

# EQUITY STRATEGY

First Capital Research | 28 Aug 2025



**First Capital**  
A Janashakthi Group Company

***“Bullish Run, Cautious Eye”***

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# Executive Summary

## *ASPI fair value for 2026E maintained at 21,000-22,000*

First Capital maintains its ASPI target of 21,000-22,000, supported by sustained momentum driven by macroeconomic stability and improved corporate earnings. Investors are advised to take early gains and gradually shift to a defensive stance as the index nears the high-end of the range. With current market strength, the ASPI could exceed the 2026E fair value within 2025E, before facing a potential slowdown due to softening economic activity and earnings growth. However, if structural reforms continue and GDP growth remains above 5%, the market could experience a further re-rating beyond current projections.

### **Sector-Specific Recommendations**

- **Banking & Financial Services:** Beneficiaries of the low-interest rate environment driving loan growth as well as improving trade finance. Focus on banks with strong balance sheets and those that are aggressive on their lending book for 2026E.
- **Consumer Staples & Retail:** Rising disposable incomes and public sector salary hikes should boost consumption. Companies with strong brand positioning and pricing power stand to gain.
- **Capital Goods:** Earnings will be driven predominantly by JKH through the commissioning of its mega projects such as the City of Dreams Sri Lanka and the West Container Terminal.
- **Construction & Infrastructure:** Anticipated increases in government capex to stimulate GDP growth could enhance the segment's future profitability.
- **Export-Oriented Industries:** Although the apparel sector may face a slight setback amid increased tariffs, the other manufacturing exports may benefit from improved global demand and a stable currency outlook.

Investors are advised to **rotate into defensive sectors** as the ASPI surpasses our 2026E target, while maintaining exposure to high-growth sectors where fundamentals remain strong.





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# **1.0 Equity Outlook for 2026E Maintained**

# ASPI fair value maintained at 21,000-22,000; Outlook remains Bullish

## *Conditions favour a breach in fair value*



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### Market Outlook

First Capital maintains a positive outlook for the Sri Lankan stock market heading into 2026E, supported by strong macroeconomic fundamentals and improved corporate profitability. The ASPI has recorded a YTD gain of 25%, recently surpassing the 20,000 mark following a series of record highs and elevated market turnover. Given the current trajectory, we believe that the ASPI could reach our 2026E target range of 21,000-22,000 prior to the end of 2025E.

#### ❑ Earnings Growth Maintained at 25% for 2025E and 17% for 2026E

Sri Lanka's economic resurgence remains strong, backed by the lower than anticipated inflation levels, coupled with the lower interest rate environment supporting business expansion. Corporate earnings are set to rise, supported by better margins from reduced borrowing costs and higher factory utilization rates, further strengthened by political stability.

#### ❑ Sustained Low-Interest Rate Environment

The low-interest rate environment is expected to continue up to 1H2026E, supported by reduced upcoming maturities, stable liquidity, and a sustained primary account surplus. This backdrop is expected to accelerate the shift from fixed income to equities, reinforcing a favorable environment for equity markets.

#### ❑ Macroeconomic Stability

Sri Lanka's macroeconomic outlook remains stable, with 2025E GDP growth projected at 5% amid easing inflation. Strengthening reserves, driven by tourism, remittances, and IMF support have stabilized the LKR and improved external sector resilience.

#### ❑ IMF Program Continuation

Continuation of the IMF program is expected, with the GoSL achieving the targets set by the IMF, despite slight delays.

### Market conditions illustrates a like breach in ASPI fair value range

We maintain our 2026E fair value target for the ASPI at 21,000-22,000, anticipating that strong momentum, backed by solid corporate earnings growth and macroeconomic stability, could push the index into this range by 2025E. Beyond this level, we expect a gradual slowdown as earnings and economic growth moderate. However, if Sri Lanka maintains GDP growth above 5% and pursues key reforms aimed at enhancing transparency, governance, and financial management, the market's upward trend could continue past the 22,000 mark.



# Profit-Taking Strategy if ASPI overshoots 22,000

## Profit-Taking Strategy

**Ride the Momentum:** The second half of 2025 (2H2025) is expected to remain bullish, supported by strong corporate earnings, low interest rates, and overall macroeconomic stability. Investors are encouraged to ride this momentum but remain vigilant for early signs of market overheating.

**Profit Taking beyond 22,000:** As the ASPI approaches 22,000, especially with a PER above 12.0x, investors should consider a more decisive shift to profit-taking, as overvaluation combined with potential domestic or global volatility could increase the risk of a market correction.

**Phased Profit Taking:** Should the index move beyond 22,000, a phased profit-taking strategy is recommended, particularly for stocks with elevated valuations, while retaining positions in fundamentally strong companies with sustainable earnings growth. Beyond the 22,000 mark, it would be prudent to shift exposure toward defensive sectors or reduce equity exposure and move to alternative asset classes in anticipation of a potential slowdown in 1H2026E.

## Key Triggers and Risks

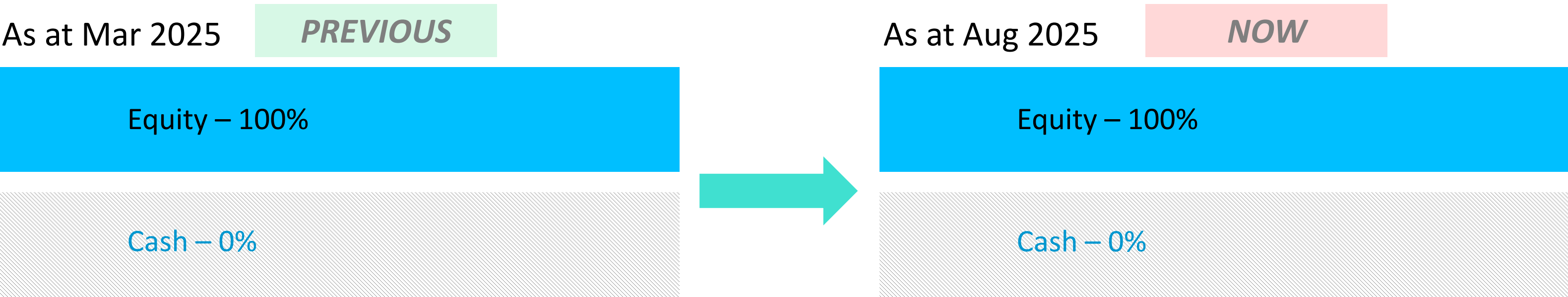
- ❑ **Positive Triggers:** Strong GDP growth exceeding 5%, SOE restructuring benefits (especially for banks and consumer stocks) and rising public sector wages
- ❑ **Potential Risks:** 2026 Budget, Inflation spikes, slowing reserve growth, delayed IMF tranches, liquidity tightening, and global shocks (e.g., US trade policies or geopolitical uncertainty) may force corrections. Policy missteps or governance setbacks could also weigh on sentiment.

# Equity Portfolio Recommendation:

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



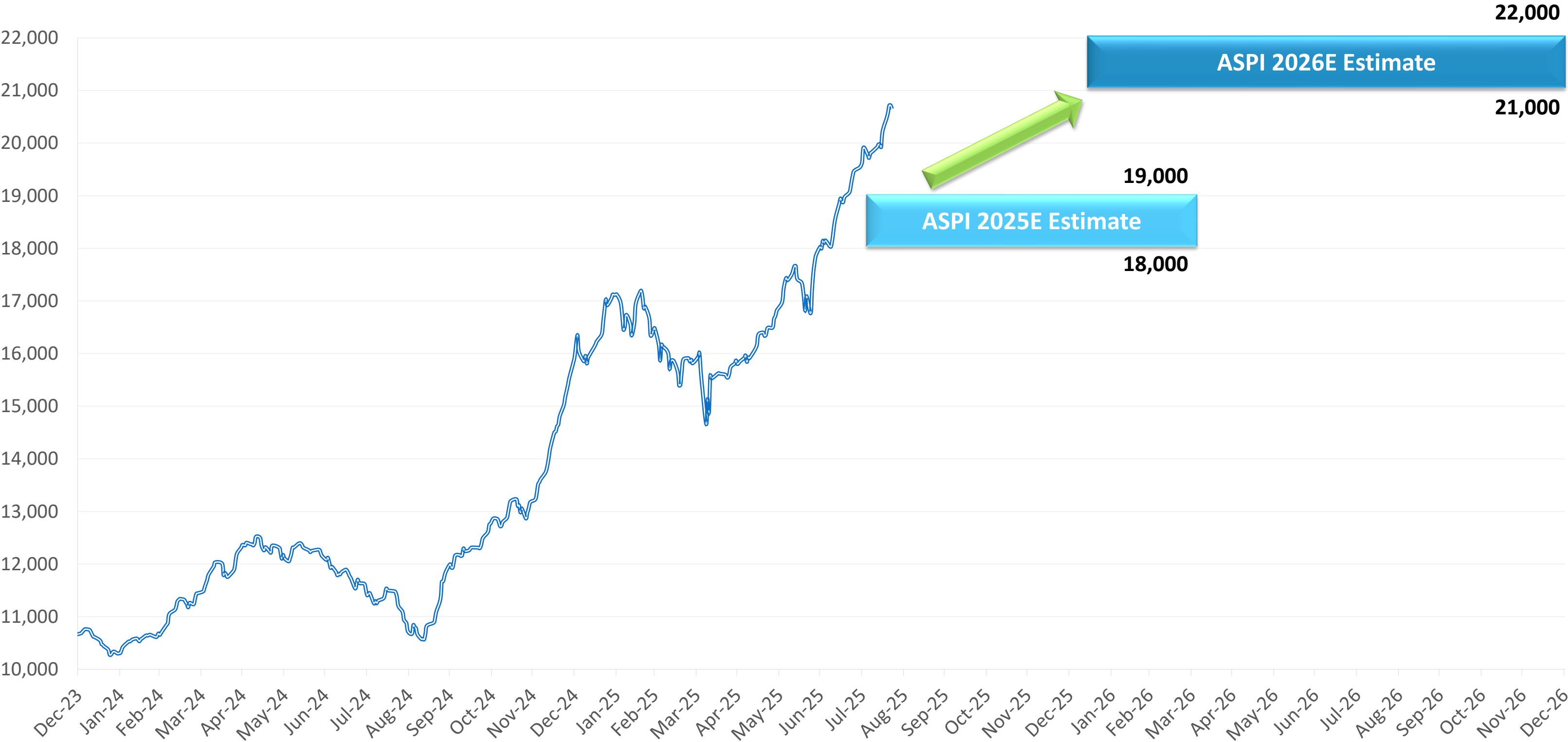
## Recommendation for Funds allocated purely for Equity investments



### 28 Aug 25 - Approach to Equity Investments during 2026E:

The stronger-than-expected performance of listed corporates, combined with expectations of a prolonged low-interest environment, is likely to support the re-rating of the ASPI toward the projected 2026E targets. Out of the funds purely allocated for equity we have been advising on investing in the equity market in full, 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.

# ASPI 2026E target set at 21,000–22,000





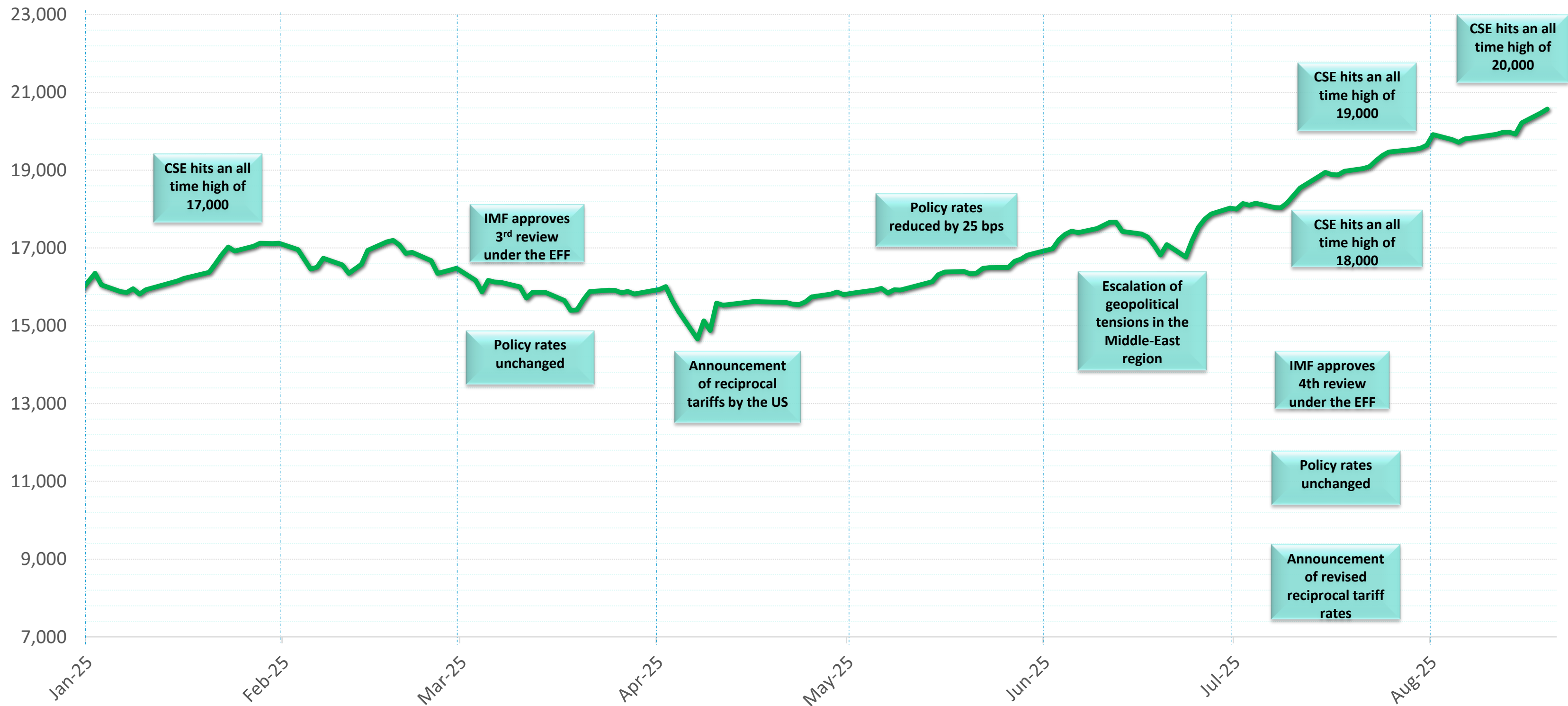


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## 2.0 Performance of the CSE

