



# INTEREST RATE FORECAST STOCK MARKET TO BENEFIT STRONGLY FROM FURTHER RATE CUTS

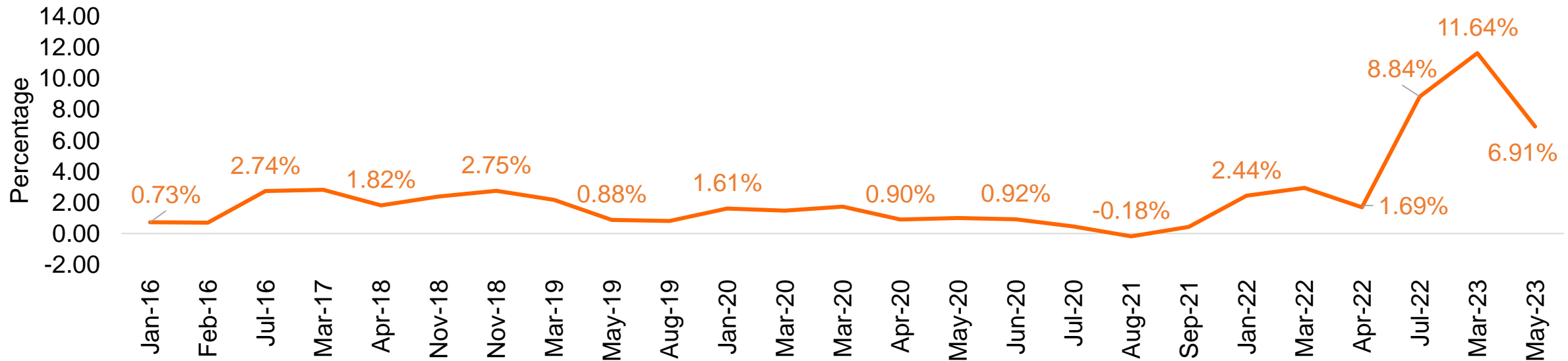
 Capital Trust

Capital TRUST Research (Pvt) Ltd.  
A Capital TRUST Group Company

# RISK PREMIUMS ON 364-DAY T-BILL WAS ON AVERAGE c. 1.50%

- The Risk Premiums on 364-day T-Bills for the 5-year period between 2017 and 2022, prior to the Economic crisis in April 2022 was **only c. 1.50%** , compared to the Risk premium of **6.91%** on 31st May 2023. Risk Premium for the 364-day T-Bill rate is calculated as the difference between Average Standing Deposit Facility Rate (SDFR) and the Standing Lending Facility Rate (SLFR) and the 364-Day T-Bill Rate.
- When the Ministry of Finance finalises the Domestic Debt Optimisation Framework, we expect **Risk Premiums to normalise closer to the historical 5-year average of 1.50%**. This will result in a further decline in the Yields across Government Securities.

364-Day T-Bill Risk Premium (%)



