

# SRI LANKA

Steering through uncertainty ; Markets poised for a post election rebound

PRESIDENTIAL CANDIDATES  
ARE MORE FOCUSED ON  
ACHIEVING ECONOMIC  
STABILITY THAN EVER  
BEFORE

# ALL CANDIDATES' PRIME FOCUS; ECONOMIC STABILITY & RECOVERY

## POTENTIAL SETBACKS POST ELECTIONS LIKELY TO BE SHORT-LIVED

- The upcoming Presidential election on 21<sup>st</sup> September has three front runners, the current President Ranil Wickramasinghe, opposition leader Sajith Premasda and NPP leader Anura Kumara Dissanayake. Despite various populist measures proposed by each candidate, this election stands out from the previous elections, due to its heightened focus on stabilizing the economy especially economic recovery and long-term fiscal stability taking center stage. All candidates seem to be showing commitment to address the financial challenges and while appealing to the voters there is a growing recognition of the need for sustainable economic policies .
- Though we think there could be a temporary setback in economic activities and interest rates likely edging up in the immediate aftermath, stability is expected to return once the new president comes in to power as regardless of the election outcome, the new administration will have limited room to deviate from the current economic agreement.
- We also think while there may be negotiations for modifications, the IMF will likely agree to adjustments only if the new administration presents credible alternative policies that align with the program's goals, as each candidate is aware that continuity is crucial for maintaining economic stability which also suggest any disruptions post elections likely be short lived.



# SRI LANKA IS ALREADY ON THE RIGHT PATH TO RECOVERY

## IMF REFORMS TO FUEL STABILITY DESPITE POLITICAL UNCERTAINTY

- Since entering into an agreement with the International Monetary Fund (IMF) in March 2023, Sri Lanka has made notable progress in stabilizing its economy by reducing inflation, stabilizing the currency, restructuring debt, and implementing critical fiscal and structural reforms and addressing the severe financial crisis it faced.
- In terms of macro economic front, inflation was reduced from 70% levels seen in 2022 to less than 5% with the government implementing tighter monetary policies and structural reforms. The Central Bank of Sri Lanka moved toward a more flexible exchange rate regime under the IMF agreement help stabilizing the LKR, which had been extremely volatile due to the balance of payments crisis in 2022. Series of tax reforms were also introduced under the program aimed at increasing government revenue while rationalizing public expenses.
- Sri Lanka also managed to achieve one of the key critical milestones by restructuring both domestic and external debt where relief is expected to be obtained by both bilateral and commercial creditors.
- Greece serves as an excellent example of a country that successfully emerged from a severe crisis. After renegotiating terms and implementing tough austerity measures and reforms, it returned to international markets within a few years of declaring bankruptcy. Similarly, we believe Sri Lanka has the potential to achieve economic growth of over 5-6%, compared to more conservative outlook of some of the agencies specially given its low base, the size of the country, and key development strategies already in place.



# MARKETS BRACE FOR POST ELECTION REBOUND

EQUITIES TO BOUNCE BACK TO TRADING MULTIPLES OF >10X PER

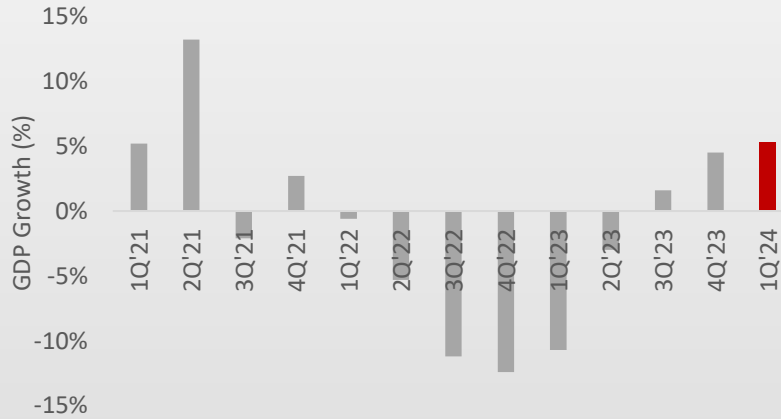
- Therefore, regardless of the political outcome, we expect this trajectory to continue with only minor adjustments, as it is vital to securing economic stability and sustainability at this critical juncture.
- Despite this, the equity market has overreacted ahead of the elections, dropping over 8% in the last two months—an unprecedented decline in comparison to past election cycles. We see this as a temporary setback, and a market rebound to be imminent, especially since no major changes are expected in the reform agenda post elections.
- We anticipate the market to trade at least 10x-12x P/E (from the current 9.0x) within the next year, driven by potential earnings growth spurred by economic recovery and increased investor confidence. Consequently, market is expected to reach the psychological 12,500-13,000 mark by 2024E and potentially move towards 14,000-15,000 as the economy begins to recover.



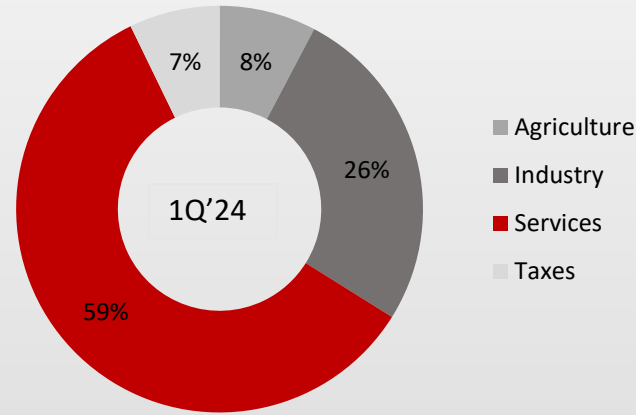
# ECONOMY IS ALREADY SHOWING SIGNS OF IMPROVEMENT

KEY ECONOMIC INDICATORS ARE REFLECTING POSITIVE PROGRESS

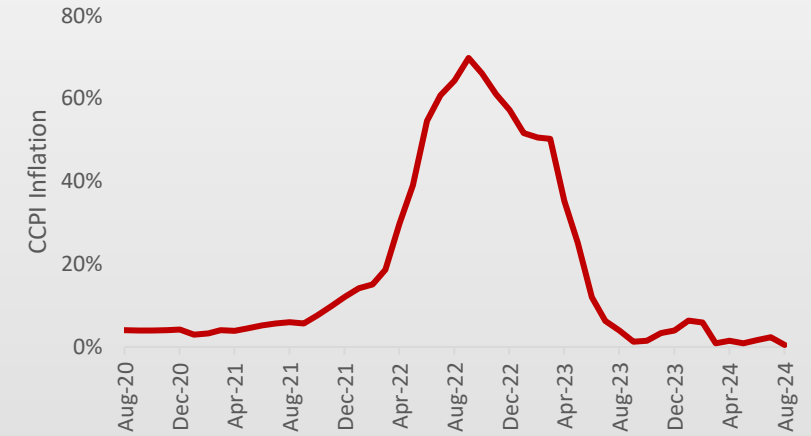
**GDP is on the rise for the third consecutive quarter after 7 quarters of dip**



**Services sector continue to be the biggest contributor**



**Inflation remains well below CBSL's 5% target level**



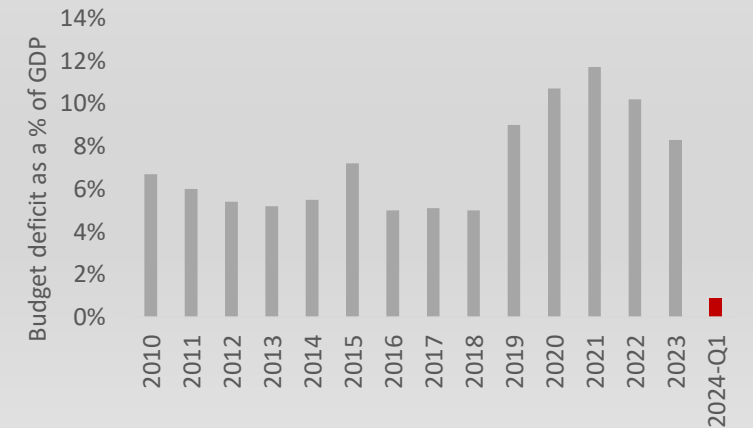
**Reserves stood at USD 5.6Bn, comfortably covering over 3 months of imports**