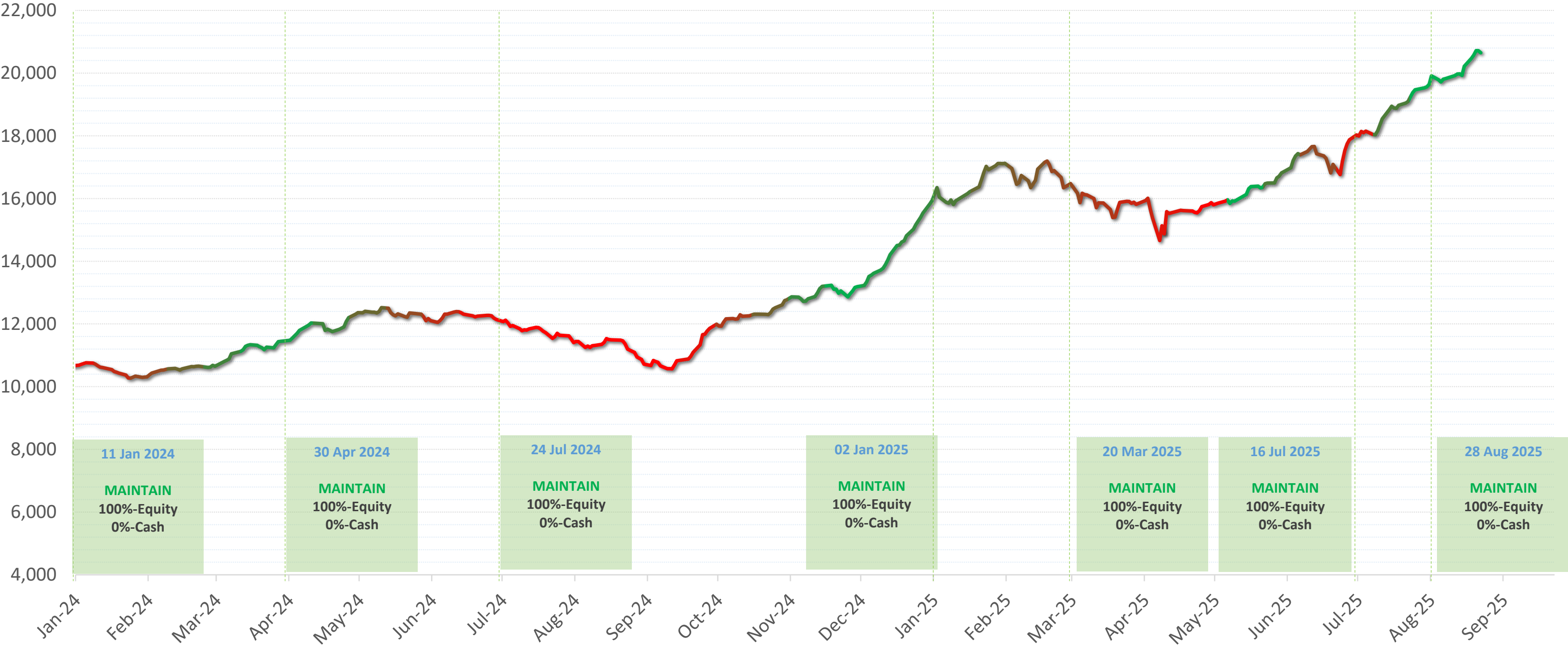
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# ASPI performance and key highlights



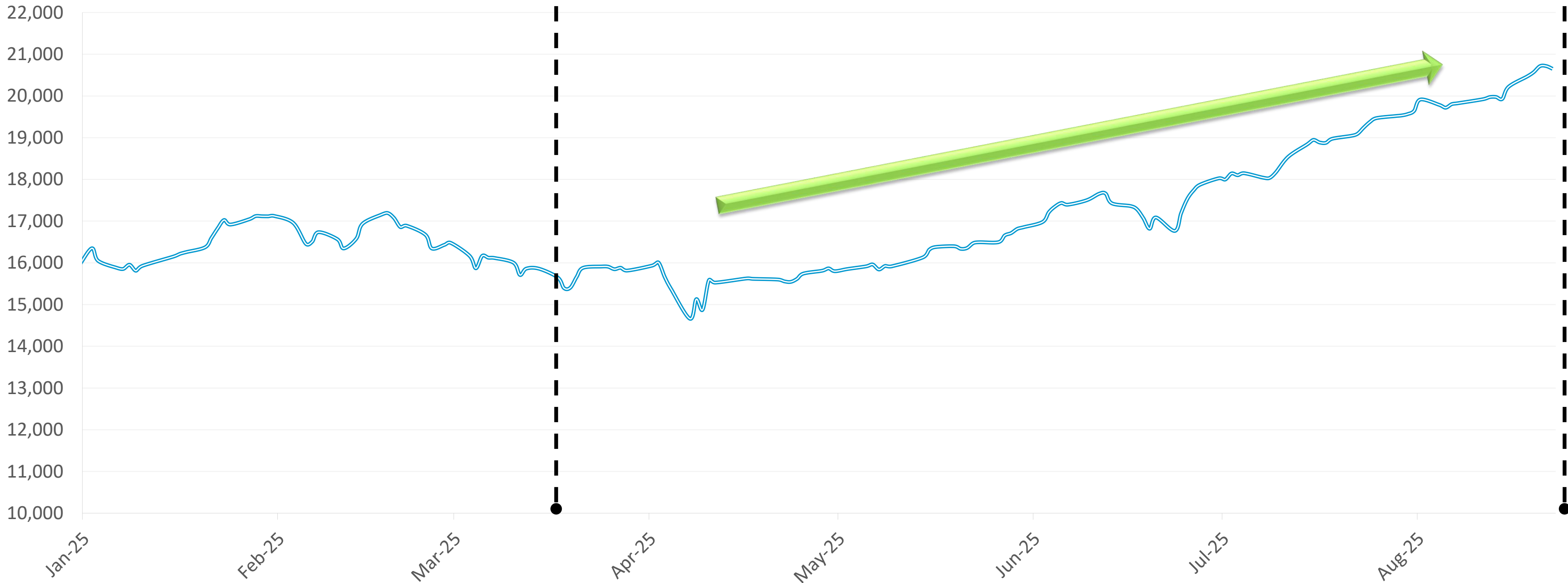


First Capital *Maintains* Equity Exposure at 100% and Cash at 0%



# Recap: ASPI movement Mar-25 to Aug-25

The ASPI remained largely flat with minimal volatility in early March 2025, on the back of delays in the IMF’s 3rd review, initially scheduled for October 2024 but only concluded in March. In April, the index experienced a brief dip following the announcement of reciprocal tariffs by the U.S. on Sri Lankan imports. However, investor sentiment recovered after the implementation was deferred, allowing the market to regain momentum. Despite external headwinds, including rising geopolitical tensions between Iran and Israel in mid-June, the index maintained its upward trajectory. The rally was further supported by strong corporate earnings, a sustained low-interest rate environment, the implementation of downward-revised tariffs, and the successful completion of the IMF’s 4th review in July. These factors continued to drive investor rotation into equities, with elevated turnover levels being recorded at the CSE. By 28 August 2025, the ASPI reached a new all-time high of 20,800, supported by elevated turnover and broad-based buying interest.





# ASPI continues bull rally...

- ❑ Since our previous report in Mar 2025, the ASPI has largely sustained its bullish trajectory, recording multiple all-time highs and elevated turnover levels, ultimately reaching 20,800 on 28 August 2025.
- ❑ This upward momentum has been primarily driven by strong corporate earnings growth, a persistently low-interest rate environment, and broad macroeconomic stability supported by subdued inflation and ongoing IMF assistance.
- ❑ In early April, the market experienced a brief setback following the announcement of increased reciprocal tariffs by the U.S. However, the delayed implementation allowed the index to maintain its upward trajectory.
- ❑ By mid-June, the ASPI faced some volatility due to the escalation of geopolitical tensions between Israel and Iran, with the 12-day conflict introducing temporary uncertainty and a modest pullback.
- ❑ Market sentiment improved in July, following the IMF's completion of its 4th review and the announcement of revised, lower-than-expected reciprocal tariffs.
- ❑ This, combined with strong corporate earnings reported for the June 2025 quarter, reinforced investor confidence and helped the index regain momentum, leading to further record highs and sustained high turnover.







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## 3.0 Key Drivers for Equity

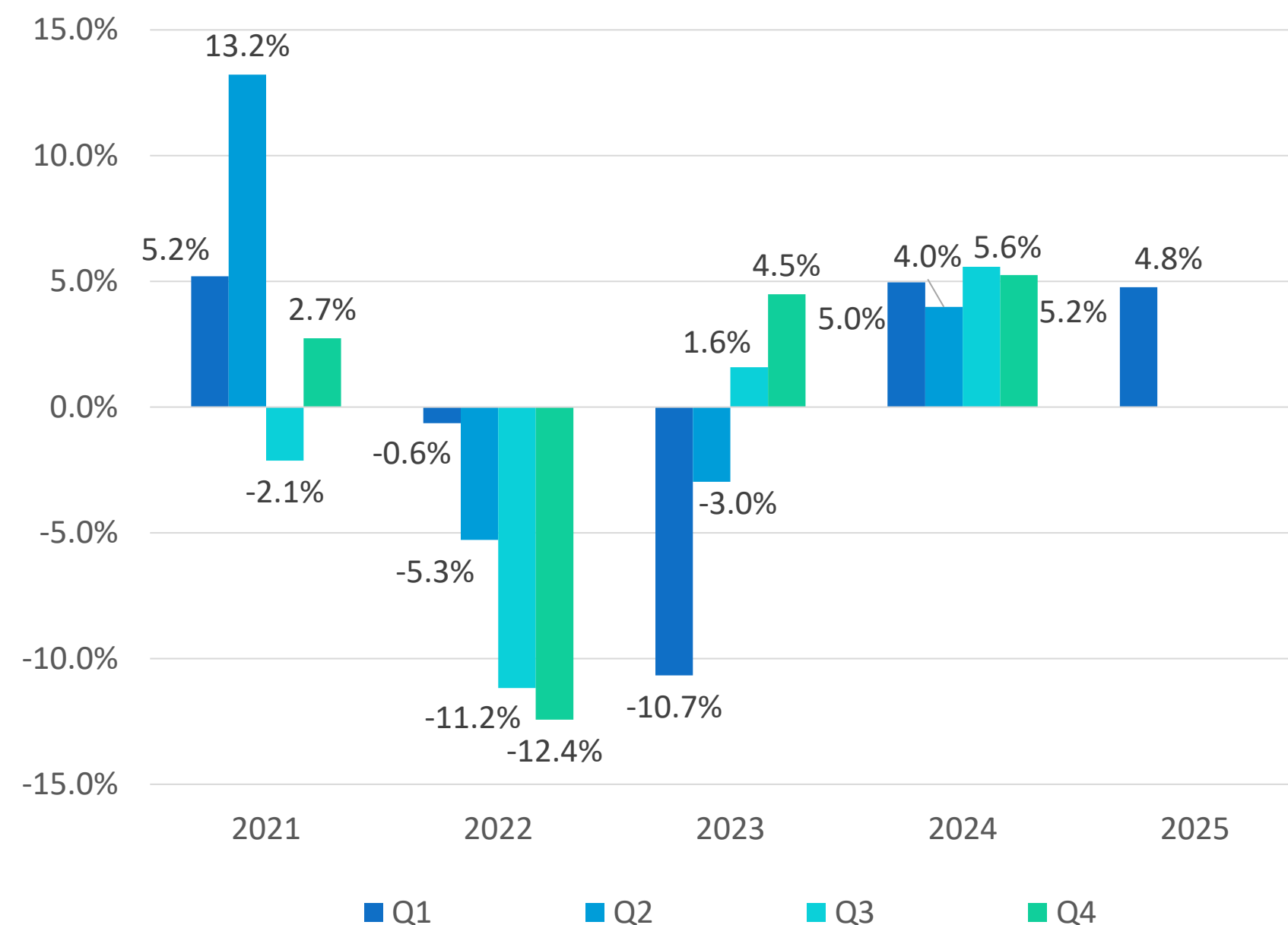
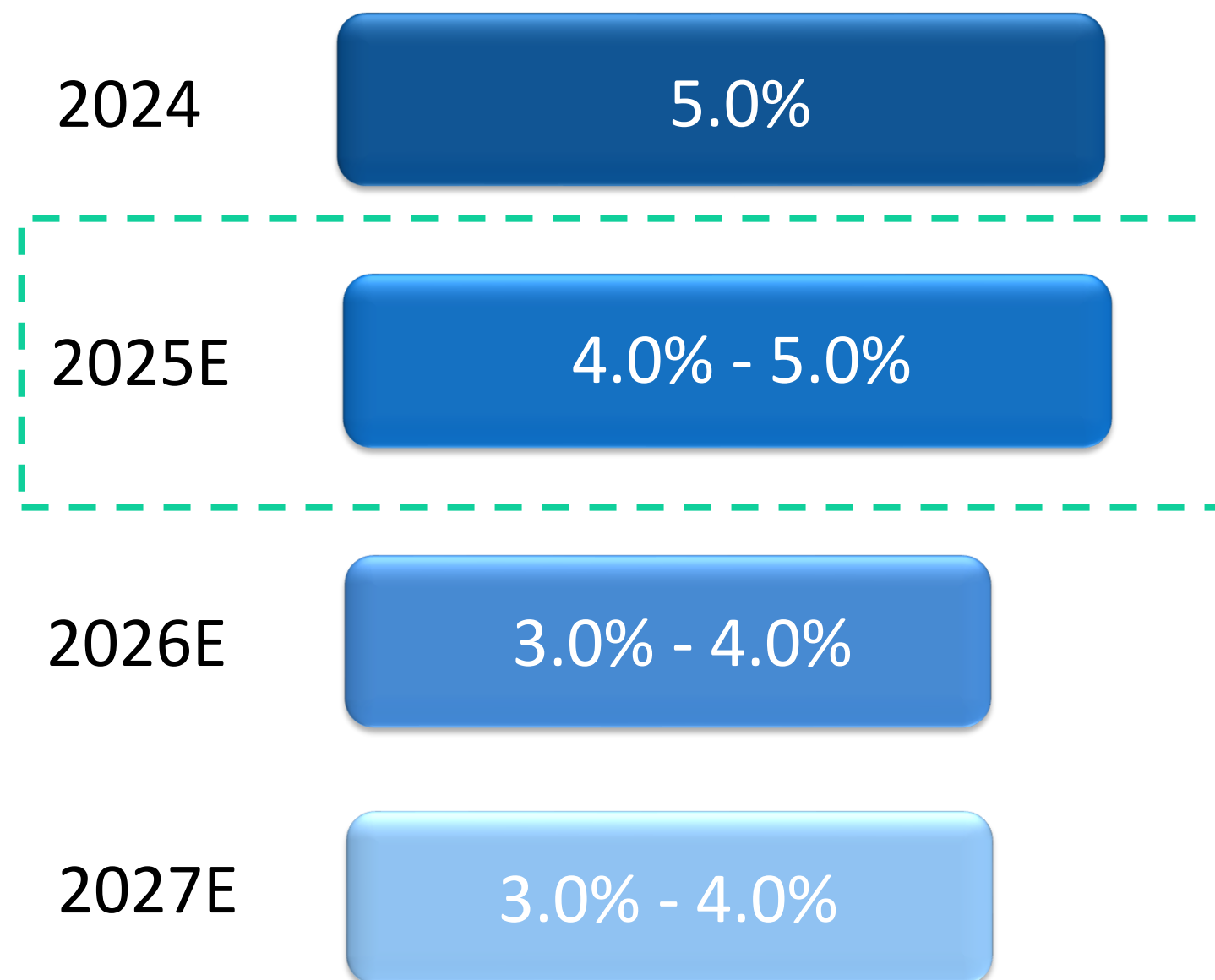
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# GDP growth for 2025E is expected to remain between 4% and 5%...

