cent in 2018, from 0.61 per cent in 2017 (Table II-14). Over the years, the Fund has maintained its operational expenditure below 1 per cent of the total gross income.

Table II-14
Operational Expenditure

| Item | Amount (Rs.mn) | | Change (%) |
|--|----------------|----------------|-------------|
| | 2017 | 2018 | |
| Personnel expenses | 847.3 | 967.3 | 14.2 |
| Administrative expenses | 454.1 | 470.0 | 3.5 |
| Other expenses | 47.3 | 68.0 | 43.7 |
| Total | 1,348.7 | 1,505.3 | 11.6 |
| Total Expenses as a % of Gross Income | 0.61 | 0.68 | |

Source: EPF Department, Central Bank of Sri Lanka

(d) Payment of Interest on Member Balances

Over the last 10 years, EPF was able to pay consistently high rate of interest to its members (Table II-15). The relevant details are given in Chapter 8.

Table II-15
Rate of Interest paid on Member Balances

| Year | Interest Rate Paid (%) | Effective Interest Rate (%) ¹ |
|----------|------------------------|--|
| 2008 | 13.20 | 13.44 |
| 2009 | 13.75 | 13.92 |
| 2010 | 12.50 | 12.65 |
| 2011 | 11.50 | 11.58 |
| 2012 | 11.50 | 11.62 |
| 2013 | 11.00 | 11.14 |
| 2014 | 10.50 | 10.60 |
| 2015 | 10.50 | 10.57 |
| 2016 | 10.50 | 10.51 |
| 2017 | 10.50 | 10.51 |
| 2018 (a) | 9.50 | 9.54 |

(a) Provisional

Source: EPF Department, Central Bank of Sri Lanka

¹ EIR = (Interest paid to members) / [(Beginning of the year member balances + year end member balances before crediting interest) / 2]

(e) Engaging in Member Services

(i) Issuing of Member Account Statements

During 2018, member account statements for the 1st half and 2nd half of 2017 were issued to the active members of EPF, through their employers as given in Table II-16.

Table II-16
Issue of Member Account Statements

| Period | No. of Employers | No. of Statements (Active Members) |
|---------------------------|------------------|------------------------------------|
| 2017 1 st half | 69,020 | 2,176,952 |
| 2017 2 nd half | 76,308 | 2,711,049 |

Source : EPF Department, Central Bank of Sri Lanka

(ii) Issuing of Certificates of Guarantees to members to facilitate obtaining Housing Loans

The Housing Loan Scheme, introduced in 1988 with the objective of facilitating the members to obtain housing loans from the participating lending institutions, viz., Housing Development and Finance Corporation Bank, State Mortgage and Investment Bank, Bank of Ceylon, People's Bank and Co-operative Rural Banks, continued in 2018. Under this scheme, during 2018, EPF Department issued 10,036 certificates of guarantees to members against their EPF balances to the participating lending institutions for the approval of housing loans amounting to Rs. 4,974 million (Table II-17). Further, during 2018, nearly Rs. 2,759 million was deducted from relevant member accounts and remitted to the participating lending institutions in 2018 to settle the overdue loans during the year 2017.

Table II-17
Housing Loan Guarantee Facility

| Year | Issued Certificates (No.) | Credit Approved (Rs. mn) | Amount Remitted to Lending Institutions (Rs. mn) |
|---------|---------------------------|--------------------------|--|
| 2008 | 12,519 | 3,008 | 1,192 |
| 2009 | 10,383 | 2,680 | 1,552 |
| 2010 | 13,848 | 4,512 | 2,093 |
| 2011 | 20,041 | 6,355 | 1,896 |
| 2012 | 11,234 | 3,973 | 2,019 |
| 2013 | 16,268 | 6,914 | 2,178 |
| 2014 | 17,786 | 8,021 | 2,394 |
| 2015 | 13,132 | 5,489 | 2,522 |
| 2016 | 12,780 | 5,414 | 2,541 |
| 2017 | 10,998 | 4,946 | 2,485 |
| 2018(a) | 10,036 | 4,974 | 2,759 |

(a) Provisional

Source: EPF Department, Central Bank of Sri Lanka

(iii) Pre-Retirement Refund Scheme

In terms of the provisions in Employees Provident Fund (Amendment) Act, No. 02 of 2012 and the subsequent procedures passed by the Parliament, payments of 30 per cent EPF pre-retirement refund scheme, has been in operation since 1st July 2015. The scheme is in high demand by beneficiaries and since the inception a sum of Rs. 73.1 billion has been refunded to over 130,000 beneficiaries by the end of 2018. During 2018, Rs.14.8 billion has been released to 28,377 beneficiaries under this scheme.

(iv) EPF Mobile Service Programme

EPF continued the conducting mobile services in 2018 as well with a view towards enhancing delivery of member services at their convenience and the enhancement of public awareness on EPF operations.

The mobile services offered almost all services a member could obtain by visiting the EPF Department located in Colombo, at their own area or work place. The services included issuing of EPF balance statements, amendment of EPF member details, clearing of dummy

numbers, EPF account amendments, awareness for employers on e-media and direct debit system, re-registration of member details, promoting SMS & internet member services and providing advice on overall EPF procedures.

Accordingly, during the year EPF Department conducted 20 mobile services and 03 major awareness programmes. Some of these mobile services were conducted in collaboration with the Department of Labour, Department of Registration of Persons, Registrar General's Department, Police Department and respective District/Divisional Secretariats.

EPF Department also participated in mobile services organized by other Government and non-Government organizations/Ministries at the invitation of them to provide EPF related services and to educate the participants. Further, EPF Department was also invited for events/exhibitions organized by other government or non-government organizations where there were large public gathering. EPF Department was awarded the "Best Digital Government Solution in Digital Government Pavilion at the exhibition, INFOTEL 2018.

In addition, awareness programmes were conducted in parallel to the mobile services, targeting members, employers and other stakeholders on the services offered by the EPF using a mix of communication media such as e-mail, posters, leaflets, video clips and presentations.

Prior to each mobile service programme, a special awareness programme is conducted for relevant employers, managers and other administrative staff members of respective employers with a view to enhance the effectiveness of the mobile services.

(v) EPF Contribution through Electronic Media

The e-Return system which facilitates collection of EPF contributions and respective member details in electronic means was introduced by the EPF Department with an objective of improving its operational efficiency in a paperless operating environment. This system was operated on voluntary basis until the respective enactment, i.e., EPF (amendment) Act. No. 02 of 2012 came in to force. Accordingly, submission of EPF contribution details through an electronic media became mandatory for the employers having more than 50 employees in their employments. In 2011, LCBs joined this system as facilitators to collect EPF contributions via their own online portals which made a remarkable improvement in employer participation and speedy member accounts updating process while strengthening its administrative and monitoring functionalities. The e-Return system achieved its highest technological breakthrough in 2016 with the introduction of the online member information validating mechanism which brought 100% process automation and real time updation of member accounts. Accordingly, eight LCBs, including the two LCBs joined in 2018, are facilitating EPF online payments while four of them provide online member

information validation and real-time member accounts updating facility for their customers.

In addition, actions were taken to make the employers further aware regarding the e-Return submission procedure and its benefits for EPF stakeholders. Accordingly, participation of employers in e-Return submission system was increased from 7,900 to 8,540 covering approximately 81% of the active member accounts and nearly 88% of the total monthly EPF contribution by end 2018.

Further, with a view of introducing new methodologies for paying EPF, initiatives were taken to develop the EPF official website enabling employers to submit their e>Returns through the website and to implement the Lanka Clear's Common Electronic Fund Transfer System which enables employers to pay monthly contributions from any participating bank.

(vi) Re-registration of EPF Members

The special project launched in 2010 by the Employee's Provident Fund Department in collaboration with the Department of Labour (DL) to re-register its members with a view of providing an efficient service to both employers and employees was continued in year 2018. Accordingly, the collection of member information with National Identity Card (NIC) details and re-registration of such members as per the NIC data were carried out, facilitating the identification of the members with a Unique Identification (UID) Number and enabling both EPF and the DL to establish a common Member Centric Database (MCD). This programme helps both EPF and DL to provide the services to its stakeholders productively through the improved quality of member information.

By end of 2018, NIC details of around 1.91 million of active EPF members (contributing members) have been collected. Accordingly, 81 percent accounts of these members (1.55 million accounts) were assigned UIDs, while the verification of remaining members' details is in progress. A system has also been established in parallel, to monitor the error-free updation of NIC details of all new members whose member contributions are received for the first-time, on a monthly basis. Further, necessary actions initiating to expedite the process and to re-register all active member accounts of EPF through an electronic validation system.

(vii) Other Services

EPF Department strives on efficient and effective delivery of services to its members. In today's fast, paced environment members demand excellent service delivery. Thus the Public Relations and Inquiries Counter of EPF Department has concluded a challenging year in 2018. In 2018, the number of member/employer visits to the Department is recorded as 173,595, while the Department had received 82,454 member inquiries through calls and 9,542 member inquiries through e-mails. The Department has also received 100,058 letters in 2018 through members, employers and other stakeholders.

The Department also receives a large number of member requests through letters and through the members visiting the Department, for amendment/correction of details in the member accounts. In 2018, the Department has performed approximately 60,532 amendments in EPF Member Accounts. The Amendments performed in EPF member accounts can be mainly categorized into two components. That is error correction in Name/NIC details of an EPF member account and corrections of contributions credited to a member account. During the year 2018, the Department has performed 57,602 Name/NIC amendments and 2,750 Account Amendments. Further, with the implementation of the Image Scanning Project the facility for the performance of EPF member account amendments was extended to the Regional Offices of the CBSL. Accordingly, in 2018, EPF Department attended to 10,343 EPF member account amendments referred from Regional Offices of the Bank.

(f) Other Functions

Furthermore, EPF is in the process of reviewing and restructuring its investment strategy and framework under the Financial Sector Modernization Project of World Bank (WB) and GOSL. Furthermore, WB is providing financial assistance for the implementation of a comprehensive ICT solution for EPF. In view of this, a Business Process Review (BPR) is being conducted with the technical assistance of Asian Development Bank (ADB) under the Capital Market Development Programme GOSL and ADB. Phase I of the BPR was conducted in 2018.

09. FACILITIES MANAGEMENT

The Facilities Management Department (FMD) implemented several projects during 2018 to upgrade its Head Office building and equipment to ensure business continuity, while continuing maintenance services. More emphasis was given during the year for fast tracking the Head Office Building Retrofit Project where a major refurbishment of the building interior, plant and equipment is envisaged. A comprehensive building survey to assess the condition of the building including structural testing of building components was carried out with the assistance of the project consultant. As a part of this project, procurement work was initiated for the replacement of the standby generator control system of the building, and the audio-visual system of its main conference hall. Further, enhancing the facilities for the CBSL's operations, contracts were awarded for the installation of a call recording system and a IP based CCTV system at the Head Office building.

During the year under review, FMD took initiatives to enhance operational facilities at several key departments

of the CBSL. FMD implemented projects to install a currency dust extraction system for improving the working environment inside the Currency Department and to construct a new currency storage facility to meet additional capacity requirements for currency operations. New projects were implemented for upgrading the CBS and its associated buildings including a new canopy roof for the auditorium entrance, a new standby generator, a new cafeteria for course participants, and improved accommodation facilities at the Sovereign Residencies. A full repair of the roof of the Lloyd's Building, where the EPF is located, was also carried out.

With the aim of catering to the requirements of the staff of the CBSL who travel outstation on duty and for holidays, the FMD took steps to expand the available holiday home facilities. Furnishing and interior work of the new holiday home in Kilinochchi was completed during this period and a project consultant was appointed to undertake the design and construction of a new holiday home facility in Anuradhapura as the condition of the existing building has been deteriorated due to aging. Several upgrading works were carried out at the holiday home in Nuwara Eliya including reconstruction of the boundary wall, repairing of roof, and installation of a new standby generator.

FMD undertook several administrative measures to streamline its facilities management activities in 2018. An online reservation system for holiday homes was introduced for the convenience of the employees and pensioners, and the facility of hiring a web-based cab service was introduced to provide easy transport access for the staff. In line with a decision by the Cabinet of Ministers, FMD was able to dispose the two overseas properties of the CBSL in May 2018 by transferring their ownership to the Ministry of Foreign Affairs. While attending to the various new projects for upgrading and expansions, FMD continued to maintain the buildings, equipment and landscaping and provide necessary support services in transport and telecommunication as part of its key responsibilities.

10. FINANCE

The Finance Department (FD) undertakes the financial reporting function of the CBSL in terms of International Accounting Standards /International Financial Reporting Standards and relevant provisions of the MLA. Functions of FD include preparation of the financial statements of the CBSL, preparation and monitoring of the annual budget of the CBSL, maintaining a payment system for internal and external financial transactions of the CBSL, disbursement of donor funds and repayment of foreign loans of the government, maintaining systems for internal reporting of financial transactions, management of 17 internal funds, maintaining the Fixed Assets Register for the CBSL and maintaining the database of staff loans.

10.1 Preparation of the financial statements

(a) **Monthly Balance Sheet:** As per the requirement of the MLA, No 58 of 1949, the monthly Balance Sheets for December 2017 and January to November 2018 were prepared.

(b) **Quarterly Reports:** Quarterly financial performance and positions were reported to the Monetary Board in the year 2018.

(c) **Annual Financial Statements:** International Accounting Standards (IAS) and International Financial Reporting Standards (IFRS) have been adopted since 2002. Financial statements are published in the Annual Report of the CBSL. Accounting systems and procedures were updated to comply with relevant accounting standards and requirements on a continuous basis during the year 2018. Audited Financial Statements of the CBSL for the year 2018 are presented at Part II of this Report.

(d) **Compliance with IFRS 9:** The CBSL Financial Statements as at 31 December 2018 have been prepared and presented in compliance with IFRS 9, effective date of which was for the annual period beginning on or after 01 January 2018.

10.2 Preparation of the Annual Budget

The annual income and expenditure budget and capital budget of the CBSL for the year 2019 were prepared in line with action plans under the strategic plan of each department of the CBSL using the "On-line Budget System". The approval of the Monetary Board for the budget of the CBSL was obtained in December 2018 and the budget was made available to the departments on the first working day of 2019. Meanwhile, quarterly budgetary performance statements for the year 2018 were submitted to the Monetary Board in the interest of effective monitoring of budgetary control.

10.3 Payment System for Internal and External Financial Transactions

(a) All internal payments for employee remunerations, staff loans, operational expenses, etc., were facilitated by the payment system in 2018 within the time targets.

(b) All external payments to local and foreign suppliers were made as per the procedures laid down under the standing orders of the CBSL. During the year 2018, the total number of payments were 4,603 of which included 4,354 to local suppliers and 249 to foreign suppliers.

(c) Nearly 2,753 disbursements amounting to Rs 3,220.2 billion to the General Treasury and relevant projects and 597 installments amounting to Rs 2,409.2 billion on repayment of foreign loans were made during the year 2018. In addition, three banking arrangements were signed with two foreign banks for various projects.

10.4 Management of internal funds

(a) A separate unit that was established under FD and commenced operations in March 2016 to centrally manage the investments of Central Bank's internal funds (excluding EPF) as per the decision taken by the Monetary Board, managed 17 internal funds consisting of 8 superannuation funds of the staff and pensioners and 4 other funds administered by FD, Deposit Insurance and Liquidity Support Fund administered by the Resolution and Enforcement Department, 3 funds administered by the Staff Services Management Department and project funds administered by the Regional Development Department. All funds are invested under a common Investment Policy by the FD and the respective owner departments perform as the administrators of their funds. The fund management governance system includes an independently operating front office, middle office and a back office and decisions taken at the Internal Investment Oversight Committee (IIOC) chaired by a Deputy Governor of the CBSL which met 12 times during the year 2018 to advise and monitor the investments of funds. Performance of these investments were reported monthly to the Monetary Board for information purposes.

(b) The funds are invested mainly in Government Securities, Fixed Deposits, high rated Corporate Debentures and Short Term Reverse Repos. The audited financial Statements of six superannuation funds for 2017 were submitted to the Monetary Board as per the rules of those funds. As at end 2018, the total fund base had been increased to Rs. 112.84 billion.

Table II-18
Performance of Fund Management –
2018 (Rs. bn.)

| Department | Portfolio value as at 31 Dec 2018 (invested values) | Portfolio value as at 31 Dec 2017 (invested values) |
|----------------------------|---|---|
| Finance | 55.16 | 52.22 |
| Resolution and Enforcement | 53.96 | 38.47 |
| Regional Development | 3.64 | 3.12 |
| Staff Services Management | 0.08 | 0.07 |
| Total | 112.84 | 93.88 |

10.5 Maintaining Fixed Assets Register

FD maintained all records of the fixed assets of the CBSL in the Fixed Assets Register in the Fixed Asset Module of the General Ledger System. All changes such as new purchases and locations, change of locations, revaluations, depreciation and disposals were recorded in this register during the year 2018. The register was updated during the year 2018 with 957 items procured and 606 disposals.

10.6 Maintaining the database of staff loans

FD continuously updated the loan database of the CBSL staff with the assistance of the Information Technology Department to facilitate the loan recovery record process and to supply information to employees and the management during the year 2018. Accordingly, 1,556 loans amounting to Rs 1.9 billion have been granted to the employees during 2018.

10.7 Other Operations - Procurement Process

According to the Rules of the CBSL, FD is represented in all Technical Evaluation Committees and Tender Boards for the procurement of goods and services and the Boards of Survey of the CBSL for disposal of fixed assets. During the year 2018, FD officers represented around 229 Tender Boards and 84 Technical Evaluation Committees related to procurements, one Board of Survey and one Vehicle Disposal Committee related to disposal of fixed assets.

11. FINANCIAL INTELLIGENCE UNIT

The Financial Intelligence Unit (FIU) has been providing its services locally as well as internationally for over a decade now. Since its establishment in 2006 under the Financial Transactions Reporting Act, No. 6 of 2006 (FTRA), it functions as an independent statutory authority. FIU acts as the lead Anti-Money Laundering and Combating the Financing of Terrorism (AML/CFT) regulator of the country. In addition, FIU has provided a comprehensive coverage for country's financial and non-financial establishments to comply with the AML/CFT regulations issued by Financial Action Task Force (FATF) and supervise by FATF jointly with Asia Pacific Group on Money Laundering (APG). The key functions of FIU include collection and receipt of information on financial transactions for the purpose of detecting possible links to Money Laundering (ML) and Terrorist Financing (TF) and other related unlawful activities as defined in the FTRA, analysis of suspicious financial transactions relating to the above unlawful activities and dissemination of information of such analyses to relevant law enforcement agencies for investigation. Furthermore, the functions of FIU are also enforced under the Prevention of Money Laundering Act, No. 5 of 2006 (PMLA) and Convention on the Suppression of Terrorist Financing Act, No. 25 of 2005 (CSTFA).

11.1 Receipt, Analysis and Dissemination of Information

FIU has made it mandatory for reporting institutions to submit information on financial transactions, including suspicious transactions, from Reporting Institutions through a web-based system, "LankaFin", especially designed to assist in reporting on ML and TF. Accordingly, Licensed Commercial Banks (LCBs), Licensed Specialised Banks (LSBs), Licensed Finance Companies (LFCs), Insurance Companies, Stock Brokers (SBs) and Money or Value Transfer Service (MVTs) providers continued to report to FIU on cash transactions and electronic fund transfers (both

local and foreign) of Rs. 1.0 million and above or its equivalent in foreign currencies. In addition, Suspicious Transactions Reports (STRs) were filed with FIU by the Reporting Institutions in terms of Section 7 of the FTRA. Accordingly, over 11.9 million of cash/funds transfers and 1,022 STRs were reported during the year 2018. Moreover, Authorised Money Changers (AMCs) also reported their cash transactions exceeding the threshold amount through the Director of Foreign Exchange who monitors and regulates the AMC sector. In 2018, FIU disseminated 317 STRs to law enforcement agencies and regulatory authorities for further investigation.

11.2 Regulation of Reporting Institutions

FIU continued to issue regulations for its reporting entities to streamline the regulatory framework further. Accordingly, Gazette (Extraordinary) No. 2053/20 dated January 10, 2018 on Designated Non-Finance Business (Customer Due Diligence) Rules, No. 1 of 2018 was issued to Designated Non-Finance Businesses to conduct the customer due diligence based on "Risk-Based Approach". Furthermore, during the year, FIU issued seven guidelines to Financial Institutions as well as Designated Non Finance Businesses and Professions on the areas such as Money Laundering and Terrorist Financing Risk Management, AML/CFT Compliance Obligations for Casinos and Gambling Houses, AML/CFT Compliance Obligations for Dealers in Real Estate, Precious Metals, Precious and Semi-Precious Stones, Identification of Beneficial Ownership, Implementing United Nations Resolution (Sanctions in relation to Democratic People's Republic of Korea and Iran) and Suspicious Transactions Reporting. Apart from this, a circular on Procedure of Conducting Risk-Based Onsite Examinations, was issued to strengthen the process of AML/CFT supervision.

11.3 Domestic and International Cooperation

During the year, FIU entered into a number of Memorandum of Understanding (MOUs) to share information among them and represented in several international cooperation events to enhance the knowledge of the FIU staff and knowledge sharing basis.

a) Memorandum of Understanding

In 2018, FIU signed three MOUs domestically with the Department of Motor Traffic, Insurance Regulatory Commission of Sri Lanka and Securities and Exchange Commission of Sri Lanka. Accordingly, the total number of MOUs signed by FIU with domestic agencies increased to 08 as at end 2018.

b) Egmont Group

The FIU obtained assistance from members of the Egmont Group, the Association of the FIUs consisting of 155 member FIUs globally, in order to carry out investigations and collaborate with member countries to gather intelligence on their investigations. Total number of instances that FIU exchanged information with Egmont members was 94 in the year 2018. FIU responded for 24 requests from counterpart

FIUs and made 70 requests from counterpart FIUs to share information relating to on-going investigations. Further, the FIU officers participated in the Egmont Group of Financial Intelligence Units' Meetings held in Buenos Aires, Argentina in March 2018 and the Egmont Plenary meeting held in Sydney, Australia in September 2018.

c) Asia Pacific Group on Money Laundering (APG)

The FIU officers participated in the APG Plenary and Technical Assistance Sessions held in Kathmandu, Nepal in July 2018 where the Director of the FIU co-chaired the Plenary and the APG Typologies and Capacity Building Workshop held in Russia in December 2018.