**Balance of position has turned positive, BOP surplus stands at USD 1.76Bn as at 2Q'24**



**Fiscal position is now at comfortable levels; primary balance is now recording a surplus**



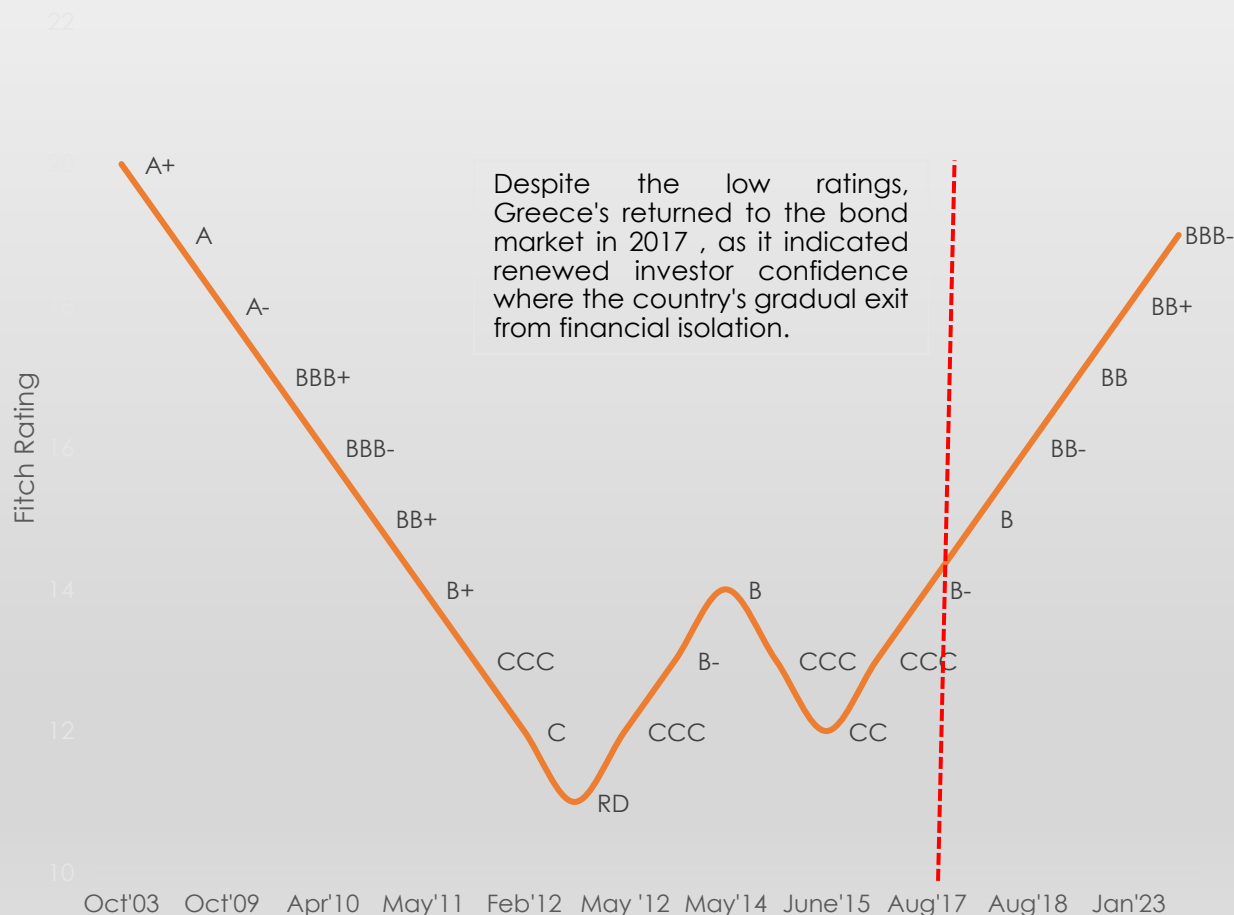
# SRI LANKA IS MOVING TOWARDS THE RIGHT DIRECTION

COUNTRY LARGELY IN LINE WITH THE TARGETS SET BY IMF, MOVING TOWARDS GREATER DEBT SUSTAINABILITY

Key Indicators	2022	2023	2024E	2025E	2026E
Real GDP growth	-7.3	-2.3	2.0	2.7	3.0
Revenue to GDP	8.4	11.1	13.6	15.1	15.3
Expenses to GDP	18.6	19.4	20.9	20.3	19.9
Budget deficit to GDP	-10.2	-8.3	-7.3	-5.2	-4.6
Primary deficit/surplus to GDP	-3.7	0.6	1.0	2.3	2.3
Debt to GDP	115.9	109.8	108.8	108.4	108.3
Inflation (Average)	45.2	17.4	7.0	5.8	5.4
Reserves (USD Bn)	1.8	4.3	5.6	7.1	9.2
Exports (USD Bn)	13.1	11.9	12.9	13.6	14.2
Trade balance (USD Bn)	-5.2	-4.9	7.2	-8.9	-9.4

# GREECE SERVES AS AN EXEMPLARY SUCCESS STORY, HAVING SUCCESSFULLY EMERGED FROM BANKRUPTCY

COMBINATION OF DOMESTIC REFORMS, FISCAL DISCIPLINE , INTERNATIONAL SUPPORT HELPED GREECE. SRI LANKA IS CURRENTLY ON A SIMILAR PATH, WORKING TOWARDS SIMILAR OUTCOMES.



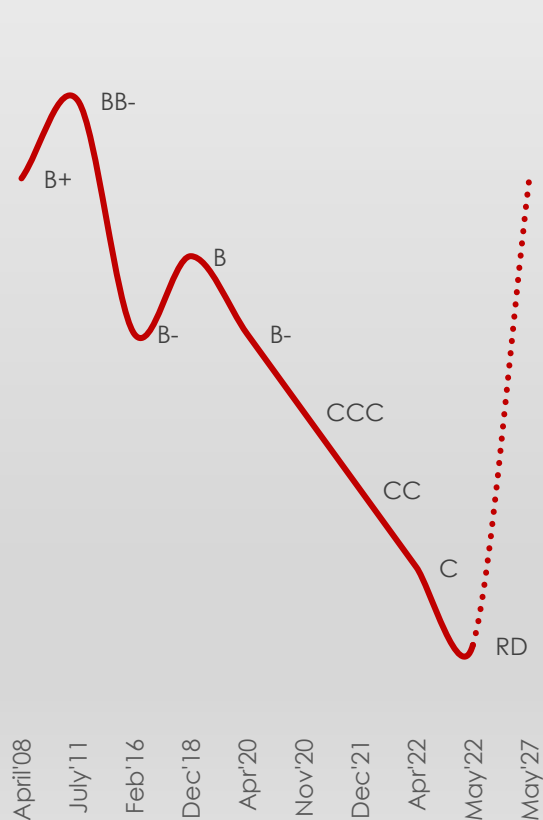
## Greece – Key Milestones

- 2010-2015 : Bailout Programs and International Assistance
- 2012- Sovereign bond restructuring
- Austerity Measures and Fiscal Consolidation – government spending cuts, tax reforms , recorded a budget surplus in 2016.
- Economic reforms – labor market reforms, privatization
- Banking sector stabilization – recapitalization of banks, imposing capital controls in 2015
- Improve debt sustainability – debt relief by EU , re entered the bond market in 2017
- Tourism , foreign investments , political stability and commitment for reforms helped Greece to regain its market confidence.



# IMF PROJECTS SRI LANKA TO RE-ENTER THE GLOBAL CREDIT MARKET BY 2027E, INDICATING A POTENTIAL IMPROVEMENT IN ITS CREDIT RATING TRAJECTORY

IMF therefore expect SL's sovereign rating to least reach B- / BB by 2027E



Cost reflective pricing for fuel & electricity	✓
Domestic debt restructuring	✓
External debt restructuring	✓
Approval of welfare benefits	✓
Fiscal reforms	✓
Obtain Cabinet approval of the fiscal strategy statement (FSS) containing a medium-term fiscal framework (MTFF).	✓
Cabinet approval of quarterly revisions of electricity tariffs, starting in 2024	✓
Cabinet approval of a comprehensive strategy to restructure the balance sheets of the CEB, CPC, Sri Lankan Airlines, and the Road Development Authority	✓
Cabinet approval of a reduction in the limit on government guarantees to 7.5 percent of GDP	✓
Approval for CBA	✓
Publication of Governance diagnostic report	✓
Publication of a government action plan for implementing recommendations in the Governance Diagnostic report.	✓

Approval of Appropriation Act	✓
Introduction, tracking and reporting quarterly KPIs of tax compliance	✓
Government and CBSL to develop a detailed recapitalization plan for the remaining four banks	✓
Approval for revenue measures to support fiscal consolidation	Pending
Completion of recapitalization of two large state banks private sector banks and restructuring of CPC loans	Pending
Submitting other revenue measures	Pending
Establish public debt management agency	Pending
Enact new anti corruption legislation	Pending
Enact comprehensive asset recovery law	Pending
Obtain a cabinet approval of the repayment schedule of CEB's legacy debts, starting in April 2025	Pending
Publish on a semi-annual basis on a designated website on all public procurement contracts	Pending

# SL COULD UNRAVEL THE FULL POTENTIAL OF UNTAPPED RESOURCES

## SRI LANKA TO UNLOCK ITS POTENTIAL, READY TO SOAR TO NEW HEIGHTS OF GROWTH

### Leveraging on India

SL strategically positions to a market of 1.3Bn people. India's high growth potential to help with SL's trade, tourism and investments.



### Port City

Transform Sri Lanka into a regional financial hub, attract investments, and boost growth.

### Air port expansions

Enhance connectivity, to boost tourism and economic growth



### Timely Reforms

Key reforms to restore economic stability, boost investor confidence, and ensure sustainable growth.

### Strategic location

Increased trade opportunities as Sri Lanka attracts shipping lines and airfreight services.



### Tourism

Focus on generating foreign exchange by targeting 5Mn tourists by 2030.