FCR forecasts real GDP growth to range between 4.0%-5.0% YoY in 2025E, with the first quarter of 2025 already showing a 4.8% YoY increase, based on data from Sri Lanka's Census and Statistics Department. For 2026E and 2027E, growth is expected to moderate to a range of 3.0%-4.0% YoY. This softer outlook is driven by subdued government spending and a challenging global environment, with rising tariffs and geopolitical tensions weighing on external growth prospects.

## GDP Growth Expectations

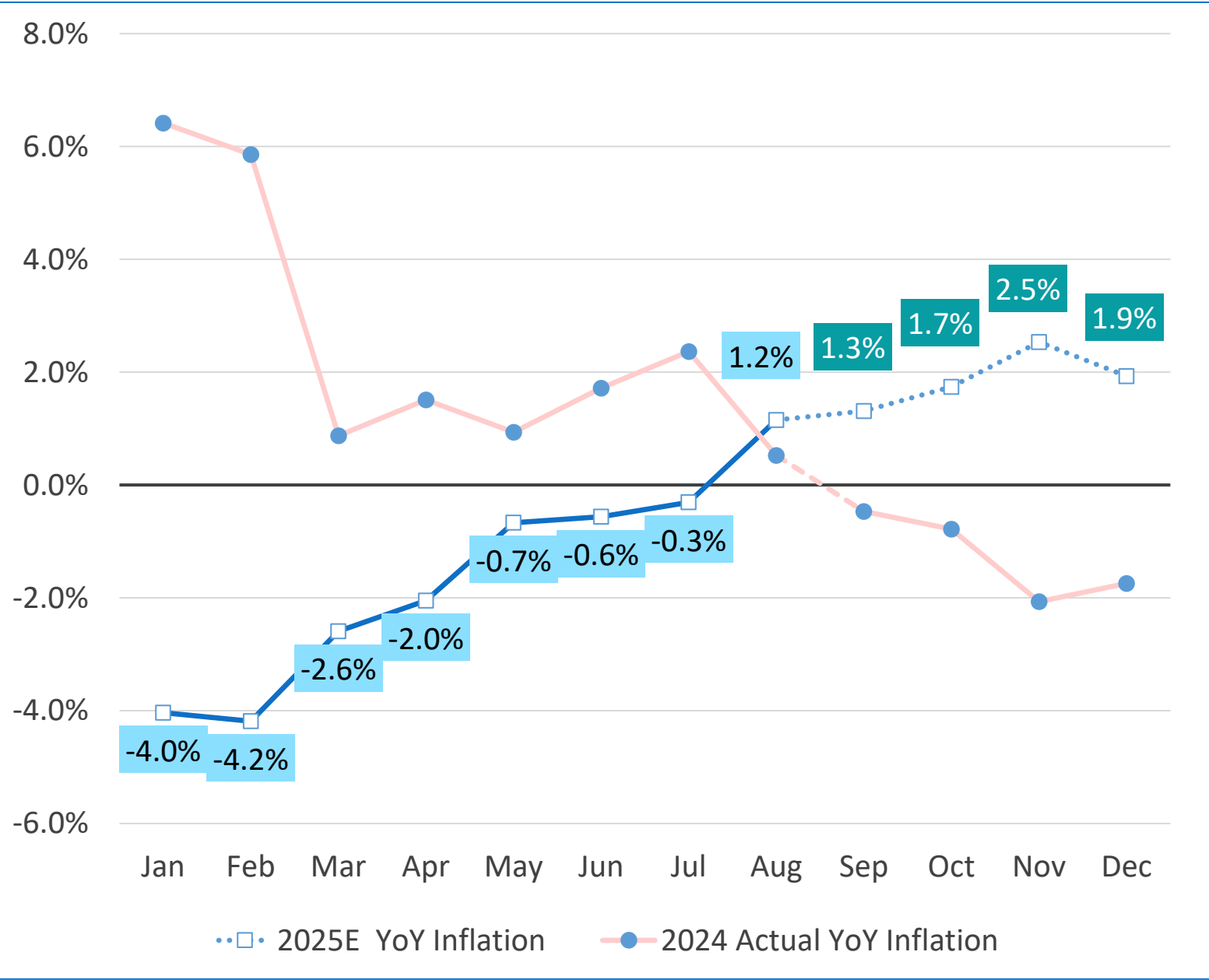


# ...primarily due to lower-than-anticipated inflation

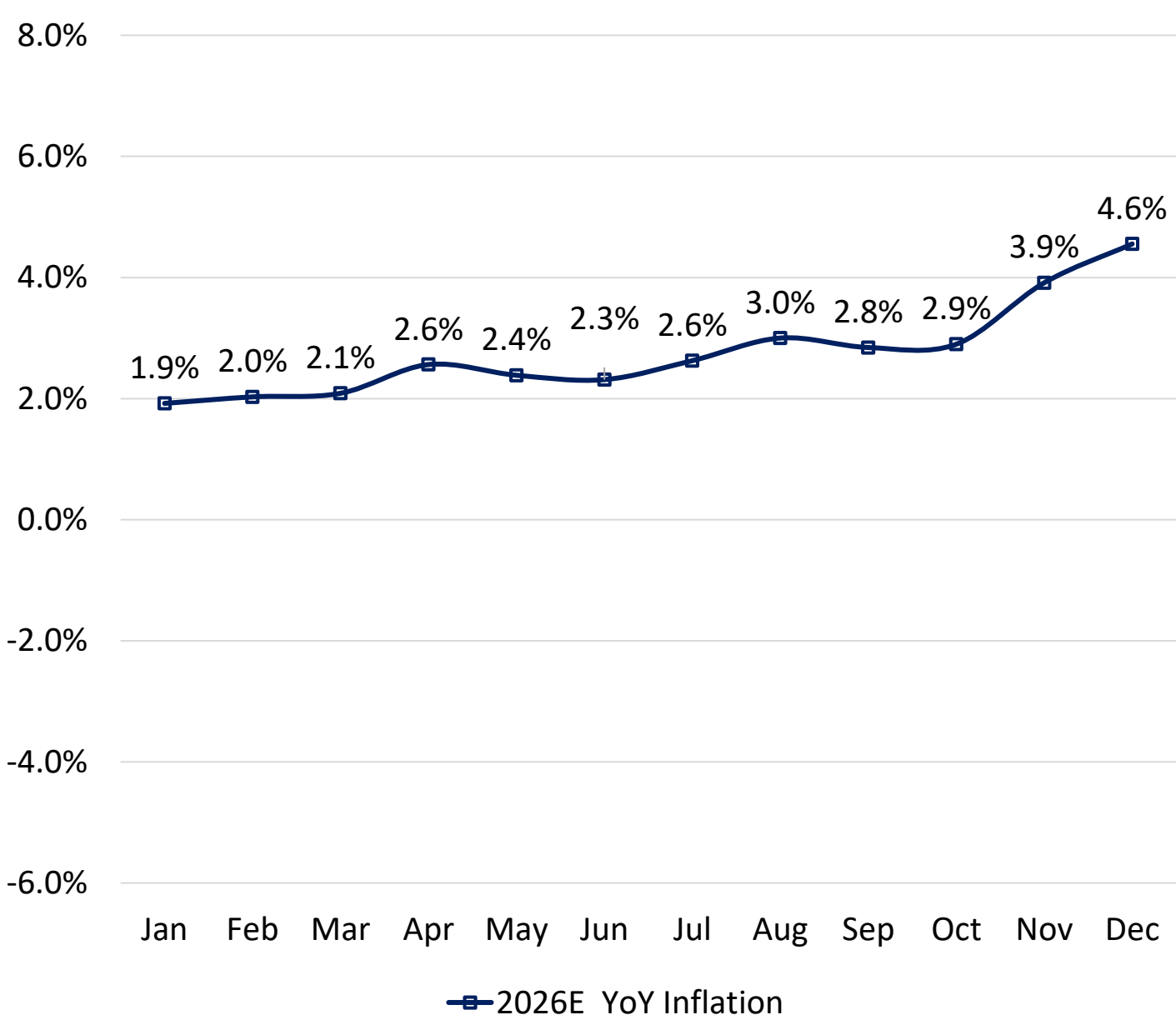
FCR expects the upward trend in inflation, which began in August 2025, to persist through the remainder of the year, driven primarily by the reversal of electricity tariffs as well as the base effect starting from Sep 2025.

In 2026E, FCR expects inflation to remain positive, though below the CBSL target of 5%, with average inflation expected at around 2.8%.

