NEWS ROUND UP

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Germany calls for more transparency in SL as bilateral ties expand

Amidst growing bilateral ties, Germany is calling for improved efficiency and transparency in Sri Lanka to achieve a more robust and win-win partnership.

"Germany's footprint in Sri Lanka and vice versa have been growing, resulting in greater bilateral cooperation," German Ambassador in Sri Lanka Jörn Rohde told Daily FT, adding that in recent years, the German Foreign Minister visited Sri Lanka followed by a State visit to Germany by President Maithripala Sirisena in 2016.

"There have been high level visits during the past three years. Besides that, we have taken concrete steps to increase Germany's footprint in Sri Lanka whilst Sri Lanka too has made greater inroads. Our relations and initiatives have been mutually beneficial," the Ambassador emphasised.

In the first half of this year, there will be a host of Sri Lanka-German private sector interactions by way of top-level business and industry delegations visiting each other. Sectors include apparel, rubber, renewable energy, agriculture, furniture and interior, transportation and logistics, and IT.

Achieving a major milestone towards enhancing economic ties, Germany opened a fully-fledged trade office in Colombo last year. "It professionalises the trade relations," he explained.

"This is a proactive office which also has a German Chamber of Commerce desk. The Embassy with limited personnel resources could not have achieved this professional level in trade and business promotion and facilitation alone, but this office manned by dedicated and focused professionals can do so," he said.

Bilateral trade is a record € 1 billion plus which is a 10% growth. Sri Lanka's return to the EU GSP-Plus program as well as exchange of trade delegation were key contributors to the increase. He said that Sri Lanka's exports to Germany had enjoyed double-digit growth regularly, which was a good sign. The Trade Office will further help this momentum though global trade is facing headwinds.

Noting that Sri Lanka had an extraordinary year in 2018, especially with the state of emergency in the first and the Constitutional crisis in the last quarter, he said that this impacted the economy with faster fall of the rupee, a dip in tourist bookings and a revision in Sovereign Ratings.

"Since the reinstatement of the Prime Minister Ranil Wickremesinghe and the Government, we see greater stability and renewed positive international interest. We also welcome the announced recommencement of the IMF program with the Government," he said.

The German Ambassador said Sri Lanka continued to face many challenges – political, social and economic, hence the need to remain dynamic in addressing those challenges.

"In my view, the most important challenge is to regain investor confidence, for which greater political stability and faster reforms process are key factors. For the latter, the IMF program is helpful and Sri Lanka needs to modernise its economy with much-needed reforms," he said.

"Sri Lanka must further open up its economy to foreign companies, especially shipping and freight forwarding. The restriction on foreign ownership to 40% in this sector should be immediately removed as it has been done by many other competing and progressive nations in the region," he stressed.

According to him, Sri Lanka's strategic geographic location enhances the potential to be a maritime hub and this advantage can be maximised and realised faster via liberalisation and not protecting vested

local interest. If Sri Lanka fails to open up, other competing nations stand to gain and it will be Sri Lanka's loss of opportunity.

"Past liberalisation measures in the shipping sector have been beneficial and propelled Sri Lanka to be a popular port and brought in much-needed foreign investment in the development of container terminals. To remain competitive, the challenge is to complete the liberalisation process by allowing foreign investments into shipping and freight forwarding activities," he said.

"In that context I don't see any economic sense in limiting foreign ownership. Instead, the failure to liberalise sends wrong signals to the international business community and suggests that it is not serious in modernising the economy," Ambassador Rohde added.

Another key challenge for Sri Lanka is corruption, which can be addressed by ensuring greater transparency and accountability, especially in the procurement and tender practices.

"Corruption and lack of transparency dampens investor confidence. Tender procedures must be clear and transparent and concluded without delay," Rohde emphasised.

Macroeconomic crisis in Oct-Dec. quarter triggers Rs. 327 m loss at Softlogic

A macroeconomic crisis-filled third quarter October to December 2018 has triggered a Rs. 327 million loss at Softlogic Holdings PLC, as against a profit of Rs. 953 million a year earlier, whilst for the first nine months the Group post-tax profit managed a 29% gain to cross Rs. 2 billion mark.

Softlogic Chairman Ashok Pathirage said the Group's operating environment in the third quarter of FY19 was assailed by the sudden and steep depreciation of the rupee, particularly, affecting the retail imports and the leisure sector which has dollar-denominated borrowings. Furthermore, the 100% cash margin imposition, which affected the retail imports, and 200% margin for motor vehicles and motorbikes, disrupted cashflow timings leading to increased working capital requirements.

