NEWS ROUND UP

Monday, May 21, 2019

Contents

Delay in VAT relief irks tourism industry

The delay in legalising the VAT reduction from 15% to 5% for travel and tourism businesses has irked the private sector, despite industry efforts for a fast-track revival post-Easter Sunday setback.

"The Cabinet approved the reduction in VAT for the industry two weeks ago, but there has been no follow up to operationalise it, and this is very disappointing," an industry source told the Daily FT.

The frustration was evident, especially during the long weekend in resorts, who lured lots of locals with massive discounts, but couldn't give benefit of the VAT reduction to guests and those who patronised restaurants for dining.

"The Government has been telling the industry to get the locals back, and we are doing so by offering many discounts. Guests are disappointed that VAT continues to be charged at the higher rate of 15%, despite announcements earlier that it has been reduced," a hotelier complained.

The much-publicised one year moratorium for all registered/approved travel and tourism businesses on capital and interest repayment of their performing loans is also yet to be implemented.

Banks are awaiting a new directive from the Central Bank to effect the relief package to the travel and tourism industry, which includes concessionary working capital for two years.
(Dailyft)

Public debt estimated at 90% of GDP by end-2018: IMF

- Debt increased by weaker economy, rupee depreciation last year
- Treasury bills and bonds account for 42% of GDP
- Obligations of 42 SOEs estimated to be 11.8% of GDP
- CPC, CEB and SriLankan losses account for 1.3% of GDP
- With fiscal consolidation, debt can drop to 75.4% of GDP in 2024
- External debt 59% of GDP, but can reduce to 56% by 2024
- But IMF warns deviating from program could see sharp increase in debt
- Chinese loans amount to 15% of Govt. external debt, or 7% of total public debt

Public debt is estimated to have increased significantly to about 90% of GDP at end-2018, the International Monetary Fund (IMF) said in its latest staff report, with losses of State Owned Enterprises (SOEs), particularly Ceylon Electricity Board (CEB), Ceylon Petroleum Corporation (CPC) and SriLankan Airlines, accounting for 1.3% of GDP.

The increased debt reflected weaker economic performance and the sizable depreciation of the rupee as at the end of last year. Based on disaggregated data for 2018, the composition of public debt includes debt owed by the central Government (83.3% of GDP), outstanding amount of loans guaranteed by the central Government (5.2% of GDP), and outstanding Fund credit (1.6% of GDP).

Domestic debt (mostly treasury bills and bonds) accounted for about 42% of GDP. External debt consisted of multilateral and bilateral loans (20.6% of GDP), international sovereign bonds and syndicated loans (15.4% of GDP), and non-residents' holdings of Treasury bills and bonds (1.1% of GDP).

“Foreign-currency denominated debt accounted for about 50% of total, while debt owed to official and multilateral creditors accounted for about a quarter of the total. Sri Lanka’s debt to GDP ratio remains higher than the median for emerging economies (53%; excluding major oil exporters), and gross funding needs are the third largest among them,” the report said.

The financial obligations of non-financial SOEs are estimated to be 11.8% of GDP based on the latest available data as of end-2017. Sri Lanka has more than 200 state-owned enterprises, and the Ministry of Finance publishes financial performance of 42 non-financial SOEs. Three major SOEs—the Ceylon Petroleum Corporation (CPC), the Ceylon Electricity Board (CEB), and Sri Lankan Airlines (SLA)—recorded a combined loss of 1.3% of GDP in 2018. There is scope to improve the quality of public debt data by adopting the 2014 Government Financial Statistics Manual and publishing audited SOE financial data promptly, the IMF added.

External debt is estimated at 59% of GDP at end-2018. External debt is predominantly owed by the public sector (36% of GDP by the general government and 2% by the central bank). Private external debt remained broadly stable at around 21% of GDP. The ratio of external debt to exports of goods and services is high, at 258% in 2018.

“Although rollover risks remain contained, as 85% of private and public debt is medium or long term, several sovereign bond repayments fall due in 2019–22. More than half of the central Government’s external debt stock is denominated in U.S. dollars. In terms of composition of central Government debt, the largest creditors include the Asian Development Bank (13% of external central Government debt), World Bank (10%), Japan (10%) and China (9%).”

Chinese loans to the Sri Lankan public sector, including SOEs, amount to 15% of central Government external debt, or 7% of total public debt.

