NEWS ROUND UP

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SL could face refinancing risks over next 5 years: Moody's

- Rating agency says credit profile dominated by higher exposure to refinancing risk
- Could face tougher borrowing conditions, weaker debt affordability
- Negative outlook signals upgrade unlikely
- Advocates build-up of non-debt foreign exchange inflows, better liability management, fiscal reforms
- Warns deviation from fiscal consolidation and lack of monetary policy independence could prompt downgrade

Due to significant debt repayments from 2019, Moody's Investor Services yesterday warned Sri Lanka remained exposed to higher external refinancing risk over the next five years, particularly if external financing conditions tighten and the currency depreciates.

The credit profile of Sri Lanka (B1 negative) is supported by the authorities' progress in implementing their reform program, which entails fiscal consolidation and a build-up of foreign exchange reserves, the agency said.

Sri Lanka also benefits from moderate per capita income levels and stronger institutions than those of many similarly-rated sovereigns. Credit challenges include high Government debt, very low debt affordability and a fragile external payments position. Under its International Monetary Fund (IMF) Extended Fund Facility (EFF) program, the Government is committed to broadening and deepening its revenue base, strengthening the credibility and effectiveness of monetary policy, implementing liability management strategies, and pursuing legislation that ensures deficit and debt consolidation efforts endure after the program ends in June 2019.

"The Negative Outlook on the sovereign rating reflects our view that Sri Lanka's credit profile is dominated by the Government's and country's elevated exposure to refinancing risk. Sri Lanka could face significantly tighter external refinancing conditions during the next five years, which would quickly lead to much weaker debt affordability, especially if the currency were to depreciate at the same time," Moody's said in its annual credit analysis.

"The Negative Outlook signals that an upgrade is unlikely. We would consider returning the Outlook to Stable should we conclude external and domestic refinancing risks were likely to diminish.

That conclusion could be prompted by a faster and more sustained build-up of non-debt-creating foreign exchange inflows than we currently expect, the demonstrated effectiveness of liability management strategies to smooth and lengthen maturity payments and, over time, significant fiscal reforms that markedly improve fiscal strength."

Moody's said the agency would consider downgrading the rating if they were to conclude external and domestic refinancing capacity would not improve, and Sri Lanka was likely to face difficulties in refinancing its domestic or external debt affordably.

Evidence that the implementation of key policies – including further fiscal consolidation, monetary policy independence from fiscal developments, and the diversification of financing sources or liability management – is not effective would likely negatively affect Sri Lanka's access to and cost of finance.

A marked weakening in reserve adequacy from already low levels, and a halt or reversal in fiscal consolidation that raised the prospect of higher Government debt and prevented the expected decline in gross borrowing requirements could also prompt a downgrade.

This credit analysis elaborates on Sri Lanka's credit profile in terms of economic strength, institutional strength, fiscal strength and susceptibility to event risk, which are the four main analytic factors in Moody's Sovereign Bond Rating Methodology.
(DailyFt)

Trade Adjustment Programme draft released by Ministry

- Ministry posts document on website for stakeholder feedback
- Details sweeping proposals, setting up Trade and Productivity Commission and Competitiveness Councils
- Labour law changes, Fin. Min. unit to arbiter TAP, countrywide retraining and job placement hubs
- Suggests accelerated investment program for emerging sectors

The International Trade and Development Strategies Ministry has released an outline for implementing the long-awaited Trade Adjustment Programme (TAP) for stakeholder feedback that details how domestic enterprises would be supported through regulatory and policy reforms as well as specific schemes of grant support.

The document, which has been posted on the ministry website, is open to private sector and other responses till Thursday. TAP aims to provide comprehensive assistance for firms and workers and institutional mechanisms to ensure transparent, credible and timely delivery of trade adjustment assistance.

