

**NEWSLINE***Daily by Faraz***“Questioning
The Answers”**

THE CENTRAL BANK HAS **LEFT RATES ALONE.** INFLATION HAS NOT RETURNED THE FAVOUR.





NEWSLINE

Daily by Faraz



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THE CENTRAL BANK HAS LEFT RATES ALONE. INFLATION HAS NOT RETURNED THE FAVOUR.

Sri Lanka's policy interest rate remains at 8.75 percent while inflation has climbed to 8 percent. The Central Bank believes the tightening already undertaken should be given time to work. For households and businesses, however, the question is whether prices will be equally patient.

The Central Bank has decided against another immediate increase in interest rates, keeping the Overnight Policy Rate at 8.75 percent as it attempts to balance two competing dangers. Tighten too aggressively and the recovery could be damaged. Wait too long while inflation is accelerating and the country risks allowing price pressures to become considerably more difficult to contain.

Headline inflation reached 8 percent in August, up from 7.3 percent in July, while core inflation also increased to 5.1 percent. The distinction matters because headline inflation can be pushed around by food and energy prices, whereas core inflation attempts to identify the more persistent price pressures developing underneath them.

Sri Lanka's present inflation problem has an important external component. The Middle East crisis pushed international petroleum prices sharply higher, and a country importing its fuel cannot insulate itself completely from what happens thousands of kilometres away. Higher petroleum costs eventually find their way into transport, electricity, manufacturing and food distribution, spreading the original shock much further through the economy.

The Central Bank's difficulty is that increasing interest rates in Colombo cannot reduce the international oil price. Monetary policy can suppress domestic demand and credit, but it cannot reopen a shipping route, increase global petroleum production or reduce the insurance premium on a tanker travelling through a conflict zone. Increasing rates too aggressively in response to imported inflation could therefore punish domestic borrowers without addressing the original cause.

There is nevertheless a danger in assuming that imported inflation remains imported. Businesses confronted with higher energy and transport costs pass them onwards. Workers whose purchasing power is being eroded seek higher wages, suppliers increase prices and expectations begin adjusting. An external price shock can eventually become domestic inflation, which is precisely what the Central Bank must prevent.

The wider economy is in considerably better condition than it was during the crisis. Growth continued in the second quarter, official reserves reached approximately US\$6.9 billion by the end of August and the financial system remains substantially stronger.

Those are important achievements, but they do not alter what inflation means to the person standing at a supermarket checkout.

There is a particularly misunderstood feature of falling inflation. If something costing Rs 100 rises to Rs 108 and inflation subsequently falls from 8 percent to 5 percent, the price does not return to Rs 100. It continues rising, only more slowly.

That distinction between falling inflation and falling prices explains why official declarations of improving inflation can sound rather different from the experience of a household paying its bills.

The Central Bank is therefore making a calculated judgment that its previous tightening should be allowed to work through the economy before further action is considered.

Credit conditions are already responding, while additional government measures have attempted to contain some of the pressures created by higher energy prices.

That judgment may prove correct. Monetary policy works with a delay and repeatedly changing direction can create its own instability.

The difficulty is that Sri Lanka has spent several painful years restoring price stability and has relatively little room for complacency if inflationary expectations begin moving upwards again.

The number to watch is consequently not merely the 8.75 percent policy rate. It is what happens to inflation, core inflation, private credit, the rupee and energy prices during the months ahead.

If those begin moving in the wrong direction together, leaving interest rates unchanged becomes a considerably more difficult decision to defend.

For now the Central Bank has decided to wait. Inflation, unfortunately, has not.

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RS 21 TRILLION IN DEPOSITS. MORE THAN RS 1 TRILLION BORROWED AGAINST GOLD. WHAT DOES THAT TELL US?

Sri Lanka has an extraordinary amount of money sitting in banks and finance companies. At the same time, Sri Lankans are borrowing enormous sums against their jewellery. The two numbers are not contradictory. They may instead reveal something much more important about where the country's wealth actually sits.

At the end of 2025, deposits in Sri Lanka's banking system amounted to approximately Rs 19.93 trillion. Savings deposits accounted for around Rs 5.24 trillion while time deposits, principally fixed deposits, amounted to approximately Rs 13.04 trillion. Add approximately Rs 1.27 trillion held by finance companies and the combined pool of deposits moves beyond Rs 21 trillion.

That is an enormous stock of financial savings for an economy that has spent much of the past four years discussing hardship, falling living standards and household financial distress. It immediately raises an obvious question. If Sri Lanka has more than Rs 21 trillion sitting in banks and finance companies, how poor are Sri Lankans really?

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The answer lies partly on the other side of the financial system. At the end of 2025, commercial banks had approximately Rs 898 billion outstanding in pawning advances, while finance companies had around another Rs 465 billion in lending secured against gold. On that basis alone, identifiable institutional lending against gold was already approximately Rs 1.36 trillion, without attempting to count every other form of pawning activity outside those categories.

