



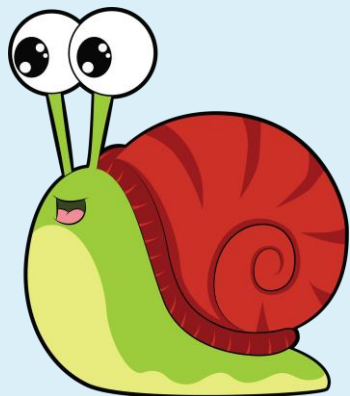
# Post Election Scenario Analysis

Scenario Analysis | Aug 2024 | SRI LANKA

# Multiple scenarios are possible based on the political and policy outlook

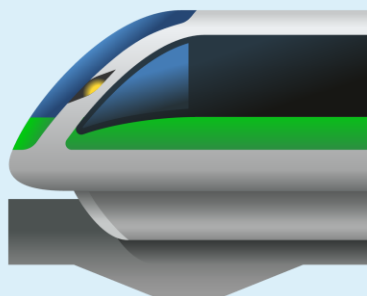
## Snail Pace Stroll

*Base Case Low Scenario*



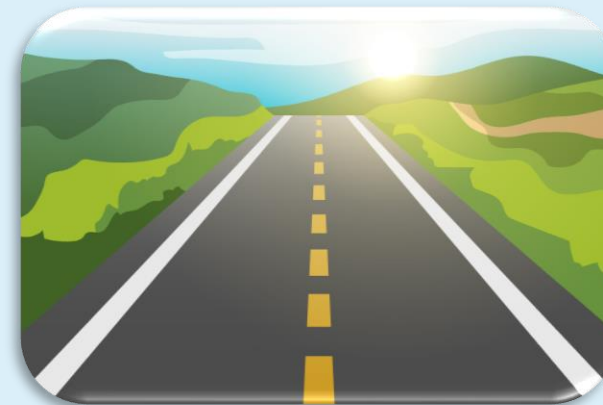
## Monorail Dream

*Base Case High Scenario*



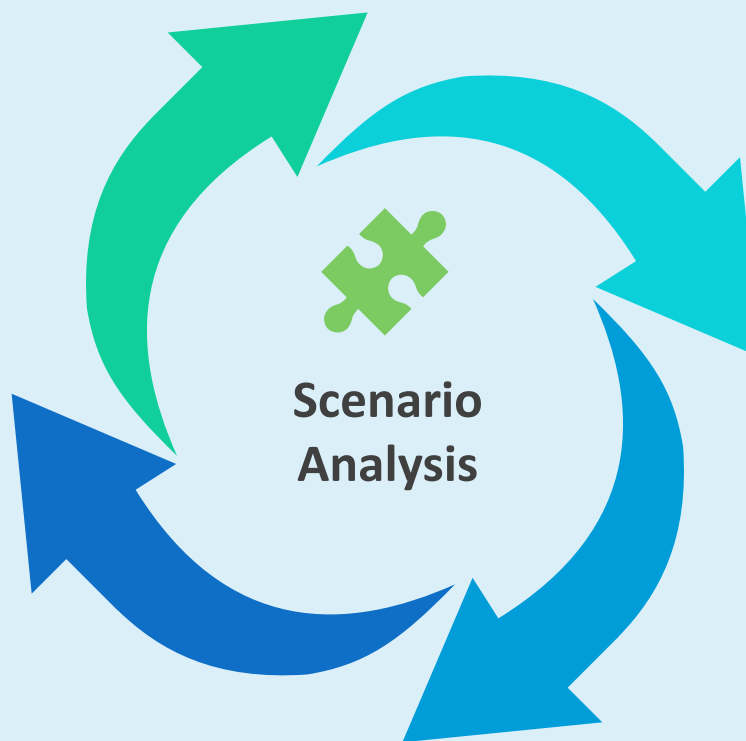
## Super Grade Highway

*Super Case Scenario*



## The Lankan Pothole

*Worse Case Scenario*



# Scenario 1 – Snail Pace Stroll



## Scenario 1 Base Case Low Scenario

### Highlight

- Hung Parliament / Unwillingness for drastic change
- IMF program barely on course
- Governance related reforms completed to keep IMF on course
- Slow economic growth
- Potential new tax hike if tax not broad based



### Possible Outlook

Interest rate stagnant or elevated (10%-12%)

Gradual awareness growth

Slow search for alternative investment options

Slow rise in equity market

### Potential Landscape

- ❑ Sri Lanka may face a stagnant political landscape with a hung parliament and reluctance for drastic reforms, leading to slow economic growth. While governance reforms keep the IMF program barely on track, a potential tax hike looms if tax reforms are not broad-based.

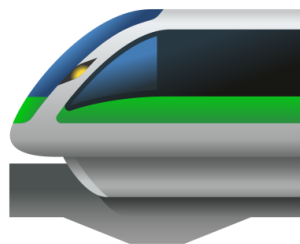
### Potential Impact

- ❑ Interest rates may stagnate or rise slightly, limiting economic momentum. A slow rise in the equity market reflects cautious investor sentiment, while gradual awareness and a slow search for alternative investment options signal subdued financial dynamism.