It is focused on data-driven decisions, making use of analytical tools to assess vulnerable industry sectors, a skills retraining and labour market flexibility program alongside tariff liberalisation, mechanisms for industry sectors to reveal their productivity constraints and have them resolved, and clear communication to stakeholders of the why, what and how of TAP, the document said.

The draft said a Trade and Productivity Commission (TPC) would be established to be the independent body that analyses TAP, that examines quantitative and qualitative evidence, investigates and responds to industry requests on tariff phase out, monitors the recommendations from the Industry Competitiveness Councils (ICCs) that are established to solve productivity constraints of affected sectors and make recommendations to the Ministry of Finance for action.

The TPC will consist of independent Commissioners (possibly appointed by the Constitutional Council) and accountable to Parliament, supported by a Secretariat of qualified professionals who are competent in trade and industry economics (initially can be seconded from the Department of Commerce and Central Bank).

“A new unit at the Ministry of Finance will be the ultimate arbiter of TAP and would be headed by the Secretary to the Treasury who will take final decisions regarding TAP matters, following the recommendation of the TPC. For example, taking the final decision to slow the tariff phase out for a particular sector, following the investigation and recommendation by TPC,” it said.

In both of the above submissions received by industry sectors, the recommendations by the TPC and the decisions by the Ministry of Finance and their justification will be published online and available for anyone to see to ensure transparency and credibility. TPC hearings on particular sectors’ submissions and representations can be open to the public to ensure further transparency and mark a departure from the typical industry lobbying process.

TAP proposes to establish Industry Competitiveness Councils (ICCs) as and when required to reveal and resolve productivity constraints faced by firms in an industry or sector. This will help build confidence among the industry that although the trade liberalisation will impact them and take them out of their comfort zone, the Government is able to help them navigate this process and find solutions to their problems, it said.

Recommendations given below were also included:

Implement a minimum level of labour market flexibility reforms in order to allow workers in affected sectors to move into new sectors and adjust better to new market conditions.

Establish a network of TAP-approved skills retraining centers and job placement hubs across the country (from within the established government TVET institutions and agencies) which will be primarily tasked with helping impacted workers obtain the new skills they need to move to another sector or find new job openings. As part of TAP, the Sri Lankan Government will cover part of the costs of skills retraining for TL-affected workers.

Launch an accelerated program of investment promotion in emerging sectors (for example, the National Export Strategy sectors) in order to boost new opportunities for job creation and absorb displaced workers from sectors previously enjoying high protection and now facing a decline due to trade liberalisation.

Identify some key indicators to keep track on an ongoing basis (e.g. every quarter or biannually) to identify early signs of socioeconomic stress due to trade liberalisation, either in specific demographic groups or in geographic locations. The National Planning Department is to be mandated to produce a quarterly or bi-annual report on these indicators (and can be tabled for the Cabinet of Ministers) and flag any concerns. (DailyFt)

Secondary bond market remains active as yields fluctuate

The secondary bond market remained active during the week ending yesterday, with yields initially decreasing towards the early part of the week prior to bouncing back up towards the later part.

The yields of the liquid 01.03.21 and 15.03.23 maturities were seen decreasing to weekly lows of 9.42% and 9.81%, respectively, against its previous weeks closing levels of 9.47/53 and 9.80/88. This downward trend was well-supported by the considerable decrease in the weighted average yields of the 15.07.23

maturity by 60 basis points and the 15.03.28 maturity by 52 basis points, at the bond auction held on 13 August when compared against previously recorded average yields of similar maturities, as well as the decrease in yields at the weekly Treasury bill auction.

However, global uncertainty coupled with profit taking resulted in yields increasing once again towards the latter part of the week to hit highs of 9.50% and 10.00%, to close marginally higher than the previous week. Activity was also witnessed consisting of the 2019's (i.e. 01.07.19 and 15.09.19), 2020's (i.e. 01.05.20 and 15.12.20), 2021's (i.e. 01.05.21, 01.08.21, 15.10.21 and 15.12.21), 15.07.23 and 15.03.28 maturities, within the range of 9.04% to 9.10%, 9.25% to 9.35%, 9.46% to 9.80%, 9.87% to 9.98% and 10.20% to 10.30%, respectively.