### Improve road network

For better economic integration, stimulate trade, boost tourism and reduce travel time & cost



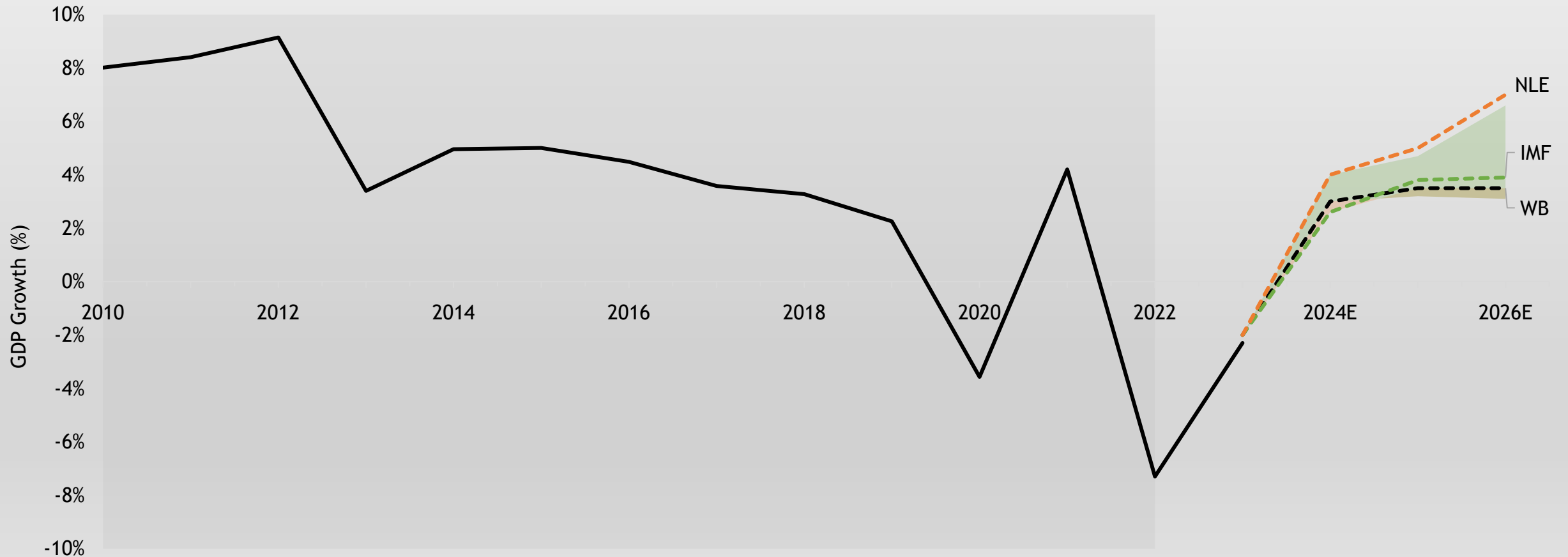
### Expand Exports

Plans to develop export zones, expand markets, and improve trade agreements.

# ECONOMY SET TO RETURN TO HIGH GROWTH PATH

AS POTENTIAL PRESIDENT SHOULD ADHERE TO IMF GUIDELINES WHICH WILL EVENTUALLY STABILIZE ECONOMY

NLE is more positive on the economic recovery than some of the conservative predictions taken by other institutions Low economic base, higher remittances and tourism earnings, SL's strategic geographical location, relief through debt restructure, political stability, reforms to push the growth to higher levels



# CAPITAL MARKETS POISED TO REBOUND POST ELECTIONS

# AS THE ECONOMY GROWS, EQUITY MARKETS TEND TO FOLLOW SUIT, WITH GDP AND STOCK PRICES MOVING IN PARALLEL.

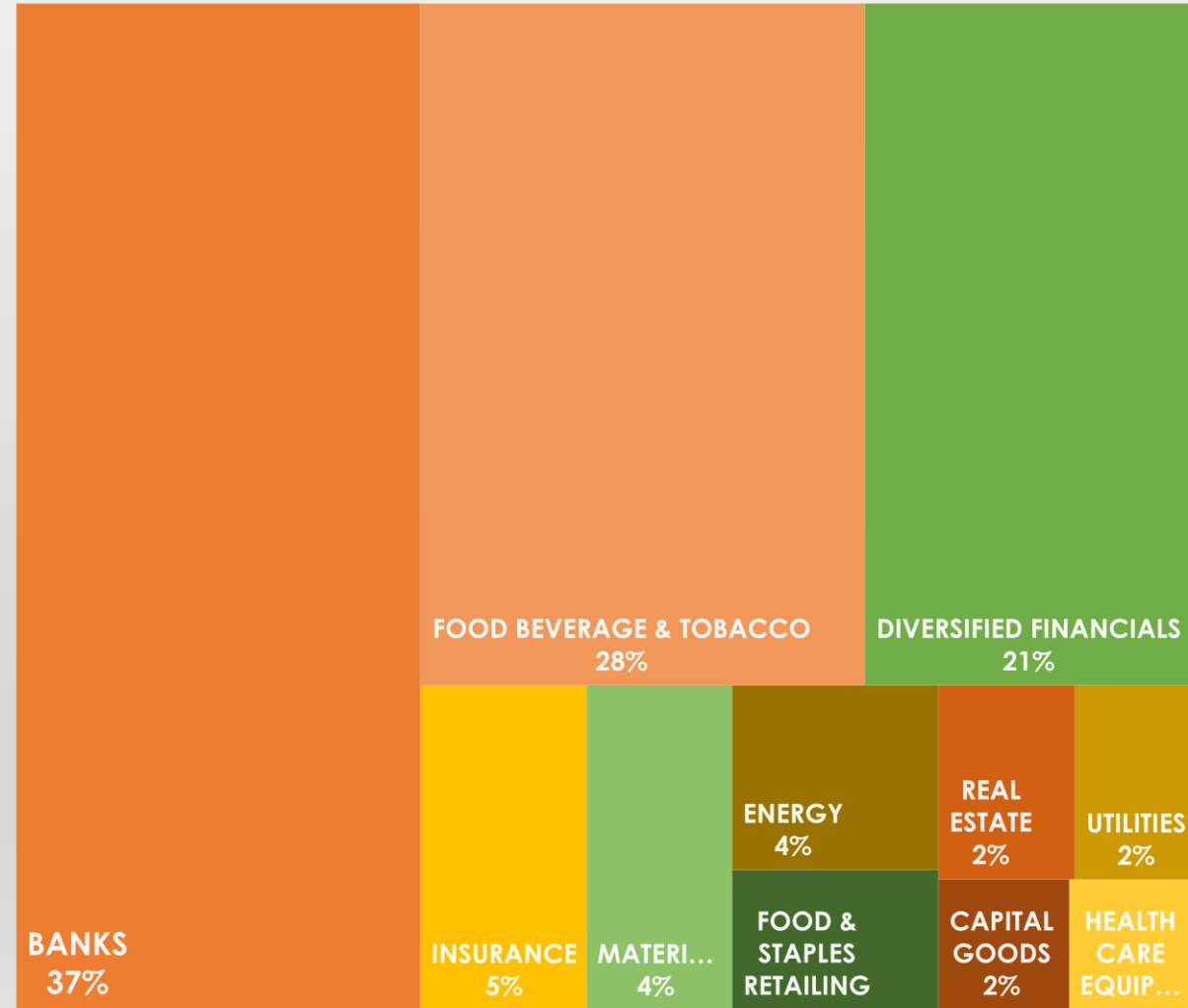
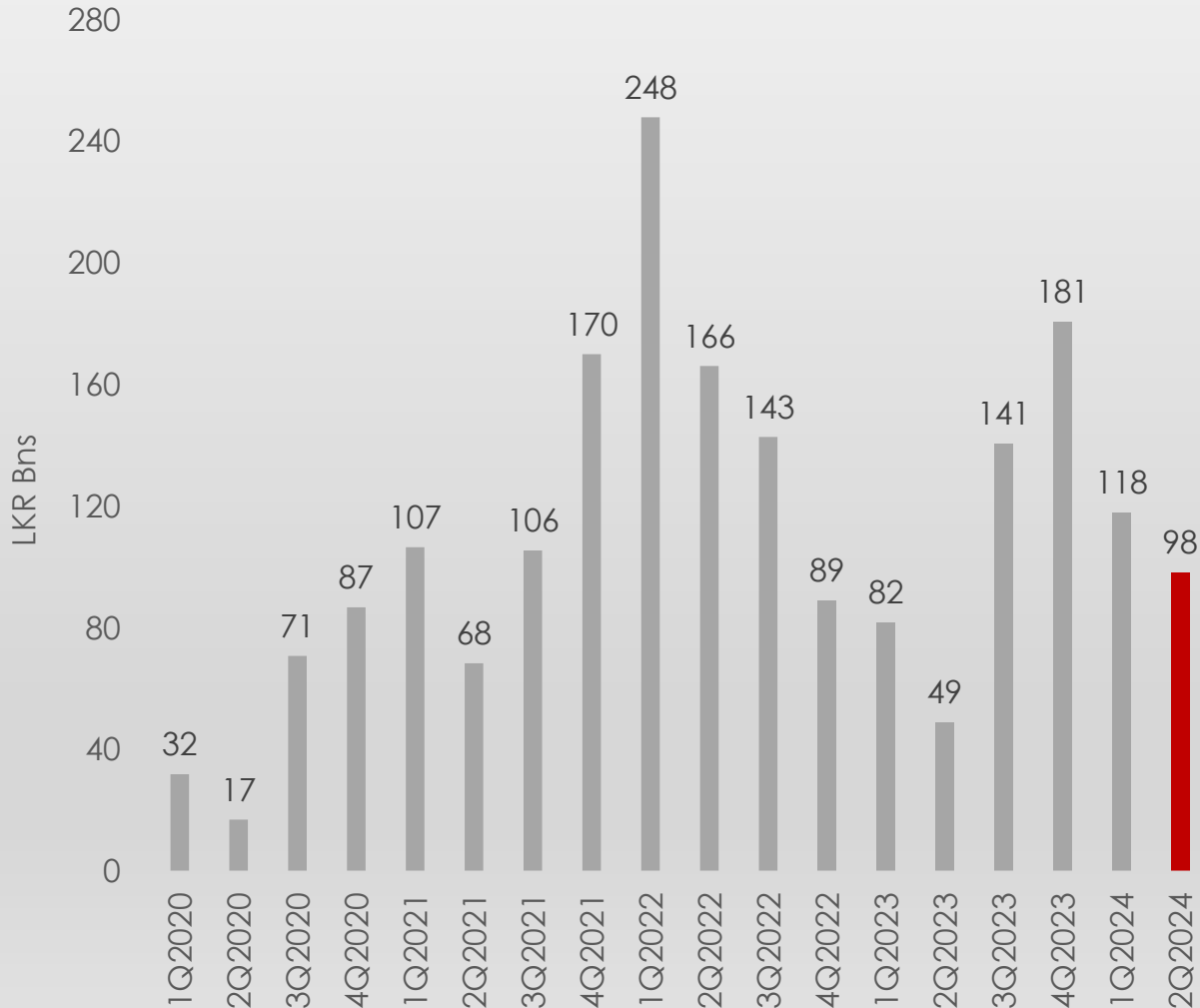
We therefore anticipate the market to trade at 10x-12x P/E (from the current 9x) within the next year, driven by potential earnings growth spurred by economic recovery and increased investor confidence. The market could reach the psychological 12,500-13,000 mark by 2024E and possibly move towards 15,000 as the economy begins to recover.