Gold-backed lending has continued expanding rapidly. Finance-company lending secured against gold was growing by 69.2 percent year-on-year at the end of the

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RS 21 TRILLION...

first quarter of 2026, sufficiently quickly for the Central Bank to intervene by imposing a maximum loan-to-value ratio of 70 percent.

The regulator was concerned not simply about borrowers but about the potential financial-system consequences of rapidly expanding collateral lending while gold prices themselves were volatile.

Put the deposit and pawning numbers beside each other and what initially appears contradictory begins making sense.

The Sri Lankan placing Rs 20 million into fixed deposits and the Sri Lankan pawning jewellery to meet an urgent expense are both represented in national financial statistics. They are not necessarily the same Sri Lankan.

Aggregate numbers disguise distribution. A country can possess substantial private wealth while large numbers of its people have very little liquid financial security. One household may be searching for another half percentage point on a fixed deposit while another is calculating how much can be borrowed against a chain or sovereign. Both are participating in the same financial system from opposite ends.

This brings us to another intriguing question. Is there substantially more money available in Sri Lanka that could be attracted into deposits, particularly by finance companies prepared to offer higher interest rates than the major banks?

There almost certainly is, but movement into deposits should not automatically be confused with the creation of new savings. If Rs 10 million moves from a commercial bank fixed deposit to a finance company offering a better return, the country has not acquired another Rs 10 million.

The same money has changed institutions. Similarly, moving money from a savings account into a fixed deposit changes its classification without increasing national wealth.

There are nevertheless pools of wealth outside conventional bank deposits. Sri Lankans hold Treasury securities, unit trusts, equities, insurance and pension assets, foreign currency, businesses, property, cash and gold. Higher deposit rates can persuade some of that money to migrate, particularly when investors become more interested in income than capital appreciation.

This is where finance companies become interesting. An additional percentage point or two on a substantial fixed deposit can produce meaningful additional income, and licensed finance companies compete aggressively for deposits. But the additional interest should never be examined separately from the institution paying it.

A finance company accepting a deposit must put that money to work at a sufficiently higher return to pay the depositor, meet its operating expenses, absorb defaults, satisfy regulatory requirements and still produce a profit.

The question for the depositor is therefore not merely what interest rate is being offered, but how the institution is earning enough to pay it.

The recent expansion of finance-company lending provides part of the answer. Credit from the sector was growing by more than 50 percent year-on-year at the end of the first quarter, with vehicle finance and gold-backed lending particularly strong.

One person's fixed deposit may therefore become another person's vehicle loan or another family's borrowing against jewellery.

There is nothing improper about that. It is financial intermediation, which is precisely what banks and finance companies exist to do.

What matters is the quality of the lending and whether depositors understand that a higher return does not remove risk.

Licensed finance companies are regulated and participate in Sri Lanka's deposit insurance system, but the protection is limited.

The maximum compensation is presently Rs 1.1 million per depositor. Someone considering placing Rs 10 million or Rs 20 million with an institution because it offers a higher fixed-deposit rate should therefore be examining considerably more than the advertisement.

Capital strength, liquidity, profitability, bad loans, ownership, management and the composition of the loan book matter. An additional percentage point becomes considerably less exciting if the principal itself is exposed to unnecessary risk. Sri Lanka's previous finance-company failures provide sufficient reason for depositors to understand that distinction.

Gold adds another dimension because jewellery performs two completely different financial functions.

For a financially comfortable household it can be accumulated wealth, held for years and passed between generations. For a household short of cash it becomes an emergency credit facility that can be converted into liquidity without actually selling the asset.

That may make the growth in gold-backed lending one of the more revealing indicators of household finances in Sri Lanka. A pawning loan is not automatically evidence of poverty because businesses and investors also borrow against gold. But growth approaching 70 percent in one part of the regulated financial system deserves attention, particularly when it occurs alongside a vast stock of deposits elsewhere.

Sri Lanka therefore appears to have plenty of money. What it may not have is an even distribution of money.

The more interesting question is consequently not simply whether another trillion rupees can be attracted into fixed deposits.

It is where that trillion would come from, where the financial institutions would subsequently lend it and whether the country's savings are ultimately financing productive investment or another expansion of consumption, vehicles and borrowing against family gold.

More than Rs 21 trillion in deposits tells us something about Sri Lanka's wealth. More than Rs 1 trillion borrowed against gold may tell us rather more about its people.

SRI LANKA'S IMF PROGRAMME WILL END. THE ARITHMETIC WILL NOT.

Sri Lanka is approaching the latter stages of an IMF programme that helped restore stability after economic collapse. The more important question is what happens when the programme eventually disappears but the discipline it imposed is still required.

For several years Sri Lanka has had a convenient explanation for almost every difficult economic decision. Taxes increased because of the IMF. Electricity tariffs changed because of the IMF.

State enterprises had to recover their costs because of the IMF, while tighter government spending and a multitude of reforms could similarly be attached to the programme negotiated after the economic collapse.

There is one problem with that explanation. The IMF did not invent Sri Lanka's arithmetic.