"This coupled with increasing interest rates triggered by poor market liquidity and rising Fed rates impacted cost of financing for the Group which dampened the quarter's performance," he said.

"Group diversity, scale of operations, and financial adaptability, however helped weather these macroeconomic shocks to a greater extent," he added.

Group revenue grew 8.4% to Rs. 53.6 billion during the first nine months of this financial year while quarterly revenue grew 7.5% to Rs. 19.7 billion.

Group's core sectors which includes Retail (51% contribution to Group topline), Financial Services (19%) and Healthcare Services (18%) emerged as strong contributors to Group performance, while its non-core operations – IT, Leisure and Automobile – together made up 12% of Group topline.

Net profit attributable to holders of the parent however was down by 6% to Rs. 75 million in the first nine months, whilst for the third quarter it was a loss of Rs. 346.6 million as against a profit of Rs. 77 million a year earlier. In FY18, Softlogic's bottom-line was Rs. 204.2 million.

Gross Profit increased 11.2% to Rs. 19.6 billion during the 1-3QFY19, indicating improvements in GP margin from 35.7% in 1-3QFY18 to 36.6% in 1-3QFY19. The quarter also witnessed GP margin improvements from 35.3% in 3QFY18 to 37.7% in 3QFY19 to report a Gross Profit of Rs. 7.4 billion (up 14.8%).

Distribution expenses increased marginally to Rs. 944 million (up 2.8%) during the three months under review. However, the cumulative period reported a marginal decline in distribution expenses to Rs. 2.5 billion (down 0.7%). Administrative expenses increased 21.3% to Rs. 11.9 billion during the nine months while an increase of 38.7% to Rs. 4.8 billion was noted for the quarter. This increase in administrative expenses is led by the Group's increase in headcount, lease rentals and depreciation for strategic expansions. Consequently, cumulative operational cost margins edged up to 26.8% in 1-3QFY19 from 24.9% in the comparative period. Quarterly operational cost margin also witnessed an increase of 28.9% (23.7% in 3QFY18).

Other operating income declined 63.4% to Rs. 578 million during 1-3QFY19 (Rs. 1.5 billion in 1-3QFY18) while the quarter also witnessed a decline of 72.1% to Rs. 201 million. This decline primarily emerged from Asiri Group, which reported a one-off gain in the comparative period.

Cumulative Group EBITDA was Rs. 7.9 billion while quarterly EBITDA touched Rs 2.7 billion. Cumulative operating profit amounted to Rs. 5.8 billion while the quarterly operating profit reached Rs. 1.9 billion.

Softlogic Life Insurance PLC's investment portfolio is the prime contributor to Group's finance income which reported Rs. 872 million for the nine months under review while an increase of 36.6% to Rs. 421 million was reported during the quarter.

Group foreign exchange losses for the period amounted to Rs. 335 million. This was particularly in the aftermath of the rupee depreciation in the retail and leisure sector.

Net finance expenses increased 15.7% to Rs. 1.5 billion during the quarter while the cumulative period witnessed a marginal increase of 7.5% to Rs. 3.8 billion. A transfer of Rs. 1.5 billion to insurance policyholders was witnessed during the cumulative period as opposed to Rs. 1.3 billion in 1-3QFY18 while the quarter witnessed a change in insurance contract liabilities of Rs. 645 million (Rs. 455 million in 3QFY18).

Commenting on the future outlook, Chairman Pathirage said although these are challenging times, the Group expansion plans in core sectors will continue as "we are optimistic about future consumer demand."

"Sri Lankans are becoming more sophisticated and are aware of modern global lifestyle changes, and hence continued demand for premium brands is expected to grow in conjunction with the tourist influx," he added.

With this in mind, Softlogic is making every effort to improve Group synergy, with a view to focus on cost-discipline, and plans are afoot to buff equity at subsidiary levels to support expansion plans.

"With the stabilising of the Rupee at these levels, we expect the Group to consolidate its efforts with a view to enhance the existing synergies. We believe that Government policies would be calibrated to inspire the country towards becoming a tourist shopping destination given its strategic location," Chairman Pathirage added.

Following is his review of the performance of core verticals.

Retail

Cumulative revenue of the retail sector grew 2% to Rs. 27.4 billion while the quarter reported a topline of Rs. 9.7 billion. This import-oriented sector was impacted by the depreciation of the Rupee (LKR/USD increased from Rs. 155.97 as at 29 March 2018 to Rs. 182.75 as at 31 December 2018). This sector was

also clouded by various other macro-economic challenges including 100% cash margin imposition on imports of selected durables and other import restrictions on footwear and apparel. Tourist shopping, brand-conscious customers, accelerated migration of population to urban regions are the core drivers of upmarket retail trade in Sri Lanka. Our retail outlets at Colombo City Centre received strong customer response. As we are probably the only retailer with over 100 international retail brands, our presence as anchor tenants in the upcoming malls have become essential for a shopping mall's value proposition for success. It is noteworthy that our calculated expansion of fashion and retail stores has not cannibalised revenue growth at our other existing stores.

