



MONTHLY ECONOMIC UPDATE January

Economy at a glance for January 2022

Economy up to a modest start

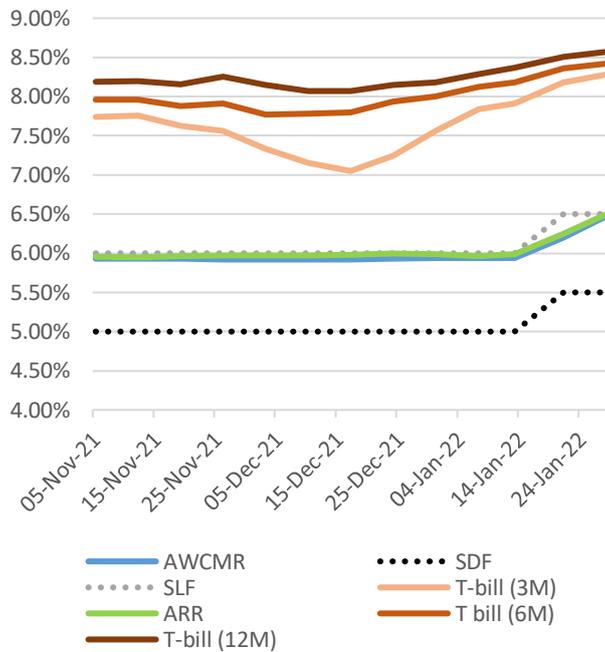
Highlights

- SDF and SLF rates were increased by 50 bps in January by the CBSL, stimulating further monetary tightening.
- Liquidity deficit in the money market gradually widened during the month and reached a new low of LKR 466 Bn by the end of the month.
- The rate hike triggered a substantial growth in the T-bill yields in both primary and secondary markets in January.
- Inflation continued to rise during January (Y/Y) as headline inflation increased to 14.2%.
- Sri Lanka had over USD 1.1 Bn forex obligations pending for January. This included the settlement of USD 500 Mn sovereign bond, which was repaid on the 18th of January.
- CBSL exploited the strong rebound in gold and sold about USD 83 Mn and by the end of the month total reserves stood at around USD 2.3 Bn.
- The strong gains that were evident in the stock market at the start of the year were short lived as foreign investors began exiting the market following the rating downgrade by S&P.
- Tourism generated about USD 10 Mn in the month showcasing consistent recovery.
- Global oil prices rose sharply in January, reaching a seven year high.

Interest Rates

Short-term rates

Figure 1: Treasury bill yield and money market rates



Notes: AWCMR- Average Weighted Call Money Rate, SDFR- Standing Deposit Facility Rate, SLFR- Standing Lending Facility Rate, T-bill yields are for the secondary market, ARR – simple average of daily repo rates
Source: CBSL

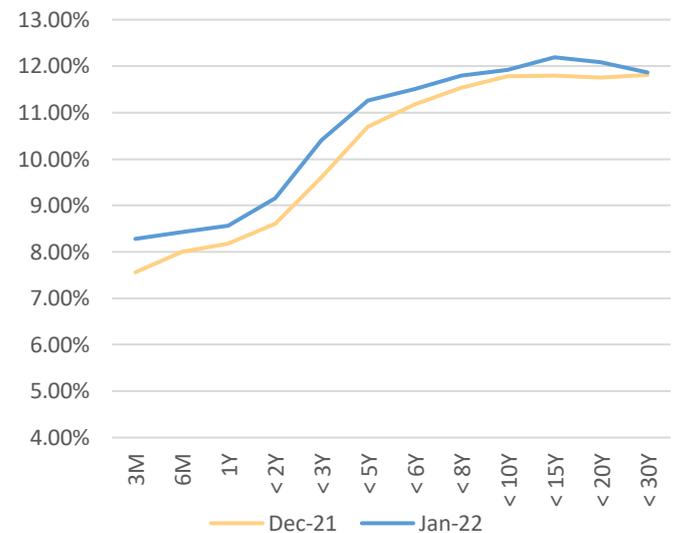
January saw further monetary tightening by the Central Bank as they increased the SDF and SLF rates by 50 bps. The Central Bank stated the reason for the rate hike was to “curtail the possible build of underlying demand pressures in the economy which would in turn ease pressures in the external sector.” This resulted in call and repo rates moving towards the new upper bound of the policy corridor.

