

# JUPITER CAPITAL PARTNERS

## Sri Lanka Private Equity Market Newsletter

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*Liberalization of private debt market is likely to attract more private equity investors to private capital market. Although current market interest rates have fallen substantially, still Sri Lanka's interest rates are higher compared to other markets.*

### PE DEALS & OTHER PE NEWS

**SG Holdings Global (Pvt) Ltd., a Singaporean firm linked to Sagawa Logistics of Japan, bought a 30% stake in Expolanka Holdings PLC for US\$ 48 Mn** and announced plans to increase its stake to at least 51% through a mandatory offer. Expolanka's promoters' partial exit, though at market price, is at a 23.5% discount to the price at which company went public in 2011. Company's US\$ 18 Mn IPO in 2011 also came under spotlight due to another partial sell down by founding promoters at 57% discount to IPO price (to several local PE investors a few months prior to the IPO). Expolanka, which was earlier positioned as a diversified company, has been divesting its non-core assets to focus on core logistics and transport businesses. For the FY 2013/14, firm reported 34% increase in profits to US\$ 10.9 Mn on an 8% top line growth to US\$ 417 Mn. Expolanka's bottom-line for 2013/14 includes US\$ 7.6 Mn reported as other income and gains comprising profits from divestments.

**Hong Kong based CLSA (Credit Lyonnais Securities Asia) invested US\$ 2 Mn for a 25% stake in CT Smith Holdings.** CT Smith Holdings is a leading player in Sri Lankan capital market and has stock broker business, advisory firm, and a fund management arm (which manages mutual funds). Company's stock broker unit accounts for around 40% of foreign trading activity in Colombo bourse, and CLSA has channeled around 70% of CT Smith's foreign businesses. **CLSA which is now owned by China's CITIC Group is also likely to encourage more Chinese portfolio investments in Sri Lanka.** Earlier this year India Infoline exited its loss making Sri Lanka stock broking and asset management businesses after two and half years since entering Sri Lankan..

**A Malaysian PE investor is expected to infuse US\$ 2 Mn for a 15% stake in a Malaysian venture promoted by Sri Lanka's Hybrid Homes.** Hybrid Homes converts ship containers into living spaces and other commercial uses like modular shops. Sri Lanka's **Frontier Capital Partners**, a financial advisory firm has seeded Hybrid Homes with a million dollar investment.

In debt finance deals, **Standard Chartered Bank announced a US\$ 100 Mn deal with John Keells Holdings PLC.** Funds are to part finance company's US\$ 650 Mn mixed property project commenced recently. Last year company raised US\$ 177 Mn through a rights issue for this project.

According to new foreign exchange rules, **foreign PE investors can now freely participate in private debt issues** without having to obtain approvals. Earlier foreign investors could freely participate only in government and other listed corporate bonds. New regulation is likely to offer more flexibility in structuring PE deals in Sri Lanka. However, investing in tradable debt securities carry tax advantages compared to private debt investments.

Many **Sri Lankan PE/investment firms are experiencing increase in deal flow.** Slow growth in private sector credit also hints shifting preference to equity funding over debt funding. Another reason for increase in PE dealflow is the lack of investor interest in IPO market. As interest rates are expected to remain low in the medium term, some excess capital in the financial system is likely to be channeled to PE market searching higher return. However, there are only a handful of financial intermediaries focusing on channeling funds into primary private capital markets.

## OTHER BUSINESS & INVESTMENT NEWS

India's **Tata Housing** finalized a deal with Sri Lanka's **Urban Development Authority** for a US\$ 430 Mn mixed development project. Under the proposed deal which was under negotiation for some time, Tata Housing will bear the cost of relocation and developing alternative housing for over 500 low-income households and over 150 small shop owners in 3 acre plot. Another 5 acre plot will be utilized for mixed use commercial development.

Another property project announced in May is the US\$ 3.2 Mn serviced apartment project promoted by **Macksons Group** – a local business group engaged in manufacturing paints.

**Raigam Wayamba Salterns PLC** said it is increasing production of pure powder dried salt with an investment of US\$ 1.9 Mn. With the proposed expansion, company is aiming to cater to country's total demand of dried power salt estimated at 10,000 MT per year.

State owned **Ceylon Petroleum Corporation** has entered into a joint venture with Malaysia's **Hyrax Oil** to build a US\$ 9 Mn lubricant blending plant. This venture will mainly cater to growing local demand.

Bombay Stock Exchange listed Indian FMCG firm **Future Consumer Enterprises Ltd** announced that they are investing in a 50% owned joint venture in Sri Lanka to manufacture oats and breakfast cereals.

**Noorani Estate (Pvt) Ltd.**, a leading poultry firm announced a US\$ 7.5 Mn expansion plan. Company currently sells eggs and day-old chicks. Proposed expansion plan includes diversifying into ready-to eat meat products market.

**VVS Holdings Lanka**, a Chinese owned firm said they plan to expand gems and jewellery business in Sri Lanka. Company expects to cater to growing gems and jewellery market in China. Company recently became the single largest shareholder in **Blue Diamonds Jewellery Worldwide PLC**, a specialist diamond jewellery maker listed in the Colombo bourse.

Danish solid tire maker **Starco Europe SA** is planning to expand its Sri Lankan operations to enhance capacity and production flexibility. **Starco Lanka (Pvt) Ltd** commenced producing solid forklift tires in 2012 with a US\$ 4.4 Mn investment. **Montanstahl AG**, another privately owned Swiss company producing stainless steel shapes also said it is looking at establishing a manufacturing base in Sri Lanka.

