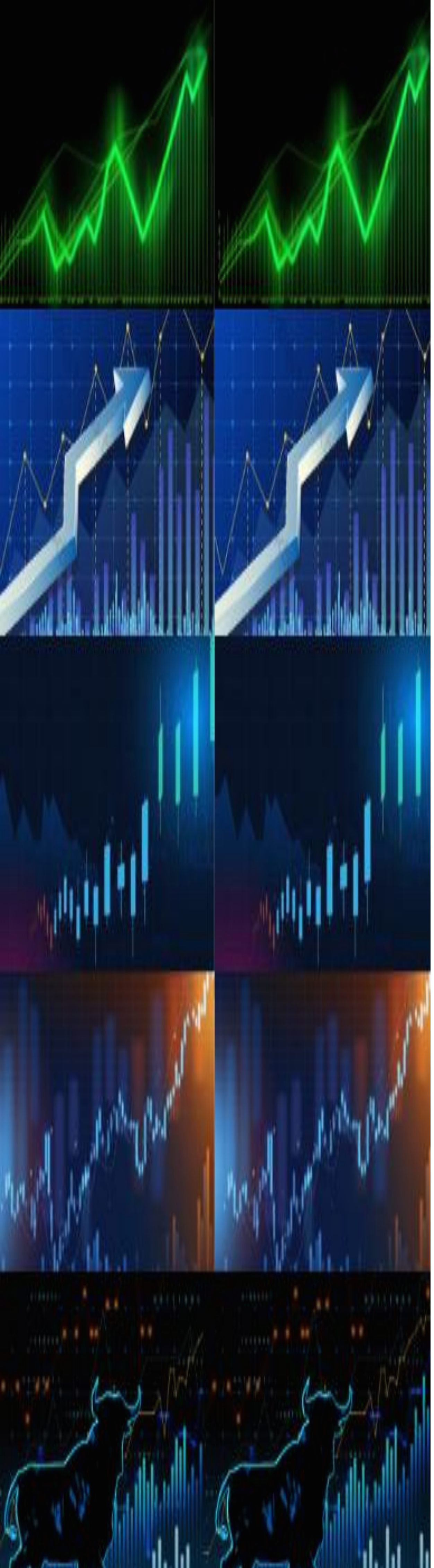

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# Outlook 2025

In 2024, Sri Lanka's investment landscape underwent significant transformations, marked by economic stabilization, policy reforms, and renewed investor confidence. The approval of a USD 12.55Bn debt overhaul led to credit rating upgrades by agencies like Moody's and Fitch, signaling improved fiscal health. The International Monetary Fund (IMF) and few other agencies like World Bank upgraded their growth forecast for Sri Lanka 2024. with IMF projecting the growth at 3% while WB forecasting at 4.4%, well above the initial projections of 2%-3% . These developments have collectively enhanced Sri Lanka's appeal as an investment destination, fostering a more robust and dynamic investment environment.

*Approval of a USD 12.55Bn debt overhaul led to credit rating upgrades by agencies signaling improved fiscal health*

In our view, it is crucial for Sri Lanka's newly appointed government to adhere to IMF guidelines to maintain economic stability and recovery. We believe that the budget speech to be presented in Parliament in February 2025 will be a key milestone for Sri Lanka's economic recovery, fiscal management, and long-term growth strategy. A well-received budget that aligns with the IMF's expectations will be vital for securing continued access to international financial assistance, which is particularly important as Sri Lanka continues its recovery.

The IMF's endorsement of the budget, which would potentially emphasize fiscal discipline to reduce the budget deficit, implementing structural reforms in taxation and governance, managing inflation through appropriate monetary policies, and ensuring social protection for vulnerable populations, will reassure investors and stakeholders. This will signal that Sri Lanka is on the right path to economic stability.

*Upcoming budget: crucial to adhere to IMF guidelines, IMF endorsement, would potentially emphasize on fiscal discipline*

Sri Lanka's economy is on the path to recovery following contractions in 2022 and 2023. The real GDP growth rebounded to 5.5% in the 3Q’24, after declining by 7.4% in 2022 and 2.2% in 2023. This recovery was primarily driven by an 11.1% increase in industrial growth, while services expanded by approximately 2.8%. The proposed salary hikes for government employees, savings from the PAYE tax system, reduced inflation, and low interest rates are expected to significantly boost consumption in Sri Lanka. Higher salaries will increase disposable income, while savings from PAYE will leave employees with more money to spend. Lower inflation will stabilize prices, making goods and services more affordable, and low interest rates will encourage borrowing for both consumption and business investment. Together, these factors will drive demand across various sectors, stimulate economic activity, and contribute to higher economic growth through a cycle of increased spending, business expansion, and job creation. ACS thus anticipate growth to reach 5.4%-5.5% in 2024 and continue with its trajectory in 2026E.

*Anticipated government salary hikes, savings from the PAYE, reduced inflation, low interest rates to boost consumption leading to >5% YoY GDP growth*

As of November 2024, Sri Lanka's inflation rate decreased to a deflation of 1.7% YOY, marking the lowest in nine years. We expect the inflation to be around mid single digits unless external factors such as global commodity price fluctuations, exchange rate volatility, supply chain disruptions, geopolitical risks, a potential global economic slowdown, could create significant risks to Sri Lanka's inflation outlook in 2025.

*Inflation to comfortably remain in desired mid single digit levels. AWPLR to remain relatively stable*

The Central Bank of Sri Lanka (CBSL) meanwhile set a new single policy rate at 8%, aiming to support economic recovery while also cutting down rates since Jun’23 by 775 bps. The introduction of an overnight policy rate (OPR) in our view would help markets more easily adjust to lower rates and help foster growth in our view where we expect AWPLR to remain relatively stable or even rise slightly in response to inflationary pressures. Private sector credit growth also should follow with 13%-15% growth in 2025E ( cf. 9.2% YoY growth as at Oct’24 )

The exchange rate may experience slight depreciation in 2025, primarily due to the relaxation of vehicle imports in February. If demand is not managed gradually, a surge in imports could potentially put pressure on LKR. Additionally, the import bill is expected to rise, with consumer demand increasing, which could widen the trade deficit to around USD 5.9Bn in 2025E. While there may be additional external debt servicing requirements due to the debt restructuring, we do not foresee undue pressure on the LKR, especially with the anticipated IMF 4th tranche of USD 333Mn expected in 1Q'25 which will further unlock multilateral support and generate foreign income through both equity and debt markets. Tourism and remittances are expected to support the trade deficit, with tourism potentially bringing in USD 4.2Bn, driven by over 2.8Mn tourists in 2025E. Remittances are expected to contribute more than USD 7.0Bn by then. Sri Lanka has also built foreign reserves, reaching around USD 6.4Bn by November 2024, well above the IMF's target for 2024. The Central Bank of Sri Lanka (CBSL) has been actively purchasing foreign currency, accumulating over USD 2.6Bn by November 2024, covering more than four months of imports and helping to stabilize the exchange rate.

*LKR may slightly depreciate in 2025 due to higher imports, but strong reserves of USD 6.4Bn, tourism (USD 4.2Bn), and remittances (USD 7.0Bn) should help stabilize it.*

On the fiscal front, the government is expected to continue adhering to IMF program parameters throughout 2025E to maintain access to financial support and stabilize the economy. The IMF guidelines emphasize debt sustainability, managing both external and domestic debt, and set ambitious targets, including raising the tax-to-GDP ratio to 15% by 2027E and reducing the budget deficit to 5% of GDP, while maintaining debt levels at 98.8% of GDP. Sri Lanka successfully increased its revenue by 34%YoY, reaching LKR 3.25Tn by January-October 2024, while reducing the deficit by 31%YoY to LKR 1.06Tn, aligning with the IMF's targets. We expect the new government to remain committed to these goals to ensure continued progress.

*Sri Lanka aims to sustain IMF-backed fiscal reforms, targeting a 15% tax-to-GDP ratio by 2027 and reducing debt, with revenue up 34% YoY in 2024 and the deficit down 31%.*

We anticipate the Colombo Stock Exchange (CSE) will benefit from reduced risk premiums following external debt restructuring and greater economic stability, leading to a convergence with emerging market valuations. The restructuring underscores strengthened fiscal discipline and improved access to concessional financing, contributing to an upgrade in the country's credit rating. As a result, we expect foreign investors to renew their focus on Sri Lanka, with foreign institutional investors—who have remained relatively inactive in recent years—likely to increase their allocations, signaling growing confidence in the market.

*Sri Lankan equities are poised for growth, driven by reduced risk premiums, credit rating upgrades, and renewed foreign investor interest, supported by global liquidity and easing US monetary policy.*

Global liquidity and risk appetite is expected to follow along with US's accommodative monetary policy, prompting investors to allocate capital to emerging markets. Sri Lankan equities could benefit from such conditions, as reduced global yields to draw foreign inflows into underweighted markets like Sri Lanka.

The CSE is poised to benefit further as improved local investor participation drives activity. Local investors are expected to return to equities due to low fixed income returns and compelling valuations, with the CSE still trading below 10x earnings. This shift is supported by a favorable economic outlook, characterized by record-low inflation and reduced political uncertainties. Additionally, tax exemptions on capital gains enhance the appeal, fostering greater local participation and bolstering market momentum in our view.

*The CSE is set to gain from increased local investor participation, driven by low fixed income returns, attractive valuations below 10x earnings, and tax exemptions on capital gains amid a stable economic outlook.*

We anticipate that lower inflation, stable exchange rates, rising consumer demand, and low interest rates to significantly boost corporate profitability, particularly in consumer-focused and import-driven sectors. The ongoing economic recovery is expected to create broad-based benefits across industries, with some sectors standing out for their potential to outperform.

In the banking sector, profitability is likely to surge due to provision reversals, a more favorable economic environment, increased loan disbursements, and improved loan quality, reflected in lower non-performing loan (NPL) ratios. The finance sector is set to gain from the relaxation of vehicle import restrictions, which is expected to stimulate demand in ancillary industries such as lubricants, spare parts, and energy.

The tourism and leisure sector stands to benefit from a rise in tourist arrivals, driven by improved global travel sentiment and Sri Lanka's enhanced appeal as a destination. Concurrently, the construction sector is poised for recovery, supported by improved private sector credit growth from low interest rates and bolstered by fresh investments from both government initiatives and foreign direct investments (FDIs).

Increased domestic demand is expected to drive growth in manufacturing and consumer goods, while a potential easing of global monetary policies could further enhance export demand, providing a significant boost to export-oriented businesses.

*Key areas like Banking, Finance, Leisure, consumer, Manufacturing , Diversified segments to benefit*

# 2025, Building Momentum for Sustained Growth

ASPI is expected to reach 19,300, with a PE ratio of 12-12.5x, driven by earnings growth of 15-20%.

Diversified conglomerates are well-positioned to capitalize on these trends, benefiting from robust local and international demand. Additionally, improved import volumes are likely to support growth in ports and shipping, further fueling economic activity and enhancing overall demand across multiple sectors.

**This combination of sector-specific drivers and a broader economic recovery highlights the potential for sustained growth and value creation in Sri Lanka's equity market, with earnings projected to grow by at least 15%-20% YoY in 2025E.**

**Sri Lankan equities are attractively valued, trading below 10x earnings. With anticipated earnings growth of 15%-20% in 2025E and a valuation re-rating to 12.0x-12.5x, we project the ASPI to surpass 19,300 in 2025E, delivering over 20% upside and outperforming fixed-income and other asset classes.**

*With anticipated earnings growth of 15%-20% in 2025E and a valuation re-rating to 12.0x-12.5x, we project the ASPI to surpass 19,300 in 2025E, delivering over 20% upside*

# Market Valuations & Returns

# Equities to grow amid stable economy

Economic growth backed by political stability, low rates and higher disposable income to play key roles in driving the equity market



- Political stability plays a crucial role in fostering investor confidence, as it reduces uncertainty and promotes a favorable environment for economic growth. As Sri Lanka stands on the brink of economic recovery, its equity markets are poised to benefit significantly with recovery in overall demand conditions improving.

- Interest rates are moving down resulting in shift to equities

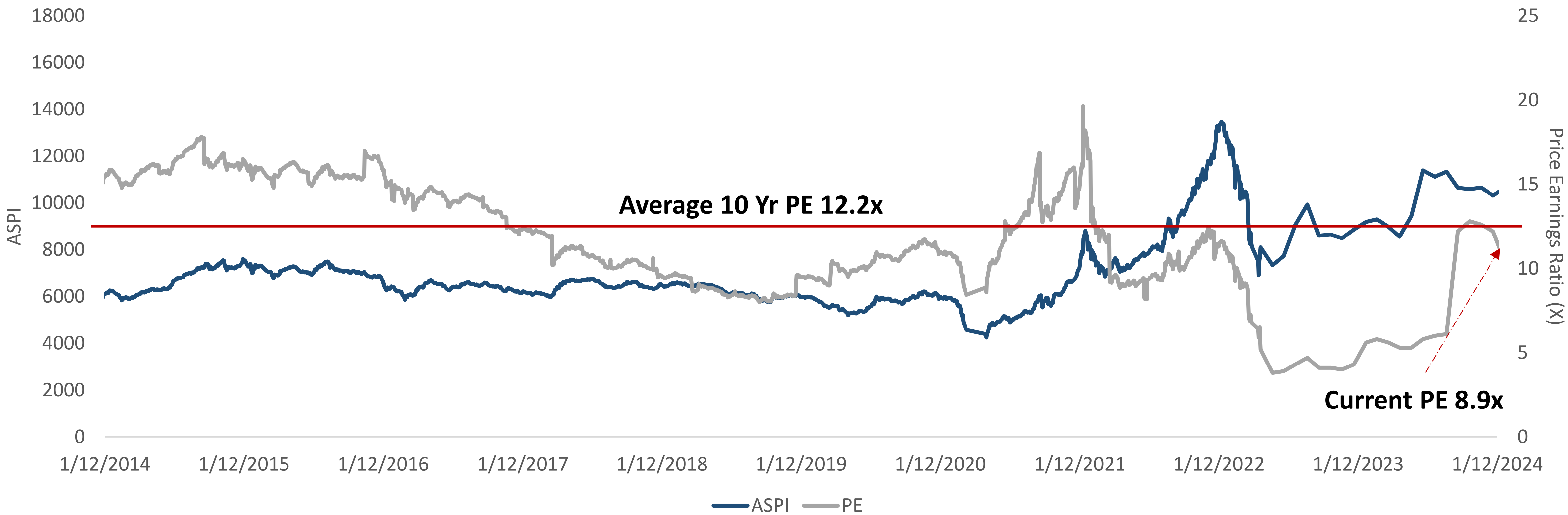
- Inflation is at low levels leading to higher disposable income and loose monetary policy stance

- Minimal level of uncertainties in the horizon specially with the monetary and fiscal policies