Liquidity deficit in the money market gradually widened and reached a new low of LKR 466 Bn towards the end of the month. Borrowing through the Standing Lending Facility (SLF) crossed LKR 500 Bn/day. The Central Bank also absorbed liquidity through short-term repos. At the same time the CBSL injected about LKR 150 Bn on a more permanent basis by purchasing treasuries.

The T-bill yields in both primary and secondary markets increased sharply this month following the rate hike. 3M T-bills in primary auctions continued to out-perform 6M and 12M. However, increase in yields of the 3M T-bills were observed as market participants were expecting more rate hikes in the near term. Activity levels in the secondary market also rose during the month.

Long-term rates

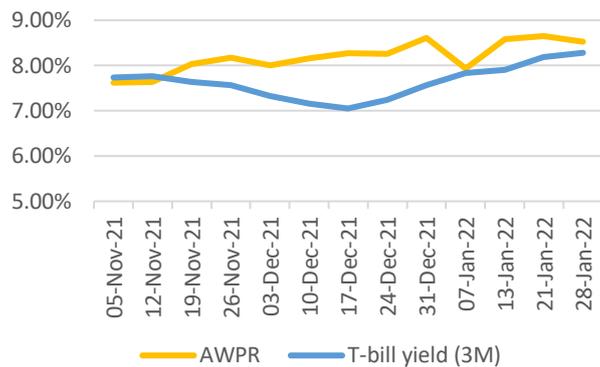
Figure 2: Yield curve of treasuries



Notes: Yields are based on the weekly average prevailed at the last week of the month, shorter end – less than 2Y, mid/intermediate tenor – 2 to 10Y, longer tenor – above 10Y, Source: CBSL

The overall yield curve shifted upwards with near-term maturities experiencing a higher shift. The market absorbed LKR 90 Bn in fresh bond issuances amid healthy volumes in the secondary market.

Figure 3: AWPR¹ and 3M T-bill yield

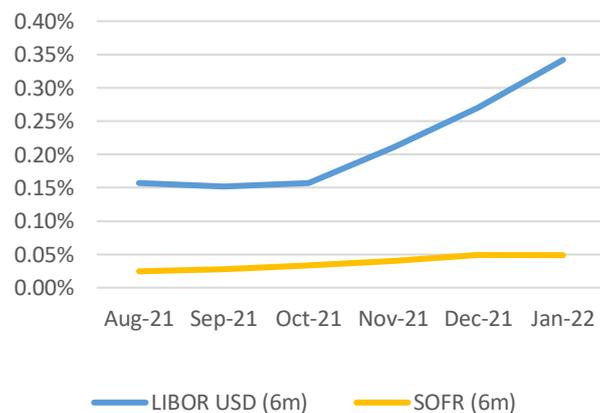


Note: T-bill yield for secondary market, Source: CBSL

The private sector credit increased by LKR 60.5 Bn (M/M) in November, a faster rate than the two earlier months, as businesses were heading for the festive season. Reserve money expansion in January was relatively strong. Therefore, private credit may have continued to expand at a modest rate during the said time period. The AWPR jumped over 70 bps following the rate hike.

International rates

Figure 4: Month open international lending rates



Notes: The SOFR Averages are compounded averages of the SOFR over rolling 180-calendar day periods. Source: New York Federal Reserve and global-rates.com

US short term treasury yields rose at the start of the month after the Fed hinted that the initial interest rate hikes may come as soon as March following

positive sentiments from December jobs report. Short term yields rose to a 2-year high during the middle of the month as consumer prices rose further to 7%. Yields on the medium and long-term treasuries declined marginally after successful bond auctions which saw rates slightly rise. Treasury yields rose again towards the end of the month as the Fed reaffirmed expectations for the rate hike in March.