# EARNINGS TOO ARE ON AN UPWARD SWING; BROAD MARKET EARNINGS ARE EXPECTED TO GROW >35%YOY

Corporate earnings continued its growth trajectory with profits soaring over 2xYoY in 2Q'24. We expect the earnings to grow >30% in the next two years

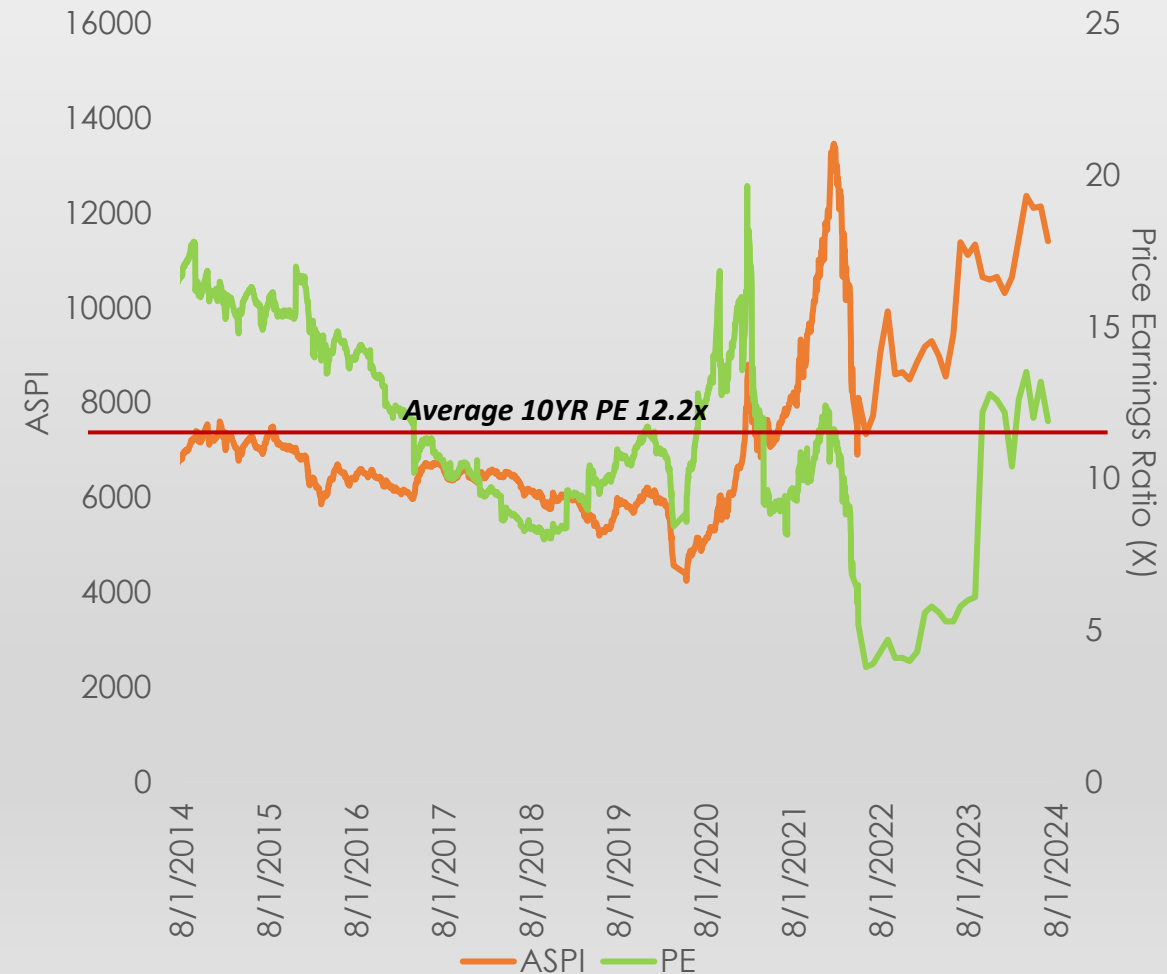
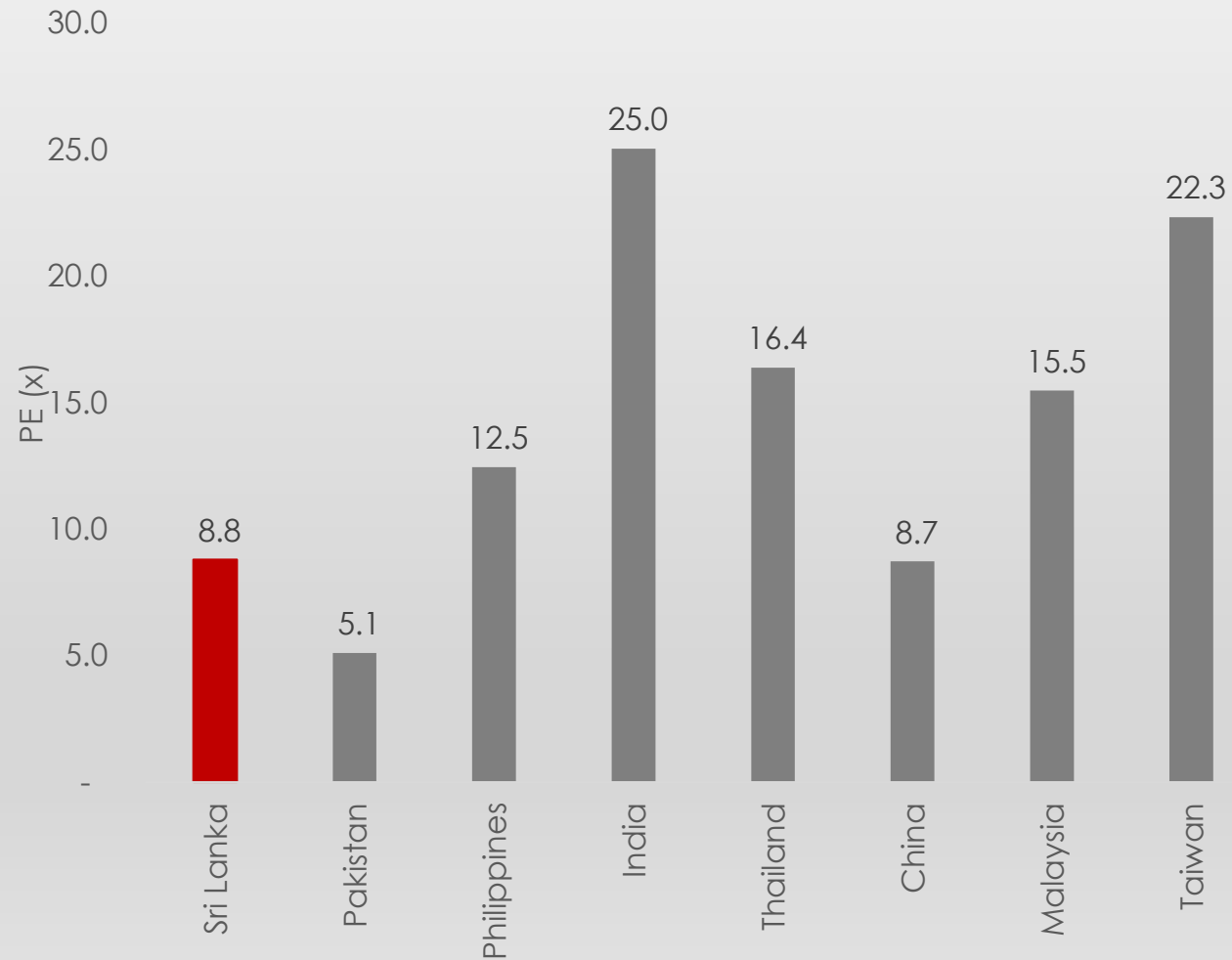
Banks, Food, Beverage & Tobacco sectors contributed to over 65% of the total earnings



# VALUATIONS HAVE FALLEN TO LEVELS THAT PROVIDE AN ATTRACTIVE RISK-REWARD BALANCE FOR NEW INVESTMENTS

Sri Lanka is still cheaper than most of its regional peers, trading at a 63% discount to India, a 59% discount to Taiwan, and 44% discount to Thailand.