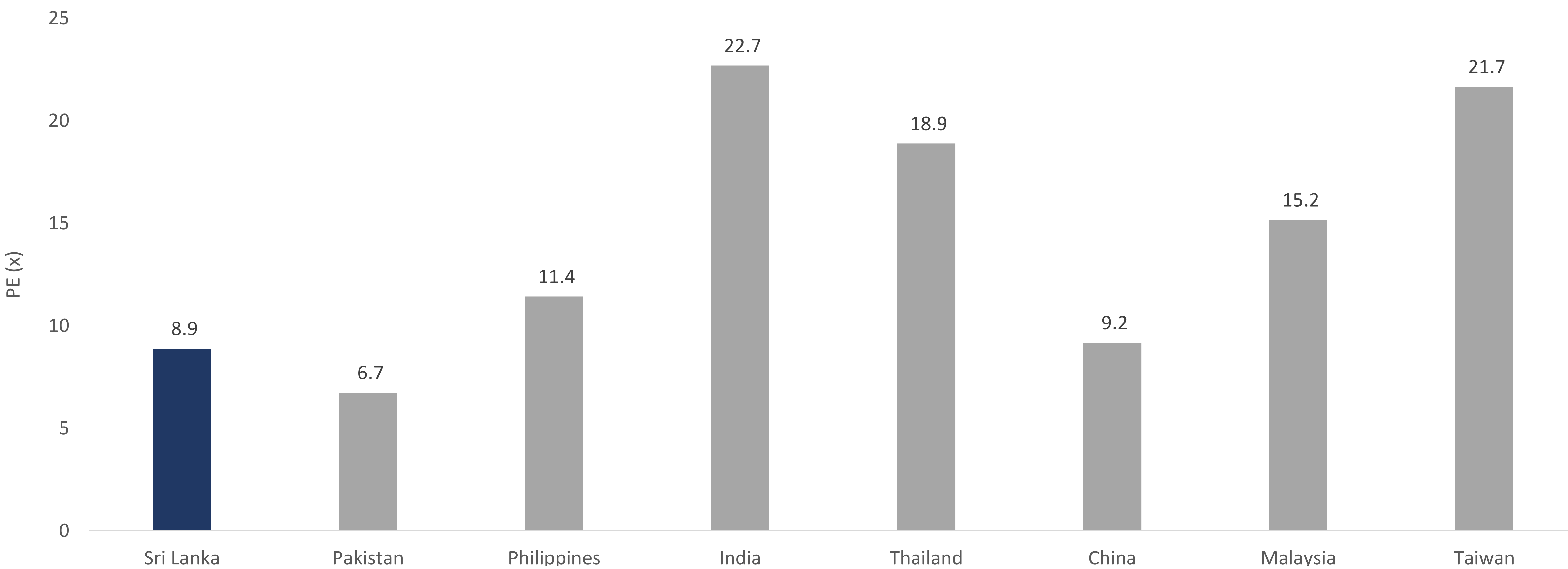
- Valuations are at low levels where it's indicating a BUY signal

- Taxes are in favour of equities with capital gains not been taxed

*Sri Lanka still trades at a significant 27% discount to 10 Yr average PE of 12.2x*

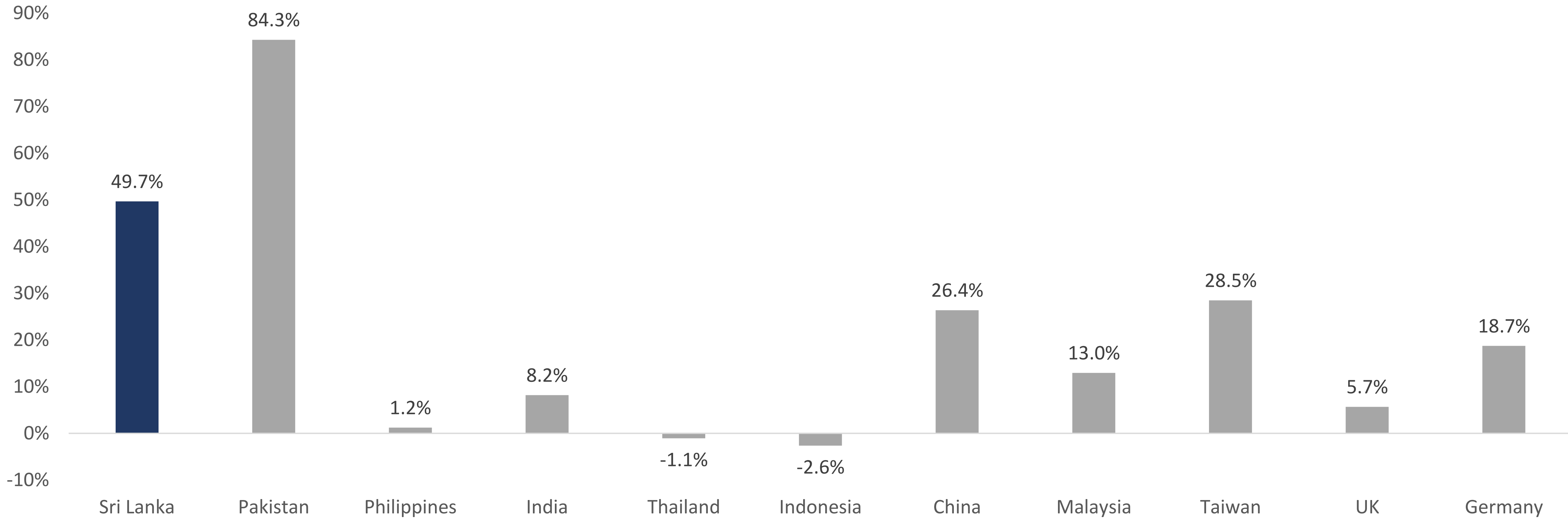



*Sri Lanka is still cheaper than most of its regional peers, trading at a 61% discount to India, a 59% to Taiwan and 53% discount to Thailand*

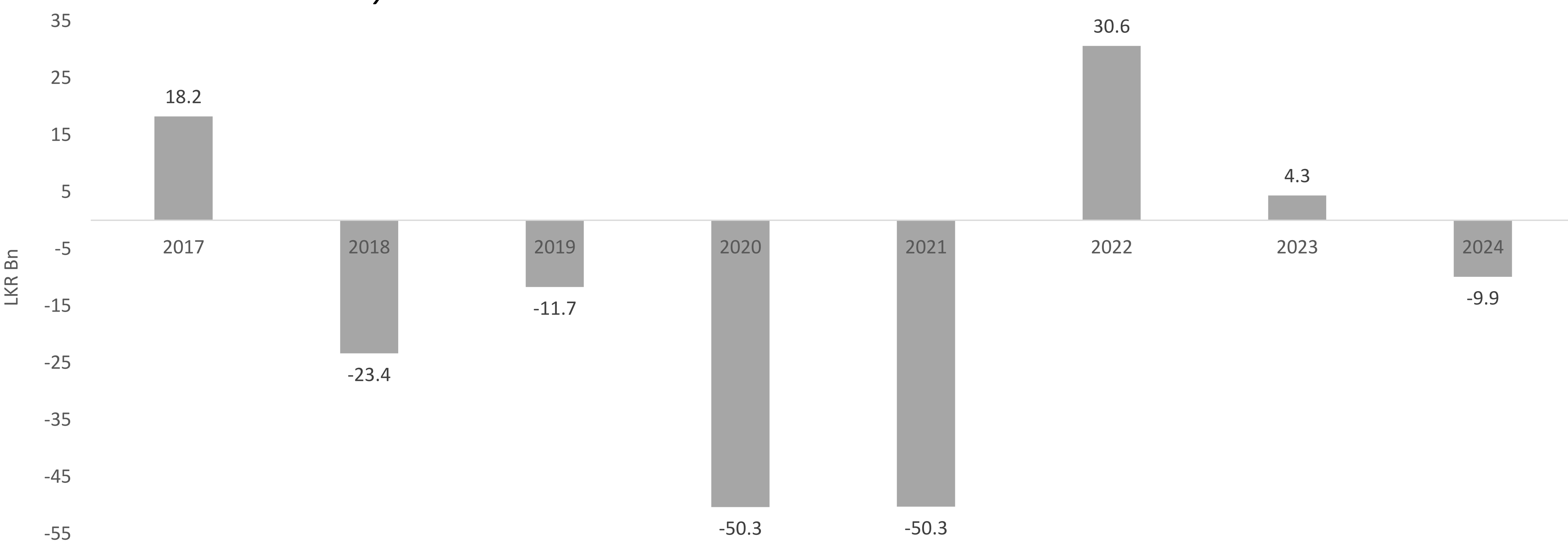



*Source : CSE, CBSL, Bloomberg, ACS Research*

## *Sri Lanka records an impressive return of 49.7% for the year 2024*




## *Foreign participation in the CSE to gradually pick up, buoyed by improved investor sentiment stemming from both political & economic stability*

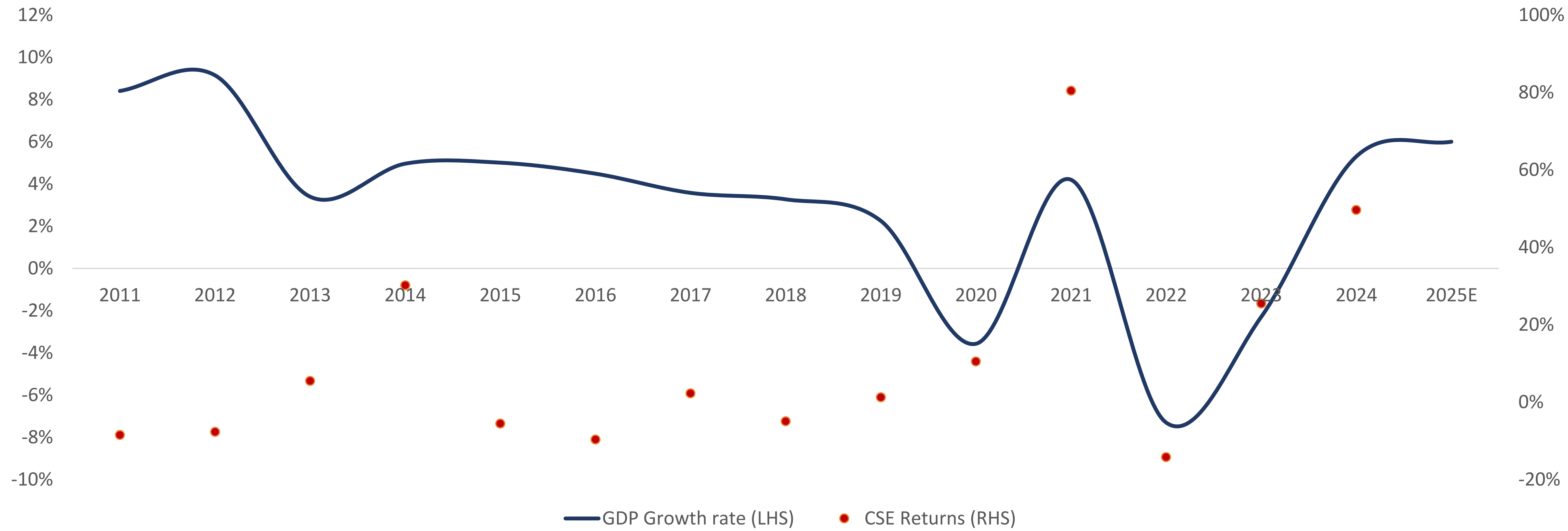


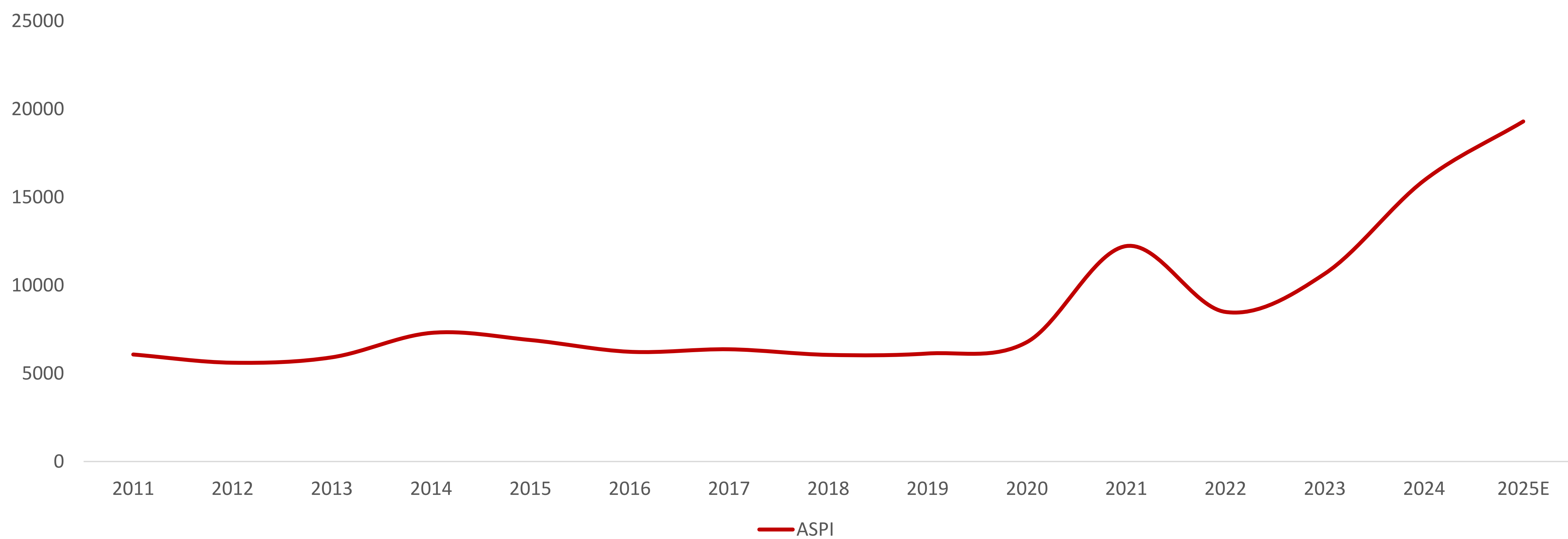

*Source : CSE, Bloomberg, ACS Research*

# As the economy grows equity markets tend to follow suit

Markets to continue with its growth trajectory

*We therefore anticipate the market to trade at 12x-1.2.5x P/E (from the current 9x) within the next year, driven by potential earnings growth spurred by economic recovery and increased investor confidence.*



