



First Capital  
A Janashakthi Group Company

# EQUITY STRATEGY

First Capital Research | 30 Apr 2024

***“Bull run to charge ahead”***

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A close-up photograph of a person's arm wearing a black blood pressure cuff. A hand is shown adjusting the cuff. The cuff has a white arrow pointing left and the text 'INDEX' and 'OK'. The person is wearing a dark blue long-sleeved shirt with a small American flag patch and the letters 'CO' visible.

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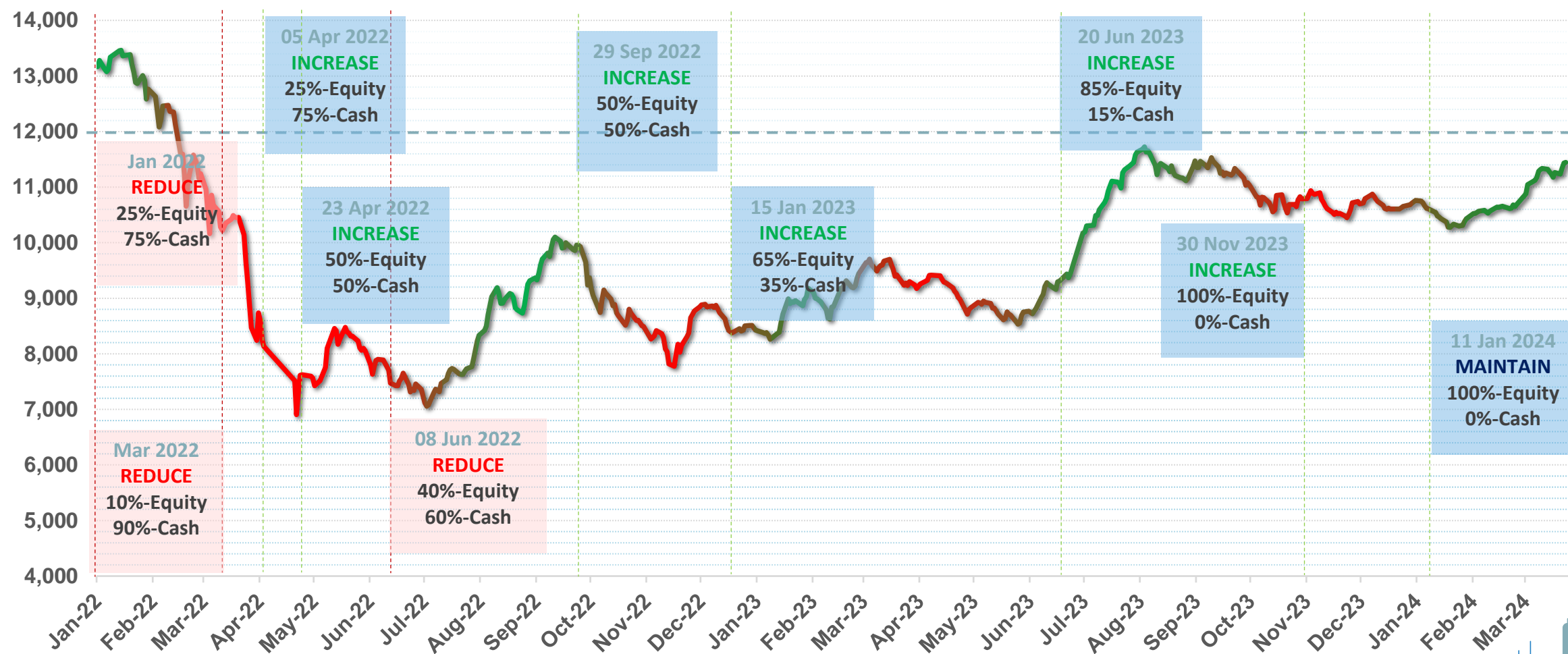
## 05 Top Picks