(d) BIMSTEC Sub-Group on Anti Money Laundering and Combating the Financing of Terrorism (BIMSTEC SG-AML/CFT)

The FIU officers participated in the 10th SG-AML/CFT meeting of the Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation (BIMSTEC) held in Kathmandu, Nepal during 19-20 November 2018.

11.4 Institutional Capacity Building and Awareness Programmes

In continued efforts to enhance the awareness on detecting, reporting and analysing of ML and TF related transactions, 61 awareness/training programmes were conducted during the year, accommodating 3,258 participants from LCBs, LSBs, LFCs, MVTs providers, DNFBPs, Stock Brokers and Insurance Companies. The 4th and 5th Technical Assistance Mission of the International Monetary Fund (IMF) was conducted by experts from the IMF during the period 26 February – 07 March 2018 and 26 November - 04 December 2018, respectively. The Mission continued to provide technical assistance to strengthen AML/CFT regime in Sri Lanka, in the areas of risk-based supervision, FIU capacity development and legislative amendments. Further, the Resident Advisor from the US Department of Treasury also continued to provide technical assistance in the areas of FIU Operational Effectiveness, Financial Sector Supervision and AML/CFT Case Development and Asset Management.

11.5 Review by International Cooperation Review Group

The 2nd Mutual Evaluation (ME) on Sri Lanka was conducted during 2014/15 by the APG, with the intention of assessing Sri Lanka's AML/CFT compliance with international AML/CFT standards. The Mutual Evaluation Report (MER) adopted in July 2015 recommended a series of actions to be implemented by Sri Lanka under the APG's 'expedite enhanced follow up' process. In October 2016, the FATF informed that Sri Lanka will be subjected to a review of the International Cooperation Review Group (ICRG) of the FATF to assess the progress of AML/CFT effectiveness. After several discussions and progress reports, the FATF informed that Sri Lanka has not made sufficient

progress in 4 areas, namely International Cooperation, Supervision, Legal Persons and Arrangements and Targeted Financial Sanctions on Proliferations (North Korea & Iran). As a result, the FATF at its Plenary held at Buenos Aires, Argentina in October 2017, listed Sri Lanka as a jurisdiction with strategic AML/CFT deficiencies in the FATF's Compliance Document which is more commonly identified as the "Grey List". Upon listing, a time-bound action plan to address the strategic deficiencies identified was provided to Sri Lanka.

Since the listing in November 2017, Sri Lankan authorities have taken effective and tangible steps to implement the FATF Action Plan including the passing of Trust Ordinance (Amendment) Act, No. 6 of 2018, Mutual Assistance in Criminal Matters (Amendment) Act, No. 24 of 2018, issuance of regulation/directives/guidelines on implementing United Nations Security Council Resolutions on Democratic People's Republic of Korea and Iran, extending the AML/CFT coverage to Designated Non Finance Businesses and Professions (DNFBPs) by issuing Customer Due Diligence Rules, implementation of risk-based supervision, enforcement actions and outreach for financial institutions and DNFBPs.

The FATF assessed Sri Lanka's progress in implementing the Action Plan through the Asia Pacific Joint Group (AP/JG). Three progress reports were submitted and face-to-face discussions were held with the AP/JG on the progress made by Sri Lanka during January, May and September 2018, respectively. The AP/JG had acknowledged the progress made by Sri Lanka. Hence, it is expected that Sri Lanka would exit the "Grey List" by mid-2019.

12. FOREIGN EXCHANGE

The Department of Foreign Exchange (DFE) was established in terms of Section 2 of the Foreign Exchange Act (FEA) No. 12 of 2017, with effect from 20 November 2017. The main purpose is to implement the provisions of FEA by the CBSL of Sri Lanka as the agent of the government, in order to ensure proper promotion and regulation of foreign exchange in Sri Lanka.

In discharging the functions entrusted to the department, DFE authorises persons i.e., Authorised Dealers (ADs), Restricted Dealers (RDs) and other persons prescribed by the Minister, to deal in foreign exchange in terms of FEA, facilitate issuance of Regulations, Orders and Directions pertaining to foreign exchange operations with necessary approvals, monitor the compliance with such Regulations, Orders and Directions by respective authorised persons and conduct investigations on non-compliances with the provisions of FEA.

Accordingly, DFE is organised under three divisions namely, Policy and Research Division, Capital Transactions Division and Statistics, Monitoring and Investigation Division in order to perform the following main functions in an efficient and effective manner. The main activities carried out by DFE during 2018 are summarised below.

12.1 Reviewing the FEA and the Regulations, Directions and Orders issued thereunder in 2017, facilitating the issuance of Government Gazettes and issuing new Regulations, Directions and Orders

a) Reviewing the FEA and the Regulations, Directions and Orders issued thereunder in 2017

DFE has continuously reviewed and identified the gaps between the provisions of repealed Exchange Control Act and FEA while further simplifying processes and procedures involved with deal in foreign exchange transactions and submitted such recommendations to the GOSL on necessary amendments to be made to FEA including provisions for carrying out investigations and enforceable sanctions to combat unauthorised activities involving foreign exchange such as illegal possession, transfers and exchange of foreign exchange within Sri Lanka, which may lead to unnecessary foreign exchange outflows from the country and currency smuggling.

The Regulations, Orders and Directions issued under FEA in 2017 were reviewed mainly to incorporate feedback received from the stakeholders focusing on further simplification and improving clarity on such Regulations, Orders and Directions.

b) Facilitating the issuance of Government Gazette Notifications

DFE facilitated the issuance of the Gazette Notification No. 2063/12 dated 19 March 2018, which permits the government to issue International Sovereign Bonds in 2018 and to make any payments in relation to such issuance, for non-resident investors. The Gazette Notification is given in Part III of this Report.

c) Issuance of Directions to ADs

Two Directions issued to ADs during 2018 under the FEA are given in Part III of this Report and a summary is given below.

- (i) Directions No. 01 of 2018: Along with several measures introduced by the CBSL of Sri Lanka to curtail imports to reduce adverse impact on the exchange rate, ADs were informed not to release foreign exchange to importers of goods which involves the conversion of Sri Lankan rupees for making payments for the importation of certain non-essential consumer goods under the advance payment (Cash-in-advance) terms, until further notice.
- (ii) Directions No. 02 of 2018: ADs were permitted to facilitate transactions related to investments by Foreign Institutional Investors via an account maintained in Sri Lanka by a Non-Resident Intermediary.

12.2 Granting of Permission for Foreign Exchange Transactions

- a) Special Permissions were granted under the FEA as illustrated in Table II-19 below.

Table II-19
Special Permissions granted under the FEA

| Purpose | No. of approvals | Value in USD million |
|--|------------------|----------------------|
| Government of Sri Lanka (GOSL) to issue a Sovereign guarantee | 1 | 58.19 |
| GOSL to borrow from abroad | 8 | 1,272.64 |
| Resident Companies to invest abroad | 6 | 44.17 |
| Resident Companies to borrow from abroad | 3 | 2,001.69 |
| Resident Companies to issue bank/corporate guarantees in favor of residents outside Sri Lanka | 5 | 41.45 |
| ADs to open and maintain Special Foreign Currency Accounts | 42 | N/A |
| ADs to process certain miscellaneous foreign exchange transactions that are not covered from the general permissions granted under FEA | 283 | N/A |

b) Granting of Permission to RDs, other than for money changing business

During the year, MMBL Money Transfer (Pvt) Ltd. (MMBL) and the Sri Lanka Export Credit Insurance Corporation (SLECIC) were authorised as RDs to deal in foreign exchange within Sri Lanka in terms of Section 4 of the FEA. MMBL was authorised to make outward remittances of salaries of expatriate employees to their beneficiaries abroad subject to a maximum limit of US dollars 500 per person per month, through Western Union Money Transfer System. SLECIC was authorised to issue Pre/Post Shipment Credit Guarantees in foreign currency to ADs on account of local exporters.

c) Issuance of permits for RDs to engage in money changing business and cessation/discontinuation of such operations

- (i) Five new permits were issued in 2018 to two limited companies (i.e., money changers) for buying and exchanging foreign currency, two tourist hotels for buying foreign currency and to one Licensed Finance Company for buying, selling and exchanging foreign currency.
- (ii) Approval was granted to three existing money changers to open three new branches.

- (iii) One money changer totally ceased its operations during 2018, while two other money changers discontinued their operations in two branches.
- (iv) The position of permits that have been issued to each RD to engage in the money changing business is illustrated in Table II-20 below.

Table II-20
Permits issued to RDs to engage in money changing businesses

| Category of Institution | Permitted business | No. of permits issued |
|--|---|-----------------------|
| Limited Companies who are solely engaged in the money changing business (money changers) | Buying and exchanging foreign currency | 58* |
| | Buying, selling and exchanging foreign currency | |
| Licensed Finance Companies | Buying, selling and exchanging foreign currency | 09 |
| Tourist Hotels | Buying foreign currency | 05 |
| Total | | 72 |

* Permits were issued to 58 companies which include 67 money changing outlets / branches. Out of those 67 outlets, 55 were permitted to buy and exchange foreign currency while remaining 12 were permitted to buy, sell and exchange foreign currency.

Accordingly, as at 31 December 2018, 28 ADs and 74 RDs, including MMBL and SLECIC, were in operation and the list of ADs and RDs is included in Annex II-2 and II-3 respectively.

d) Transfer of Migrants' funds

During the year, ADs were permitted to open 2403 Capital Transaction Rupee Accounts (CTRAs) in order to release the migration allowance to Sri Lankan emigrants and to facilitate the outward remittances of inherited funds to non-nationals.

12.3 Monitoring and Surveillance/Investigations of Foreign Exchange Transactions

a) On-site Inspections

28 on-site inspections were conducted in order to ascertain the status of compliance of RDs in accordance with the terms and conditions stipulated in the respective permits issued to them.

b) Investigations

- (i) 209 investigations initiated under the provisions of the repealed Exchange Control Act, No. 24 of 1953 (ECA), on non-compliances with the foreign exchange regulations were pending at the beginning of 2018. In terms of Section 30(2)(b) of FEA, 52 investigations were

concluded following the due investigation procedure in terms of ECA and Rs. 2.56 million was transferred to the Consolidated Fund being penalties imposed against relevant parties of such investigations.

- (ii) The remaining 157 investigations lapsed by 19 May 2018, in accordance with Section 30(2)(b) of FEA. Most of the investigations were on non-compliances with the procedure set out in the general permissions with respect to the issuance and transfer of securities/shares, unauthorised payments made by residents to non-residents, non-compliances by ADs with Directions/Operating Instructions issued under ECA, violation of conditions in permits issued to Authorised Money Changers and unauthorised possession of foreign currencies.

- (iii) Further, 03 investigations were carried out under the provisions of the FEA and concluded during 2018.

- c) **In addition, law enforcement authorities were further assisted in litigation and juridical proceedings by providing expert evidences/ testimonies by the Department.**

12.4 Enhancing Awareness on Foreign Exchange Regulations

- a) Five awareness programmes/lectures on prevailing foreign exchange regulations were conducted for ADs in collaboration with the CBS of the CBSL and the Institute of Bankers of Sri Lanka. These programmes were conducted in order to enhance the knowledge of banks' staff on existing regulations enabling them to be competent and effectively engage in day to day foreign exchange operations and transactions while providing efficient customer service.
- b) Nine presentations/panel discussions and seminars were carried out to professional members/stakeholders and public in collaboration with the Professional Association of Bankers, the Ceylon Chamber of Commerce, the Income Tax Payer's Association, the Police Tourists Division, the Association of Accounting Technicians of Sri Lanka, the Bar Association of Sri Lanka and the Chartered Institute of Management Accountants on the provisions of the FEA and recent relaxations on FEA regulations.
- c) Four seminars/workshops were conducted in collaboration with Regional Office Management Department of the CBSL to bankers, money changers and other interested parties with a view to enhance the knowledge on recent relaxations of foreign exchange transactions.
- d) The official website of DFE (www.dfe.lk) was duly updated to enhance public awareness on foreign exchange regulations and DFE continued to provide clarifications for queries raised through e-mails, telephone calls and visits to the Department.

Annex II-2
List of Authorised Dealers (ADs) as at 31.12.2018

| Licensed Commercial Banks | |
|-----------------------------------|---|
| 1 | Amana Bank PLC |
| 2 | Axis Bank Ltd |
| 3 | Bank of Ceylon |
| 4 | Bank of China Ltd |
| 5 | Cargills Bank Ltd |
| 6 | Citibank, N.A. |
| 7 | Commercial Bank of Ceylon PLC |
| 8 | Deutsche Bank AG |
| 9 | DFCC Bank PLC |
| 10 | Habib Bank Ltd |
| 11 | Hatton National Bank PLC |
| 12 | ICICI Bank Ltd |
| 13 | Indian Bank |
| 14 | Indian Overseas Bank |
| 15 | MCB Bank Ltd |
| 16 | National Development Bank PLC |
| 17 | Nations Trust Bank PLC |
| 18 | Pan Asia Banking Corporation PLC |
| 19 | People's Bank |
| 20 | Public Bank Berhad |
| 21 | Sampath Bank PLC |
| 22 | Seylan Bank PLC |
| 23 | Standard Chartered Bank |
| 24 | State Bank of India |
| 25 | The Hongkong & Shanghai Banking Corporation Ltd |
| 26 | Union Bank of Colombo PLC |
| Licensed Specialised Banks | |
| 27 | National Savings Bank |
| 28 | Sanasa Development Bank PLC |

Annex II-3
List of Restricted Dealers (RDs) as at 31.12.2018

| RDs permitted to buy and exchange foreign currency | |
|---|----------------------------------|
| Money Changers | |
| 1 | A.O.Lakshmi Jewels (Pvt) Ltd |
| 2 | Abdeen Money Changers (Pvt) Ltd |
| 3 | Ariyawansa Enterprises (Pvt) Ltd |
| 4 | Aruna Forexc (Pvt) Ltd |
| 5 | Asian Money Exchange (Pvt) Ltd |
| 6 | Brescia Grameen (Pvt) Ltd |
| 7 | Bullion Money Exchange (Pvt) Ltd |
| 8 | Capital Exchange (Pvt) Ltd |
| 9 | Carlo International (Pvt) Ltd |

| | |
|----|---|
| 10 | Colombo Money Exchange (Pvt) Ltd - Colombo 01 |
| 11 | Dadigama Group (Pvt) Ltd |
| 12 | Data Exchange International (Pvt) Ltd |
| 13 | Daya Authorized Money Changer (Pvt) Ltd |
| 14 | Delta Sarath Holdings (Pvt) Ltd |
| 15 | Galle Money Exchange (Pvt) Ltd |
| 16 | George Michael Holdings (Pvt) Ltd |
| 17 | Global Village Exchange (Pvt) Ltd |
| 18 | Golden Money Changers (Pvt) Ltd |
| 19 | International Exchange (Pvt) Ltd |
| 20 | Jayes Investments Ltd |
| 21 | Jewel Lanka Money Exchange (Pvt) Ltd |
| 22 | Kamal Enterprises (Pvt) Ltd |
| 23 | Keyser Exchange (Pvt) Ltd |
| 24 | Kudamadu Money Exchange (Pvt) Ltd |
| 25 | M.P. Money Changer (Pvt) Ltd |
| 26 | Majestic Jewellery (Pvt) Ltd |
| 27 | Maruthi Money Exchange (Pvt) Ltd - Jaffna |
| 28 | Mayurie Money Changers (Pvt) Ltd |
| 29 | Midna Mini Market (Pvt) Ltd |
| 30 | Milano Money Exchange (Pvt) Ltd |
| 31 | Monte Carlo Exchange (Pvt) Ltd |
| 32 | Narmatha Gold Centre (Pvt) Ltd |
| 33 | New Natasha (Pvt) Ltd |
| 34 | New Regal's Money Changer (Pvt) Ltd |
| 35 | Pearl Exci (Pvt) Ltd |
| 36 | Rafeek's Gems (Pvt) Ltd |
| 37 | Rimha Jewellery (Pvt) Ltd |
| 38 | Rivindu Enterprises (Pvt) Ltd |
| 39 | Royal Money Exchange (Pvt) Ltd - Colombo 01 |
| 40 | Royal Money Exchange (Pvt) Ltd - Colombo 06 |
| 41 | Royal Money Mart (Pvt) Ltd - Aluthgama |
| 42 | Royal Money Mart (Pvt) Ltd - Colombo 01 |
| 43 | Salaka Trust Investment (Pvt) Ltd |
| 44 | Sharanga Money Exchange (Pvt) Ltd |
| 45 | Shifaz Money Exchange (Pvt) Ltd |
| 46 | S S D D Money Exchanging (Pvt) Ltd |
| 47 | Swiss Money Exchange (Pvt) Ltd - Colombo 01 |
| 48 | Swiss Money Exchange (Pvt) Ltd - Colombo 06 |
| 49 | Thomas Cook Lanka (Pvt) Ltd - Colombo 03 |
| 50 | Thomas Cook Lanka (Pvt) Ltd - Kandy |
| 51 | Thomas Cook Lanka (Pvt) Ltd - Galle |
| 52 | Unic Forex (Pvt) Ltd |
| 53 | Vasanthas Intl. Money Exchange (Pvt) Ltd |
| 54 | Western Money Exchange (Pvt) Ltd |
| 55 | Windsor Money Exchange (Pvt) Ltd |

| RDs permitted to buy, sell and exchange foreign currency | |
|--|--|
| Money Changers | |
| 56 | Arrujina Jewellery (Pvt) Ltd |
| 57 | Colombo Money Exchange (Pvt) Ltd - Colombo 06 |
| 58 | Crown Money Exchange (Pvt) Ltd |
| 59 | City Exchange (Pvt) Ltd |
| 60 | Devi Forex (Pvt) Ltd |
| 61 | Maruthi Money Exchange (Pvt) Ltd - Colombo 06 |
| 62 | Metro Forex (Pvt) Ltd |
| 63 | Prasanna Money Exchange (Pvt) Ltd - Colombo 01 |
| 64 | Prasanna Money Exchange (Pvt) Ltd - Colombo 06 |
| 65 | Pushpa Money Changer (Pvt) Ltd |
| 66 | Ravi Forexae (Pvt) Ltd |
| 67 | Thomas Cook Lanka (Pvt) Ltd - Bandaranaike International Airport |
| Licensed Finance Companies | |
| 68 | Asia Asset Finance PLC |
| 69 | Bimpuh Finance PLC |
| 70 | Citizens Development Business Finance PLC |
| 71 | Lanka Credit and Business Finance Ltd |
| 72 | LOLC Finance PLC |
| 73 | L B Finance PLC |
| 74 | Senkadagala Finance PLC |
| 75 | Sinhaputhra Finance PLC |
| 76 | Singer Finance (Lanka) PLC |
| RDs permitted to buy foreign currency | |
| Tourist Hotels | |
| 77 | Mandarina Colombo |
| 78 | Pearl City Hotel |
| 79 | Shangri-La Hotel Colombo |
| 80 | Shangri-La's Hambantota Resort & Spa |
| 81 | Sigiriya Jungles |
| Other Entities | |
| 82 | MMBL Money Transfer (Pvt) Ltd. |
| 83 | Sri Lanka Export Credit Insurance Corporation |

13. HUMAN RESOURCES

Human Resources Department (HRD) undertook various activities in 2018 such as developing a new human resources management policy, performance evaluation, job rotation, succession planning, granting class and grade promotions and maintaining industrial harmony to create a conducive environment to maintain better employer-employee relations. These activities are aimed at ensuring the availability of a highly productive, motivated and contented team of employees who could contribute towards the achievement of the CBSL objectives. The structure of the human resources of the CBSL

with a summary of activities carried out by HRD during the year 2018 are given below.

13.1 Human Resources Structure

As at the end of 2018, the total number of staff of the CBSL was 1,421 consisting of 686 Staff Class (SC) officers, 576 Management Assistant Class (MAC) officers and 159 Office Assistant Class (OAC) employees. The percentage compositions of SC and MAC slightly changed, while that of OAC remained unchanged when compared to that of the previous year. The average age of an employee of the CBSL was 39 years at the end of 2018. The class-wise, gender-wise and age-wise composition of the staff as at the end of 2018 is shown in Chart II-4.

13.2 Educational and Professional Qualifications of the Employees

As indicated in Table II -21 below, the CBSL owns a diverse and talented pool of human resources with high level of academic and professional qualifications.

13.3 Human Resource Management

(a) Recruitments

In 2018, steps were taken to recruit 30 Management Trainees, 21 Assistant Security Officers (Trainee) and 12 Junior Personal Assistants under the general recruitment process and a Chief Librarian and 10 Legal Officers under the lateral recruitment process in order to fill the specific competency requirements of the CBSL. In addition, actions were taken to call applications for the posts of Curator, Maintenance and Project Engineer (Civil/ Electrical/ Mechanical), Technical Officer (Civil/ Electrical/ Mechanical) and Technician (Telephone cum Audiovisual).

(b) Performance Management

The Performance Management system of the CBSL includes preparation and review of job descriptions of employees, setting goals for individual employees, monitoring of employee performance and evaluation of performance.