Snail Pace Stroll



# Scenario 2 – Monorail Dream



## Scenario 2 Base Case High Scenario

### Highlight

- Strong Parliament
- IMF program on accelerated course with fiscal positive reforms
- FDI Flows
- Digital ID and Govt move into digitalization
- Increase in financial literacy



### Possible Outlook

Interest rate decline & global rates fall – may be 8%-10%

Strong search out for alternative investment options

Strong rise in equity market

Increase in IPO & M&A

## Potential Landscape

- ❑ In a scenario where Sri Lanka has a strong parliament, the accelerated IMF program with positive fiscal reforms may enhance economic stability and attract increased foreign direct investment (FDI). The government's push towards digitalization and the adoption of Digital ID may streamline public services, fostering a more efficient economy. Financial literacy is likely to rise under the identified scenario.

## Potential Impact

- ❑ As financial literacy rises, so will the demand for alternative investment options, fueling a strong equity market surge. Declining interest rates, possibly down to 8%-10%, may further stimulate growth, alongside a marked increase in IPOs and M&A activity, reflecting robust economic dynamism and investor confidence.

Monorail Dream



# Scenario 3 – Super Grade Highway



## Scenario 3 Super Case Scenario

### Highlight

- Capitalistic President & Parliament
- IMF program on accelerated course with privatizations
- Reverse brain drain
- Lower Taxes
- Move towards digital economy



### Possible Outlook

Interest rate decline & global rates fall – Maybe 6%-8%

Extremely strong rise in equity market

Majority of the 25-45 population search for capital market products

Steep rise in IPOs and M&A transactions

### Potential Landscape

- ❑ Under a capitalistic president and parliament, Sri Lanka's economy will be transformed by accelerated IMF-led privatizations and lower taxes, encouraging business growth while Sri Lanka may move a digitalized economy with strong improvement in efficiency and productivity. A reverse brain drain may bring back skilled professionals, boosting innovation

### Potential Impact

- ❑ As the country shifts towards a digital economy, falling interest rates (6%-8%) will lower borrowing costs, spurring investment. The equity market is set for an extremely strong rise, driven by a surge in demand from the 25-45 age group seeking capital market products. This will lead to a steep increase in IPOs and M&A transactions, reflecting robust economic activity and investor confidence.

Super Grade Highway



# Scenario 4 – The Lankan Pothole



## Scenario 4 Worse Case Scenario

### Highlight

- Weak President / Hung Parliament
- IMF program falls apart
- Rise in inflation
- Currency Depreciation
- Brain Drain
- Tax Hike
- Demand for Non-liquid assets



