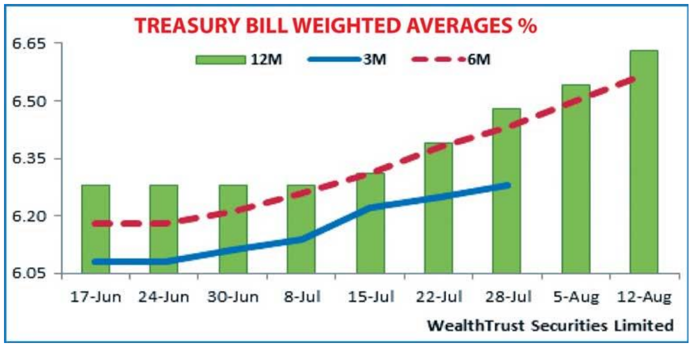
NEWS ROUND UP

Thursday, August 13, 2015

Contents

Treasury bill weighted averages increase to pre rate cut levels

Maturity	Amount mount	Bids received	Amount accepted	Weighted Average
91 day	not offered			
182 day	Rs 8.000 Billion	Rs 28.093 Billion	Rs 18.568 Billion	6.57%
364 day	Rs 12.000 Billion	Rs 19.880 Billion	Rs 3.395 Billion	6.63%



The weighted averages on the 182 day and 364 day bill maturities increased by 07 and 09 basis points respectively to 6.57% and 6.63% at its weekly auction held yesterday to reach levels last seen prior to the policy rate cut of 50 basis points in April 2015. The demand generated for the 182 day bill in the absence of the 91 day bill saw a massive amount of Rs.18.5 billion been accepted against its initial offered amount Rs.8 billion, translating to 84.54% of the total accepted amount.

Meanwhile in secondary market bonds, activity were seen drying up drastically yesterday with yields moving up marginally on its two way quotes. A very limited amount of activity was witnessed on the 01.05.2020, 01.10.2022 and 01.08.2025 maturities within the range of 8.38% to 8.40%, 9.10% to 9.13% and 9.60% to 9.64% respectively.

In money markets, the overnight call money and repo rates increased marginally to average 6.11% and 5.90% respectively as surplus liquidity decreased further to Rs.67.11 billion yesterday.

Rupee dips to a three week low

The USD/LKR rate on spot contracts lost ground once gain to hit a three week low of Rs.133.80 yesterday. The total USD/LKR traded volume for the previous day (11-08-15) was US $ 40.20 million. Some of the some forward dollar rates that prevailed in the market were 1 Month - 134.40/50; 3 - Months - 135.45/65 and 6 Months -136.60/90.

(Daily FT)

Treasury Bills		
91 Day Bills	-	6.20 / 6.35
182 Day Bills	-	6.53 / 6.65
364 Day Bills	-	6.68 / 6.70
Treasury Bonds		
01/11/15	-	6.25 / 6.45
01/04/16	-	6.45 / 6.65
15/05/17	-	7.06 / 7.12
01/06/18	-	7.80 / 7.90
01/07/19	-	8.13 / 8.18
01/05/20	-	8.37 / 8.43
01/08/21	-	8.91 / 8.94
01/10/22	-	9.10 / 9.12
01/09/23	-	9.25 / 9.32
01/01/24	-	9.30 / 9.55
01/08/25	-	9.61 / 9.65
15/03/35	-	9.60 / 10.25
01/03/45	-	10.40 / 11.00

CB on policy of issuance of Treasury bonds through public auctions

The Central Bank commenced issuing Treasury bonds only through public auctions from the auction of 30 year Treasury bonds held on 27 February. In response, several reports published in the media have alleged that the sole reliance on issuing Treasury bonds through auctions conducted since 27 February has led to additional costs to the government.

Accordingly, they appear to support that issuance of Treasury bonds through a mix of private/direct placements method and auctions that have been followed during the past several years should be reintroduced to reduce such costs. The some reports hypothetically calculate the additional costs to the government based on certain assumptions. In this regard, the Central Bank wishes to provide following clarifications for awareness of the general public.

In terms of the Operational Manual of the Public Debt Department, issuance of Treasury bills and bonds should be undertaken as much as possible through public auctions based on market conditions and any balance funding requirement could be raised through private/direct placements as per the procedure laid down in the Manual.