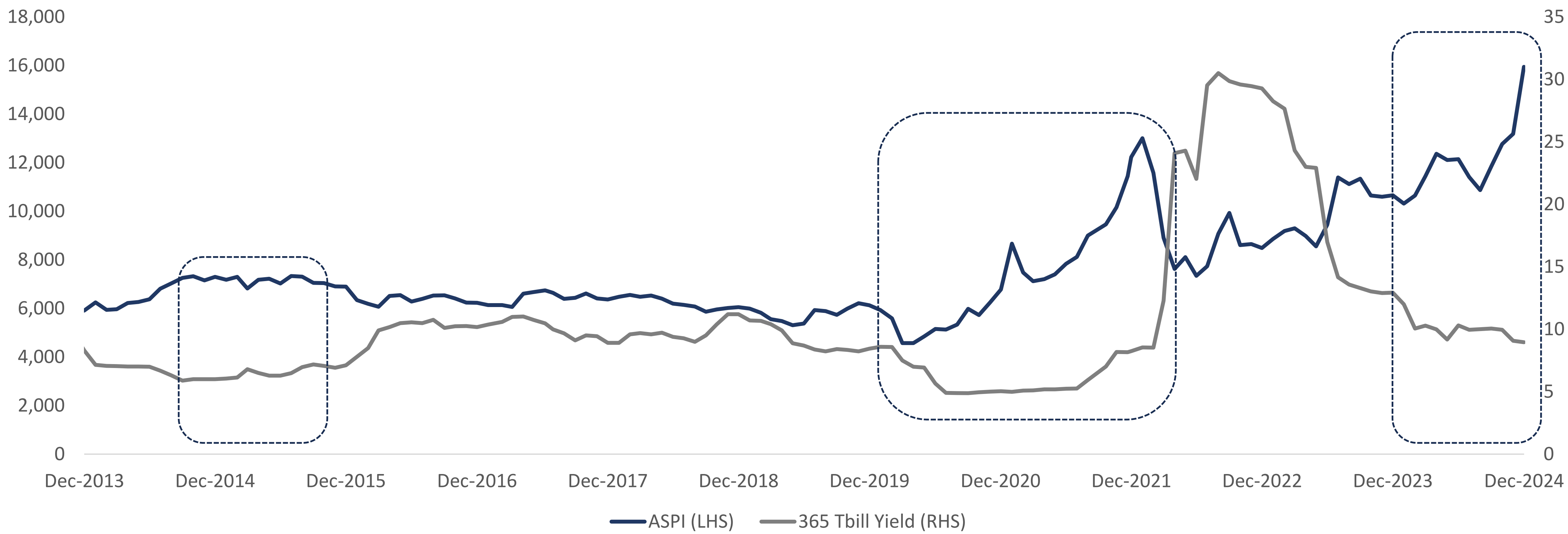

*Source : CSE, CBSL, ACS Research*

# Equities has an inward relationship with interest rates

Sri Lanka taxes are in favor of equities



*The reduction in T-bill rates to single digits, provide impetus to allocate funds from fixed income to equities*




*The ASPI's 50% return in 2024, positions CSE as the leading performer, delivering attractive tax-exempt returns to investors.*

| Investment | Return | Effective Return | Tax |
|---|---|---|---|
| Equity | 50% | 50% | 0% Tax on Capital Gains (15% Withholding Tax on Dividends) |
| 6 Month T Bill Rate | 8.77% | 5.61% | 36% Tax on interest income |
| 3-year T Bond Rate | 10.42% | 6.67% | 36% Tax on interest income |
| Fixed Deposits | 7.5% | 4.32% | 10% Withholding Tax, Interest income liable for income tax |
| Real Estate Price Index | 14% | 12.6% | 10% Tax on capital gain |

*Source : CSE, CBSL, ACS Research*

# Earnings

*Corporate earnings maintain steady growth amid improved macroeconomic conditions*

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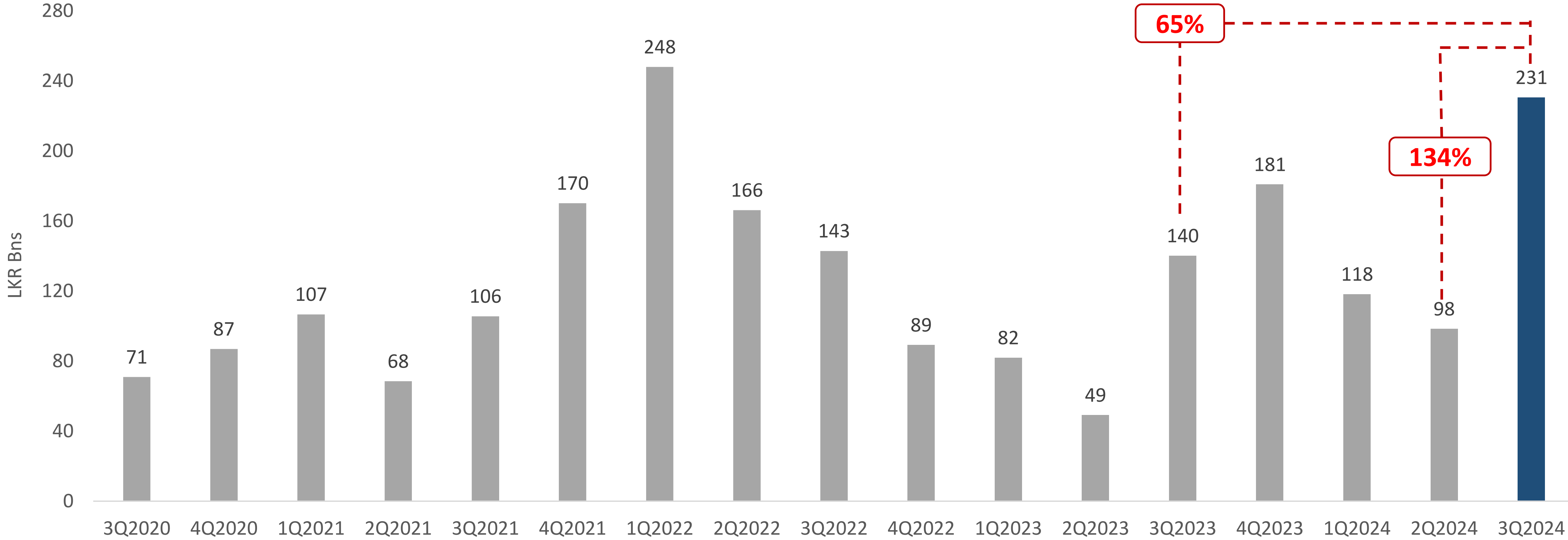
*Corporate earnings rebounded strongly in 3Q'24, with profits surging over 1.5x YoY & doubling QoQ*




*Food, Bev & Tobacco, Diversified Financials, Capital Goods and Banks contributed to significant portion of earnings*


*Source : CSE, Company Reports, ACS Research*

# Earnings are on an upward swing

Enhanced profit margins set to drive higher dividend payouts

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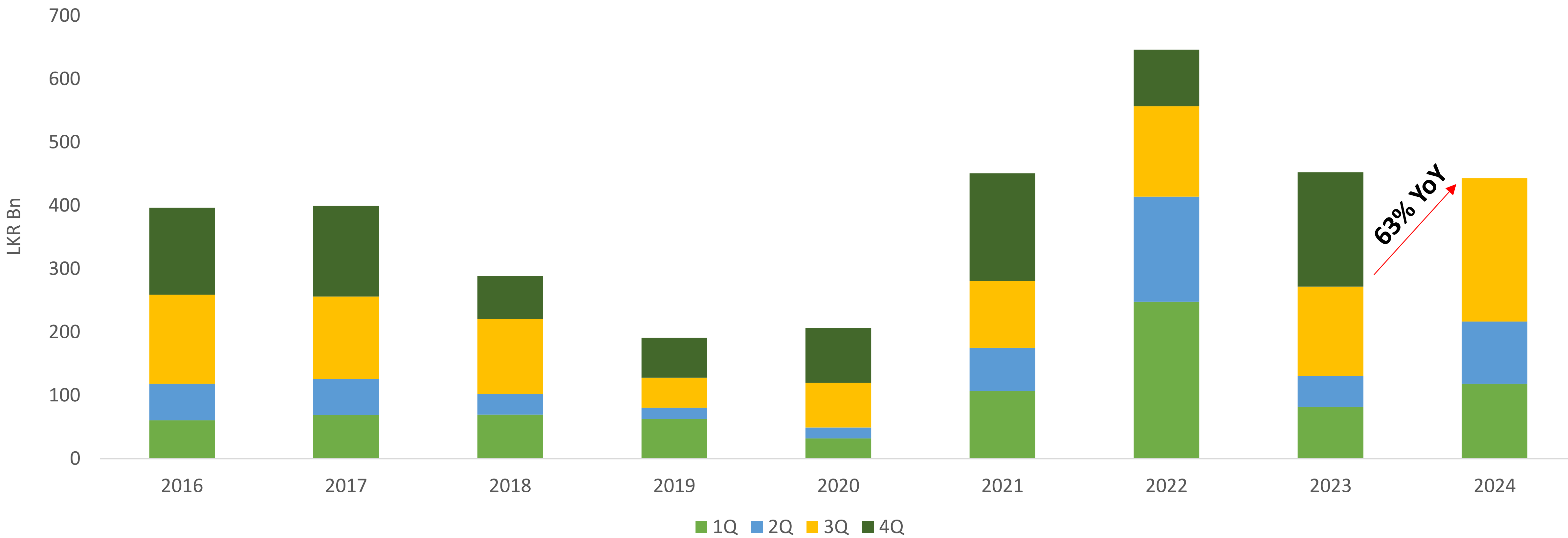
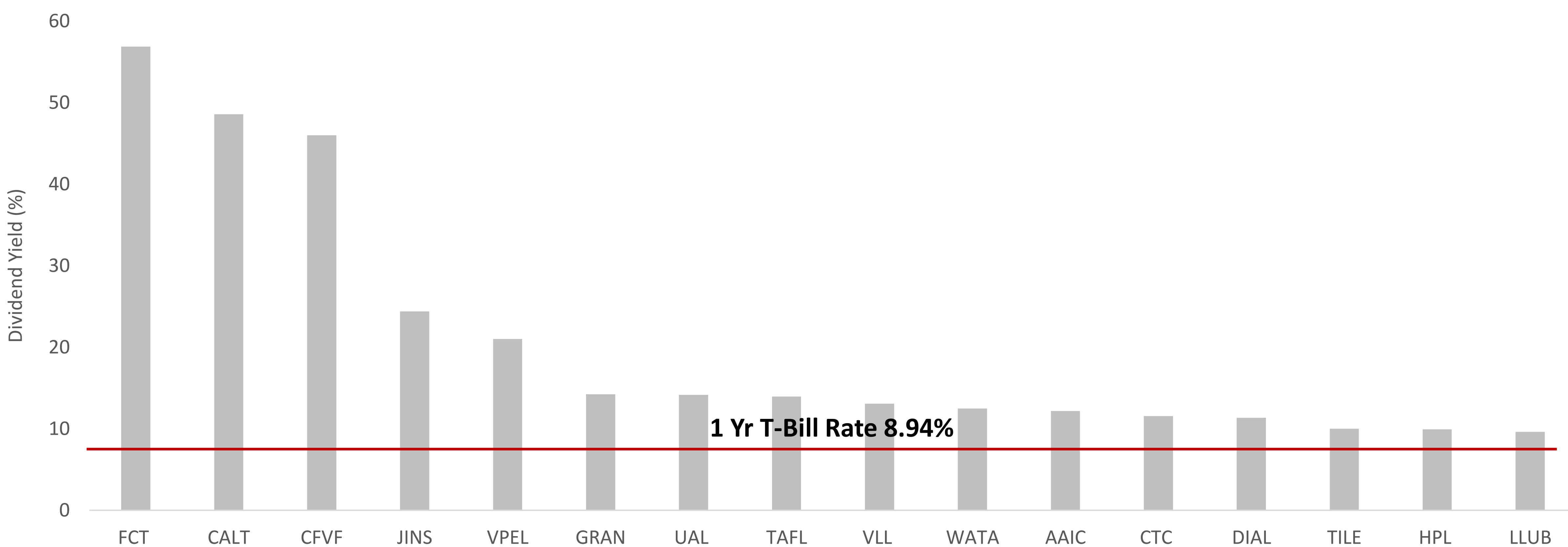
Member of the Colombo Stock Exchange

*Earnings for 9M'24 have already surged by 63%YoY, led by lower finance cost, higher demand and low provisions*




*Majority of companies are offering higher dividend yields, exceeding the returns on govt securities*



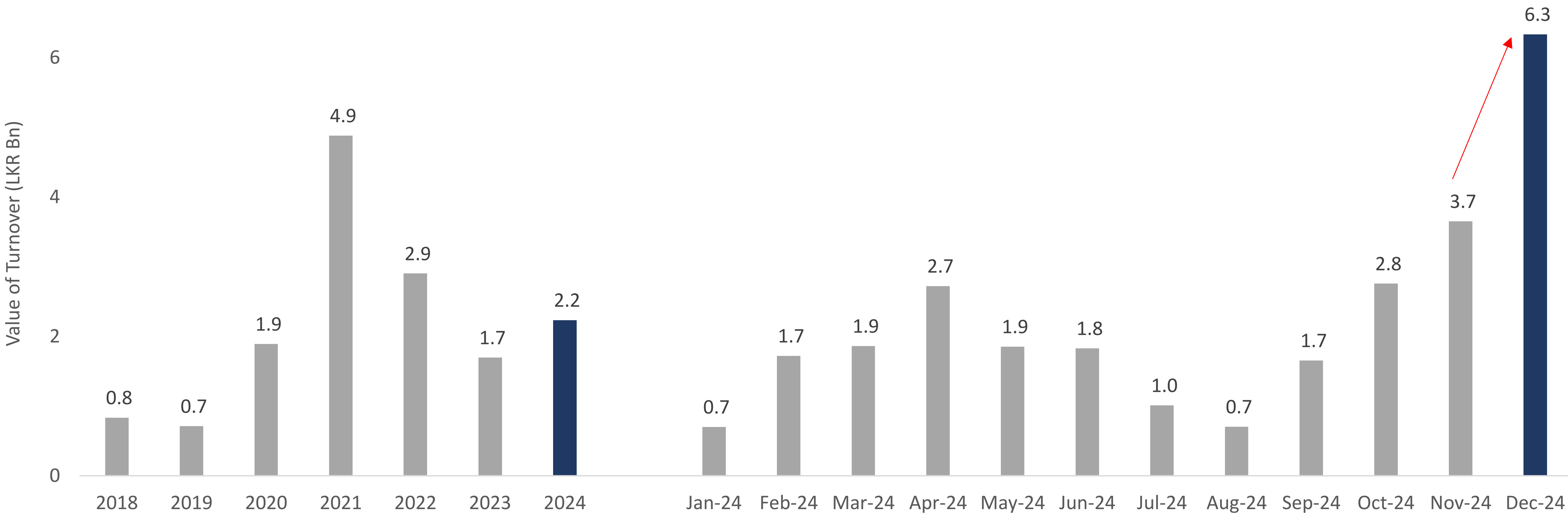

*Source : CSE, CBSL, Company Reports, ACS Research*

# Turnover levels have improved

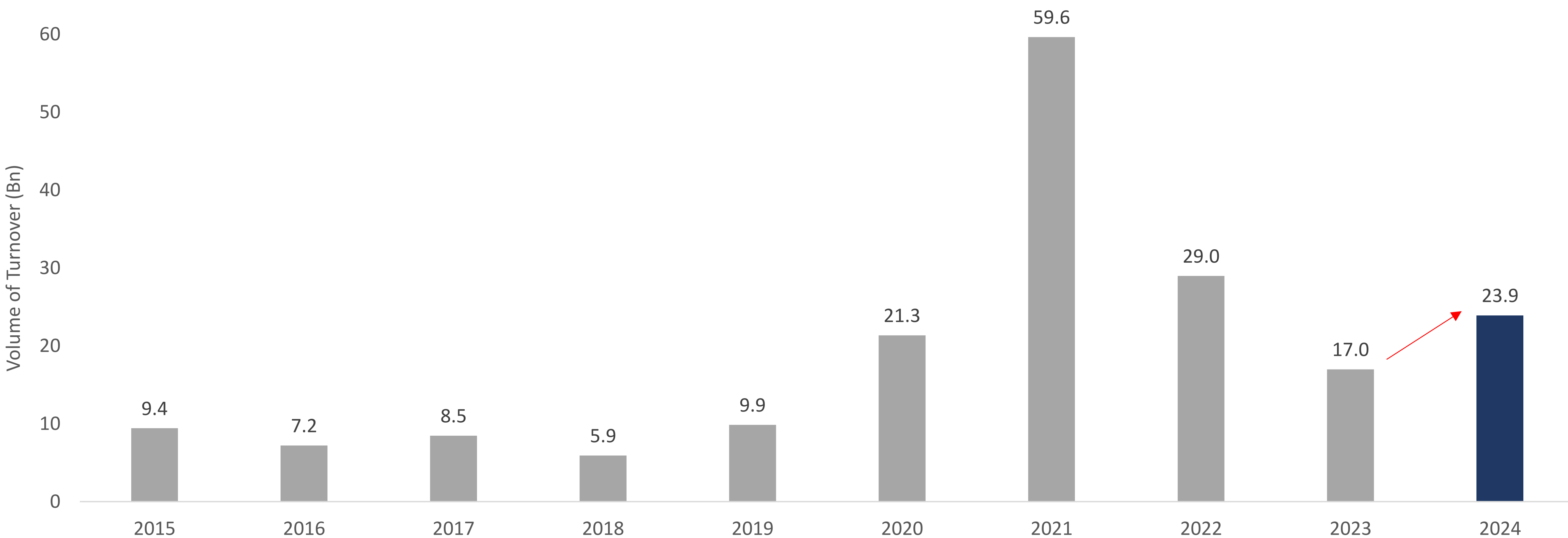
*Country rerating, lower rates, higher retail and HNI participation to drive up market activities in 2025*



