

# Equity Strategy Perspectives

Upgrading our Positive View on Equity for 2017

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*9<sup>th</sup> June 2017*

## Getting more positive on the market

Our view of where the market will end the year has continued to get more positive over recent months and as such we are upgrading the probabilities of where we expect the market to stand at year end.

In January, when we last upgraded our end-2017 probabilities for the market, the probability we placed for the market being over 7,000 was 30%. We have now increased the probability of this scenario to 40%, while the overall probability that the market would be below 6,000 has been reduced from 25% to 15%. The 6,000-7,000 range probability remains unchanged at 45%.

### Updated ASPI end- 2017 view

ASPI Range	Mid-Point of view	Probabilities (given on 25th Jan)	Updated probabilities (9 <sup>th</sup> June)
Over 7000	7500	30%	40%
7000-6000	6500	45%	45%
6000-5000	5500	15%	10%
below 5000	4500	10%	5%

## Positive rates view to support equities outlook

One of the key reasons for the upgrade is that our positive expectations for rates, which we have been highlighting since end 2016, have now become more accepted. Economic fundamentals have seen an improvement in recent months, with investor sentiment also gradually turning positive. The favourable rate and high demand for the sovereign bond issued in early May is a clear indication of a more positive investor attitude towards the domestic market.

Emerging and frontier markets have also been seeing fund inflows during the first few months of 2017 on positive global growth prospects, a commodity rally and a more dovish outlook by the US Federal Reserve. (See [Page 4](#) & [6](#))

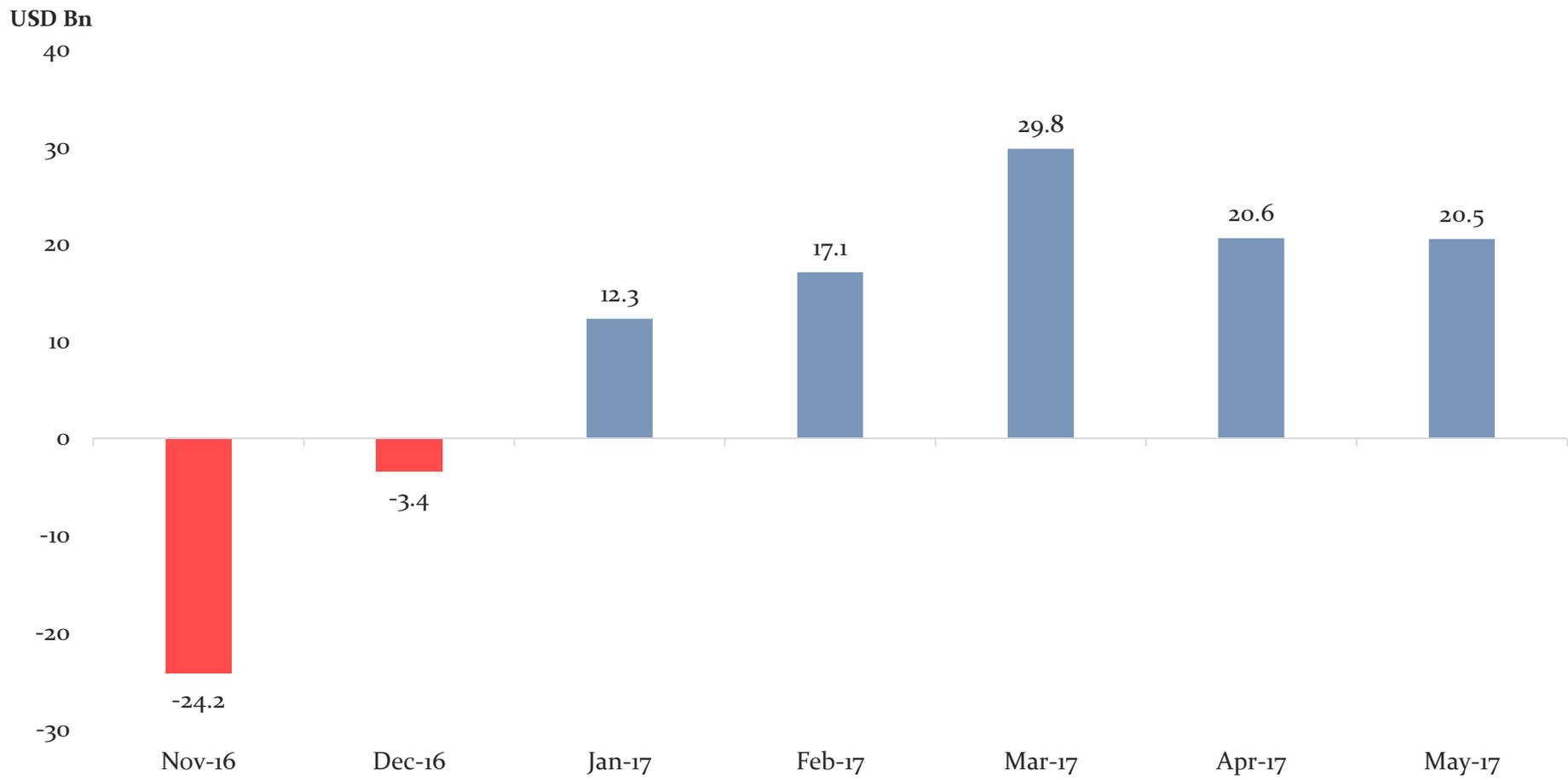
This has resulted in inflows into Sri Lankan equities, with the CSE seeing up to Rs. 19.42 bn in net foreign buying during the first 5 months of the year, despite a marginal net outflow in January. April in particular saw a surge in foreign buying, though this pace has reduced in May. (See [Page 8](#))