2024 YoY & 2025E YoY Inflation



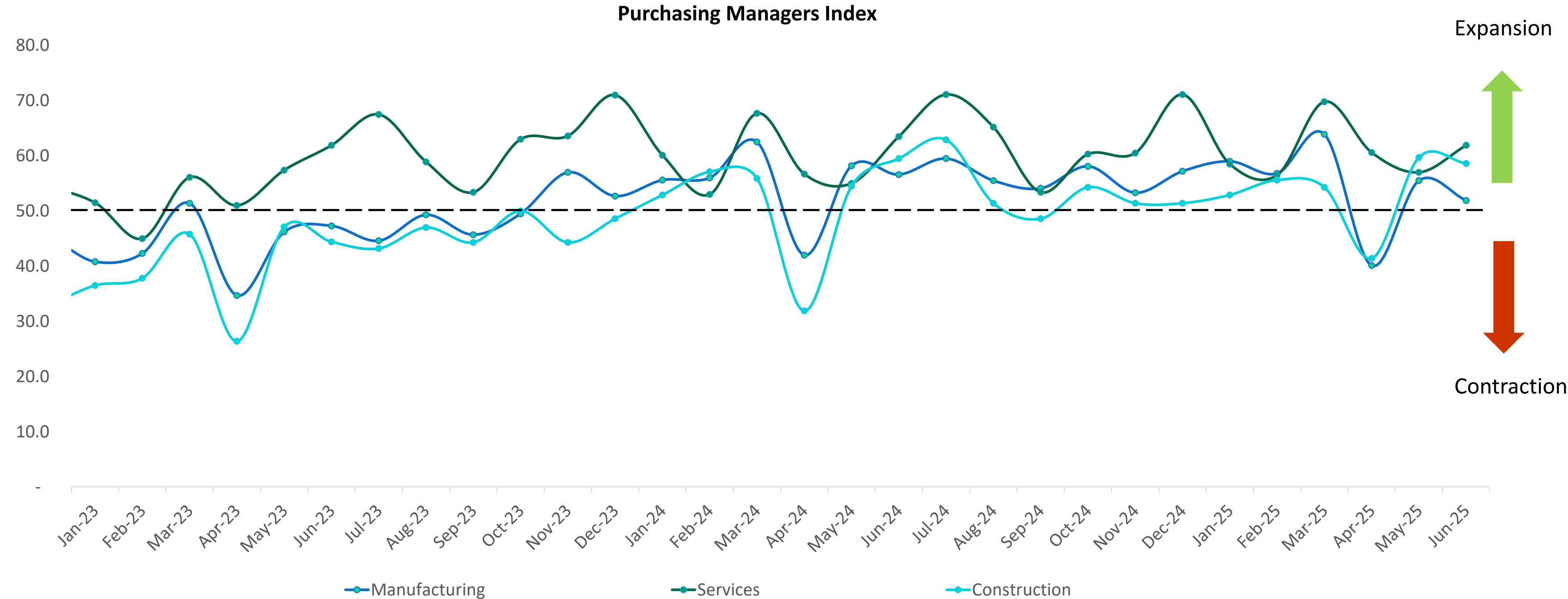
2026E YoY Inflation





# As business activity continues to expand...

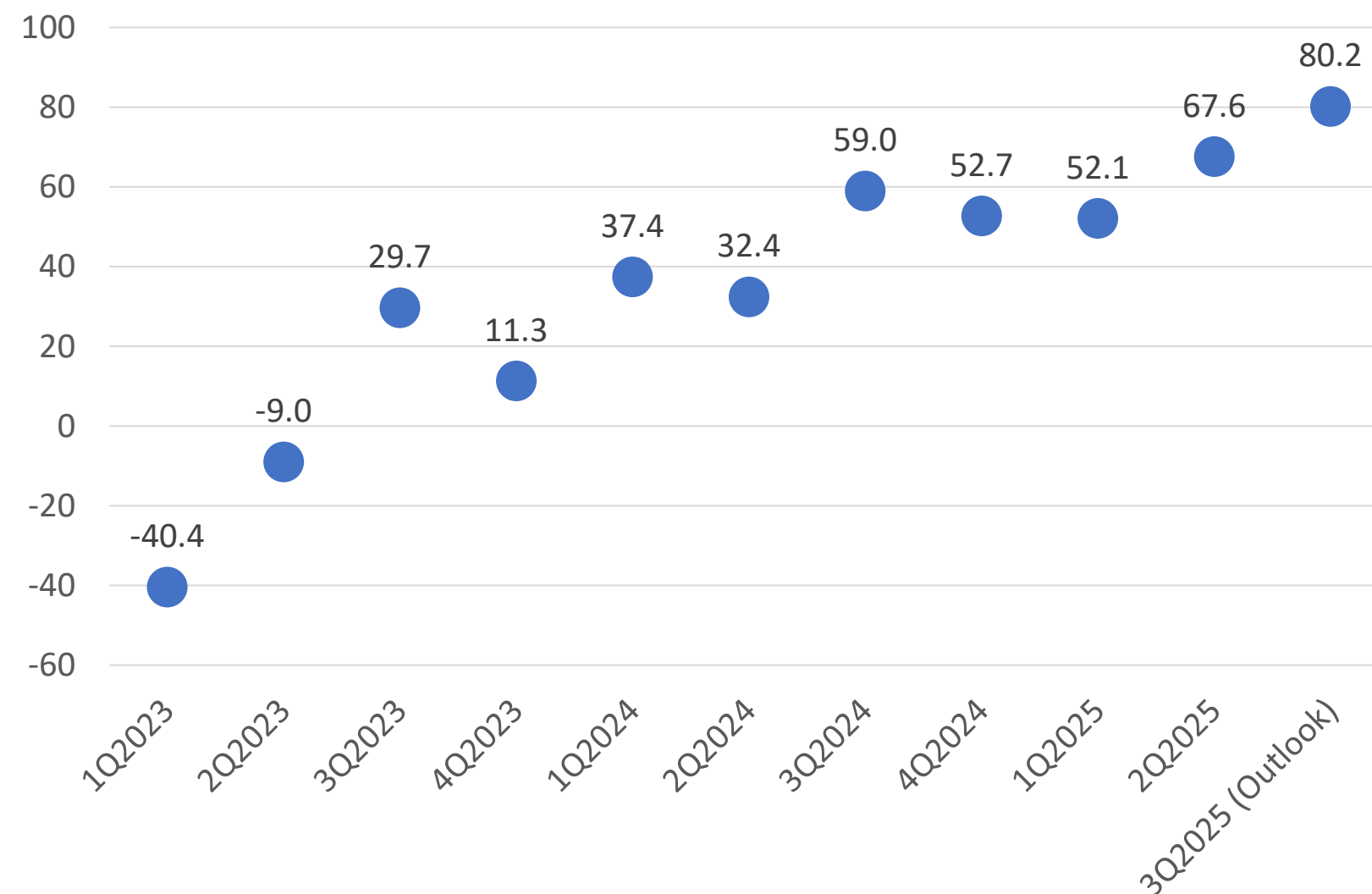
The broad-based expansion across all three sub-sectors of the Purchasing Managers' Index (PMI) points to continued economic momentum. Although FCR expects GDP growth to ease slightly in the coming quarters, this moderation is likely to stem from a slowing consumption growth, partially impacted by higher tax burdens and a measured approach to government CapEx.



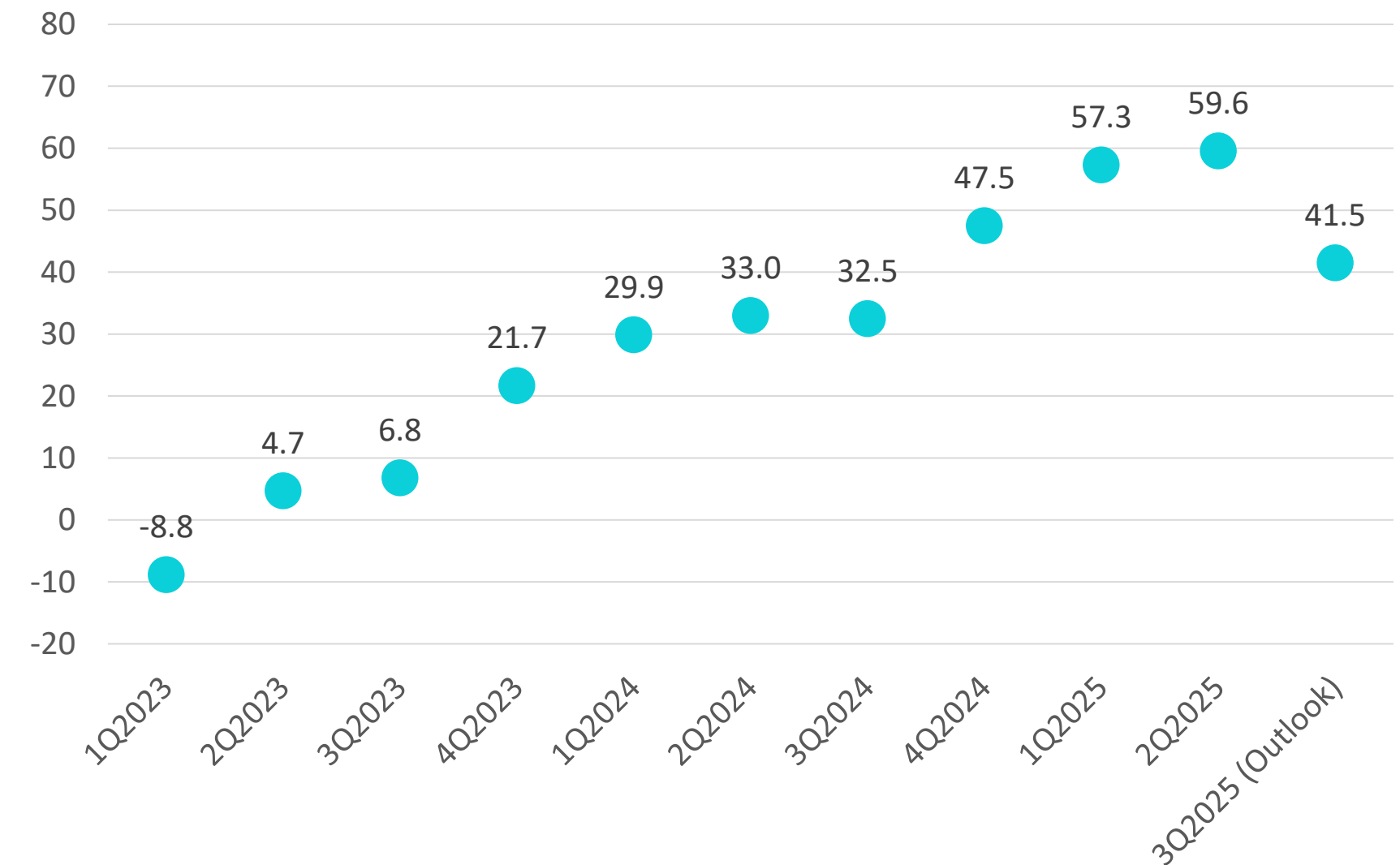
# ...lower rates lighten the burden of funding this growth, reducing business hurdles...

The ongoing economic recovery, driven by strong consumer demand, improved macroeconomic fundamentals, and rising investor confidence has contributed to a notable increase in both credit demand and lending activity. In the forthcoming quarters, demand for credit is anticipated to rise further, supported by expected reductions in interest rates, a potential resurgence in vehicle imports, and enhanced business confidence. Concurrently, the willingness of financial institutions to extend credit is likely to improve, underpinned by favourable liquidity positions, continued economic recovery, and a broadly positive economic outlook, though this improvement may occur at a slightly slower pace than in previous quarters.