Sri Lanka spent beyond its sustainable means, borrowed heavily, accumulated debt, maintained politically attractive prices and eventually exhausted its foreign currency resources. By 2022 the country could no longer meet its external debt obligations and lacked sufficient foreign exchange for essential imports. The IMF arrived after the disaster rather than before it.

The present Extended Fund Facility subsequently provided an economic framework around which debt restructuring, revenue reform, monetary discipline and other changes could be organised. It also provided something equally important to a country that had defaulted: an external measure of credibility.

The seventh review has still not been completed. Recent discussions between the IMF and Sri Lankan authorities ended without a staff-level agreement, although talks are continuing.

The Fund has simultaneously acknowledged that the economy has shown considerable resilience, including growth of 4.2 percent in the second quarter and official reserves reaching US\$6.9 billion by the end of August.

That combination is worth examining carefully. Sri Lanka is recovering, but the institution overseeing the rescue programme is not yet prepared to sign off on the next review. The unfinished business includes medium-term revenue, energy pricing, capital expenditure and the continuing structural reforms required to make the recovery sustainable.

Eventually, however, the present programme will end. Whether Sri Lanka then seeks another arrangement, a precautionary facility or attempts to proceed without further IMF financial assistance will depend upon conditions at the time.

The more important issue is whether the country can retain economic discipline when that discipline no longer arrives attached to an IMF review.

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SRI LANKA'S IMF PROGRAMME...

Sri Lanka will still need sufficient government revenue. Debt will still have to be serviced, foreign exchange reserves maintained and state enterprises prevented from becoming unlimited claims upon taxpayers. A government cannot permanently spend substantially more than it collects merely because an IMF programme has expired.

This is where the next political argument is likely to begin. Economic stability is valuable, but stability that permanently places the burden upon people least able to afford it will eventually encounter resistance.

The Government therefore has to demonstrate that fiscal discipline and economic growth can translate into improving living standards rather than simply improving ratios on a spreadsheet.

The Middle East crisis has provided a useful warning about how quickly circumstances can change. Sri Lanka did not create the oil shock, yet higher petroleum prices have already affected inflation, the external account and the amount of foreign currency required for imports. El Niño, international trade disputes and geopolitical instability present additional risks over which Colombo has very little control.

That is precisely why reserves, manageable debt and responsible public finances matter. Economic buffers can appear unnecessarily conservative during good times and become invaluable the moment something goes wrong.

Sri Lanka has spent decades treating economic reform as something to be undertaken during a crisis and relaxed once the immediate danger has passed. That cycle helped produce the circumstances of 2022. The real test of the present recovery is therefore not whether Sri Lanka successfully completes an IMF programme.

It is whether, after the IMF programme ends, Sri Lanka can finally resist the temptation to need another rescue.

**THE RUPEE IS AROUND
330 TO THE DOLLAR. THE
NUMBER IS NOT THE
STORY.**

The Sri Lankan rupee is again trading around 330 to the US dollar as the country absorbs higher energy costs and renewed external uncertainty.

There is no reason for panic, but there is every reason to understand what is moving underneath the exchange rate.

Sri Lanka has traditionally treated the exchange rate as though it were a national scorecard.

A stronger rupee is presented as evidence that economic management is succeeding, while a weaker currency immediately becomes evidence for the opposite argument. Neither interpretation tells us very much without examining why the currency is moving.

The exchange rate is fundamentally a price. Sri Lanka requires dollars to purchase fuel, medicines, machinery,

food, vehicles, industrial inputs and thousands of other imports, while foreign currency enters through exports, tourism, workers' remittances, investment and borrowing. The balance between those flows ultimately influences what a dollar costs in rupees.

The Middle East has complicated that balance. Sri Lanka imports petroleum and higher international oil prices mean more dollars are required to purchase the same physical quantity of fuel. Shipping disruption, insurance costs and other consequences of the conflict can add further pressure even before a cargo reaches Colombo.

Import demand has also been recovering with the economy. Vehicle imports have returned, businesses are purchasing more inputs and economic normalisation naturally increases demand for foreign currency.

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That is not necessarily unhealthy. A recovering economy is supposed to import machinery, equipment and productive inputs, but those purchases still have to be financed.

Against this, Sri Lanka is earning substantial foreign exchange from workers' remittances and tourism while official reserves had reached approximately US\$6.9 billion by the end of August. That leaves the country in an incomparably stronger position than during 2022, when shortages of foreign currency became shortages of fuel, medicine and other essentials.

US\$6.9 billion is nevertheless a buffer rather than an inexhaustible bank account. The Central Bank can intervene to prevent disorderly movements in the currency market, but permanently defending an exchange rate that underlying economic conditions do not support eventually consumes reserves. Sri Lanka has already experienced the consequences of attempting that.

A moderate depreciation is therefore not automatically evidence of economic failure. What matters is whether the currency is adjusting to changing supply and demand in an

orderly market or coming under sustained pressure because the country's external position is deteriorating.