This positive global investor sentiment has also seen foreign inflows trickle in to the Sri Lankan government securities market, with the pace of inflows accelerating during the month of May. Since reaching its lowest point in mid-February, foreign holdings of local government securities have recorded a net inflow of US\$ 152mn (Rs. 23bn) by the end of May. Should this pace of inflows continue, it could weigh positively on market interest rates.

Overall, a key reason for our positive rates view is the reduced level of debt obligations in 2017, particularly during the second half of the year. Given this, in our opinion, the sovereign issuance together with the syndicated loan and the IMF program should further assist in refinancing the remaining debt for the year. However, it should be noted that a turn in global financial markets could change our base views.

As such, given the positive global and local developments we are increasing our positive outlook on the local equities market.

# Emerging Market inflows to both debt and equity – in the positive



Source - IIF

## Strong first quarter might be a high point for EMs

According to data from the Institute for International Finance (IIF), portfolio inflows to Emerging Markets (EMs) were [around \\$100 billion](#) in the first five months of the year. This has been helped by a record EM debt issuance in the year so far, [almost a \\$100 billion](#).

“Global markets have been so positive this year that we are seeing a lot of front-loading of supply, people are particularly aware that US rates are rising and that affects the rate at which they can borrow” - *Rajiv Shah, BNP Paribas* ([FT](#))