## Demand for loans (Index value)



## Willingness to lend (Index value)



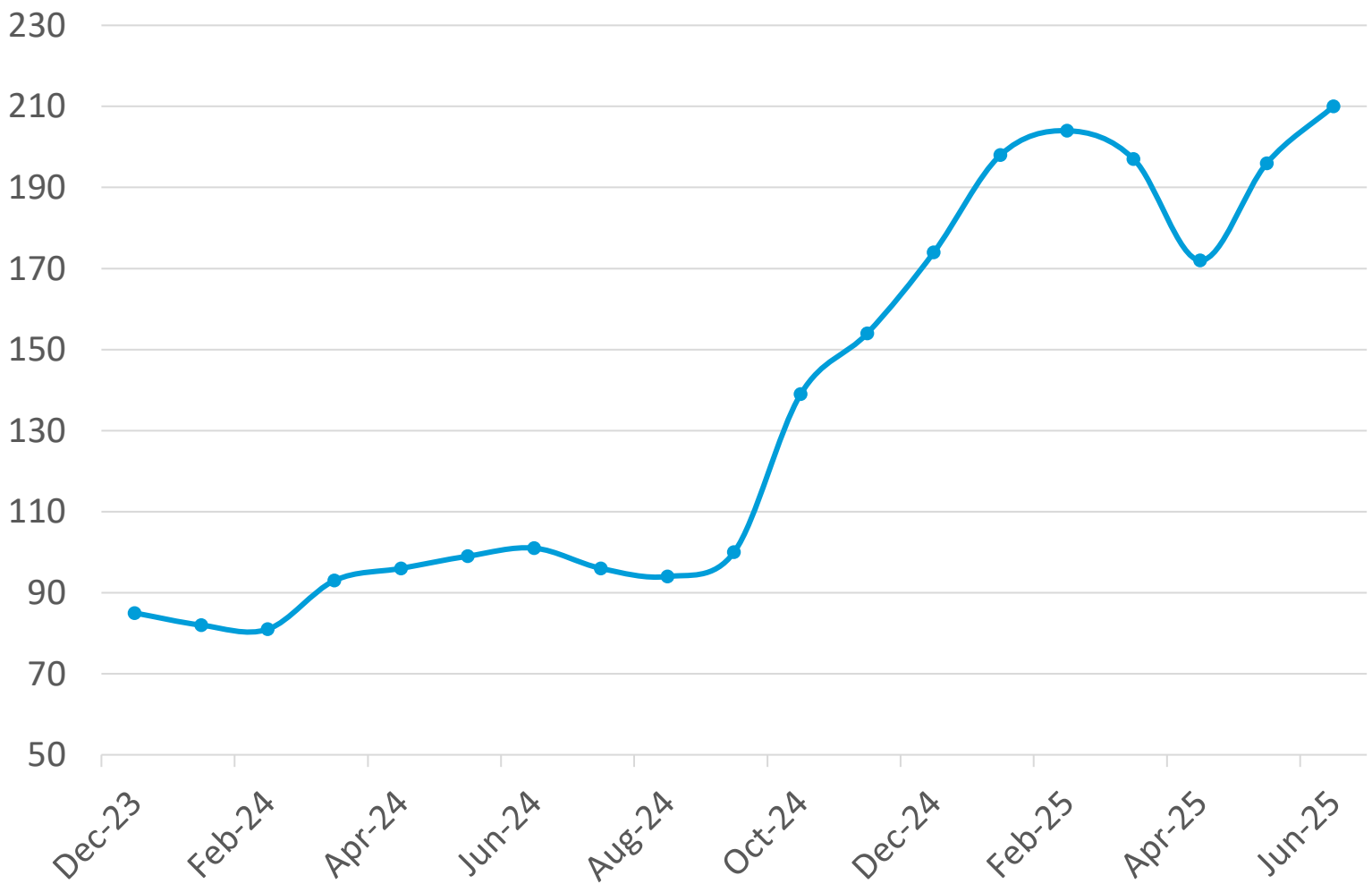


# ...thereby, fueling consistent gains in business confidence

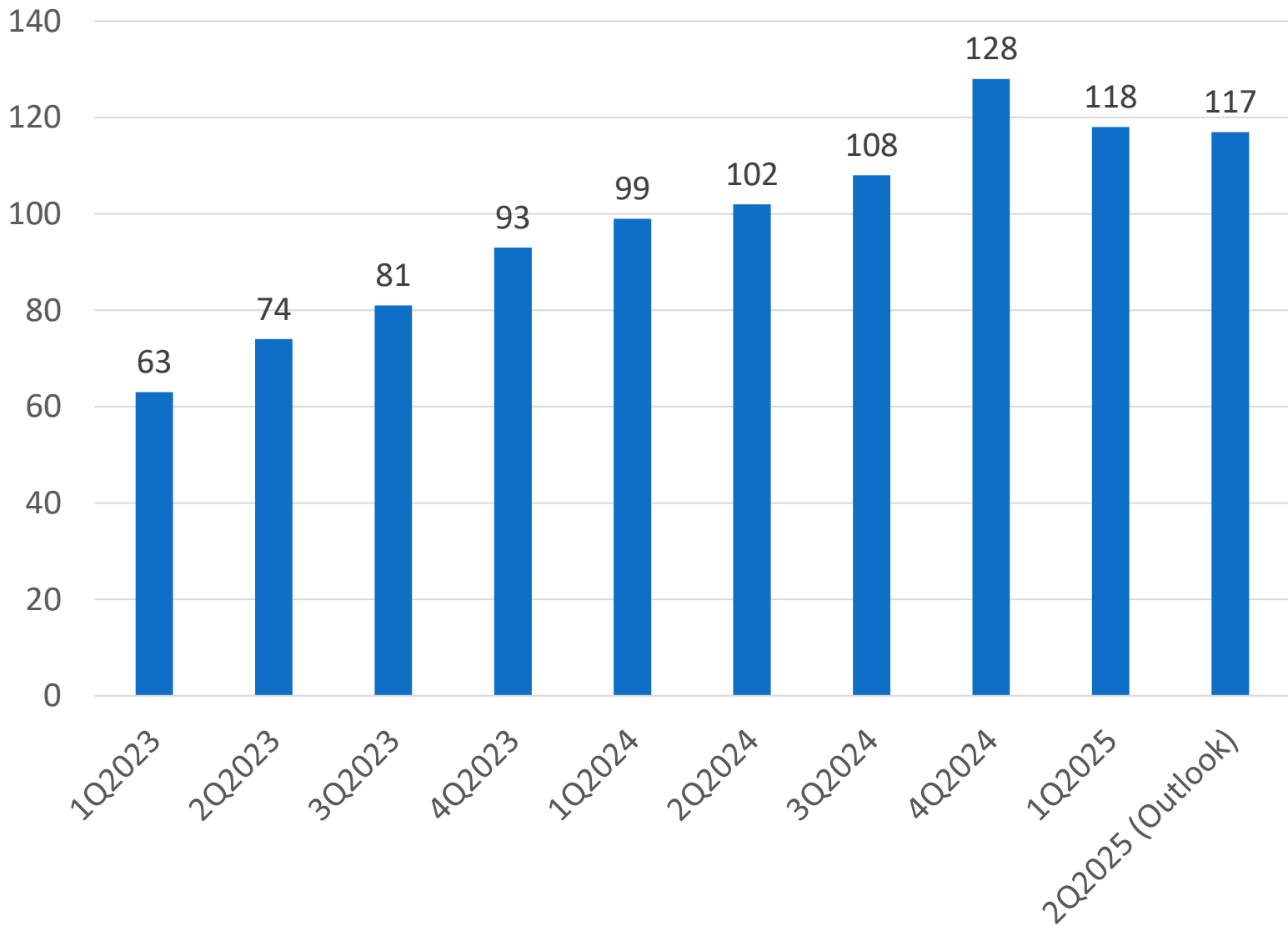
The Business Confidence Index soared to a record high in June, climbing 14 basis points to reach an unprecedented count of 210, up from 196 in May. June’s milestone consolidates the upward momentum observed in May, which was largely driven by the outcome of local government elections.

The Business Condition Index, which captures the firms’ assessment of the current and future business environment, indicates improvements in Q1 2025. Furthermore, the outlook for Q2 2025 continues to remain above the neutral threshold.

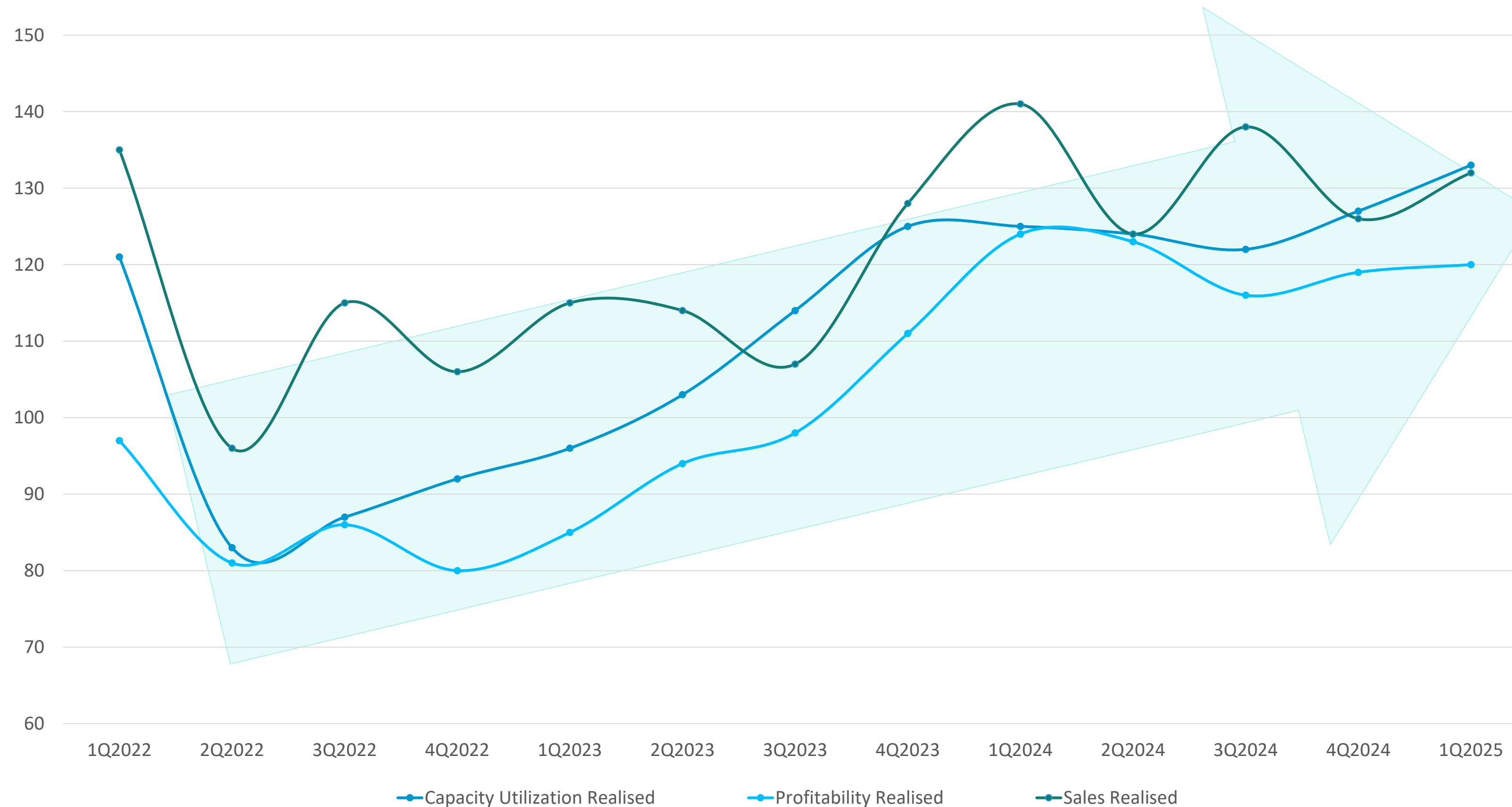
Business Confidence Index



Business Condition Index



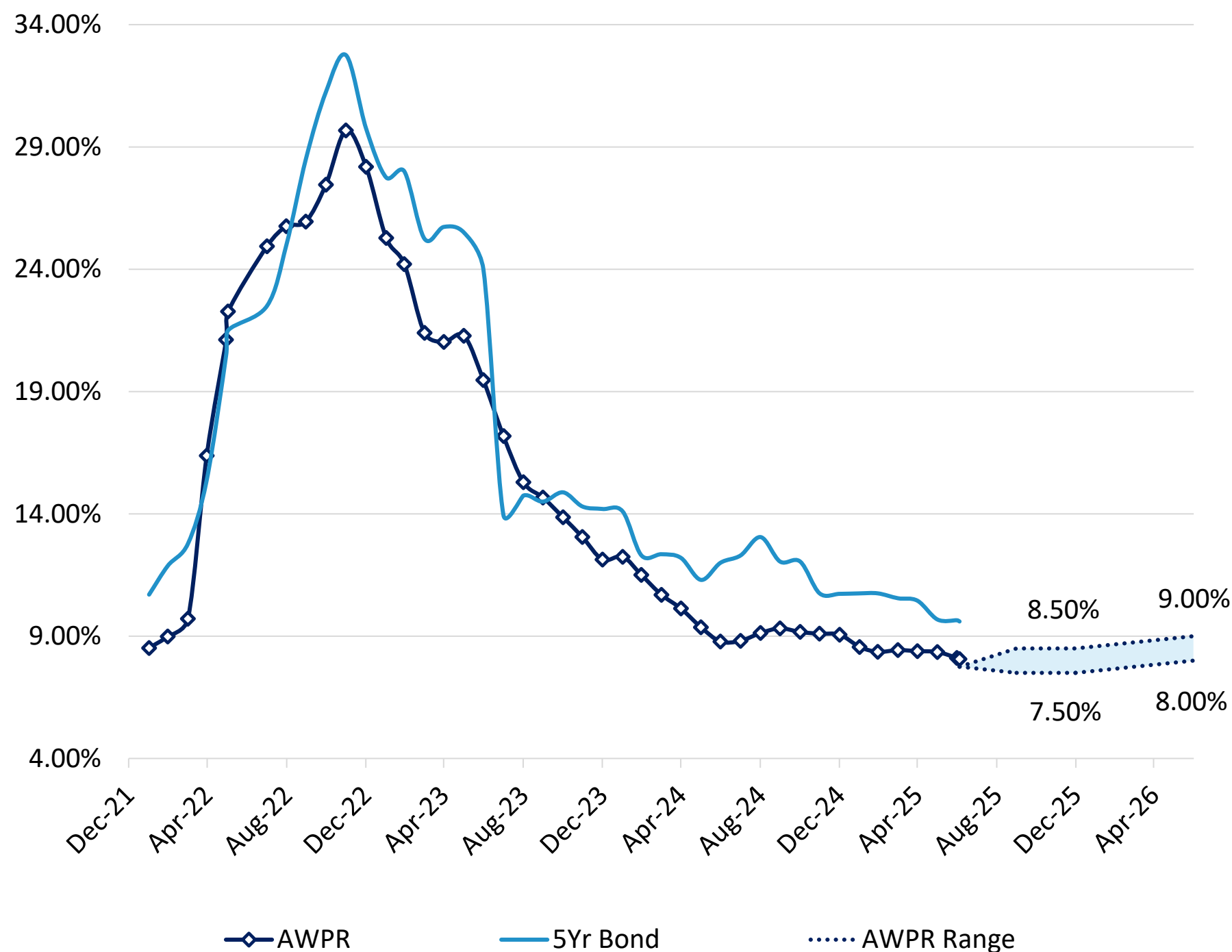
# Higher factory utilization rates driven by increased activity...





# ...reduction in finance costs stemming from lower rates...

Expectations for AWPR



## AWPR to reduce further

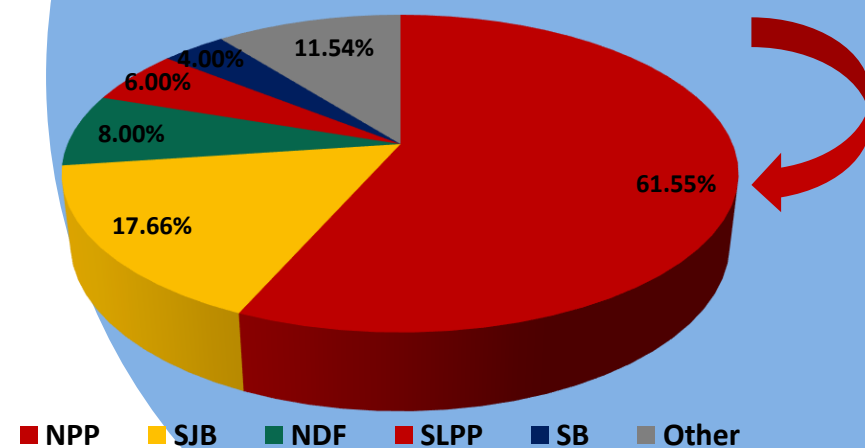
**AWPR to fall further:** Weaker than expected consumer demand coupled with increased demand for credit from corporates and lower risk appetite of banks, pushed down AWPR beyond our expectations and towards the risk-free rate in 1H2025. However, on the back of an expectation of another 25bps rate cut by the monetary board of the CBSL, AWPR is expected to decrease to between 7.5% - 8.5% by 2H2025E.

**AWPR target upgraded to 8.0%-9.0%:** Gradually rising state credit, along with sustained private sector demand, is expected to push the AWPR into our target range by 1H2026E.