Toronto Stock Exchange listed **Elcora Resources** has signed a deal to acquire a 40% stake in Sri Lanka's **Sakura Graphite (Pvt) Ltd**. Sakura is re-developing a historical graphite mine spanning 70 acres. In another development related to graphite mining ventures, **Saint Carbon Inc.**, another Canadian listed mining firm said it had amended its Sri Lanka deal in **Han Tal Holdings (Pvt) Ltd**. Australia's **MRL Corporation** also said its stock price continued to rise as the company is preparing to start commercial production in several (historic) mines in Sri Lanka. MRL holds an exploration license covering 6,300 hectares.

**Scandinavian Agritex Co. Ltd.**, a UK based agricultural technology and textiles company is reportedly venturing into organic cotton farming in Sri Lanka. Company has recently struck a funding deal with a Middle Eastern investment firm.

Two new hotels commenced operations during May. **Centara Ceysands Resort and Spa** is **Softlogic Holdings PLC group's first leisure sector venture** to commence operations. Softlogic Group spent US\$ 24 Mn to redevelop the property it acquired for US\$ 7 Mn in 2010. Thailand's **Centara** is managing the hotel. Newly built **OZO Colombo**, a 159 room business hotel is a US\$ 34 Mn investment by **Sino Lanka Hotels**. Sino Lankan Hotels is a venture promoted by several local and overseas investors. Thailand's **Onyz Hospitality Group** is managing the hotel under OZO brand. (see pictures on right)

**Diesel Motor Engineering Co PLC**, distributor of **Mercedes Benz** vehicles in Sri Lanka opened South Asia's most modern service cum sale center in Colombo. This US\$ 27 Mn facility was opened as company marked its 75<sup>th</sup> anniversary of selling Mercedes Benz vehicles in Sri Lanka.

*In 2013 Sri Lanka exported gems worth US\$ 109 Mn (down from US\$ 111 Mn in 2012). Approx 90% of exports are sapphires and "blue" color sapphires accounts for over 50% Sri Lanka's gem exports (in terms of value).*



*OZO Colombo (pictured above) is the latest addition to business hotels in Colombo.*

*Centara Ceysands Resort and Spa (pictured below) is a re-developed hotel property under new ownership/management.*



## POLICY INITIATIVES & UPDATES

*Sri Lanka differs from many other frontier and emerging markets in demographic trends. Recent research report issued by Renaissance Capital also notes that Sri Lanka's investment case is weakened due to slow down in the growth in working age population.*

Sri Lanka's **Parliament revised law to increase retirement age of government officials to 70 from current 60**, based on the aptitude of the employee. The moves come as many government institutions continued to avail the service of persons up to age of 65 due to shortage of experienced professionals in some fields.

**Central Bank of Sri Lanka announced further relaxation of foreign exchange controls.** Among several relaxations, significant measures include allowing foreign investors to participate in private debt investments (non listed debt investments or debentures). Another important change is that Sri Lankans who earn foreign income are now able to borrow foreign currency loans from licensed commercial banks.

As a measure to combat slow growth in private sector credit, **Central Bank is proposing to provide state guarantee to gold backed loans.** Private sector credit growth slowed to 4.3% in May amid easing of interest rates further. According to analysts slow down of credit is mainly due to sharp decline in gold loans. As gold prices dropped lending institutions cut lending against gold collateral. In 2013 non performing bank loans jumped to 5.6% from 3.7% year ago and gold loans accounted for 75% of the increase according to reports.

## COLOMBO STOCK MARKET UPDATES

*M&A activities contributed a larger share of net foreign portfolio investment inflows into Colombo Stock Market during last few years.*

Stock Market's main **All Share Price Index gained by 0.6% in April** on top of 4.3% gained in April. Stock market has increased by 5.9% for 2014. Average daily turnover improved to US\$ 9.5 Mn from US\$ 8.5 previous month. May recorded a net foreign inflow of US\$ 73.6 Mn thus reversing cumulative net outflow of US\$ 55.1 recorded as at end of April.

First ever public bond issue by a plantation firm was successfully closed in May. **Kotagala Plantations PLC** raised US\$ 7.6 Mn through a series of 4-7 year bonds with rates ranging from 14.25% - 15.5%.

## ECONOMIC HIGHLIGHTS

*77% of first quarter FDI has come in to tourism, utilities and infrastructure related projects. Industrial and apparel manufacture related projects have received only 15% of FDI.*

**Inflation (YoY) dropped to 3.2%** from 4.9% in April. Average annual inflation rate also eased to 5.3% from 5.6% month ago. As Central bank held policy rates unchanged, treasury bill rates remained mostly unchanged at 6.56%. Three month treasury bill rate year ago was 8.73%. Commercial Bank average deposit rate dropped to 7.74% in May compared to 8.06% last month (and 10.74% year ago). Commercial Bank average lending rate stood at 14.18% as at end of April. Sri Lankan rupee appreciated marginally by 0.12% to close the month at 129.00 – 131.88 to the US\$. Private sector credit growth further slowed to 4.3% (YoY) in March compared to 4.4% month ago.

**Exports for Q1 2014 reached US\$ 2.8 billion which is a 19.1% growth compared to last year.** Export growth was helped by strong 20.5% growth in textiles and apparel exports which comprise 75% of country's exports. Imports grew at a slower pace of 3.6% to US\$ 4.67 billion. Foreign remittances also grew by 12.2% to US\$ 1.6 billion. Earnings from tourism during first quarter was US\$ 0.6 billion which is a 34% increase compared to last year. Tourist arrivals increased by 24.8% compared to 2013. Foreign inflows to government (Including international bond offers) also increased by 18.3% to US\$ 2.2 billion.

According to a latest news release **Sri Lanka achieved US\$ 0.44 billion FDI during first quarter** compared to US\$ 1.4 billion recorded for the full year in 2013.

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