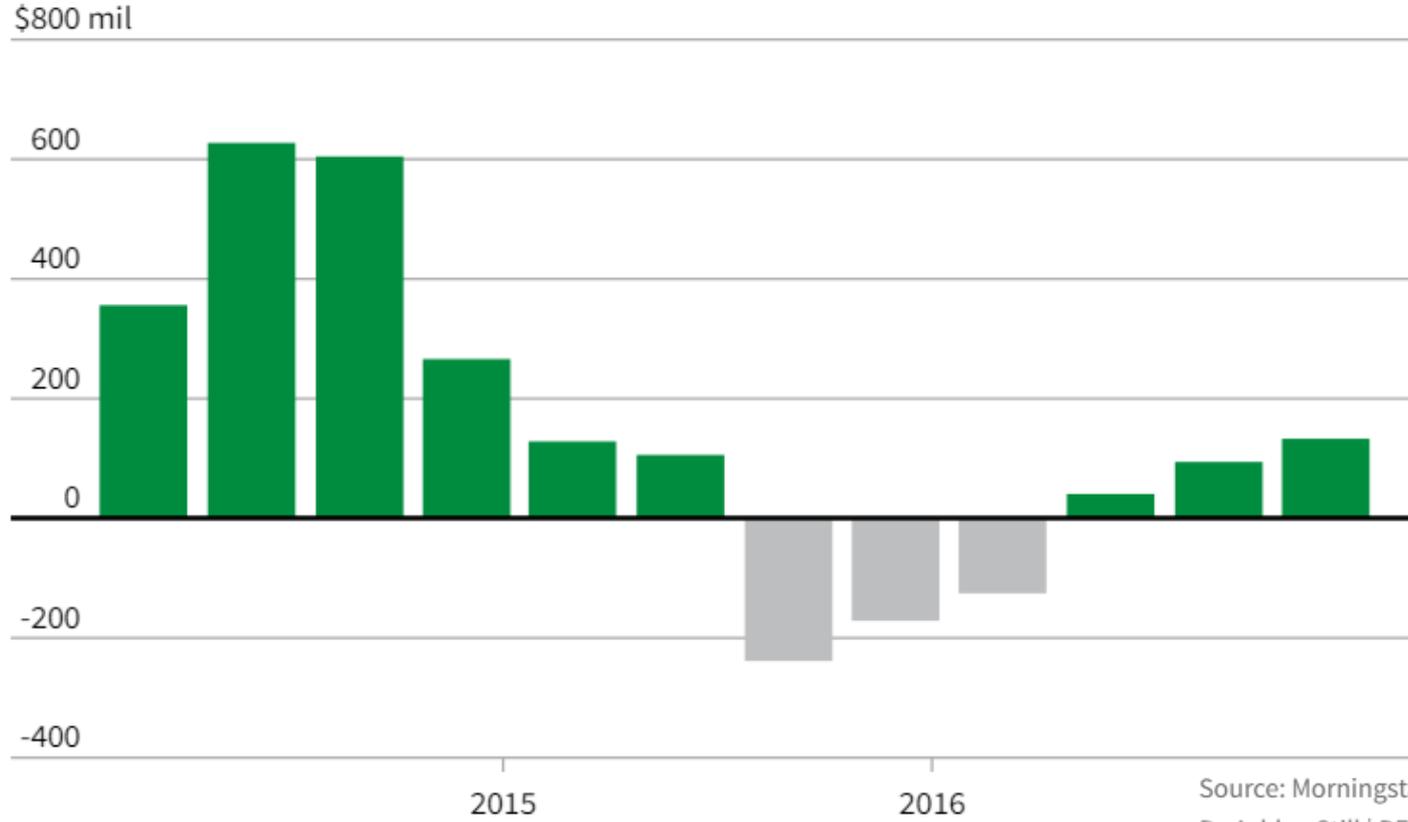
The EM advance may have started to slow in April and will level out at around 4 percent this year. “We had anticipated that Q1 would mark the high point of the EM recovery,” - *Neil Shearing, Capital Economics* ([Bloomberg](#))

“EMs have performed well and remain an enticing, and under-owned, owned asset class despite their strong earnings and attractive valuations” - *Sean Taylor, Deutsche Asset Management* ([CNBC](#))

“Large institutional investors have without fail provided support for the asset class through down and up markets. This speaks to their longer- term view that emerging market debt is a durable investment to consider” - *Owi Ruivivar, Goldman Sachs Asset Management* ([Straits Times](#))

## INVESTORS WADE BACK IN

After a brief downturn, frontier market funds are again seeing positive net flows.



Source: Morningstar Inc.  
By Ashlyn Still | REUTERS GRAPHICS

Since the second quarter of 2016, net inflows for actively managed frontier market equity funds have totalled \$267.7 million, after three consecutive quarters of overall outflows.

So far this year, MSCI's frontier market index is up 10.3 percent, beating the S&P 500's 6.8 percent rise, which may account for revived investor interest.

The market has been helped by its relatively low correlation to US equities; MSCI's frontier index shows a 42 percent correlation to the S&P 500, compared with 91 percent for MSCI's emerging markets index, according to Reuters data.