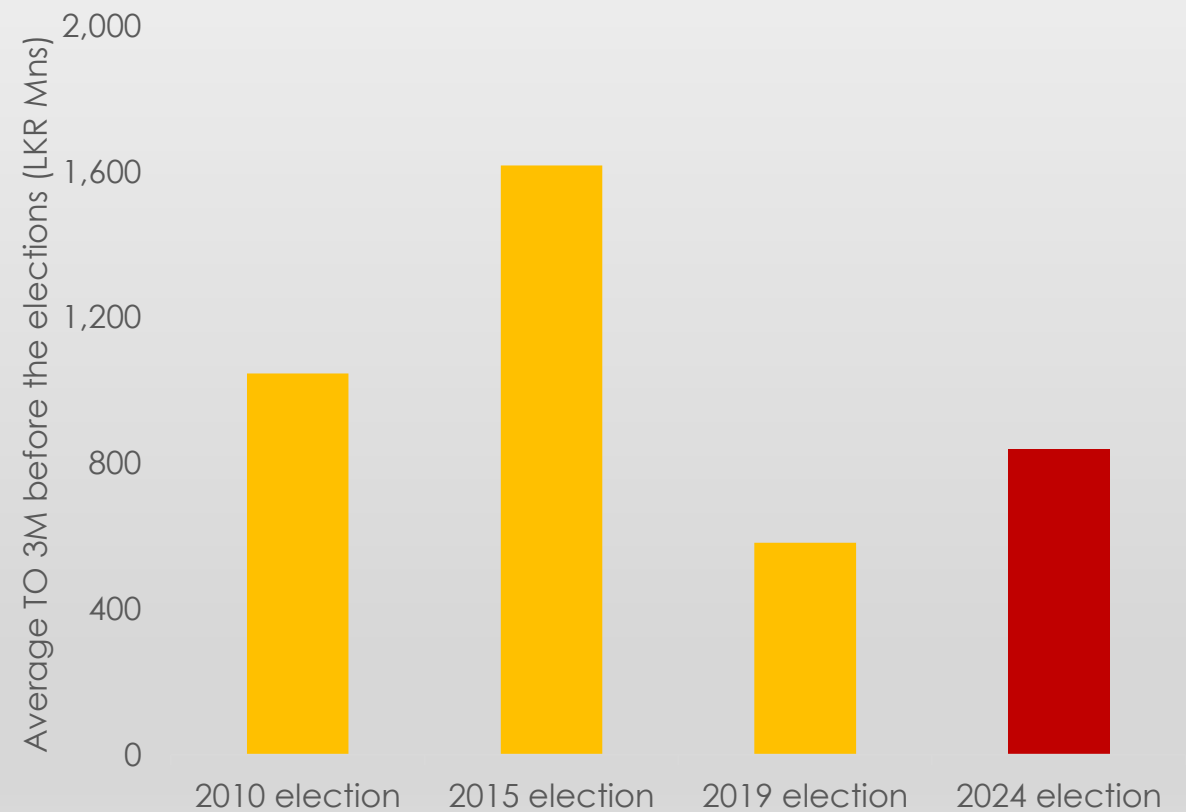
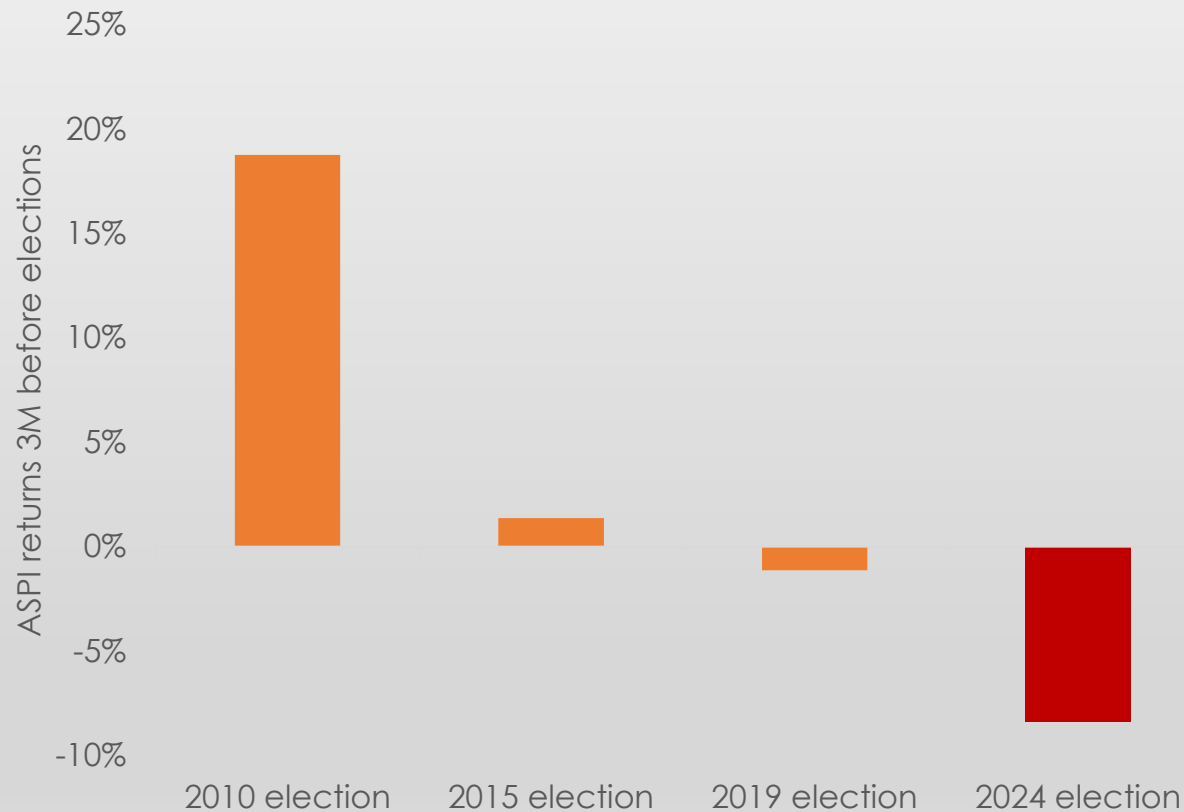
Sri Lanka trades at a significant 25% discount to 10 Yr average PE of 12.2x & 35% discount to 14yr average of 14.4x



# CURRENT VOLATILITY IN THE MARKET THEREFORE IS SHORT LIVED

## MARKETS PREPARE TO REBOUND FOLLOWING ELECTIONS

Market has declined more than previous elections whilst average turnover levels have also fallen amid ongoing uncertainty , which could be temporary



Prices as at 10.09.2024



MARKET REMAINS HEAVILY  
UNDERVALUED. MANY KEY  
SECTORS TO BENEFIT

# UNDERVALUED SRI LANKA POISED FOR GROWTH

## BANKING, CONSTRUCTION, TOURISM, RETAIL SECTORS SET TO REBOUND

- The Colombo Stock Exchange (CSE) is currently trading at relatively low multiples, reflecting undervaluation in several key sectors, despite multiple catalysts that suggest potential for significant growth ahead. Some of the factors and sectors poised to benefit include Banking, construction, Retail and tourism.
- With the International Sovereign Bond (ISB) restructuring largely completed, the overhang of uncertainty around debt sustainability has been addressed, leading to reduced impairments in the banking sector. Low-cost borrowings should spur loan book growth in the coming quarters benefiting banking sector counters coupled with the overall recovery in the economy reducing the nonperforming loans. Moreover, many banking counters are currently trading at a significant discount to their book value, providing attractive entry points for investors.
- Construction sector activities are picking up with both private and public sector investments starting to pick up. The recent rebound in private sector credit is also positive to the sector, benefiting many counters in this segment in our view.
- Retail segment would also be a key beneficiary, with expected wage adjustments and improvement in the economy. Higher discretionary income therefore will drive growth in the retail segment specially with the demand for consumer goods and services strengthening.
- Tourism sector, meanwhile, is also rebounding post pandemic and economic crisis with a rise in foreign tourist arrivals. The occupancy levels and room rates are also steadily increasing with the demand, benefiting the counters listed in the exchange in our view.
- Sri Lanka is also seen the major macro economic factors stabilization such as inflation, interest rates and investor confidence. Several companies are trading below their intrinsic value, suggesting the market has not fully priced in their recovery potential, which indicates a notable opportunity for long term investors.