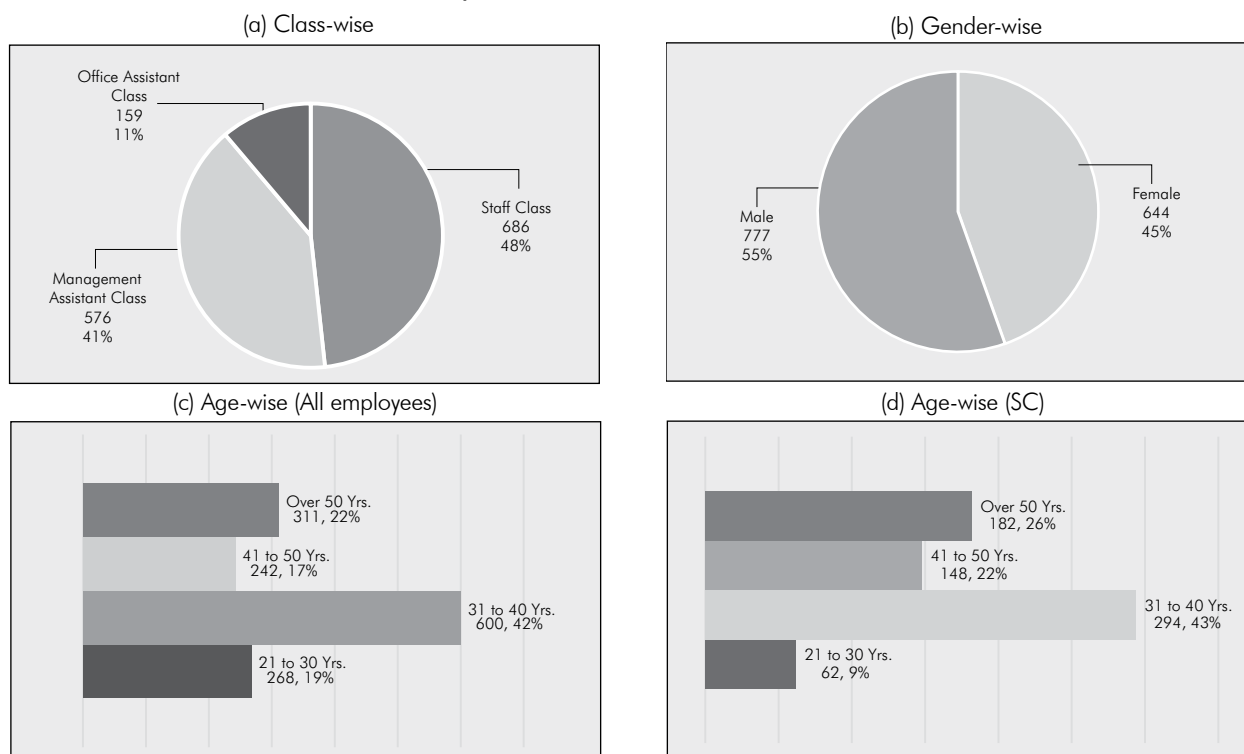
Under the performance evaluation process, the level of performance of each employee is evaluated by assigning ratings for the performance achieved based on the generic and technical competencies as specified in the evaluation criteria. The final performance marks of employees are used as one of the requirements in the promotion criteria.

HRD carried out the employee performance evaluation process as planned during the year. Further, HRD reviewed the mid-year performance review process of the departments. It provided an opportunity to understand the level of performance of the staff members during the first half of the year to the relevant parties.

(c) Promotions

In line with the applicable promotion criteria, HRD made necessary arrangements to grant promotions for the employees ensuring their career progression, and thereby, a total of 216 staff members were granted their class and grade promotions in 2018. On this basis, 2 Assistant Governors were promoted as Deputy Governors. Further, 44 Staff Class Grade III (1) officers were promoted

Chart II-4
Composition of the Staff as at 31.12.2018



as Deputy Heads of Department, 10 Staff Class Grade III (2) officers were promoted as Additional Heads of Department, and 120 officers were granted their grade promotions while promoting 38 officers to SC from MAC.

(d) Job Rotation

With a view of providing opportunities for employees to groom themselves in several areas of experiences of the operations of the CBSL, HRD has taken actions to transfer 6 SC officers, 9 MAC officers and 3 OAC officers with effect from 15 February 2018 under the Annual Job Rotation Policy of the CBSL.

(e) Industrial Harmony

HRD continued to perform its role as the facilitator for

maintaining a closer dialogue between the Management and Trade Unions. Accordingly, 12 discussions were arranged in 2018, giving the opportunity to the Management and Trade Unions to resolve some of the issues relating to remuneration, promotions, training, welfare, recruitment and general administration of the CBSL.

13.4 Closing down and Establishment of Departments

In accordance with the provisions of Section 33 of the MLA No. 58 of 1949 and as per the Monetary Board decision made at its Meeting No. 21/2017 held on 16 June 2017, the Resolution and Enforcement Department was established with effect from 01 January 2018.

Table II-21
Educational Qualifications/ Professional Memberships of Employees of the CBSL
As at 31.12.2018

| Employee Class | PhD Holders | Masters Degree, First Degree and Professional Membership Holders | | | | | | | |
|----------------|-------------|--|--|---------------------------------------|---|---|--------------|-------------------|-------------------------------|
| | | Categories | Masters Degree, First Degree & Professional Membership Holders | Masters Degree & First Degree Holders | First Degree & Professional Memberships Holders | Masters Degree & Professional Memberships Holders | Masters only | First Degree only | Professional Memberships only |
| | | Total | | | | | | | |
| SC | 20 | 546 | 124 | 180 | 64 | 28 | 1 | 134 | 15 |
| MAC | - | 148 | 9 | 23 | 11 | 12 | 10 | 52 | 31 |
| OAC | - | 7 | - | - | - | - | - | 7 | - |
| Total | 20 | 701 | 133 | 203 | 75 | 40 | 11 | 193 | 46 |

13.5 Overseas Meetings attended by the Governor during the year 2018

- (i) Attended the “Invest Sri Lanka Investor Forum” which was organized by the Colombo Stock Exchange (CSE) in association with the Securities and Exchange Commission of Sri Lanka (SEC) and the Singapore – Sri Lanka Business Association, to deliver a speech on Economic Outlook on 02 March 2018 in Singapore.
- (ii) Attended the IMF/World Bank Spring Meetings 2018 in Washington, D. C. from 18 – 22 April 2018.
- (iii) Travelled to The People’s Republic of China to head a delegation from the CBSL to meet officials of China Development Bank (CDB), Asian Infrastructure Investment Bank (AIIB), People’s Bank of China (PBC) and China International Capital Corporation (CICC) from 15 – 18 July 2018.
- (iv) Attended the meeting with senior bank officials in The Sultanate of Oman, Qatar and United Arab Emirates, as the head of a delegation of senior banking sector officials from Sri Lanka from 9 – 13 September 2018.
- (v) Attended the Financial Action Task Force (FATF) Plenary and Working Group Meetings in Paris from 15 – 16 October 2018.

13.6 Promotions/Appointments

- (i) Mr. S R Attygalle, Assistant Governor, who had been released to the Ministry of Finance as a Deputy Secretary was appointed as a Deputy Governor with effect from 31 October 2018.
- (ii) Mr. H A Karunaratne, Assistant Governor, was appointed as a Deputy Governor with effect from 31 October 2018.
- (iii) Mr. D A G K Wijetunga, Director of the Department of Supervision of Microfinance Institutions, was appointed as Director of the Training and Development Department with effect from 01 January 2018.
- (iv) Mr. S K Ranasinghe, Director of the Training and Development Department, was appointed as Director of the Resolution and Enforcement Department with effect from 01 January 2018.
- (v) Mr. V Baskaran, Additional Director of the Department of Supervision of Microfinance Institutions, was appointed as the Additional Director of the Department of Supervision of Non-Bank Financial Institutions with effect from 01 January 2018.
- (vi) Mr. A M Gunathilake, Additional Director of the Payments and Settlements Department, was appointed as the Additional Superintendent of the

Currency Department with effect from 17 January 2018.

- (vii) Mr. R M Jayawardena, Additional Director of the Payments and Settlements Department, was appointed as the Additional Director of the Facilities Management Department with effect from 01 June 2018.
- (viii) Mr. A G U Thilakarathna, Additional Superintendent of the Employees’ Provident Fund Department, was appointed as the Additional Superintendent of the Currency Department with effect from 01 June 2018.
- (ix) Mr. C P S Bandara, Additional Superintendent of the Public Debt Department, was appointed as the Additional Director of the Payments and Settlements Department with effect from 01 June 2018.
- (x) Dr. P K G Harischandra, Additional Director who had been released to the Ministry of Finance, was appointed as the Additional Director of the Economic Research Department with effect from 01 June 2018.
- (xi) Mrs. K Dassanayake, Director of the Risk Management Department, was appointed as the Secretary of the Central Bank of Sri Lanka with effect from 19 July 2018.
- (xii) Dr (Mrs). R A Perera, Additional Director of the Bank Supervision Department, was appointed as the Acting Director of the Risk Management Department with effect from 19 July 2018.
- (xiii) Mr. C A Abeysinghe, Additional Director of the Domestic Operations Department, was appointed as the Acting Director of the Domestic Operations Department with effect from 17 August 2018.
- (xiv) Mr. M R M Abeyratne, Additional Director of the Bank Supervision Department, was appointed as the Additional Director of the Resolution and Enforcement Department with effect from 03 September 2018 and subsequently, he was appointed as the Additional Director of the Training and Development Department with effect from 20 October 2018. Thereafter, he was appointed as the Acting Director of the Training and Development Department with effect from 23 November 2018.
- (xv) Dr. H Amarathunga, Director (Special Projects) attached to the Governor’s Secretariat, was appointed as the Director of the Regional Office Monitoring Department with effect from 20 October 2018.
- (xvi) Mr. B L J S Balasooriya, Director of the Regional Office Monitoring Department, was appointed as the Director of the Resolution and Enforcement Department with effect from 20 October 2018.

(xvii) Mr. W R M K Fernando, Acting Additional Director of the Risk Management Department, was appointed as the Acting Additional Director of the Resolution and Enforcement Department with effect from 29 October 2018.

(xviii) Mrs. W A Dilrukshini, Additional Director of the Economic Research Department, was appointed as the Additional Director of the Macprudential Surveillance Department with effect from 16 November 2018.

(xix) Mr. R R Jayaratne, Additional Director of the Department of Foreign Exchange, was appointed as the Acting Director of the Department of Foreign Exchange with effect from 01 December 2018.

13.7 Officers on Release

- (i) Mr. K M M Siriwardana, Assistant Governor, to the IMF as Alternate Executive Director
- (ii) Mrs. S Ratnayake, Staff Class Grade II officer, to the IMF as an Administrative Assistant
- (iii) Ms. S Amitha, Staff Class Grade II officer, to the IMF Resident Representative Office in Sri Lanka.

13.8 Retirements

- (i) Mr. D K Wijesuriya, Additional Director of the Financial Intelligence Unit, retired from the CBSL service with effect from 01 January 2018.
- (ii) Mr. M I Sufiyan, Chief Accountant, retired from the CBSL service with effect from 18 February 2018.
- (iii) Mr. V Baskaran, Additional Director of the Department of Supervision of Non-Bank Financial Institutions, retired from the CBSL service with effect from 10 May 2018.
- (iv) Miss. K G R K Dheerasinghe, Acting Additional Director of the Staff Services Management Department, retired from the CBSL service with effect from 01 September 2018.
- (v) Mr. H M Wimal, Acting Additional Secretary of the Secretariat Department retired from the CBSL service with effect from 16 September 2018.
- (vi) Mr. B W Jinasena, Secretary of the CBSL, retired from the CBSL service with effect from 19 October 2018.
- (vii) Mr. C J P Siriwardana, Deputy Governor, retired from the CBSL service with effect from 31 October 2018.
- (viii) Mr. P W D N R Rodrigo, Director of the Domestic Operations Department, retired from the CBSL service with effect from 17 November 2018.

(ix) Mr. R D W Pallegama, Acting Additional Director of the Department of Supervision of Non-Bank Financial Institutions, retired from the CBSL service with effect from 03 December 2018.

(x) Mr. K D R Piyatilleke, Additional Director of the Facilities Management Department, retired from the CBSL service with effect from 31 December 2018.

14. INFORMATION TECHNOLOGY

The Information Technology Department (ITD) continued its dynamic role of providing enterprise level integrated applications to achieve the core objectives of the CBSL.

During the year ITD made its contribution under five major areas, namely, (a) Delivering cost-effective business solutions; (b) Continuous enhancements of the IT infrastructure of the CBSL; (c) Contribution to establish national payment system infrastructure; (d) IT security and resilience; and (e) Upgrade ICT competencies among the staff under strategic and operational activities of the CBSL.

(a) Delivering cost-effective business solutions

A Budget Information Submission and Processing System was implemented for the Finance Department to automate and streamline the Bank's annual budgeting process. A new web based auction system was developed for the primary issuance of Treasury Bills by the Public Debt Department. The Central Integrated Market Monitoring System (CIMM) was further enhanced with the addition of a new interface for the International Operations Department to get instant quotes thereby facilitating real-time CBSL interventions in the inter-bank forex market. In addition, a new interface was developed in CIMM System for the Economic Research Department to automate the compilation of existing interest rates (SLIBOR, AWLR, AWDR).

The Central Database System (FinNet) used by several departments to monitor information reported by the financial institutions regulated by the CBSL was enhanced with the introduction of new regulatory returns. The ForexNet System used by the Department of Foreign Exchange was further enhanced with the revamping of the Foreign Currency Sales and Purchases Monitoring Module. The Inward Investment Account (IIA) inflows and outflows monitoring system was also upgraded fulfilling the requirements of the new FEA.

The management of Monetary Board decisions and subsequent review and status monitoring of related actions were made easier with the development of the Task Tracker System. The Holiday Homes Booking System was developed for the Facilities Management Department enabling the CBSL staff to reserve rooms online and utilise the holiday home facility with ease.

The LankaSettle System, which is the National Payments and Settlement System, was enhanced to comply with the best practices to maintain transparency in the government securities market for the protection of investors, by introducing an e-mail and SMS alert facility for securities movements settled in the System. In addition, the LankaSettle System was enhanced to capture the price and yield of primary and secondary market transactions of Government securities, to improve the price discovery mechanism.

Using an IT based solution, over one million National Identity Card numbers were updated in the EPF member register.

(b) Continuous enhancements of the ICT infrastructure

ITD continued to enhance the ICT infrastructure of the CBSL during the year 2018, in order to strengthen the resilience of information systems while keeping in par with the latest advancements in technology.

Firewalls function as a critical line of defense against cyber-attacks and insider threats. Firewalls in both the internal perimeter and the external perimeter of the corporate network were replaced with new state-of-the-art firewalls.

CBSLNet, which is the Virtual Private Network (VPN) that connects Participant Institutions to the CBSL Primary Site and Disaster Recovery (DR) Site to access business critical systems, was enhanced by implementing dual connectivity through two Telecommunication Service Providers to establish failover and high availability in the VPN. Further, to enhance the security of the network, end to end encryption was enforced over the VPN.

An SMS gateway, which allows the sending or receiving Short Message Service (SMS) transmissions to or from a telecommunications network, was implemented. It facilitates to send SMS alerts by the LankaSettle System to beneficial owners for securities movements that credits or debits their accounts. This SMS gateway will provide the facility for any other system that may need similar services in the future.

(c) Contribution to establish national payment system infrastructure

ITD continued to function as an advisor and a provider of technical expertise for projects of national interest. ITD Officials contributed their expertise to several national projects during the year.

An important national project set in motion is the establishment of an Electronic Trading Platform with a Central Counter Party System to strengthen the Financial Market Infrastructure. ITD officers served in the Technical Evaluation Committee (TEC) appointed for the selection of a suitable consultant for the project implementation.

In addition, ITD officials contributed to two committees appointed by the National Payment Council (NPC), the Committee on Fintech Developments and Committee on Blockchain Technology.

ITD officials provided technical expertise to the Payments and Settlements Department (PSD) to carry out onsite examinations on Dialog eZ cash and Mobitel mCash Systems. ITD officials also assisted the Department of Supervision of Non-Bank Financial Institutions to perform regulatory actions on some financial institutions.

(d) Strengthening IT security and resilience

ITD took several measures to enhance IT Security and protect the Bank's IT assets from any cyber security threats. As a proactive approach, continuous vulnerability assessments were carried out on business-critical IT systems to identify vulnerabilities and necessary remediation actions were taken where necessary to mitigate them and reduce exposure to cyber-attacks.

ITD revised the CBSL's Information Security Policy (ISP) and published the ISP Version 4.0 which specifies the baseline security standards and procedures for the information security of the CBSL.

Social Engineering tests were carried out to identify potential vulnerabilities in the human network. In this regard, spam emails were sent to targeted users to check on their awareness and subsequent advice was provided on best practices to stay safe.

ITD played a major role to obtain compliance to the SWIFT Customer Security Program (CSP) which was mandatory by end December 2018.

A training session on cyber security was conducted for Departmental IT Liaison Officers (DLOs).

(e) Upgrade ICT competencies among the staff

With an aim to enhance the IT knowledge of all employees in the CBSL, ITD continued to publish awareness banners on the intranet and circulate security advisory alerts through email. Training programs on Internet and Email Technology were conducted for CBSL Office Assistants.

Further, in order to uplift the knowledge and skills in the relevant fields, the staff of ITD attended short term training both locally and abroad.

15. INTERNAL AUDIT

The internal audit function has been in operation in the CBSL since 1951. The mission, scope of work, accountability, independence, responsibility and the authority of the Director and the staff of the Internal Audit Department (IAD) have been included in the Internal Audit Charter approved by the Monetary Board. In conducting audits, global standards are followed. A summary of the activities carried out by the Department during 2018 is given below.

15.1 Internal Audit Plan

The Internal Audit Plan prepared for the year 2019 was reviewed by the Monetary Board Advisory Audit Committee (AAC) and approved by the Monetary Board.

15.2 Conduct of Audit Assignments

(a) Process and Information Systems Audits

In 2018, process and information systems audits were conducted as per the internal audit plan. Each audit engagement was carried out in four sequential steps, i.e., planning, performing, communicating audit results and taking resolution actions. The four step process, which was followed for the communication of audit results; conduct of closing conference with Auditee department to get audit observations validated, issuing of observation communication memo, issuing of draft audit report and issuing of final report, was changed into a three step process by eliminating the observation communication memo as recommended by the AAC and approved by the Monetary Board during the year. Implementation of audit recommendations by process owners was also followed-up during the year on a quarterly basis.

b) Conduct of Spot Audits

Spot audits were also conducted in 2018 as required and audit results were communicated to the process owners and other stakeholders.

c) Special Assignments

A spot check on files/documents related to investments in equities and government securities (2002 - end 2016) of EPF Department was carried out by IAD to facilitate forensic audits as per the instructions of the Monetary Board.

d) Reporting the Progress of the Conduct of Audits

Progress of the conduct of audit assignments was reported to the AAC and the Monetary Board, quarterly. Activity reports were submitted to the Auditor General on half-yearly basis.

15.3 Awareness Programmes and Provisioning of Training

IAD conducted a presentation for the Audit Coordinating Officers on the 'Internal Audit Facilitation Guidelines'. Further, as per the request of the Human Resources Department, IAD continued to provide training on internal audit and related disciplines to undergraduates during the year.

15.4 Facilitation to the Monetary Board Advisory Audit Committee

AAC is a sub-committee appointed by the Monetary Board which advises the Monetary Board on financial reporting, internal controls, risk management systems, compliance, whistleblowing, fraud, internal audit, external audit and any other matter assigned by the Monetary Board. Secretary to the Monetary Board is the Secretary to the AAC. Director of IAD functions as the Assistant Secretary to the AAC. Accordingly, IAD provided secretarial facilitation to the AAC during the year.

16. INTERNATIONAL OPERATIONS

In terms of the Monetary Law Act (MLA), the CBSL is responsible for managing the official foreign exchange reserves of the country. In this regard, the International Operations Department (IOD) has been entrusted to perform the function of management of foreign exchange reserves and the monitoring of domestic foreign exchange market activities to ensure its smooth operation.

The MLA provides the necessary legal framework for international reserves management, covering areas on the maintenance and composition of international reserves, actions to preserve the international stability of the rupee, scope of foreign exchange operations of the CBSL and the powers and responsibilities of the Monetary Board pertaining to international reserves management activities. In this aspect, Section 67 of the MLA deals with the parameters in respect of asset types, counterparties, instruments and issuers. The Monetary Board may also direct to further widen the scope of reserves management activities to enhance the safety, liquidity and return objectives of reserves management.

16.1 International Reserves Management

Investments of international reserves are undertaken in accordance with the Foreign Reserves Management Guidelines as amended and approved by the Monetary Board, under the supervision of the Foreign Reserves Management Committee (FRMC) taking into consideration the safety, liquidity and return objectives. The international reserves are denominated in several key currencies and are mainly invested in Fixed Income Securities (FIS), Money Market Investments and Gold. The FIS portfolio consists of highly rated government securities, government guaranteed securities, securities of government agencies and supranational institutions. Transactions undertaken by IOD for reserve management purposes, are performed with central banks, highly rated commercial banks and investment houses, which are counterparties approved by FRMC as per the parameters stipulated in the Counterparty Credit Risk Management System (CCRMS) subject to the necessary limit allocations by the Risk Management Department, paying due consideration to the strength and creditworthiness of each counterparty.

Since 2016, CBSL is involved with the Reserve Advisory and Management Programme (RAMP) of the World Bank which provides advisory services and training to official sector investment managers enabling efficient management of foreign currency reserves and other investment portfolios. Accordingly, a new model based Strategic Asset Allocation (SAA) was formulated based on the liability structure of the CBSL which mainly considered the objectives of capital preservation, liquidity requirements, income generation and the risk tolerance of the CBSL. As such, since 2016, the CBSL foreign reserves were objectively divided into three main tranches which comprise of different portfolios and are

assigned with an investment horizon, currency composition and an asset composition. Each portfolio defined under those tranches are assigned with international benchmarks. Accordingly, the performance of the portfolios is reviewed against the respective benchmarks in order to be in line with the globally accepted best practices of performance reviewing.

Under the RAMP, the World Bank Treasury was also appointed as an external manager for CBSL reserve management by allocating US dollars 200 million out of the foreign reserves with a pre-defined mandate with an investment horizon of three years.

During 2018, two missions for technical assistance on foreign reserves management were facilitated as in-house trainings in CBSL with the assistance of World Bank technical experts. These missions focused on risk budgeting for foreign reserves and technical assistance on portfolio management and risk management.

16.2 Performance Analysis and Facilitation Activities

Under Performance Analysis and Facilitation, the following main functions relating to the CBSL's reserves management are conducted.

(a) Performance Measurement

IOD daily assesses performance of its reserve management activities on a total return approach and presents monthly to the FRMC, and quarterly to the Monetary Board, together with an analysis of reserve position. The returns of FIS and MM investments are measured against respective benchmarks according to the SAA approved by the Monetary Board. Comparison against benchmarks helps to determine the effectiveness of the Active reserves management strategy by measuring the excess returns generated over the benchmarks. This approach is useful in identifying whether the return objective of management of reserves is achieved to a reasonable extent by investing within the approved guidelines. Performance attribution was introduced in 2018 to further elaborate total returns generated through foreign reserves management. This process helps to evaluate the performance of the portfolios by measuring returns generated by various sources of risk factors, and the resulting findings are used as value adding inputs in the CBSL's foreign reserve management strategy.

