

Market Modes

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MONTH OF DECEMBER IS NOT A PERIOD WHEN you would expect hectic activity in the financial markets. December '97 was no exception. In fact watching the activity at the stock market, at times, was as interesting as waiting for paint to dry. Except for a few large parcels traded, activity was definitely low key. Foreigners, as expected, were net sellers. They were looking for opportunities to sell whenever the market nudged up a bit, due to bargain hunting by locals. Better opportunities in Far Eastern markets, optimism on the near term performance of European and US markets and uncertainty regarding the future of the Rupee kept them from making any long term commitments in our market. December, in any case, is not a month when institutional investors would make heavy investments in stocks. The need for window dressing Financial Statements, generally, prompt corporate treasurers to unload their portfolios towards the end of their financial year. For a large majority of international institutions the accounting period end falls on December 31st. Ethnic Chinese seldom make any significant investments in the period immediately preceding the Chinese New Year (Early February). Therefore funds from sources in the Far East will come in a trickle during this period.

Have we seen the bottom?

All Share Index (ASI) reached 666 on 26th November and bounced up, a bit uncertainly, in the days that followed and reached 701 by the 11th of December. Thereafter the market receded towards 688 before bouncing back to 702 by the end of the month. The movement of the market is typical of a sideways consolidation in anticipation of a significant move up or down. A break below 666 shall confirm a downward move towards the 630 level. On the other hand a momentary move above 715 will be a preliminary signal of bullish sentiment. A substantial recovery of the market, pushing the ASI above 745, convincingly, shall confirm a short/medium term upward trend.

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A Great Opportunity to Hedge

Vulnerability of the Rupee makes investment in shares a great opportunity, for local investors, to hedge their idle funds. The eventual fall of the Rupee, and the inevitable inflationary pressure that would ensue, shall send nominal values of assets and corporate earnings up and reduce their real wage costs (since wages seldom keep pace with rising inflation). The stock market shall climb significantly as a result.

Plantations' Shares

Trading in Watawala shares commenced, on the first day of December, with a Bang. The stock's spectacular performance on its debut took everybody by surprise. The share which started at 33.50 hit a staggering 40.25 within a few hours and closed, a little below the peak, at 39.00 on brisk profit taking by retail investors. A stunning 160% return in a period of less than two months. The inadequacy of the, recently installed, sophisticated trading system at the stock exchange was laid bare, when many who wanted to cash in on the Watawala bonanza had to wait impotently in front of blank screens, not knowing what is happening at the market. The state of the art computer based trading system

caved in as the deluge of orders from the fifteen brokerage firms. flooded the exchange. This is not the first time, though. When Maskeliya shares started trading less than a month ago a similar traffic jam occurred. Despite widespread speculation, Madulsima may not, after all, be the next plantation IPO. Either Agarapatana or Hapugastenne or both are likely to come next. From January, 1998 two IPO's of plantation companies are likely to be made each month till all the remaining IPOs are completed. Despite widespread speculation these IPOs too will, most likely, be made at Rs.15 per share. Plantations IPOs shall keep the interest in the local bourse alive in the coming months, just as they did in the past couple of months. The likelihood of a amicable settlement to the wages dispute between the plantation management and the workers is good news for the forthcoming IPOs. Record prices currently obtained in the market for our tea is another plus favouring the plantations sector. Tea prices are likely to remain high in the coming year due to two factors. One is the high domestic consumption of tea in India, which customarily occurs during any election campaign there, that would curtail their tea exports. The other factor is the 'El Nino', that is predicted to bring in a prolonged period of dry weather in 1998, severely restricting the supply of tea. With the profits rising year after year, since the privatization programme got under way, this sector is most likely to be the one that will pull the market out of the doldrums in the immediate future.