# EQUITY MARKET IS AT 8.6X PER, INDICATING VALUE

LOW MARKET CAP/GDP IMPLIES POTENTIAL FOR GROWTH REFLECTING INCREASED INVESTOR OPPORTUNITIES



**Market Cap**  
LKR 4.3 Tn/ USD 14.4 Bn



**Market PE/ PBV**  
8.60x/ 0.91x



**No of listed companies/Industry Groups**  
285/20



**Primary indices**  
All Share Price Index and S&P  
SL 20



**T12 Average Daily turnover**  
LKR 1.4 Bn/ USD 4.7 Mn



**Main Boards**  
Main/Dirisavi/Empower

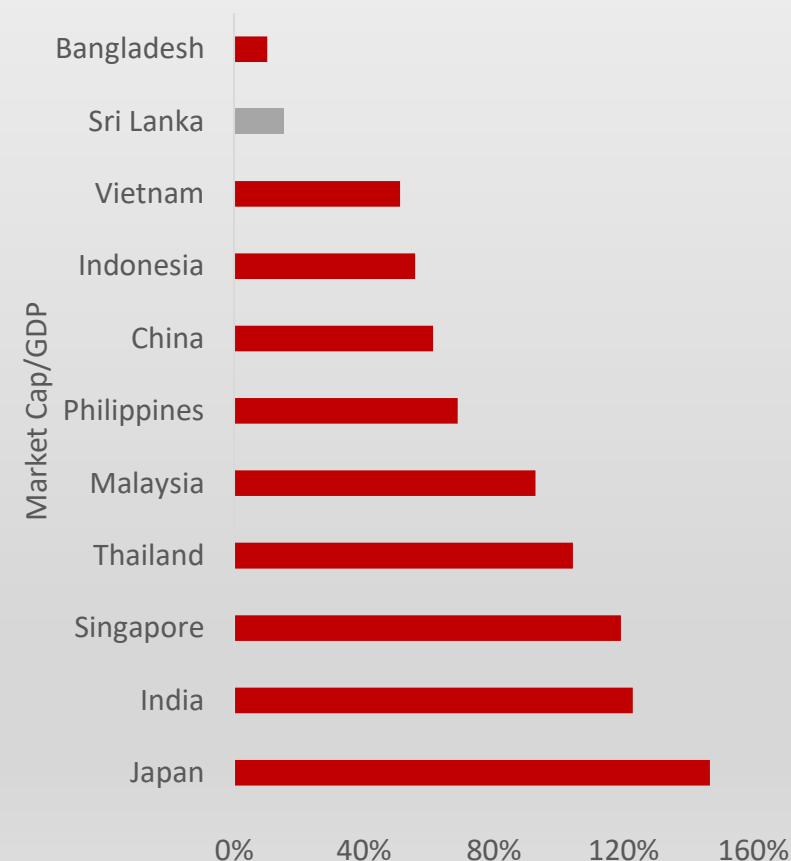


**T12 Average volume traded**  
62.9 Mn Shares



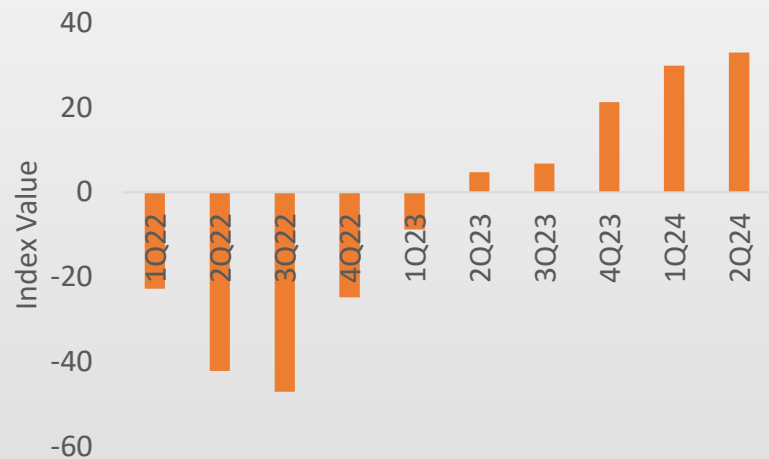
**Foreign participation**  
25%

## Market Cap to GDP

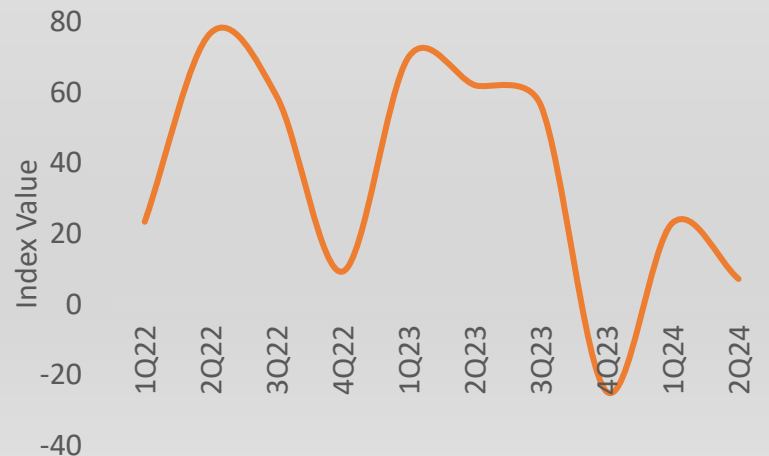


# BANKS ARE UNDERWEIGHT

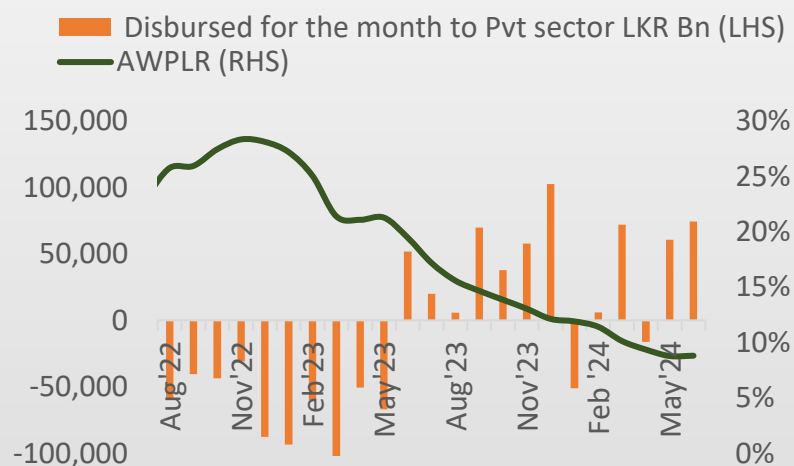
## Willingness to lend is picking up



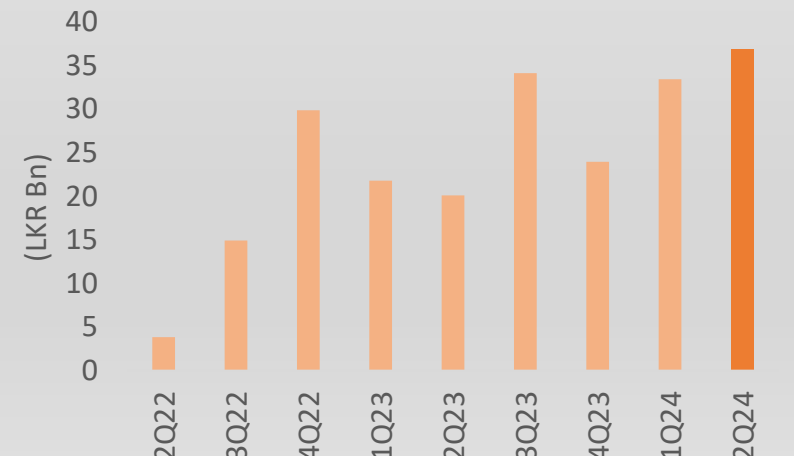
## NPL ratios are slowing



## AWPLR is <10% , pvt sector credit picking up



## Banking sector earnings growth continues



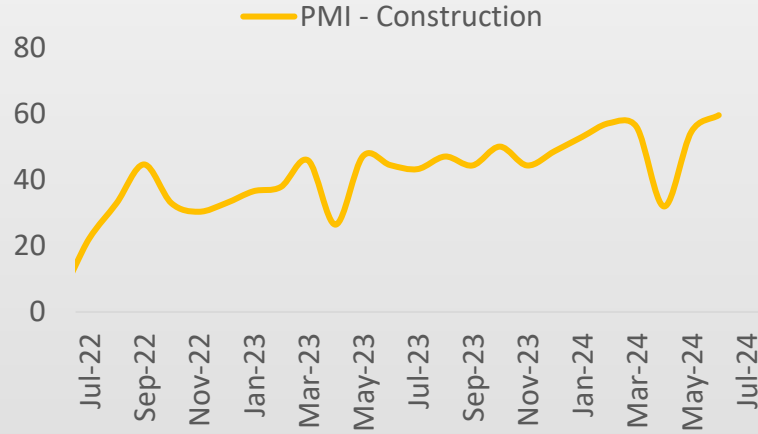
## Key beneficiaries

Ticker	Mkt Price	TTM PER(x)	PBV (x)	ROE (%)	TTM DY(%)
<b>Banking Sector</b>		<b>3.50</b>	<b>0.45</b>	<b>13.0</b>	
COMB.N	80.40	4.1	0.58	14.1	8.1
HNB.N	157.00	3.1	0.39	12.8	5.1
SAMP	68.00	3.6	0.49	13.6	8.6
NTB.N	105.50	2.6	0.50	19.4	4.7

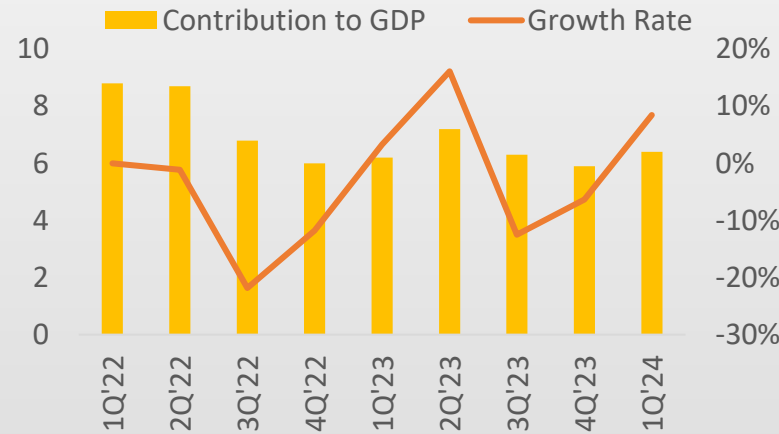
Prices as at 10.09.2024

# CONSTRUCTION SECTOR REBOUNDED AMID RENEWED INVESTMENTS & GROWTH

## Outlook for construction sector remains positive



## Contribution from construction sector to GDP is picking up

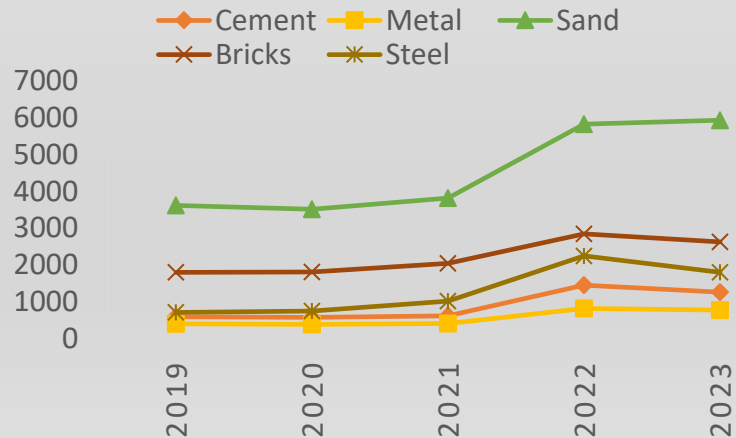


## Key beneficiaries

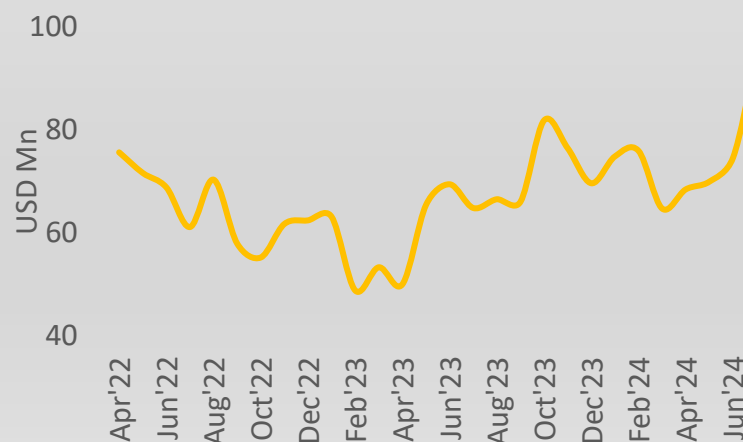
Ticker	Mkt Price	TTM PER(x)	PBV (x)	ROE (%)	TTM DY(%)
AEL	20.00	2.7	0.5	19.9	7.5
ACL	76.10	4.7	0.7	13.8	1.6
TKYO.N	43.00	8.4	0.7	8.0	4.7
RCL	28.50	4.4	0.7	16.2	10.2