We will be occupying around 110,000 sq. ft. at One Galle Face by Shangri La. We will be retailing Odel, Armani Exchange, Diesel, Love Moschino, Mango, Body Shop, Furla, Tommy Hilfiger, Mothercare, Toy Store, Charles & Keith, Aldo, Hallmark, Swarovski, Longines, Tissot, Adidas, Nike, Yamamy, Cotton Collection, Sketchers and Guess at this mall which is expected to open in June.

Consumer Electronics business has an islandwide network of 211 stores with the latest store being opened in Kegalle in December.

We now have a total retail space of 325,500 sq. ft. in the Consumer Electronics business. The expansion strategy of this segment now focuses on 'Softlogic Max' and larger company-managed stores in prime cities and towns. These stores now retail a range of furniture manufactured in-house and fitness equipment in addition to top-of-the-line TVs, electric appliances, phones and computers.

Performance of Samsung and Nokia business progressed amidst numerous systemic challenges.

Our supermarket outlet, 'Softlogic Glomark', in Delkanda has attracted positive customer response with the outlet performance exceeding expectations. We will be opening in Kottawa, Mount Lavinia, Colombo 7, Negombo and Malabe. An essential outlet concept of around 2,000-3,000 sq. ft. is being developed to be set up at Asiri Central, Asiri Kandy, Orion City and in Kurunegala.

Sector's operating profit was Rs. 2.2 billion during 1-3QFY19 while the quarter reported an operating profit of Rs. 624 million. Sector EBITDA was Rs. 2.8 billion for the cumulative period while Rs. 836 million was reported during the quarter. Sector PAT for the cumulative period was Rs. 181 million.

Healthcare Services

Performance of Asiri Group continued on a positive note as the hospital chain awaits the opening of its 190-bed multi-specialty facility in Kandy soon. This facility will provide a range of state-of-the-art medical solutions which would be the first for the region.

Asiri Health revenues steadily increased 10% to Rs. 9.9 billion during 1-3QFY19 while the quarter reported a topline of Rs. 3.4 billion (up 12.9%). The revenue was led by Central Hospital Ltd., (36.5% contribution), followed by Asiri Hospital Holdings PLC (30.7%) and Asiri Surgical Hospital PLC (25.6%). Sector's operating profit declined 14.1% to Rs. 2.4 billion during the cumulative period while the quarterly operating earnings reported Rs. 825 million (down 35.5%). This decline is attributable to one-off gain reported in the comparative period.

Sector EBITDA was Rs. 3 billion during the period under review with the quarter reporting an EBITDA of Rs.1 billion. Asiri's profitability for the period was Rs. 1.3 billion while the quarter registered a PAT of Rs. 443 million.

Information Technology

IT sector, which now comprises the B2B IT solutions business, saw its revenue for the cumulative period improving 12.3% to Rs. 2.9 billion while the quarter reported revenues of Rs. 1.1 billion. Quarterly operating earnings increased 38.7% to Rs. 89 million taking cumulative operating earnings to Rs. 208 million (up 42.5%). EBITDA of the sector moved up 52% to Rs. 108 million for the quarter while cumulative EBITDA reported a 31.3% growth to Rs. 266 million. Sector PBT was Rs. 54 million for the cumulative period while the quarter reported Rs. 18 million PBT. The sector concluded the nine months with a PAT of Rs. 41 million.

Financial Services

Financial Services witnessed a topline growth of 24.1% to Rs. 10 billion during 1-3QFY19 as the quarterly revenue also improved 23.4% to Rs. 3.6 billion. Cumulative Operating profit was Rs. 1.4 billion while the quarter reported an operating profit of Rs. 521 million. Sector PBT for the quarter was Rs. 148 million while cumulative PBT reached Rs. 387 million. PAT of the sector registered a 160.2% growth to Rs. 2.6 billion during 1-3QFY19 while the quarter reported a profitability of Rs. 171 million.

Softlogic Life Insurance holds the status as the fastest growing life-insurance company in Sri Lanka with Gross Premiums reaching Rs. 10 billion (up 32%) for its financial year 2018. The Company has produced a 6-year CAGR of 30.4%, consistently more than doubling the industry growth. Global Insurance Fund, Leapfrog Investments, purchased shares from FMO who previously held 19% of the company since 2012. This transaction which was over Rs. 2 billion was executed at a substantial premium to market.