The rupee also matters because depreciation can feed directly into inflation. A product costing US\$100 requires Rs 32,000 when the dollar is Rs 320 and Rs 33,000 when it reaches Rs 330, even if the international price of the product has not changed. When the dollar price itself is also rising, as has happened with petroleum, the two effects compound each other.

That connects the exchange rate directly to the Central Bank's interest-rate decision. Inflation is already at 8 percent, oil remains expensive and the policy rate is being held at 8.75 percent while previous monetary tightening works through the economy. A sustained deterioration in the rupee would make that balancing exercise more difficult.

There is no single exchange rate at which Sri Lanka suddenly develops a problem. Rs 330 is not a magical boundary any more than Rs 320 was a guarantee of economic health. What matters is the direction of travel and the forces producing it.

Watch oil prices, imports, tourism receipts, remittances, Central Bank intervention and reserves. Taken together, they will tell us whether the present movement is an ordinary adjustment or something requiring more serious attention.

The question is therefore not why the dollar costs around Rs 330.

It is what Sri Lanka must spend, earn and borrow to keep it there.

**THE GOVERNMENT IS
SUBSIDISING FUEL.
SOMEBODY STILL HAS
TO PAY THE BILL.**

Sri Lanka has deliberately prevented the full international increase in fuel prices from reaching consumers, and the Central Bank says that has helped contain inflation. It probably has. But a subsidy does not make an expensive barrel of oil cheaper. It merely changes who pays for it, and when.

There is a wonderfully reassuring quality to the word subsidy. International oil prices rise sharply, the Government intervenes, the increase at the pump is restrained and the consumer is protected from the full impact. In the middle of a cost-of-living squeeze there are perfectly reasonable arguments for doing precisely that.

The Central Bank has now confirmed that the Government's fuel subsidy has helped contain inflation during the Middle East energy shock. Together with the surcharge imposed on vehicle imports, the measures have reduced some of the inflationary pressure that would otherwise have appeared more directly in consumer prices.

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GOVERNMENT IS SUBSIDISING...

That matters because fuel does not remain at the filling station. Diesel moves buses, lorries and machinery. Petrol moves cars, motorcycles and three-wheelers. Petroleum products enter industry, agriculture and distribution. Increase their prices sharply and the effect eventually appears in the cost of almost everything that has to be manufactured, transported or delivered.

There is therefore a perfectly respectable economic argument for cushioning a sudden external shock rather than allowing its entire impact to strike consumers immediately. Sri Lanka is emerging from several years in which real household incomes were severely damaged by inflation and taxation. Another violent increase in fuel prices would inevitably have reduced disposable income further.

The subsidy nevertheless creates an accounting question that cannot be wished away. If the international cost of petroleum is higher than the price being recovered domestically, somebody is absorbing the difference. It may be the Treasury, the Ceylon Petroleum Corporation or another part of the State, but eventually the cost belongs to the public finances.

The distinction is important because the consumer and the taxpayer are frequently the same person. A Government can prevent somebody paying another Rs 20 at the pump today, but if the resulting cost ultimately requires higher taxation, additional borrowing or reduced expenditure somewhere else, the economic burden has not disappeared. It has moved.

Sri Lanka has been here before. For decades administered prices were used to shield consumers from the real cost of electricity, fuel and other politically sensitive commodities. The resulting losses accumulated inside state enterprises until they eventually became obligations of the Government and, ultimately, the taxpayer.

That does not mean every subsidy is irresponsible. Governments everywhere intervene during exceptional circumstances, particularly when price shocks threaten vulnerable households or the wider economy. The more important questions are how large the subsidy is, how long it will continue and whether it is targeted towards those who actually require assistance.

A blanket fuel subsidy is inherently imprecise. The person driving a small motorcycle to work benefits from a lower fuel price, but so does the owner of a large luxury vehicle. The delivery van supporting a small business receives the benefit, but so does somebody consuming considerably more fuel simply because he can afford to.

Targeted assistance is administratively more difficult but economically more defensible. If the purpose is protecting lower-income households, public transport, fisheries, agriculture or other particularly exposed sectors, directing assistance towards them reduces the amount of public money required to subsidise everybody else.

There is another complication. A lower domestic fuel price can suppress measured inflation temporarily, which is useful when the Central Bank is trying to prevent inflation expectations from becoming entrenched. But if the subsidy is eventually withdrawn while international prices remain high, the delayed increase simply arrives later.

Sri Lanka therefore needs to distinguish between a bridge and a permanent road. A temporary subsidy carrying the economy across an exceptional energy shock can make sense. An indefinite subsidy that gradually becomes politically impossible to remove recreates precisely the pricing distortions the country spent the past several years trying to eliminate.

The Middle East crisis has confronted the Government with a genuine dilemma. Passing the full cost immediately to consumers risks worsening inflation and damaging household finances.

Absorbing it indefinitely risks weakening public finances and transferring today's petroleum bill into tomorrow's taxes or debt.