However, in recent years, nearly 80 to 90% of government funding raised through Treasury bonds was via direct placements method, alternative to auctions, based on strategies followed at that time. The current policy of issuance of Treasury bonds via public auctions only is expected to enable further market development process initiated in the past several years by moving to a full scale auction arrangement for issuance of Treasury bills and international Sovereign Bonds which will be bring more benefits to both the Government and investors in the near future.Untitled-4

At the 30 year Treasury bond auction held on 27 February, Rs. 10.06 b was raised at the weighted average yield to maturity of 11.73%. Prior to this auction, at the previous 30 year Treasury bond auction held on 27 May 2014, Rs. 2 b was raised at the yield to maturity of 11.75%. After this auction, further Rs. 77.8 b was raised from direct placements of around 30 year maturity Treasury bonds at yield rates ranging from 8.85% to 11.80% as per the prevailing practice and the overall weighted average yield covering the auctions and direct placements was 11.47%. At other previous issuance of Treasury bonds of around or close to 30 years, lower or higher yield rates have been determined.

However, the yield rates of Treasury bonds or any security issued at auctions in the market are not directly comparable across the auctions or across different maturities of securities because each auction in the market environment involves different market conditions and factors. Changes in market liquidity, policy interest rates, foreign investors' behaviour and market expectations will have diverse impact along with demand and supply forces on the yield rates. Therefore, commenting on the additional costs or saving to the government from issuance of a Treasury bond at a particular auction compared with the yield rate of a Treasury bond issued at another auction or in a particular period is not acceptable and justifiable.

The calculation of additional cost to the government due to the 30 year Treasury bond issuance at the auction held on 27 February in some analyses is solely based on the assumption that if Rs. 1 b as announced for the auction was accepted on bids at the weighted average yield to maturity of 10.38% as per those bids up to Rs. 1 b and direct placement window was opened after the auction at that auction weighted average yield rate to fund the balance funding as per the prevailing practice.

Accordingly, the additional cost to the government as per such calculations is 1.35% being the difference between the yield rate of 11.73% at the auction for Rs. 10.06 b and the yield rate of 10.38% applicable to Rs. 1 b at the auction. However, the two issuing options are completely different as the full auction system is market-based whereas the limited auction with direct placements is a funding method combined of market and administratively determined arrangement. Therefore, such additional cost calculation has no practical grounds.

Some analysts calculate a further addition to the above additional cost by calculating the increase in yield rates of Treasury bonds of other maturities issued at auctions after 27 February compared to yield rates of such matures issued at the latest auction or direct placement made prior to the 30 year Treasury bond auction on 27 February. Such analysts update the total additional cost on an on-going basis as and when a new Treasury bond is auctioned. As the yield rates at different auctions are not comparable due to different market conditions and factors as stated above, the calculation of such additional cost has not justification.

The auction based issuance arrangement will contribute to the development of Government securities market in many ways and some are highlighted below.

a. The benefit of price discovery realised in the market mechanism is not available in the direct placement led issuances. Therefore, it is not possible to gauge whether the yield rate in this system is lower than the yield rate to be realised from the full auction system. In economics, it has been established that market mechanism is more beneficial than administratively managed market arrangements to market participants in terms of the efficient pricing in place of administered prices. In the medium term, when the full auction system comes into place, the funding cost to the government will be determined based on market mechanism with close monitoring by the Central Bank with a mix of debt-raising instruments to reduce the excessive volatility in yield rate or costs. Accordingly, the immediate increase in the yield rates at auction on 27 February and the aftermath would be corrected by market forces. In addition, removal of special standing facility rate of 5% by the Central Bank on 3 March also led to the increase in the yield rates which is a factor external to the issuance of the Treasury bond under reference. However, as shown in the subsequent auctions without direct placements, yield rates gradually started adjusting and stabilising in a market environment. Also, the demand increased across several maturities of government securities from the short to long term. Therefore, the overall cost of borrowing through Treasury bonds has been declining and moderating in general. However, the cost at individual auctions may vary due to changes in market conditions.