The IMF was optimistic that fiscal consolidation envisaged under the ongoing $1.5 billion Extended Fund Facility-supported program would steadily reduce public debt. The consolidation path envisaged under the program scenario is projected to bring down the ratio of public debt to GDP from 90%in 2018 to 75.4% in 2024. The reduction in the debt to GDP ratio beyond 2019 is supported by favourable debt dynamics, with a negative interest-rate-and-growth differential and primary surpluses. Gross financing needs are projected to decrease to 11% of GDP by 2024, as fiscal consolidation reduces the overall deficit and debt amortisation over the medium term.

“Nevertheless, there are significant downside risks to the program scenario. If fiscal consolidation were to stall and the primary balance to return to its historical level (-1.5% of GDP), the debt-to-GDP ratio would remain at about 90% until 2024.”

Debt reductions would become less significant under individual shock scenarios on primary balance (lower primary surplus by 0.5 percentage points of GDP for 2019–20), GDP growth (2 percentage points lower than in the program scenario for 2019–20), the exchange rate (15% real depreciation in 2019 vis-à-vis the program scenario), and the interest rate (an increase by 300 basis points for new borrowings during 2018–21 vis-à-vis the program scenario). When these shocks are combined, the debt to GDP ratio would reach 97% in 2024.

Similarly, in a SOE-related customised contingent liability shock scenario where the central government becomes liable for additional debt of 7% of GDP in 2019, the debt to GDP ratio would initially jump to 99% of GDP and gradually decline to 92% of GDP in 2024. In the combined shock scenario and the contingent liability shock scenario, gross financing needs would remain elevated at 15% of GDP in 2024. Also, the debt level is high relative to revenues, constraining repayment capacity. In terms of the realism of baseline assumptions, the envisaged improvement in the cyclically-adjusted primary balance of around 3% points of GDP over 2019−24 is higher than in 74% of international experiences, highlighting the challenges of the fiscal consolidation plan.

The ratio of external debt to GDP is projected to gradually decline over the medium term. Under the program scenario, external debt is projected to decrease from about 59% of GDP in 2018 to around 56% in 2024. The decline is driven by GDP growth, a steady pace of fiscal consolidation, and gradual current account adjustments. (Dailyft)

Union Assurance continues focus on sustainable growth

UA has reported Rs. 2.5 billion gross written premiums for the first quarter of 2019. This was 1% below the figure reported in the prior period, mainly due to decline in new business premiums as the company aligned its distribution channels to target market segments with potential to generate sustainable growth.

Profit before tax amounted to Rs. 246 million, compared with Rs. 304 million reported in the first quarter of 2018. The drop in profit is mainly due to reduced investment yields and amortisation of expenses related to expanding the bancassurance distribution channel.

Profit after tax of Rs. 178 million was 41% lower than previous period due to Rs. 68 million tax charge as per the Inland Revenue Act which came into effect from 1 April 2018. The tax expense was set off against the deferred tax asset.

Profit in the quarter does not include a surplus from the life business which is actuarially valued at year end.

The company reported a 10% increase in investment income from Rs. 983 million in 2018 to Rs. 1.1 billion in 2019. The decline in equity investments is reflected in fair value losses which increased from Rs. 128 million in 2018 to Rs. 497 million in 2019. Hence total revenue declined by 7% to Rs. 3.1 billion for the period under review. Net insurance claims and benefits increased by 31% mainly due to maturities and other payouts in line with contractual obligations. Underwriting and net acquisition costs increased by 1% while operating, administrative and selling expenses increased by 9% mainly due to increases in staff, branch infrastructure and distribution related expenses.

As a result of the above changes, UA’s life fund stood at Rs. 32 billion as at 31 March 2019, with a healthy solvency ratio indicating the financial strength of the business.

As per the LMD Brands Annual, Union Assurance brand was valued at Rs. 2.5 billion for the year 2019. This is an increase of Rs. 700 million compared to 2018 reflecting that the company has doubled brand value within a short span of three years. Further the company’s brand rating was upgraded from (AA-) to (AA).

UA is anchored by a team of experienced and dynamic professionals, and is backed by a strong capital base and reinsurance partnerships with highly rated global reinsurers. Celebrating over 30 years of excellence, Union Assurance continues to invest in people, products and processes to become a true partner in success for all our stakeholders. (Dailyft)

One year T-bill yield crashes

The secondary bond market ending 17 May witnessed a week of volatility, with yields increasing during the beginning of the week on the back of renewed selling interest, and thereafter decreasing towards the latter part of the week, backed by fresh local as well as foreign buying.