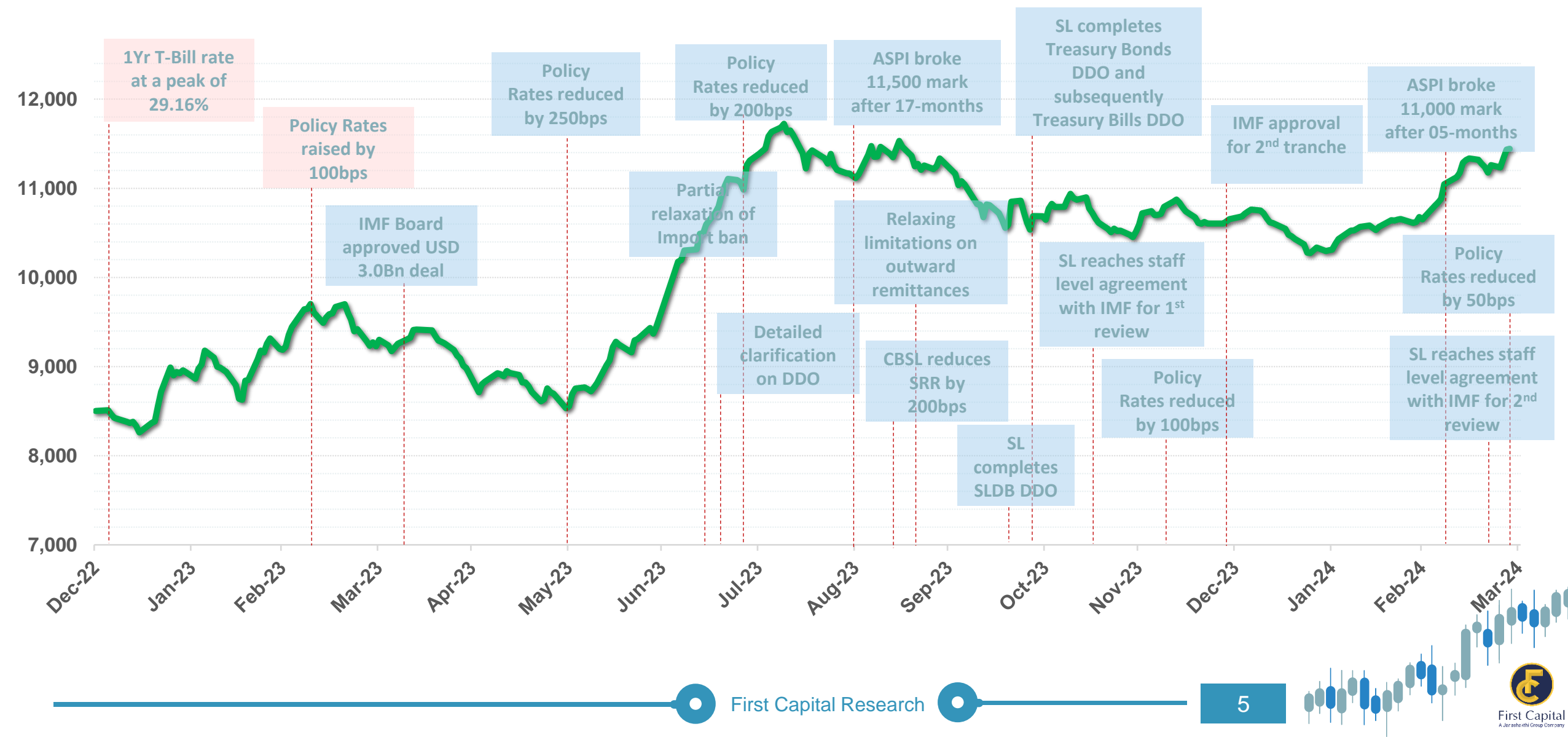
2023 Performance

# Recap 11 Jan 2024

First Capital *Maintains* Equity Exposure to 100% reducing cash to 0%

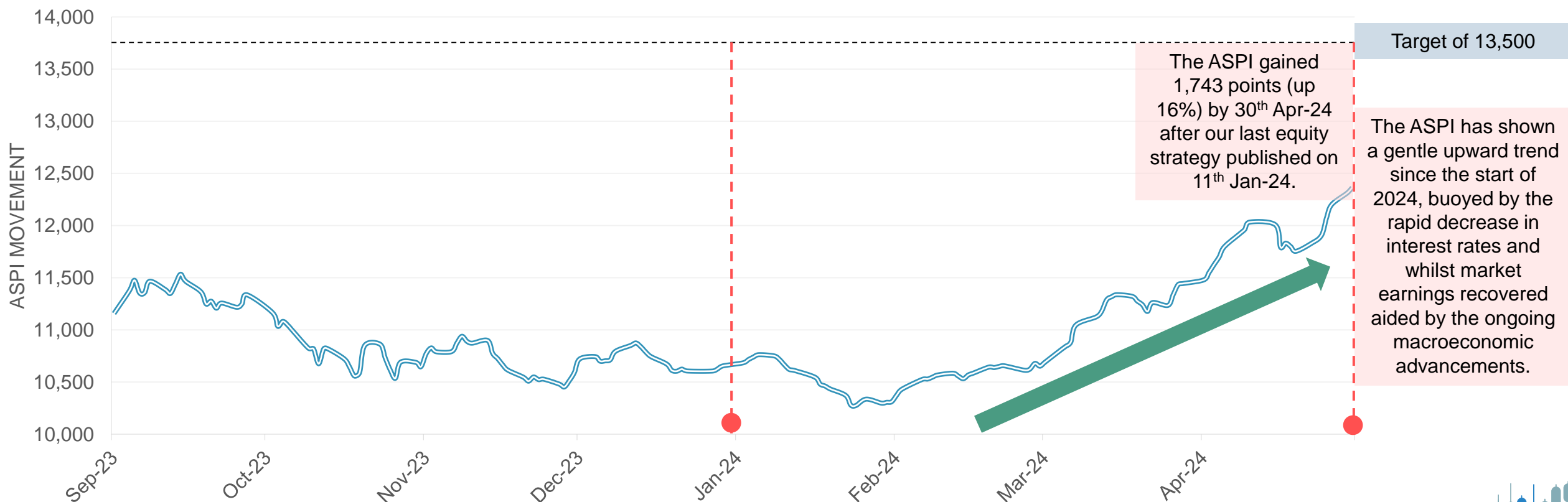


# ASPI performance and key highlights



# Recap: ASPI Movement Sep 23 – Apr 24

*First Capital Research set a target range for ASPI to be 11,000-12,000 for 2023. ASPI peaked in a range of 11,700 during the 2H2023 and fell amidst the delay in finalizing the IMF 1<sup>st</sup> review. However, gradual upswing has been evident as ASPI gained over 1,000 points during the first 4 months of 2024 while the ASPI hiked to 12,000 in April after 2 years.*





# Revving Up for Market Momentum...

- Since our last update, the ASPI observed a persistent upswing during Jan-Mar 2023, almost breaking the 11,500 psychological level closing at 11,479.
- Market earnings have begun to display early signs of recovery in the last two quarters (Sep-23 & Dec-23) at a faster rate than anticipated.
- Accelerated decline in interest rates with AWPLR declining below the 12.0% mark for the first time in nearly 2 years largely aided the positive movement in ASPI.
- Successful progression on IMF front and External Debt restructuring talks has helped reinstate confidence among market participants.
- IMF staff and the Sri Lankan authorities reached the staff-level agreement on economic policies to conclude the second review of the 4-year EFF-supported program, positively impacting the sentiment in the equity market.