*Avg daily turnover level improved by 32%YoY to LKR 2.2Bn in 2024, with 4A'24 leading monthly turnover*




*Volume also shows an uptick in tandem with turnover levels*




*Source : CSE, ACS Research*

# Year end roundup

Sri Lanka's equity market ended 2024 on a high note, with the main share price index recording an impressive gain of 49.7%, while the more liquid S&P SL 20 surged by 58.5% to close the year at 4,862.1. This remarkable rally was primarily concentrated in the 4Q'24, during which the market rose by over 34% compared to the end of 3Q'24. For much of the year, performance had been subdued due to uncertainties surrounding debt restructuring and political stability. However, a series of positive developments in the latter part of the year significantly boosted investor confidence.

*Sri Lanka ended on a high note with ASPI recording a 49.7% return*

Key among these developments was the successful completion of Sri Lanka's debt restructuring process in a record timeframe, which was followed by an upgrade in the country's credit rating by international rating agencies. Political stability also played a crucial role, with the current government securing a landslide victory, fostering optimism about the nation's governance and economic trajectory. Additionally, macroeconomic indicators such as interest rates and inflation plummeted to more favorable levels, signaling a brighter economic outlook for the country.

*Completion of debt restructuring, political stability, credit rating upgrades and broader macro economic stability drove the market up*

Corporate earnings further supported the market's upward trajectory. For the nine months ending September 2024, profits surged by a notable 63%YoY, driven by increasing demand, lower price levels, reduced financing costs, and an improved macroeconomic environment that benefited company cost structures. Banks also reported lower provisioning levels, contributing positively to overall profitability. Global stability in commodity prices enhanced corporate margins, while adjustments in domestic fuel and electricity prices reduced operational expenses. These factors collectively resulted in robust earnings across sectors, with the market ending the year at less than 10x earnings.

*Corporate earnings followed suit with 12M trailing profits surging by 73%YoY*

# Year End Round Up

*Trading activities too spiked up to LKR 4.0Bn in 4Q'24 due to favorable macro factors*

Trading activity also experienced a significant boost in the 4Q'24. Average daily turnover levels surged to over LKR 4 Bn, compared to approximately LKR 1.5 Bn earlier in the year. This increase was primarily fueled by heightened investor sentiment, particularly among local and institutional investors. Despite this, foreign investors ended the year as net sellers, offloading nearly LKR 10Bn worth of equities. This trend was largely driven by lingering uncertainties earlier in the year, prompting foreign investors to exit the market. However, this dynamic is expected to shift as Sri Lanka emerges from its bankruptcy phase, with the country's underweight status and improving economic conditions likely to attract renewed foreign interest.

*Average daily turnover levels spiked to LKR4.0Bn in 4Q'24 from LKR 1.5Bn from 1-3Q'24*

Looking ahead, the outlook for Sri Lanka's equity market appears promising. The combination of political stability, favorable macroeconomic indicators, and strong corporate earnings creates a solid foundation for sustained growth. As global portfolios adjust to include underweight markets like Sri Lanka, the potential for increased foreign inflows and broader market participation could further bolster the market's performance in 2025.

*Equity market outlook remains promising underpinned by favourable macro indicators, strong corporate earnings, increased foreign inflows, political stability etc.*

Sri Lankan equities are attractively valued, trading below 10x earnings. With anticipated earnings growth of 15%-20% in 2025E and a valuation re-rating to 12.0x-12.5x, we project the ASPI to surpass 19,300 in 2025E, delivering over 20% upside and outperforming fixed-income and other asset classes.

# Bourse exhibits an exceptional growth in 4Q'24, advancing by 35%

*Markets ended 2024 with a 49.7% return*

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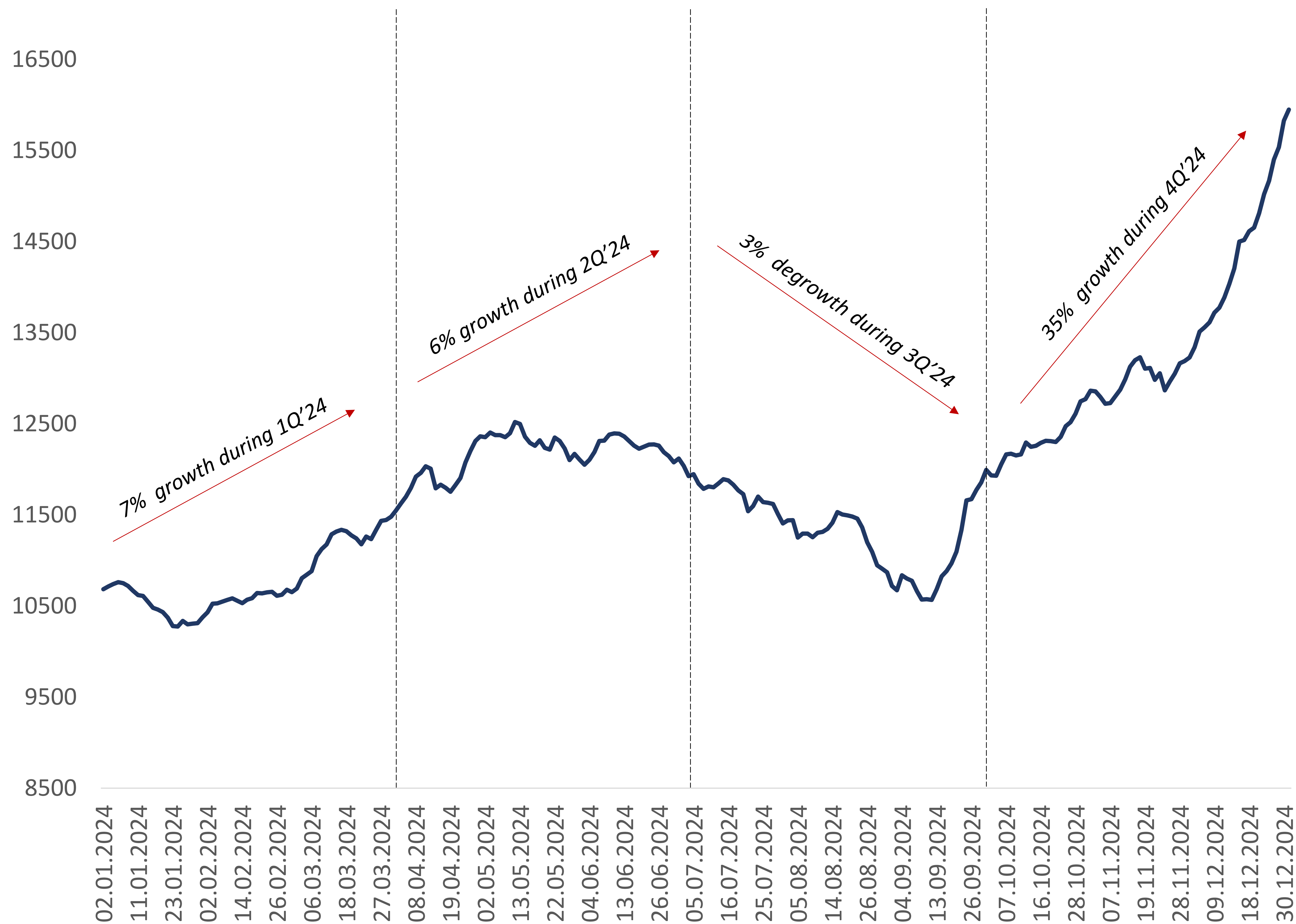
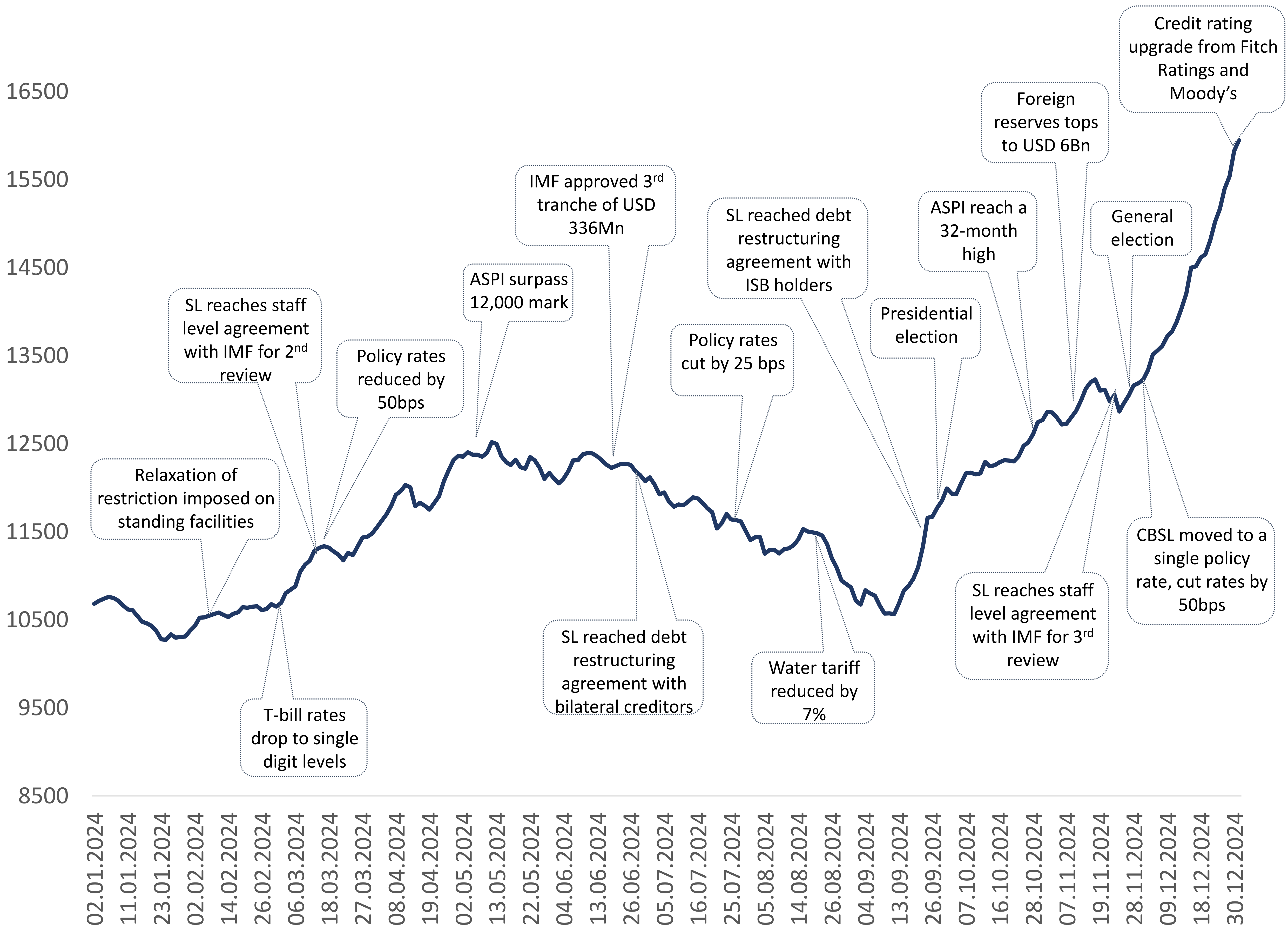



*Source : CSE, ACS Research*

# Significant events that took place in 2024

*Successful debt negotiations coupled with political & economic stability contributed heavily on the market growth*



