

Sunil Mendis: Is it time for a common currency in the SAARC region?

Inauguration speech by Mr Sunil Mendis, Governor of the Central Bank of Sri Lanka, at the 15th Forex Conference of the Forex Association of India, Colombo, 20 August 2004.

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It is with great pleasure that I accepted the invitation from the Forex Association of India to inaugurate its 15th Annual Forex Conference here in Colombo. I would like to extend a warm welcome to this distinguished gathering of forex professionals from Sri Lanka as well as from many of our neighboring countries. I am sure that this is an excellent opportunity for all of us to promote goodwill among ourselves. It also gives us an opportunity for sharing our thoughts on the way forward for South Asia's currency and financial markets, which is the theme of this year's conference.

Forex, as you very well know, is the largest financial market in the world. Unlike many other markets, the international forex market is open 24 hours a day. Its daily turnover is well over US\$ 1.2 trillion. This turnover is more than the combined turnover of the world's major stock markets on any given day. Hence, the international forex market is a very liquid, and thus, a desirable market for trading. As with any other market, technology has also contributed immensely towards its expansion. Now trades are executed increasingly through the internet. It has allowed even smaller investors the access to the market.

As conservative central banks, our involvement in the forex markets is limited to strategic investments and stabilising the exchange rate. Following this role, the Central Bank of Sri Lanka does not get involved in speculative type of trading. However, it plays a major role in the development of the country's forex as well as other financial markets. We know that in a market-oriented economy, all financial market segments, namely, the foreign exchange market, money market, government debt securities market and the stock market are inter-linked. The Central Bank, while watching the operations of each market segment individually, needs to take a macro view of all the market segments to ensure financial market stability. The focus today, however, should be on the foreign exchange market.

In the exchange rate area, it is appropriate to mention at this juncture, Sri Lankan authorities made a fundamental change to its policy on 23rd January, 2001 by moving to a freely floating exchange rate arrangement. This was necessitated by the inability of the then prevailing exchange rate system and the crawling band regime to sustain themselves. Immediately after the float, the market experienced some volatility as is usually expected. However, this volatility has been contained overall since then. This, not only brought confidence to the market, as evidenced by increased foreign exchange inflows, but also allowed greater flexibility and market opportunities to foreign exchange dealers of commercial banks. Subsequent to the float, the Central Bank became a net buyer of foreign exchange from the market, in sharp contrast to its experience in the period prior to that.

Our objective with regard to the foreign exchange market is to ensure an orderly adjustment of the exchange rate, without excessive volatility. Such adjustment should reflect the emerging economic fundamentals of the country. We should ensure that demand and supply mismatches are addressed on time so that there is no excessive volatility in the exchange rate.

Turning to the theme of this year's conference, i.e. "Is it time for a common currency in the SAARC region?", I believe that it would give rise to much interesting and thought provoking discussion and debate. We know that the SAARC was established in 1985, with the objective to provide a platform for the peoples of South Asia to work together in a spirit of solidarity, trust and understanding. It aims at accelerating the process of economic and social development of member countries. I believe the considerations of the timeliness to introduce a common currency for the region will be supportive towards the objectives and aims of SAARC as well.

While taking note that deliberations such as these would definitely lay the foundation for future developments in the SAARC region, I take great pleasure in inaugurating this conference today and wish you all success with the conference. And I would also like to urge you to take a little time off to visit some places of interest, while you are in this beautiful country, Sri Lanka.

Thank you.