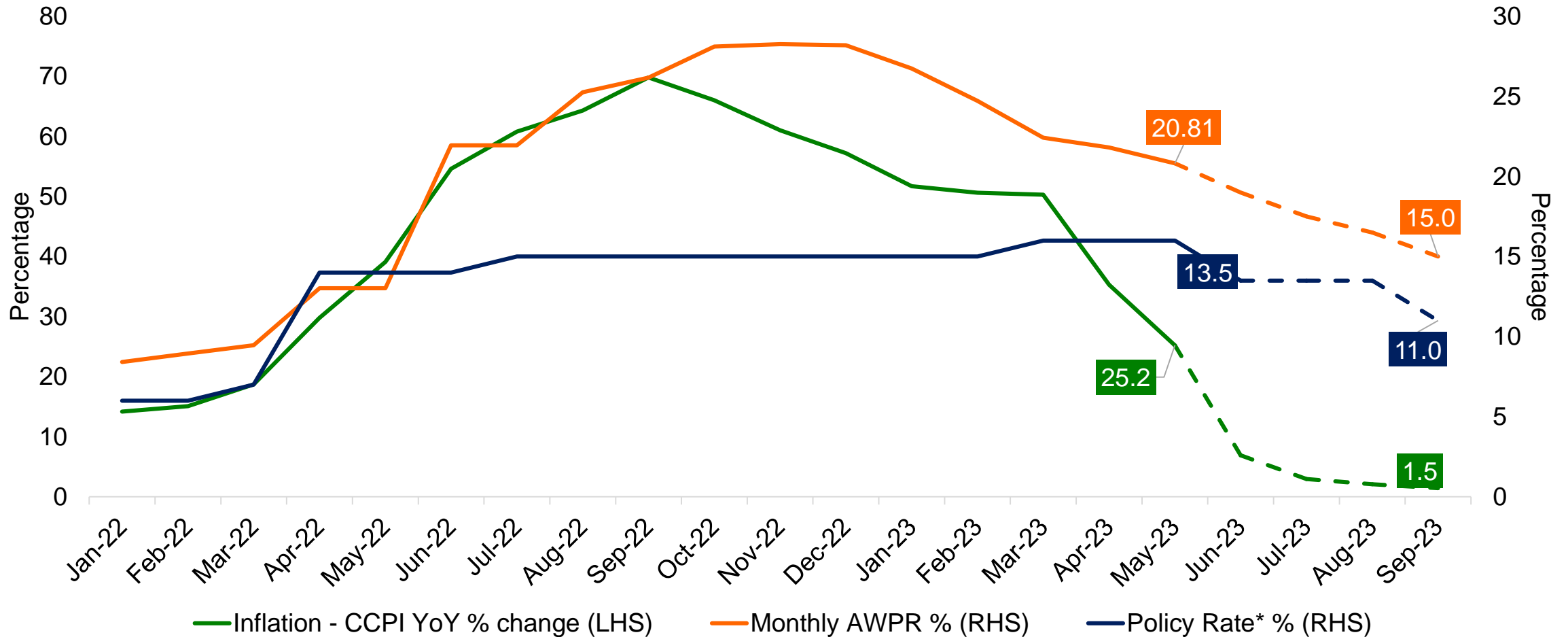
Source : Central Bank of Sri Lanka

\*Average Risk Premium of 1.50% is calculated for the period between January 2016 to March 2022

# AWPR FORECAST TO DECREASE BELOW 15.00%

- Inflation is expected to decline to **single digit by end July 2023** as mentioned by the Governor. Therefore, we forecast **Policy Rates to decline a further 250 bps** with the SDFR and the SLFR to decline to 11.5% and 12.5% **over the next 3-months**.
- With the expected decline in Policy Rates and normalisation of Risk Premiums **upon the completion of the DDO, we forecast 1-Yr T-Bills to decrease to c. 13.00% over the next three months**.
- We expect a similar trend to be followed on long term maturities with **the Bond-Yield Curve** across various maturities to **decline**.
- With the expected decline in 1-Yr T-Bill Rates to c.13.00%, we forecast Average Weighted Prime Lending Rates (**AWPR**) **to decrease below 15.00%** over the next three months.
- The following forecast assumes that the DDO Framework will be completed over the next 3 months.
- With the expected decline in AWPR below 15.00%, we can expect **GDP growth of 5% in 4Q2023** and **result in a pick up in Corporate Earnings**.
- Against this backdrop, **Equities are expected to perform** due to lower Interest Rates on Margin Facilities, movement of funds from Fixed Income to Equities, Expectations of Earnings Growth due to a pick up in Economic Activity and the Rerating of Market Multiples.

# AWPR FORECAST TO DECREASE BELOW 15.00%



Source : Central Bank of Sri Lanka

\*Policy Rate is the average value of Standing Deposit Facility Rate (SDFR) and Standing Deposit Lending Rate (SLFR)