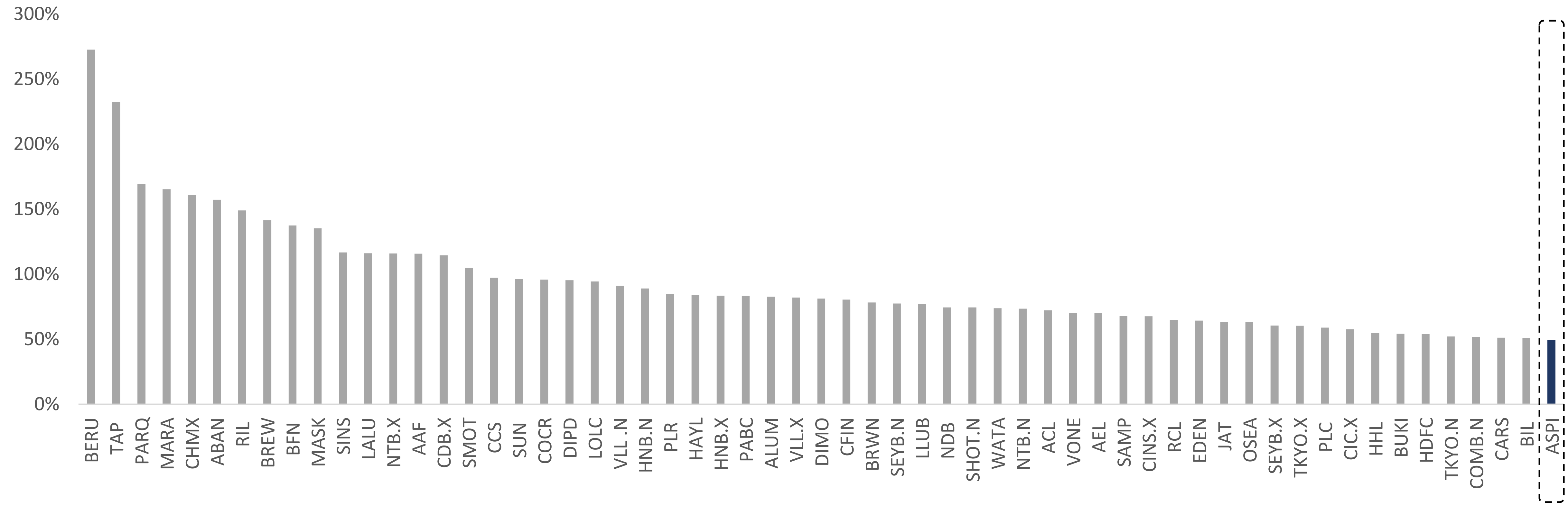

*Source : CSE, ACS Research*

# 34% of the counters have exceeded market returns in 2024

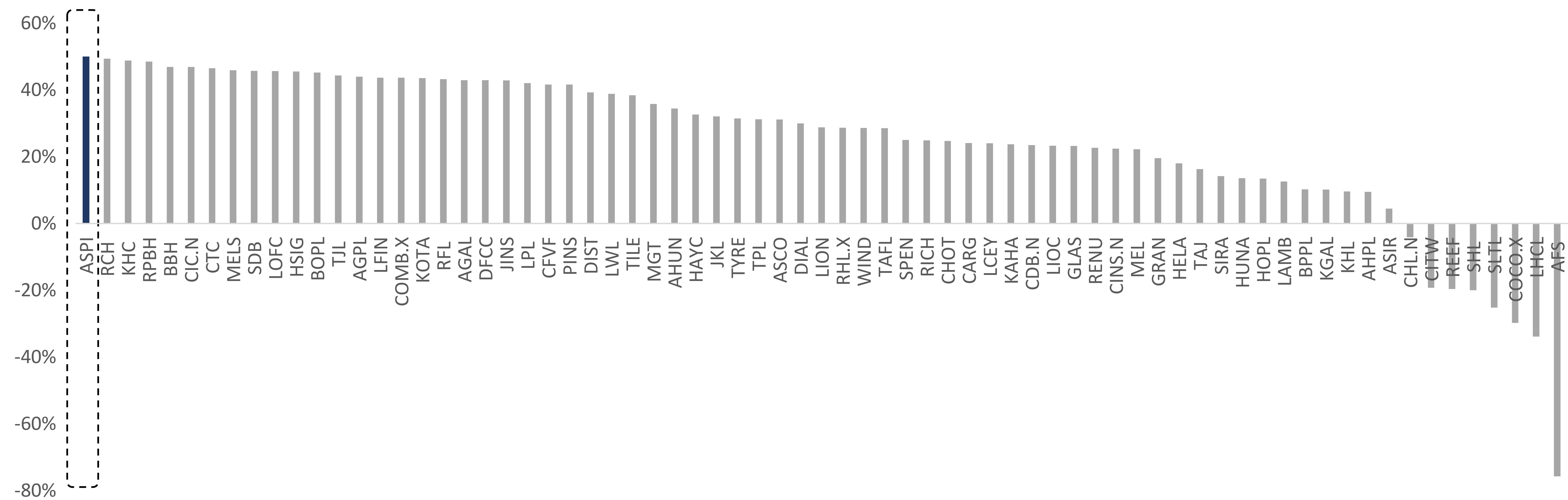
*There are many fundamentally strong counters which still has value*



*Counters that outperformed ASPI*




*Counters that underperformed ASPI*




*Source : CSE, ACS Research*

# ASPI reaches an all-time high in 2024

*Undervalued markets poised to continue its winning streak in tandem with growing economy*



| | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | 2024 |
|---|---|---|---|---|---|---|---|---|---|
| **ASPI (Year End)** | **6228.3** | **6369.3** | **6052.4** | **6129.2** | **6774.2** | **12226.0** | **8489.7** | **10654.2** | **15944.6** |
| ASPI Return (%) | *-9.7%* | *2.3%* | *-5.0%* | *1.3%* | *10.5%* | *80.5%* | *-30.6%* | *25.5%* | *49.7%* |
| S&P SL20 | 3496.4 | 3671.7 | 3135.2 | 2937.0 | 2638.1 | 4233.3 | 2635.6 | 3068.4 | 4862.1 |
| S&P SL20 Return (%) | *-3.6%* | *5.0%* | *-14.6%* | *-6.3%* | *-10.2%* | *60.5%* | *-37.7%* | *16.4%* | *58.5%* |
| Average Daily Turnover (LKR Mn) | 737 | 915 | 834 | 711 | 1899 | 4888 | 2972 | 1697 | 2240 |
| *YoY Growth* | *-30%* | *24%* | *-9%* | *-15%* | *167%* | *157%* | *-39%* | *-43%* | *32%* |
| *Avg USD =LKR* | *145.6* | *152.5* | *162.5* | *178.8* | *185.4* | *203.0* | *371.6* | *328.8* | *292.6* |
| Average Daily Turnover (USD Mn) | 5.1 | 6.0 | 5.1 | 4.0 | 10.2 | 24.1 | 8.0 | 5.2 | 7.7 |
| Foreign Purchases ( LKR Mn) | 74,583 | 113,276 | 76,621 | 56,649 | 53,901 | 34,085 | 67,508 | 41,471 | 49,797 |
| Foreign Sales (LKR Mn) | 74,199 | 95,052 | 99,979 | 68,366 | 104,233 | 86,687 | 36,906 | 37,124 | 59,722 |
| **Net Foreign flows (LKR Mn)** | **384** | **18,224** | **(23,358)** | **(11,717)** | **(50,332)** | **(50,284)** | **30,601** | **4,348** | **(9,925)** |
| Foreign Purchases ( USD Mn) | 512 | 743 | 471 | 317 | 291 | 168 | 182 | 126 | 170 |
| Foreign Sales (USD Mn) | 510 | 623 | 615 | 382 | 562 | 427 | 99 | 113 | 204 |
| **Net Foreign Flows (USD Mn)** | **3** | **119** | **(144)** | **(66)** | **(271)** | **(248)** | **82** | **13.2** | **(33.9)** |
| **Market Cap ( LKR Bn)** | **2,745** | **2,899** | **2,839** | **2,851** | **2,959** | **5,489** | **3,888** | **4,249** | **5,696** |
| **Market Cap ( USD Mn)** | **18,856** | **19,010** | **17,469** | **15,944** | **15,959** | **27,039** | **10,463** | **12,924** | **19,467** |
| **CSE - PER (Year End)** | **12.4** | **10.7** | **9.7** | **11.5** | **15.2** | **13.6** | **5.0** | **11.1** | **8.9** |

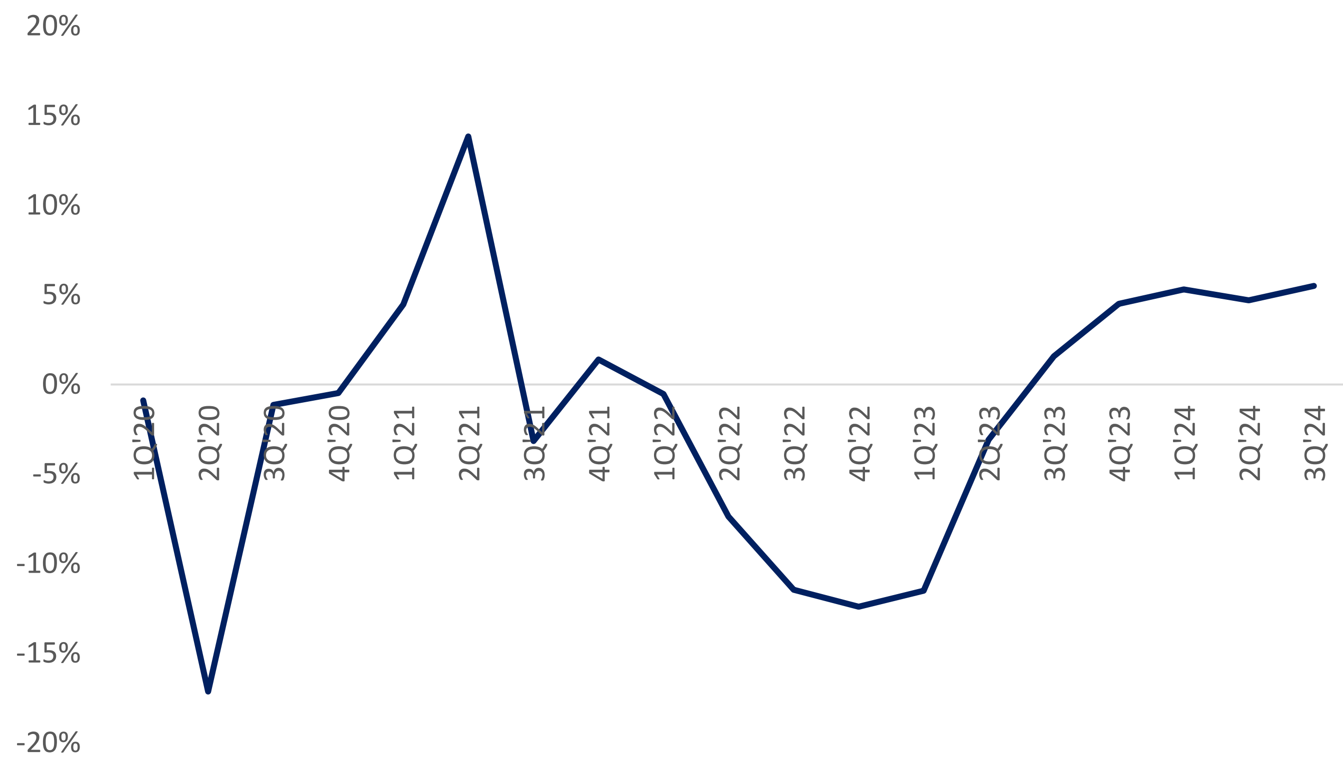
*Source : CSE, ACS Research*

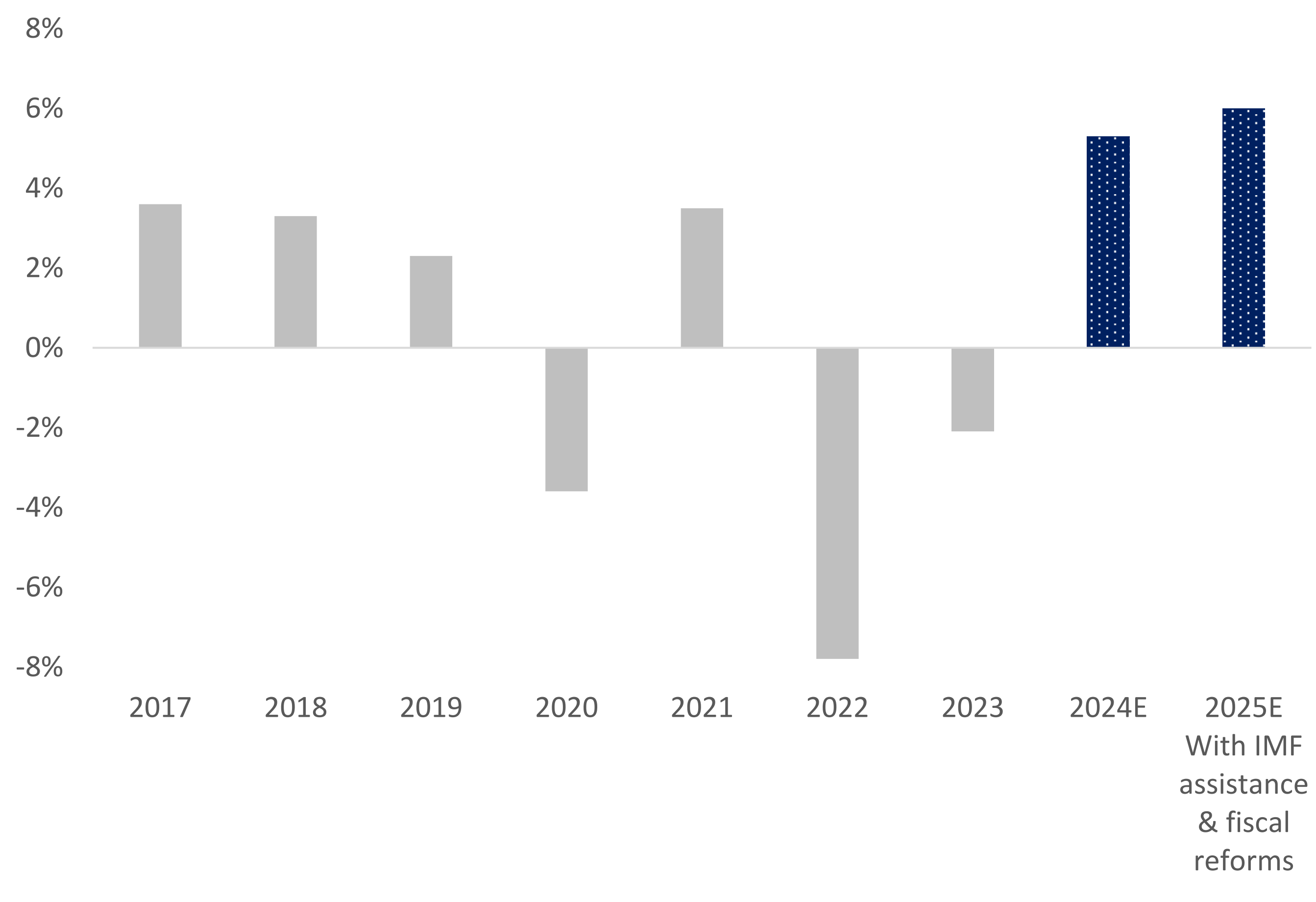
# Economic Outlook

# SL economy grew by 5.2% in 9M’24

*Lower interest rates and strong external sector to drive up GDP. Growth momentum to continue*






- The Sri Lankan economy demonstrated a commendable growth of 5.5%YoY in 3Q’24, marking its fifth consecutive quarter of expansion, which propelled the GDP growth for the first 9M’24 to 5.2%YoY. The agricultural sector recorded a modest growth of 1.9%YoY, while the industrial sector saw a robust expansion of 11.2%YoY during the 9M’24. The services sector, which constitutes the largest share of the GDP (58%), grew by 2.6%YoY for 9M’24.
- A notable decline in interest rates, with the AWPLR falling by 250 basis points to 9.10%, facilitated an easing of domestic credit availability, particularly benefitting the private sector. Concurrently, the rise in imports of investment and intermediate goods, such as textiles and cement, significantly contributed to the record growth in the apparel and construction industries, which expanded by 9.4% YoY and 17.8% YoY, respectively, for 9M’24. Furthermore, increased earnings from tourism and remittances from workers bolstered the nation’s foreign exchange reserves, strengthening the rupee’s value in the foreign currency markets.
- We anticipate that the upward trajectory will persist, particularly with the continued implementation of the reforms stipulated in the agreement with the IMF. Further, the government's emphasis on fiscal discipline, streamlining state expenditures, improving revenue generation, and reducing reliance on debt play a crucial role in stabilizing the economy. Additionally, with inflation stabilizing and the reduction in personal income taxes, disposable income is expected to rise, thereby boosting domestic demand for goods and services

*Source : Department of Census & Statistics, ACS Research*

# Export income jumped by 7%YoY during Jan-Nov'24

*Export income to touch USD 14Bn in 2025E, while relaxation of vehicle imports likely to widen trade deficit*