Prices as at 10.09.2024

## Material prices are gradually declining

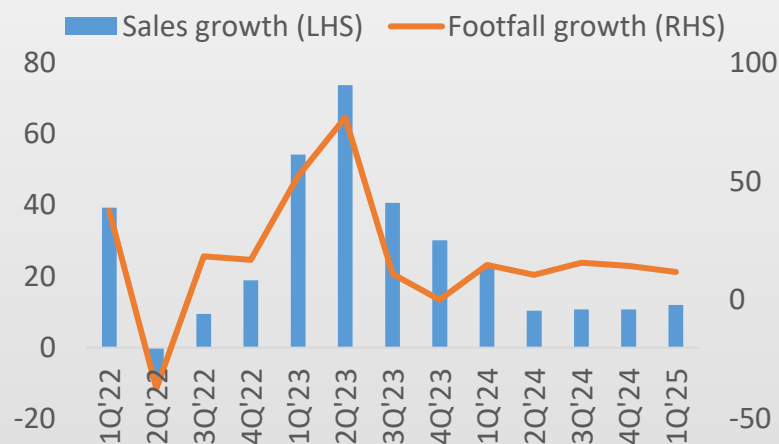


## Building Material imports are picking up

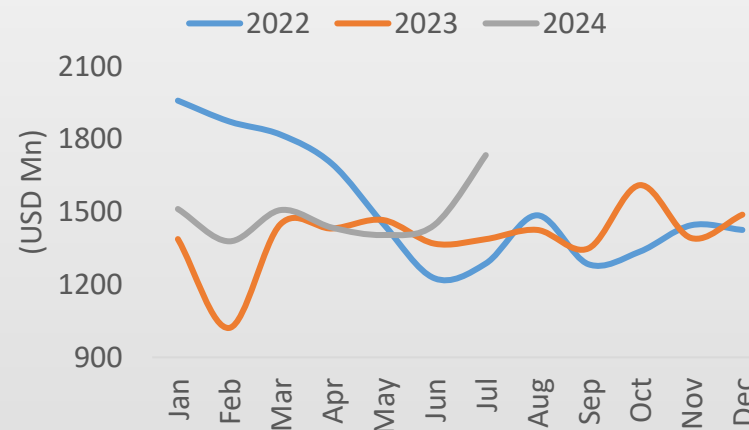


# RIISING INCOME & DEMAND TO HELP CONSUMER SEGMENT

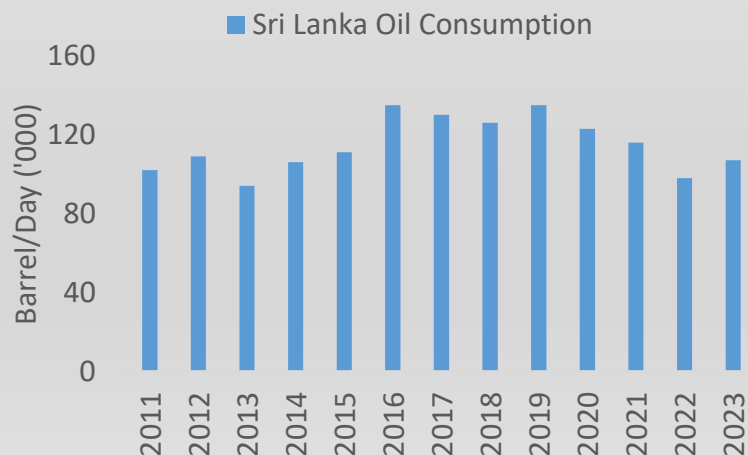
## Moden retail sales up with growing footfall



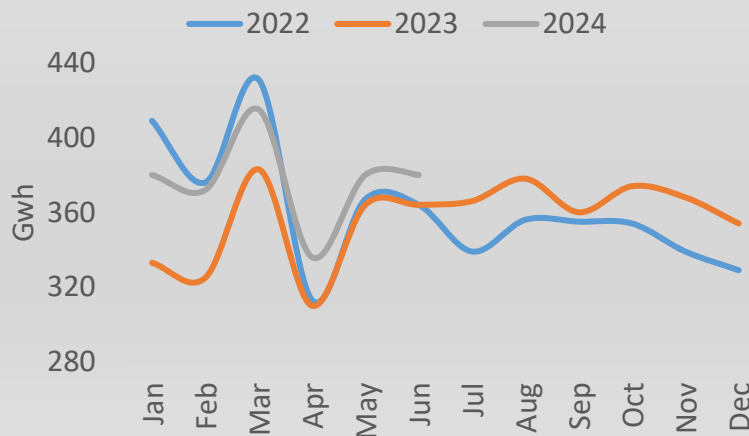
## Import bill is already picking up amid higher consumption



## Demand for fuel is gradually picking up



## Electricity usage picking up indicating higher activities



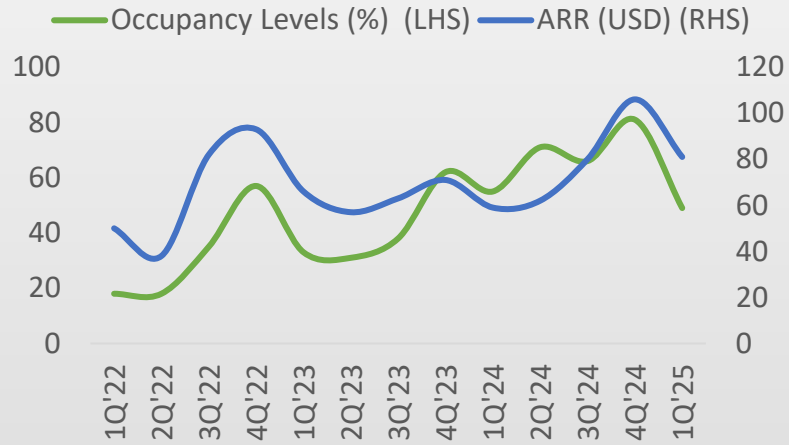
## Key beneficiaries

Ticker	Mkt Price	TTM PER(x)	PBV (x)	ROE (%)	TTM DY(%)
JKH	161.00	27.1	0.7	2.5	0.9
HHL	68.60	6.9	1.0	14.0	5.0
CARG	375.00	15.8	3.1	19.5	2.8
CTC	1179.25	7.5	21.4	285.6	13.3
CCS	50.00	11.1	2.3	20.4	6.1
LLUB	115.00	7.3	3.6	49.8	16.5
LIOC	100.50	3.5	0.7	19.8	5.0
LION	989.50	9.0	2.8	30.4	4.4
DIST	25.50	8.5	12.4	145.7	11.1
SUN	58.20	6.4	1.5	24.1	5.2
CIC.N	66.10	2.4	0.7	28.9	3.8

Prices as at 10.09.2024

# TOURISM; LOW HANGING FRUIT FOR ECONOMIC REVIVAL

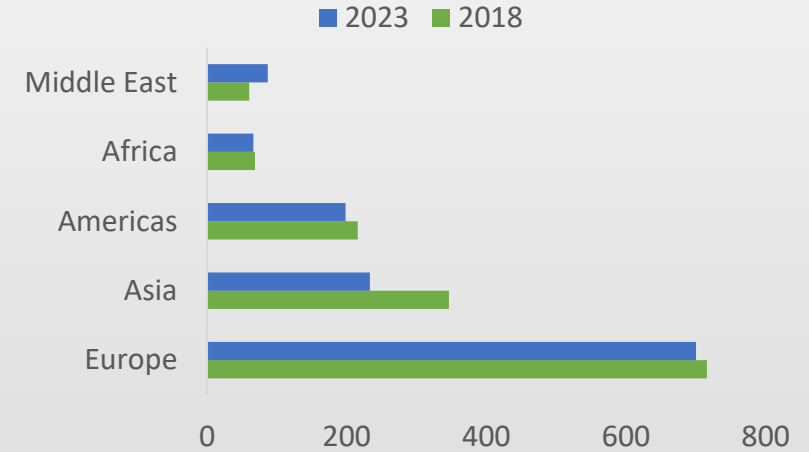
## Occupancy levels & rates improving steadily



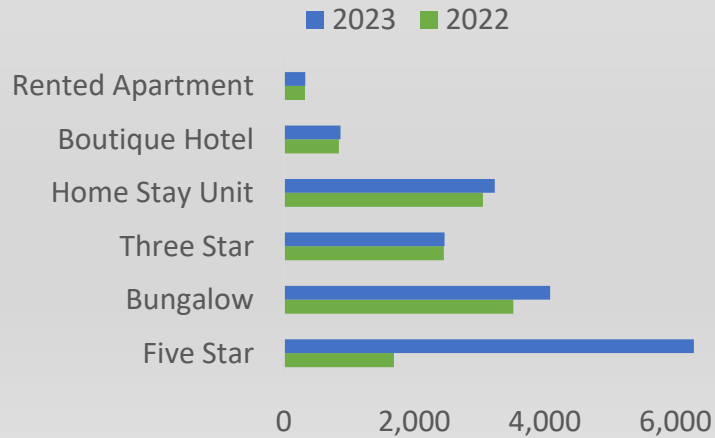
## Tourism industry experiences a massive growth



