NEWS ROUND UP

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Contents

Sri Lanka rupee closes at new low, stocks gain 0.57-pct

The Sri Lanka rupee closed at a new low against the US dollar amid inconsistent policy, and stocks gained 0.57 percent despite 546 million rupees of foreign selling in John Keells Holdings, brokers and dealers said.

The rupee weakened further to close at 161.40/45 rupees in two-way quotes against the US dollar in the spot market on foreign outflows mostly government securities, dealers said.

Excess liquidity in Sri Lanka's money markets rose to almost 58 billion rupees earlier this month which was expected to put pressure on the rupee unless it was permanently sterilized, or followed though with unsterilized sales when the money turns into credit and imports.

The central bank has a habit of buying dollars inflows to the government or private players to expand the money supply through unsterilized peg defense to prevent rupee appreciating.

After halting the appreciation through dollar purchases, the central bank suddenly switches to a floating regime and helps push the rupee down.

Some economic analysts who have studied the central bank's inconsistent policies that has led to permanent currency depreciation calls it the 'Big No No'.

"The other big danger to the peg is the practice of selling Treasury dollars to the Central Bank," EN's economic analyst Bellwether wrote last month in a column on how to improve the credibility of Sri Lanka's permanently downward crawling peg.

"If the guided peg breaks and there is an attempt to float, this is an absolute no-no, even if liquidity is short. All Treasury dollars should be sold in the market for old rupees, not to the Central Bank for new rupees."

The central bank has partially sterilized the liquidity to through term repo deals, which is better than nothing, but the money will eventually flow out and the central bank will not be able to hold on to the rupees, analyss warn,

Some of the dollar may remain as the falling rupee generates inflation expanding working capital needs of market participants at first in the traded sectors expanding reserve money.

Analysts have advocated policy consistency to improve the credibility of the peg.

Importer demand was subdued during the day and export conversions were also low, they said.

The US dollar closed Tuesday at 161.25/35 rupees.

The Central Bank is now linked to a new portal which allows it to see real time quotes from currency dealers and was seen playing a match-making rule connecting banks with excess US dollars with those that needed it, dealers said.

In the past, the Central Bank intervened via state-names to curtail volatility or used moral suasion on banks to curb their enthusiasm.

Currency dealers said the Central Bank is no longer doing either.

Gilt yields were seen easing in the secondary market for government securities.

Actual trades took place at 161.35 rupees after opening at 161.05/20 rupees, dealers said.

Bond yields edged lower in the secondary market for government securities ahead of the weekly Treasury bill auction on Wednesday.

A five-year bond maturing in 2023 closed unchanged at 9.90/97 percent in two-way quotes. A ten-year bond maturing in 2028 closed at 10.23/33 percent, down from 10.25/40 percent the previous close.

In equities, Colombo's benchmark All Share index gained 0.57 percent, up 34.44 points to 6,044.67, and the S&P SL20 index of more liquid stocks closed a sharp 0.88 percent higher, up 28.21 points to 3,225.15.

Market turnover was 1.1 billion rupees with 91 stocks gaining during the day and 35 declining. Turnover was 374.8 million rupees the previous day.

Foreign investors sold stocks worth 546 million rupees on Wednesday.

Ceylon Tobacco (up 24.60 rupees to 1,324.60 rupees), John Keells Holdings (up 1.90 rupees to 140 rupees) and Commercial Bank (up 2 rupees to 123 rupees) contributed to the benchmark index gain.

Softlogic Holdings gained 1.10 rupees to 21.70 rupees and Hemas Holdings closed 2 rupees higher at 93 rupees.

Net foreign selling was 590 million rupees, up sharply from selling of 24.3 million rupees on Tuesday. Foreign selling in John Keells Holdings was 546 million rupees, according to Asia Securities.

Crossings, or off-market negotiated trades, amounted to 488.7 million rupees, and were 43 percent of market turnover.

Three crossings in John Keells Holdings amounted to 418.6 million rupees and a crossing each for 42 million rupees in Sampath Bank and 28 million rupees in Commercial Bank.

Sampath Bank closed 1.40 rupees higher at 280.30 rupees. (EconomyNext)

Sri Lanka's 01-yr Treasury yield eases to 8.99-pct

Sri Lanka's 12-month Treasury bill yield edged down one percentage point to 8.99 percent at Wednesday's auction, according to data from the state debt office, a unit of the central bank.