Reflecting expectation for rate hikes, LIBOR USD increased during January. Nevertheless, LIBOR USD's replacement, SOFR remained more-or-less flat during the said period.

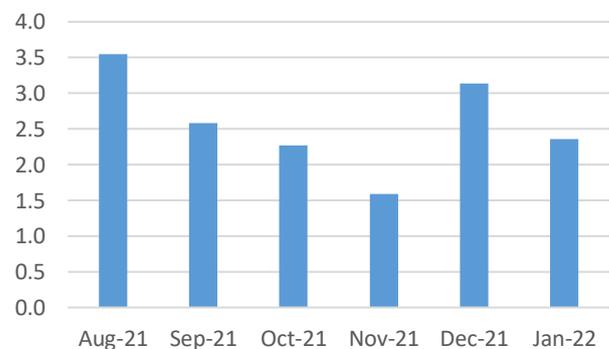
The yields of the SLISBs were mixed with near-term maturities posting gains while longer dated maturities posted a decrease amid the downgrade of Sri Lanka's Long-Term Foreign-Currency Issuer Default Rating (IDR) to 'CC', from 'CCC' by Fitch.

External Sector

Sri Lanka's trade deficit widened markedly to over USD 1 Bn in December as merchandize imports shot up to around USD 2.2 Bn. Increase in the fuel bill is the main contributor to increase in imports.

Tourism brought about USD 110 Mn in January. Net capital outflow from equities (-USD 13 Mn) continued while treasuries managed to record a minor inflow (+USD 4 Mn). The CBSL's intervention in the forex market caused USD 231 Mn net outflow from the gross official reserves.

Figure 5: Gross official reserves (Mn USD)

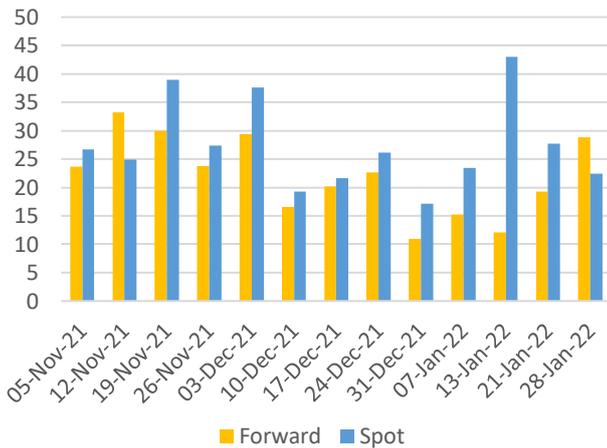


Source: CBSL

¹ AWPR is calculated based on the submissions made by the commercial banks to the CBSL on the rates offered to customers who borrowed more than LKR 10 Mn for less than three months. Page | 3

Total forex obligations pending for January was over USD 1.1 Bn including the settlement of USD 500 Mn sovereign bond. The CBSL exploited the strong rebound in gold and sold down about USD 83 Mn. By the end of the month total reserves stood at around USD 2.3 Bn.

Figure 6: Interbank forex market daily avg. volumes (USD Mn)

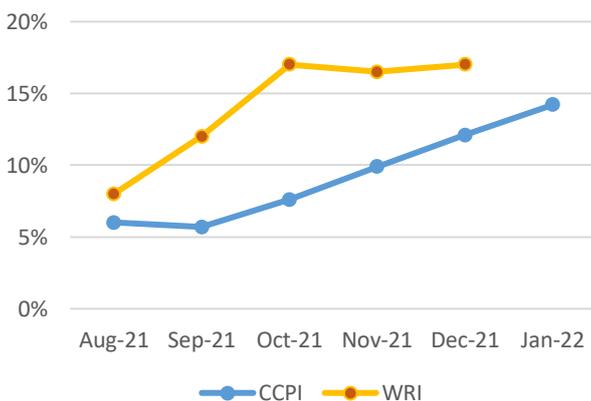


Source: CBSL

The interbank spot volumes increased in January, while forward volumes slowed down after growing in the previous month.