Yields of the 15.07.23, 15.03.24, 01.08.26, 15.01.27 and 01.05.29 were seen increasing to weekly highs of 10.48%, 10.60%, 10.77%, 10.80% and 10.92% respectively during the early part of the week. However, subsequent to the weekly Treasury bill auction, where the weighted average yield of the 364 day bill crashed by 26 basis points to 9.18%, considerable local as well as foreign buying interest returned to the market driving yields down once again. The said maturities were seen hitting weekly lows of 10.23%, 10.28%, 10.60%, 10.60% and 10.80% respectively, reflecting a parallel shift downward of the overall yield curve for the third consecutive week.

On the back of this momentum, yields were seen hitting weekly lows of 9.60%, 9.68%, 9.88% and 10.00% respectively on the two 2021 maturities (i.e. 01.08.21 and 15.12.21) and two 2022 maturities (i.e. 15.03.22 and 01.10.22) while on the long end of the yield curve the 15.06.27 and 01.09.28 maturities traded at a low of 10.65% and 10.71% respectively. The foreign holding in Sri Lankan Rupee bonds recorded an outflow for the 3rd consecutive week to the tune of Rs. 0.43 billion for the week ending 15 May, with the total money market liquidity increasing further to hit a 70 week high of Rs. 73.99 billion by the end of the week.

The daily secondary market Treasury bond/bill transacted volume for the first four days of the week averaged Rs. 11.40 billion.

In money markets, the average overnight net surplus liquidity in the system stood at Rs. 26.49 billion for the week as the Open Market Operations (OMO) Department of the Central Bank continued to drain out liquidity during the week by way of overnight, two day, three day, four day, five day, six day, seven day and ten day repo auctions at weighted averages ranging from 8.38% to 8.54%. The overnight call money and repo rates averaged 8.39% and 8.49% respectively during the week.

Rupee gains further during the week

In the Forex market, the USD/LKR rate on the spot contracts were seen closing the week marginally higher at Rs. 175.90/00 in comparison to the previous weeks closing levels of Rs. 176.30/40, subsequent to trading at levels of Rs. 175.68 to Rs. 176.92.

The daily USD/LKR average traded volume for the first four days of the week stood at $ 68.19 million.

Some of the forward dollar rates that prevailed in the market were 1 month - 176.80/95; 3 months - 178.55/70 and 6 months - 181.25/45. (Dailyft)

MTI shares global learnings on responding to tough times

Every economy and every enterprise at some point of their life cycle will encounter tough times. This is the Sri Lankan ‘moment’ of tough times, but we are not the only economy or enterprise to have been in such a tough situation. Think Egypt, Turkey, Thailand, Bali, Kerala. So, there are a lot of learnings we can take from such economies and enterprises, which have come out strong from challenging situations.

How a company responds to tough times varies. Based on MTI’s research and international experience (having worked on assignments in over 40 countries), broadly there are two types of companies in terms of how they respond to tough times.

We have called them the ‘Chop & Cripple’ companies, and the ‘Trim & Fit’ companies. The names clearly reflect how they respond to tough times.

The following table demonstrates how the two types of companies respond to tough times.

MTI Corporate Finance, is the corporate finance arm of MTI Consulting, a boutique strategy consultancy with a network of associates across Asia, Africa and Middle East. MTI Corporate Finance provides a comprehensive range of services, including due diligence, feasibility studies, funding new businesses or capitalisation of existing ones – from IPOs to private placement facilitation, M&A facilitation, and advisory on governance, compliances and risk management. (Dailyft)

Chamber of Tourism and Industry appeals for relief for SMEs

The Chamber of Tourism and Industry has appealed for urgent relief for small and medium enterprises in the sector who have been seriously affected following the Easter Sunday terror attacks. The appeal was handed over by Chamber President A.M. Jauferto Tourism Minister John Amaratunga recently.

Following is the full text of the appeal by the Chamber of Tourism and Industry:

Asyou are aware our tourism industry has been severely affected consequent to the recent Easter Sunday terrorist attacks.The small and medium stakeholders in the industry,such as internal airlines, cabs, taxi and three-wheel drivers, (popular tuk-tuk service) tour guides, small vegetable and fish suppliers to the hotels and restaurants, small shop owners, surfing board suppliers and supporting labour helpers and material suppliers to the construction industry in the hotel sector, tour operators and those engaged in the sale of gem and jewellery to tourists,etc. are the immediate affected people.

In addition to the above, small staff ofhotels are also suffering due to this unfortunate situation since they have lost avenues ofmaking additional income from guest service charges, tips, etc. During the tourism season, more tourists visit the Pasikudah, Arugambay, Nilaweli areas in the Eastern Province.

Hon. Sir, I wish to take this opportunity to make the following requests with the intention of granting little relief to the people who are engaged in this industry. We are confident that as the Minister of Tourism Industry and Wildlife you will consider taking appropriate action to minimise the hardships and problems faced by these people as early as possible.