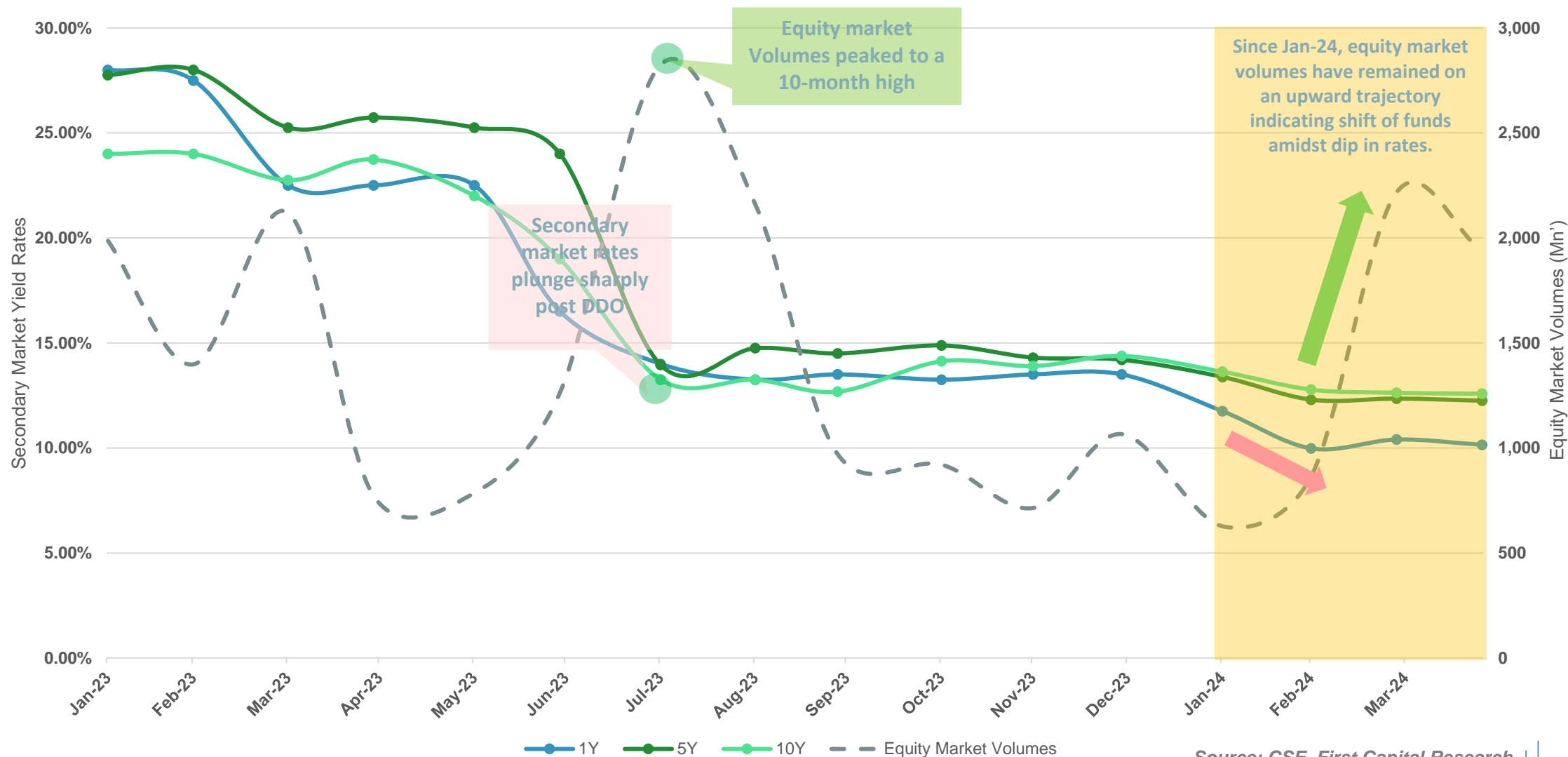




Key Indicators support improvement in investor confidence



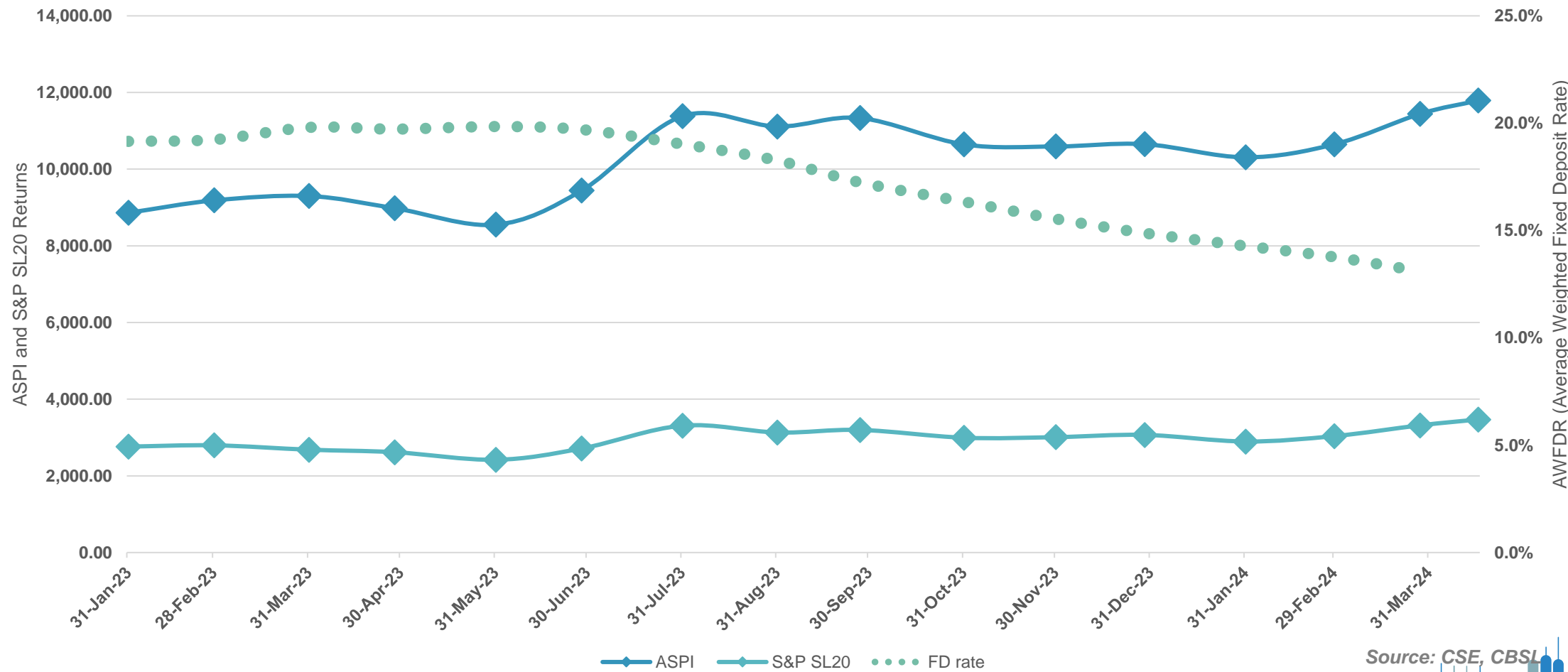
# Market interest rates rapidly ease off, aiding the shift to equity market from Fixed income investments



Source: CSE, First Capital Research

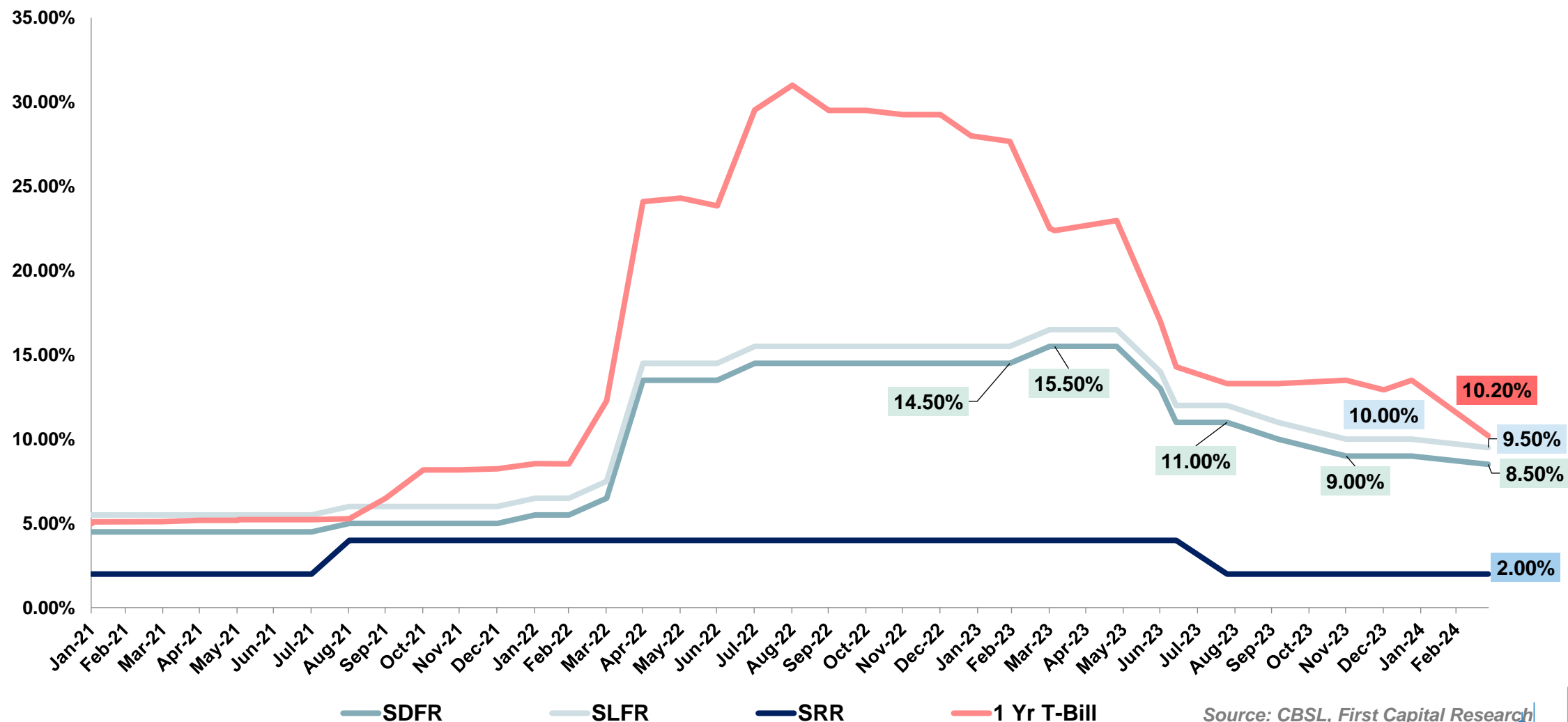
# The stock market is seeing a resurgence in green as it continues its steady ascent, as the AWFDR index takes a downturn

As at Mar-24, Average Weighted Fixed Deposit Rate (AWFDR) has plunged by 670bps cf. Mar-23 in line with the fast decline in policy rates making Fixed Deposits a less sought investment option. As AWFDR plunges low, equity market return have begun to thrive on the green territory signaling strong bullish sentiment.



Source: CSE, CBSL

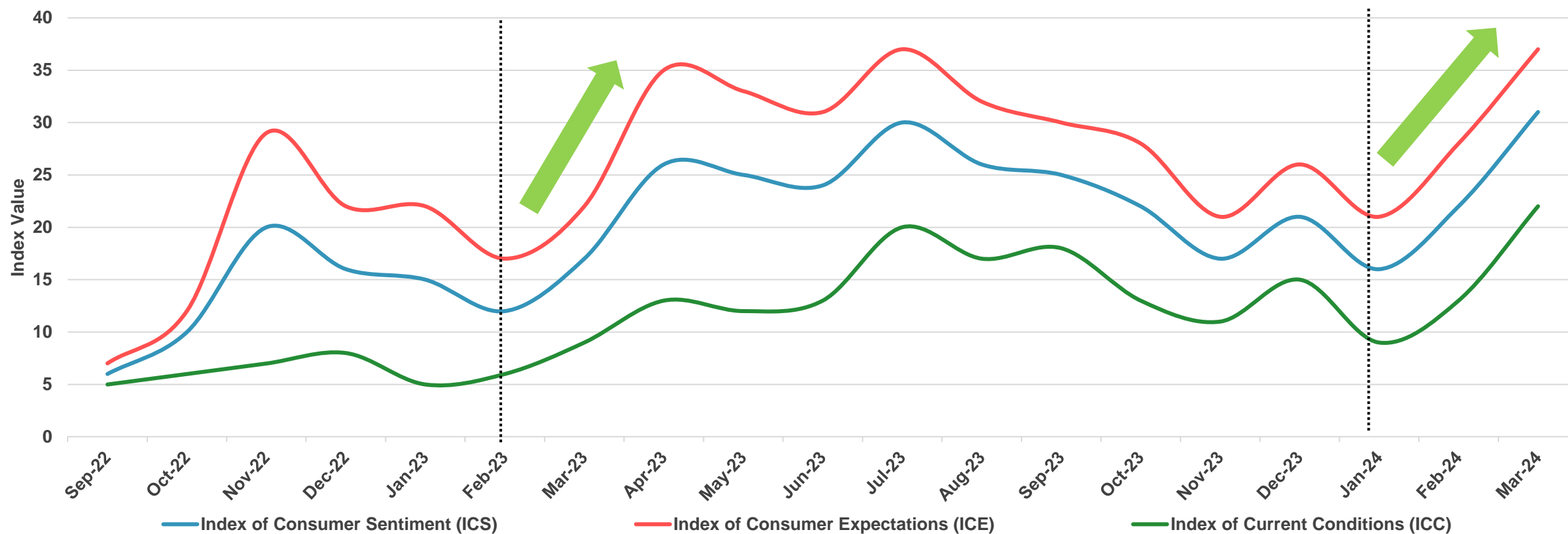
# CBSL Policy Rates further cut by 50bps in March Policy meeting, further supporting the downtrend in interest rates



Source: CBSL, First Capital Research

# Consumer sentiment strengthens despite the VAT hike upto 18%, whilst consumer expectations are on the bright side

As the Business communities adapt to the current economic conditions following the value-added tax (VAT) hike and the consumer confidence in the economy and expectations of sustaining sales volumes over the next year have contributed to the rise in business confidence. Additionally, increased interest in expanding the workforce within the corporate sector, also has shown improvement since January and February.