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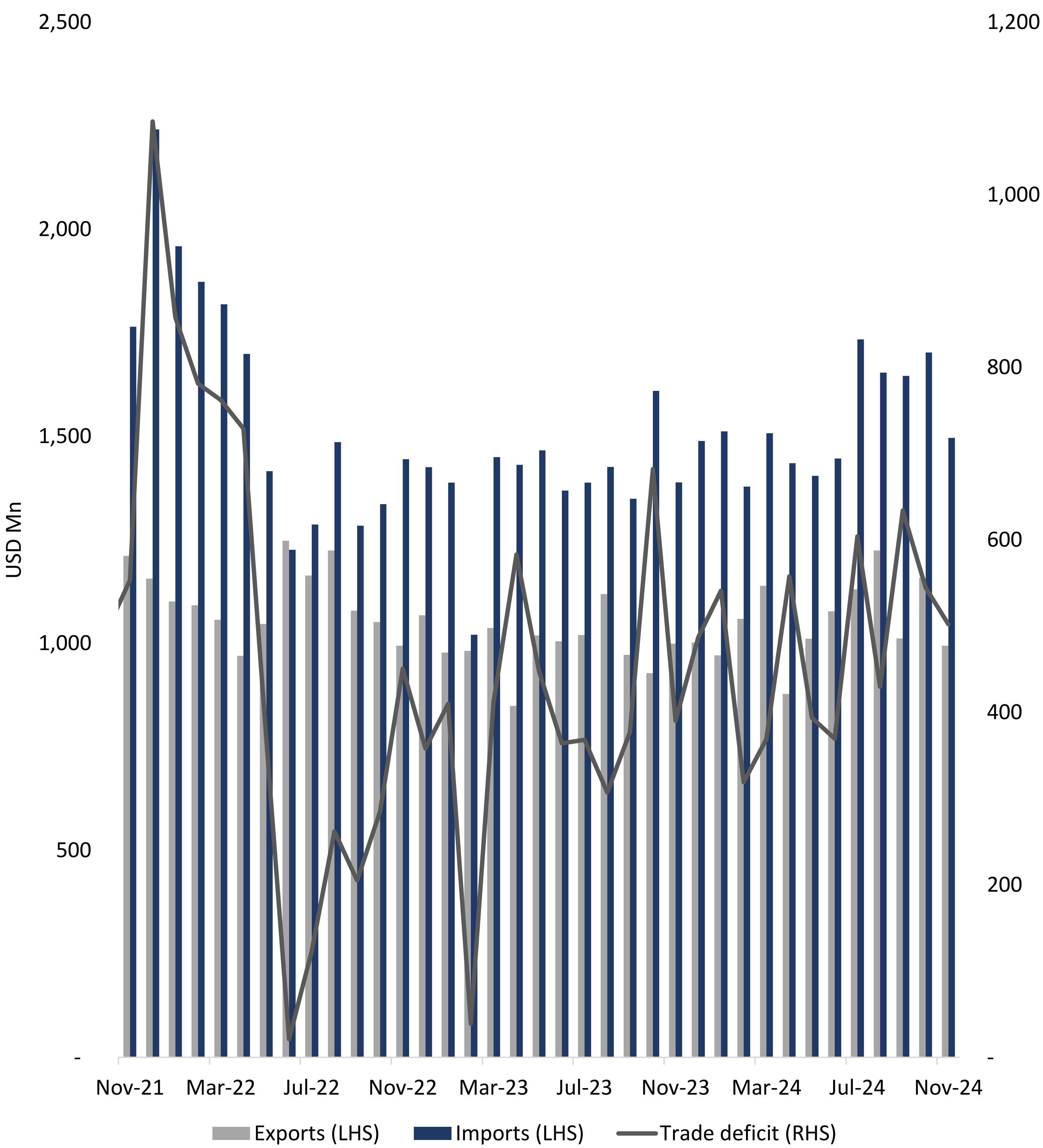



- During Jan-Nov'24, cumulative export income grew by 7%YoY to USD 11.7Bn while cumulative imports also surged by 10%YoY to USD 16.9Bn. Consequently, the cumulative trade deficit widened by 19%YoY to USD 5.2Bn during the same period.
- Meanwhile, industrial exports soared by 7.3%YoY to USD 9.1Bn, primarily driven by the increase in textile and garments exports by 3.9%YoY to USD 4.6Bn (constituted half of industrial exports) and substantial surge in petroleum products exports by 104%YoY to USD 975.5Mn. Further, agricultural exports also grew by 6.7%YoY to USD 2.5Bn, mainly led by 8.8%YoY increase in tea exports to USD 1.3Bn.
- On the other hand, intermediate goods imports surged by 7.3%YoY to USD 10.8Bn (led by textiles and textile articles) and investment goods imports increased by 23.2%YoY to USD 3.1Bn (driven by machinery and building material).
- We estimate export income to hover around USD 14Bn for 2025E, largely driven by a boost in orders in the apparel sector, particularly from Europe and from the US, where potential Fed rate cuts may spur demand. However, Import expenses should expand (6%-7%) to around USD 19.8Bn, due to relaxed vehicle import restrictions, lower global commodity prices, and stronger consumer demand in a low-inflation, low-interest-rate environment.

*Source : CBSL, ACS Research*

# External sector performance in a nutshell

*Cumulative Imports bill on fuel plummeted by 9%YoY, while textile and garments exports grew by 4%YoY during Jan-Nov'24*



| USD Mn | Nov'23 | Nov'24 | Variance | Jan - Nov 2023 | Jan - Nov 2024 | Variance | Contribution to Exports |
|---|---|---|---|---|---|---|---|
| **Total Exports** | **999** | **994** | ***0%*** | **10,909** | **11,670** | ***7%*** | |
| **Industrial Exports** | 766 | 763 | *0%* | 8,487 | 9,105 | *7%* | 78% |
| Textiles and garments | 396 | 398 | *0%* | 4,439 | 4,613 | *4%* | 40% |
| Rubber Products | 77 | 75 | *-3%* | 824 | 897 | *9%* | 8% |
| **Agricultural Exports** | 215 | 228 | *6%* | 2,360 | 2,518 | *7%* | 22% |
| Tea | 113 | 118 | *5%* | 1,199 | 1,304 | *9%* | 11% |

| USD Mn | Nov'23 | Nov'24 | Variance | Jan - Nov 2023 | Jan - Nov 2024 | Variance | Contribution to Imports |
|---|---|---|---|---|---|---|---|
| **Total Imports** | **1,389** | **1,497** | ***8%*** | **15,323** | **16,917** | ***10%*** | |
| **Consumer Goods** | 265 | 320 | *21%* | 2,771 | 3,068 | *11%* | 18% |
| Food and beverages | 133 | 164 | *23%* | 1,541 | 1,672 | *8%* | 10% |
| **Non-food consumer goods** | 132 | 156 | *18%* | 1,230 | 1,396 | *14%* | 8% |
| Medical and pharmaceuticals | 57 | 58 | *2%* | 620 | 515 | *-17%* | 3% |
| **Intermediate goods** | 868 | 920 | *6%* | 10,058 | 10,790 | *7%* | 64% |
| Fuel | 317 | 311 | *-2%* | 4,289 | 3,920 | *-9%* | 23% |
| Textiles and textile articles | 203 | 242 | *19%* | 2,188 | 2,595 | *19%* | 15% |
| **Investment goods** | 255 | 256 | *0%* | 2,478 | 3,052 | *23%* | 18% |
| Machinery and equipment | 168 | 168 | *0%* | 1,693 | 2,073 | *22%* | 12% |

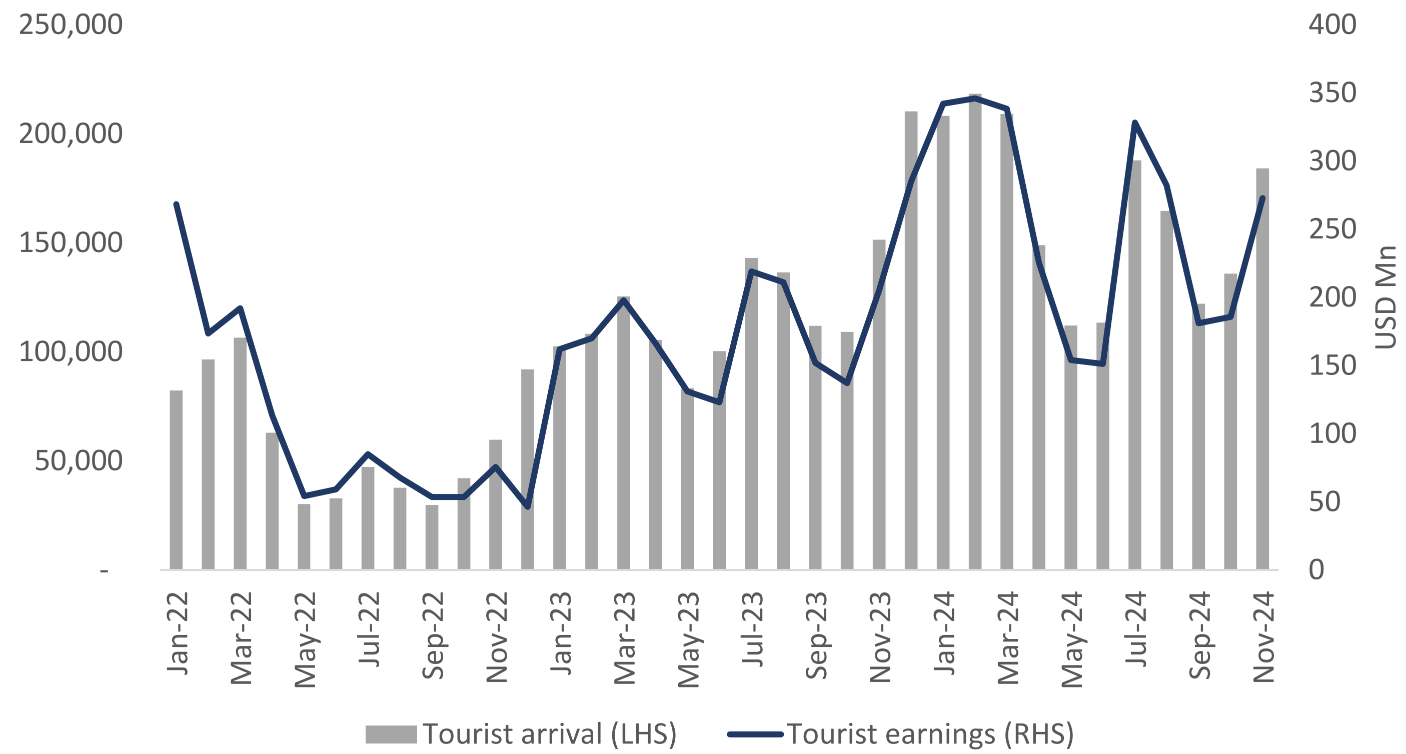
| USD Mn | Nov'23 | Nov'24 | Variance | Jan - Nov 2023 | Jan - Nov 2024 | Variance |
|---|---|---|---|---|---|---|
| Trade balance | -390 | -502 | *29%* | -4414 | -5,247 | *19%* |
| Earnings from tourism | 205 | 273 | *33%* | 1,799 | 2,807 | *56%* |
| Workers' remittances | 537 | 530 | *-1%* | 5,400 | 5,962 | *10%* |
| Foreign Direct Investment | - | - | - | - | - | - |
| **Overall Balance** | | | | **1,908** | **2,913** | ***53%*** |

*Source : CBSL, ACS Research*

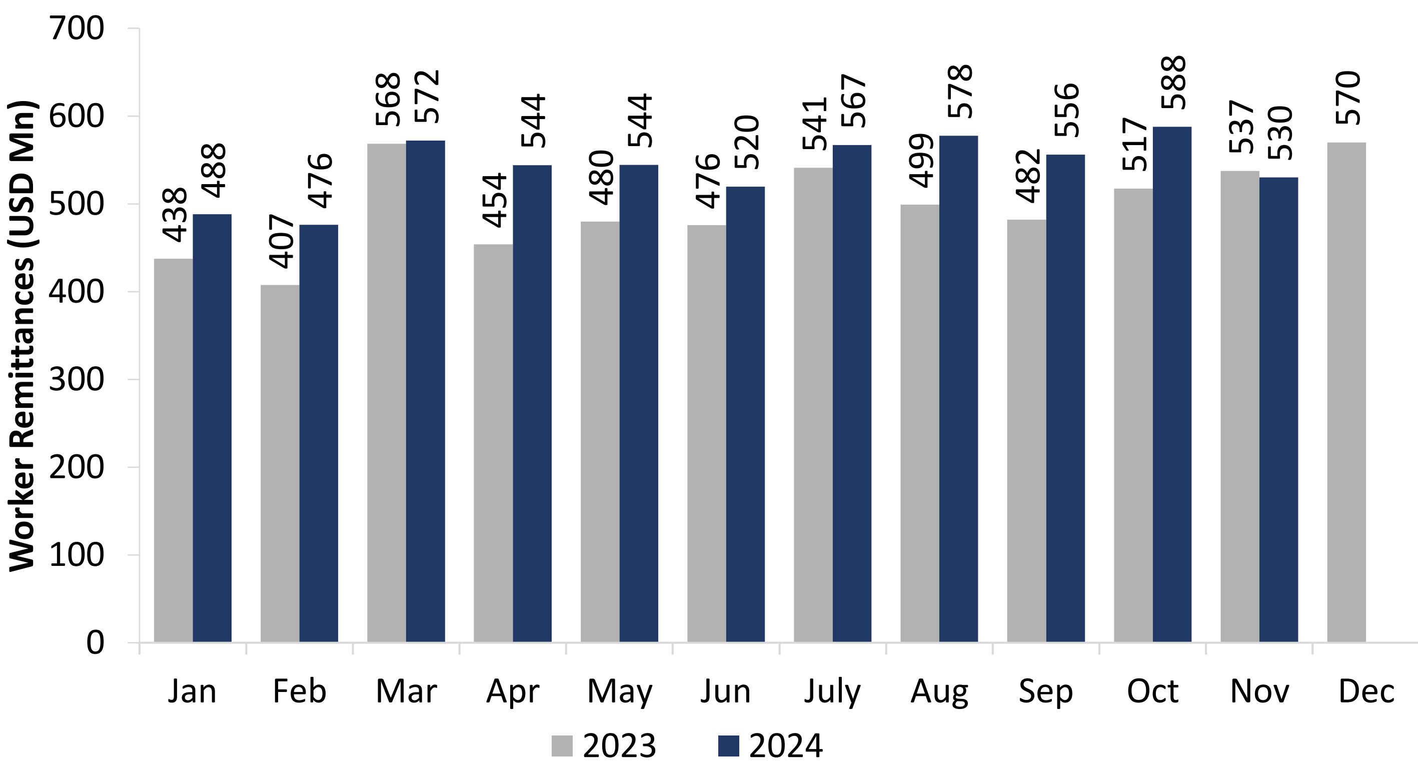
# Tourists' arrivals to pass 3Mn in 2025E

*Recognition as a premier global travel destination, free visa plans coupled with digital campaigns to boost the resilience of the tourism sector*






- Tourist arrivals ended 2024 with 2.05Mn arrivals (up by 38%YoY), recording the highest annual figure since 2019. Meanwhile, tourism income reached to USD 2.8Bn by the end of Nov'24, surpassing the total revenue of USD 2.0Bn generated throughout 2023. Further, India retained its position as the largest source market, contributing 20% of total tourist arrivals, followed by Russia, the UK, Germany and China. For 2025, ACS anticipate close to USD 4Bn earnings and arrivals closing near 3 Mn.