The debt office accepted 7.5 billion rupees of 12-month bills, the same amount offered, having received bids worth 25.7 billion rupees.

The 3-month bill yield fell 06 basis points to 8.03 percent, with 5.0 billion rupees of bills, sold, the same amount offered.

Six-month bills were not offered. (EconomyNext)

Central bank independence must be matched by accountability

Central Bank independence must be matched by accountability and a mechanism for public oversight, a top economist said as Sri Lanka is moving towards a modified inflation targeting framework with legal changes to end interference from the finance ministry.

In Sri Lanka and elsewhere central banks have been forced to print money to finance budget deficits, generating balance of payments troubles, currency depreciation and inflation, a phenomenon known as fiscal dominance of monetary policy.

However central banks themselves can depreciate currencies through Mercantilist ideology in a type of trade-oriented monetary policy, or print money in the course of policy errors to create inflation and asset-price bubbles hurting the common man.

In Sri Lanka due to past experience, economists and analysts have called for central bank independence in the hope that that its managers will generally will want to provide better money.

As part of a law to bring in modified inflation targeting, the central bank is on track to get more independence.

"However independence without accountability will have the adverse repercussion of creating a monster within the sovereign government of Sri Lanka," W A Wijewardene, a former Deputy Governor of the Central Bank, said delivering the agency's 68 the anniversary lecture.

"That will not be acceptable to either the political authority or to the public.

"Hence, greater public scrutiny and oversight should be exercised over the work of the Central Bank once it is granted a greater degree of autonomy."

He said that in the US, the Chairman of the Federal Reserve has to come to the Congress (parliament) and answer questions from legislators every quarter.

Wijewardene said since not all legislators will know enough about monetary policy, they have to be backed up by a group of expert of the field.

But the process first has to start by the appointment of the Governor of the central bank and members of the monetary board.

"First, it is necessary to introduce a nomination, screening and selection process for the Governor and the board members as is being done in the case of the Bank of Canada or the Bank of England," Wijewardene explained.

"The present method, though it is not a reflection on the incumbent office holders, is marred with the possibility of subjugating themselves to the wishes of the political authorities which have appointed them."

Before the appointment of the current Governor Indrajit Coomaraswamy, the central bank was embroiled in a securities scam, and amid pressure from the public and civil society groups, President Maithripala Sirisena refused to re-appoint then Governor Arjuna Mahendran.

A Presidential Commission which went into the securities scam has suggested that the laws be changed so that the central bank governor is appointed via a constitutional council.

The body was set up to make senior public officials to be independent and allow them to act impartially without being punished or transferred by politicians for doing the right thing, after the abolition of the position of permanent secretaries destroyed Sri Lanka's public service and made it a rulers' service instead.

Wijewardene said the administration and financial works of the central bank should be made transparent.

"At present, such a disclosure policy has been adopted by Bank of Canada with respect to foreign travel and entertainment by senior officers and board members of the bank," he explained.

Under inflation targeting the central bankers have to raise interest rates until inflation is brought down to a target set usually in agreement with the parliament of finance ministry.

Central banks can no longer control money supply in the hope of getting inflation down and give real economy excuses to a gullible public for failing to generate the low level of inflation agreed.

When New Zealand first introduced inflation targeting, the architects of the law dropped the monetary policy committee which allows those responsible for inflation to 'pass the buck' and made the Governor personally responsible.

The Governor can in theory be sacked for generating too high inflation. Inflation fell remarkably. (EconomyNext)

Sri Lanka Access Engineering says real estate strategy seeing results

Sri Lanka's Access Engineering says a transition from construction into a real estate firm is seeing early results with apartment and office pre-sales on track to bring more profits, Chairman Sumal Perera has said.

"In the long term, especially following 2020, our real estate projects of Capital Heights and Marina Square Colombo will contribute extensively to our bottom line," Perera told shareholders in the annual report.

"We are also hoping to extend Access Tower II by adding a new wing dubbed Tower III,"

"Our drive is to position ourselves as a key player in the real estate sector, and maintain leadership."

When Access Engineering listed in 2012, the construction business contributed 95 percent to group revenue, but was down to 58 percent in 2017/18.

Property and real estate contributes just 1.9 percent to group revenue. The balance comes from automobile sales (31.35 percent) and construction material sales (9.88 percent).

There were concerns that the real estate market is overheated, but may have cooled since then.