Prices & Wages

Figure 7: CCPI and Nominal Wage Rate Index of the informal private sector (Y/Y)



Notes: WRI (100=2012), CCPI (100=2013)
Sources: CBSL, CSD

Private sector wage remained strong in December mainly due to the second-round effects of inflation while recruitments by businesses to meet the

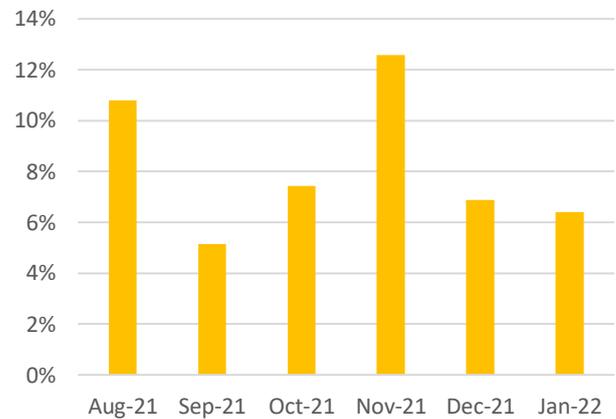
demand during festive season also fed into the wage growth.

Inflation continued to rise during January (Y/Y) as headline inflation increased to 14.2%. Food inflation rose to 25% from 22.1% due to hikes in prices of milk powder, rice, fresh fruits and bread. Non-food inflation increased to 9.2% from 7.5% due to increase in prices of transport, housing, water and electricity.

Equities

Domestic Market

Figure 8: ASPI (M/M)



Source: CSE

The stock market continued to remain subdued in January after falling sharply in the previous month. The ASPI gained 6.4% while the S&P recorded a gain of 3.9%. The market saw strong gains at the start of the year, despite the LKR 229 Bn rupee relief package announced by the government. However, the market lost momentum after the S&P rating downgrade which caused foreign investors to exit the market. Towards the end of the month, the market loss exceeded LKR 285Bn. Healthcare and Retail were the top performers. Overall PBV (Price-to-Book-Value) increased from 1.67 to 1.77 favoring sellers.

Figure 9: GICS sector performance- January

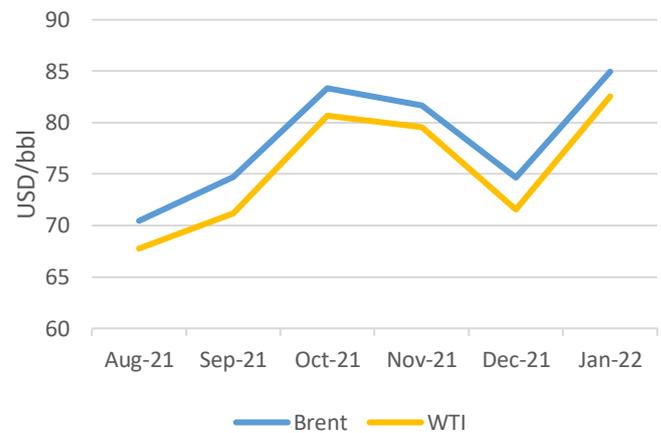
Sector	Index Points Gained
Health Care Equipment & Services	457
Retailing	408
Insurance	323
Diversified Financials	217
Capital Goods	141
Consumer Durables & Apparel	138
Telecommunication Services	118
Utilities	79
Automobiles & Components	72
Food, Beverage & Tobacco	57
Materials	49
Real Estate	27
Banks	19
Commercial & Professional Services	14
Consumer Services	10
Food & Staples Retailing	8
Household & Personal Products	-79
Energy	-156
Software Services	-215
Transportation	-3298