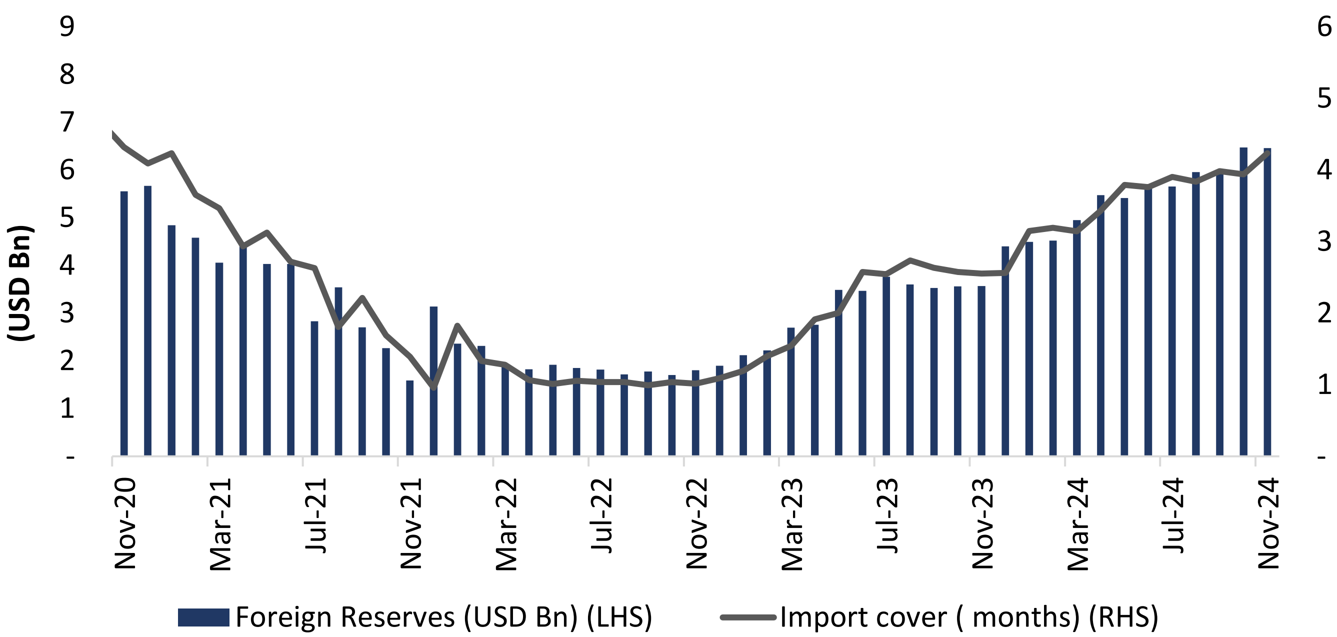

- Workers' Remittances soared by 10.4%YoY to USD 5.96Bn in the first 11 months of 2024, from USD 5.4Bn during the same period in 2023. Meanwhile, workers' remittances continued to record monthly inflows of over USD 500Mn since Mar'24 where we anticipate the remittances to touch USD 7.0Bn mark by 2025E.

*Source : CBSL, SLTDA, ACS Research*

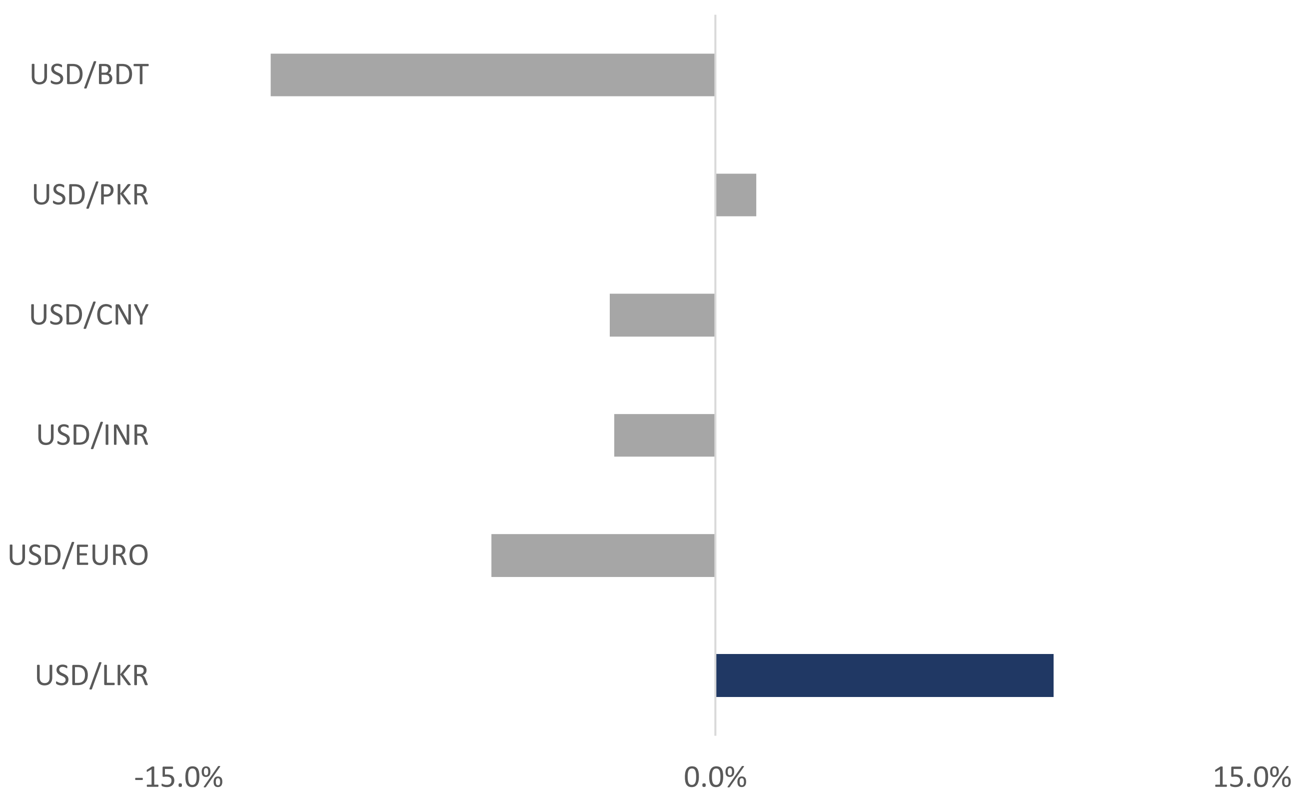
# Multilateral & Bilateral funding to support reserves

*Sri Lanka to work towards increasing reserves to cover least 4-5 months of imports*






- Sri Lanka's Gross Official Reserves stood at USD 6.5Bn at end Nov'24, recording over USD 2Bn increase from end 2023. This increase of the GOR was mainly due to the CBSL's net purchases of foreign exchange from the domestic market and the funds received from the World Bank and Asian Development Bank. The monthly import bill is also around USD 1.5Bn, which is comfortable to cover above 4 month's worth of imports.




- Official exchange rate of LKR, and PKR against USD appreciated by 9.4%, and 1.1% YTD respectively. While the EURO, INR, CNY and BDT depreciated by 6.3%, 2.8%, 2.9% and 12.4% YTD against USD.

*Source : CBSL, ACS Research*

# Inflation is at a stable level, in line with the CBSL's 5% target

*Annual average inflation stood at 1.2% in 2024*




Food Inflation (Y-o-Y)

0.8%

Non-Food Inflation (Y-o-Y)

-3.0%

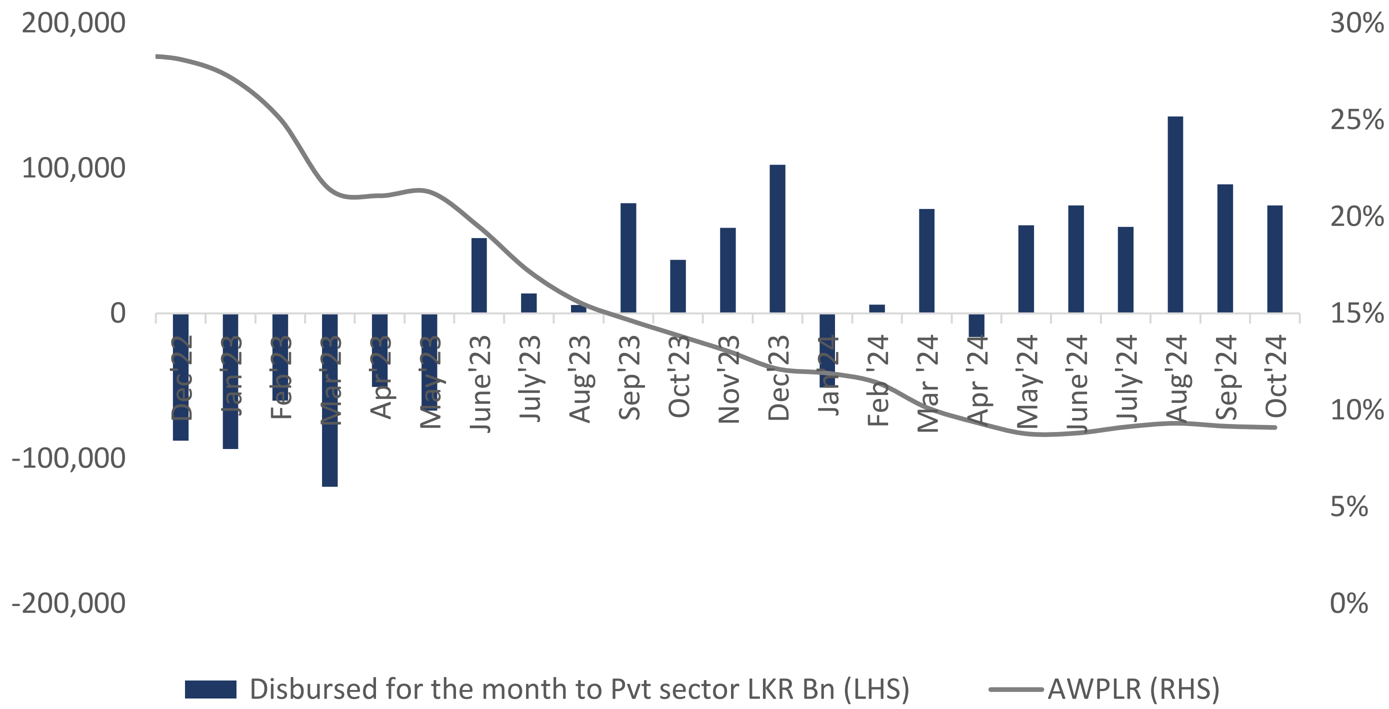
- CCPI headline inflation continued to remain in the negative territory for the fourth consecutive month, recording a deflation of 1.7%YoY in Dec'24 compared to a deflation of 2.1%YoY in Nov'24. The food inflation increased to 0.8%YoY (from 0.6%YoY in Nov'24), while non-food deflation moderated to 3.0%YoY (from -3.3% YoY in Nov'24).
- The contribution to inflation by food commodities was 0.25% and the contribution of Non-Food item was -2.01%. This was mainly due to price decreases in the groups of 'Housing, Water, Electricity, Gas and Other Fuels' (3.16%) and Transport (0.19%). However, price increases in groups of items were reported 'Education' (0.31%), 'Alcoholic beverages Tobacco and Narcotics' (0.27%), 'Health' (0.21%), 'Miscellaneous Goods and Services' (0.14%), 'Restaurants and Hotels' (0.14%), 'Clothing and Footwear' (0.12%), 'Recreation and Culture' (0.08%), 'Communication' (0.06%) and 'Furnishing Household Equipment and Routine Household Maintenance' (0.01%) when compared to the month of Dec'23.
- We expect the inflation to be around mid single digits unless external factors such as global commodity price fluctuations, exchange rate volatility, supply chain disruptions, geopolitical risks, a potential global economic slowdown, could create significant risks to Sri Lanka's inflation outlook in 2025.

*Source : CBSL, Department of Census & Statistics, ACS Research*

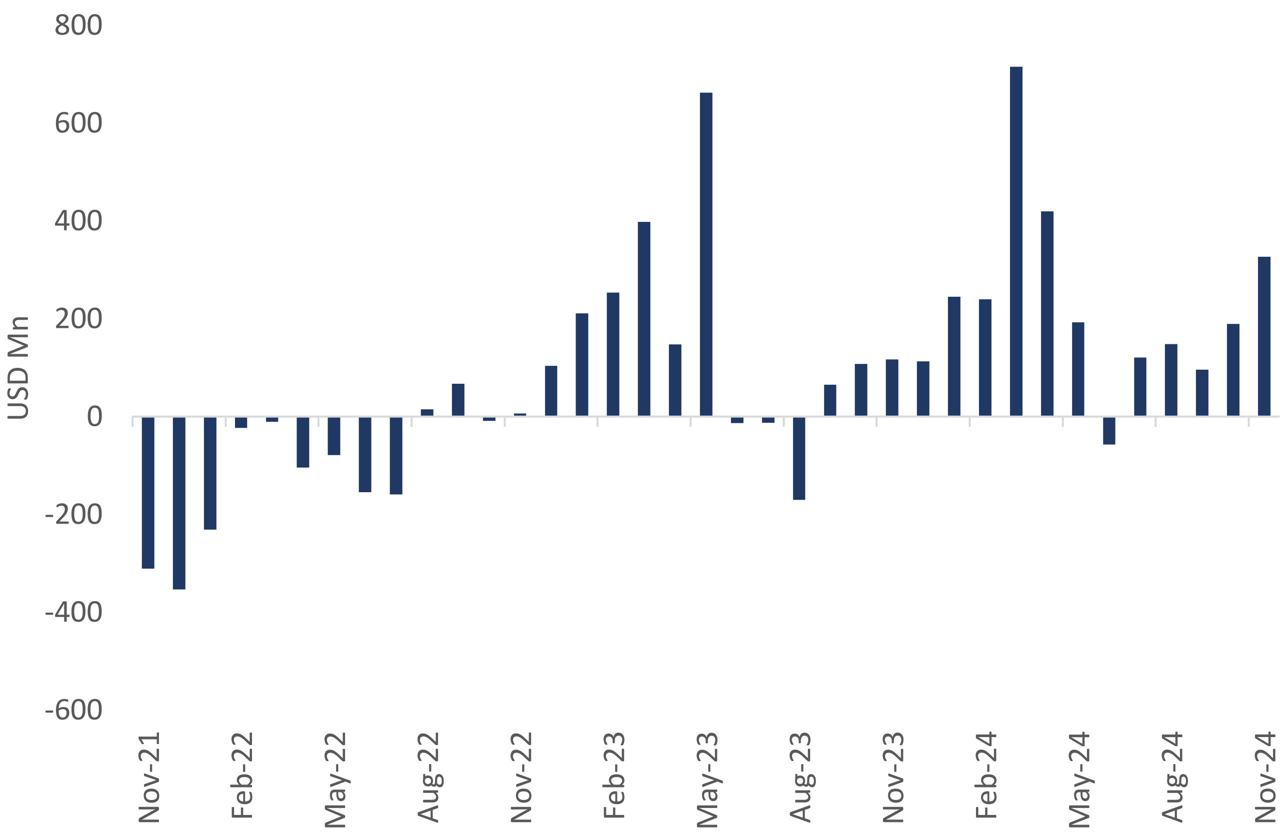
# Private sector credit is picking up amid low-interest rate climate