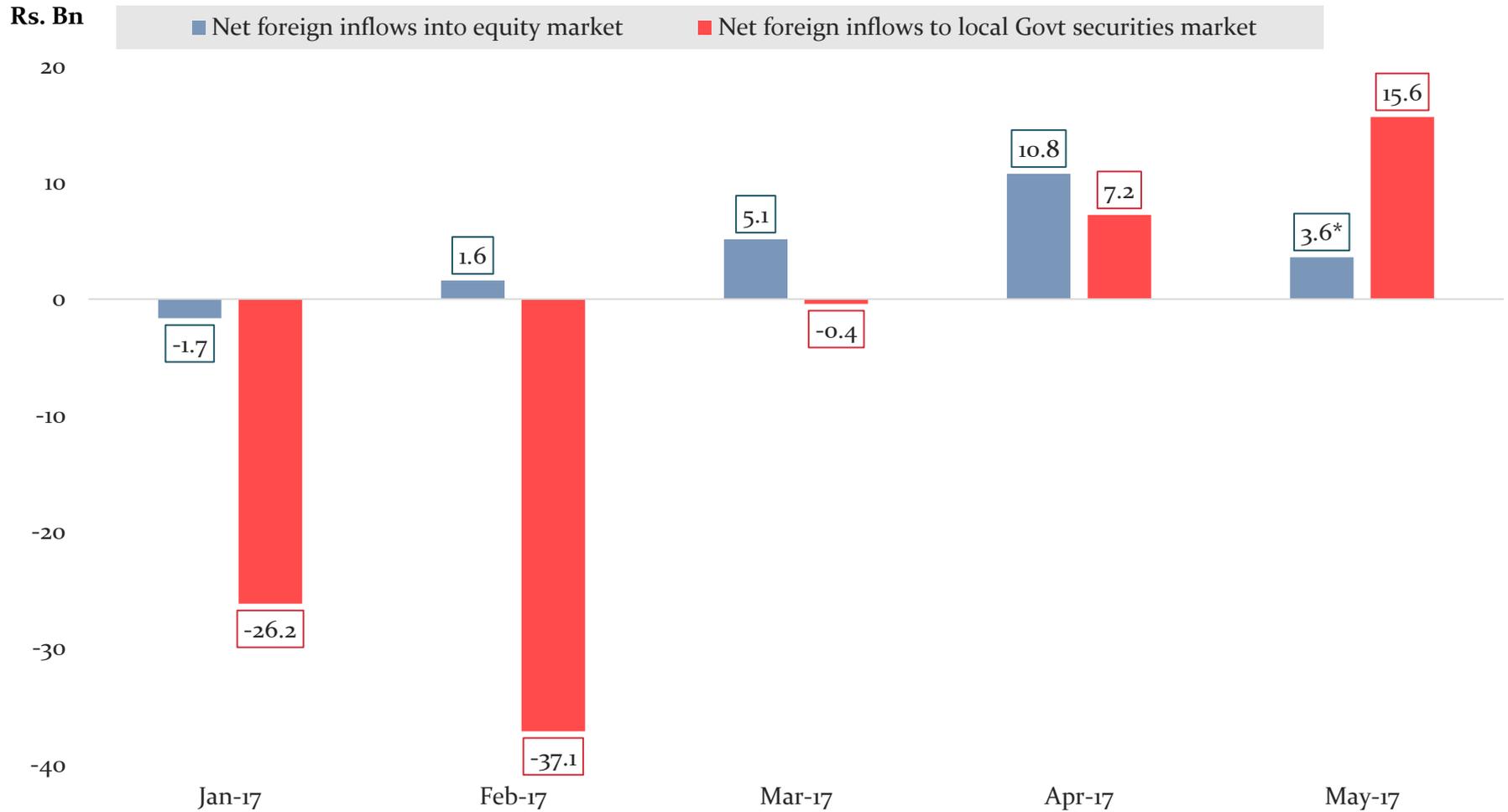
The growing uncertainty in developed markets due to events like Brexit and Donald Trump's upset election has encouraged investors to seek assets that won't be affected by U.S. or European stocks taking a dive.

- [\*Reuters\*](#)

However, there is some uncertainty with regards to the future of equities within the MSCI Frontier Market Index. The upgrade of Pakistan to the Emerging Market index, with the possibility of Argentina and Nigeria following on, risks the market losing further liquidity.

- [\*Bloomberg\*](#)

# Monthly net foreign inflows into local equity and debt markets



Source – CBSL, CSE, \*Reuters

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