b. The auction process improved tremendously as shown by increased participation by dealers and investors in the primary and secondary markets. As a result, the Government could raise as much as Rs. 316.4 b through Treasury bonds at auctions since the issuance of 30 year Treasury bond in reference supported with other debt instruments to meet the government funding requirements.

c. The secondary market of government securities (Treasury bonds and bills) also expanded due to active auctions in 2015. As a result, investors who are not in a position to access the auctions or large institutional investors who fail to secure bids at the action started bidding in the secondary market across the Primary Dealers looking for yields comparable with primary market/auction yields. As a result, an active secondary market has now begun to operate in the country. The active secondary market will improve further competition in the government securities market facilitating the government to raise funds at competitive yield rates.

d. The promotion of the open market mechanism for government securities will attract international investors to the government securities market and the stability in investment flows and investor confidence will improve in the medium term.

e. In addition, the issuance Treasury bills and Sri Lanka Development Bonds will further facilitate the Government to raise funds through the auction system in a market environment.

In view of the above, the current policy initiative for issuance of Treasury bonds only at public auctions should be evaluated with a medium to long-term view to understand the benefits of the market mechanism to all participants. (Daily FT)

AIA Sri Lanka 1H revenue up 5% to Rs. 7.1 b

AIA Insurance Lanka PLC (AIA Sri Lanka) has announced a consolidated revenue of Rs. 7.1 billion in the first half up by 5% over the corresponding period of last year.

In a statement AIA Sri Lanka said delivering steady premium growth, consolidated revenue was up 5% to Rs. 7,105 million and the increase was due to higher net earned premiums in both life and general insurance businesses.

Composite gross written premium (GWP) income grew by 18% to Rs. 5,844 million and GWP of conventional life products grew 21% to Rs. 3,314 million, accounting for 86% of the overall life GWP.

AIA Sri Lanka’s GWP of life business up by 10% to Rs. 3,867 million and GWP of general insurance increased by 38% to Rs. 1,977 million.

The Company’s consolidated profit after tax amounted to Rs. 72 million in the first half, down from Rs. 146 million in the corresponding period in 2014. “The lower profit was mainly attributable to reduced investment income driven by lower interest rates and an increase in claims in the general insurance business,” AIA said. The surplus of the life insurance business is reported annually at the year end and is therefore not included in the half-year profit.

Shah Rouf, Chief Executive Officer of AIA Sri Lanka, said: “AIA Sri Lanka delivered a solid performance with 18% increase in our overall combined GWP compared with the first half of 2014 and will build on this growth momentum in the second half.”

William Lisle, Chairman of AIA Sri Lanka, said: “I am pleased to see the solid performance achieved by AIA Sri Lanka as I recently assumed my new role as the Chairman of the Company.

I believe a strong foundation has been laid for AIA Sri Lanka to benefit from the dynamic growth opportunities in the country. We will continue to leverage on AIA Group’s expertise and understanding of the Asian business for the benefit of our customers in Sri Lanka.” (Daily FT)

DFCC posts Rs. 637 m profit after tax in 1Q

The DFCC Group has recorded a consolidated profit after tax of Rs. 637m for the three months ended 30 June 2015 compared with Rs. 1,138m in the corresponding period of the previous year (comparable period).

The prior period included a one off adjustment due to a change to the impairment assessment process.

The Banking Business comprising the DFCC Bank (DFCC), a licensed specialized bank and its 99% owned subsidiary DFCC Vardhana Bank PLC (DVB), a licensed commercial bank contributed Rs. 643m to profit after tax. The contribution from all other subsidiaries, joint venture and associate company collectively was Rs. 1m.

BANKING BUSINESS

The Banking Business of the DFCC Group is undertaken by DFCC and DVB. Both banks function as one economic entity and as such it is appropriate to analyse the consolidated performance of the two banks as DFCC Banking Business (DBB). A consolidated Income statement for DBB has been released to the Colombo Stock Exchange as supplementary financial information.

This statement was derived from the interim financial statements. Since the financial year of DVB ends in December, the accounts of DVB are consolidated with a 3 month lag.

DBB recorded a profit after tax (PAT) of Rs. 643 m during the current quarter. The PAT for the previous comparable period included an adjustment arising from a change to the impairment assessment processes which contributed Rs. 553 m to PAT. The PAT for the current period of Rs. 643 is an increase of 20% over that for the previous period excluding the one off adjustment.