Global Markets

Rising treasury yields, elevated levels of inflation and the hawkish stance of the Fed ended up rattling the stock market in January. The Dow Jones dropped 3.3% while S&P500 fell by 5.3% and Nasdaq lost 9.0%. Companies within the Consumer discretionary, Technology and Communication Services experienced the largest losses. European markets remained broadly lower with Germany and France experiencing losses but the UK experiencing gains. Asian markets were mostly down as well with India, Japan and Hong Kong experiencing losses.

Commodities

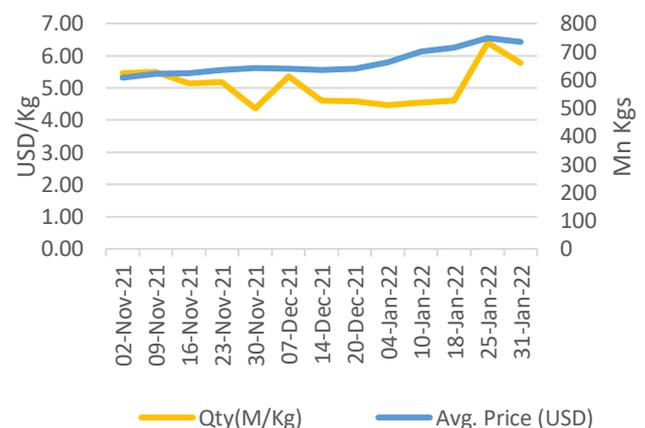
Figure 10: Crude oil price



Source: Bloomberg quoted in CBSL

Global oil prices rose sharply in January and reached a seven-year high and averaged around USD 89/barrel as investors believed that political tensions involving major producers such as UAE and Russia could result in supply shocks. Prices gained another boost towards the end of the month as the Fed announced three potential interest rate hikes in 2022.

Figure 11: Tea (All Elevations) price and quantity sold at weekly auctions

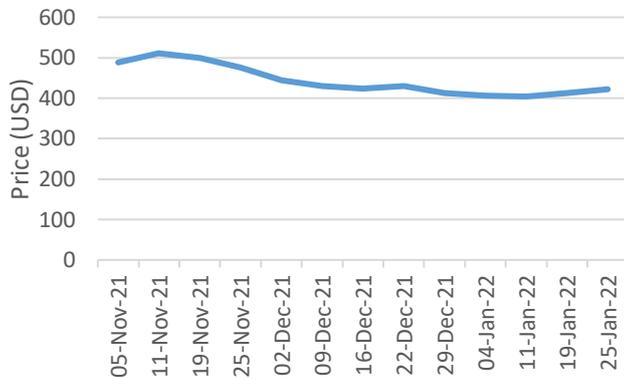


Source: Forbes & Walker

Tea prices at the Colombo auction increased in January as a result of higher overall demand following the festive season. Supply also improved due to favorable weather conditions. Prices too remained strong at international auctions.

Read ICRA Lanka's report, [Sri Lanka plantations at a fork in the road, thrive or survive?](#)

Figure 12: Rubber price weekly auctions



Note: Price of Latex 4X
Source: RRISL

Global rubber prices remained robust after declining in the previous month, as global industrial activity along with demand for rubber is unlikely to pick up anytime soon.