Significant flows from foreign clients and local high net-worth clients enabled Softlogic Stockbrokers to retain its position as the No; 2 player in the Industry despite lacklustre market conditions.

Softlogic Capital has commenced an initiative that will target Portfolio Management, Equity and Debt Capital Markets, Research and Corporate Advisory to address the vast market potential that is expected in the near future. Softlogic Finance's assets was Rs. 22.5 billion as at 31 December 2018 while Customer Deposits was Rs. 16 billion. The uptick in interest rates has made credit more expensive, while restrictions on motor vehicle imports has dampened business zeal in this respect with several hurdles evident for the RFC.

Automobile

Automobile sector generated revenues of Rs.1.5 billion (up 21.9%) during the nine months of financial year end 2019. A contract to supply ambulances to the Ministry of Health, the delivery of which was completed in February.

Suzuki Motors is capitalising on Group's financial strength and existing distribution infrastructure to support its aggressive expansion phase. The company now has 70 dealers (26 dealers at time of acquisition in 2017).

Leisure and Real Estate

Leisure sector topline increased to Rs. 1.9 billion (up 11.3%) during 1-3QFY19. Quarterly revenue rose 12.9% to Rs. 769 million in 3QFY19. Centara emerged to be the key contributor to the sector while Mövenpick is yet to contribute to earnings. Mövenpick's performance was affected by unrealised forex losses resulting from the hotel's dollar-denominated borrowings.

Japan's Odakyu Group partners TAD Group for Rs. 4.5 b investment in Sri Lanka

One of the largest conglomerates operating in a multitude of mandates in Transport, Real Estate and Retail in Japan; the Odakyu Group together with its consortium partners Stasia Capital and UDS, is no stranger to grand ventures. For the first time in its illustrious 70-year history, it reaches far beyond Japan as it establishes its first offshore partnership in Sri Lanka.

TAD Group Founding Directors Dhanuka Samarasinghe, Atheeq Ansar and Toshiaki Tanaka

Enabling this historic venture is the TAD Group, a multifaceted conglomerate in its own right, operating in Sri Lanka. With ongoing mandates engaging numerous partners in the Property, Energy and Investment sectors in the country, the exclusive Odakyu-TAD partnership brings in an expected investment of Rs. 4.5 billion with a number of significant further investment mandates to bolster the Sri Lankan economy over the upcoming years.

The Odakyu Group operates as a diversified conglomerate with interests in transport, real estate, merchandising and hospitality. One of its most significant ventures is the Odakyu Railway Line. Operating a number of these across Japan, the line bridging the Tokyo Central Business District (CBD) and Kanagawa alone sees over two million passengers daily. To put that in perspective, Sri Lanka sees an influx of around two million visitors to the country annually.

Spread across 44 subsidiaries and generating annual revenues in excess of $ 4.6 billion, one of the pioneering drivers of Odakyu's powerhouse success in Japan lies in its unique model of diversification. UDS, a fully owned subsidiary of the Odakyu Group, is a renowned end-to-end property solutions provider that has mastered the development and fulfilment of star class award-winning properties in South Asia. Its services reach out from business planning and architectural design to commercial operations.

This, coupled with the UDS drive for innovation and knowhow, extends beyond ownership and into partnerships, much like that of TAD Group. Stasia Capital, a global real estate management and consulting firm, is another such partnership that Odakyu has leveraged upon. Together, this innovative trifecta of partnerships hope to create a renewed era of growth and leadership in the Sri Lankan economy.

The TAD Group prides itself on being one of a handful of end-to-end facilitators for FDIs in Sri Lanka. With interests in property, energy, retail and investments, TAD has disrupted many industries in its wake. Headed by a dynamic trio at the helm and powered by a versatile team of professionals in a multitude of industries, TAD is poised to expand exponentially with the advent of renewed interest in Sri Lanka as a 'hub' for investment and development.

Securing yet another first, the exclusive partnership with Odakyu is not only the latest in the TAD Group's efforts to bring in world-class investments to the country, but also one of the largest Japanese companies to invest in Sri Lanka.

Govt. to resume shipping links between Kankasanthurai and Talaimannar

Work has started on re-establishing transportation of goods and people from Kankasanthurai (KKS) and Talaimannar to ports in South India, the Prime Minister's Office said yesterday.

Upgrading KKS Harbour has already started with work being observed by Prime Minister Ranil Wickremesinghe during a recent visit. Plans to upgrade the jetty at Talaimannar has already been made and work on it will be started soon by the Sri Lanka Ports Authority (SLPA), the Prime Minister's Office said in a statement.

