Share market scandal erupts in Sri Lanka

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A scandal over the manipulation of shares on the Colombo stock exchange has erupted in recent weeks after former Sri Lankan Securities Exchange Commission (SEC) chairman Thilak Karunaratne accused government ministers of acting in league with speculators.

Karunaratne was pressured by President Mahinda Rajapakse to quit his position, just nine months after his appointment. The apparent reason for his ouster was that the SEC had commenced investigations into 17 companies accused of abusing the share market.

After his resignation, Karunaratne told the media of "daylight robbery" by a "stock market mafia" closely connected to government leaders, including Rajapakse.

Karunaratne is a politician as well as a businessman. He was a founding leader of the Sinhala chauvinist Jathika Hela Urumaya (JHU), then joined the right-wing United National Party (UNP). Just before the presidential election in January 2010, he switched to Rajapakse's Sri Lanka Freedom Party (SLFP).

The SEC is the "regulating authority" appointed by the president to oversee the Colombo stock market. Rajapakse has used his powers to install chairpersons loyal to the government. Karunaratne's predecessor Indrani Sugathadasa, who resigned in similar circumstances, is the wife of the president's secretary, Lalith Weeratunga.

The latest scandal has provided a glimpse into the operations of a parasitic layer of financial speculators who have been nurtured by the Rajapakse government since the end of the country's longstanding civil war. After the defeat of the Liberation Tigers of Tamil Eelam (LTTE) in May 2009, the Colombo all share price index soared—from 1,631 points in 2008 to 7,800 points in February 2011.

Rajapakse pointed to the rocketing share prices as proof of his government's economic success. The financial press hailed "one of the best performing share markets in the world," but the "success," amid the global financial crisis, was built on rampant speculation. In early 2011, the bubble burst and the index is currently hovering around 5,000 points. Foreign investors have been withdrawing funds and Colombo is rated as one of the world's "worst performing" markets.

Karunaratne admitted that speculation had been a major factor in the share price rises. "[T]he major contribution came from people who used unfair means in pumping up the market, which made it reach extreme high levels," he told the media.

The former SEC chairman has not named the 17 companies that he placed under investigation. But he hinted at their identities by citing cases where prices had dramatically risen between the end of 2009 and end of 2010. Over that year, the share prices of Dankotuwa Porcelain, Blue Diamonds, Asian Alliance Insurance, Lanka Hospitals and HVA Foods stock increased by 226, 270, 177, 204 and 394 percent respectively.

A *Sunday Times* editorial last weekend, entitled "Jackals and mafia of crooks," commented: "It is common tattle that many of the 17 'suspects' are closely linked to the ruling elite. This linkage extends to the level of financing the political campaigns of the rulers, and even more, acting for them as front men."

In a scheme known as "pumping and dumping," major dealers encouraged investors to put money into

particular shares, promising huge returns. When the share price reached a certain level, the dealers sold out, making staggering profits, and prices fell sharply. Small share holders, who had in many cases invested their savings and pensions, were hit with heavy losses.

The Central Bank encouraged this speculative frenzy by releasing money from the Employees Provident Fund (EPF), the country's biggest pension fund, to purchase shares, including in ailing companies such as Galadari Hotels, Laugfs Gas, Piramal Glass Ceylon, Ceylon Grain Elevators and Browns. The release of EPF cash for private sector investment was a longstanding demand of the International Monetary Fund (IMF).

The results have been disastrous. For example, the EPF purchased 23.7 million shares in the loss-making Galadari Hotels at a price of 32.50 rupees a share in 2010 from Nawaloka Hospitals. By July 2012, the share price had plummeted to 11 rupees, resulting in a loss of 500 million rupees for the EPF. Overall, the EPF had lost about 6 billion rupees by the middle of this year.

The newly-appointed SEC chairman, Nalaka Godahewa, is well connected to the government as well. He was given the job despite heading the Colombo Lands and Development (CLD), which is also under a cloud for share manipulation.

The CLD had been a prominent Colombo real estate developer but was restructured into a joint venture with the Urban Development Authority (UDA). In 2010, the government put the UDA, a civilian body, under the Defence Ministry, which is headed by Gotabhaya Rajapakse, the president's brother. The UDA is central to the government plans to develop Colombo as a major "commercial hub," primarily through the eviction of some 70,000 shanty dwellers. The security forces have already forcibly removed hundreds of families.

One of those recently identified by the media as a member of the "stock market mafia" also has government connections. Dilith Jayaweera, head of Divasa Equity, recently admitted meeting with Gotabhaya Rajapakse to discuss share market affairs. Gotabhaya Rajapakse arranged for Jayaweera, who was known for demanding a free hand for share dealers, to meet with SEC chairman Karunaratne.

The eruption of the share market scandal points to deep dissatisfaction among layers of the corporate elite with the Rajapakse government and its business cronies. The Ceylon Chamber of Commerce has expressed concern over Karunaratne's resignation, warning that it would send the wrong signal to foreign investors.

These divisions in ruling circles have opened up amid the worsening global economic breakdown, which is impacting heavily on the Sri Lankan economy through declining exports and an emerging balance of payments crisis. The scandal has revealed a parasitic layer of speculators and share price manipulators operating in collaboration with the government, which will inevitably attempt to pass the burden of the losses onto the working people.