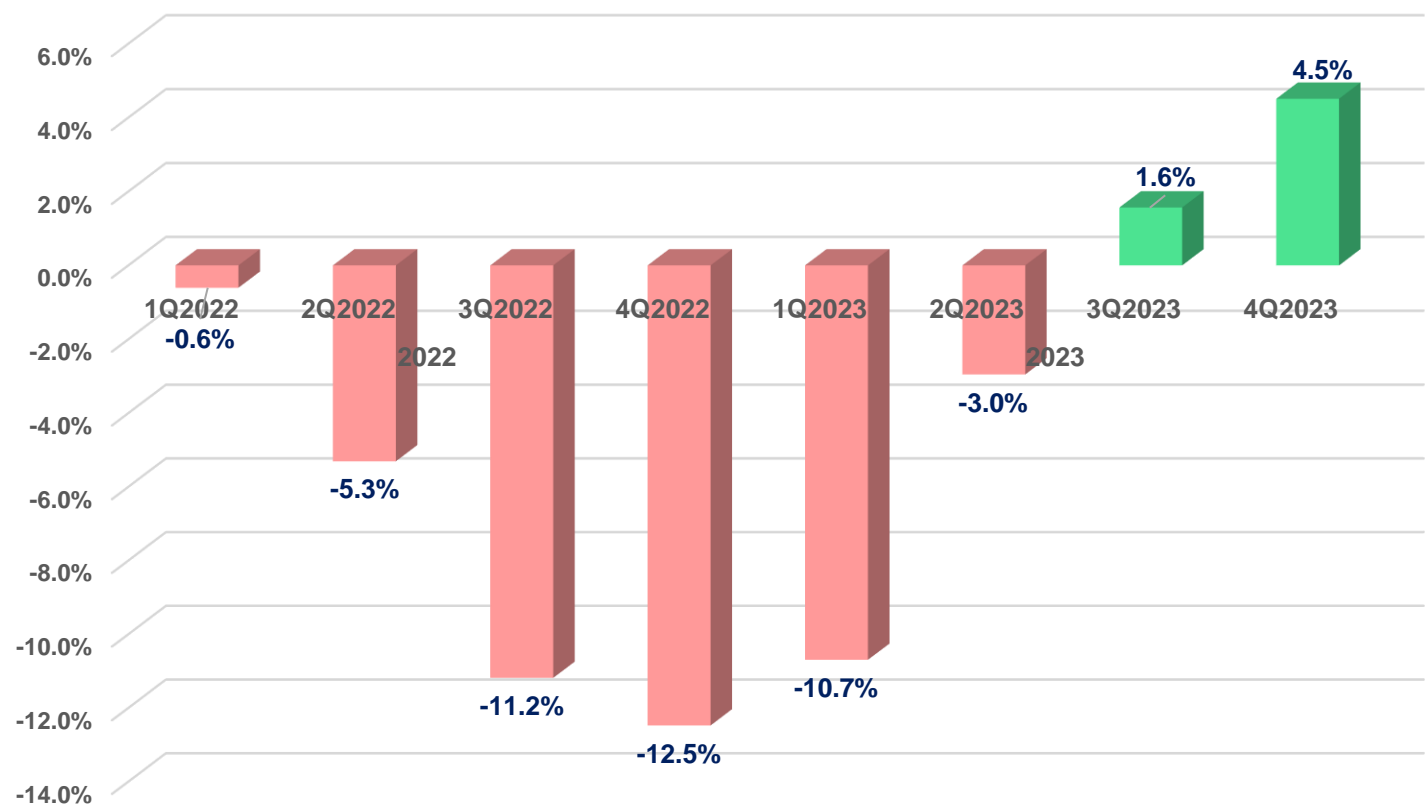
Source: IHP and LMD






# GDP turns around positively, signaling the resurgence of economic activity after enduring a tumultuous 2-year-history of crises

In 2023, the Sri Lankan economy displayed a mixed performance, with negative growth in the first half of the year followed by a return to positive growth in the latter half. Despite initial uncertainty, stability ensued with increased foreign currency inflows from workers' remittances. The anticipated tourism revival towards the year's end boosted economic prospects. However, challenges persisted in sectors like manufacturing and construction due to high input prices. Agricultural activities faced input availability issues but still reported favorable growth rates in many crops and paddy cultivation.

Real GDP Growth (%)



	2022 Annual -7.3%	2023 Annual -2.3%
 Agriculture	-4.2%	2.6%
 Industry	-16.0%	-9.2%
 Services	-2.6%	-0.2%

Source: CBSL, DCS

# World Bank upgrades growth prospects for Sri Lanka given the faster than expected recovery

## Other Projections

2024E  
+1.8%



2024E  
+1.9%



2024E  
+2.2%



First Capital estimates a GDP growth of +2.0% to +3.0% during 2024E.

2024E

+2.0% - +3.0%

+3.0% - +4.0%

2025E



World Business Markets Sustainability Legal Breakingviews Technology Investigations

Asia Pacific

## World Bank raises Sri Lanka's growth forecast to 2.2% for 2024

By Uditha Jayasinghe



COLOMBO, April 2 (Reuters) - The World Bank raised its forecast for Sri Lanka's economy on Tuesday, projecting growth of 2.2% for 2024 as the crisis-hit nation makes a faster-than-expected recovery from its worst financial crisis in decades.

Sri Lanka secured a \$2.9 billion bailout from the International Monetary Fund (IMF) in March last year, helping it temper inflation, increase state revenues, and rebuild foreign exchange reserves after its economy crumpled in 2022.

## Bloomberg

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Economics

## Sri Lanka's Economy Expands For a Second Straight Quarter

- Authorities are in talks with IMF on next loan tranche
- Lower borrowing costs aid recovery in industrial sector

Sri Lanka's economy expanded for a second straight quarter as industrial activity picked up pace, buoyed by an International Monetary Fund bailout and lower interest rates.

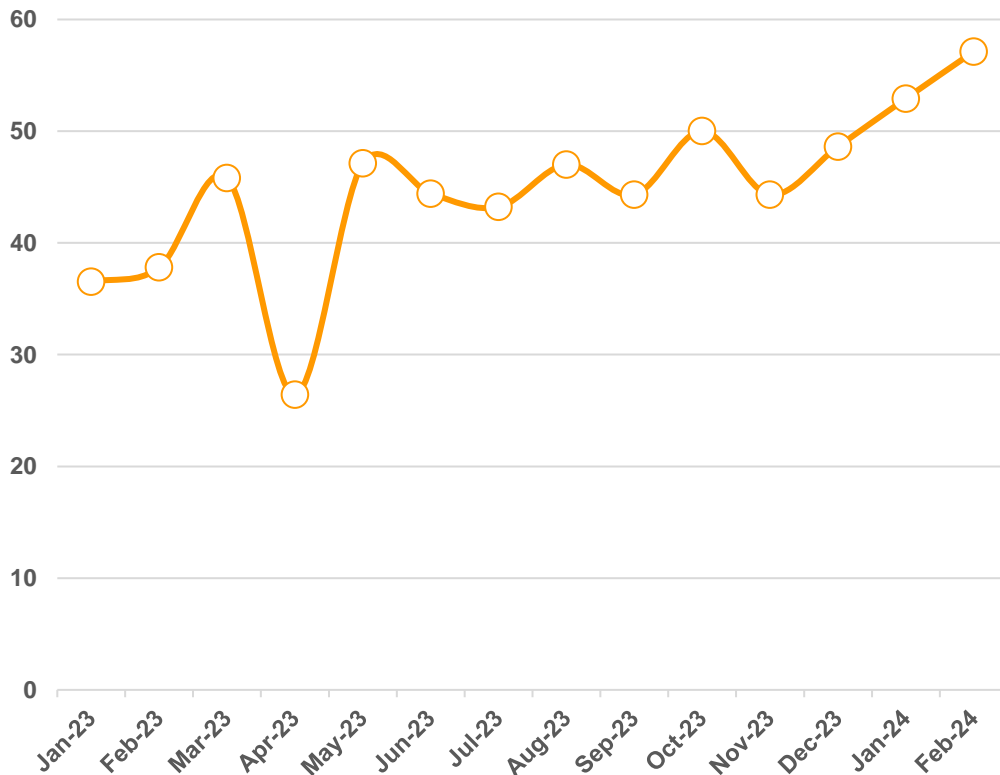
Gross domestic product rose 4.5% in the three months to December from a year ago, the Statistics Department said Friday. That's higher than the median forecast of 3.7% growth in a Bloomberg survey of economists and compares with a print of 1.6% in the July-September period. For the year, the economy clocked a contraction of 2.3%.