The construction industry has a lot more room to grow with the development of the Colombo Port City project, Perera said.

"Our short to medium-term strategy remains the same with the main focus being on our core business lines of engineering and construction," he said.

Access Engineering established itself specialising in infrastructure projects building roads, bridges and water and drainage systems, and Sumal Perera says he'll be disappointed if Access Engineering remained a construction company 10 years from now.

Access Engineering is diversifying into real estate, building high-rises for rent income to bring a steady revenue stream and also to increase the group's net asset base.

Capital Heights comprising 242 luxury apartments will be completed in 2020 with 40 percent of the apartments already sold. Access Engineering holds a 50 percent stake in the project.

Marina Square is a mixed development project comprising 1,068 condominium apartment units and around 150,000 square feet of commercial space, has recorded presales of 25 percent.

Marina Square is owned by Harbour Village Private Limited a joint venture between Access Engineering, China Harbour Engineering and Musthafa's Singapore and will overlook the Colombo Port.

Access Engineering holds over 60 percent of Harbour Village.

Access Tower 2, built and owned by Access Engineering commenced operations early 2018.

"The A-Grade, office tower of 200,000 square feet of rentable office space was preleased three months prior to opening," Perera said.

The 30-storey Access Tower 2 was built at a cost of 5.3 billion rupees and has parking facilities for 300 vehicles.

Access also owns 21 acres of land though subsidiaries within the IT zone in Malabe which is proposing to build a private university Horizon Knowledge City offering tech, science, law, engineering and paramedical degrees.

Access Engineering is building 608 housing units for government employees at Borella for the Urban Development Authority costing 4.9 billion rupees.

The company completed 941 low-cost housing units comprising two bed rooms, living area and kitchen, toilet and balcony for 3.3 billion rupees, which also for the UDA.

Access Engineering saw profits fall 39 percent from a year earlier to 364.9 million rupees in the June 2018 quarter on falling margins from construction, despite improving earnings from condominium sales and rent.

Earnings were 36 cents a share in the June quarter, latest interim accounts filed with the Colombo Stock Exchange showed. The Share last traded at 15.10 rupees.

Revenue grew 10 percent from a year earlier to 5.8 billion rupees.

Real estate saw revenue increase 312 percent to 196 million rupees, with profits increasing 179 percent to 183 million rupees.

This segment which comprises rents from high-rise buildings owned by the group and apartment sales made the highest contribution to group earnings.

The construction segment reported revenue growth of 5 percent from a year earlier to 3 billion rupees, but profits fell a sharp 82 percent to 86 million rupees.

Construction material sales grew 89 percent to 894 million rupees and profits increased 106 percent to 72 million rupees.

Automobile sales increased 11 percent to 2 billion rupees but profits fell 68 percent to 41.2 million rupees. (EconomyNext)

Markets move higher on trade deal euphoria

Wall Street forged further into record territory on Wednesday as Canada and the United States signaled they were closing in on a deal to remake the North American free trade pact.

European and Asian stocks also mostly rose.

US President Donald Trump joined Canadian Prime Minister Justin Trudeau in suggesting a deal was possible this week.

Good economic news also buoyed stocks after the Commerce Department reported US GDP grew 4.2 percent in the second quarter, even stronger than initially reported due to a bump in business investment.

The broad-based S&P 500 and Nasdaq, led by a rally in tech stocks, then popped their fourth straight set of record closes.

Adam Sarhan of 50 Park Investments told AFP the recent bullish trend reflected the combination of strong corporate earnings, robust economic growth, tax cuts and fiscal stimulus.

"We have a very bullish fundamental backdrop, which has warranted higher stock prices," he said.

- Post-Brexit deal -

But Peter Cardillo of Spartan Capital Securities said Wednesday's upward momentum was largely due to "hopes of a breakthrough in the Canadian trade talks."

In Europe, markets were affected by the European Union's top negotiator saying the bloc was willing to strike an "ambitious" deal with post-Brexit Britain far beyond any agreements made with other countries in the past.

The main stock indices in Paris and Frankfurt both flipped higher after the announcement and closed the day 0.3 percent higher.

The pound spiked higher, gaining over one cent to climb over $1.30. But as a stronger pound depresses earnings of many London-listed firms who make most of their sales abroad, the FTSE-100 ended the day 0.7 percent lower.