*Credit to private sector could see an uptick of 15% in 2025E*






- Private sector credit growth saw monthly disbursements rising since May 2024 adding a cumulative LKR 504Bn from Jan-Oct'24 (up 9.2%YoY). Private sector credit growth is expected to recover gradually in 2025, supported by improved economic stability, declining interest rates, and increased business confidence following debt restructuring. The Central Bank's accommodative monetary policy and easing inflation, which reached record lows in 2024, are likely to further encourage borrowing, with private sector credit growth reaching >15%YoY for 2025E

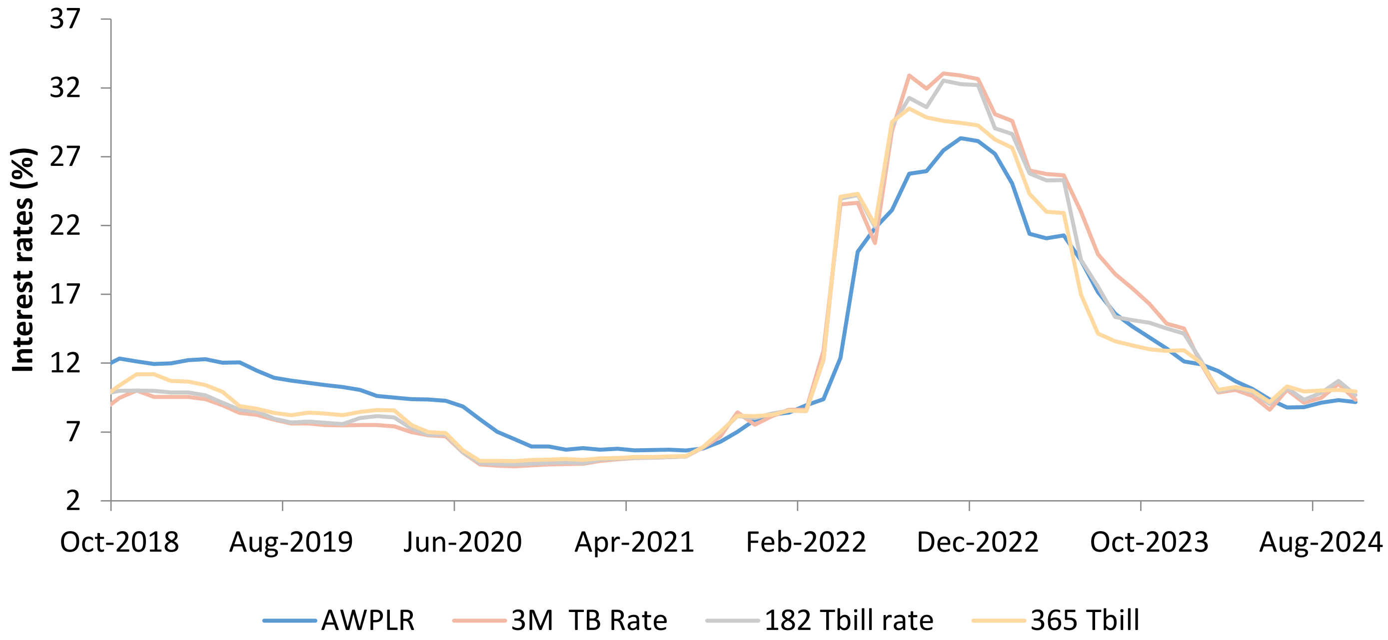


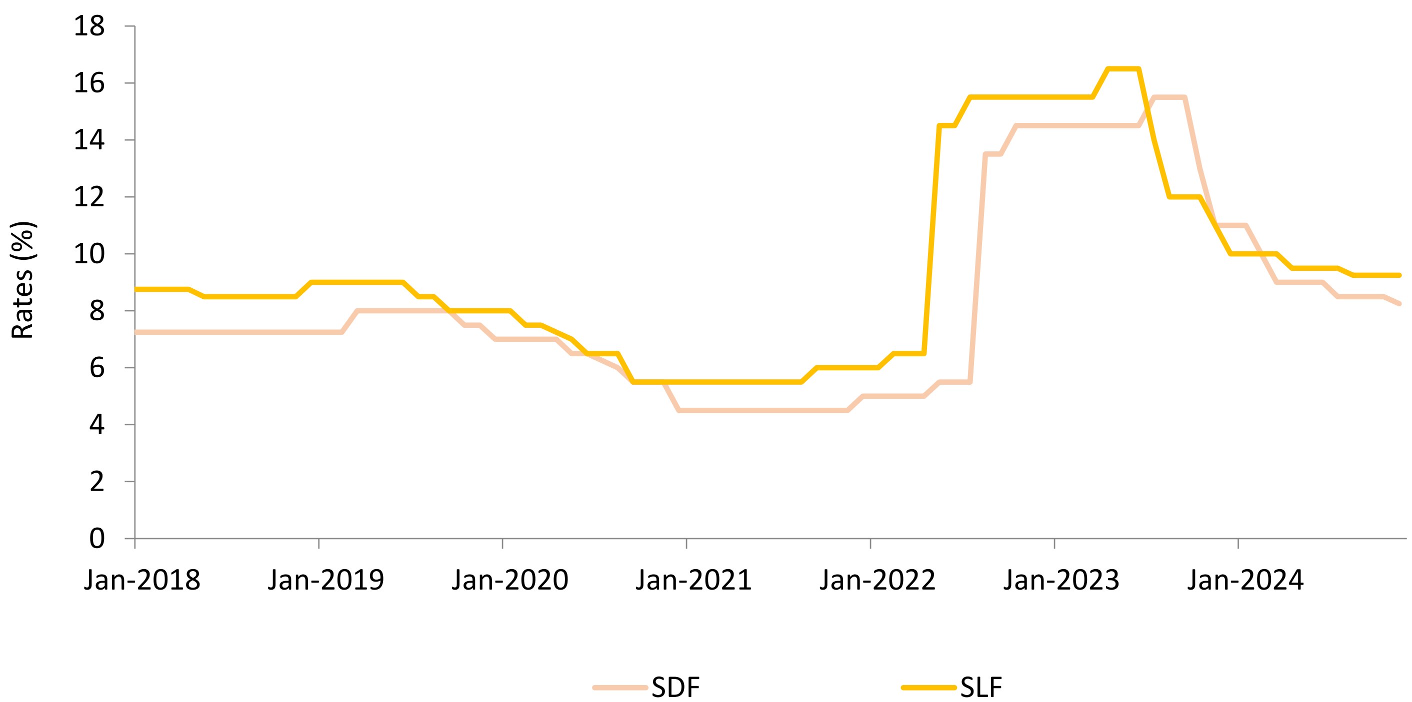

- Sri Lanka was a net purchaser of dollars up to USD 2.6Bn for first 11 months of 2024.

*Source : CBSL, ACS Research*

# CBSL's dovish monetary policy stance to continue

*Market rates to remain stable*



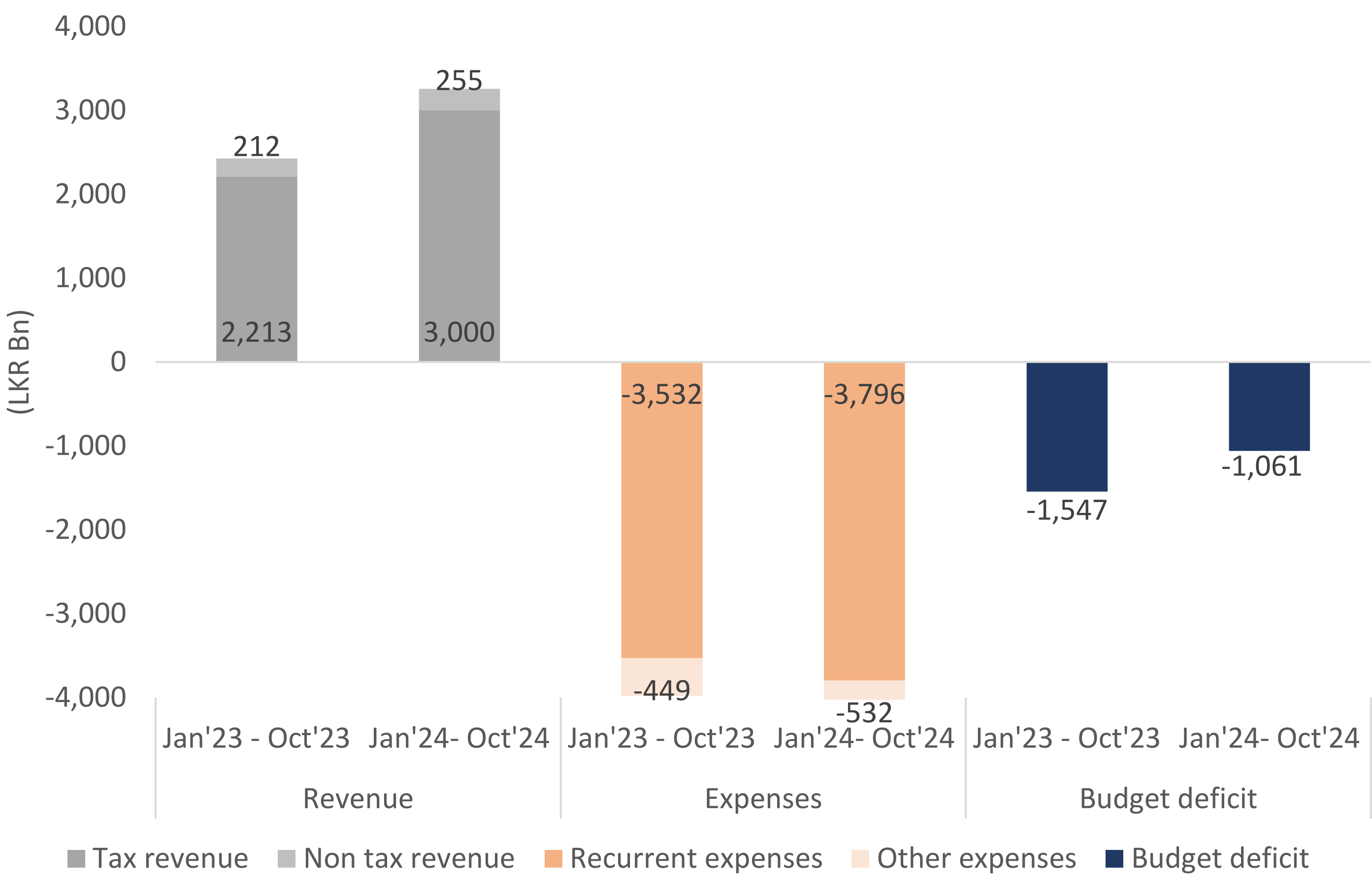

- SL T bill rates more dropped drastically during the year especially with dovish monetary policy stance followed since June'23. CBSL also moved to a new single policy rate at 8% aiming to support economic recovery while also cutting down rates since Jun'23 by 775 bps. We anticipate the AWPLR to be relatively stable or even rise slightly in response to inflationary pressures. Private sector credit growth also should follow with 13%-15% growth in 2025E ( cf. 9.2% YoY growth as at Oct'24. ( AWPLR ended the year at 9.1% (cf. 12.13% in Dec'23) , 3M bill – 8.73% (cf. 14.51%(, 6M bill 8.97% (cf. 14.16% in Dec'23) and 1Yr bill -9.08% (cf. 12.93% in Dec'23)

*Source : CBSL, ACS Research*

# Government revenue surged by 34% YoY to LKR 3.3Tn in Jan-Oct'24

*New tax avenues and rationalizing state expenditures to narrow down the budget deficit*






- Government revenue for Jan'24 – Oct'24 have increased by 34%YoY to LKR 3.25Tn, with tax revenue growing by 36%YoY to LKR 3.0Tn (accounts to 92% of total revenue). In the meantime, recurrent expenses and capital expenses increased by 7%YoY to LKR 3.79Tn and 16%YoY to LKR 531Bn respectively. Meanwhile, the budget deficit plummeted by 31%YoY to LKR 1.06Tn during the same period.
- On the fiscal front, the government is expected to continue adhering to IMF program parameters throughout 2025E to maintain access to financial support and stabilize the economy. The IMF guidelines emphasize debt sustainability, managing both external and domestic debt, and set ambitious targets, including raising the tax-to-GDP ratio to 15% by 2027E and reducing the budget deficit to 5% of GDP, while maintaining debt levels at 98.8% of GDP. Sri Lanka successfully increased its revenue by 34%YoY, reaching LKR 3.25Tn by January-October 2024, while reducing the deficit by 31%YoY to LKR 1.06Tn, aligning with the IMF's targets. We expect the new government to remain committed to these goals to ensure continued progress.

*Source : CBSL, ACS Research*

# All indicators are pointing at the right direction

Inflation , rates, state revenue , balance of payment and growth are intact



| Indicator | 2022 | 2023 | 2024YTD | | 2024E | 2025E |
|---|---|---|---|---|---|---|
| Real GDP growth (%) | (7.3) | (2.3) | 5.2 | as 9M'24 | 5.4 | 5.7 |
| CCPI 12M Average inflation | 46.4 | 17.4 | 1.2 | as at 31.12.24 | 1.2 | 3.8 |
| AWPLR (%) (YE) | 27.2 | 12.1 | 9.1 | as at 27.12.24 | 9.1 | 9.5 |
| 1YR T bill rate (%) (YE) | 29.3 | 12.9 | 8.9 | as at 01.01.25 | 9.0 | 9.2 |
| Private Sector Credit Growth | 6.2 | -0.6 | 9.1 | as at 31.10.24 | 10.0 | 15.0 |
| USD/LKR ( spot) YE | 363.1 | 323.9 | 293.3 | as at 0 2.01.25 | 292.58 | 310-315 |
| Total Government Revenue ( LKR Bn) | 2,013 | 3,074 | 3,267 | as at 31.10.24 | 4,027 | 4,632 |
| Budget Deficit ( LKR Mn) | (2,460) | (2,282) | (1,061) | as at 31.10.24 | (1,380) | (1,352) |
| Exports (USD Bn) | 13.11 | 11.91 | 11.67 | as at 30.11.24 | 13.0 | 13.9 |
| Imports (USD Bn ) | 18.29 | 16.81 | 16.92 | as at 30.11.24 | 21.1 | 22.4 |
| Trade Deficit ( USD Bn) | -5.19 | -4.90 | -5.25 | as at 31.11.24 | (5.9) | (6.1) |
| Remitances ( USD Bn) | 3.8 | 6.0 | 6.0 | as at 30.11.24 | 6.5 | 7.0 |
| Tourist Income (USD Bn) | 1.2 | 2.1 | 2.8 | as at 30.11.24 | 3.2 | 4.2 |
| Tourist Arrivals (Mns) | 0.7 | 1.5 | 1.8 | as at 30.11.24 | 2.1 | 2.9 |

*Source : CBSL, ACS Research*

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