# Manufacturing and Construction activities expand, reflecting the economic recovery and improving consumer sentiment

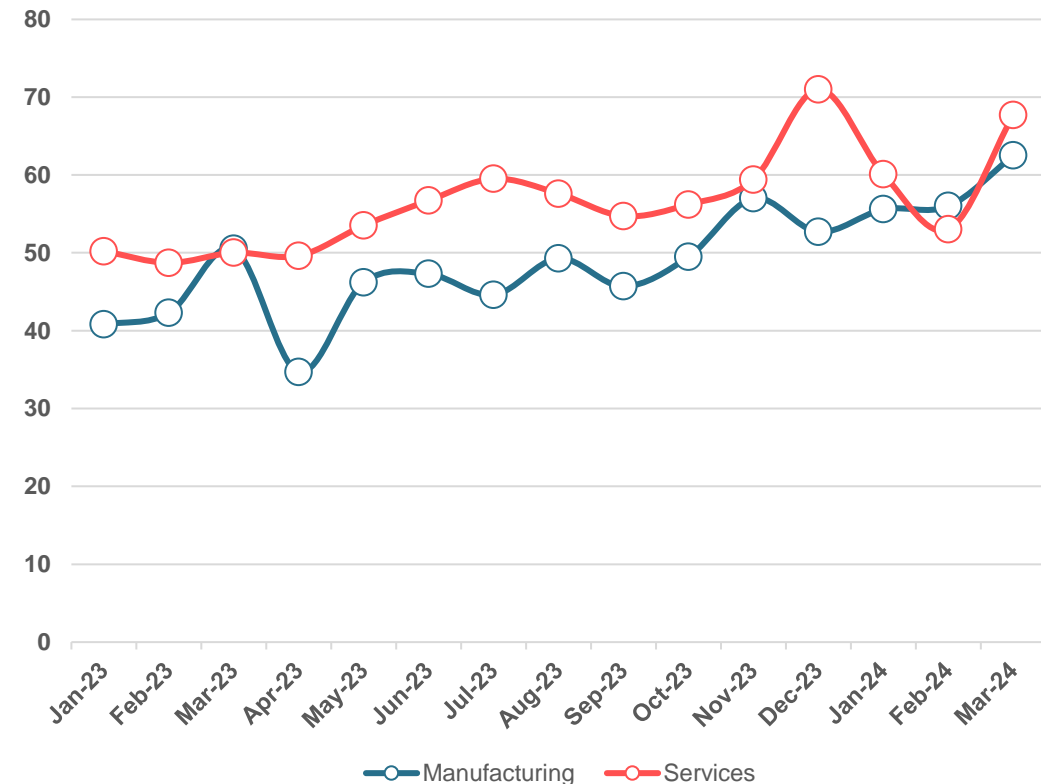
Construction activities continued to exceed the neutral threshold of 50, at a rising rate amidst the current conducive environment and the resumption of multiple, temporarily suspended projects. Large-scale infrastructure projects, particularly foreign-funded ones, are also among the available tender opportunities.

## Construction PMI



Manufacturing PMI continued to gain traction amidst the expansion in new orders from Food & Beverage and Textile & Apparel sectors. Services too reflected massive expansion with the uptick in wholesale and retail trade sub-sectors.

## Manufacturing PMI



Source: CBSL

# Staff-level deal completed between Sri Lanka and IMF for second review

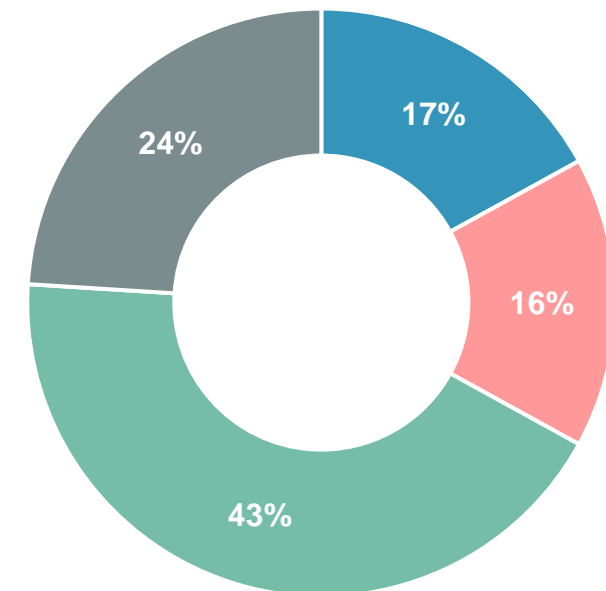
🎯 The IMF reached staff-level agreement on the economic policies to conclude the second review of the 4-year EFF supported program.

🎯 The staff-level agreement is contingent upon approval from IMF management and subsequent review by the IMF Executive Board. This review process necessitates two key components:

- *Implementation of predefined prior actions by Sri Lankan authorities.*
- *Fulfillment of financing assurances, including confirmation of contributions from multilateral partners and an assessment of satisfactory progress in debt restructuring.*

🎯 Upon successful completion of the Executive Board review, Sri Lanka stands to gain access to approximately USD 330.0Mn, thereby augmenting the total IMF financial support under the program to approximately USD 1.0Bn following three disbursements.

## IMF Tracker as at 31<sup>st</sup> March 2024



■ Met ■ Not met ■ Pending ■ Unknown

Source: Manthri.lk





# IMF 3<sup>rd</sup> tranche pending...

*The IMF timeline has consistently aligned with the projections made by First Capital Research, and as expected, the staff level agreement for the second review for the 3<sup>rd</sup> tranche was reached on Mar 21<sup>st</sup> – 2024.*



# FCR Projected Timeline for 2024



“ FCR expects a delay in finalization of bondholder negotiations pushing down the implementation of the EDR to Aug-24 from May-24 and Rating upgrade expectations to Aug-24 from previous Jun-24 timeline. ”