"Once transport by sea is re-established, efforts will be made to link passenger and goods services with rail services in South India. This step will be taken by the Transport Ministry. Before the war, such links existed with a passenger able to cross between the two countries with one ticket," the statement said.

With the resumption of these services, it would be possible for Buddhists to undertake pilgrimages to India at lower cost.

The Government has already started implementation of a $45.27 million development project for the KKS Harbour. In addition to the general upgrade, a new 167m jetty will also be constructed for commercial purposes. A new breakwater will also be built under the project. The funds for the project have been obtained under preferential basis from the Indian Government.

The KKS cement factory also is to be reconstructed under this effort. The SLPA has already begun initial work on a 15-acre area within the KKS harbour premises, and it is expected to be expanded to a 50-acre area in the next phase. Under the mixed development projects, there are plans to establish tourist hotels and create a tourism zone. Similar plans are afoot for Talaimannar as well to develop tourism in the region.

Govt. and IMF begin talks for new staff level agreement

A delegation from the International Monetary Fund (IMF) has been engaged in discussions with top officials this week on reaching a staff level agreement on continuing the $1.5 billion Extended Fund Facility (EFF).

The delegation arrived in Colombo last Thursday, and has already had meetings with officials from both the Central Bank and Finance Ministry. Finance Minister Mangala Samaraweera and Central Bank Governor Dr. Indrajit Coomaraswamy, along with other top officials, participated in the meetings. Prime Minister Ranil Wickremesinghe is also expected to meet the delegation.

During the talks, the two sides discussed the possibility of taking forward the EFF, which was suspended last year following the constitutional crisis.

"The Government is considering enhancing the program and possibly expanding it to have a higher disbursement, but such a move could come with new structural goals," a top source at the Finance Ministry told Daily FT. The IMF and the Government are expected to release a statement outlining the particulars of a new staff level agreement over the next few weeks.

The IMF has disbursed over $ 1 billion out of a $ 1.5 billion three-year EFF loan it had agreed in 2016. Central Bank Governor Dr. Indrajit Coomaraswamy in the first week of January said the Sri Lankan Government has the option of extending the three-year program, which is scheduled to end in June, by one year, and also enhance the funding limit.

The International Monetary Fund had approved a three-year extended arrangement on 3June 2016, in the amount of about $ 1.5 billion in six instalments. The 5th instalment of this loan facility was scheduled to be given in November last year.

The IMF and the Government had reached a staff level agreement just hours before President Maithripala Sirisena appointed Opposition Leader Mahinda Rajapaksa as Prime Minister, triggering the constitutional crisis.

Economists have pointed out that it is important for the Government to put the IMF program back on track, to boost confidence in international capital markets before it seeks to raise as much as $2 billion from international sovereign bonds, as well as panda and samurai bonds. The Government last month approved the Central Bank issuing bonds to raise up to $2 billion dollars, to finance $5.9 billion in debt for 2019. The Central Bank is expected to go to the markets as soon as possible to raise the funds.

Rs. 15 b from AFD for waste water disposal project

A loan agreement was signed between the Government of Sri Lanka and Agency for French Development (AFD) for a Rs. 15 billion waste water disposal project in Ratmalana and Moratuwa yesterday.

The financing agreement was signed by Finance and Mass Media Ministry Secretary Dr. R. H. S. Samaratunga and AFD Country Director Martin Parent, in the presence of Ambassador of France for Sri Lanka and the Maldives Eric Lavertu at the Ministry of Finance and Mass Media.

The Ratmalana/Moratuwa Wastewater Disposal Project aims at improving access to the sewerage service for 45,000 residents of Ratmalana and Moratuwa. It will include significant extensions of the sewerage network and more than 10,000 domestic, commercial and industrial connections. Sewage will be treated by the existing Ratmalana wastewater treatment plant.

In order to enhance the expected positive impacts, the project will include information, education and communication campaigns to promote sanitation and hygiene.

The National Water Supply and Drainage Board (NWSDB) will implement the project over a period of five to six years. NWSDB already prepared the project design with the support of an AFD-financed Engineering Consultant.

Blue Economy is key for Sri Lanka, being an island. Blue Economy is a major source of foreign currency, jobs but also food security. It is also a challenge for the environment and the sustainability itself of its strong potential. As many as 70% of the 2.2 million tourists and four million expected by 2020 are focusing on the coastline, AFD said in a statement.

Furthermore, today more than three million inhabitants live less than a kilometre away from the coast. In that context, projects like this AFD-funded project, which will mitigate negative impacts of human activities (water pollution above all) while enhancing Blue Economy potential are very important for Sri Lanka's development.