(b) Administration of Treasury Management System (TMS)

IOD, the main user of the TMS, is responsible for the general administration function of the system and ensures a proper coordination among other user Departments, the software provider and its local partner. Accordingly, IOD ensures that the TMS is updated with relevant modifications/ patches and is fully connected with internal systems such as Society for Worldwide Interbank Financial Telecommunications (SWIFT), Real Time Gross Settlement (RTGS) and General Ledger (GL) as well as external interfaces such as Bloomberg

and Reuters to ensure efficient functioning of TMS related procedures and processes.

(c) Monitoring of Non-Financial Risks

IOD identifies the non-financial risk profile relating to the reserves management activities and proposes relevant risk mitigation actions to the Non-Financial Risk Management Committee (NFRMC) on a quarterly basis.

(d) Annual review of existing counterparties for their adherence/compliance to Anti Money Laundering (AML) and Combating Financing of Terrorism (CFT)

During 2018, IOD carried out its "Know Your Customer (KYC)/ Customer Due Diligence (CDD) rules for the Central Bank of Sri Lanka for the foreign counterparties" to ensure compliance with rules and regulations and international best practices in relation to AML and CFT with regard to management of foreign reserves.

16.3 Domestic Foreign Exchange Market Developments

During the year, IOD made continuous efforts to ensure smooth operations in the domestic foreign exchange market, allowing more flexibility while curbing excess volatility in the exchange rate.

(a) Intervention to Domestic Foreign Exchange (FX) Market

The CBSL continued to intervene in the domestic FX market, as and when required during 2018 in order to curtail the excessive volatility of the exchange rate. In doing so, a new volatility based intervention framework executable through a transparent mechanism named "Request for Quote" (RFQ) was implemented by the CBSL from July 2018 onwards. This new mechanism enhanced market transparency as it necessitated LCBs to bid competitively by providing two-way quotes when the CBSL enters the market for foreign exchange interventions (on both selling and buying sides) to manage excess volatility in the exchange rate.

(b) New Monitoring System

As a step forward, in developing the domestic foreign exchange market, IOD introduced a new integrated market monitoring system named "Central Integrated Market Monitor" (CIMM) for real time reporting and monitoring of interbank FX transactions, at the beginning of the year. Further, in order to enhance the transparency and competition among LCBs, IOD commenced publishing the details of the last five outright trades, traded in the interbank SPOT market on real time basis on CIMM screen for LCBs and Authorised Money Brokers (AMBs) enabling them to trade in the foreign exchange market with a better knowledge of market movements.

(c) Dissemination of Information

IOD continued to publish USD/LKR indicative exchange rate along with indicative exchange rates for fifty six world currencies and average buying and selling exchange rates of nine major currencies against LKR provided by LCBs

for Telegraphic Transfers (TT) on the CBSL website on daily basis. In addition, IOD discharged its duties on the dissemination of information by providing exchange rate data to government organisations and various other parties, including the general public, at their request.

(d) Revision to Net Open Position (NOP)

With a view to support foreign exchange market developments, the NOP limits applicable to foreign exchange operations of the Licensed Banks (LBs) were revised in May and October 2018.

(e) Affiliation with Market Participants

IOD conducted several meetings with LCBs, AMBs, major importers and exporters in order to discuss their concerns with regard to the stress situation in the market and initiated several measures to overcome such issues with a view to streamline the FX market operations. Further, IOD continued to conduct Treasures' meetings with LCBs on a quarterly basis to share information and to discuss issues relating to domestic foreign exchange operations. While doing so, IOD commenced supervision of LCBs and AMBs with regard to foreign exchange trading as and when required and took necessary actions in order to ensure market participants' adherence to the global standards.

(f) Observation on Market Sentiments

Throughout the year 2018, as a key department responsible for monitoring the domestic FX market activities, IOD provided its views, observations and recommendations for various proposals, regulations, amendments and policy matters submitted by other departments of the CBSL and external organizations, with regard to the possible implications of such proposals on the exchange rate movements.

(g) Maintaining International Relations

IOD closely worked with the IMF staff missions that visited Sri Lanka to review the IMF – EFF and the South Asia Regional Training and Technical Assistance Center (SARTTAC) missions during the year and discharged the responsibility of regular data reporting requirements.

17. LEGAL AND COMPLIANCE

Legal and Compliance Department (LCD) has been established with a view to enhance the level of compliance of the CBSL with all legal and procedural aspects in achieving its core statutory objectives. Currently, LCD is entrusted to develop new laws to enhance the regulatory and supervisory authority of the CBSL, to amend the existing laws administered by it, to enhance such authority, governance and accountability standards in relation to all functions performed by the CBSL and to formulate an effective compliance framework, within which the management takes appropriate corrective action when potential compliance breaches are identified. In this respect, LCD undertakes wide range of activities of the CBSL and to ensure timeliness of the legal and regulatory framework on par with the international

standards and best practices. LCD is also required to contribute to achieve the strategic priorities of the CBSL. While being actively involved in all strategic priorities of the CBSL, LCD carried out following major activities during 2018.

During the year, LCD engaged in the introduction of legal reforms to the statutes administered by the CBSL. Amendments were proposed to the MLA, No. 58 of 1949 to facilitate a FIT monetary policy framework, enhanced governance standards and macroprudential authority of the CBSL. The Registered Stock and Securities Ordinance, No. 7 of 1937 was reviewed to enhance the accountability and transparency requirements in the issuance of Treasury Bonds. Amendments were proposed to the Banking Act, No. 30 of 1988 to enhance the regulatory supervisory framework. Further, LCD contributed to introduce the Active Liability Management Act, No. 8 of 2018 as a new legal framework to facilitate active management of public debt. In order for the financial sector regulators to pursue their respective statutory objectives for a stable and robust financial system and to contribute to the enhanced macroprudential surveillance in the financial sector, LCD engaged in drafting the Sharing of Information among Financial Sector Regulators Bill which was approved by the Cabinet of Ministers and worked with the Legal Draftsman's Department to facilitate enactment of the Bill. Actions have been initiated to introduce amendments to the Debt Recovery (Special Provisions) Act, No. 2 of 1990 enabling all licensed banks under the Banking Act to receive benefit from the expeditious procedures provided therein to recover debts. All such activities were finally aimed at strengthening the financial system infrastructure.

When achieving its compliance objectives, LCD developed a Comprehensive Compliance Manual for the CBSL, which provided for a department-wise decentralised compliance framework to manage its legal, reputational and compliance risks. To strengthen the governance structures of the CBSL, a whistleblowing policy was introduced. Bridging a considerable gap in the governance framework, two codes of conduct were finalised for the members of the Monetary Board and the employees of the CBSL. Further, LCD took initiatives to assure that the CBSL has complied with the legal requirements provided for in the Right to Information Act, No. 12 of 2016 in association with the other departments.

LCD was responsible for handling litigation for which the Monetary Board, CBSL or its employees were parties, in consultation with the relevant authorities. In the year 2018, LCD initiated legal actions against certain financial institutions regulated by the CBSL and their directors. In relation to resolution measures initiated by the CBSL against some distressed financial institutions in 2018, LCD actively engaged with the supervisory departments in such deliberations and developed necessary legal instruments such as regulations, agreements, operational procedures etc., to effectively carry out such regulatory measures with a minimal legal risk.

Furthermore, in the pursuit of safeguarding the interests of the CBSL when dealing with internal and external parties, LCD engaged in vetting of agreements, to ensure that such instruments are in line with the legal requirements. LCD provided

legal advice on matters arising out of such agreements as and when necessary. In relation to the other operational activities of the CBSL, the opinion of LCD has always been sought by other departments of the CBSL to minimise the legal, compliance and operational risks in such activities.

In addition to above, during the year 2018, LCD represented several special committees established within the CBSL in respect of multiple subject matters pertaining to the activities of the CBSL.

During the year 2018, LCD as one of the key assurance functions, has successfully contributed to safeguard the legal interests of the CBSL and thereby to achieve its core objectives and strategic priorities.

18. MACROPRUDENTIAL SURVEILLANCE

Maintaining the financial system stability is one of the two statutory objectives of the CBSL. To achieve the financial system stability objective, the CBSL conducts microprudential supervision on a continuous basis. With the view of facilitating to achieve the same objective, the Macroprudential Surveillance Department (MSD) conducts a wide range of analysis on subsectors within the financial sector which complements microprudential supervision. In addition, MSD assesses the impact of broad macroeconomic factors on the domestic financial system and its stability. Financial sector surveillance is carried out using data reported by regulated financial institutes and the data collected through surveys conducted by MSD. The findings of such assessments contribute significantly to the financial sector policy making process of the CBSL. A summary of the main activities undertaken by MSD in 2018 is given below.

(a) Macroprudential Surveillance

MSD conducted macroprudential surveillance to identify systemic risks and/or buildup of systemic risks to the financial sector and to assess the ability of the financial system to withstand such risks. Said surveillance covered global and domestic macroeconomic developments, financial market activities and the risk exposures of financial institutions. MSD continued to compile a number of composite financial system stability indicators based on the stability and soundness of different sub sectors of the domestic financial system. In addition, the top-down macro stress testing for the banking sector was conducted to assess the impact of credit risk, interest rate risk, and foreign exchange risk on the level of capital of the banking system and also individual banks. Further, MSD continued to improve the stress testing model. Findings of these analyses were submitted to the Monetary Board in the quarterly Board Papers. In addition, MSD submitted a number of papers to the Monetary Board on contemporary concerns over Financial System Stability in 2018, including the impact of LTVs on vehicle imports, stickiness of Average Weighted Lending Rate (AWLR), high banking sector exposure on the construction sector and consumption loans and issues relating to the LFCs and SLC sector.

(b) Surveys and Data Collection

Systemic Risk Survey (SRS): MSD conducted the bi-annual Systemic Risk Survey which was initiated in 2017. The SRS is aimed at identifying market perceptions on the potential risks to the financial system stability. Findings of the survey was found important for policy making and regulatory purposes as it provides an opportunity to gauge confidence of stakeholders on financial system stability. Findings also provide policymakers a more futuristic view of emerging risks to the financial system and thereby help to prioritise risks to be dealt with. Systemic risks are found to be complex and measuring them with precision has been a challenging endeavor for MSD. However, the market perceptions gained through SRS provides reasonable insights to the stability of the financial system, and complements to macroprudential surveillance process.

Household Sector Creditworthiness Survey (HHCS): HHCS was initiated by MSD due to the increasing financial and social concerns on household sector indebtedness in Sri Lanka. The primary objective of HHCS is to establish a comprehensive data set on the household sector financial information that would enable assessment of debt servicing capacity of the households and its implications on the financial stability. In 2018, MSD collected required information on household sector and such information would be assessed to evaluate the magnitude and depth of the household sector dependence on formal and informal sources for their borrowings.

Data Collection: MSD continued to gather granular level data from several external parties to enrich its database. The Department continued to collect data regularly from external institutions such as the Colombo Stock Exchange, Department of Co-operative Development, Department of Labor, Department of Pensions, Employees' Trust Fund Board, Insurance Regulatory Commission of Sri Lanka, SANASA Federation, the Securities and Exchange Commission of Sri Lanka and the Unit Trust Association of Sri Lanka. In addition, MSD initiated to collect more granular level data from the Credit Information Bureau and Sri Lanka Customs to enrich its analysis.

(c) Publishing the FSSR and Contributing to Statutory Reports and Other Publications of the Central Bank

The Financial System Stability Review (FSSR) 2018: FSSR was published in December 2018. The purpose of this report is to disseminate a comprehensive risk assessment on financial institutions, markets and infrastructure. MSD will continuously endeavor to apprise the public on performance, associated risks, opportunities and regulatory developments of the nation's financial system on an annual basis. The FSSR 2018 contained three chapters titled on International and Domestic Developments Affecting Financial Stability; Financial Sector Development and Stability and Special Notes on significant new developments.

Other Publications: MSD coordinated and compiled the Chapter on “Financial Sector Developments and Stability” of the CBSL Annual Report 2017 and the “Recent Economic Developments 2018”, published by the CBSL. Further, the Department contributed to the Chapter on Financial Sector Developments in the September 15th Report which is submitted to the Minister in charge of Finance. These reports provide comprehensive analyses on financial institutions, financial markets and financial infrastructure of the country with particular emphasis on performance, risks and risk management, resource availability and regulatory developments pertaining to each area, together with an assessment of potential implications on the overall financial system stability of the country. The Department also contributed to other publications of the CBSL by way of compiling financial sector data and providing analysis on subsectors of the financial system.

(d) Coordination of the Committees on Financial System Stability

Financial System Stability Committee (FSSC): MSD served as the secretariat for the FSSC in 2018. The FSSC was reconstituted in 2017 and the first meeting was held on 17 May 2018. FSSC is an inter-departmental forum which represents 14 departments of the CBSL and their respective Assistant Governors and Deputy Governors. FSSC is a forum for the identification of risks affecting the financial sector, discussion of measures to mitigate risks and the co-ordination of efforts to promote financial system stability. Three FSSC meetings were held during 2018.

Financial System Stability Consultative Committee (FSSCC): The FSSCC members appointed by the Governor consists of key personnel from external sector institutes prominent in the Sri Lankan financial system and the current FSSCC comprises of seventeen members. FSSCC provides views and advice to the CBSL on financial sector issues, and held four meetings during the year. MSD provides the secretarial services to FSSCC.

19. PAYMENTS AND SETTLEMENTS

Payments and Settlements Department (PSD) was established in 2002 to discharge the responsibilities entrusted to the CBSL under Section 62A of the MLA which provides authority to the CBSL to establish and operate systems for the transfer of funds, settle payment obligations and issue system rules to participating institutions. In addition, with the enactment of the Payment and Settlement Systems Act, No. 28 of 2005, PSD was entrusted with regulating, supervising and monitoring payments, clearing and settlement systems and money service providers, and discharging other responsibilities entrusted to the CBSL under this Act.

Main functions carried out by PSD are operations of the RTGS System, providing back-office service for financial

transactions, management of the SWIFT Communication Network, facilitating transactions under the Asian Clearing Union (ACU), facilitating the development of the National Payment Switch and regulation and oversight of Payment and Settlement Systems. A summary of the functions performed during 2018 is given below:

19.1 Operations of the Real Time Gross Settlement System

- (a) PSD continued to operate the RTGS System, which settles time critical large value inter-participant payments as well as customer payments on real time gross basis, and to ensure the smooth functioning of the RTGS System, PSD facilitated and monitored the provisioning of the Intraday Liquidity Facility (ILF) to the Participating Institutions (PIs) which requested extra funds. PIs of the RTGS System are the CBSL, LCBs, standalone PDs, EPF and the Central Depository System of the Colombo Stock Exchange.
- (b) As at end 2018, the number of PIs of the RTGS System was 37. In 2018, the Bank of China Limited was admitted as a Participant of the LankaSettle System. During the year, the RTGS System settled 405,200 transactions with a total value of Rs. 100,473 billion. The average volume and value of RTGS transactions settled per day were 1,688 and Rs. 419 billion, respectively. With regard to ILF operations, on average, Rs. 55 billion per day was released to PIs. Adhering to international best practices, the LankaSettle System availability was maintained at a high level of 99.90 per cent during the year.

19.2 Providing Back-office service for financial transactions of the CBSL

(a) Back-office service for Foreign Exchange Transactions

During 2018, back-office services provided to facilitate international reserve management of the CBSL covered the following:

- i. Settled 11,626 transactions relating to foreign exchange trading and funding, money market, fixed income securities, gold trading, ACU and Repo/Reverse Repo amounting to US Dollars 342.3 billion during 2018.
- ii. PSD was involved in pre-testing the upgrade for the Treasury Management System (TMS) of the CBSL in 2018 in order to comply with the International SWIFT Standards.

(b) Back-office service for Open Market Operations

The settlement of open market operations related transactions with LCBs and PDs was carried out to facilitate the management of market liquidity. Accordingly, during

2018, PSD effected and facilitated 722 Repo transactions amounting to Rs. 1,125 billion, 3,049 Standing Deposit Facility transactions amounting to Rs.4,504 billion, 4,005 Standing Lending Facility transactions amounting to Rs.3,057 billion, 2,387 Reverse Repo transactions amounting to Rs.3,386 billion, 83 Outright Purchase transactions amounting to Rs. 40 billion and 38 Outright Sale transactions amounting to Rs. 64 billion.

19.3 Management of the SWIFT Communication Network

PSD continued to use the SWIFT platform for secure financial messaging, and manage the SWIFT system on behalf of all users of the CBSL. PSD maintains the system following the standards set by the SWIFT Head Quarters on software, hardware, processes, procedures and risk management controls. To maintain a robust connectivity and provide an efficient service, the CBSL maintains the connectivity to SWIFT-Net, via Lanka Financial Services Bureau Ltd.

In 2018, the CBSL has implemented the Relationship Management Application (RMA) Plus facility for the Business Identification Code (BIC) for CBCELKX. RMA Plus enables institutions to define which SWIFT FIN messages they want to send to and receive from each counterparty. Further, it provides additional granularity and control over correspondent relationships, by mitigating operational and compliance risk. The SWIFT System was upgraded to a new version (Version 7.2.50) in 2018. The aim of the new version was to continue to provide a highly secure and more efficient service for its users. Accordingly, the CBSL has successfully installed the new version and complied with the international standards of the facilities introduced by the SWIFT service. The CBSL also maintained the appropriate security level of SWIFT division throughout the year.

19.4 Facilitating Transactions under the Asian Clearing Union

PSD continued to facilitate the settlement of eligible trade and trade related transactions among member central banks of the ACU on a multilateral net basis during the year 2018. The total number of transactions effected through the ACU mechanism was 6,467 and the value of total transactions was Rs. 585.0 billion. The value of net settlements made under the ACU mechanism was Rs. 490.5 billion.

The preparatory Standing Technical Committee (STC) meeting was held in Colombo in April 2018 and the Secretary General of ACU and delegates of seven member central banks and monetary authorities had participated in this meeting. The 47th meeting of the Board of Directors and the STC meeting were held in Kathmandu, Nepal in June 2018. Relevant CBSL officials participated in the above meetings.

19.5 Facilitating the Development of the National Payment Switch

PSD continued to facilitate the implementation of sub switches of the Common Card and Payment Switch (CCAPS) operated by LankaClear (Pvt) Ltd. (LCPL) under the brand name of 'LankaPay'. CCAPS, which is designated as the National Payment Switch of the country, consists of five sub switches i.e. Common ATM Switch (CAS), Common Electronic Fund Transfer Switch (CEFTS), Shared ATM Switch (SAS), Common POS Switch (CPS) and Common Mobile Switch (CMobS). The progress of the implementation of CCAPS can be summarized as follows;

- (a) CAS, which is the first phase of CCAPS, started live operations in July 2013. At the end of 2018, membership of CAS increased to 28 institutions. During the year 2018, CAS settled 40 million transactions amounting to Rs. 344.6 billion.
- (b) CEFTS, which is the second phase of CCAPS, was implemented on 21 August 2015. CEFTS provides a common infrastructure to clear payments effected through multiple payment channels such as ATM, Internet Banking, Mobile Banking, Kiosks and over-the-counter. During 2018, 05 financial institutions integrated with CEFTS increasing the members of CEFTS to 38 institutions.
- (c) Lanka Pay Online Payment Platform (LPOPP) was launched on 20 July 2017 to facilitate real time payments to Sri Lanka Customs. At present, 08 LCBs had connected to LPOPP. During 2018, approval was granted to LCPL to integrate Ministry of Provincial Councils and Local Government, Board of Investment of Sri Lanka and Sri Lanka Ports Authority with LPOPP to facilitate online payments.
- (d) In order to streamline the interbank settlement process of transactions carried out through CAS and CEFTS, the number of clearing cycles in the RTGS System were increased to 4. Further, a Circular was issued to prescribe minimum liability limits for primary participants in CAS and CEFTS.
- (e) CPS, which is the fourth phase of CCAPS, will facilitate switching and clearing of domestic point-of-sale transactions. Accordingly, in order to ensure smooth operations of CPS, PSD issued the General Direction No. 02 of 2018 on the Operations of the CPS.

19.6 Regulation and Oversight of Payment and Settlement Systems

PSD continued its regulatory and oversight activities to ensure the safety and efficiency of the electronic payment systems. Accordingly, the following major activities were carried out by PSD during 2018:

- (a) The Direction on Acquiring Payment Card based Electronic Commerce Transactions through Service Providers was issued in January 2018 to stipulate conditions on acquiring payment card based transactions through payment platform providers. This direction was issued with the objective of minimizing the risks of third party payment platform providers getting involved in e-commerce transactions while ensuring timely payments to merchants.
- (b) Guidelines on Minimum Compliance Standard for Payment Related Mobile Applications were issued in January 2018, to set minimum compliance standards for mobile applications used by financial institutions to provide payment services. These guidelines were issued to secure transactions carried out using mobile applications.
- (c) In terms of the provisions of the Payment Cards and Mobile Payment Systems Regulation No. 1 of 2013, granted approval to a LCB and a Finance Company which were authorized to issue debit cards as Licensed Service Providers of Payment Cards to issue credit cards. In addition, approval was granted to a LCB, licensed as a Service Provider of Payment Cards to function as a financial acquirer of payment cards.
- (d) Conducted on-site supervision on Licensed Operators of Mobile Phone based e-money systems to ensure the implementation of the recommendations made in order to ensure the reliability and smooth functioning of the said systems.
- (e) Evaluated the Business Continuity Plans of the LankaSettle participants and LCPL in order to ensure their ability to continue business operations in a contingency situation.

19.7 National Payment Council

The National Payment Council (NPC), which is the industry consultative and monitoring committee on payment systems, appointed two committees to study developments in the FinTech sector and Blockchain technology in order to look into the possibility of introducing emerging innovative payment technologies to the payment and settlement systems of the country. PSD initiated following actions to implement the recommendations made by these committees.

- (a) The National Quick Response (QR) Code standard was issued in October 2018 to promote customer convenience, safety and ensure interoperability of different payment mechanisms and instruments.
- (b) Facilitated the preparation of a National Transit Card and Infrastructure Framework for Ticketing and Fare Collection in the transport sector. This initiative will standardize the transportation industry payment mechanisms and contribute to the national objective of a less-cash society.