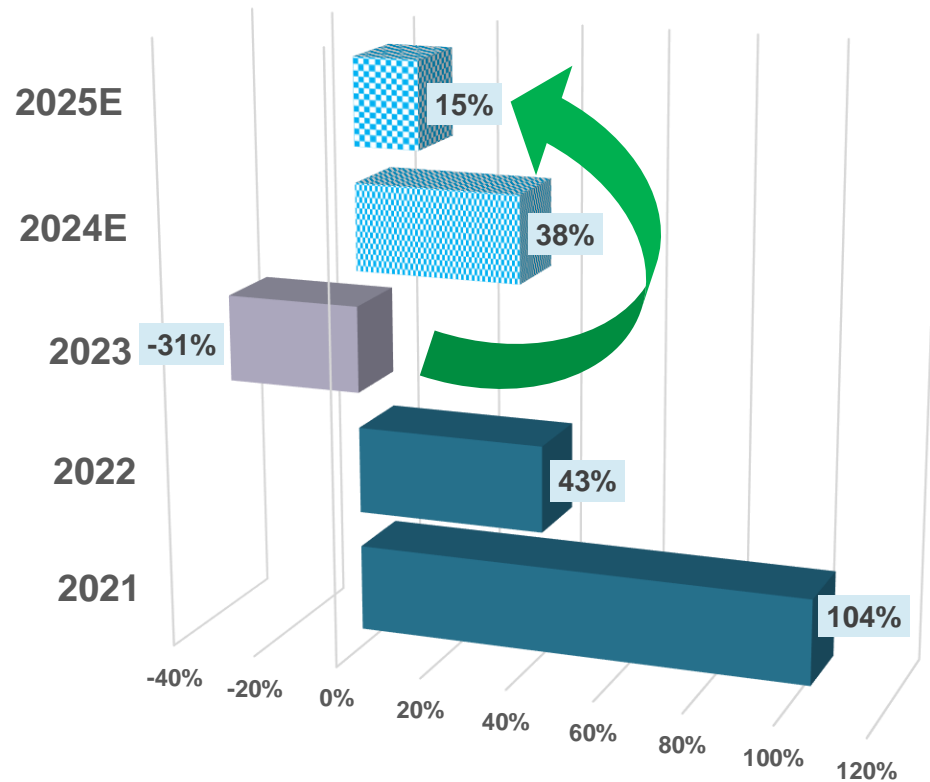
Source: First Capital Research



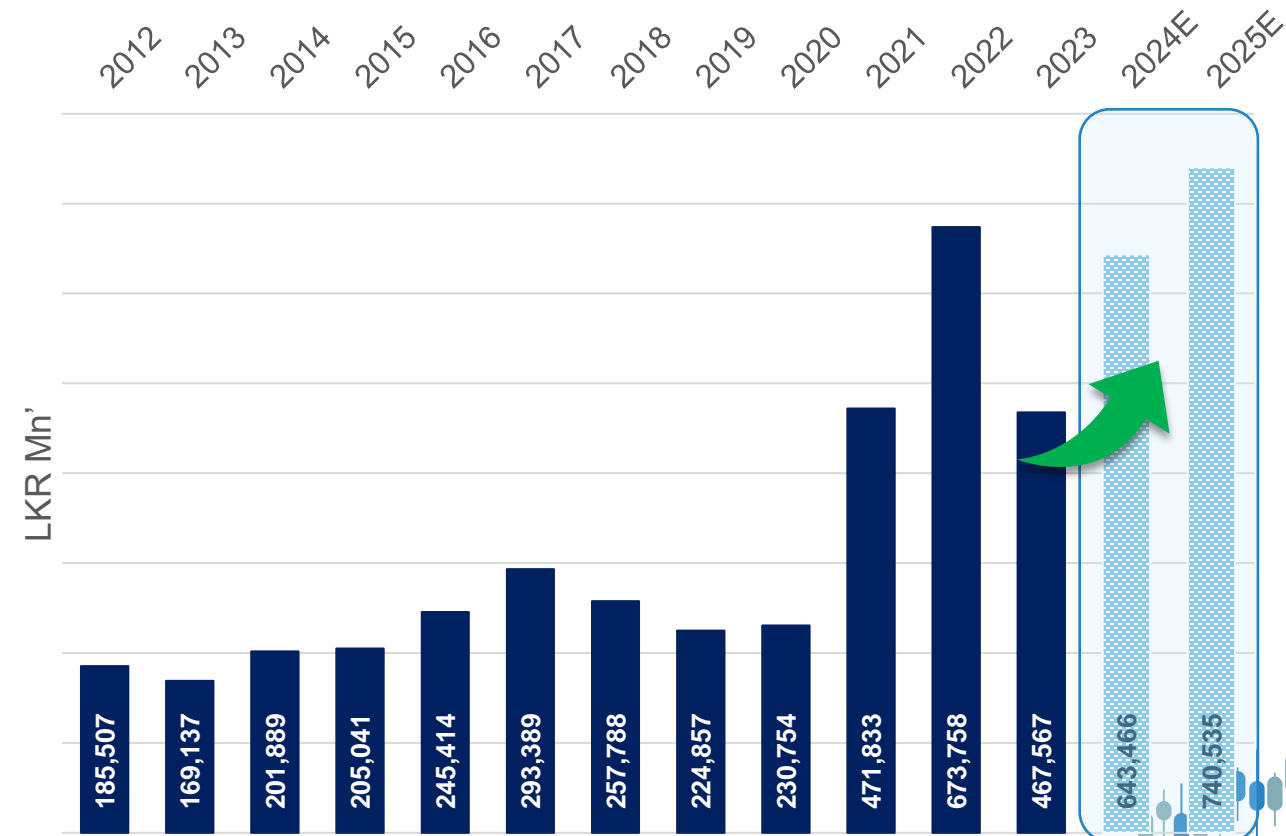
ASPI to reach 13,500 in 2024

# Rebound in market earnings anticipated from 2024E onwards...

Market Earnings in 2023 falls at lower rate than expected



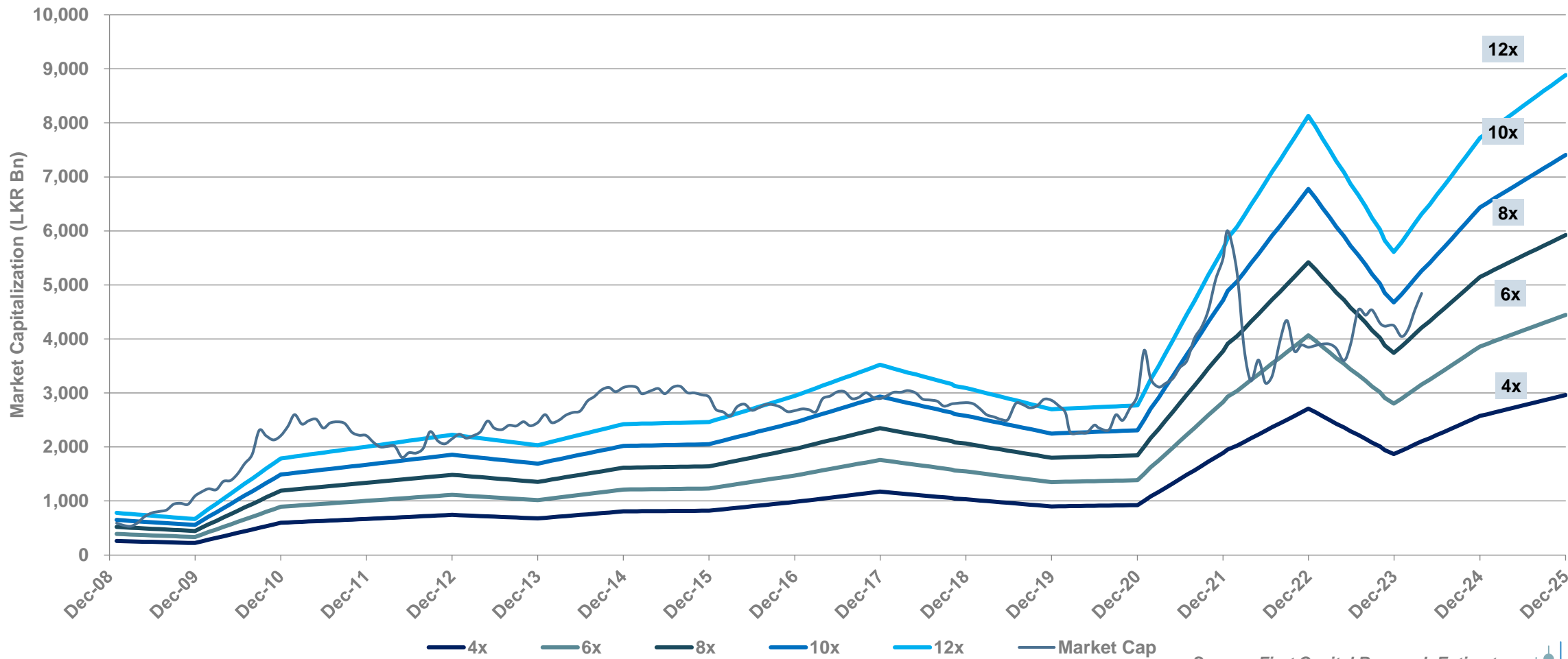
Market Earnings bottom out in 2023 and to recover afterwards



Source: First Capital Research, CSE



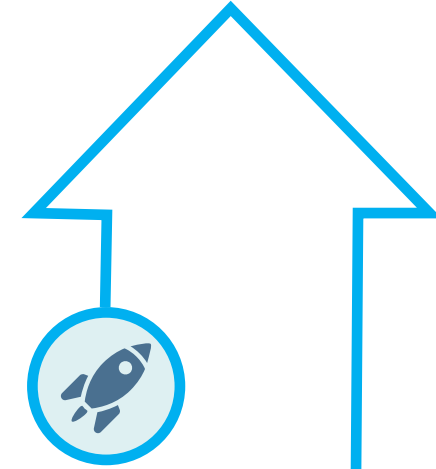
# ...with ASPI trading below 8.4x on 2023 earnings



Source: First Capital Research Estimates



# ASPI Dec-24 target maintained at 13,500



First Capital maintains ASPI 2024E fair value range of **13,000-14,000** owing to the anticipated moderate recovery in earnings on the back of tax revisions, declining interest rates and improving domestic and global economic conditions



# Market to re-rate with the completion of External Debt Restructuring

*First Capital Research maintains stance on buying*

## Riding the Bull: reap gains in the period ahead

### **Interest Rate Dynamics**

As macroeconomic uncertainties ease, there's a notable uptick in business confidence. This has coincided with a surge in economic activity, propelled by credit expansion, further supported by the ongoing decline in interest rates, which has already fallen below 12.0% in the first 4 months of 2024.