# GOVERNMENT SECURITY YIELDS DECLINE YTD IN 2023

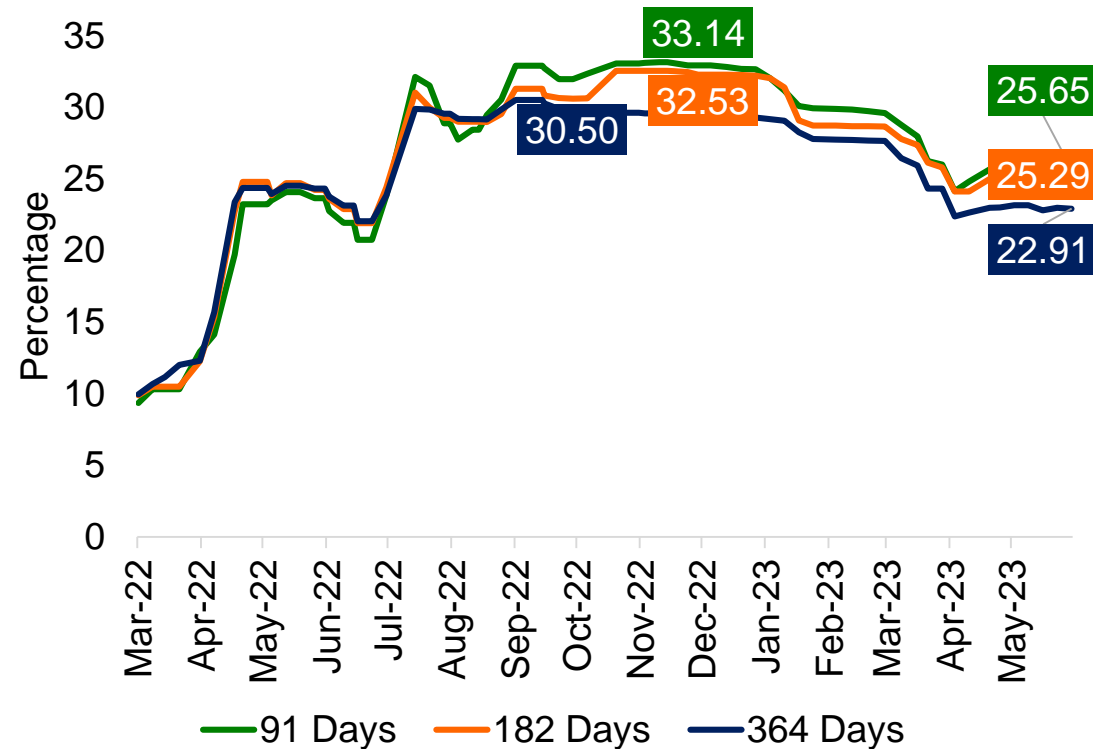
The 91 day, 182 day and 364 day T-bill Yields are down **749 bps, 724 bps** and **759 bps** since the Yields peaked in September and October 2022.

Secondary market Risk Premiums on short term (<1 year) maturities declined by **399-455 bps** between 31<sup>st</sup> March 2023 to 2<sup>nd</sup> June 2023.

Similarly Risk Premiums for medium term (<2years-<5years) and longer term maturities (<6 year-<10years) declined by **97-236 bps** and **205-486 bps** for the same period respectively.

Which should Increase Trading Income for Financial Institutions such as Banks and Primary Dealers in 2QCY2023.