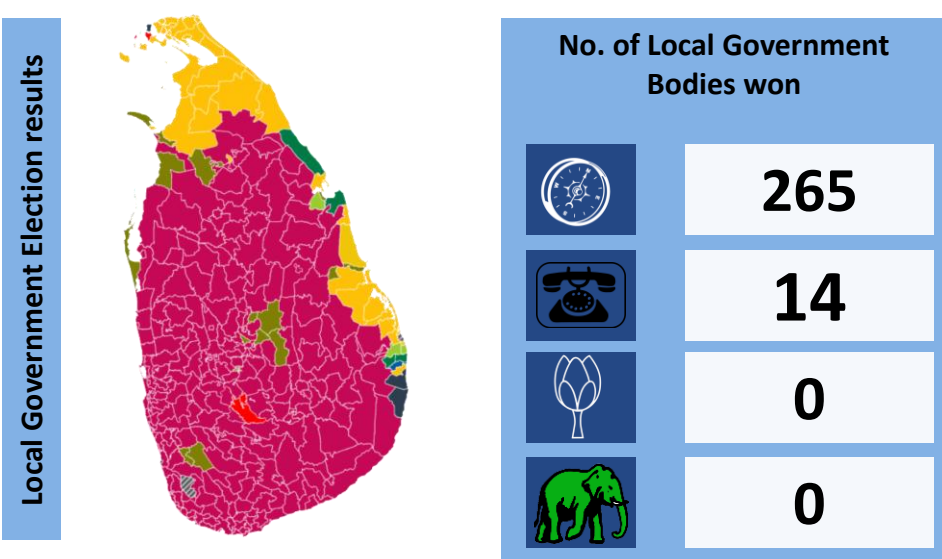
# ...reinforced by political stability and ongoing IMF engagement...

## 2024 ELECTIONS

During 2024 Presidential Election, which was on 9<sup>th</sup> September 2024, Sri Lanka elected Mr. Anura Kumara Dissanayake as the 9<sup>th</sup> Executive President of the Democratic Socialist Republic of Sri Lanka, with him receiving a majority of 42.31% of the total votes cast.



The General Election which was held on 14<sup>th</sup> December 2024 resulted in a decisive victory for the President's party, the NPP, which secured over **2/3 majority**, enabling it to form a government.



The NPP's 2/3 majority in Parliament and its victory in the Local Government Elections have reinforced political stability, supporting stronger policy implementation. Although voter turnout was low and the NPP secured only 43.26% of the vote at the LG polls, the party is still expected to maintain its lead in the upcoming Provincial Elections, likely to be held within the next 12 months. Moreover, the government's continued commitment to good governance and adherence to the IMF program, further enhances policy credibility. Together, these factors create a stable political and economic environment, encouraging long-term investor confidence and sustainable economic growth.

The IMF completed the 4th EFF review in July 2025, delayed from April due to a new government and the 2025 budget. As a result, remaining IMF tranches are also likely to be delayed.

**Table 9. Sri Lanka: Reviews and Purchases Under the Four-Year Extended Arrangement**

Availability Date	Amount (millions of SDR)	Percent of Quota (%)	Conditions
At arrangement approval	254	43.9	Board Approval of the Extended Arrangement
September 1, 2023	254	43.9	Completion of the 1st review based on end-June 2023 and continuous performance criteria
April 1, 2024	254	43.9	Completion of the 2nd review based on end-December 2023 and continuous performance criteria
October 1, 2024	254	43.9	Completion of the 3rd review based on end-December 2024 and continuous performance criteria
April 1, 2025	254	43.9	Completion of the 4th review
October 1, 2025	254	43.9	Completion of the 5th review based on end-June 2025 and continuous performance criteria
April 1, 2026	254	43.9	Completion of the 6th review based on end-December 2025 and continuous performance criteria
October 1, 2026	254	43.9	Completion of the 7th review based on end-June 2026 and continuous performance criteria
March 1, 2027	254	43.9	Completion of the 8th review based on end-December 2026 and continuous performance criteria
<b>Total</b>	<b>2,286.0</b>	<b>395.0</b>	

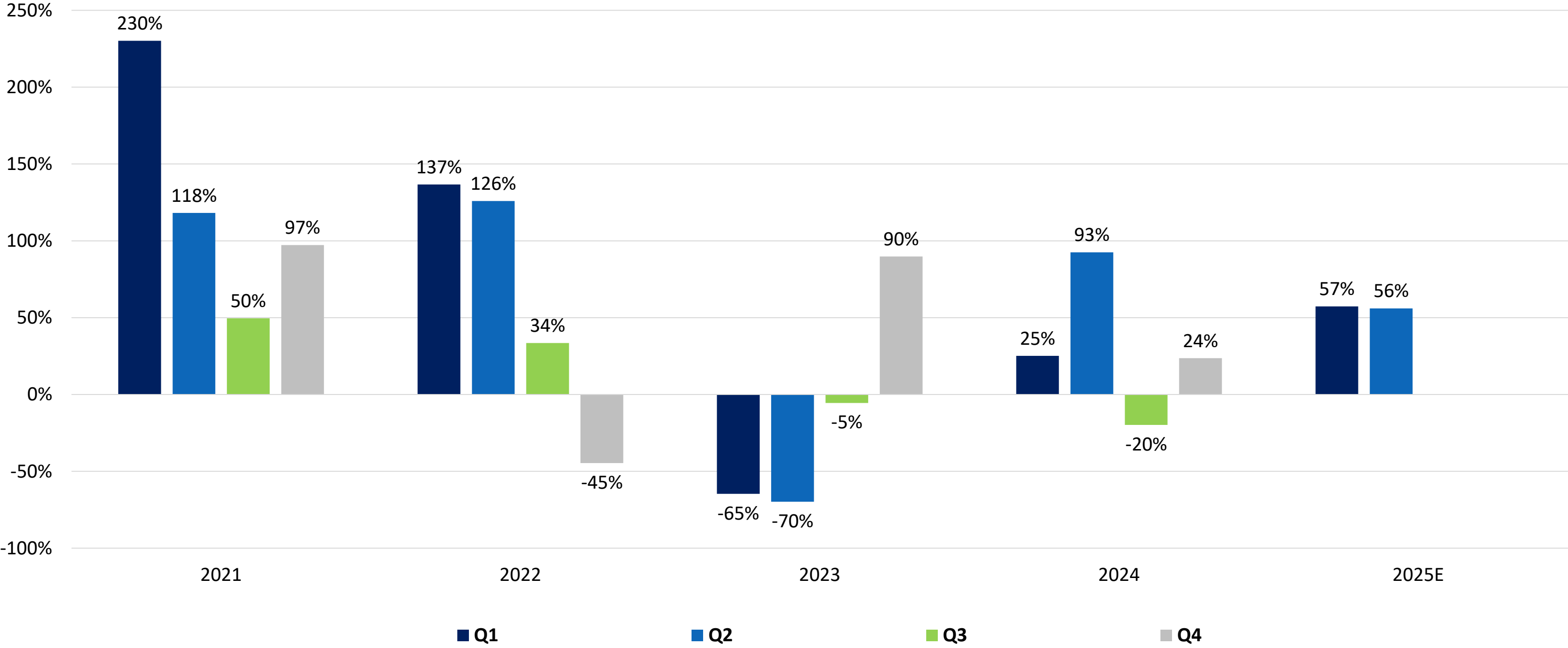
Source: IMF staff.



# ...underpin strong corporate earnings growth...

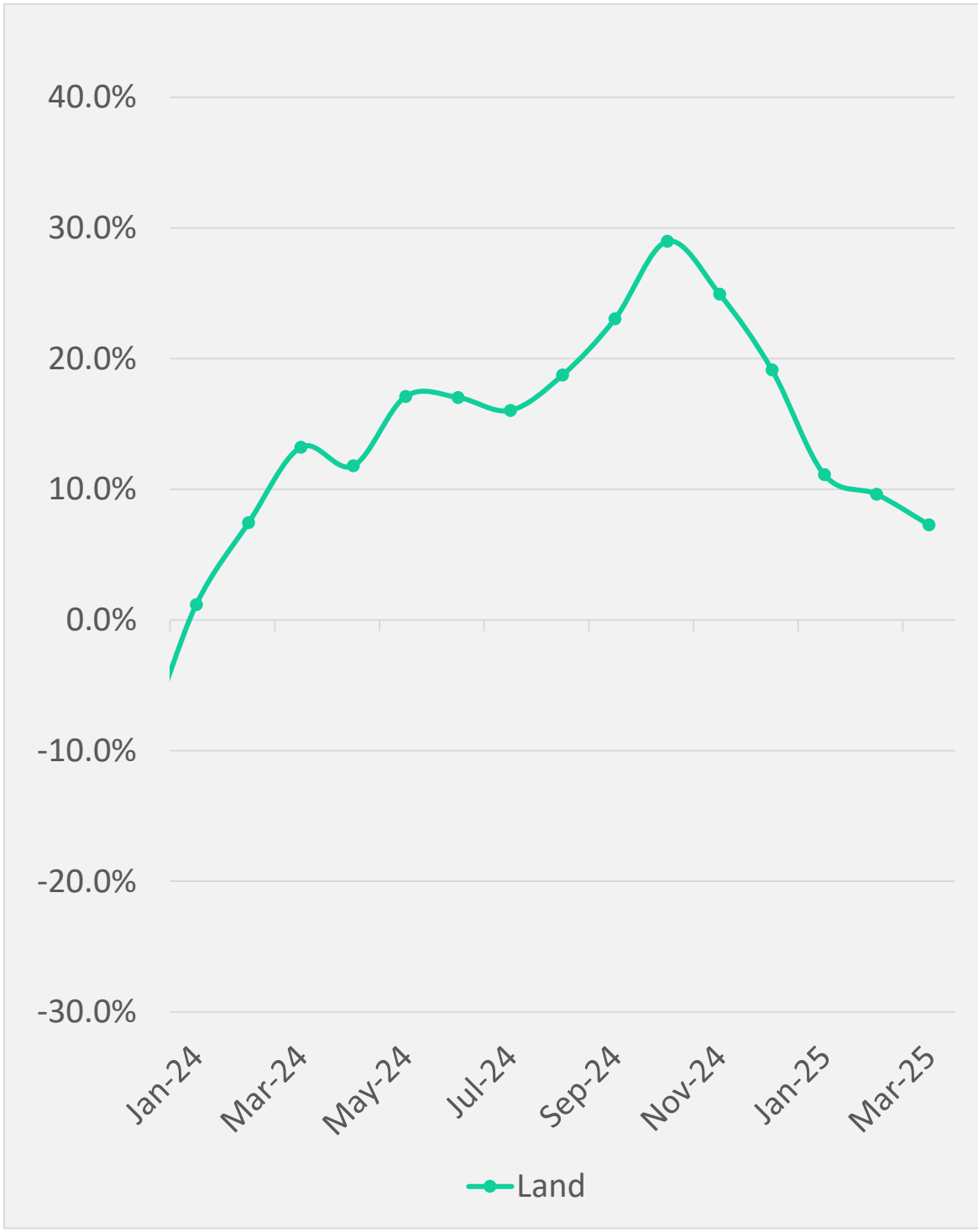
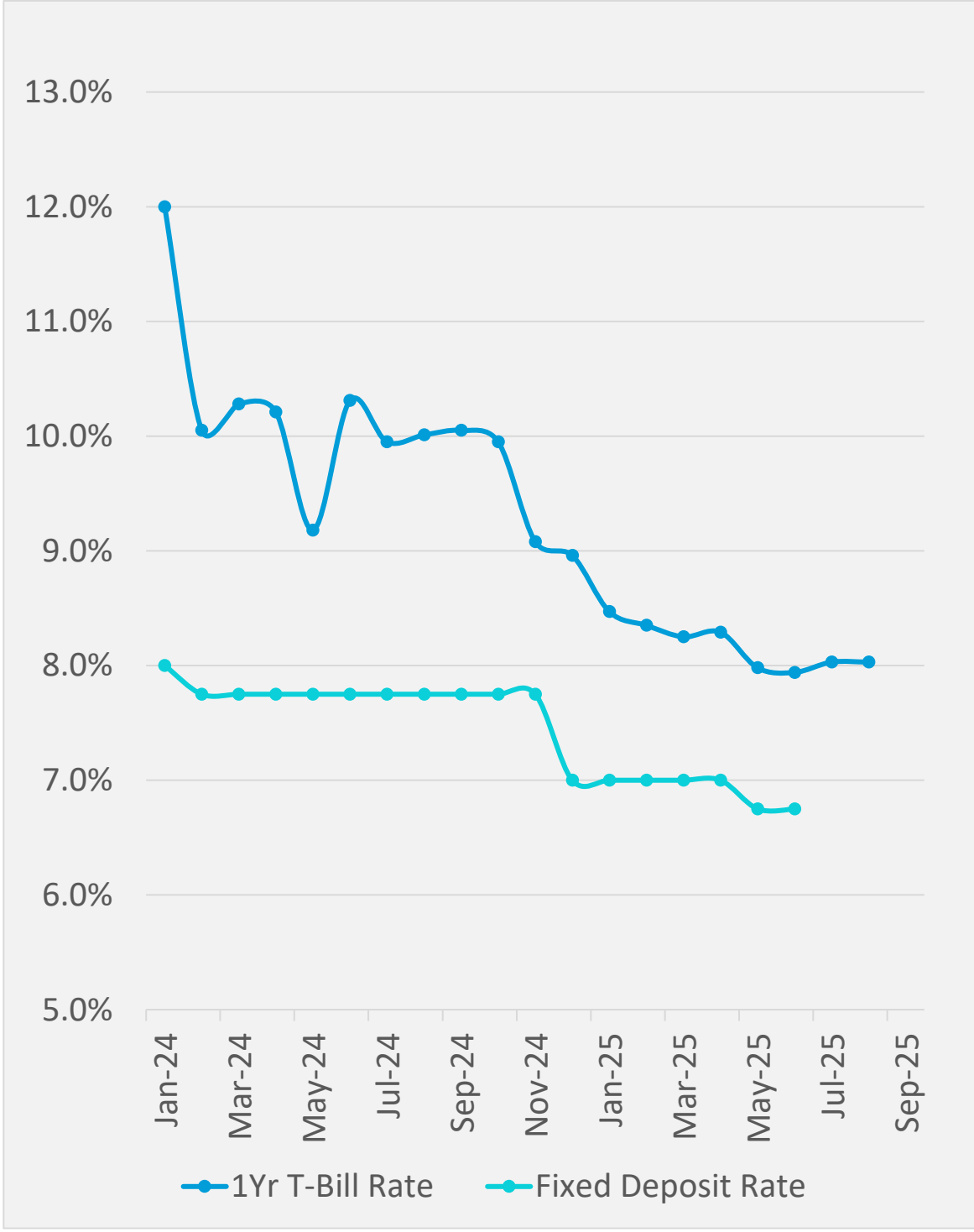
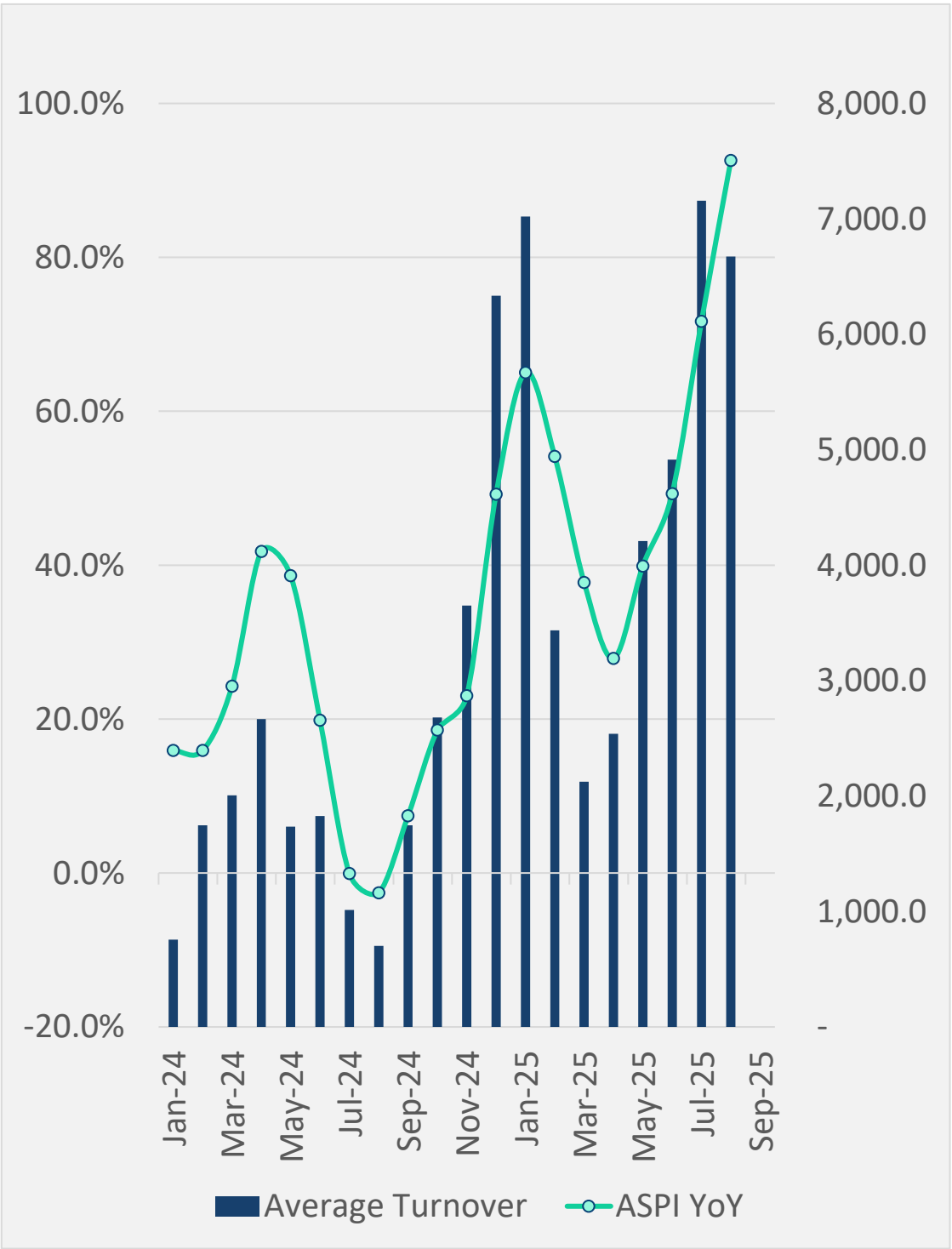
Listed companies recorded a 56% YoY earnings increase in 2Q2025, marking the seventh consecutive quarter of annual growth, driven by strong performances in Diversified Financials, Banking, Telecommunications, and Food, Beverage & Tobacco sectors.