### **Debt Restructuring Progress**

Discussions are ongoing with bilateral creditors and bondholder groups, showing substantial advancement in negotiations regarding external debt restructuring. Terms for restructuring have been received from both China's EXIM Bank and the Paris Club, with the current focus on reaching an agreement with private creditors. With IMF conditions to meet and future disbursements pending, these negotiations are expected to reach a conclusion shortly.

### **IMF's upcoming 3<sup>rd</sup> Tranche**

Following the staff-level agreement reached for the 2<sup>nd</sup> review and upon successful completion of the Executive Board review, Sri Lanka stands to gain access to approximately USD 330.0Mn, thereby augmenting the total IMF financial support under the program to approximately USD 1.0Bn following three disbursements.

### **Market Outlook**

The substantial decline in interest rates stands as a key catalyst, poised to prompt a market re-rating. This shift is anticipated to drive a notable liquidity transition from fixed income to equity, potentially resulting in a market range of 13,000-14,000 for 2024E.

# First Capital *Maintains* Equity Exposure to 100% retaining cash to 0%

Recommendation for Funds allocated for purely Equity investments



- With the completion of the external debt restructuring process and progress in the SoE reforms, Sri Lanka's debt is likely to be classified as sustainable improving confidence and pushing yields down. Thereby, in relation to the equity allocated funds, we recommend to be fully invested.
- Amid the improving economic indicators and the potential developments, Equity Market warrants a higher exposure to benefit from the potentially gradual growth in returns in 2024E.
- Out of the funds **purely allocated for equity** we have been advising on investing in the equity market, emphasizing the potential for substantial upside. However, it's crucial to note that all investments carry inherent risks, and we encourage regular reviews of portfolio in light of evolving market conditions and individual circumstances.

**\*First Capital Research assumes that investors have separately allocated funds for equities, and our recommendation is to fully utilize 100% of the allocated funds for equity investments.**



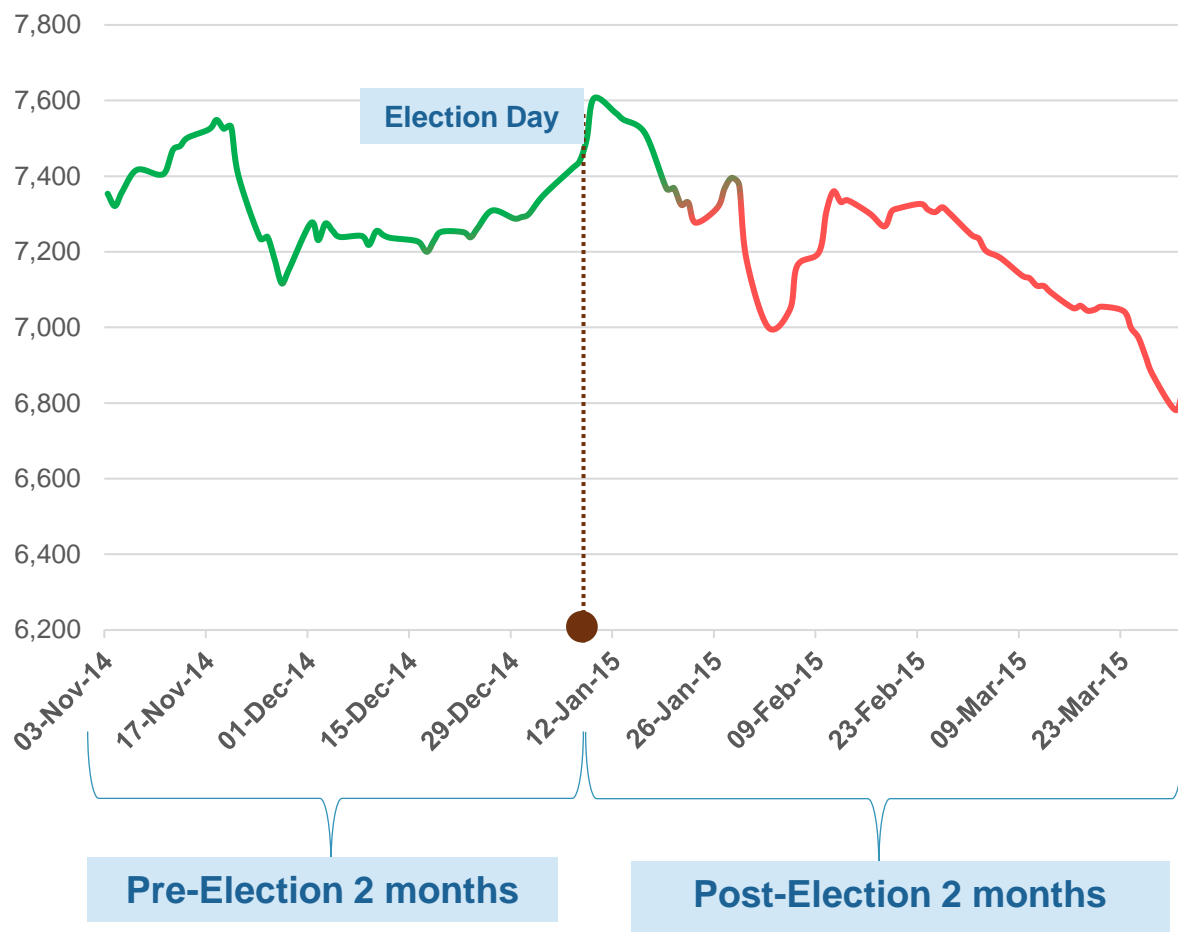




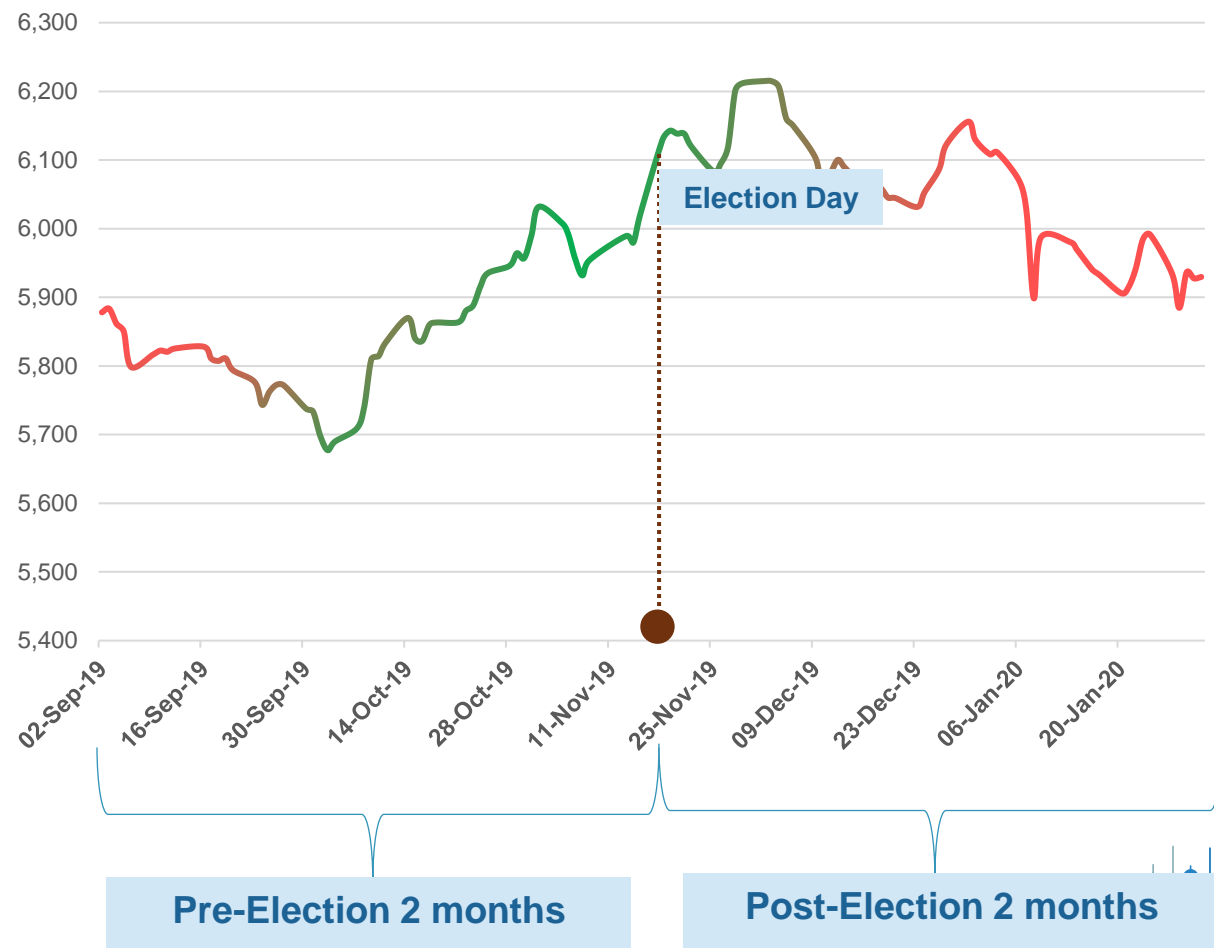
Key risks posing threats to upside potential