T-Bill Auction - Weighted Average Yields



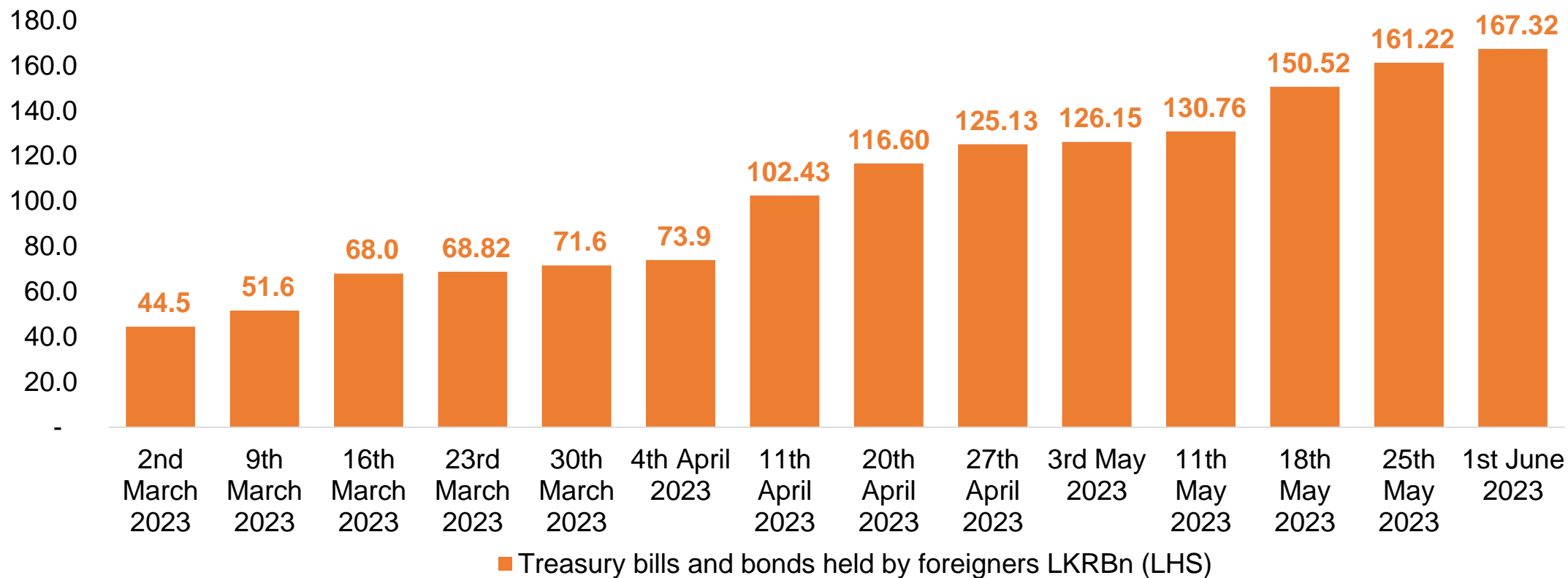
Secondary Market Yields

Duration	Average Yields		Movement (bps) 28th Dec 22-30th Mar 23	Yields on 2nd Jun 2023	Movement (bps) 30th Mar 23- 2nd Jun 23
	28th Dec 2022	30th Mar 2023			
91 Day	30.89	25.49	-540	21.50	-399
182 Day	29.50	25.45	-405	20.00	-545
364 Day	28.50	23.98	-452	19.50	-448
< 2 Years	28.22	28.13	-9	26.50	-163
< 3 Years	28.39	26.85	-154	25.88	-97
< 4 Years	27.62	26.91	-71	24.75	-216
< 5 Years	26.76	25.86	-90	23.50	-236
< 6 Years	25.98	25.05	-93	23.00	-205
< 8 Years	26.01	24.65	-136	21.50	-315
< 10 Years	26.08	23.86	-222	19.00	-486

# INCREASED FOREIGN INTEREST IN TREASURY SECURITIES

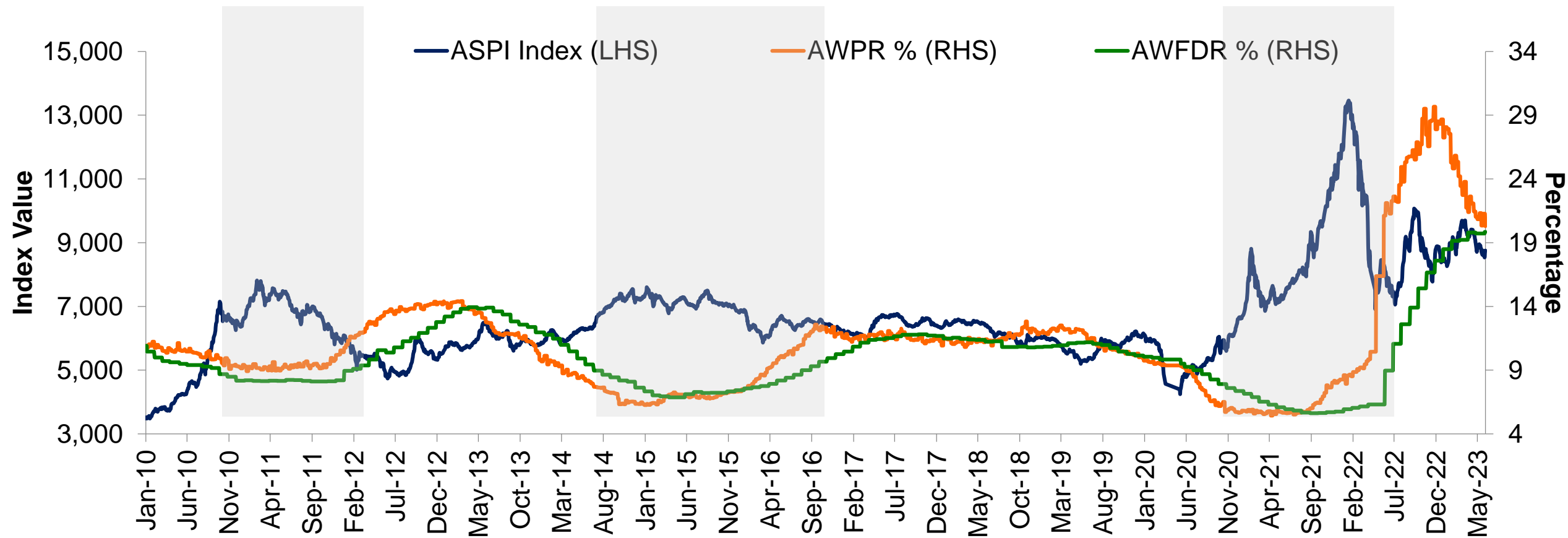
During the week ending 1<sup>st</sup> June 2023, outstanding stock of T-bills and T-bonds held by foreigners increased by **3.8%** in LKR terms compared to the previous week.