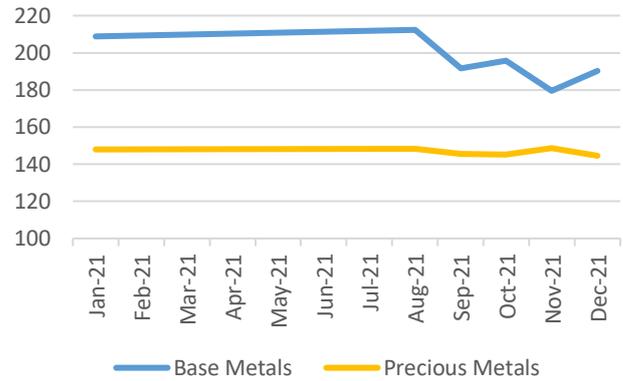
Figure 13: Coconut price weekly auctions



Source: CDA

Prices at the coconut auctions increased at the start of the month as lower harvesting volumes caused supply to fall. Prices however recovered towards the end of the month as supply recovered.

Figure 14: Metal price index (2016=100)



Notes: Base metals index includes Aluminum, Cobalt, Copper, Iron Ore, Molybdenum, Nickel, Tin, Uranium, and Zinc, precious metals index includes Gold, Silver, Palladium, and Platinum

Source: IMF

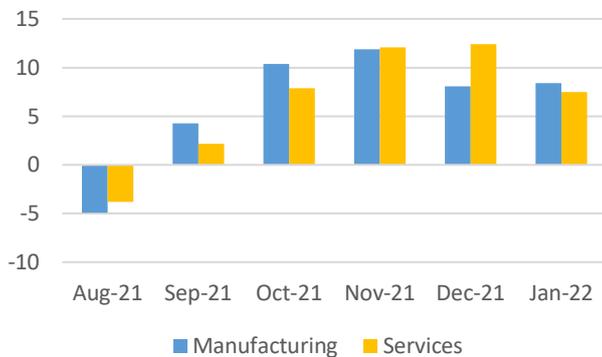
Gold prices grew strongly during the first three weeks of January as US inflation figures hit a new high of 7.5%. Further geopolitical tensions over uncertainty regarding Ukraine caused gold prices to increase further. However, gold prices slid sharply towards the end of the month as the potential Fed rate hike pushed the dollar value up making bullion less attractive for other investors.

Overall base metal prices rose during the month as a result of potential supply shocks coupled with rate hikes. Aluminum prices rose sharply on concerns about future supplies from Russia which is a major producer. Iron ore prices also saw a rise as increasing Omicron cases in Australia are likely to affect prices. Nickel prices also reached 10-year highs as a result of dwindling supply.

Read ICRA Lanka's report on the [implications of rising commodity prices for Sri Lanka.](#)

Real Sector

Figure 15: PMI deviation from point of neutrality (Index points)



Notes- negative values indicate the sector is generally contracting on a month-on-month basis while positive values indicate the sector is expanding. The strength of contraction or expansion is manifested by the magnitude of the figure. Source: CBSL

The PMI index for manufacturing and services expanded in January as well indicating the pandemic's toll on the real economy is relatively lower than in previous waves.

Read ICRA Lanka's take on what lies [beyond the pandemic for Sri Lanka](#)

Outlook for January - February

The month ahead will center around several topics; domestically from inflation worries to internationally, Ukraine crisis. The Ukraine crisis will have a major bearing on the prices of energy in the global markets. Rising oil price is already hurting the bleeding current account of the country. Rapid rise in oil prices may further burden the economy. In this setting the main challenge for the central bank is how aggressive it can be against inflation without upsetting the general functioning of the economy.

Rating Actions

Following rating actions were taken by ICRA Lanka during the month of **January**. Visit <https://www.icralanka.com/ratings/> to read the rating rationales.