We are asking stable institutional support and recognition of the contribution we are making to this industry in order to sustain our country’s economy andalso generate more employment within the industry.

Some mechanism should be implemented to either waive off the loan taken through the banks or similar relief such as reduced interests and opportunities to apply for loans in order to uplift the standard of the stakeholders who engage in small and medium scale business in the tourism sector, such as financial assistance and support.

Tsunami loan scheme under the ETB credit line to be waived off especially because this loan was given to mostly tourism sector enterprise.

We also appreciate the security provided by the Sri Lanka Navy, Sri Lanka Air force, Sri Lanka Army, Sri Lanka PoliceDepartment and Special Task Force.

Finally Sir we are confident that his Excellency the President together with the Hon.PrimeMinister will take every effort to rebuild the tourism stakeholders with the support and assistance of Foreign Ambassadors and High Commissionersto ensure the vital recovery of the tourism industry. Sir we know that you understand our industry and that you have a passion for tourism. We are confident that you will implement the above suggestions and formulate practical solutions.
(Dailyft)

Asia Stocks Mixed as U.S.-China Tech Tensions Rise: Markets Wrap

Asian stocks were mixed Tuesday as investors digested moves by Washington against Huawei Technologies Co. that sank U.S. technology shares overnight. The yuan steadied near a six-month low.

Chinese shares had the strongest gains in the region, while stocks dipped in Tokyo and fluctuated in Hong Kong. Samsung Electronics Co. helped bolster Korean shares, on bets it may benefit from Huawei's need to shift away from U.S. suppliers. S&P 500 Index futures climbed after the benchmark dropped Monday, with semiconductor stocks among the biggest laggards as the White House blacklisted China's top telecom company. Australia's dollar dropped after the central bank governor flagged that an interest-rate cut will be considered next month. Treasury yields stabilized with the dollar.
Asia, U.S. stocks still up on year despite trade breakdown

"The U.S.-China trade war is in danger of assuming Brexit-like characteristics -- long and drawn out with a series of false dawns, but with no discernible progress," Jeffrey Halley, senior market analyst at Oanda Corp. in Singapore, wrote in a note. Any China retaliation for the Huawei moves could see a more powerful hit to markets than that from the U.S. measures, he wrote.

Markets remain on edge as the trade dispute develops. Trump said in an interview he was "very happy" with the trade war and that China wouldn't become the world's top superpower under his watch. In response, China could retaliate as Chinese companies' "legitimate rights and interests are being undermined," Zhang Ming, the nation's ambassador to the European Union said.
Fed's Bostic Doesn't See Rate Move More Likely in One Direction

Atlanta Federal Reserve President Raphael Bostic discusses trade risks affecting U.S. businesses, Fed policy.

Meanwhile, crude firmed on optimism production curbs from major oil producers will be maintained.

Here are some notable events coming up:

- On Tuesday, Bank of England Governor Mark Carney testifies to Parliament about the May inflation report, and Reserve Bank of Australia Governor Philip Lowe speaks in Brisbane.
- The Fed minutes of its FOMC April 30-May 1 policy meeting will be released Wednesday.
- Counting of votes from the Indian general elections takes place Thursday as Prime Minister Narendra Modi attempts to secure a second term.
- ECB President Mario Draghi speaks in Frankfurt on Wednesday.
- The European Parliament holds continent-wide elections May 23-26.
- On Thursday, the ECB publishes its account of the April monetary policy decision.

And these are the main moves in markets:
Stocks

- Japan's Topix index fell 0.6% as of midday in Tokyo.
- Australia's S&P/ASX 200 was little changed.
- South Korea's Kospi index added 0.7%.
- Hong Kong's Hang Seng Index rose 0.2%.
- Shanghai Composite Index rose 1.5%.
- S&P 500 futures rose 0.4%. The S&P 500 fell 0.7%. The Nasdaq 100 dropped 1.7%.

Currencies

- The yen dipped 0.1% to 110.19 per dollar.

- The yuan rose 0.2% to 6.9259 per dollar.
- Bloomberg Dollar Spot Index rose 0.1%.
- The euro held at $1.1165
- The Aussie fell 0.1% to 69.97 U.S. cents.

Bonds

- The yield on 10-year Treasuries was little changed at 2.42%.
- Australia's 10-year bond yield held at 1.68%.

Commodities

- West Texas Intermediate crude gained 0.3% to $63.29 a barrel.
- Gold lost 0.2% to $1,275.77 an ounce.

(Bloomberg)