"Strength in the pound, despite reports an October deadline for Brexit divorce talks is dissolving into a November deadline, saw FTSE 100 shares back off from a two-week high," said Jasper Lawler, head of research at London Capital Group.

Meanwhile, the Turkish lira tumbled to its lowest value against the US dollar in two weeks, despite Ankara's attempts to reassure investors after Moody's downgraded its credit ratings on 20 Turkish financial institutions.

The lira was trading at 6.47 to the dollar around 2100 GMT, down from around 6.27 at the close of Tuesday. It also fell against the euro.

Lawler noted that Turkish bank shares fell alongside the lira on the Moody's rating action.

"It is going to be increasingly difficult to get business done in Turkey under US sanctions and banks are the obvious pressure point in markets," he said.

- Key figures around 2100 GMT -

New York - Dow Jones: UP 0.2 percent at 26,124.57 points (close)

New York - S&P 500: up 0.6 percent at 2,914.04 (close)

New York - Nasdaq: UP one percent at 8,109.69 (close)

London - FTSE 100: DOWN 0.7 percent at 7,563.21 (close)

Frankfurt - DAX 30: UP 0.3 percent at 12,561.68 (close)

Paris - CAC 40: UP 0.3 percent at 5,501.33 (close)

EURO STOXX 50: UP 0.3 percent at 3,456.13 (close)

Tokyo - Nikkei 225: UP 0.2 percent at 22,848.22 (close)

Hong Kong - Hang Seng: UP 0.2 percent at 28,416.44 (close)

Shanghai - Composite: DOWN 0.3 percent at 2,769.29 (close)

Euro/dollar: UP at $1.1709 from $1.1698 at 2100 GMT

Pound/dollar: UP at $1.3028 from $1.2896

Dollar/yen: UP at 111.68 yen from 111.07 yen

Oil - Brent Crude: UP $1.19 cents at $77.14 per barrel

Oil - West Texas Intermediate: UP 98 cents at $69.51 (AFP)

How would the stock market react if Trump is impeached?

During a Fox News interview last week, President Donald Trump said that if he was ever impeached, the stock market would crash.

The interview followed last week's conviction of Paul Manafort, Trump's one-time campaign manager, and the guilty plea of Michael Cohen, the president's former personal lawyer. We asked three economists — M. Todd Henderson, Eric Zitzewitz and Larry Hatheway — to weigh in on how the market might react if Trump gets the boot.

M. Todd Henderson is a professor of law and economics at the University of Chicago. The opinions expressed in this commentary are his own.

Political games in Washington typically don't matter very much on Wall Street.

The fundamental value of a stock is based on the cash that the underlying company is expected to generate over its lifetime, discounted to present value. Therefore, the value of the stock market is simply the sum of the values of all the individual stocks (or, for an index, like the Dow, the value of the stocks in the index). If businesses expect to make more money, more investors will buy than sell, driving up stock prices.

What's more, the probability of a political event like an impeachment is already baked into the stock price of every company. Markets (meaning buyers and sellers of stock) are constantly adjusting their estimates based on news of all kinds, whether it's about consumer demand for a particular product, tariffs, the president's latest tweet or even his impeachment. The prices of stocks today reflects these estimates.

Notably, markets didn't move at all on the news of Manafort's conviction and Cohen's guilty plea. This means the market as a whole does not believe Trump will be impeached, or knows that Trump's impeachment wouldn't have a big impact on the value of American businesses. Investors could also think a President Pence with a Democratic-controlled House (and even Senate) might be good for business. Even if Trump is impeached, his tax cuts for corporations and the rollback of regulations are not likely to be reversed for many years should Pence become president.

Eric Zitzewitz is a professor of economics at Dartmouth. The opinions expressed in this commentary are his own.

There was already a low probability that President Trump would finish his term, then get renominated and be reelected, according to betting markets at Betfair. So last week's news of Manafort's conviction and Cohen's guilty plea caused his odds of finishing the term and of being renominated to drop even further (from 70.4% to 63.3% and from 70.0% to 60.6%, respectively).

But the stock market has seemed remarkably unaffected. When last Wednesday's news broke, the S&P 500 was basically flat.