### Possible Outlook

Interest rate rise 15%-20% initially and may surge further

Some demand for Fixed Income, but higher demand for non-liquid assets

New domestic debt restructuring possibility

Equity market crash

The Lankan Pothole



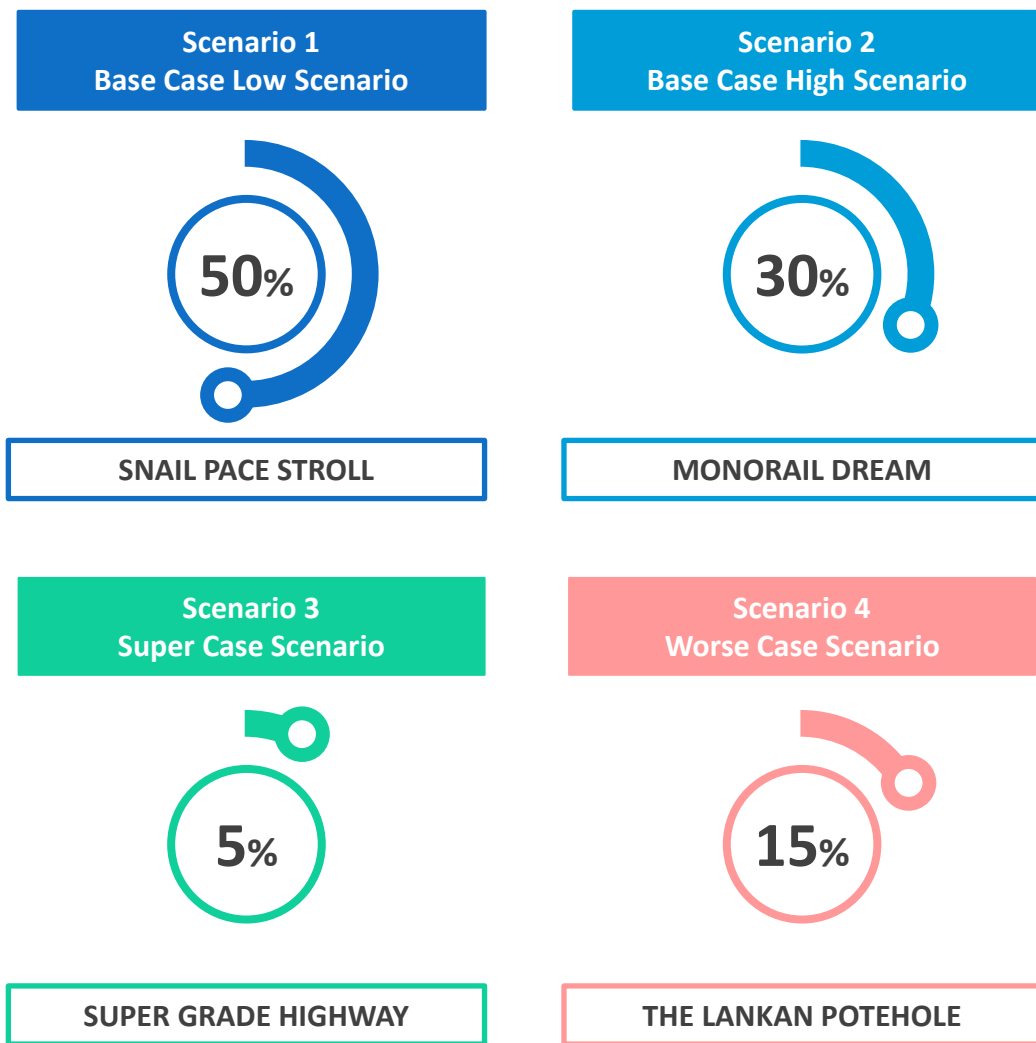
## Potential Landscape

- ❑ Facing a weak president and a hung parliament, Sri Lanka could see political paralysis with the inability and extensive delay in taking reform decisions leading to the collapse of the IMF program. This may likely trigger inflation, currency depreciation, and a brain drain, with possible tax hikes adding further strain on businesses and consumers. As economic stability erodes, demand for non-liquid assets may rise.

## Potential Impact

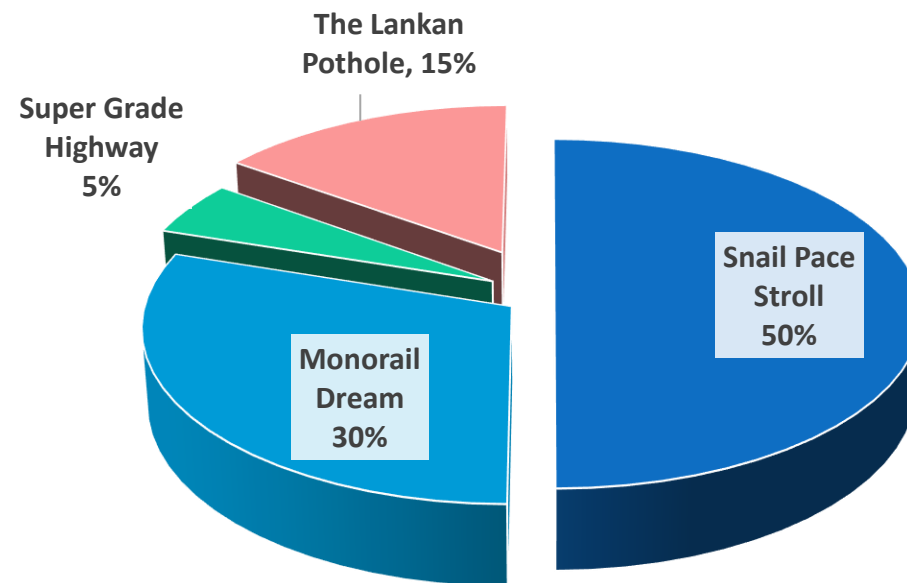
- ❑ Soaring interest rates (15%-20%) could drive some demand for fixed income, but new domestic debt restructuring may be necessary. An equity market crash could ensue, deepening the crisis and emphasizing the need for strategic resilience to navigate these severe economic challenges.

# Potential Scenario Probabilities



## Outlook for Capital Market Investments with an 85% Probability of Positive Returns!

- ❑ Considering Scenarios 1, 2 & 3, the outlook is moderately or highly positive (depending on the scenario) towards investment in fixed income and equity with a cumulative 85% probability.
- ❑ The risk for investments lie in Scenario 4, namely “The Lankan Pothole” with potentially high level of negative returns at a 15% probability.





First Capital Holdings PLC



No. 2, Deal Place, Colombo 3



research@firstcapital.lk



+94 112 651 651



**Dimantha Mathew**

Chief Research & Strategy Officer

T: +94 11 2639 853

E: dimantha@firstcapital.lk

**Ranjan Ranatunga**

Manager- Research

T: +94 11 2639 863

E: ranjan@firstcapital.lk

**Vinodhini Rajapoopathy**

Assistant Manager- Research

T: +94 11 2639 866

E: vinodhini@firstcapital.lk

**Tharusha Ashokgar**

Senior Research Analyst

T: +94 11 2639 866

E: tharushaash@firstcapital.lk

**Zaeema Jihan**

Senior Research Associate

T: +94 11 2639 866

E: zaheema@firstcapital.lk

**Anjali Mathews**

Senior Research Associate

T: +94 11 2639 866

E: nethmi@firstcapital.lk

**Nethmi Fernando**

Research Associate

T: +94 11 2639 866

E: nethmi@firstcapital.lk

# Thank You

“Successful investments is about managing risks”