

The Impact of Exchange Rate Movements on the Stock Returns of Commercial Banks in Sri Lanka

Bandara, A.W.M.S.S.C.¹ and Thilakerathne, P.M.C.²

¹sanduni9501@gmail.com, ²lal@kln.ac.lk

Abstract

Foreign exchange rate is price of the local currency stated in terms of another currency. It is widely held that foreign exchange rate is important financial and economic factor which affects the value of common stocks. Exchange rate movements are highly affected for creating risk in banking institutions. This paper investigates the impact of exchange rate on the stock returns of commercial banks listed in Colombo Stock Exchange (CSE). Data were extracted from the Central Bank of Sri Lanka (CBSL) and CSE. Data were analyzed by using linear regression analysis for the period of July 2013 to June 2018 using monthly observations. The results of the study indicates that there is significant exposure of Sri Lankan listed commercial banks to major exchange rate movements suggesting that an appreciation (depreciation) of domestic currency value (Sri Lankan Rupee) against four major currencies such as US Dollars, Japanese Yen, Euro and Great Britain Pounds delineates positive as well as impact on stock returns of the respective banking institutions. The important characteristic in this study is that estimation of the exposure coefficients are based on the individual firm level data.

Keywords: Stock Returns, Exchange Rates, Commercial Banks, Sri Lanka