



First Capital
First Capital Research

“CUT EXPOSURE; COUNT ON SEQUEL”

First Capital Fixed Income Report – 05th Sep 19

Lead Analyst: Atchuthan Srirangan
Secondary Analyst: Dimantha Mathew

1.0 Previous Recommendation

Jul 2019 Re Cap

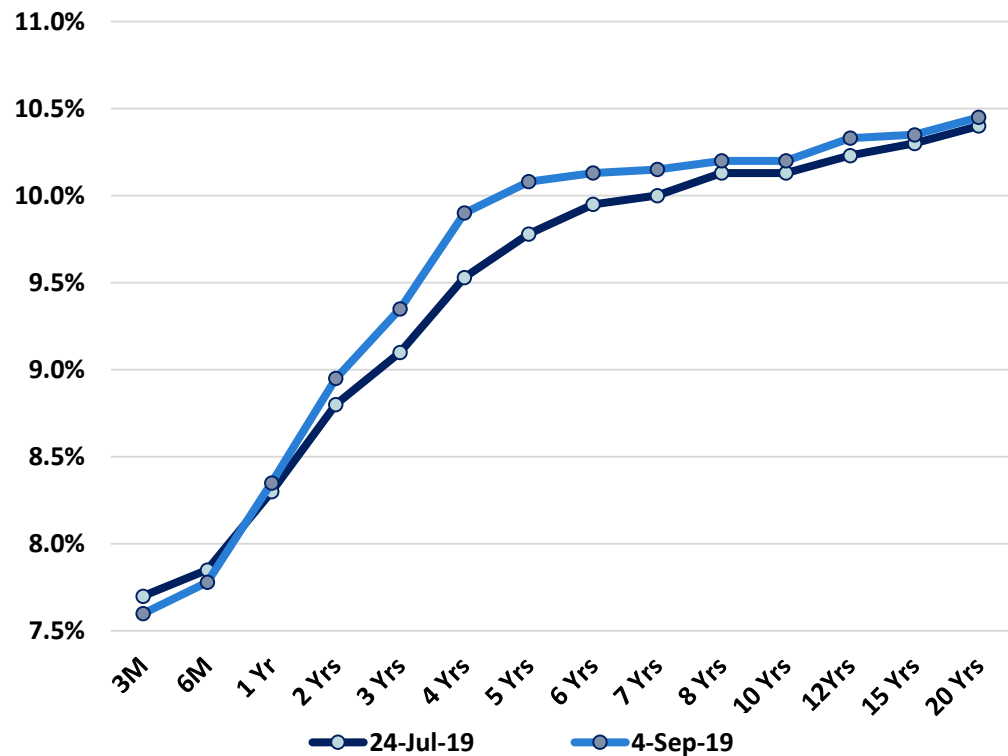
29th Jul Recommendations and Yield curve movement

Recommendation for 29th Jul 2019

– Portfolio Recommendation: **Reduce overall portfolio to 45% from 60%.**

- Decrease Carrying Portfolio to 30% from 50%.
- Increase Trading Portfolio to 15% from 10%.

We recommend to cut 2021 and 2022 maturities of the carrying portfolio amidst the significant reduction in yields while we recommend an increase in 2023 and 2024 maturities in the trading portfolio amidst the slight rise in yields.



2.0 New Recommendation

Portfolio Recommendation

Surprise CBSL policy rate cut has aggravated foreign selling in government securities adding more pressure on the rupee in coming weeks. **Present macro economic environment, we recommend to maintain exposure in the carry portfolio while completely exiting the trading portfolio considering the volatile environment.** Yields of mid to long tenors 4Y, 5Y, 6Y and 7Y are trading at attractive price levels to accumulate. We recommend to **avoid accumulation in the secondary market** in order to bid for the auctions.

