

EXCHANGE RATE FLUCTUATION AND THE STOCK RETURN OF LISTED MULTINATIONAL COMPANIES IN SRI LANKA

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According to the availability of resources, countries make the choice between production, export, and import, and they usually attempt to gain comparative advantage through foreign trade activities. Thus, internationally active firms have to face the currency fluctuation risk frequently and disclose the foreign currency gains and losses during the year in their financial statements. Though the literature provides evidence on the impact of exchange rate fluctuation on stock return, studies about the Sri Lankan context are limited. This study, following a quantitative research approach, investigates the relationship between the exchange rate fluctuation and the stock return based on secondary data from selected 31 listed multinational companies in Sri Lanka for the period from 2010 to 2020. 'Exchange rate fluctuation' and 'stock return' are measured using the change in the trade-weighted exchange rate, and stock prices plus dividends respectively. Market portfolio rate of return (MPRR) and inflation rate are used as control variables. By applying panel regression analysis, findings reveal a negative relationship between stock returns and trade-weighted exchange rate (TWER). A unit change in trade-weighted exchange rate deducts stock return by 0.011. However, there is a positive relationship between MPRR and the stock return, as a unit change in market portfolio rate of return causes an increment of 0.899 in stock return. Contrary to MPRR, there is a negative relationship between exchange rate fluctuation and stock return, as indicated by the reduction of 4.17 in stock return due to a unit change in inflation rate.-Thus, as a fresh study conducted in the Sri Lankan context, these findings provide insights and direction towards introducing and regulating policies connected with the exchange rate to mitigate abrupt impacts of exchange rate fluctuations on individual firms and the economy. Accordingly, the findings of this study would be beneficial for policymakers in promoting international trade of the country.

Keywords: *Inflation Rate; Market Portfolio Rate of Return; Multinational Companies; Stock Returns; Trade-weighted Exchange Rate*