The Government has chosen, for now, to absorb part of the shock. The Central Bank says that decision has helped restrain inflation, and that is significant.

But the oil producer has still been paid. The only unanswered question is who in Sri Lanka eventually pays instead.

SRI LANKANS ARE BORROWING MORE. THE CENTRAL BANK NOW WANTS THEM TO BORROW A LITTLE LESS.

Private-sector credit grew rapidly as Sri Lanka emerged from economic crisis, providing businesses and households with money to spend and invest. It is now slowing after monetary tightening, but still growing at 24.5 percent. The more important question is not simply how much Sri Lanka is borrowing, but what all that borrowed money is buying.

Credit is one of those economic indicators capable of producing completely opposite interpretations depending upon when it is measured. When an economy is depressed and businesses refuse to borrow, weak credit growth can signal stagnation. When lending expands too quickly, the same indicator can become a warning about inflation, asset prices and future bad debts.

Sri Lanka has travelled remarkably quickly from one condition towards the other. Private-sector credit from licensed commercial banks expanded by approximately Rs 2.1 trillion during 2025, growing by 25.2 percent over the year. For six consecutive months during the second half of 2025, with the exception of December, monthly credit expansion exceeded Rs 200 billion.

That expansion was not accidental. Interest rates had fallen, economic activity was recovering and businesses and households were again sufficiently confident to borrow. Vehicle imports had resumed after restrictions were relaxed, creating another substantial source of demand for finance.

By early 2026 the expansion had become strong enough for the Central Bank to begin worrying about the other side of the equation.

Rapid credit growth increases spending power and can add to inflationary pressure, particularly when an economy is already confronting higher imported energy prices.

The Central Bank tightened monetary policy in May. Private-sector credit growth has subsequently slowed from around 30 percent several months ago to 24.5 percent year-on-year in August. The Bank's present view is that this slower rate of expansion remains sufficient to support economic growth.

That sounds reasonable. A country recovering from a severe contraction requires credit. Businesses need working capital, manufacturers need machinery, exporters need financing and entrepreneurs need money with which to expand. A functioning credit system is one of the mechanisms through which economic recovery becomes investment.

But Rs 1 borrowed for productive investment and Rs 1 borrowed for consumption are not economically identical.

Borrow money to purchase machinery that allows a company to produce more, employ additional workers or earn foreign currency and the debt may create the income required to repay itself.

Borrow money for an imported consumer asset and the economic effect can be rather different, particularly when the purchase simultaneously creates demand for foreign currency.

That is why the composition of Sri Lanka's credit expansion deserves as much attention as the headline growth rate.

Finance companies provide a particularly striking example. Their credit expanded by 52.4 percent year-on-year at the end of the first quarter of 2026, with vehicle-backed lending increasing 52.8 percent and gold-backed lending growing 69.2 percent.

Those are remarkable growth rates.

Vehicle financing is not inherently unproductive. A van can support a business, a truck moves goods and a car can be an essential working asset. Gold-backed lending can similarly finance a business or temporary cash-flow requirement rather than consumption.

The numbers nevertheless raise a question about where Sri Lanka's renewed appetite for debt is heading. An economy does not become more productive merely because more people have acquired loans.

What matters is whether the borrowed money increases the economy's capacity to generate income.

There is also a financial-stability issue. Lending can grow rapidly while bad-loan ratios appear to improve because the denominator itself is expanding. Problems generally become visible later, particularly after interest rates rise or economic conditions deteriorate.

Sri Lanka's banks remain well capitalised and the proportion of Stage 3 loans has fallen as the economy recovered. Finance companies have also

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SRI LANKANS ARE BORROWING...

maintained satisfactory liquidity and profitability, although the Central Bank has noted some moderation in capital adequacy and has already acted to restrain risks in vehicle and gold-backed lending.

The timing is important. Inflation has risen to 8 percent, interest rates were tightened in May and the Middle East crisis has introduced a new external shock. Credit that looked easily serviceable when rates were lower and economic conditions benign may feel different if household costs continue rising.

The Central Bank therefore appears to be attempting something rather delicate. It wants enough credit to sustain economic growth but not so much that lending itself becomes another source of inflation or financial instability.

That balance cannot be measured simply by celebrating a large credit number or worrying about a smaller one.

Sri Lanka needs credit.

What it needs rather more urgently is credit that creates something capable of repaying it.

RS 9.92 TRILLION. THAT IS THE NUMBER BEHIND THE 2027 BUDGET.

President Anura Kumara Dissanayake will present the 2027 Budget on November 12, but the first important numbers are already available. The Appropriation Bill provides for Rs 4.99 trillion in service expenditure and approximately another Rs 4.92 trillion already charged by law. Before the Budget promises begin, Sri Lanka should understand the size of the State it is financing.

Budget speeches are wonderful occasions for concentrating on the new. A tax is reduced, an allowance increased, a road promised, a welfare payment announced or several billion rupees allocated to something sufficiently attractive to earn applause in Parliament.