Meanwhile, the foreign holding of rupee bonds continued to decrease for a sixteenth consecutive week with an outflow of Rs. 0.8 billion during the week ending 15 August.

The daily secondary market Treasury bond/bill transacted volume through the first four days of the week averaged Rs. 15.98 billion.

In money markets, the Open Market Operations (OMO) Department of the Central Bank, started to drain out liquidity by way of overnight repo auctions, at a weighted average yield ranging from 7.52% to 7.62% as the net liquidity surplus in the system stood at Rs. 45.22 billion on average per day. The overnight call money and repo rates averaged 7.94% and 7.91% respectively during the week.

Rupee dips to a low of Rs. 160.55

The USD/LKR rate on spot contracts depreciated during the week to a low of Rs. 160.55 and closed at Rs. 160.50/58 against its previous weeks closing levels of Rs. 160.05/10 on the back of continued importer demand.

The daily USD/LKR average traded volume for the first four days of the week stood at $ 68.96 million.

Given are some forward dollar rates that prevailed in the market: one month – 161.30/50; three months – 162.90/20; six months – 165.30/60.
(DailyFt)

Asia Stocks Mixed; Dollar, Treasuries Steady: Markets Wrap

Asian equities were mixed Monday as traders look for clues from earnings reports, developments in the trade war and a meeting of central bankers in Jackson Hole later in the week to gauge the outlook for markets.

Japan's shares fell, while stocks rose in Hong Kong and were little changed elsewhere in Asia. The dollar steadied and the 10-year Treasury yield was little changed. The offshore yuan was stable after signs China may be propping up the currency just as it prepares to restart trade negotiations with the U.S., while the yuan traded onshore strengthened.

Bond traders are betting recent market turmoil won't throw the Federal Reserve off its tightening course. They expect the Fed will raise rates at its next meeting and this week's Jackson Hole symposium could provide clues as to whether such confidence is warranted as the spread between 2- and 10-year yields narrowed to the least since 2007 on Friday.
U.S. Tariffs on $16 billion of Chinese Goods to Take Effect This Week

U.S. is set to impose tariffs on a further $16 billion on Chinese goods on Aug. 23.
Source: Bloomberg

Elsewhere, Turkish markets are closed this week. That may mean low trading volumes and the possibility of sharp currency swings.

Here are some key events coming up this week:

- Companies announcing earnings include Alibaba, Royal Bank of Canada, Lowe's, Target, BHP Billiton, Qantas, Ping An and China's Bank of Communications.
- Central bankers gather at the Kansas City Fed's annual Jackson Hole symposium, where Federal Reserve Chairman Jerome Powell speaks Friday.
- Fed releases the minutes from its July 31 - Aug. 1 FOMC meeting.

These are the main moves in markets:
Stocks

- Japan's Topix index fell 0.4 percent as of the break in Tokyo.
- Australia's S&P/ASX 200 Index rose 0.1 percent.
- South Korea's Kospi index gained 0.1 percent.
- Hong Kong's Hang Seng Index rose 0.5 percent.
- The Shanghai Composite Index lost 0.3 percent as it swung between gains and losses.
- S&P 500 futures were flat.

Currencies

- The yen was little changed at 110.53 per dollar.
- The offshore yuan fell 0.1 percent to 6.8432 per dollar.
- The Bloomberg Dollar Spot Index was up less than 0.1 percent. It declined 0.5 percent Friday.
- The euro bought $1.1429.

Bonds

- The yield on 10-year Treasuries was at 2.86 percent.
- Australia's 10-year bond yield fell almost two basis points 2.53 percent.

Commodities

- WTI crude slipped 0.4 percent to $65.63 a barrel.
- Gold rose 0.1 percent to $1,185.52 an ounce.

(Bloomberg)