Listed Corporates - Quarterly Earnings Growth (%)



# ...supporting equity inflows amid weakening alternative returns...

Improvement in average turnover at CSE indicates a possible shift in asset classes as interest rates and government security yields remains moderate.





# Geopolitical tensions have escalated across key global regions...

## Ukraine vs Russia

- Lower tourist arrivals
- Higher energy costs
- Lower import of wheat and other food products
- Lower tea exports

## Israel vs Iran

- Higher energy costs
- Lower worker remittances
- Lower tea exports
- Lower tourist arrivals

## India vs Pakistan

- Lower tourist arrivals
- Maritime trade disruption
- Lower FDIs and capital flows



# ...triggering downgrades in global growth forecasts by major agencies...

**ALJAZEERA** News + Middle East Explained Opinion Sport Video M

Donald Trump > Live updates: When will Trump's bill take effect? How world leaders massage Trump's ego

Economy | World Bank

## World Bank slashes global economic outlook as trade tensions continue

*The bank warned that without a swift course correction, the harm to living standards could be 'deep'.*



10 Jun 2025

The World Bank has slashed its 2025 global growth forecast, citing trade tensions and policy uncertainty as the United States imposed wide-ranging tariffs that weigh on global economic forecasts.

On Tuesday, the bank lowered its projection for global gross domestic product (GDP) growth to 2.3 percent in its latest economic prospects report, down from the 2.7 percent that it expected in January. This is the most recent in a series of downgrades by international organisations.

**Reuters** World Business Markets Sustainability Legal Commentary More

## IMF cuts growth forecasts for most countries in wake of century-high US tariffs

By Andrea Shalal

April 23, 2025 1:17 AM GMT+5:30 · Updated April 23, 2025

Summary

- IMF sees global growth of 2.8% in 2025, down from 3.3% in January forecast
- IMF chief economist says new era ushered in by trade reset
- Escalating trade tensions could further dampen growth
- Click here for a table of the IMF's economic projections for 2025 and 2026 with comparisons to prior WEO forecasts

## US tariffs, China slowdown cloud developing Asia's growth outlook, says ADB

By Reuters

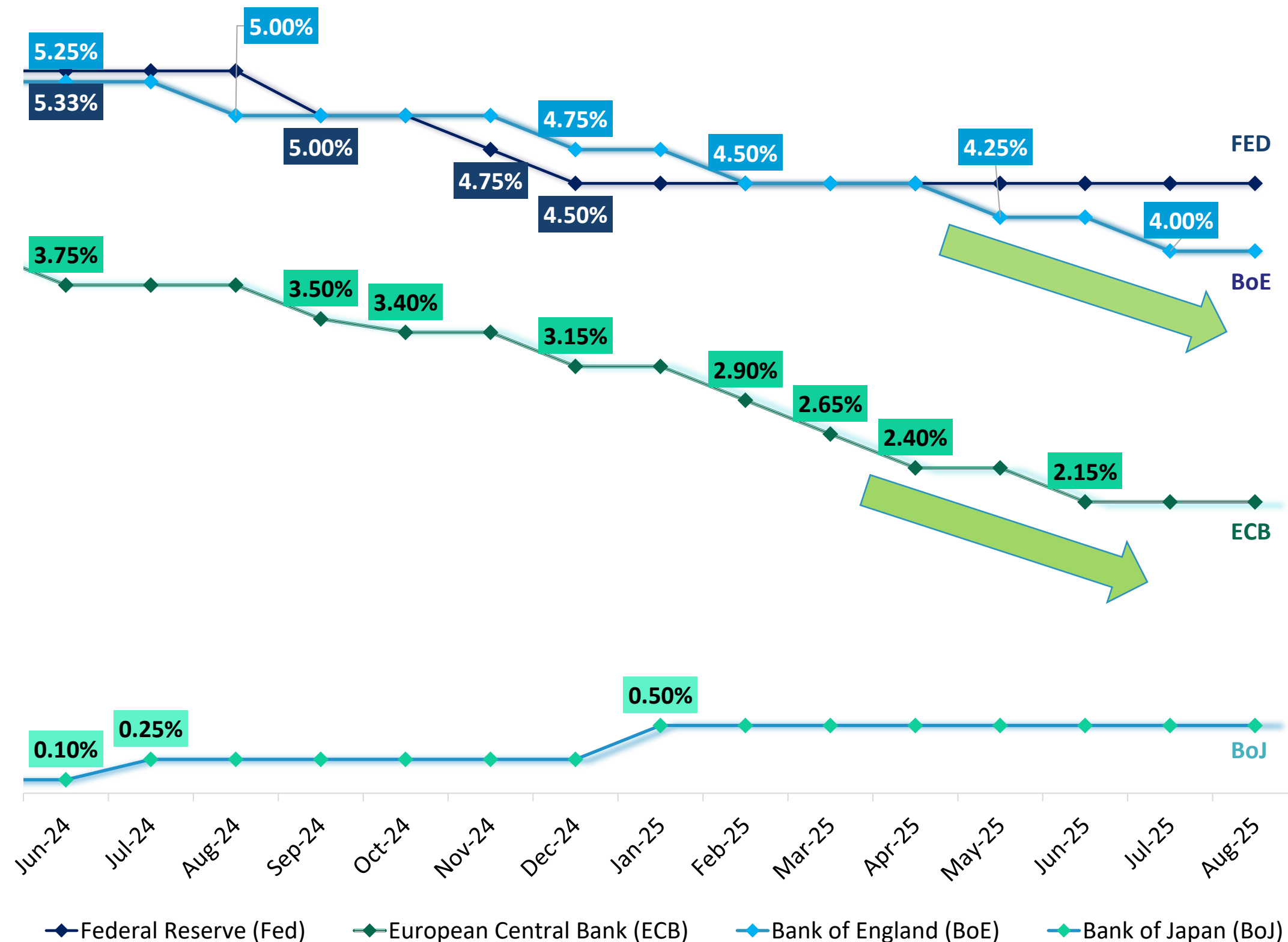
April 9, 2025 5:37 AM GMT+5:30 · Updated April 9, 2025

MANILA, April 9 (Reuters) - The full implementation of U.S. tariffs could cut developing Asia's growth by about a third of a percentage point this year and nearly a full percentage point in 2026, the Asian Development Bank said on Wednesday.

In its Asian Development Outlook report, the ADB projected that growth in developing Asia will ease slightly to 4.9% in 2025 — the slowest pace since 2022 — and slow further to 4.7% in 2026, from 5.0% in 2024.



# ...driving Central Banks to lower rates...



**The Federal Reserve** - The Fed's most recent dot plot projections indicate two additional interest rate cuts in 2025.

**Next Policy Announcement Date: 17 Sep 2025**

**The Bank of England** - In Aug 2025, the BoE reduced interest rates to 4.00%. However, as inflation is expected to peak in September, analysts now see a reduced likelihood of a rate cut at the next meeting.

**Next Policy Announcement Date : 18 Sep 2025**

**The European Central Bank** - The ECB maintained rates in Jul 2025, after eighth consecutive reductions since last Jun. The ECB has now signaled confidence in the current path, suggesting no further easing in the near term.

**Next Policy Announcement Date : 11 Sep 2025**

**The Bank of Japan** - In Jul 2025, the BoJ kept rates at 0.5%, continuing its cautious policy stance. Analysts now expect a rate hike only in early 2026 amid inflation concerns and growing risks from U.S. tariffs.