The considerably larger numbers already committed to keeping the State operating receive rather less excitement.

Sri Lanka's 2027 Appropriation Bill puts estimated service expenditure for ministries and departments at approximately Rs 4.99 trillion. Separately, approximately Rs 4.92 trillion is provided as statutory expenditure already charged to the Consolidated Fund under existing law.

Put the two together and the expenditure provided for approaches Rs 9.92 trillion.

That distinction is important because simply describing the 2027 Budget as Rs 4.99 trillion does not convey the full scale of public expenditure represented in the legislation. A substantial part of the State's financial obligations exists before the President stands up in Parliament on November 12.

The Bill also allows net outstanding Government borrowing during 2027 of up to Rs 3.8 trillion. Borrowing is not automatically evidence of fiscal irresponsibility, particularly when debt is refinanced or money is being raised for productive investment, but after Sri Lanka's sovereign default the scale and purpose of borrowing deserve rather more attention than they once received.

The individual allocations also reveal the Government's priorities before the Budget Speech provides the political narrative around them.

The Ministry of Finance, Planning and Economic Development receives the largest ministerial allocation at approximately Rs 856.9 billion.

Public Administration, Provincial Councils and Local Government receives around Rs 651 billion, while Health and Mass Media is allocated approximately Rs 590.5 billion.

Transport, Highways and Urban Development is allocated around Rs 500 billion, Defence approximately Rs 458 billion and Education, Higher Education and Vocational Education approximately Rs 328 billion. Those numbers will inevitably generate political arguments about whether one ministry receives too much and another too little.

The more useful question is what Sri Lanka receives for the money.

An allocation is not an achievement. Governments can announce billions for hospitals, schools, roads and development programmes, but the value lies in whether the money is actually spent efficiently and produces the intended result.

Sri Lanka has repeatedly experienced the peculiar combination of inadequate public services and substantial public expenditure.

The 2027 Budget also arrives at an awkward economic moment. Inflation has risen, the Middle East crisis has increased energy costs, the Government is subsidising fuel and the IMF's seventh review remains unfinished. At the same time, President Dissanayake has stated that there will be no property tax in 2027, despite earlier commitments made during Sri Lanka's economic reform programme.

Every concession therefore has to be reconciled with the revenue side of the Budget.

If a tax expected to produce revenue is postponed or abandoned, the money must either be found elsewhere, expenditure reduced or borrowing increased. There is no fourth column in public finance marked "somebody else's problem."

This Government also carries an unusual political advantage. With its commanding parliamentary majority, it does not face the numerical uncertainty that has paralysed weaker administrations attempting difficult fiscal reform. If it believes a measure is necessary, it has the parliamentary strength to legislate it.

That makes the 2027 Budget a particularly revealing test. The Government can no longer argue that reform is impossible because Parliament will not cooperate. It effectively controls Parliament.

The first reading of the Appropriation Bill takes place on October 7. The President delivers the Budget Speech on November 12, the second reading debate continues until November 20 and the Committee Stage runs from November 21 to December 14.

There will be plenty of speeches during those weeks.

Sri Lanka should perhaps concentrate on the numbers before listening to them.

Rs 9.92 trillion is a useful place to start.

LAUGFS HAS A NEW MAN AT THE TOP. WHAT EXACTLY IS HE BEING BROUGHT IN TO CHANGE?

Dhanusha Muthukumarana takes over today as Group Managing Director and Group Chief Executive Officer of LAUGFS Holdings. The company talks about transformation, operational excellence and sustainable growth. Those are impressive words. The more interesting question is what transformation actually means for a sprawling Sri Lankan group operating across more than 20 industries.

LAUGFS Holdings begins October with a significant change at the top, appointing Dhanusha Muthukumarana as Group Managing Director and Group Chief Executive Officer with effect from today.

He arrives with more than 26 years of experience spanning banking, consumer goods, manufacturing, healthcare, logistics, enterprise software, technology consulting and diversified businesses.

The appointment becomes more interesting when placed against the company he is being asked to lead.

LAUGFS began life in 1995 as Gas Auto Lanka but has developed into a diversified group employing more than 3,500 people and operating across oil and gas, renewable energy, industrial and engineering businesses, logistics, retail and consumer operations, healthcare and services.

Diversification can be a great strength. A business exposed to several industries is not entirely dependent upon the fortunes of one.

Cash generated in a mature operation can support investment in a growing business, while management expertise and infrastructure can sometimes be shared across the group.

Diversification can also become complexity. A conglomerate operating across more than 20 industries has to decide continually where capital produces the best return, which businesses deserve additional investment, which require restructuring and whether every operation still belongs inside the same group.



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That makes Muthukumarana's background particularly relevant. He is not arriving principally as an oil and gas executive.

Much of his career has been built around technology, enterprise architecture, business transformation and aligning operating systems with corporate strategy.