- (c) Initiated the process to establish a FinTech Regulatory Sandbox in order to provide a safe space in a controlled environment for innovators to test their products and services without infringing on regulatory requirements. Accordingly, requested interested parties to share their knowledge and experiences to determine the scope of the Regulatory Sandbox.
- (d) A working committee was appointed to further study the adoption of Blockchain technology in the financial sector. The working committee is evaluating the feasibility of a shared KYC Blockchain solution to be used in the banking sector.

19.8 Public Awareness

PSD continued to publish the quarterly "Payments Bulletin" on the CBSL website for the dissemination of information and statistics on payment and settlement systems operating in the country. Further, PSD conducted awareness programs on a need basis to educate the general public and the banking community on payment systems and other related issues. In order to promote the National QR code, PSD published an advertisement in daily newspapers to educate customers and merchants on QR code based payments. Further, a press release was issued in April 2018 cautioning the public of the possible risks involved in using cryptocurrencies.

20. POLICY REVIEW AND MONITORING

Policy Review and Monitoring Department (PRMD) is responsible for facilitating the entire strategic planning process of the CBSL in order to realize the medium to long term goals of the CBSL. In line with this objective, the department conducted the annual retreat, reviewed the quarterly progress of implementation of the Strategic Plan and Departmental Action Plans and reported the progress to the Corporate Management Committee (CMC) and to the Monetary Board during the year under review.

20.1 Preparation of Strategic Plan 2018 - 2020 and Strategic Priorities 2018 - 2020

The Strategic Plan of the CBSL 2018 - 2020 was launched at the New Year Work Commencement Ceremony held on 02 January 2018, followed by the departmental staff awareness sessions on Bank-wide Strategic Priorities and individual Departmental Action Plans. The identified six Bank-wide Strategic Priorities for the three-year period commencing from 2018 are as follows;

- i. Introduction of an effective Flexible Inflation Targeting Regime
- ii. Promoting a dynamic and resilient financial sector to support sustainable growth
- iii. Modernisation of infrastructure of Payments and Settlements Systems:paving the path towards a less cash society

- iv. Improving the prudent debt management endeavoring debt sustainability
- v. Formulating and implementing a comprehensive HR Strategy
- vi. Implementing Enterprise-wide Risk Management (ERM) framework and strengthening compliance.

With regard to the strategic priorities, time bound strategic actions were identified by the task forces appointed and strategic Key Performance Indicators (KPIs) were identified by the relevant departments for each strategic priority. Lead departments were responsible for coordinating and implementing the strategic priorities whereas the PRMD closely monitored the progress of strategic priorities in collaboration with the lead departments.

20.2 Reviewing the Progress and Reporting to the Management

Progress of implementation of strategic priorities and Departmental Action Plans 2018 were reviewed at the quarterly review meetings during the year. An added feature to the monitoring mechanism was the introduction of classification status of KPIs: i.e. "fully completed", "partly completed" or "not-commenced as expected". This has given the opportunity to identify reasons that hindered the timely completion of KPIs by departments and also to make corrective actions. Subsequent to the progress review meetings, a comprehensive report was submitted to the CMC and to the Monetary Board. The level of achievement of strategic activities and operational activities of the CBSL at the end of 2018 stood at 90.57 percent and 93.42 percent, respectively, resulting in an overall achievement of 92.69 percent.

20.3 Strategic Planning Retreat 2018

PRMD conducted the thirteenth consecutive Strategic Planning Retreat on 20 - 21 October 2018 at the Atrium of the CBSL to discuss the strategic direction of the Bank, the overall progress of the first three-year strategic priorities and the Departmental Action Plans for the upcoming year with the participation of the Monetary Board and the Senior Management. Prior to the retreat, the PRMD conducted progress review meetings for Jan-Sep 2018 and the progress was presented at the retreat. Further, Departmental Action Plans 2019 were extensively discussed at the retreat and finalized, thereafter, incorporating the improvements proposed at the retreat.

21. PUBLIC DEBT

Public Debt Department (PDD) is responsible for discharging statutory responsibilities of the CBSL as the agent of the government for management of public debt in terms of Section 113 of the MLA. In order to meet these responsibilities, PDD was established on 28 August 1950, at the inception of the CBSL. The major functions of PDD include raising funds to meet the gross borrowing requirement of the Government as per the Appropriation Act, meeting the Government debt

service payments on time, maintaining the LankaSecure system in order to facilitate the smooth functioning of settlement of market transactions in Government securities and maintaining the title Registry of Government securities in the Central Depository System (CDS). In addition, the PDD also engages in developing the Government securities market, contributing towards in assessing debt management strategy and liability management initiatives.

21.1 Raising of funds to meet the Government gross borrowing requirement as specified in the Appropriation Act.

- a) The issuance of Treasury bills (T-bills), Treasury bonds (T-bonds), Sri Lanka Development Bonds (SLDBs) and International Sovereign Bonds (ISBs) were the main debt instruments used for financing the government's gross borrowing requirement in 2018.
- b) An abridged table of activities under each of the source of funds is given below.

Table II-22
Instruments and Auction Performance
2017 and 2018

| Instrument | 2017 | | 2018 | |
|--------------------------------------|--------------------------|--------------------|--------------------------|--------------------|
| | Issuances Rs. billion | No. of Auctions | Issuances Rs. billion | No. of Auctions |
| Treasury bills | 1,624.3 | 52 | 1,653.3 | 51 |
| Treasury bonds | 548.8 | 16 | 763.02 | 11 |
| | Issuances USD million | No. of Auctions | Issuances USD million | No. of Auctions |
| | | | | |
| Sri Lanka Development Bonds (SLDBs) | 2,231.4 | 4 | 1,492.05 | 6 |
| International Sovereign Bonds (ISBs) | 1,500.0 | 1 | 2,500.00 | 1 |

- (c) Total net outflow of investments in T-bonds and T-bills by foreign investors in 2018 amounted to US dollars 990.7 million, which consisted of net outflow of US dollars 96.4 million in T-bills and US dollars 893.6 million in T-bonds.
- d) In line with movements of primary market yield rates, a parallel upward shift was observed in the secondary market yield rates particularly during the latter part of 2018. Further, the upward shift in secondary market yield rates could be mainly attributed to the pressure arising from the withdrawal of foreign investments from emerging market economies including Sri Lanka mainly due to the normalisation of interest rates in the United States and the challenging domestic as well as global economic conditions that prevailed particularly towards the latter part of the year.
- e) Average Time to Maturity (ATM) of the outstanding domestic debt stock increased to 5.91 years by end 2018 from 5.78 years by end 2017 due to the regular issuance of medium term T-bonds, emanated as a result of continuous engagement with market participants, advance issue calendar of T-bonds and aligning issuances with resource availability in the market.

21.2 Servicing of Government Debt

Domestic debt service payments of Rs. 1,515.7 billion and foreign debt service payments of Rs. 534.9 billion, totaling Rs. 2,050.6 billion was made during the year 2018.

21.3 Facilitation of the Settlement of Government Securities

The LankaSecure system is used for the settlement of primary and secondary market transactions in Government securities. The system consists of 34 Dealer Direct Participants (26 LCBs and 8 primary dealer companies) maintaining accounts on their own behalf and on behalf of other investors who will be their customers and 3 direct participants (Colombo Stock Exchange, Central Bank of Sri Lanka and EPF who hold accounts on their own behalf only. The PDD plays a main role in facilitating settlements by ensuring uninterrupted real-time operation of LankaSecure. The total face value of holdings in scripless securities as at end December 2018 amounted to Rs. 5,103 billion. This consisted of Rs. 758.8 billion in T-bills and Rs. 4,344.2 billion in T-bonds.

21.4 Maintenance of the Registry in Government Securities

Facility for real-time updates in the Title Registry of Government securities in the CDS, which is maintained at the PDD, has ensured the safekeeping of Government securities. Periodic statements to CDS account holders on their holdings, transactions and payments have been sent continuously throughout the year. PDD has sent 1,832 statements in electronic form and 16,026 semi-annual statements of holdings, 42,681 monthly statements of transactions and 18,744 payment statements by post to CDS account holders during 2018. In addition, CDS account holders are provided with the facility to view account details online. As at end December 2018, there were 94,082 registered CDS account holders.

21.5 System Reforms

In order to enhance the efficiency, effectiveness and transparency as well as to develop the Government securities market, the following system reforms were undertaken during 2018.

a) Enactment of the Active Liability Management Framework

The Parliament has approved the Active Liability Management Act (ALMA) in March 2018 and has passed the resolution to raise Rs. 310 billion by way of loans in or outside Sri Lanka. This will enable the government to proactively address part of the refinancing requirements ahead of time (reduce rollover peaks) and extend the maturity duration and / or smoothen repayments structure of ISBs and other debt maturities. In general, liability management will help the government to diversify the investor base, provide opportunities to streamline

the cost of borrowing based on market conditions, extend the duration of the liability portfolio, reduce refinancing risk in near term and create a favorable price tension for any new issuances. Further, the ALMA would enable the CBSL to initiate liability management exercises in the domestic and foreign market in the form of building buffers, switching, buy-backs, reverse auctions etc. The PDD in consultation with Ministry of Finance will initiate necessary actions to implement liability management on future debt obligations.

b) Institutionalisation of Medium Term Debt Management Strategy (MTDS)

The Public debt management in Sri Lanka has become one of the key policy priorities in recent years primarily due to the rapidly increasing debt stock and the related debt service component in government expenditure. The MTDS will quantify the main risks of Sri Lanka's public debt portfolio, specify an appropriate currency and maturity composition of debt issuance and a strategy to achieve it, present debt issuance options based on cost risk tradeoffs and be consistent with monetary and fiscal policy objectives. In line with that, PDD is closely coordinating with the Ministry of Finance in formulating MTDS for Sri Lanka and will be strategized and published by first quarter of 2019.

21.6 Way forward

- a) The delivery of real-time notification to the customers of the LankaSecure System by way of an SMS or/and E-mail alert for each and every debit and credit record of scripless securities in the LankaSecure System, carried out for each Securities Account will be implemented in the first Quarter of 2019.
- b) Explore the possibility of extending the new primary issuance system for T- bills and an electronic bidding arrangement for primary issuances of SLDBs to further improve transparency and efficiency of government borrowings from the domestic market. Further enhance the market based arrangements of the new primary issuance system for T-bonds and applicability in market participants in T-bond subscriptions.
- c) Measures to strengthen the current legislations
Amendments have been proposed to improve the Registered Stocks and Securities Ordinance (RSSO) and Local Treasury Bills Ordinance (LTBO) to enhance transparency and to be on par with current market developments. Also, amendments have been suggested to Foreign Loans Act No. 29 of 1957 to be in line with international standards of accounting for external liabilities.

21.7 Coordinating Sovereign Rating Review Missions

In 2018, the PDD facilitated international rating agencies (Fitch Ratings Ltd., Moody's Investor Services, Standard & Poor's) for their annual rating reviews in order to ensure the availability of international sovereign ratings for Sri Lanka.

22. REGIONAL DEVELOPMENT

Regional Development Department (RDD), with the objective of supporting the achievement of inclusive and balanced economic growth, continued to coordinate, facilitate and implement various refinance, interest subsidy and credit guarantee schemes funded by the CBSL, the government, donor agencies and Participating Financial Institutions (PFIs) while promoting financial inclusiveness in the country. Complementing these conventional credit operations, RDD continued to develop new strategies and initiatives started in the previous years and delivered a range of credit supplementary services in 2018.

During 2018, RDD continued to engage in improving access to finance of individuals and business ventures especially targeting the vulnerable groups in lagging regions. These initiatives were intended further to develop the capacities of potential entrepreneurs and their ability to meet the challenges that they have to face as entrepreneurs, while achieving a solid financial foundation and high self-reliance. In this effort, the micro, small and medium entrepreneurs of a wide spectrum of sectors including Agriculture, Animal Husbandry, Industry and Services were catered by providing affordable credit facilities and credit supplementary services. In addition, RDD conducted a series of financial literacy, awareness building and skill development programmes island-wide during the year, mainly focusing on those who were outside the formal financial sector and underprivileged, with regard to the access to formal financial services, with the objective of building financially literate entrepreneurs.

In the policy front, RDD continued to take a number of proactive measures for the effective implementation of RDD operations in 2018, marking several important milestones. During 2018, the development of the National Financial Inclusion Strategy (NFIS), which was initiated in 2017, has witnessed positive developments ensuring its expected completion in 2019. The development of NFIS brings in the international exposure and experience in improving financial inclusiveness in the country. Further, six new refinance loan schemes were introduced under the Smallholder Agribusiness Partnerships Programmes (SAPP) funded jointly by the International Fund for Agriculture Development (IFAD) and the Government. The introduction of these six loan schemes marked a significant turning point in Sri Lankan concessionary lending tradition to the Agricultural Sector, as these schemes consist of the Public-Private-Producer-Partnerships (4Ps). The credit component of SAPP loan schemes were implemented by RDD with the support of the Project Management Unit (PMU) of SAPP operated under the Presidential Secretariat.

22.1 Providing Concessionary Financial Facilities

During 2018, RDD continued its credit operations by implementing eleven refinance, interest subsidy and credit guarantee schemes increasing the financial outreach. Information on refinance loan schemes and interest subsidy

schemes implemented by RDD, are given in Table II – 23. In financial terms, 105,867 number of beneficiaries accessed the formal financial sector through loan schemes implemented by RDD and obtained Rs. 16,431.7 million by means of concessionary loans granted through PFIs in 2018. The government funded loan schemes contributed 72.9 per cent to the total loans provided through loan schemes operated by RDD while the CBSL and IFAD contributed by 25.1 per cent and 2.0 per cent, respectively. Out of these funding, 71.5 per cent of loans were directed towards the Agriculture and Livestock Sector, while 14.2 per cent and 14.3 per cent were delivered to the Services Sector and the Industry Sector, respectively.

Status of the loan schemes implemented by RDD in 2018, is given below.

22.2. Implementation of the Government and PFI funded Schemes

Being the main source of the credit schemes implemented by RDD, the Government and PFI funded loan schemes contributed Rs. 11,986.7 million or 72.9 per cent to the total loan disbursements in 2018. These funds were directed to the beneficiaries through PFIs under 8 schemes which consist of 7 refinance loan schemes and an interest subsidy scheme. Among these schemes, “Sarusara” or the New Comprehensive Rural Credit Scheme (NCRCS) served as an interest subsidy scheme and a credit guarantee scheme. Under the NCRCS, the Government provided an interest subsidy for the loans granted by PFIs using their own funds.

- (a) During 2018, the Government provided Rs. 245.6 million of interest subsidy on account of Rs. 9,021.7 million worth of concessionary loans granted by PFIs to 78,215 small-scale farmers of 33 short-term crop varieties. The lending by PFIs under the NCRCS increased by 15.0 per cent to Rs. 9,021.7 million in 2018 from Rs. 7,845.2 million in 2017 demonstrating the commitment of PFIs in lending to the agricultural sector. Accordingly, the interest subsidy provided by the Government also increased by 8.0 per cent in 2018 compared to that of Rs. 227.5 million in 2017.

Out of the total loans disbursed by PFIs under the NCRCS, the highest percentage of disbursements were recorded from the Ampara district, which accounted for 12.6 per cent (Rs. 1,137.9 million) of the total disbursements under the scheme. It was followed by the Polonnaruwa and Anuradhapura districts which contributed Rs. 966.2 million (10.7 per cent) and Rs. 948.3 million (10.5 per cent), respectively, to the total disbursement of the NCRCS.

- (b) The “Athwela” loan scheme which was introduced in August 2017 as a refinance scheme with government intervention to facilitate post-disaster economic activity recovery efforts, performed well in 2018. Of Rs. 1,500 million received from the Government, Rs. 1,499.7 million was disbursed to meet the refinance claim

made by PFIs against 3,543 loans disbursed by them. The “Athwela” loan scheme was implemented with the intention to provide concessionary financial facilities at 2 per cent per annum to the targeted beneficiaries in order to resume any economic activity affected by any disaster identified by the Government.

- (c) In addition to the NCRCS and “Athwela” loan schemes, RDD implemented 4 other refinance loan schemes during 2018. These refinance schemes were the “Swashakthi” loan scheme, Poverty Alleviation Microfinance Project – Revolving Fund (PAMP-RF), Poverty Alleviation Microfinance Project II – Revolving Fund (PAMP II-RF) and Self-Employment Promotion Initiative Loan Scheme – Phase II (SEPI – II). In addition, RDD provided interest subsidy for the loans given under the Working Capital Loan Scheme for Tea Factories (WCLSTF) which was concluded in 2017. Out of these schemes, the PAMP-RF and PAMP II-RF refinance schemes collectively disbursed 7.1 per cent of the disbursements of the government funded loan schemes which amounted to a total of Rs. 855.9 million.
- (d) Moreover, the PAMP II – RF was successfully completed on 15 July 2018 as scheduled, contributing to the poverty alleviation of the country, by granting loans amounting to Rs. 7 billion among 94,893 beneficiaries over its project duration.
- (e) Continuing the past trend, a majority of the funds, i.e. Rs. 9,922.3 million or 82.8 per cent of the total funds provided by the government and PFIs were utilised to grant concessionary loans mainly to the Agriculture and Animal Husbandry sector. Individual and business ventures in the Services sector who required access to finance during 2018 obtained Rs. 1,366.6 million or 11.4 per cent of the government funded loan schemes implemented by RDD. Disbursements made to the Industry sector, which amounted to Rs. 697.7 million in 2018, accounted for 5.8 per cent of the total disbursements.
- (f) More importantly, the Government entered into a Financing Agreement in early 2018 with the IFAD in relation to the implementation of SAPP and agreed to allocate US dollar 11.8 million for the implementation of the Revolving Fund (RF) Loan Schemes of SAPP as counterpart financing. RF Loan Schemes consist of three refinance schemes, namely, RF Capital Loan Scheme, RF Seasonal Loan Scheme and Income Generation Loan Scheme, which will be funded by the Government using the recoveries of the previous IFAD funded loan schemes. Detailed information in this regard is given in section 22.4 where the structure of the SAPP is discussed. Under the RF loan schemes, Seasonal, Capital/Working Capital and Income Generation loans are granted to the farmers or farmer/producer organizations engaged in 4P arrangements including women, youth, farmers, grass

root institutions, tea/rubber factories, tea/rubber nurseries and farm managers.

In 2018, 578 loans amounting to Rs. 112.7 million were registered under the RF Income Generation Loan Scheme of SAPP which is funded by the government. During the operational period of seven months ending December 2018, 527 loans amounting to Rs. 106.4 million were refinanced by the CBSL under the SAPP RF Loan Schemes.

22.3. Implementation of the Central Bank and PFIs funded Schemes

In 2018, Rs. 4,123.0 million or 25.1 per cent of loans were disbursed through the loan schemes funded by the CBSL and PFIs. The Central Bank funded refinance under the “Saubagya” Loan Scheme (SLS) and the interest subsidy under Commercial Scale Dairy Development Loan Scheme (CSDDL).

- (a) Disbursing Rs. 3,850.1 million or 93.4 per cent of the total funds disbursed through the CBSL and PFI funded refinance schemes, the SLS continued its position as the main refinance loan scheme implemented by RDD in 2018. During 2018, SLS served 5,445 number of beneficiaries, island wide.
- (b) Moreover, SLS successfully achieved its Rs. 3,800 million refinancing target before the end of 2018. A majority of refinance, which is Rs. 465.0 million (12.1 per cent), has been disbursed among the beneficiaries in the Kalutara District. A closer look at the geographical distribution of the loan disbursements of SLS shows that the loan disbursements directed to Kurunegala District (Rs. 301.6 million or 7.8 per cent) and Kandy District (Rs. 294.9 million or 7.7 per cent) recorded the second and third highest performing districts, respectively. Majority of the disbursements of SLS, which accounted for Rs. 1,628.1 million or 42.3 per cent of the disbursements, was directed to the Industry sector while Rs. 1,234.6 million (32.1 per cent) was disbursed among the beneficiaries in the Agriculture and Animal Husbandry sector. The balance of Rs. 987.4 million (25.6 per cent) was provided to the services sector.
- (c) The CSDDL, the interest subsidy scheme funded by the CBSL, achieved its target of registering loans worth Rs. 6 billion expected over its project duration. During the first half of 2018, loans worth Rs. 272.9 million was disbursed through the CSDDL among 287 beneficiaries. Under this scheme, loans are granted by PFIs using their own funds whilst interest subsidy is provided by the CBSL to PFIs. The scheme grants loans for the dairy farmers covering all aspects of activities related to dairy business in order to support the national objective of achieving self-sufficiency in milk.
- (d) During 2018, a majority of the funds allocated by the CBSL for financing of SLS and CSDDL were directed to the Industry sector. Funds disbursed through these schemes to the Industry sector amounted to Rs. 1,628.2

Table II-23
Lending Programmes Implemented by the Regional Development Department in 2018

| Information on the Lending Programme/Concessionary Credit Scheme | | | | | | | | Amounts in Rs. mn |
|--|--|---|----------------------------|--|-------------------------|--|--|---|
| Source of Funds | Name | Objective | Refinance/Interest Subsidy | Total Fund Allocation for 2018 | Funds Disbursed in 2018 | Balance Funds to be Disbursed | Interest Rate to the End Borrower – Year End (p.a) | Remarks |
| GOSL Funded | Poverty Alleviation Microfinance Project – Revolving Fund (PAMP-RF) | Poverty alleviation through promotion of income generating activities and organizing low income groups to link them with formal banking system. | Refinance | Rs. 400.0 million | Rs. 519.7 million | Recoveries will be revolved | 12% | |
| | Poverty Alleviation Microfinance Project II Revolving Fund (PAMP II – RF) | | Refinance | Rs. 300.0 million | Rs. 336.2 million | Concluded | 10% from PFI to borrower | |
| | “Swashakthi” Loan Scheme | Generate employment opportunities, for both new entrants and existing entrepreneurs engaged in income generating activities MSME Sectors. | Refinance | Rs. Rs. 3,500 million for the Loan Scheme. No specific yearly allocation | Rs. 375.4 million | Rs. 930.5 million | 5.5% | Rs. 47.3 million has been utilized for the Media Campaign of the “Swashakthi” Loan Scheme |
| | “Athwela” Loan Scheme for the Resumption of Economic Activities affected by Disasters (READ) | Providing concessionary financial facilities to resume any economic activity affected by any disaster as informed by the GOSL. | Refinance | Rs. 2,000 million for the Loan Scheme. No specific yearly allocation | Rs. 1,499.7 million | Funds to be received from the GOSL | 2% | |
| | Self-Employment Promotion Initiative Loan Scheme (SEPI) Ph II | To provide financial assistance to youth trained by recognized vocational training institutions for establishment of their own self-employment projects. | Refinance | Rs. 127.4 million | Rs. 127.4 million | Funds will be allocated for 2019 by the GOSL | 7% | |
| | Smallholder Agribusiness Partnerships Programme (SAPP) -Income Generation Loan Scheme | Contribute to Sri Lanka's smallholders' poverty reduction & competitiveness & increase the income & quality of diet of 57,500 smallholders involved in commercially oriented production & marketing systems. | Refinance | USD 18,5 million for all RF Loan Schemes. No specific yearly allocation | Rs. 106.4 million | N.A.* | 6.5% | |
| | “Sarusara”- New Comprehensive Rural Credit Scheme (NCRCS)* | Uplifting the socioeconomic conditions of micro and small-scale farmers who engage in cultivation of paddy and short-term crops. | Interest Subsidy | Depends on the demand for funds | Rs. 9,025.3 million | N.A.** | 7% | PFI's own funds and Interest Subsidy by CBSL |
| CBSL Funded | The prosperity Loan Scheme (“Saubagya”) | To start up or expand any micro, small and medium scale enterprise (MSME) or any MSME affected by disasters | Refinance | Rs. 3,800 million | Rs. 3,850.1 million | | 8% | |
| | Commercial Scale Dairy Development Loan Scheme (CSDDL) | Support to achieve self – sufficiency in milk and milk products through promoting commercial scale dairy farms. | Interest Subsidy | Depends on the demand for funds | Rs. 272.9 million | | 6% | PFI's own funds and Interest Subsidy by CBSL |
| Donor Funded | SAPP – 4P Capital Loan Scheme | Contribute to Sri Lanka's smallholders' poverty reduction & competitiveness & increase the income & quality of diet of 57,500 smallholders involved in commercially oriented production & marketing systems.. | Refinance | USD 11,8 million for all 4P Loan Schemes. No specific yearly allocation | Rs. 67.8 million | N.A.* | 6.5% | Funded by the International Fund for Agriculture Development (IFAD) |
| | SAPP – 4P Seasonal Loan Scheme | | Refinance | | Rs. 254.2 million | N.A.* | 6.5% | |
| * Abbreviations stands for; N.A. ; Not applicable | | | | | | | | |

million, which accounted to 39.5 per cent of the CBSL funding. Of the total disbursements through RDD operated schemes, 36.6 per cent of the funding was granted to the Agriculture and Animal Husbandry sector (Rs. 1,507.5 million) which was followed by the 23.9 per cent of disbursements made to the Services sector (Rs. 987.4 million).