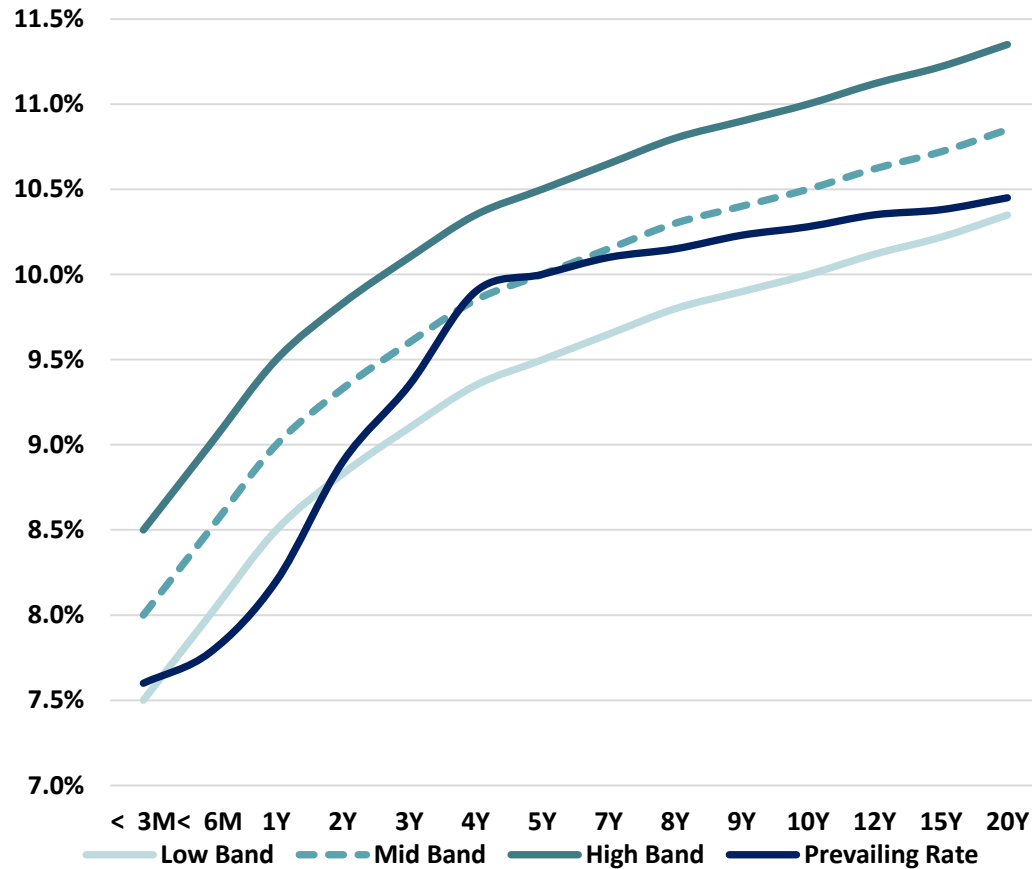
Fixed Income Portfolio Recommendation

Portfolio Recommendation: **Reduce overall portfolio to 30% from 45%.**

- Maintain Carrying Portfolio at 30%.
- Decrease Trading Portfolio to 0% from 15%.



Yield Curve Recommendation



Tenure			Current Yield	Recommendation
< 91 Days	< 3M	Short	7.60%	Sell
< 182 Days	< 6M	Short	7.78%	Sell
< 364 Days	1Y	Short	8.35%	Sell
01-May-21	2Y	Short	8.95%	Sell
15-Jul-22	3Y	Short	9.35%	Hold
15-Jul-23	4Y	Mid	9.90%	Sell
15-Mar-24	5Y	Mid	10.08%	Sell
01-Aug-26	7Y	Mid	10.13%	Sell
15-Jun-27	8Y	Mid	10.15%	Sell
01-Sep-28	9Y	Mid	10.20%	Sell
01-May-29	10Y	Long	10.20%	Sell
15-Mar-31	12Y	Long	10.33%	Sell
15-Jan-33	15Y	Long	10.35%	Sell
15-Mar-35	20Y	Long	10.45%	Sell

