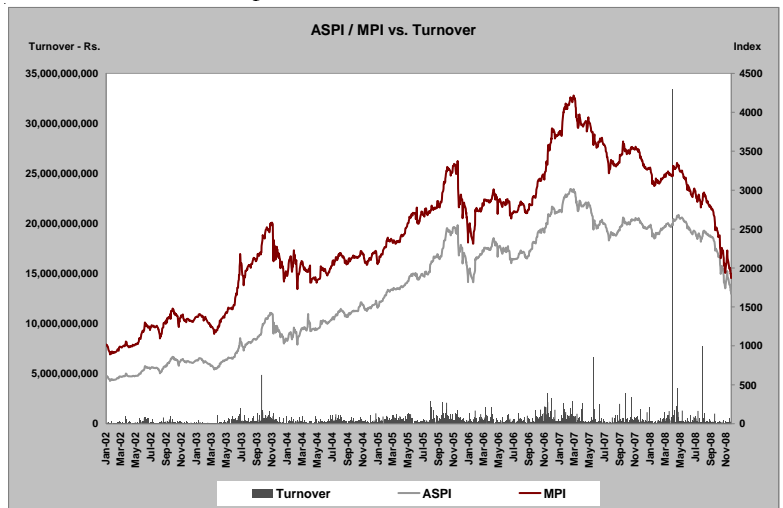


Overview of Trading Activity

- After a healthy CAGR of 25.4% from 2003 to 2007, the benchmark ASPI declined 7.3% in CY07 and 7.2% in 1HCY08 on concerns stemming from the return to hostilities, spiraling inflation and increasing opportunity costs. Mirroring the decline in the indices, average daily turnover has slipped to Rs.396m during the 1HCY08 (ex. SLT 35% stake transaction), from over Rs.440m through CY05-07. With concerns over global recession, the ASPI has tumbled 32% from July to date accompanied by a further deceleration in activity.
- Strategic acquisitions have boosted net foreign inflows to a daily average of Rs.70m YTD compared to Rs.47m in CY07.



Chinthaka Ranasinghe

chinthaka@jkstock.keells.com

John Keells Stock Brokers (Pvt) Ltd.

Company No. PV 89
130, Glennie Street,
Colombo 2,
Sri Lanka.

Tel: 94 11 242 1101-9 (Gen.)
94 11 234 2066/7
94 11 243 9047/8

Fax: 94 11 234 2068
94 11 232 6863

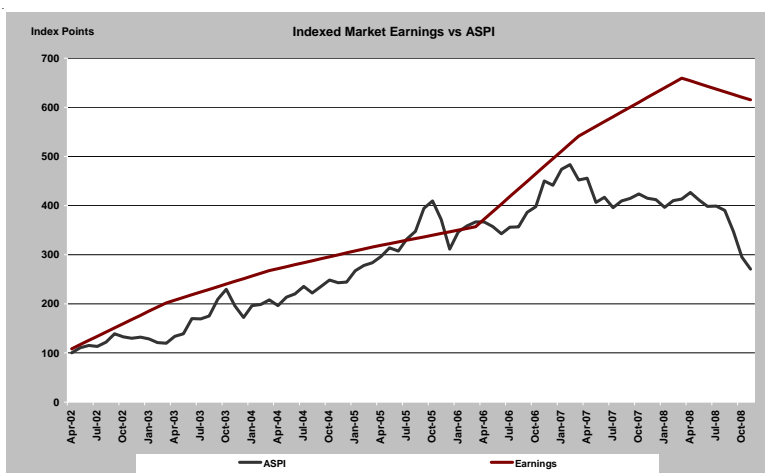
November 2008

Corporate Earnings

- Corporate earnings grew by a CAGR of 24% through FY04-FY08 driven by Telcos, Conglomerates and Banks, despite escalating security concerns.
- However, the combined weight of high borrowing costs, escalating inflation have begun to bite into earnings, with earnings for the July-September quarter indicating a 15% decline on results released to-date. Whilst inflationary pressure will decline especially with reduced energy and transportation costs following reduced diesel and furnace oil prices, additional worries have arisen with the global woes, as export oriented industries and bank lending to the affected sectors tighten up. We expect earnings to decline by 10% in FY09. The relatively mild decline is influenced by the banking sector whose predominantly December year end companies enjoyed a relatively stable first half.



- ✓ With inflation subsiding, the key issue in FY10 will be the duration of the global economic meltdown.



Valuations and Recommendation

- ✓ Despite the sharp earnings growth during FY04-08, the market has markedly lagged behind, even during its period of sharp growth in FY03-06. The gap has widened with the current downturn in the market, with the Colombo bourse currently trading at 7.63x FY09E earnings.
- ✓ Whilst standalone valuations are attractive, it should be treated with caution, when viewed in the context of the entire spectrum of the global financial and commodity markets searching for base value, with the search daily trekking downwards.
- ✓ However, despite the global gloom, there are emerging positive trends, with the most promising being the strong gains made by the military, leading to indications of a marginalization of the LTTE. The economic positives of a clearing of the North combined with our anticipation of a sharp drop in inflation can set up the stage for an economic rebound, global woes notwithstanding.
- ✓ The short term concerns however remain. Gilt edge rates currently at 19%+, sets a high hurdle rate compounding the fears over the fallout of the global crisis. And, the conflict can well escalate when the cornered LTTE tries to break free, before the North is finally cleared. However, with the longer term emerging positives in mind, further short term weakness can be utilized to accumulate long term positions in a buyers market.

Country	P/B (x)	12 mth Trailing PER (x)	12 mth Forward PER (x)	ROE
China	1.43	8.71	8.16	16.24
Hong Kong	0.91	6.87	9.02	13.40
India	2.06	10.18	10.01	21.34
Indonesia	1.60	8.40	7.21	16.89
Pakistan	1.69	6.52	7.29	25.82
Philippines	1.25	9.55	9.86	14.09
Malaysia	1.29	8.78	9.55	16.79
Singapore	0.96	6.58	7.56	13.16
Taiwan	1.06	8.40	9.61	13.76
Thailand	0.97	5.95	5.52	14.16
Emerging Markets	1.58	9.47	7.38	19.86
Asia Pacific Emerging Markets	1.32	8.70	8.81	15.80
*Sri Lanka	1.06	6.86	7.63	13.82

Source: S&P/Citigroup Global Equity Indices
* JKSB Research