22.4. Implementation of Donor funded Schemes

During 2018, the IFAD extended both financial and strategic support to fulfill the regional development goals of RDD, as a long-term funding partner.

- (a) SAPP was introduced with the closure of the major IFAD funded Agribusiness Development Loan Schemes operated under the National Agribusiness Development Programme (NADeP). NADeP consisted of NADeP Microfinance, Tharuna Diriya, Out Grower Farmers (Capital and Seasonal loan schemes) and Post-Disaster Economic Activity Recovery Loan (PEARL) schemes. The SAPP is jointly funded by IFAD and the Government by creating a consolidated Line of Credit incorporating the new financing provided by IFAD and the existing and future recoveries of the previous IFAD funded projects. Through the SAPP Financing Agreement, IFAD agreed to fund the SAPP by contributing US dollar 11.8 million to the programme. The Government agreed to contribute US dollar 18.5 million as counterpart financing utilising the recoveries of NADeP, the Smallholder Plantation Entrepreneurship Development Programme and the Dry Zone Livelihood and Support Programme - Revolving Fund.
- (b) In terms of the Financing Agreement, RDD has been identified as the agency for channeling loan proceeds from IFAD under the programme Revolving Fund. The Presidential Secretariat has been identified as the Lead Programme Agency (LPA) of the SAPP for the implementation of the activities related to increasing access to finance. The SAPP is coordinated by the Programme Management Unit (PMU), which operates under the Presidential Secretariat being the LPA.
- (c) The main objective of the SAPP is to contribute to poverty reduction and increase competitiveness in the Sri Lankan smallholder community. It also intends to increase the income and quality of nutrition of 57,500 smallholder farmer households involved in commercially-oriented agriculture production and marketing system. SAPP consists of 6 loan schemes namely;
 - i. Public-Private-Producer-Partnership (4P) Loan Schemes; Capital Loan Scheme, Seasonal Loan Scheme, Youth Loan Scheme – Funded by IFAD
 - ii. Revolving Fund (RF) Loan Schemes ; RF Capital Loan, RF Seasonal Loan, Income Generation Loan Scheme – Funded by the Government Counterpart Financing
- (d) The operation of the SAPP loan schemes, which were introduced in April 2018 are currently at the initial stage. As at end December 2018, 2,121 loans amounting

to Rs. 437.9 million were registered under the SAPP 4P Loan Schemes. During the operational period of 7 months that ended December 2018, 1,699 loans amounting to Rs. 322.0 million were refinanced by the CBSL under the SAPP 4P Loan Schemes.

- (e) In the policy front, actions were taken to amend the Operating Instructions of SAPP loan schemes by increasing the maximum repayment period and the grace period of the loans granted under Seasonal Loan Schemes. It was mainly expected to address the practical difficulties faced by the farmers who carry out seasonal farming activities. Accordingly, actions were taken to increase the grace period of SAPP Seasonal Loan Schemes from 12 months to 18 months with regard to bullet/lump sum payments and to introduce monthly repayments up to a maximum repayment period of 30 months for the Seasonal Loans.

22.5. Strategic Initiatives of RDD

22.5.1. Developing a National Strategy for Financial Inclusion

RDD initiated actions to develop a National Financial Inclusion Strategy (NFIS) for Sri Lanka. In this regard, RDD has made arrangements to obtain technical and financial assistance of the International Finance Corporation (IFC), a member of the World Bank Group (WBG), to develop a comprehensive NFIS, which is aimed at promoting a more effective and efficient process to improve financial inclusion across the country. In this regard, the CBSL signed a Cooperation Agreement with the IFC in January 2018.

Through the proposed NFIS, it is expected to introduce a comprehensive strategy framework including an Action Plan assigning the responsibilities to stakeholders to increase the financial inclusion in the country. By implementing such a comprehensive framework, it is expected to provide each and every individual and business entity in the country, a fair and accessible financial system, which is inclusive and consists of adequate, quality, and affordable financial services. Moreover, the proposed NFIS which is expected to be implemented in 2019, will be accompanied with a National Level Financial Literacy Programme to cater to the need of improving financial literacy among all stakeholders in the economy including students who will be the future economic decision makers in the country.

Based on the knowledge exchange visit to the Bangko Sentral ng Pilipinas by RDD Officers, to learn from the experience of developing a NFIS in the context of Philippines, it was proposed to take steps particularly to improve consumer empowerment via financial education. Moreover, an island-wide Financial Inclusion Survey was conducted in 2018 covering 480 Grama Niladari Divisions in all the districts through a dedicated survey firm selected for this purpose. It was mainly conducted to identify the state of financial inclusion in the country. Moreover, a group of WBG consultants visited the CBSL in

2018 and conducted a series of meetings and workshop with various stakeholders to gather their views, opinions and issues relating to financial inclusion in the country. Following these meetings, an outline for the NFIS was drafted and reviewed by the stakeholders. It is expected to have the second consultative workshop on NFIS with the participation of WBG consultants, during the first quarter of 2019.

22.5.2. Automation of the Operations of Loan Schemes implemented by RDD

During 2018, the RDD initiated preliminary actions to automate the registration and refinance of loans under the schemes operated by the RDD. This automation process, which is to commence from SAPP loan schemes, will be funded by IFAD under the Institutional Strengthening component of the SAPP Financing Agreement. The process is expected to be completed in collaboration with the PMU of SAPP, PFIs and the other relevant stakeholders.

The automation of the loan schemes of SAPP will enhance the smooth implementation of these schemes. This process will also pave the way to automate the operations of the entire loan portfolio of RDD, increasing the efficiency and effectiveness of its operations. The system will also act as a comprehensive Management Information System which will support the decision-making process of RDD more effectively.

In this regard, RDD conducted several meetings and workshops on user requirements and operational concerns, with the participation of relevant stakeholders. RDD expects to complete the project in 2019.

22.5.3. "One Village- One Product" Programme

With the intention of increasing the domestic agricultural production to ensure food and nutrition security of the country, the Central Bank initiated actions to promote "One village One-product" (OVOP) concept for commercial scale agriculture products by selecting potential villages. The broader objective of this programme is to support the sustainable development goals of the National Food Production Programme of the Government.

The OVOP programme can be set up as an integrated community development programme with a vision to increase income and wealth through adding value to local resources. Moreover, it is expected to lead to maximum utilization of resources available in designated villages through innovation, Research and Development (R&D), enhanced value addition of locally available resources, thereby developing products into locally, regionally and globally recognized products of unique quality benefitting the community by way of enhancement of income and improving standards of living.

22.6. Financial Literacy and Capacity Building

Identifying the importance of financial literacy and awareness as dynamic parts of the journey towards the comprehensive financial inclusion, RDD in 2018 conducted 163 awareness programmes compared to the target of conducting 150

programmes. The programmes were mainly focused on financial literacy, entrepreneurship development and skills development etc. to educate community leaders and other stakeholders who are involved in social mobilizing activities and financially excluded groups at the grass root level of society.

These programmes were intended to create awareness on the drawbacks such as household indebtedness caused by financial illiteracy. Further, these programmes highlighted the recompense of entering and linking with the formal financial sector. The focus groups were educated on good banking habits, financial discipline and new financial instruments and services as where they are financially literate, they have the ability to make informed financial choices regarding saving, investing, borrowing, etc. RDD reached both developed and lagging areas intending to create awareness on the drawbacks caused by financial exclusion. The target groups of these programmes consisted mainly of vulnerable groups identified by RDD based on its regional development experience over the period.

Details of the programmes conducted by RDD are given in Table II-24.

Table II-24
Awareness Programmes Conducted by
RDD during 2018

| Type of Programme | No. of Programmes |
|--------------------|-------------------|
| Financial Literacy | 110 |
| Capacity Building | 44 |
| Media Campaign | 9 |
| Total | 163 |

23. REGIONAL OFFICE MANAGEMENT

In terms of Section 7 of the MLA, "the Central Bank of Sri Lanka shall have its principal place of business in Colombo and may have such branches, agencies and correspondents in other places in Sri Lanka or abroad as may be necessary for the proper conduct of business of the Bank." Accordingly, starting from 1981, the CBSL took steps to establish seven Regional Offices (ROO) in the districts of Matara, Anuradhapura, Matale, Jaffna, Trincomalee, Kilinochchi and Nuwara Eliya with the view of carrying out CBSL functions and promoting the development activities of respective regions. RO – Jaffna was amalgamated with RO – Kilinochchi in June 2017 in order to provide effective services to people in the region with the use of resources and facilities available at RO – Kilinochchi. Further, with the approval of the Monetary Board, from 2018, the districts of Rathnapura, Kegalle and Monaragala not covered by any ROO earlier were assigned under RO – Matara, RO – Matale and RO – Nuwara Eliya, respectively. Three districts in the Western Province, not covered by any ROO earlier came under Regional Office Management Department (ROMD) as well. Accordingly, functions of ROMD and ROO covered all 25 administrative districts in the country by 2018.

ROO and ROMD contribute to achieve sustainable and balanced regional development by promoting development activities while conducting various awareness programmes and training programmes and arranging trade fairs, technology transfer workshops and exposure visits for the benefit of entrepreneurs. Moreover, ROMD and ROO also play an important role in extending CBSL services at regional level.

23.1 Development Activities

During the year, 148 awareness programmes on formal and affordable financial services were conducted by ROMD and ROO targeting 12,781 beneficiaries island-wide including entrepreneurs, public servants, students, undergraduates and other general public. Further, ROO promoted the credit delivery mechanism of respective regions while establishing 1,953 credit links and provided credit counseling services to the borrowers who faced difficulties in repayments of their loan installments due to various reasons.

ROMD and ROO conducted training programmes covering the areas of entrepreneurship development, setting-up SMEs, skills development, technology transfers and application of best practices in businesses. Accordingly, 80 training programmes on areas such as preparation of business plan, accounting, taxation, marketing and other areas were conducted for the benefit of 4,476 persons. Further, 09 exposure visits/technology transfer programmes were arranged for 103 entrepreneurs while 132 capacity building programmes including best practices programmes were conducted for 6,860 entrepreneurs. Those beneficiaries were engaged in activities related to agriculture, dairy farming, floriculture, mushroom cultivation, food processing, footwear manufacture, batik printing, garments, tourism etc. ROO also facilitated the marketing of products by arranging market linkages, buyer-seller dialogues, trade fairs and exhibitions. Accordingly, 05 trade fairs were organized and a total of 373 entrepreneurs were benefited through them.

Meanwhile, ROO also conducted open day programmes for the public and a large number of people were benefited through resolving of EPF matters, exchanging of damaged notes, exhibition of the currency museum, sale of CBSL publications and commemorative coins and facilitating to obtain loans at these programmes. Further, several awareness programmes and trade fairs were also conducted in parallel to the above events. ROMD in collaboration with Governors' Secretariat, organized Governor's visits to ROO of Nuwara Eliya, Trincomalee and Anuradhapura during the year 2018. Indebtedness Review Programmes were also conducted in order to find out the issues faced by rural communities with regard to their indebtedness and address such issues with the help of relevant ministries. Accordingly, a total number of 1,290 persons were benefitted from those programmes. Separate forums were also conducted in parallel to open day programmes with the participation of senior officials from banks and other financial institutions.

23.2. Representing CBSL at Regional Level

ROO and ROMD conducted various programmes related to other departments of the CBSL in the regions, thereby making certain CBSL functions actively available at regions. ROO attended to 91,931 EPF inquiries, maintained sales counters for commemorative coins and CBSL publications, managed CWDCS data collection centers and currency museums throughout the year. Further, several programmes were also conducted on subjects such as clean note policy, identification of forged notes, unauthorised financial institutions, prohibited schemes, government securities market and foreign exchange regulations. Educational programmes were arranged for students and teachers. Accordingly, 155 awareness programmes on different subjects were conducted and 17,516 individuals participated in such programmes. Moreover, ROMD and ROO engaged in conducting surveys on topics such as credit demand, awareness on customer charter and financial inclusiveness during the year 2018. Regional Managers and officers from ROMD attended meetings, discussions and special events arranged at regional levels.

24. RESOLUTION AND ENFORCEMENT

Pursuant to the decision taken at the Monetary Board at its meeting No 21/2017 held on 16 June 2017, the Resolution and Enforcement Department (RED) was established with effect from 01 January 2018 by transforming the Enforcement Unit operated within the LCD. The Deposit Insurance Unit operated within the BSD and the Special Police Unit initially established under the LCD were also brought under the purview of the newly formed RED.

The main objectives of the RED are resolving distressed financial institutions, conducting special investigations against officials of institutions who have acted in contravention of provisions of relevant regulations in laws of Banking Act and Finance Business Act including prohibited schemes and unauthorized deposit taking entities etc. In order to achieve these objectives the Department consist of three divisions namely Resolution Division, Enforcement Division and Deposit Insurance Unit based on the core functions assigned to the department.

24.1. Resolution of Distressed Financial Institutions

Resolution and Enforcement Department is in the process of developing a comprehensive Resolution Framework for the Financial Institutions (FIs) licensed by the CBSL. It will be developed within the existing regulatory framework in which the resolution authority and its resolution powers are specified. At present almost all resolution powers are vested with the relevant regulators, i.e. Director of Bank Supervision Department in the case of licensed banks and Director Non-Bank Supervision Department in the case of Non-Bank FIs, as per the relevant legal enactments.

24.2. Enforcement Activities

Enforcement functions of RED are being conducted under operating procedures prepared including internal arrangements in terms of the prevailing legal provisions. Accordingly, for conducting of investigations on unauthorized finance businesses, Director of the Department of Non-Bank Financial Institutions authorizes officers of the RED under Section 42(1) of the Finance Business Act, No.42 of 2011 (FBA) and to conduct investigations on prohibited schemes, the Governor appoints officers of RED under Section 83C of the Banking Act, No.30 of 1988 (BA).

The officers of the RED initiated four investigations on the conduct of alleged prohibited schemes. Reports of two investigations along with the determination of the Monetary Board (MB) were submitted to the Attorney General Department for prosecutions. Further, officers of RED assisted CID and FCID for another two investigations on prohibited schemes and the completed investigation reports has been sent to the Attorney General Department for further proceedings.

RED concluded an investigation on an unauthorised deposit taking institution and initiated legal action as the directors of the company failed to comply with the determination and directions of the Monetary Board. One director of the company was taken into police custody and the courts directed Criminal Investigation Division (CID) to conduct further investigations.

As a preventive measure the enforcement division conducts awareness programmes island-wide on regular basis to enhance financial literacy among rural communities and on prohibited schemes and unauthorised deposit taking institutions. The RED conducted 43 awareness programmes for government officers, police officers, community leaders and general public island-wide during the year 2018.

Table II-25
Awareness Programmes

| Target Group | No of Programmes | No of Participants |
|-----------------------------|------------------|--------------------|
| School Students | 08 | 1,053 |
| Government Officers | 16 | 2,058 |
| General Public | 15 | 1,984 |
| Police Officers | 01 | 150 |
| Air Force and Navy Officers | 03 | 233 |
| Total | 43 | 5,478 |

24.3. Administration of the Sri Lanka Deposit Insurance and Liquidity Support Scheme (SLDILSS)

As at 31 December 2018, the Scheme comprised 76 member institutions with a total fund of approximately Rs. 53 billion (unaudited). Book value of the investments in Government securities by the fund and the loan granted to a member institution during the year 2014 under the liquidity support facility for restructuring, as at 31 December 2018 were Rs.49.8 billion and Rs.1.9 billion, respectively. Financial highlights of SLDILSS are given in Table below.

Table II - 26
Financial Highlights of the Sri Lanka Deposit Insurance and Liquidity Support Scheme

| Item | Amount (Rs. Mn) | |
|-------------------------------------|------------------|-------------------|
| | As at 31.12.2017 | As at 31.12.2018* |
| Size of the fund | 44,123 | 53,710 |
| Total Income | 12,115 | 14,024 |
| Total Expenditure | 2,249 | 3,240 |
| Profit for the Year (before tax) | 9,866 | 10,784 |
| Investment in Government Securities | 39,646 | 49,843 |
| Loans and Receivables | 6,129 | 1,902 |
| Available for Sale Reserve | 2,392 | (1,528) |
| *Provisional | | |

- Licensed banks that maintained a capital adequacy ratio of 14 per cent or above at the end of the immediately preceding financial year were required to pay a premium of 0.10 per cent per annum on the total amount of all eligible deposits. All other banks were charged a premium of 0.125 per cent per annum. The premium applicable for licensed finance companies was 0.15 per cent per annum. Premia and penalties from member institutions during the year of 2018 amounted to Rs. 8.8 billion.
- With effect from 01.01.2018, the deposit insurance coverage per depositor per institution is Rs. 600,000.

24.4.Compensation Payments to the Depositors of Distressed Finance Companies

The Monetary Board granted approval to cancel the licenses issued to two distressed member institutions namely Central Investments and Finance PLC (CIFL) and The Standard Credit Finance Ltd (TSCFL) with effect from 05 March 2018 and 25 July 2018 respectively. Accordingly, compensation payments to the depositors of CIFL commenced from 27 August 2018 in accordance with the Sri Lanka Deposit Insurance Scheme Regulations. The total compensation payments paid as at 31 December 2018 amounted to Rs. 601,539,494.66.

25. RISK MANAGEMENT

In pursuing CBSL's policy objectives, it faces various risks, both financial and non-financial in nature. Since the materialisation of any of these risks could have a severe impact on the financial position and the reputation of the CBSL, a properly designed risk management framework is vital for CBSL. Recognising the strategic importance of an integrated approach to risk management in the CBSL, led to the creation of a separate Risk Management Department

(RMD) in 2015 to overcome the conventional management of viewing risk in silos. Accordingly, risk management was recognised as a key strategic priority of CBSL for 2018-2020 and the CBSL is in the process of implementing an Enterprise-wide Risk Management (ERM) Framework for CBSL. This framework is intended to promote a culture of informed risk-taking at all levels of the CBSL.

The Risk Governance Framework which was approved by the Monetary Board in July 2018 comprises both a Risk Governance Structure and a Risk Management Structure and covers both, financial and non-financial risks confronted by the CBSL. The Risk Governance Structure consists of the Monetary Board (MB), and two board sub-committees, the Board Risk Oversight Committee (BROC) and the Monetary Board Advisory Audit Committee (MBAAC). The MB holds the ultimate responsibility for the overall risk management function of the CBSL and sets the "Tone at the Top". Further, MB is responsible for setting the risk appetite and risk tolerance level for CBSL and approving the risk management/compliance framework.

The BROC was set up in August 2018 and is chaired by Mr. Chrishantha Perera, independent member of the Monetary Board and comprises external experts (Mr. Ravi Abeyseriya, Director HNB Assurance from 01.08.2018 to 05.10.2018 and Mr. Priyan Fernando, Chairman Brandix and Senior Advisor, Boston Consulting Group from 05.10.2018 onwards). The BROC oversees CBSL's overall risk management and compliance functions via a formal delegation from the MB, and is responsible for laying the broad strategy and policies for the Bank's risk management and compliance functions. The BROC also assists the MB to ensure a dedicated focus on risk management and compliance at the CBSL.

The risk management structure that has been put in place follows the three lines of defence model. In the first line of defence, operational departments are expected to identify, assess, control, and mitigate risks and implement internal policies and procedures to ensure that activities carried out are consistent with the Bank's goals and objectives. The Risk Management Department (RMD), as a part of the second line of defence shall facilitate the risk management process, by coordinating activities to direct and guide CBSL with regard to risk management.