3.0 Economic Health Score

Sep 2019 Economic Health Score

Health score further improves

Primary Criteria	-	55	- 07	-	48
Secondary Criteria	-	13	- 01	-	12

Economic Health Score (Sep 2019) - 60

[As against 68 in Aug 2019 & 53 in Sep 2018 (1 Year ago)]

Changes to Health Score – Priority Criteria

Criteria	Update	Current Score	Add / Deduct Score	New Score
Foreign Reserves	Foreign reserves dropped by USD 519Mn during the month of July to end at USD 8.34Bn which is well above the comfortable level of USD 6.5Bn.	14/15	-01	13/15
Liquidity	Liquidity level shifted to negative territory after 4 months.	12/15	-03	09/15
Inflation	CCPI at 3.4% in Aug mainly due to deflation in food items.	11/15		11/15
Foreign Activity	Net outflow of LKR 25.8Bn in government securities over the last 4 weeks; Foreign holding reduced to 2.0%.	06/10	-02	04/10
Credit	Private credit negative during July 2019.	06/10		06/10
CBSL Holdings	CBSL sold down its treasury bill stock steadily mopping up liquidity generated from dollar purchases.	06/10	-01	05/10




Primary Criteria - 55 - 07 = 48


Changes to Health Score – Secondary Criteria

Criteria	Update	Current Score	Add / Deduct Score	New Score
Rating Outlook	No major changes.	02/05		02/05
External Environment	Rupee started to weaken from 19 th Aug to close at 180.30 on 29 th Aug mainly due to foreign selling in Govt. Sec.	03/05	-01	02/05
BoT & BoP	Trade deficit narrowed to USD 316Mn in Jun 2019, the lowest since Oct 2010.	03/05		03/05
Political Risk	Political stability reinstated to some degree amidst the possible Presidential election in 2019.	03/05		03/05
Investor Confidence	BCI which scaled up to 81 basis points in Jun, dropped to 74 in Jul mainly due to uncertainty around the result of the forthcoming election.	02/05		02/05

Secondary Criteria - 13 - 01 = 12

Revisiting Health Expectations

	3 Months Outlook Jan-Mar 2019	3-6 Months Outlook Apr-Jun 2019	6-9 Months Outlook Jul-Sep 2019	9-12 Months Outlook Oct-Dec 2019
Health Score Estimate	40-50	50-60	65-70	65-70
Risk Level – Jun 2019	High	Medium 	Medium-Low 	Medium-Low 
<i>Previous Expectations – Jan 2019</i>	High	Medium-High	Medium	Medium


Current Period

Risk Levels:- High: 40-50, Medium High: 50-55, Medium: 50-65, Medium Low: 65-75, Low: 75 above

Sequence of Events

9th Nov 2018 - **Reduce overall portfolio to 40% from previous 60%.** Cut Trading portfolio to 5% from 25%. Carrying portfolio to be maintained at 35%.

19th Dec 2018 - **Increase portfolio to 50% from 40%.** Increase Trading Portfolio to 15% from 5%. Carrying Portfolio to be maintained at 35%.

11th Mar 2019 - **Increase overall portfolio to 55% from 50%.** Increase Carrying Portfolio to 45% from 35%. Reduce Trading Portfolio to 10% from 15%.

28th Mar 2019 - **Increase overall portfolio to 70% from 55%.** Increase Carrying Portfolio to 50% from 45%. Increase Trading Portfolio to 20% from 10%.

16th May 2019 - **Reduce overall portfolio to 40% from 70%.** Cut Carrying Portfolio to 40% from 50% and Trading Portfolio to 0% from 20%.