To dig a little deeper, we can look at stocks that are expected to especially benefit from Trump. The Trump Long-Short Policy Index is an index I designed in collaboration with Raymond Fisman of Boston University. It tracks the difference in returns between stocks that rallied when Trump was elected and those that fell at that time. When Trump met with congressional leaders Nov. 10, 2016 and confirmed his intention of pursuing a Republican agenda, it rose. When Manafort was indicted in 2017, the index saw a statistically significant drop, but rallied one month later when the Senate passed the tax cuts.

The index's swings can be used to scale the importance of an event. For example, the fact that the index lost about 10% of its post-election gains when Manafort was indicted means that the markets estimated the indictment undid about 10% of the expected effects of Trump's election, at least as it pertains to economic policy that matters for publicly traded firms. Conversely, the large index rally that occurred when the tax cuts passed indicated that these cuts were a significant component of what investors expected Trump to deliver.

In contrast to these prior events, our index barely moved on last Wednesday's news. Not only was the increased probability of an early departure for Trump not a big deal for the aggregate market, it also appears not to matter much for individual stocks either.

Why? The explanation may lie in the fact that last week's news also did not have much affect on Trump's odds of reelection (which fell from 38.2% to 36.2%) or of the GOP keeping the House in 2018 (which fell from 35.7% to 35.2%).

Realistically, Trump is probably done passing most of his economic policy anyway. The key uncertainty now is how much of his policy will last. Ironically, while impeachment is clearly bad for Trump himself, if it divides the country, it may reduce the likelihood that a blue wave large enough to overturn the GOP and his policies will arise.

Larry Hatheway is group chief economist at GAM Holding AG. The opinions expressed in this commentary are his own.

The most important driver of the US stock markets remains the US economy. The Trump administration's achievements in delivering significant tax cuts and lighter-touch regulation clearly supported the S&P 500's solid advance in 2017. But as much as any administration wants to take credit for solid economic growth and a rising stock market, the fact is that these trends were clearly underway before the 2016 election. For this reason, the simple act of impeachment won't erode the fundamentals that have pushed the S&P 500 to record highs this year.

Since 2010, the share of US corporate profits in the nation's gross domestic product has attained levels never before seen in the post-war era.

Low corporate borrowing costs courtesy of the Fed's monetary policy easing since the 2008 financial crisis has cut debt servicing costs and boosted the bottom line. At the end of the Great Recession, profits jumped even more than usual, given that US firms shed far more jobs — and hence costs — during the recession than typical. That allowed firms to increase profits rapidly once sales began to pick up.

But other factors have been at work as well. The emergence of dominant players in key industries — like Apple, Google and Microsoft in the tech space — has created firms able to earn 'supernormal' profits. Lastly, various factors have diminished the bargaining power of labor, including globalization, labor-saving technologies and the long-term decline of union power.

As a result, wage growth has been tepid. And since wages and benefits make up over two-thirds of the total costs of the average US company, the diminished bargaining power of labor has been a key driver of historically high profits. All of this has helped cut costs and drive corporate earnings even higher.

Thanks to this rampant corporate profit growth, companies flush with cash have been hiring strongly for eight years. The US unemployment rate peaked at 10.1% in October 2009. By the end of the Obama administration it had fallen to 4.8%. Now it stands at 3.9%.

While Trump's 2017 tax cuts have clearly provided a lift to the economy, the pace of job growth has slowed in the first two years of the Trump administration relative to the last four years of the Obama administration. In part, that reflects a more fully employed US economy — talented workers are not as readily available as they were five years ago.

But this combination of strong job growth and rising company earnings has made the US economy more resilient to all manner of shocks, even political ones.

So would impeachment — and removal — of a standing US president cause the market to crash?

Richard Nixon resigned from the presidency in 1974. It was during a time of increased economic uncertainty, thanks to rising inflation that led to a "lost decade" for US investors. In the 1970s, inflation had a far larger and longer-lasting impact on investment performance than Nixon's resignation. Bill Clinton was impeached in 1998, but he was not removed from office. For investors, the tech bubble of the late 1990s was of far greater importance. Following the 1998 emerging market meltdown, equity markets surged as the Fed eased monetary policy and investors scrambled to buy Internet stocks. Clinton's Impeachment barely caused a ripple.

We can draw lessons from history. Most importantly, the health of the economy and corporate profits largely determine how stock markets perform. Today, the greatest risk for investors remains a destabilizing escalation of trade conflict or an unanticipated surge in US inflation, which would force the Fed to tighten aggressively.

Politics matters, but to paraphrase political strategist James Carville: "'It's the economy, stupid." (CNN)