RMD provides the foundation for designing, implementing, monitoring, reviewing the risk management function through risk management policies, guidelines and organisational arrangements and seeks to continuously improve the risk management process.

RMD also independently identifies, analyses, evaluates, treats, monitors, reviews and reports financial risks and ensures compliance with MB approved investment policies and guidelines. The third line of defence, Internal Audit provides assurance on the effectiveness of governance, risk

management, and internal controls, including the manner in which the first and second lines of defence achieve risk management and control objectives. Each of these three 'lines' play a distinct role within the Bank's risk governance framework.

In addition to facilitating non-financial risk management of all the departments under the three lines of defence model, RMD is also responsible for the financial risk management of the fund management activities of the International Reserves (IR), and the Internal Investment Funds (IIF) of CBSL, as well as the Employees' Provident Fund (EPF) which is carried out as an agency function for the Government. RMD revised the Investment Policy Statements (IPS) and Investment Guidelines (IG) for the EPF and IIF and set up Investment Oversight Committees (IOCs) to oversee these fund management activities. RMD also independently monitored market and credit risks pertaining to these fund management activities and reported risks emanating from them to the management. Market and credit risk indicators were presented at the monthly meetings of the Foreign Reserves Management Committee, where observations, from a risk perspective, on investment strategies and global market developments were conveyed to the Committee. Similar meetings were convened for the IOCs of the EPF and IIF on a quarterly basis, where risks and compliance issues pertaining to their investments were discussed.

In line with the new framework, RMD prepared a Risk Management Policy Statement (RMPS) for the CBSL, setting out the policies for implementation of risk management across CBSL. In this process, CBSL follows accepted standards and guidelines for managing risks, while assigning risk ownership and management among different stakeholders with clear accountability.

A survey was conducted amongst the Monetary Board and management of CBSL to determine the top bank-wide non-financial risks impacting the CBSL. The survey results would be used to develop a Risk Taxonomy for CBSL, which would help prioritise the bank-wide non-financial risk categories affecting CBSL and enable the management to concentrate on key risk categories that impact CBSL.

Recognising the importance of creating a risk culture within the CBSL, RMD conducted several risk awareness programmes for CBSL staff throughout the year at various fora, with the involvement of RMD staff and external resource personnel. Mr. Amedee Prouvost, Director, Operational Risk and Mr. Riaz Ahmed, Manager, Operational Risk at the World Bank, visited CBSL in October 2018 to share their experiences in dealing with operational risks and discuss a potential long-term technical assistance engagement with CBSL to strengthen the operational risk management function.

Going forward, RMD will continue to strive to create an environment where emerging risks that will have a material impact on the CBSL, and any risks taken beyond the risk appetite of the CBSL, are recognised, escalated and addressed in a timely manner. RMD will work with the operational departments to develop risk registers in a phased-out manner. Risk registers would enable the measurement of risk in a more consistent and uniform manner across all the operations in the bank. It would also provide risk information to the management to enable timely assessment and treatment of risks.

RMD is planning to implement an Incident Reporting Mechanism in early 2019, to facilitate reporting of risk incidents affecting the CBSL to the management and to ensure that appropriate actions are implemented to address the causes of such incidents. This on-line Incident Reporting System, would be accessible to staff at all levels. This would facilitate the development of a central repository of risk events within the CBSL to serve as a basis for analysing and assessing risk incidents, tracking progress on the implementation of corrective actions, identifying possible trends and areas of vulnerabilities and improving risk reduction measures, while strengthening the control environment and ensuring the formulation and implementation of appropriate responses to counter any negative impact on the CBSL. With respect to financial risk management, RMD's focus would be on revisiting the credit risk policies and guidelines with a view to improving the credit risk management framework of the fund management activities of CBSL, covering CBSL's counterparties, issuers and custodians.

26. SECRETARIAT

Secretariat Department (SD) is one of the first Departments established at the inception of the CBSL. The main functions of SD are procurement management, administration of superannuation funds, facilitating overseas studies and training, conducting the Board of Survey, providing secretarial and protocol assistance to the Governor and implementation of leave rules.

(a) Procurement Management

In line with the procurement guidelines set out in the CBSL Manual, SD procured goods and services through tender procedures as well as non-tender procedures in 2018. The procurement process was carried out in line with the procurement plan for the year. In addition, urgent procurements were carried out to meet certain needs of the CBSL.

(b) Administration of Superannuation Funds

SD continued to administer payments and other correspondence relating to the Superannuation Funds of the CBSL which involved around 2,200 beneficiaries. Accordingly, SD engaged in paying gratuity payments, commuted pensions, releasing provident funds and making monthly pension, W&OP and WR&OP payments while collecting life certificates on half yearly basis in line with Pension Rules specified in the CBSL Manual.

(c) Facilitating overseas studies and Training

During 2018, SD facilitated postgraduate studies and short-term trainings for employees and duty travels abroad for the senior management. In this regard, SD involved in making related payments to universities, other training institutions and to the employees who travelled abroad for the aforesaid purposes. In addition, SD assisted the staff who travelled abroad in obtaining of visa through the issuance of visa letters and Provident Fund balance confirmation letters, air ticketing and travel insurance.

(d) Conducting Board of Survey

The Board of Survey was conducted for the disposal of obsolete, damaged, unserviceable, irreparable and surplus office equipment, furniture and other fixed assets. The disposal management process included a survey of such assets in the CBSL and disposal of items as recommended by the Board of Survey.

(e) Implementation of Leave Rules and other administrative matters

SD implemented leave rules in respect of special leave, accident leave, extended sick leave, duty leave and maternity leave on half pay. In addition, SD handled correspondence relating to services provided to trade unions, clubs and associations of the CBSL during the year. Apart from that, the Secretary has also given approvals for public announcements, meetings and common email circulations.

(f) Provision of Secretarial and Protocol Assistance to the Governor

The Governor's secretariat provided secretarial and protocol assistance to the Governor. The secretarial assistance provided included scheduling of appointments and meetings, preparation and compilation of presentations and speeches for the Governor. The protocol assistance included coordinating and arranging Governor's local and foreign travels, official functions hosted by the Governor and protocol services provided to VIP visitors of the Governor and the CBSL.

(g) Other Functions

Having conducted a survey on Central Bank's properties and identifying the risk areas, SD obtained a comprehensive insurance cover for all the properties of the CBSL. SD has facilitated incoming and outgoing mails of the CBSL through its mail room service. The Department ensured sufficient stocks are available in the store through its stationery management system and provided required stationery items to Departments. Organising events for the CBSL was also another important task of the Department.

27. SECURITY SERVICES

Security Services Department (SSD) continued its operations to protect its employees, visitors, properties and currency consignments in transit during the year, while attending to system improvements and trainings of personnel, as summarised below.

27.1 System Improvements

Operational fitness of all fire-fighting equipment located at the Head Office and other premises was inspected, repaired and replaced on a regular basis during the year. Initiatives were taken to implement a separate access control system to the Sovereign Study Centre at CBS at Rajagiriya in collaboration with Information Technology Department and the Facilities Management Departments. SSD participated and coordinated all business continuity drills conducted by Payments and Settlements and Information Technology Departments.

27.2 Training

(a) Fire Prevention, Fire Fighting and First Aid Programmes

A two-day comprehensive training programme on fire prevention, firefighting, first-aid and disaster management was conducted for fire-wardens selected from all departments of the CBSL in October 2018 with the assistance of the Fire Services Department of the Colombo Municipal Council and St. John Ambulance and Disaster Management Center. Further, a demonstration on fire fighting and fire-drills was conducted in March 2018 for all employees at the Head Office with the assistance of the Air Force and Colombo Fire Brigade.

(b) Skills and Competency Building

In order to improve the skills of the security officers, the SSD arranged several educational programmes for its staff. These educational programmes covered the key areas of security, information technology and customer care.

(c) Weapon Handling and Live Firing

Weapon handling and live firing were conducted for all security officers with the assistance of the Sri Lanka Army during the last quarter of the year.

(d) Recruited twenty-one Trainee Security Officers in December 2018.

28. STAFF SERVICES MANAGEMENT

Staff Services Management Department (SSMD) continued to extend welfare facilities to all beneficiaries in an efficient and effective manner throughout the year. These welfare facilities included the provision of loans under the Staff Housing (Mortgage) Loan Scheme, Provident Fund Loan Scheme and Staff Benefit Scheme; reimbursement of expenses under the Employer Contributory Medical Benefit Scheme (MBS) and provision of medical and restaurant facilities. The number of registered beneficiaries under the MBS consisting of employees, pensioners, their registered dependents together with widows/widowers was approximately 10,000 as at end 2018.

During 2018, SSMD granted 1,551 loans which included Housing Loans, Provident Fund Loans, Vehicle Loans, Computer Loans and other loans under the Staff Benefit Scheme. The loan monitoring system enabled effective supervision of loan disbursements to employees.

The CBSL restaurant continued to provide breakfast and lunch at a reasonable price to the CBSL staff and several measures were also taken to improve the restaurant facilities during 2018.

SSMD continued to reimburse medical expenses incurred by all registered beneficiaries under the MBS. The total amount of reimbursement of medical expenditure increased by seven per cent in 2018 compared to the previous year. The medical facilities at the Medical Centre were made available to the CBSL employees during working hours by outsourcing such services. Medical tests and laboratory services were also provided at the Medical Centre at a reasonable charge. During the year, SSMD conducted three awareness programmes to enhance the knowledge of the CBSL staff on important health issues; namely, "How to protect yourself from ear, nose and throat diseases", "Self Motivation" and "Short life spans of children beyond the protection of elders."

29. STATISTICS

Statistics Department (STD) continued its contribution towards the achievement of the CBSL's objective of 'maintaining economic and price stability'. The role of STD evolved further under the new monetary policy framework, FIT, which CBSL has initiated. In this regard, STD introduced several functional modalities to facilitate the smooth transition towards the FIT framework. Accordingly, the key activities of STD during the year 2018 included (1) collection of data and information from primary and secondary sources (2) compilation of business sentiment, property price and wage indices (3) forecasting of short term key macroeconomic variables (4) compilation of regional statistics such as Sri Lanka Prosperity Index (SLPI) and Provincial Gross Domestic Product (PGDP) (5) timely and regular dissemination of information through data library, publications, reports and press releases and (6) engagement in tracking Sri Lanka's position in key global rankings. Further the Department continued to provide resources for capacity building initiatives for local and international organisations.

29.1 Collecting Data through Surveys and Other Data Sources

(a) Business Sentiment Surveys

The Business Outlook Survey (BOS) was continued on a quarterly basis during 2018 to monitor the current economic situation and the short term market developments, which are indicators of near term economic growth. The target

population of this survey was large scale enterprises covering agriculture, industry and services activities of the economy.

The Purchasing Managers' Index (PMI) Survey for Manufacturing, Services and Construction activities were conducted on a monthly basis to be used as early indicators in GDP forecasting. Further, these indices are used by researchers, economic analysts, industry experts and business decision-makers to better understand the economic condition of the country. The target population for PMI Surveys for Manufacturing and Construction activities was purchasing managers, while that of PMI Survey for Services activities was designated officers with an overall knowledge of the business activities of the firms. The surveys for manufacturing and services sectors were carried out during the last week of each month targeting responses from 100 institutions for each sector, predominantly concentrated in the Western province. The survey for Construction industry was conducted on a monthly basis and it covered major construction companies selected from the companies registered with the Construction Industry Development Authority (CIDA).

Credit Conditions Surveys, which were designed to capture the demand and supply side developments in the credit market, were also continued during the year 2018. With regard to the Credit Demand Survey, the target population was from the Small and Medium Enterprises (SMEs) of the economy in the Western province and in the provinces where the CBSL has its regional presence. The Credit Supply Survey covered all LCBs and licensed specialised banks of the country. The results of Credit Conditions Surveys were reported to the management on a semi-annual basis to facilitate policy formulation.

(b) Inflation Expectations Survey

The Department continued to conduct the Inflation Expectations Survey on a monthly basis since its introduction in 2006. The current survey includes three main categories of respondents; Corporate Sector, Household Sector and the Academia. During the fourth quarter of 2018, Country Wide Data Collection System (CWDCS) Teacher Investigators (TIs) were also added to the respondent base, to improve the representativeness and precision of the household sector. Respondents provided both quantitative and qualitative information on current and future inflation expectations upto a period of 12 months ahead. The results of the survey were reported to the management on a monthly basis to be used for policy decision making.

(c) Labour Force Information and Public Sector Employment Survey

With regard to overall labour market data analysis, information obtained from the Department of Census and Statistics (DCS) and other data providers, were analysed with respect to employment, unemployment, foreign employment, labour relations, labour market reforms and

labour productivity in the country. Collaborative data sharing was carried out with national and international agencies in order to assist the policy formulation process.

To ascertain the developments in the public sector employment, the Public Sector Employment Survey, covering all public sector institutions was carried out on an annual basis since 2018, which was previously conducted on a semi-annual basis. In addition, since 2018 the Department of Management Services (DMS) of the Ministry of Finance provides data pertaining to public sector employment. These data were analysed and published through the annual publications of the CBSL for the information of the general public.

(d) Private Sector Health Services Survey

This survey, which was designed to develop an indicator to capture the developments in private sector health services in GDP forecasting was conducted continuously during 2018 on a quarterly basis. The survey was conducted covering monthly data targeting a sample of hospitals registered under the Private Health Services Regulatory Council. Information on the number of out-patients and admissions was collected and used to capture the developments in the private health services. This was used as an indicator in forecasting the value-added growth of private sector health services.

(e) Super Market Retail Trade Survey

This survey, which was initiated in 2017 to capture trends in supermarket retail trade activities was continued on a quarterly basis in 2018. A quarterly supermarket cost of sales index was computed based on the data collected through this survey and was used as an indicator in STD's indicator based GDP forecasting. Identifying the future potential of modern retail trade activities of the country, this indicator was also used as a proxy to analyse consumer spending patterns of the economy.

(f) Condominium Market Survey

This quarterly survey was initiated in 2017 with the objective of obtaining primary data on actual sales prices, the demand, reasons for price changes, number of existing and upcoming housing units, level of occupancy in projects, buyer portfolio information and forward-looking perceptions from condominium developers. The geographical coverage of the condominiums is limited to the areas of the projects carried out by the survey respondents. Information thus collected is used in identifying the price trends and other market developments, which provide insights for policy formulation purposes.

(g) ICT-BPM Survey

STD introduced a separate business conditions survey for the Information and Communication Technology and Business Process Management (ICT-BPM) sector from June 2018 with the support of the Sri Lanka Association of Software and Service Companies (SLASSCOM). The main advantages

of this survey are, using as a proxy indicator in the GDP forecasting process, sharing such information with the DCS to monitor/support the GDP estimation and sharing the data with business decision-makers and economic analysts to help better understand the industry conditions of the ICT-BPM sector.

(h) On Demand Surveys

Survey on Household Indebtedness in North Central Province

Identifying the trend in growing household sector loans and its likeliness towards serious ramifications on the business health of the financial sector, as well as on the household sector driving low-income families to a state of indebtedness, STD together with Macropprudential Surveillance Department, Regional Development Department and Regional Office Management Department launched a survey in the North Central Province (NCP) to further scrutinise the household sector indebtedness. The sample frame for the survey was the housing units in all Grama Niladhari divisions in NCP. A two-stage stratified sampling procedure was used to ensure the collection of unbiased information ensuring the reliability of the data. The survey was carried out using a structured questionnaire covering 1,500 households and the information was collected by interviewing the selected households by employing development officers of the area as enumerators for the data collection. The results were analysed by STD and reported to the management.

Global Digitalisation Survey

A global survey on “Digitalisation” was conducted by STD during 2018 together with 16 other Central Banks who were participants of the Annual Conference on Central Bank Business Surveys and Liaison Programme, organised by the Federal Reserve Bank of Atlanta in Miami, Florida. The main objectives of conducting this survey were, to identify adoption of various forms of digital technologies by institutions and to gather information on their expectations regarding the impact of digitalisation on prices and employment. The survey for Sri Lanka was conducted by selecting institutions covering the three major sectors of the economy; agriculture, industry and services.

(i) Country Wide Data Collection System

The manual form of the CWDCS, which commenced in 1978, was revamped and a real time electronic data collection platform through tablet computers with a data collection Application (App) was initiated from 01 January 2018. The main objective of this process was to collect retail prices and producer prices on a timely basis to facilitate the forecasting of the National Consumer Price Index (NCPI) for policy making purpose. Further, the new system would facilitate on demand surveys when required. To introduce the new e-data collection arrangement to the TIs network, STD conducted four seminars during the second half of 2018.

The regular collection of information on retail prices and producer prices of consumer goods, daily wages of the informal private sector and approximations on future production levels of agriculture and fisheries commodities on a weekly, monthly and quarterly basis were continued in 2018 with the support of the new e-data collection system. Those data were extensively used for analysing seasonal variations and regional differences in prices and wages; compilation of price indices, PGDP and SLPI; forecasting price movements and inflation; evaluation of the impact of policy changes on prices; estimation of national expenditure and income; and dissemination of price and wage data to the general public.

The CWDCS used the service of government school teachers for data collection covering the island. Further, the system utilised services of non-teacher data investigators to report data on wholesale and retail prices from the Pettah Market, Maradagahamula Rice Market, Dambulla and Narahenpita Special Economic Centers and Negombo and Peliyagoda Fish Markets on a daily/weekly basis. In order to strengthen the management information system, the Department collected the wholesale and retail prices of a range of food commodities directly from selected markets as well and published it on the CBSL website on a daily basis.

29.2 Compiling Indices

(a) Business Sentiment Indices

Based on the results of BOS, Business Sentiment Indices namely; Business Condition, Profitability, Skilled Labour Availability, Sales, Demand and Capacity Utilisation were compiled. The results were presented to the MPC and detailed reports were submitted to the management for policy making purposes. Further, major indices were published quarterly in aggregate form on the CBSL website for the information of external users.

PMI Manufacturing with the sub-indices of New Orders, Production, Employment, Suppliers’ Delivery Time and Stock of Purchases, and PMI Services with sub-indices of New Businesses, Business Activity, Employment, Backlogs of Work and Expectations for Activity were compiled assessing the month-on-month change. These results were reported to the MPC and senior management for policy decision making and issued press notices for the general public.

(b) Property Price Indices

STD compiled the Land Price Index (LPI) (base year: 1998) annually from 1998 to 2008 and bi-annually from 2009 to 2017, covering 50 centres of five Divisional Secretariats (DSs) in the Colombo District. With the increasing importance of monitoring land prices due to the recent developments in the real estate sector, STD expanded the geographical coverage of LPI to 82 centers covering all DS divisions in the Colombo District during 2018 and revised its base period to the first half of 2017. Value of a perch estimated by the Government Valuation Department for bare lands was used for the index

compilation process. In view of the diverse nature of land use and to maintain homogeneity, three sub-indices for residential, commercial and industrial lands were computed separately and the overall LPI was calculated by taking the average of the three sub-indices.

Compilation of the monthly index on condominium property prices developed based on sales prices available on property websites, was continued during 2018. Improvements to this process were introduced during the latter part of the year to enhance the efficiency of data collection and to expand the geographical coverage of the index. In addition, a new index was initiated in 2018 based on the transacted prices obtained through the Condominium Market Survey on a quarterly basis, which covers the projects owned by the survey respondents.

(c) Wage Indices

STD compiled wage rate indices to assess the movements of salaries and wages in the economy. In this regard, the wage movements of the public, formal private and informal private sectors were analysed separately. Nominal and real wage rate indices for the public sector were compiled based on the public administration salary circulars. For the formal private sector, real wage rate indices were compiled using the nominal wage rate indices provided by the Department of Labour for the employees in the Wages Boards Trades. STD also continued the compilation of the new index for the formal private sector, which was introduced in 2017, with improvements in the methodology. Informal private sector wage movements were analysed in terms of the informal private sector wage rate index compiled based on information collected through CWDCS.

29.3 Forecasting Key Macroeconomic Variables

STD forecasts short term consumer price inflation and economic growth using model based and indicator based techniques. These forecasts were analysed and discussed at the Staff Level Meetings, Pre-MPC, MPC and submitted to the Monetary Board to facilitate policy decision making.

The short term inflation forecasts were mainly based on recent price trends, econometric techniques and expected price movements associated with market developments. The Department continuously explored new variables that reflect both the supply and demand side impact on inflation to improve the inflation forecasting models. Moreover, the inflation forecasts were updated frequently in line with the realised and perceived changes in variables based on the developments in input and output prices reflected through findings of surveys conducted by the Department. In 2018, improvements to the NCPI forecasting methodology were introduced through the data collected via the CWDCS TIs. Further, model based inflation forecasts were improved through judgmental adjustment based on early warning system data.

Growth forecasts were prepared on a quarterly basis, using primary and secondary data related to each sub activity of the economy based on indicator as well as model based techniques. Leading economic indicators, survey findings and other information related to sub activities of the economy were combined with expert judgment for indicator based forecasts.

In addition, STD continuously contributed to the Forecasting and Policy Analysis System (FPAS) of the CBSL with required short term forecasts of inflation and GDP, relevant analysis and other information.

29.4 Compiling Regional Statistics

(a) Sri Lanka Prosperity Index

SLPI for 2017 was compiled to assess the overall status of prosperity in the country and in each of its provinces. This is a composite indicator which reflects the economic and social developments in the country and its provinces. SLPI comprises three sub-indices namely; Economic and Business Climate, Wellbeing of the People and Socio-Economic Infrastructure, which are measured using 43 representative variables.

(b) Provincial Gross Domestic Product

PGDP, in nominal terms for 2017, was estimated by STD by disaggregating the National Accounts estimates of the DCS, using relevant indicators at provincial level. These statistics reveal the provincial contribution to the national GDP and thus are useful to the provincial authorities as well as the national planners of the central government to introduce and implement appropriate strategies to lower income disparities among provinces.

29.5 Dissemination of Information

The Department continued its data disseminations in both printed and electronic means. Accordingly, its two main statistical publications namely; "Economic and Social Statistics of Sri Lanka 2018 – Volume XL" and "Sri Lanka Socio-Economic Data 2018 – Volume XLI", were released in August and September, respectively, in all three languages. Further, Daily Price Reports of selected consumer items and Weekly and Monthly Economic Indicators were timely published in the CBSL website and the time series data spanning across Real, Monetary, Fiscal, External and Financial sectors, collected from nine internal Departments and several external institutions were included in the Data Library during 2018. The Department mainly contributed to two chapters of the CBSL Annual Report and Recent Economic Developments report and provided data to the Monthly Bulletin. In addition, the information was disseminated by way of press releases to the public at large and knowledge sharing exercises were also conducted throughout the year.