# Political risk: Market conditions may turn volatile amidst political turmoil and changes...

ASPI returns - 2015 Presidential Election



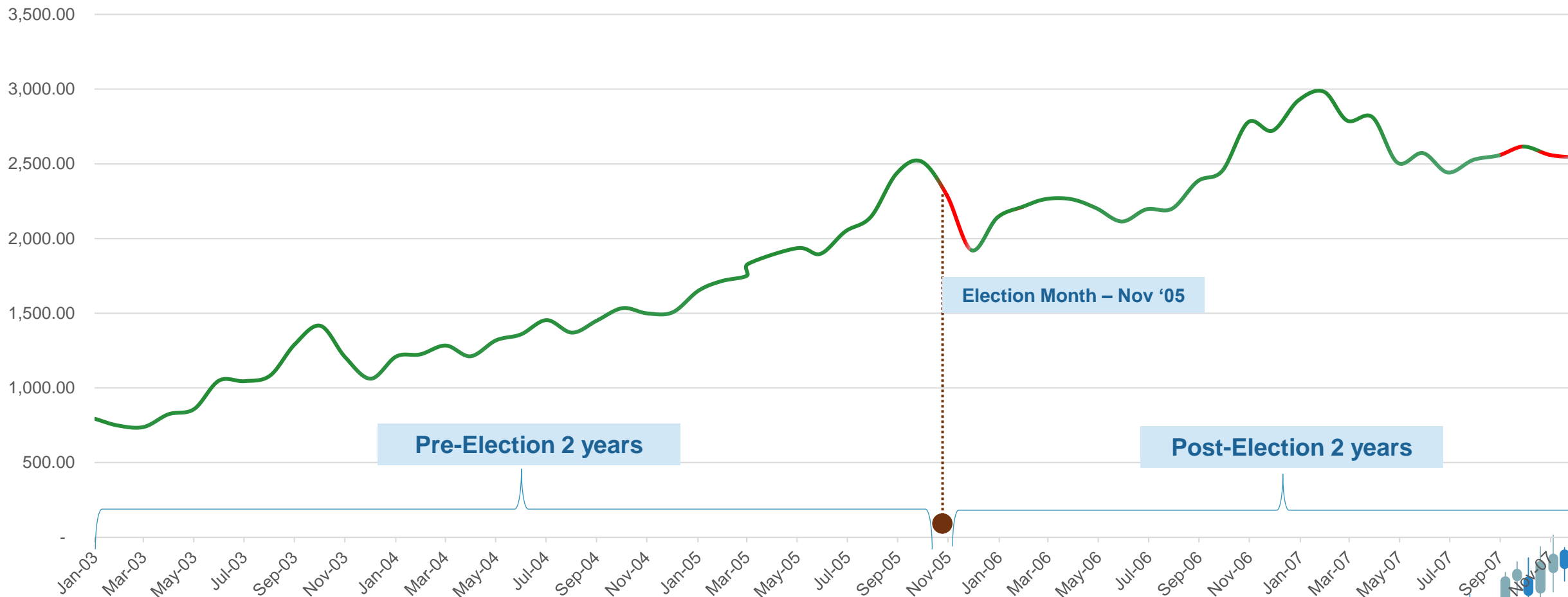
ASPI returns – 2019 Presidential Election



Source: First Capital Research, CSE

...however, risks may be eliminated if economic policies and reforms continue to stay in place, despite governance change similar to 2005 elections scenario

ASPI Returns – 2003 to 2005



Source: First Capital Research, CSE

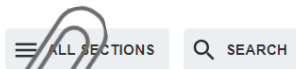
# External Debt Restructuring: Uncertainty and difficulty in reaching consensus with bond holder committee poses significant threat to future proceedings

First Capital Research emphasizes the importance of the government prioritizing consensus in the coming weeks. Delays in discussions and failure to reach agreement on conditions could potentially postpone the IMF's review process and have repercussions on future IMF disbursements.



Asian Markets

## Sri Lanka debt restructuring stumbles as govt rejects bondholders' proposal



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## Sri Lanka's Debt Restructuring Talks With Private Bondholders Hit a Snag

Is the government quibbling over small details to signal to the public that it is driving a hard bargain?

Debt restructuring negotiations with private bondholders have encountered obstacles, as announced on 16<sup>th</sup> Apr-24. Despite constructive discussions, agreement on restructuring terms could not be reached between the government and the Steering Committee of the Ad Hoc Group of Bondholders, which represents major private debt holders.

The Ad Hoc Group's proposal includes issuing a Macro-Linked Bond (MLB) linked to Sri Lanka's GDP, whereas the government's proposal aligns with IMF-supported program parameters for debt sustainability. Critics highlight the similarity between the proposals and suggest the impasse may be politically motivated, as Sri Lanka approaches presidential elections.



















Top Picks in 2024



First Capital  
A Janashakti Group Company

## FIRST CAPITAL 2024E/FY25E TOP RECOMMENDATIONS

Stock				Stock Code	26-Apr-24	PE	PBV	DY	52-Week High	52-Week Low	Target Price 2025E/FY 25E
LKR											
 COMMERCIAL BANK	Commercial Bank PLC - Voting	COMB.N0000	110.00		7.0	0.7	0.0%	107.50	50.10	200.00	
	Hatton National Bank PLC - Voting	HNB.N0000	197.00		4.9	0.5	0.0%	203.50	75.20	350.00	
	Sampath Bank PLC	SAMP.N0000	80.00		5.2	0.6	4.3%	79.20	33.00	135.00	
	Nations Trust Bank PLC	NTB.N0000	114.25		3.2	0.6	0.0%	125.00	45.80	200.00	
	Chevron Lubricants Lanka	LLUB.N0000	115.50		7.7	3.3	6.1%	109.25	78.00	160.00	
	Teejay Lanka	TJL.N0000	37.50		37.3	0.9	2.0%	40.00	28.70	50.00	
	Hayleys Fabric	MGT.N0000	40.50		6.9	1.6	1.5%	49.70	20.00	65.00	
	Hayleys	HAYL.N0000	85.00		16.0	0.8	6.3%	97.90	63.50	175.00	
	HNB Assurance	HASU.N0000	56.10		4.8	0.8	6.5%	59.00	42.00	80.00	
	Ceylon Tobacco Company	CTC.N0000	1,270.00		8.6	20.2	11.9%	1,040.00	598.00	1,600.00	
	Hemas Holdings	HHL.N0000	84.30		9.0	1.2	2.8%	85.90	51.00	95.00	
	Ceylon Cold Stores	CCS.N0000	56.10		16.2	2.6	3.1%	53.00	32.00	70.00	
	Aitken Spence Hotel	AHUN.N0000	68.00		N/A	1.2	0.0%	90.00	48.00	90.00	
	John Keells Hotels	KHL.N0000	19.40		N/A	0.9	0.0%	24.70	15.60	27.00	
	Hayleys Leisure	CONN.N0000	21.50		N/A	2.1	0.0%	28.00	19.10	30.00	
	Asian Hotels & Properties PLC	AHPL.N0000	68.10		163,875.0	1.0	0.0%	64.50	32.10	86.00	

\*First Capital Research's top recommended stocks are chosen based on the potential return and the liquidity of the stocks



# Thank You

*"SUCCESSFUL INVESTMENTS IS ABOUT MANAGING RISKS"*

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