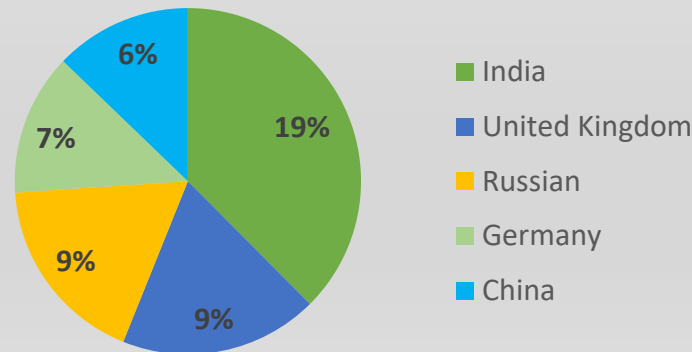
## International tourist arrivals near pre-pandemic levels



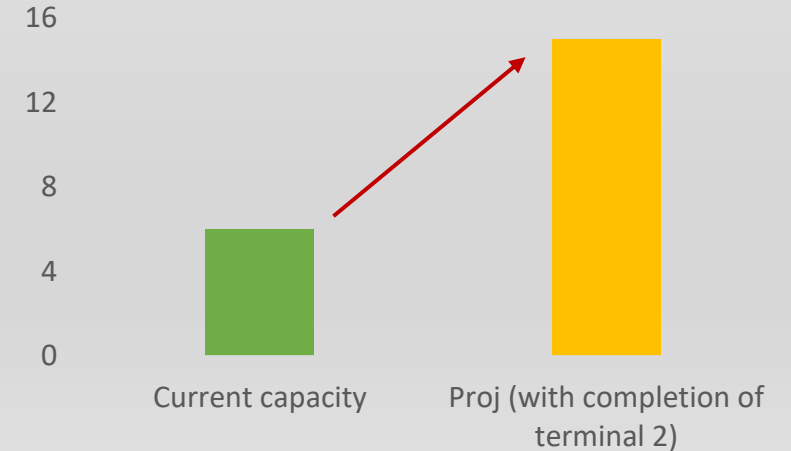
## New room inventories are on the rise



## India, UK, Russia amongst the top 3 arrivals

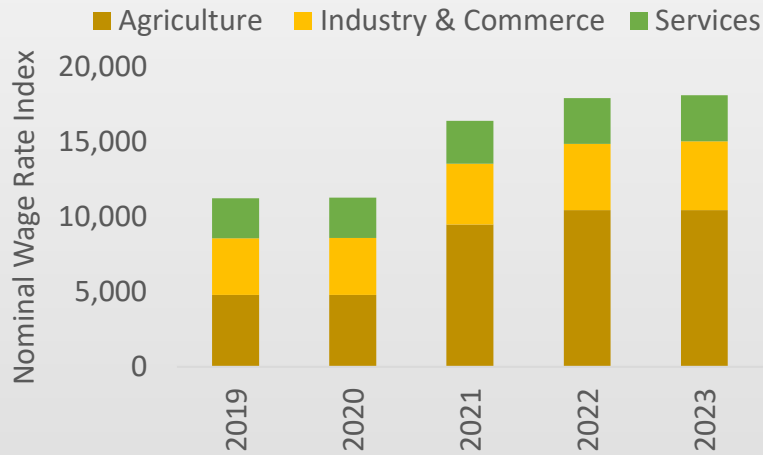


## BIA enhances capacity to facilitate more arrivals

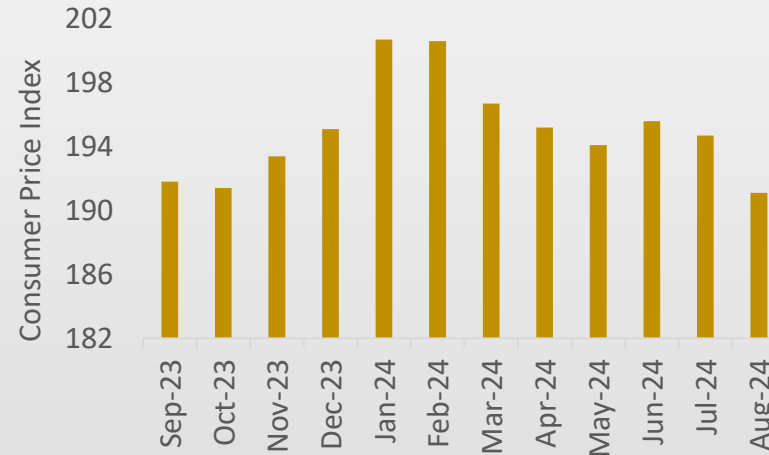


# MANY OTHER INDICATORS SHOW POSITIVE MOMENTUM

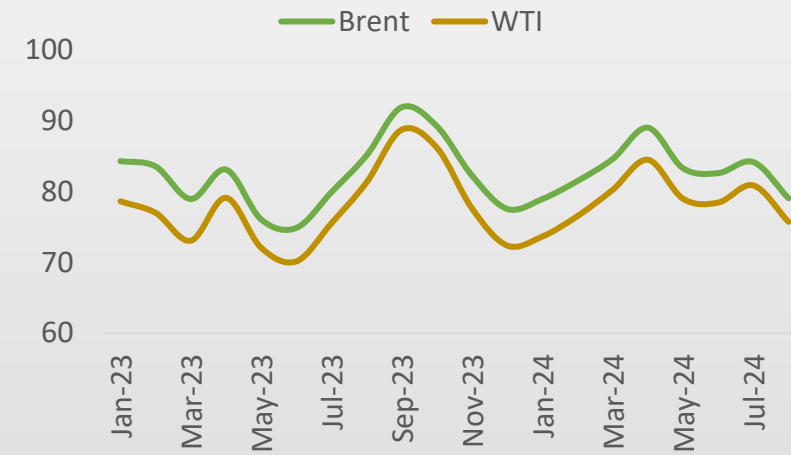
**Rising wage rates to drive up expenditures**



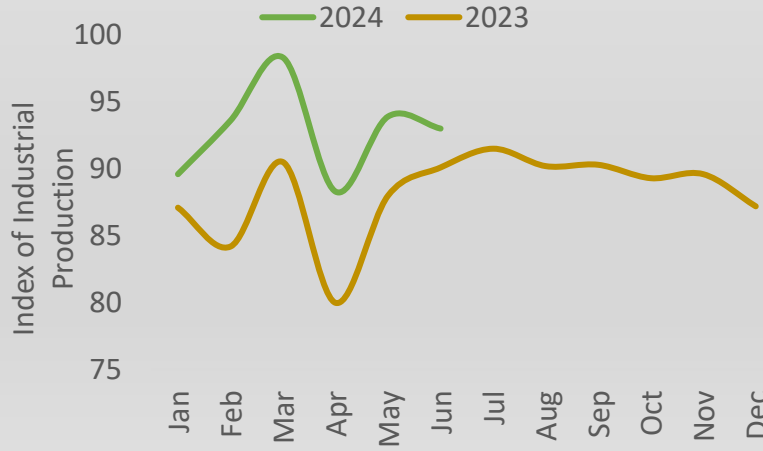
**Falling CPI to boost consumer's purchasing power**



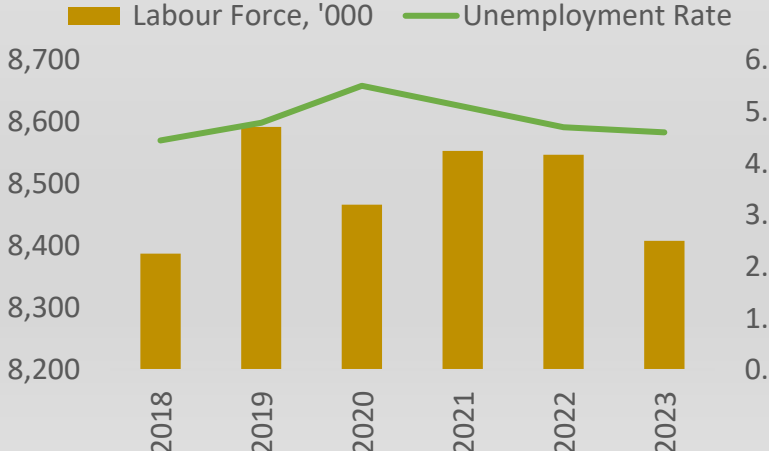
**Crude oil prices are on a downward trend**



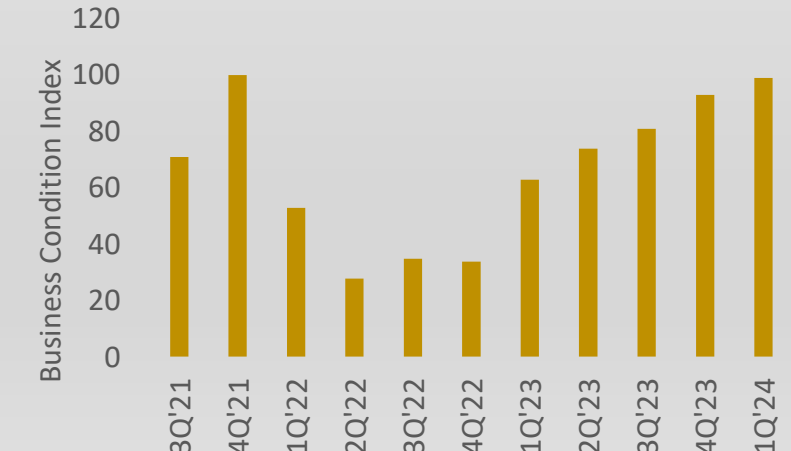
**Rising IIP signals growing consumer demand**



**Unemployment rate is steadily declining**



**Business outlook continues to strengthen**





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