**Next Policy Announcement Date : 19 Sep 2025**



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## 4.0 Market Valuations

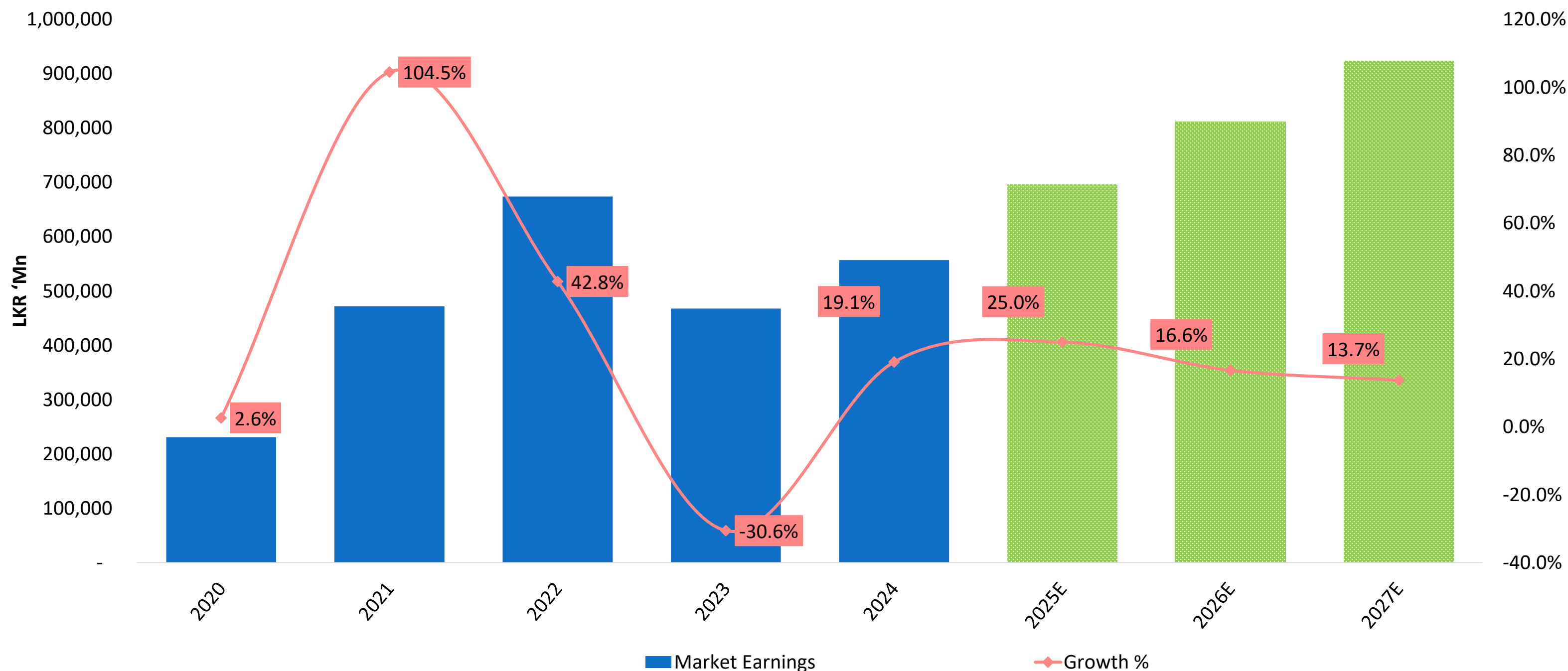
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# With corporate earnings rising 25% in 2025E and 17% in 2026E...

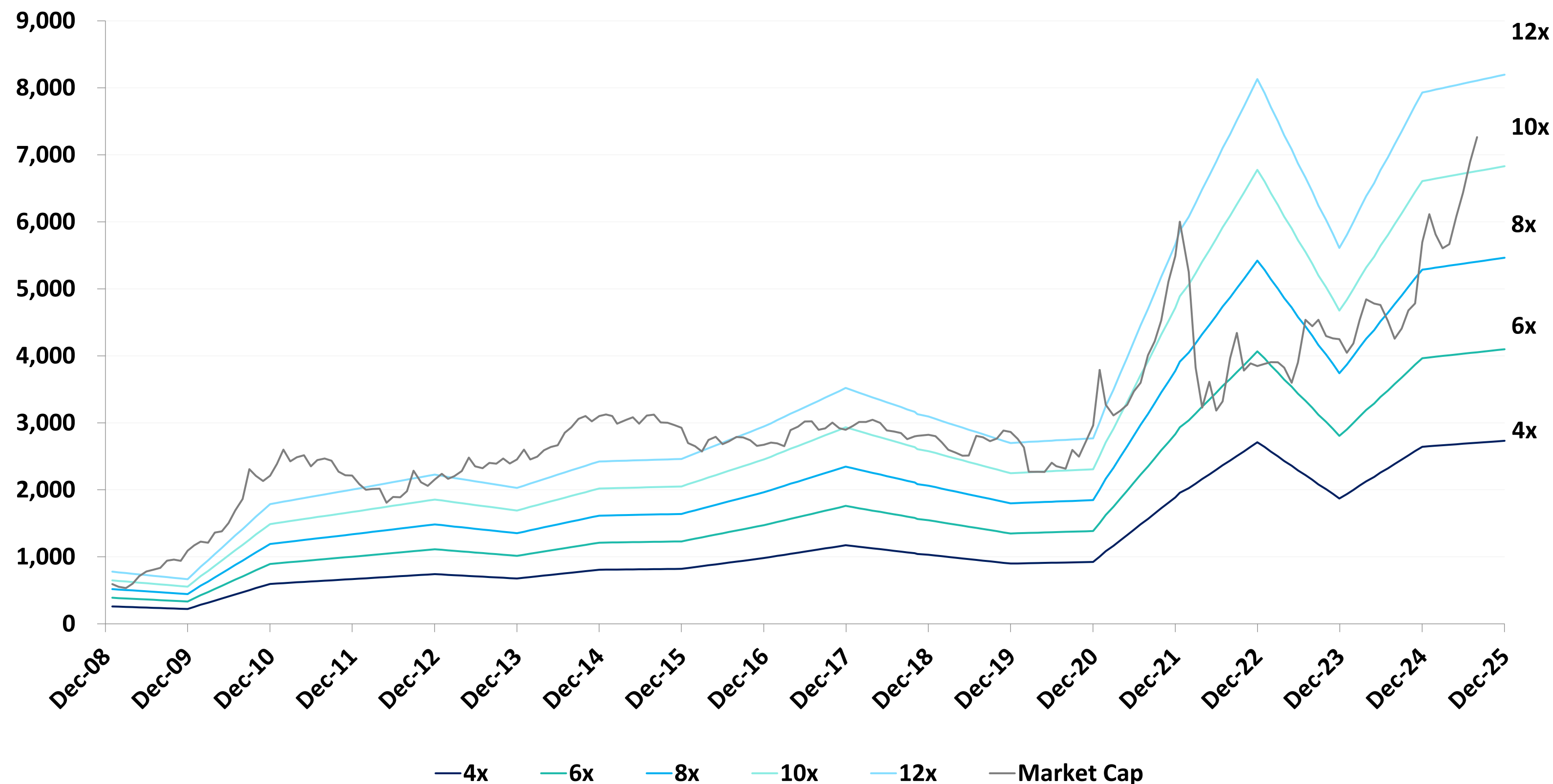
Listed corporates recurrent profits, taking off the one-off impacts from ISB reversals and gain of LKR 110.0Bn from LOLC, expected to jump by 25.0%YoY in 2025E and 16.6%YoY in 2026E. Growth is likely to be driven by the Banking & Financial Services, Consumer Staples & Retail, Capital Goods, Construction & Infrastructure, and Export-Oriented Industries.

Listed Earnings Forecast










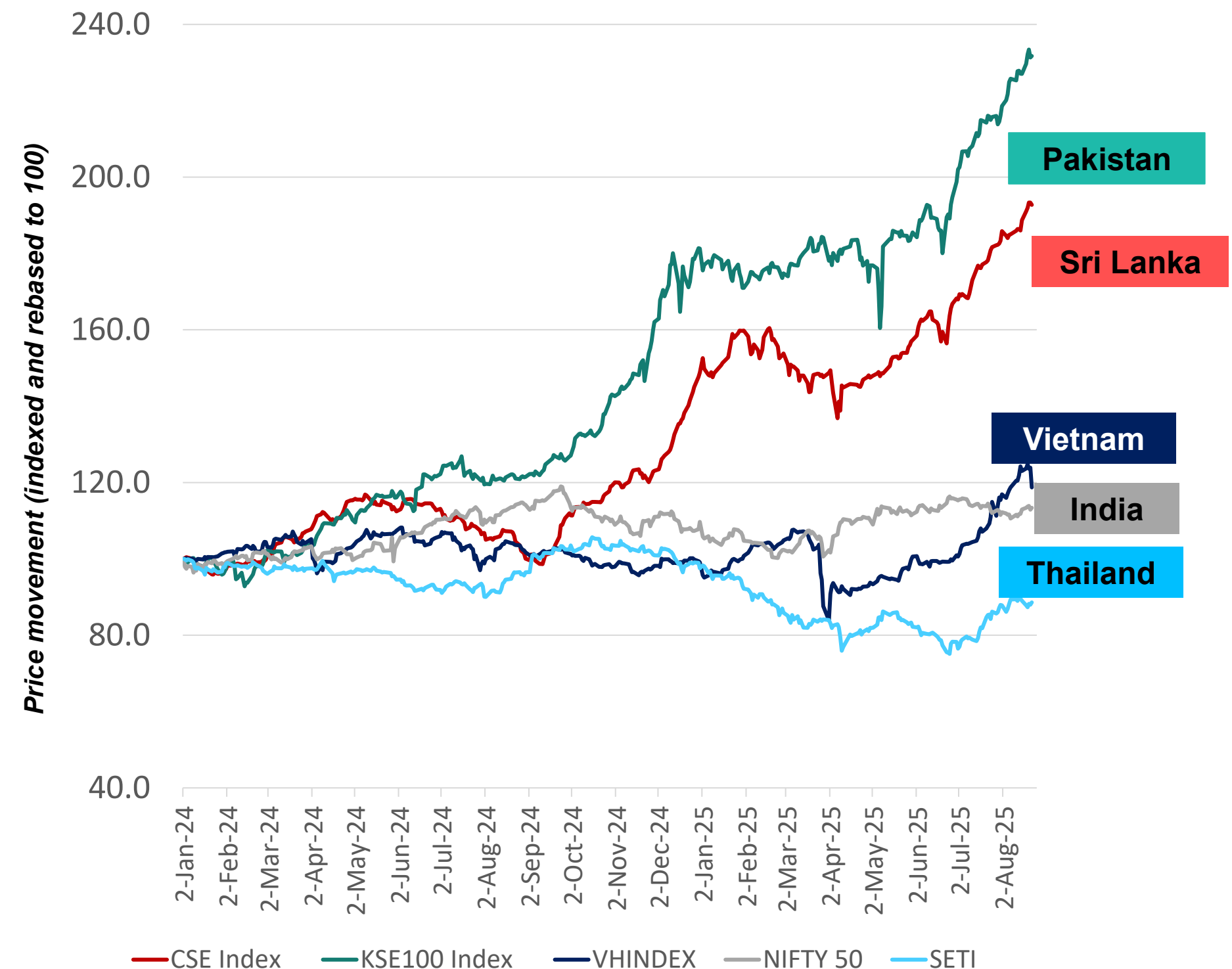
# ...the ASPI remains at a discount to 10-year PER of 12.0x...



# ...also in comparison with regional peers...

With a PER of 9.6x, higher only than Pakistan (KSE100) and a PBV of 1.4x, the ASPI remains attractively valued relative to regional peers.

Stock Exchange	Bloomberg Ticker	Last Close	Market Capitalization (USD Bn)	PER	PBV
 <b>CSE</b> COLOMBO STOCK EXCHANGE Creating Wealth and Value (Colombo Stock Exchange)	CSEALL	20,575.6	23.4	9.6	1.4
 <b>PAKISTAN STOCK EXCHANGE LIMITED</b> (Pakistan Stock Exchange)	KSE100	148,815.3	43.4	8.2	1.5
 <b>HANOI STOCK EXCHANGE</b> SỞ GIAO DỊCH CHỨNG KHOÁN HÀ NỘI (Vietnam Hanoi Stock Exchange Equity Index)	VHINDEX	266.6	216.7	21.2	1.2
 <b>Nifty 50</b> (NIFTY 50 India)	NIFTY 50	24,967.8	5,020.0	23.4	3.5
 <b>SET</b> The Stock Exchange of Thailand (Thailand Stock Exchange)	SETI	1,262.7	1,190.7	13.8	1.2




















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## 5.0 Top Picks for 2026

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## FIRST CAPITAL 2026 TOP RECOMMENDATIONS

Stock	Stock Code	28-Aug-25	PER	PBV	DY	52-Week High	52-Week Low	Target Price 2025E/FY26E	Target Status 2025E/FY26E	Target Price 2026E/FY27E
LKR										
	John Keells Holdings	JKH.N0000	23.30	78.3	1.0	0.6%	26.00	16.00	27.00	34.00
	Commercial Bank PLC - Voting	COMB.N0000	193.75	5.3	1.1	1.9%	199.25	78.00	190.00	Achieved
	National Development Bank PLC	NDB.N0000	143.50	5.6	0.8	1.4%	149.50	62.00	170.00	190.00
	Seylan Bank PLC	SEYB.N0000	102.75	6.3	0.9	1.0%	104.00	102.50	120.00	150.00
	LB Finance PLC	LFIN.N0000	139.50	7.2	1.5	4.1%	145.00	62.00	145.00	Achieved
	Commercial Credit and Finance PLC	COCR.N0000	132.00	7.3	1.5	3.0%	141.00	29.00	150.00	185.00
	Hayleys PLC	HAYL.N0000	175.25	9.8	1.4	3.1%	198.00	86.00	180.00	Achieved
	Teejay Lanka PLC	TJL.N0000	44.60	11.4	1.0	1.7%	59.00	37.00	56.00	65.00
	Hayleys Fabric PLC	MGT.N0000	44.90	8.5	1.6	4.6%	57.50	36.80	50.00	54.00
	JAT Holdings PLC	JAT.N0000	41.90	10.7	1.8	1.3%	42.70	14.50	40.00	Achieved
	Hemas Holdings PLC	HHL.N0000	30.50	11.4	1.8	2.6%	31.10	13.60	30.00	Achieved
	Ceylon Cold Stores PLC	CCS.N0000	110.00	17.3	4.3	3.9%	119.00	49.50	130.00	150.00
	Aitken Spence Hotel Holdings PLC	AHUN.N0000	87.20	12.9	1.2	0.0%	92.00	53.00	100.00	UR

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

\*HHL has been adjusted for the share sub division in the ratio 1:5

\*JKH has been adjusted for the share sub division in the ratio 1:10



# Thank you!

*“SUCCESSFUL INVESTMENTS IS ABOUT  
MANAGING RISKS”*

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