29.6 Tracking Sri Lanka's Position in Global Rankings

(a) "Ease of Doing Business" Ranking

STD continued to provide its assistance to the working committee vested with the responsibility of improving the "Ease of Doing Business" ranking of Sri Lanka, as and when required. Accordingly, during 2018, the Department participated at meetings on the progress of reforms, coordinated Sri Lankan participation at International Seminars on improving country positions and disseminated information on variables tracked under the ranking to the relevant authorities on a timely manner. In addition, the revised version of the publication "A Step-by-Step Guide to Doing Business in Sri Lanka", which contains useful information for the business community, potential entrepreneurs, foreign investors and investment promotion agencies, was released in 2018.

(b) Other Global Rankings

The Department continued to monitor global Indices namely; Worldwide Governance Indicators, The Global Competitiveness Index, Index of Economic Freedom, Human Development Index, Economic Freedom of the World Index and Corruption Perceptions Index and submitted reports to the management and other higher authorities on country positions and strategies to improve rankings, when required. Macroeconomic information and data were provided to the compilers of the above mentioned indices on a weekly and monthly basis.

30. SUPERVISION OF NON-BANK FINANCIAL INSTITUTIONS

The Department of Supervision of Non-Bank Financial Institutions (DSNBFI) is entrusted with the mandate to regulate and supervise Licensed Finance Companies (LFCs) and Specialised Leasing Companies (SLCs) under the provisions of the Finance Business Act, No.42 of 2011 (FBA) and the Finance Leasing Act, No.56 of 2000, respectively. In addition, DSNBFI supervises PD under the provisions of Local Treasury Bills Ordinance No. 08 of 1923 and Registered Stock and Securities Ordinance No. 07 of 1937. Further, the DSNBFI is in the process of issuing licences to the institutions engaged in microfinance business under the Microfinance Act, No.06 of 2016 for the purpose of regulation and supervision.

DSNBFI's supervisory function includes conduct of statutory examinations and continuous surveillance of the licensed entities while the regulatory function involves implementing prudential regulations and granting regulatory approvals. Apart from the major functions, DSNBFI also engages in several other activities such as capacity building of the sector, facilitating court proceedings and attending to public complaints.

As at end 2018, there were 43 LFCs, 5 SLCs and 8 PDs under the purview of the Department. In addition, licenses have been granted for 65 Registered Finance Leasing Establishments (RFLEs) under the Finance Leasing Act, including the 5 SLCs. The names of these LFCs, SLCs, RFLEs and PDs are provided at the end of this section. The main functions and activities performed by DSNBFI during 2018 are summarised below.

30.1. Issuance of Prudential Regulations

The prudential regulations issued during 2018 are provided in Part III of this report. A summary of the major prudential regulations is given below.

- a. Financial customer protection framework was introduced, in view of protecting the customer interests, maintaining a healthy relationship and strengthening the customer confidence on the sector to ensure the stability and soundness of the sector. This Direction establishes minimum standards on customer protection in the areas of disclosure and transparency, financial education and awareness, responsible business conduct, complaint handling and redress, equitable and fair treatment and protection of customer data and privacy.
- b. A new direction on Outsourcing of Business Operations was introduced to standardize the outsourcing arrangements by introducing a risk management guidelines to manage the risk arising from outsourcing and to impose restrictions on outsourcing core business functions/operations and activities.
- c. A new capital adequacy framework for LFCs and SLCs was implemented with a view to fostering a strong emphasis on risk management and to encourage ongoing improvements in LFC/SLC's risk assessment capabilities. Therefore, the new capital adequacy framework provides for maintenance of capital adequacy ratio on a more risk sensitive focus covering credit and operational risks under basic approach available in Basel accord. In terms of the new framework, companies with assets over Rs.100 billion will have to maintain higher capital adequacy ratios.
- d. A Direction was issued to regularize the valuation procedure of the LFCs and SLCs regarding immovable properties. The new requirements specify the valuers qualifications, frequency of valuation, threshold for internal and external valuation reports and disclosures.
- e. All LFCs were required to obtain a credit rating from a credit rating agency acceptable to the Central Bank and required to publish such rating with effect from 01 October 2018.

| Annex II - 4 | |
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| Entities regulated by DSNBFI (As at end 2018) | |
| Licensed Finance Companies | |
| 1. Abans Finance PLC | 21. LOLC Finance PLC |
| 2. Alliance Finance Co. PLC | 22. Mercantile Investments and Finance PLC |
| 3. AMW Capital Leasing and Finance PLC | 23. Merchant Bank of Sri Lanka & Finance PLC |
| 4. Arpico Finance Co. PLC | 24. Multi Finance PLC |
| 5. Asia Asset Finance PLC | 25. Nation Lanka Finance PLC |
| 6. Associated Motor Finance Co. PLC | 26. Orient Finance PLC |
| 7. Bimpuh Finance PLC | 27. People's Leasing & Finance PLC |
| 8. Central Finance Co. PLC | 28. People's Merchant Finance PLC |
| 9. Citizens Development Business Finance PLC | 29. Prime Finance PLC |
| 10. Commercial Credit and Finance PLC | 30. Richard Peiris Finance Ltd. |
| 11. Commercial Leasing & Finance PLC | 31. Sarvodaya Development Finance Ltd. |
| 12. Dialog Finance PLC (formerly Colombo Trust Finance PLC) | 32. Senkadagala Finance PLC |
| 13. ETI Finance Ltd. (a) | 33. Serendib Finance Ltd. |
| 14. Fintrex Finance Ltd. (formerly Melsta Regal Finance Ltd.) | 34. Singer Finance (Lanka) PLC |
| 15. HNB Finance Ltd. (formerly HNB Grameen Finance Ltd.) | 35. Sinhaputhra Finance PLC (a) |
| 16. Ideal Finance Ltd. | 36. Siyapatha Finance PLC |
| 17. Kanrich Finance Ltd. | 37. Softlogic Finance PLC |
| 18. Lanka Credit and Business Finance Ltd. (formerly City Finance Corporation Ltd.) | 38. Swarnamahar Financial Services PLC (a) |
| 19. L B Finance PLC | 39. The Finance Co. PLC (a) |
| 20. LOLC Development Finance PLC (formerly BRAC Lanka Finance PLC) | 40. TKS Finance Ltd. (a) |
| | 41. Trade Finance & Investments PLC |
| | 42. U B Finance Co. Ltd. |
| | 43. Vallibel Finance PLC |
| Registered Finance Leasing Establishments | |
| (A) Licensed Commercial Banks | |
| 1. Amana Bank PLC | 2. Lankaputhra Development Bank Ltd. |
| 2. Bank of Ceylon | 3. Pradeshiya Sanwardana Bank |
| 3. Commercial Bank of Ceylon PLC | 4. Sanasa Development Bank PLC |
| 4. DFCC Bank PLC | 5. Sri Lanka Savings Bank Ltd. |
| 5. Hatton National Bank PLC | |
| 6. MCB Bank Ltd. | (C) Specialised Leasing Companies |
| 7. National Development Bank PLC | 1. Assetline Leasing Co. Ltd. |
| 8. Nations Trust Bank PLC | 2. Co-operative Leasing Co. Ltd. |
| 9. Pan Asia Banking Corporation PLC | 3. Newest Capital Ltd. (b) |
| 10. Sampath Bank PLC | 4. SMB Leasing PLC |
| 11. Seylan Bank PLC | 5. Unisons Capital Leasing Ltd. |
| 12. Union Bank of Colombo PLC | |
| (B) Licensed Specialised Banks | (D) All Licensed Finance Companies listed above |
| 1. Housing Development Finance Corporation Bank of Sri Lanka | |
| Primary Dealers | |
| 1. Acuity Securities Ltd. | 9. Pan Asia Banking Corporation PLC (d) |
| 2. Bank of Ceylon | 10. People's Bank |
| 3. Capital Alliance Ltd. | 11. Perpetual Treasuries Ltd. (e) |
| 4. Commercial Bank of Ceylon PLC | 12. Sampath Bank PLC |
| 5. Entrust Securities PLC (c) | 13. Seylan Bank PLC |
| 6. First Capital Treasuries PLC | 14. Union Bank of Colombo PLC |
| 7. Natwealth Securities Ltd. | 15. WealthTrust Securities Ltd. |
| 8. NSB Fund Management Co. Ltd. | |
| <p>(a) These entities are subject to the restrictions imposed by the Central Bank of Sri Lanka under Finance Business Act No. 42 of 2011 including not to accept new deposits</p> <p>(b) Registration has been cancelled with effect from 01.03.2019</p> <p>(c) Participation in government securities primary auction was refrained w.e.f. 24.07.2017</p> <p>(d) Suspended carrying on the business and activities of a primary dealer for a period of 6 months w.e.f. 15.08.2018</p> <p>(e) Suspended carrying on the business and activities of a primary dealer for a period of 6 months w.e.f. 05.01.2019</p> | |

- f. A new Direction on the Maximum Rate of Interest on Microfinance Loans was introduced for LFCs and SLCs with the objective of protecting the customers being charged with exorbitant interest rates.
- g. The existing Loan to Value (LTV) ratio was revised to curtail imports and the resultant adverse impact on the exchange rate requiring LFCs and SLCs to adopt the new ratio with effect from 01 October 2018. Accordingly, the LTV ratio of hybrid motor cars, vans and SUVs were reduced to 50 per cent.

30.2. Supervision of LFCs and SLCs

a. Conduct of Statutory Examinations

- i. As planned, the DSNBFI conducted 13 annual statutory examinations of LFCs and SLCs during 2018. The main findings of the examinations included low efficiency, issues on corporate governance, inadequate loan loss provisioning, lapses in internal controls, potential credit risks and sustainability issues originated from the business models.
- ii. The Monetary Board approved time bound action plans and recommendations of these examinations, were communicated to the respective companies for the attention of the Board of Directors and Board sub-committees and follow-up actions were undertaken to ensure that LFCs and SLCs take corrective measures within the agreed time frames.

b. Conduct of Continuous Surveillance

- i. All LFCs and SLCs were continuously supervised based on the periodic financial information submitted through the web based Finnet system and review of other financial information including auditors' reports, management letters, external rating and press reports etc. These reviews identify the potential risks of LFCs/SLCs through early warning indicators and the internal rating system on the areas of capital, liquidity, provisioning, corporate governance and risk management.
- ii. During the year under review, new Finnet returns on capital adequacy were introduced to be in line with the newly issued Direction on minimum core capital and capital adequacy ratio. Further, two returns on sector wise credit exposures and deposit liabilities were introduced to capture more information on credit exposure of the sector and in line with the regulation of Sri Lanka Deposit Insurance and Liquidity Support Scheme, respectively.
- iii. On the basis of assessments and the severity of the finding, DSNBFI takes prompt corrective actions to rectify the supervisory concerns within a clearly stipulated time frame. Further, sector performance was

reported to the Monetary Board on a regular basis in view of keeping the senior management informed of the latest developments in the sector.

- iv. DSNBFI granted regulatory approvals to LFCs and SLCs to issue debt instruments, increase share capital, capital infusions by new investors, amend the Articles of Associations, form subsidiaries, outsource business operations, appoint new Directors and officers performing executive functions, change the name of the company, change of registered address, relocation of business places, ownerships transfers and openings of new branches. Leasing licence issued to LOLC Micro Credit Ltd was cancelled after the amalgamation of it with LOLC Finance PLC.
- v. DSNBFI mediated to resolve a large number of complaints received with regard to LFCs and SLCs from the general public, mainly with respect to unfair customer practices and seeking reliefs on the transactions they entered into with LFCs and SLCs.

c. Resolution Actions on Weak LFCs

The key focus of DSNBFI during 2018 was to resolve the insolvent companies that have been confronted with prolonged liquidity crisis for past several years. Accordingly, the following steps were taken in this regard.

- i. City Finance Corporation Ltd. was revived with the investment made by Lanka Credit and Business Ltd. and the restructuring plan is now in progress. As per the plan, the initial capital infusions, merger of two companies and repayment of part of deposits have been completed.
- ii. The licences issued to Central Investments and Finance PLC and The Standard Credit Finance Ltd. under the FBA were cancelled and are in the process of liquidation.
- iii. Regulation on "Priority of Claims in a Winding Up of a Finance Company" was prepared as provided in Section 33 of the FBA in line with the proposed resolution and enforcement framework of LFCs. This regulation will be applicable in the event of winding up of an LFC. The regulation will be published in the Gazette subsequent to the approval of the relevant authorities.
- iv. Several regulatory actions were initiated including imposing restrictions on deposits and borrowings, appointing a panel to manage the business affairs, repaying part of deposits through the disposal of subsidiaries and other investment properties etc. of three companies that were in distressed financial condition while facilitating several prospective investors to proceed with actions such as conducting due diligence with a view to restructuring those companies.

In addition, regulatory actions were initiated against the wrongdoers of these companies to recover the loss caused to the company by their actions, including impounding passports and seizing personal bank accounts. Further, regular meetings were also held with Board of Directors, Senior Management and External Auditors to monitor the progress and restructuring/revival plans of these companies in compliance with CBSL Directions.

30.3. Supervision of PDs

a. Conduct of Statutory Examinations and Continuous Surveillance

Statutory examinations of 4 PDs were completed during 2018 while continuous surveillance continued on an ongoing basis for all PDs. As supervisory measures, suspension of business activities of Perpetual Treasuries Limited (PTL) and Pan Asia Banking Corporation PLC – Primary Dealer Unit (PABC), were extended for a period of six months (PTL w.e.f. 05 January 2019 and PABC w.e.f. 15 August 2018).

Approval of the Monetary Board was granted to transfer the functions of supervision, examination and investigation and periodic evaluation of the performance of Bank PD Units to the BSD with effect from 01 January 2018. Further, the Superintendent of Public Debt (SPD) was authorised to continue to issue regulations and directions to all PDs (non-bank PDs and bank PD Units) with respect to the development of the Government securities market and market conduct, while the Director of SNBFI was empowered to issue directions and guidelines on prudential requirements for PDs.

b. Resolution Action on Entrust Securities PLC (ESP)

A systematic concern arose in 2016 with respect to illiquid financial position as a result of the unsound financial practices of ESP. The secured repo and outright investments were settled. Financial Crimes Investigation Division has initiated legal actions and investigations are ongoing. The CBSL is currently in the process of formulating a possible settlement plan. DSNBFI is also facilitating the Auditor General's Department to conduct the forensic audit on ESP as directed by the Court.

30.4. Public Awareness and Capacity Building of the LFC/SLC Sector

a. Capacity Building

With a view to enhancing the skills/competences, the officers of the DSNBFI participated in local and foreign training programmes in the areas of forensic investigations, Basel principles, stress testing, and corporate governance etc. Further, special training programs were held for all staff on implementation of new accounting standards in line with

IFRS requirements. The senior officers of the Department continued to serve as resource persons at the training sessions conducted at the CBS of the CBSL and other external institutions.

b. Meeting with LFCs/SLCs and Other Stakeholders

DSNBFI conducted 2 meetings with the Chief Executive Officers of LFCs/SLCs chaired by the Governor with the objective of sharing views between the CBSL and LFC/SLC sector on matters relating to the economy and regulatory developments. In addition, the Department held continuous meetings with LFCs/SLCs, external auditors and international agencies to discuss company and sector related issues and implement corrective actions.

c. Public Awareness Programmes

DSNBFI provided assistance to conduct such programs upon requests of other Departments such as Resolution and Enforcement Department, Regional Development Department and Regional Office Management Department as and when required.

30.5. Facilitating Court Proceedings on Unauthorised Financial Institutions

a. Golden Key Credit Card Company Ltd. (GKCC)

As per the modalities approved by the Supreme Court for the repayment to the Security Deposit Holders of GKCC, DSNBFI coordinated the repayment of Security Deposits held by the customers of GKCC.

b. Actions Relating to Unauthorised Financial Institutions

DSNBFI continued to facilitate the proceedings of the Court cases filed by the depositors of The Finance and Guarantee Property Developers Private Ltd. and F&G Real Estate Company Ltd. in 2015. Further, DSNBFI provided evidence for the cases filed with regard to unauthorised finance business as and when required by the Courts.

31. TRAINING AND DEVELOPMENT

Training and Development Department (TDD) facilitates emerging needs of the human capital development of the CBSL. In this regard, TDD identifies training needs, formulates strategies to fill up training gaps, prepares and implements annual training plan, facilitates the staff for their postgraduate studies, and provide opportunities for foreign/local short-term training for the staff. Further, TDD also facilitates knowledge sharing among staff.

31.1 Postgraduate Studies

In 2018, the TDD facilitated eight staff class officers to embark on Doctor of Philosophy (PhD) programmes and another eight officers to commence Master's degree programmes in reputed

universities in Australia and the UK. Meanwhile, three officers were facilitated to commence Master's programmes in local universities on a part-time basis during the year.

Further, 15 officers reported back to duty after completing their postgraduate studies successfully during 2018, out of which one officer had completed his PhD programme while the other 14 officers had completed their Master's degree programmes. Number of officers who have commenced and completed postgraduate studies under the Bank Scholarship Programme during the period 2014-2018 are given in Table II-27 below.

Table II-27
Postgraduate Studies under the Bank Scholarship Programme

| Studies | 2014 | | 2015 | | 2016 | | 2017 | | 2018 | |
|-----------------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|
| | Commenced | Completed | Commenced | Completed | Commenced | Completed | Commenced | Completed | Commenced | Completed |
| PhD | 5 | 2 | 3 | 5 | 5 | 2 | 3 | 3 | 8 | 1 |
| Master's Degree | 24 | 11 | 19 | 21 | 24 | 11 | 19 | 18 | 8 | 14 |

31.2 Short-term Training

With the aim of bridging the competency gaps identified during the annual competency mapping exercise carried out at the end of 2017, the TDD facilitated 1,548 short-term foreign and local training opportunities to the CBSL staff.

31.2.1 Short-term Foreign Training

The TDD facilitated the participation of the CBSL employees in relevant short-term foreign training, including training programmes, workshops, seminars, conferences, study visits and meetings conducted by the reputed foreign training institutions and foreign Central Banks during 2018.

The foreign institutions where the CBSL employees trained during 2018 included Banque de France, Bank of England, Deutsche Bundesbank, Reserve Bank of India (RBI), Bank Negara Malaysia, Bank of Korea, Federal Reserve System of USA, Monetary Authority of Singapore and State Bank of Pakistan.

Apart from that the employees of the CBSL also participated in short-term training programmes at International funding agencies, research organizations, universities and training institutes such as IMF, World Bank, Asian Development Bank, SEACEN, Bank for International Settlements (BIS), Indian Technical and Economic Co-operation (ITEC), University Putra Malaysia, Chinese University of Hong Kong etc.

Total number of such short-term training opportunities facilitated by the Department was 408. Further, the TDD facilitated 13 study visits held in India, Malaysia, Hungary, Austria, Saudi Arabia, Finland, Philippines, Korea and Lebanon during 2018 (Table II-28). TDD also facilitated two CBSL officers to contribute in foreign programmes as resource persons.

The TDD facilitated 18 Training Committee Meetings to make decisions relevant to training and development matters.

Table II-28
Short-term Foreign Training - 2018

| Field | No. of Programmes | No. of Participants |
|----------------------------|-------------------|---------------------|
| Economic & Price Stability | 67 | 101 |
| Financial System Stability | 128 | 205 |
| Agency Functions | 16 | 16 |
| Currency Management | 8 | 11 |
| Support Services and Other | 39 | 75 |
| Total | 258 | 408 |

While providing the CBSL officers the training opportunities they required, the TDD was also interested in ensuring that they make use of the knowledge and skills acquired from such programmes to improve the operations of the CBSL. For this purpose the TDD facilitated meetings of training sub-committee on post training monitoring. Fourteen (14) such training sub-committee meetings were held during 2018. Accordingly, 212 assignments have been completed out of 236 by the officers who have participated in the short-term foreign training programmes as at 28 February 2019 (Table II-29).

Table II-29
Completion of Assignments by Participants of Short term Foreign Training Programmes as at 28.02.2019

| Category | No. of Assignments |
|---|--------------------|
| Guidelines for supervision of financial institutions | 12 |
| Knowledge sharing and public awareness through articles and presentations | 130 |
| Proposals for improving systems and processes | 30 |
| Concept Papers | 40 |
| Total | 212 |

The TDD issued 2 circulars relevant to the procedures of the short-term foreign training programmes during 2018.

31.2.2 Short-term Local Training

During the year, the TDD provided 1,140 short-term local training opportunities by way of training programmes, seminars, workshops, etc. to the CBSL staff at the CBS and at other reputed local institutions. These were mainly in the areas of economics, statistics, accountancy, banking, IT, legal, auditing, fund management, risk management, secretarial practices, human resource development, supervision of banks & financial institutions, financial markets, foreign exchange, currency and regional development. Four hundred sixty six (466) officers participated in 93 training programmes conducted by local institutions while 674 officers participated in 57 training programmes conducted by the CBS during the year.

In addition, TDD facilitated to conduct two programmes on “Central Bank Governance for Senior Management of the Bank” and “Code of Ethics” for Staff Officers in the CBSL in collaboration with CBS during 2018. Further, TDD facilitated to conduct a programme on “Workshop on Cyber Security” in collaboration with ITD and CBS. The TDD conducted awareness programmes on “the Code of Conduct for the Employees of the CBSL” for all staff of the CBSL in collaboration with Legal and Compliance Department” during 2018. In December 2018, TDD conducted Induction Programmes for newly recruited Management Trainees, Legal Officers and Trainee Security Officers and for promoted probationary Staff Officers.

31.3 Knowledge Sharing and Other Activities

The TDD facilitated presentations by the CBSL officers who reported back to duty completing their Master’s studies. Further, TDD arranged Economic Forums with invited guest speakers as well as with the officers of the CBSL who have doctorates.

The TDD continued the Bank’s sponsorship scheme for Chartered Financial Analyst (CFA) qualification, a mean for encouraging the CBSL officers to acquire professional qualifications useful to the operations of the CBSL.