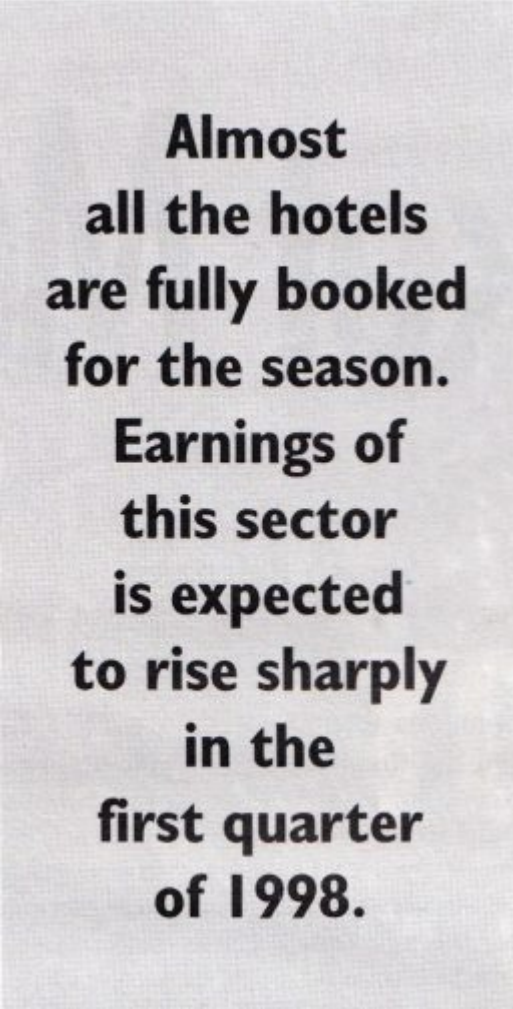
Boom in the Tourist Industry

Tourist arrivals during the month kept the industry beaming with optimism. Galadari is to receive a soft loan of Rs.150m from the Government to meet a part of the cost of repairing the sections damaged by the Fort bomb blast. Almost all the hotels are fully booked for the season. Earnings of this sector is expected to rise sharply in the first quarter of 1998. Indonesian subterranean fire and the accompanying, unprecedented, environmental pollution and hazard to air traffic shall keep the tourists away from such popular resorts like Bali. The tourists scared away by the terrorist attacks by religious fanatics in Cairo are looking Eastwards. If the Indonesian fire, which subsided somewhat with the onset of the rainy season, flares up again, as it is most likely to, we could expect an increased number of tourist arrivals from Down Under, during the winter season in the Southern Hemisphere, in July. On the other hand the heavily depreciated South East Asian currencies have made holidays in those countries cheaper than ever before. If we are to maintain our competitiveness the monetary authorities should

act fast and bring the Rupee down to its appropriate value.

Impact of War & Politics

Markets are keenly monitoring the developments in the war front in the North and the East. The Hotel & Tourism sector's



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current strong position can easily be lost by any more terrorist attacks, especially on H&T industry related targets. The future of our financial markets is closely entwined with the arrival at a lasting solution to the, economy crippling, ethnic war. The opposition UNP is due to come up with their counter proposals for a political solution to the problem, shortly. If the ruling PA government could arrive at some compromise political package, acceptable to the opposition, the markets would definitely react in a very positive manner. Successful completion of the local polls in the North, for which nominations were called and accepted during the month, would go a long way in convincing the world that the government is effectively, getting the situation, in the crisis areas, under control. This would assist, in no small way, the process of confidence building,

essential to attract direct as well as indirect foreign investment to Sri Lanka.

International Market Influence

The trend setting movements at the Colombo Stock Exchange are, in almost every occasion, a direct result of foreign participation. Activity of foreigners usually account for a substantial proportion of the market turnover. In the month of December, for instance, foreign purchases accounted for 40.24% of the month's turnover. Therefore the trends and sentiments in international markets, especially those of the regional markets, affect the mood at the local bourse. The merciless battering received by the Far Eastern currencies and equity markets in the recent past shook the confidence of the international players, in the Asian region as a whole, to the core. Though there is general consensus among market analysts, that the economies in the Asia-Pacific region shall dominate the global economy in the next millennium, there is strong optimism regarding the ability of European and US economies, and hence their equity markets, to come up with spectacular performance in the next two years. This is probably a reason for the lack of interest in our local market, shown by the foreigner investors, despite the availability of solid blue chips at absolute bargains.