Issuer	Issue	Action	Previous Rating	Current Rating
Asia Asset Finance PLC	Issuer Rating	Revised	[SL] BBB+ (Stable)	[SL] A- (Stable)
Asia Asset Finance PLC	Asset backed secure debenture program (LKR 1000 Mn)	Revised	[SL] A- (SO) (Stable)	[SL] A (SO) (Stable)
Asia Asset Finance PLC	Asset backed secure debenture program (LKR 1000 Mn)	Revised	[SL] A- (SO) (Stable)	[SL] A (SO) (Stable)
Asia Asset Finance PLC	Asset backed secure trust certificates (LKR 600 Mn)	Revised	[SL] A- (SO) (Stable)	[SL] A (SO) (Stable)
UB Finance Company	Issuer Rating	Revised	[SL] BB (Negative)	[SL] BB (Stable)
ACL Cables PLC	Issuer Rating	Revised	[SL] A+ (Stable)	[SL] AA- (Stable)
State Mortgage and Investment Bank	Issuer Rating	Reaffirmed	[SL] BBB+ (Stable)	[SL] BBB+ (Stable)
Citizen Development Business	Issuer Rating	Revised	[SL] BBB+ (Negative)	[SL] BBB+ (Negative)
Citizen Development Business	Subordinated, Unsecured, Listed, Redeemable Debenture Program (LKR 1075 Mn)	Revised	[SL] BBB (Negative)	[SL] BBB (Stable)
Citizen Development Business	Subordinated, Unsecured, Listed, Redeemable Debenture Program (LKR 928 Mn)	Revised	[SL] BBB (Negative)	[SL] BBB (Stable)
Citizen Development Business	Subordinated Guaranteed Listed Redeemable Debenture Program (LKR 2000 Mn)	Revised	[SL] BBB (Negative)	[SL] BBB (Stable)
Softlogic Holdings PLC	Issuer Rating	Reaffirmed	[SL] BBB (Negative)	[SL] BBB (Negative)
Softlogic Holdings PLC	Senior, unsecured, non-listed, redeemable, debenture program	Reaffirmed	[SL] BBB (Negative)	[SL] BBB (Negative)
Janashakthi Limited	Issuer Rating	Revised	[SL] BBB- (Negative)	[SL] BB+ (Negative)

Abbreviations

ASPI	All Share Price Index
bps	Basis points
pps	Percentage points
CBSL	Central Bank of Sri Lanka
CDA	Coconut Development Authority
CSD	Census and Statistics Department
CSE	Colombo Stock Exchange
GICS	Global Industry Classification Standard
GoSL	Government of Sri Lanka
SLDB	Sri Lanka Development Bonds
SLISB	Sri Lanka International Sovereign Bonds
SOFR	Secured Overnight Financing Rate
PMI	Purchasing Managers Index
RRISL	Rubber Research Institute of Sri Lanka
YTD	Year-to-date

To subscribe to ICRA economic updates, contact
Email: research@icralanka.com

Published date: February 16, 2022
Document #: meujan22

©Copyright, 2022- ICRA Lanka Limited. All Rights Reserved. Contents may be used freely with due acknowledgement to ICRA Lanka. All information contain herein are from sources deemed reliable; however, no representation or warranty is made to the accuracy of thereof.

About ICRA

ICRA Lanka Limited (ICRA Lanka) is a Credit Rating Agency licensed by the Securities and Exchange Commission of Sri Lanka (SEC). ICRA Lanka is a fully owned subsidiary of ICRA Limited ("ICRA") of India. The ultimate parent company of the international credit rating agency, Moody's Investors Service, is the indirect majority shareholder of ICRA.



Subsidiary of
ICRA Limited

CORPORATE OFFICE

Level 10, East Tower, World Trade Center, Colombo 01, Sri Lanka
Tel: +94 11 4339907; Fax: +94 11 2333307
Email: info@icralanka.com; Website: www.icralanka.com

Disclaimer

This publication has been prepared by ICRA Lanka solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ICRA Lanka does not represent that it is accurate or complete. ICRA Lanka does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication.

Contacts

Rasanga Weliwatta
Head of Financial Sector Ratings
+94 773553564
rasanga@icralanka.com

Shevinda Thilakaratne
Analyst
+94 774066764
shevinda@icralanka.com

Access more of our research content at
<https://www.icralanka.com/research/>

Follow us on



IcraLanka



icra-lanka