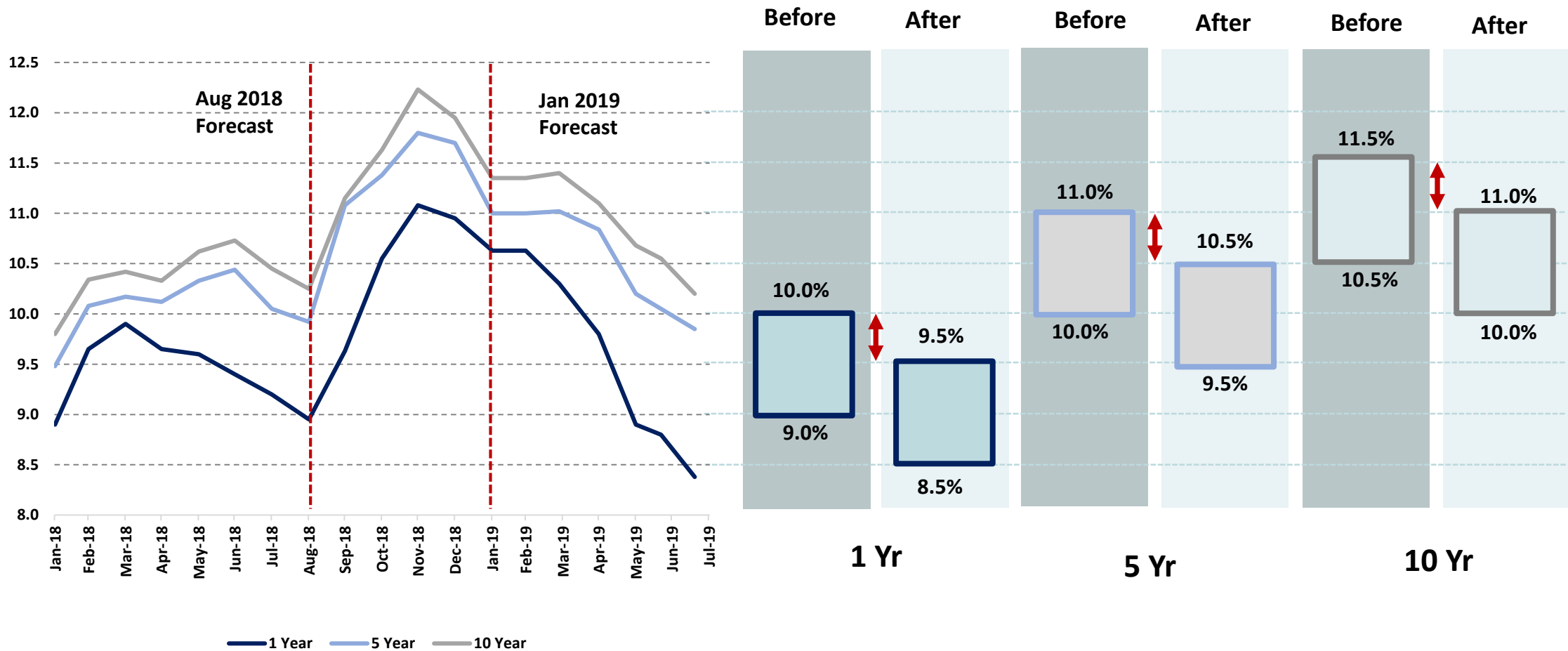
24th June 2019 - **Increase overall portfolio to 60% from 40%.** Increase Carrying Portfolio to 50% from 40%. Increase Trading Portfolio to 10% from 0%.

24th Jul 2019 - **Reduce overall portfolio overall portfolio to 45% from 60%.** Decrease Carrying Portfolio to 30% from 50%. Increase Trading Portfolio to 15% from 10%.

29th Aug 2019 - **Reduce overall portfolio overall portfolio to 30% from 45%.** Maintain Carrying Portfolio at 30%. Decrease Trading Portfolio to 0% from 15%.

Jun 2019 Re Cap

Revision of Bond Yield



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CONTACT US



First Capital

Dimantha Mathew +94 11 2639 853

Hiruni Perera +94 11 2639 864

Atchuthan Srirangan +94 11 2639 863

Nisansala Kuruppumudali +94 11 2639 866

Amanda Lokugamage +94 11 2639 868