Before joining LAUGFS leadership he founded technology consultancy POTENZA and previously held senior technology positions at the London Stock Exchange Group, Hatton National Bank, Hemas Holdings, Microsoft and John Keells Holdings. LAUGFS itself describes his appointment in the language of transformation, innovation, operational excellence and long-term value creation.

The temptation with such appointments is to concentrate upon the biography. The more useful approach is to watch what happens next.

Does LAUGFS simplify parts of its portfolio? Does it invest more aggressively in businesses where it possesses a competitive advantage? Does technology substantially alter how the group manages customers, logistics, inventory and capital? Does renewable energy become more important inside the portfolio? Are underperforming operations restructured, sold or combined?

There is also a larger Sri Lankan corporate question here. Many of the country's diversified businesses grew by entering opportunities as they appeared, producing groups containing businesses that can sometimes have remarkably little relationship with each other. The next phase of corporate growth may require considerably more discipline about where scarce capital is deployed.



LAUGFS operates in areas directly exposed to some of Sri Lanka's largest economic changes. Energy security has again become a national issue because of the Middle East crisis. Renewable energy is expanding.

Consumer spending is recovering after the economic collapse. Logistics has become strategically important while digital technology is altering almost every conventional business model.

That gives the incoming chief executive plenty to work with.

It also gives him plenty to prove.

Corporate announcements invariably promise growth, transformation and value creation. Shareholders, employees and customers eventually require those words to become numbers.

The appointment takes effect today.

IS AMERICA'S SECURITY UMBRELLA OVER THE GULF BEGINNING TO CLOSE?

For decades the basic security calculation in the Gulf was remarkably simple. America provided the ultimate military guarantee and the Gulf states built their foreign policies around it. Seven months of war, Houthi attacks and America's withdrawal from Iraq are forcing the region to ask whether that guarantee still means what it once did.

Something important is happening in the Gulf, and it has relatively little to do with the daily movement of oil tankers through the Strait of Hormuz. Saudi Arabia, Qatar, the United Arab Emirates and their neighbours are beginning to reconsider one of the assumptions upon which the modern Gulf security system was built.

That assumption was America.

For decades the United States maintained an extraordinary military presence across the region. American forces, aircraft and naval assets operated from bases throughout the Gulf, while Washington's security relationships with Saudi Arabia, Qatar, Bahrain, Kuwait and the UAE provided an implicit understanding that serious external threats to those states would ultimately encounter American power.

That relationship has never been uncomplicated, but the fundamental bargain endured. The Gulf supplied an enormous proportion of the world's energy and America helped guarantee the security architecture within which that energy could move.

The events of 2026 have begun testing whether the bargain still operates in quite the same way.

The United States and Israel entered a conflict with Iran despite opposition from Gulf states that understood rather better than most where Iranian retaliation might land.

Saudi Arabia has subsequently faced repeated Houthi missile and drone attacks against cities and economically important infrastructure, while Gulf capitals have watched carefully to see how far Washington is prepared to become involved in their defence.

Now American forces have completed their withdrawal from Iraq.

None of this means America is abandoning the Middle East. The United States retains enormous military capabilities in and around the region and extensive security relationships with individual Gulf states. But governments do not construct national security policies around reassuring language.

They construct them around what they believe another country will actually do when something goes wrong.

The Gulf appears increasingly unwilling to rely upon a single answer.

Qatar has proposed something that would have sounded extraordinary not very long ago: a regional security architecture that includes Iran itself. The argument is straightforward. If every security arrangement is constructed against Iran, Tehran will perpetually regard the arrangement as a threat and the region remains trapped in a cycle of deterrence, retaliation and escalation.

At the same time, Saudi Arabia has moved in another direction by establishing a mutual defence arrangement with Turkey and Pakistan. The so-called Mecca Accord provides that an attack upon one of the three countries is treated as an attack upon all three.



That is a significant development. Turkey possesses one of the largest and most experienced armed forces in the region, while Pakistan is a nuclear-armed state with longstanding military relationships with Saudi Arabia. Riyadh is therefore building additional layers of security that do not depend exclusively upon Washington.

The UAE and Saudi Arabia are also talking again after a prolonged period of serious disagreement. That rapprochement may have many explanations, but it is occurring at precisely the moment when both countries are being forced to reconsider the regional security environment around them.

None of these arrangements is yet a substitute for American military power. Qatar's proposed architecture including Iran remains an idea rather than an established security system.

The Saudi-Turkey-Pakistan agreement has yet to demonstrate what mutual defence means when confronted by a real crisis, while European and Chinese involvement cannot presently replicate the depth of America's regional military capabilities.

But perhaps replacement is not what the Gulf is attempting.

Diversification may be.

Saudi Arabia does not need to choose between Washington and Islamabad. Qatar does not need to abandon its American relationship in order to speak to Tehran. The UAE can maintain Western defence relationships while rebuilding its relationship with Riyadh. Security, like investment, can be spread across several relationships rather than entrusted almost entirely to one.

That would represent a profound change.

The Gulf states spent much of the post-war period operating inside an American security order.

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Daily by Faraz



**“Questioning
The Answers”**



IS AMERICA'S SECURITY...