Net Interest Income (NII) of DBB for the period increased by 4% from Rs. 1,693m to Rs. 1,757m. DBB also achieved a credit growth of 4% during the quarter to 30 June 2015. Net fee and commission income of DBB in the current period increased by 23% to Rs. 259m compared to Rs. 211m in the previous comparable period. Fee income is generated largely by DVB the commercial banking subsidiary from trade finance and commercial banking services.

The Gain on Sale of equity securities by the Bank was Rs. 37m compared to Rs. 100m in the comparable period.

The forward exchange contracts are accounted as a derivative and its fair value changes are reported as net gain / (loss) from financial instruments at fair value through profit or loss in the income statement.

The cumulative allowance for impairment for loans and advances was maintained at a healthy level of 70% as a percentage of impaired loans and advances of DBB on 30 June 2015.

Due to stringent cost management DBB was able to contain the overall operating cost increases to only 9% over that of the comparable period. The main increase in operating cost was due to an increase in personnel cost as a result of a salary revision that was effected during the second half of last year. In common with banking industry, personnel cost is a significant proportion of the operating expenses.

INVESTMENTS

Listed shares are classified as available for sale and carried at fair value. Fair value changes that represent unrealized gains/loss are recognized in other comprehensive income. During the period ended 30 June 2015, due to adverse market conditions the available for sale securities recorded a fair value loss of Rs. 669 m. In the comparable period the fair value gain was Rs. 2,289 m.

EQUITY CAPITAL

Under SLFRS, the total income for the period comprises the income reported in the income statement and other comprehensive income. The equity capital is significantly augmented due to the gain as a result of the recognition of shares listed in the Colombo Stock Exchange and owned by the bank at fair value.

PRUDENTIAL INDICATORS

The capital adequacy and liquidity ratios continued to be well above the stipulated regulatory minimum. The regulatory capital computation excludes fair value changes on financial assets classified as available for sale. (Daily FT)

Foreign selling continues at Bourse

Foreign investors continued to be net sellers at the Colombo stock market for the 9th consecutive day yesterday.

The year to date net foreign outflow is Rs. 1.17 billion with yesterday's amount being Rs. 684 million, of which Rs. 597 million was on account of biggest private sector bank, COMB. During August so far the outflow has been higher at Rs. 2.1 billion. Last two weeks foreign net selling on JKH was Rs. 929 million whilst on Commercial Bank during the two weeks ended on 31 July it was Rs. 637 million. With yesterday's selling, the figure for COMB is around Rs. 1.2 billion in recent weeks.

The week ended 24 July saw net foreign inflow of around Rs. 360 million thanks to Rs. 806 million net buying into Asiri and Rs. 448 million in to DFCC. (Daily FT)

Rupee weaker as state bank raises dollar peg

Reuters: The rupee ended weaker on Wednesday for the first time in four sessions as a state-run bank raised the currency's peg against the dollar by 5 cents to allow the exchange rate to depreciate to 133.80, dealers said.

Exporters sold some amount of dollars after the move, but there was demand for the greenback from importers, dealers said.

"The import pressure is there and exporters are not selling expecting further depreciation in line with depreciation of other currencies globally," said a currency dealer, asking not to be named.

One of the two state banks, through which the central bank usually directs the market, started to sell dollars at 133.80, ending three straight sessions when the rupee held steady, they said.

The rupee ended at 133.80/85, weaker from Tuesday's close of 133.75 per dollar. The state-owned bank raised the currency's peg against the dollar by 25 cents last Thursday to allow the exchange rate to depreciate to 133.75.

The dollar and emerging market currencies were all under pressure after China pushed the yuan lower again overnight, boosting the appeal of top-rated government bonds. (Daily FT)

China pushes yuan down further

Reuters: China's yuan hit a four-year low on Wednesday, falling for a second day after authorities devalued it in a move that sparked fears of a global currency war and accusations that Beijing was giving an unfair advantage to its struggling exporters.

Spot yuan in China fell to 6.44 per dollar, its weakest since August 2011, after the central bank set its daily midpoint reference at 6.3306, even weaker than Tuesday's devaluation.

The currency fared worse in international trade, touching 6.57. (Daily FT)