With investors moving out of risky assets amid crisis of leading global banks, Sri Lankan Treasury Securities have seen an increase of over **LKR 122.85 Bn** held by foreigners from 2<sup>nd</sup> March 2023 to 1<sup>st</sup> June 2023.

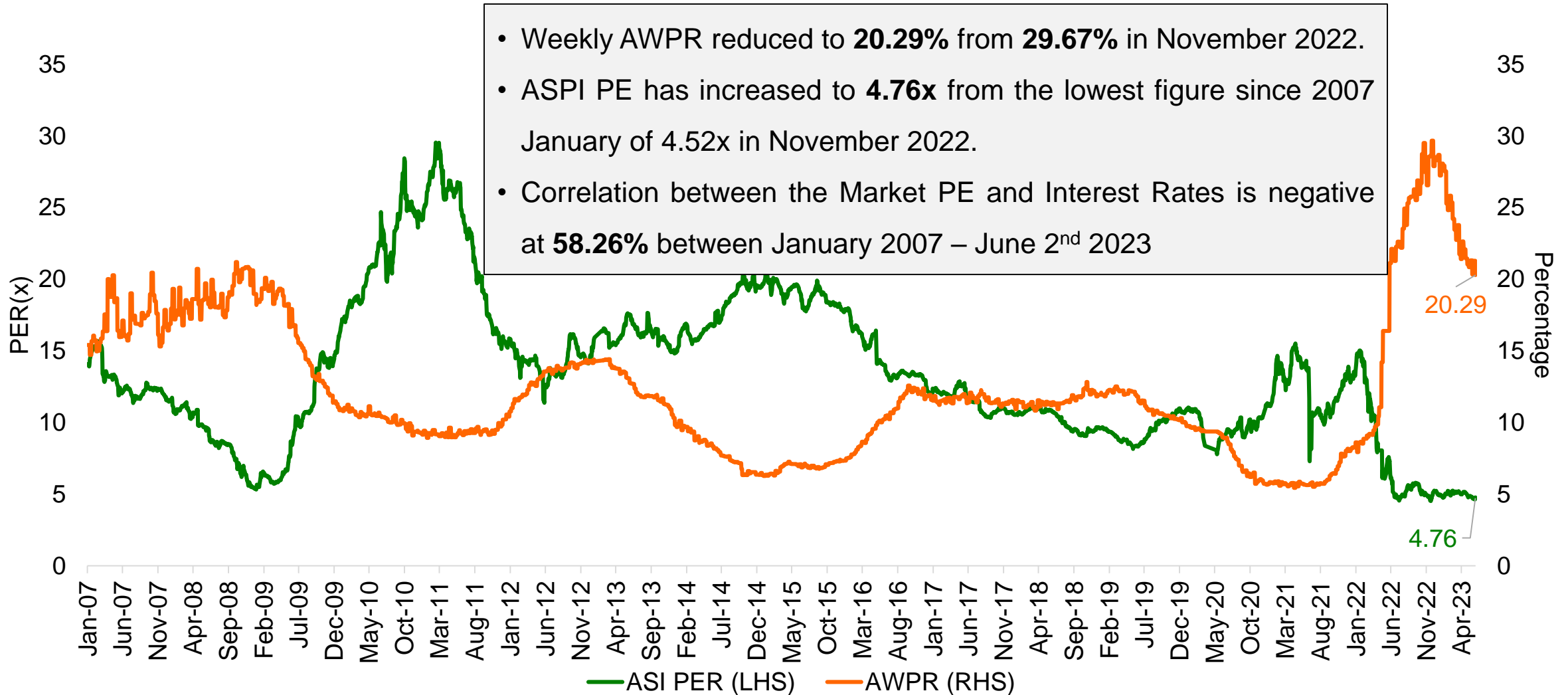


# EQUITIES EXPECTED TO PROVIDE HIGHER RETURNS

When interest rates decreased historically, the All Share Price Index (ASPI) provided higher Returns reflecting the inverse relationship between the ASPI and Average Weighted Prime Lending Rate (AWPR) Average Weighted Fixed Deposit Rate (AWFDR).



# EQUITIES TO BECOME MORE ATTRACTIVE

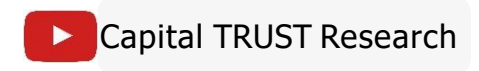
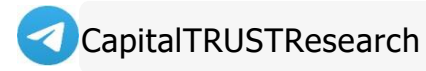
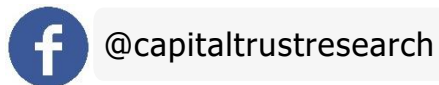




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