What now appears to be emerging is something considerably more complicated in which Washington remains enormously important but is no longer assumed to be the only ultimate guarantor.

For the rest of the world this is not merely a diplomatic curiosity. These are the countries sitting upon some of the planet's most important energy reserves and beside the shipping routes through which those resources reach international markets.

The Gulf's security architecture therefore affects the price of fuel in Colombo just as surely as it affects the calculations being made in Riyadh, Doha and Abu Dhabi.

The question is no longer whether America is leaving the Gulf. It isn't.

The more interesting question is whether the Gulf is learning how not to depend entirely upon America.

IRAN MADE AN OFFER. AMERICA HAS ANSWERED. NOW THE ARGUMENT IS ABOUT WHO MOVES FIRST.

Iran has received Washington's formal response to its latest proposal for ending the seven-month conflict and reopening the Strait of Hormuz. The contents have not been disclosed, but the diplomacy has moved beyond public insults. The obstacle now appears to be one of the oldest problems in diplomacy: neither side wants to surrender its leverage first.

For months the Strait of Hormuz has been simultaneously a shipping route, an economic weapon and a bargaining chip. Iran's ability to disrupt one of the world's most important energy corridors has imposed enormous costs far beyond the Middle East, while the American blockade and sanctions regime has imposed equally severe pressure upon Iran itself.

That mutual pain has finally produced something approaching a negotiating process.

Iran last week put forward a seven-day proposal under which it said the Strait of Hormuz could be reopened and normal maritime passage restored if Washington accepted a series of conditions. Those included lifting the American blockade of Iranian ports, easing restrictions on Iranian oil exports, releasing frozen Iranian assets and establishing a ceasefire framework.

The proposal also envisaged the resumption of negotiations over Iran's nuclear programme.

President Donald Trump publicly rejected the Iranian offer, describing it as unacceptable. It would have been reasonable at that point to conclude that the initiative was finished.

It wasn't.

Qatar continued carrying messages between Washington and Tehran, with Pakistan also involved in the diplomatic effort. Iranian Foreign Minister Abbas Araghchi subsequently received American feedback through Qatari mediators and returned to Tehran with Washington's response.

Iran has now formally acknowledged receiving it.

The contents remain undisclosed, which makes extravagant predictions particularly unhelpful. What is known is that the central disagreement appears to concern sequencing rather than simply whether the individual elements of an arrangement can be discussed.

That may sound procedural. It is actually the heart of the problem.

Iran wants relief from the economic pressure being imposed by the United States before surrendering its principal leverage over international shipping. Washington wants the Strait reopened and Iranian concessions secured before giving up the pressure that brought Tehran to the negotiating table.

Both positions make perfect strategic sense.

They are also mutually incompatible unless somebody moves first or both sides move together.

This is why a phased agreement has become increasingly important. Instead of requiring one side to surrender its leverage in advance, Washington and Tehran could take reciprocal steps according to an agreed timetable. Iran could progressively restore maritime passage while the United States simultaneously relaxed specified elements of its blockade and sanctions.

The seven-day proposal attempts to create precisely that sequence. The attraction is that each side receives something while retaining sufficient leverage to respond if the other fails to perform.

There is precedent for caution. An earlier understanding reached in June produced only a brief ceasefire before the conflict resumed. Neither side therefore enters the present negotiations with much reason to trust the other.

There is also considerable domestic politics involved.

Iran's economy has been badly damaged by war, sanctions and the American blockade, creating powerful incentives for Tehran to obtain relief. But Iranian leaders must avoid appearing to capitulate after months of conflict and considerable national sacrifice.

President Trump faces his own political calculations. Allowing Iran significant sanctions relief without obtaining visible concessions would be attacked domestically as rewarding Tehran.

The administration has simultaneously continued imposing additional sanctions even while diplomatic messages have been travelling between the two governments.

That combination of negotiation and pressure is not contradictory. It is how coercive diplomacy frequently works.

Each side is attempting to improve the agreement available at the table by making the alternative to agreement sufficiently unpleasant.

The involvement of Qatar may consequently prove critical. Doha has relationships that allow it to communicate with parties that often cannot communicate effectively with each other.

Pakistan provides another channel and carries particular significance because of its developing security relationship with Saudi Arabia and Turkey.

The Gulf states have an enormous interest in making the negotiations work. They opposed the escalation into war, have suffered attacks and disruption themselves and have watched the world's most important energy-producing region become increasingly difficult and expensive to operate.

Sri Lanka has an interest too.

Every additional week of instability around Hormuz affects oil prices, freight, insurance and eventually the cost of living thousands of kilometres away.

There is still no peace agreement. There is not even evidence yet that Washington and Tehran have accepted the same negotiating formula.

But there is something that did not exist several days ago.

An Iranian proposal went to Washington. Washington answered. And Tehran is considering the answer. After seven months of war, even that is movement.

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THE DAILY BY FARAZ
QUESTIONING THE ANSWERS

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