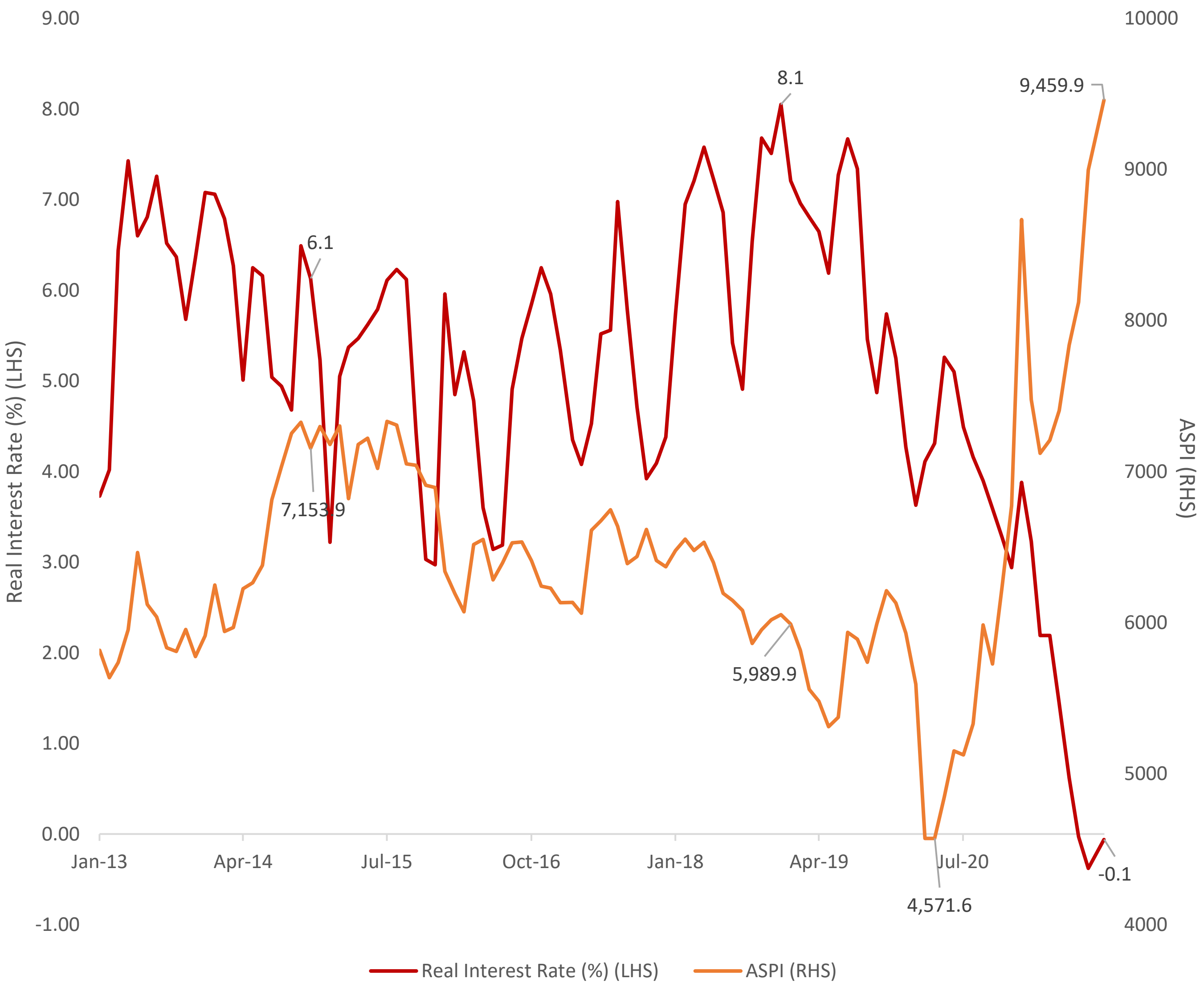
Real rates to remain muted for a while, market reaction to a rate hike seem too premature

Nation Lanka Equities (Pvt) Ltd.



- Market remained in a weaker footing citing a possible hike in policy rates. Despite the decision, AWFDR (Average Weighted Fixed Deposit Rate) has hardly seen an uptick and remained at 5.6% levels due to banking sector having excess liquidity. This has also seen the country moving to low or negative real returns on the back of inflation hovering around >5%.

- We are of the view even in an event AWFDR increases by another 100bps (to 6.5%-7.0%), the real interest rates to remain subdued with inflationary pressure likely rising over >7% specially after recent upward adjustments in essential commodity prices.

- **We believe in order to see some shift from equity markets, the real interest rates should least derive a minimum return of >5%, which intern should see an uptick of closer to 600bps in deposit rates, which is highly unlikely in the near term in our view. Therefore, moving from equity markets right away which has generated over >40% YTD return is thus believed to be unwarranted.**