



Pathfinder View Point- 7

Making Colombo a Global Financial Centre

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Since the change of government early this year, the country's new leadership has announced a few mega development projects, which when implemented, can catalyse economic transformation. The Pathfinder Foundation (PF) in this article wishes to highlight the links between the high priority mega development projects and the objective of establishing Colombo as an important world class financial centre.

The development of financial centres is of great interest to businessmen and policy-makers around the globe. Not only does it help to develop the basic infrastructure within the area, it also provides significant benefits to a country's economic growth and prosperity of the people. A well-functioning international financial centre is a vital component of an economic infrastructure needed to not only for effective inter mediation in the domestic economy but also to promote Sri Lanka as a regional/ global financial hub.

A modern financial centre has a number of components. Banking, which plays a key role in financial markets, intermediates between savers and borrowers by carrying out transactions in the local and foreign exchange markets. Bond markets are typically a source of long-term capital for governments and larger private sector businesses, and provide an alternative to debt finance offered by banks. The equity market (or stock market) is a source of risk capital for companies that need to finance their growth, in exchange for share ownership. Asset managers act on behalf of individuals and institutions, managing longer-term savings and planning pensions through collective investment vehicles, such as mutual funds. These funds are re-invested in financial markets, non-financial corporations and government agencies. Finally, insurance companies and reinsurers assist in the pooling and management of risk, facilitate trade and commerce, and act as major institutional investors providing additional

liquidity to financial markets. With the emergence of e-commerce the diversity and dynamism of a financial centre has reached a more creative and innovation-driven stage.

Stages in the Development of a Financial Centre

In spite of the Western Region Megapolis Project (WRMP) and the Colombo Port City Project (CPCP), the evolution of a financial centre in Colombo requires a considerable time span. In this regard we can identify different stages in its development. Colombo, as a local financial centre of a developing nation, is currently serving a large group of domestic participants. Local institutions and private investors purchase domestic securities, such as locally issued bonds and shares. The domestic banking system serves local retail and commercial clients. Market infrastructure, such as the payments system and exchanges, are simple and locally developed, with some restrictions on cross-border activity. With the gradual liberalisation of the trade, investment and financial regime, the Colombo has accommodated to a limited extent of foreign related transactions.

As Sri Lanka's economy grows and businesses develop increasingly sophisticated financing requirements, with domestic firms stretching the local capacity to provide the capital they need to expand and begin to seek external sources of finance. Under such circumstances foreign investors become interested in investing in the country and there will be increasing pressure to develop the financial sector. With the fast globalisation and implementation of projects such as WRMP and the CPCP, the government is likely to adopt policies to encourage much larger scale foreign investment and ensure that international financial firms can operate on an equal footing with domestic firms. The market infrastructure needs to evolve to meet the expectations of international investors and financial firms, and support the cross-border investment inflow as well as provide more sophisticated trade financing.

To Become a Regional (Probably International) Financial Hub

In the next phase of development, infrastructure being created under the WRMP, and especially the CPCP, could be the centre of attraction for the international financial giants to establish their regional headquarters. The wider base of investors, as well as the presence of large number of world renowned financial institutions, naturally leads to deeper market liquidity, and a regional hub with the best expertise, connections and liquidity it can become the natural "gateway" for investment in other countries in the region. It also becomes an attractive location for other related businesses looking to set up a branch or subsidiary from which to distribute products and services to clients across the region.

The massive effort and envisaged investment in projects, such as Megapolis, does warrant Sri Lanka to envision beyond a regional financial hub. Therefore, a further stage of development is for the Colombo financial hub to progress from regional importance to being internationally or globally significant. An international financial centre is a hub where cross-border financial business with counterparties around the world can be conducted with ease and utmost efficiency.

Assessing Sri Lanka as an International Financial Centre

An often quoted advantage for Colombo to be a financial hub has been its location in a strategically appropriate time zone. The city is located midway between the major financial markets: London, Frankfurt, Dubai to the West and Tokyo, Hong Kong, Singapore and Sydney to the East. Hence, Colombo has the potential to serve as a subsidiary market for eastern and western giants. Taking this advantageous position into consideration, it was argued since 1980s that when Sydney and Tokyo close for the day, Colombo opens and therefore, it could handle overnight financial transactions. Once, Colombo closes, operations could be transferred to London and so forth. As a result, it was argued that Colombo could conveniently insert itself into a time slot in the round-the-clock operation of global financial markets. Even at that time, there were other emerging markets like Hong Kong, Singapore and Dubai and it was argued that Colombo with its low costs could out perform these markets as a financial centre.

Weaknesses or Challenges

Poor infrastructure facilities, both hard and soft, are an important weakness or challenge to be overcome. In this regard, Colombo still lacks ultra-modern state-of-the art office space in sufficient scale which could accommodate the modern day requirements of a global financial centre. Another key factor is insufficiency of digital infrastructure to ensure high speed data transfers which is fundamental to be accepted as a financial hub. These also include country-wide fiber optic connectivity, non-monopolised gateway (to submarine cables) to international communication.

Another basic requirement is the policy, legal and regulatory framework which will further liberalise the financial sector, including transactions in foreign exchange. Almost all regional

and international transaction hubs have opened up the capital accounts of their respective countries.

What can Megapolis and Port City Project offer?

In the context of the government's drive towards making Colombo a regional hub for financial transactions, the designers and developers of WRMP and CPCP have responsibilities to ensure what they build will provide the facilities for creating the necessary environment for prospective investors. While the creation of a conducive investment climate requires intervention of the state in some areas, the developers of the magnitude of the Colombo Port City have a responsibility to bring to the market most modern infrastructure as well as high-end business community to utilise the space to be created by the project.

In this regard however, the government may need to provide its vision for the city to the developers and provide incentives to redirect, if necessary, the project to accommodate the objectives of the government's plans.

The government's own WRMP, according to the news reports, has taken into consideration the requirements of different modern sectors. As such, the megapolis planning process is likely to identify specialised zones, corridors and even cities targeting value added products and services. For example, specialised corridors for ICT industries, airline and aviation service cities, and marine services and logistics hubs are said to be identified in the planning and designing stage. It is highly possible that the financial hub concept too will also receive priority in the planning and implementation of the megapolis project.

Conclusion

Implementing the WRMP and CPCP offers an excellent opportunity to create the infrastructure necessary to supplement Sri Lanka's natural advantage for becoming an international financial centre. This needs to be supported by policies which create the relevant soft infrastructure: business climate, and skill base.

This is a View Point of the Pathfinder Foundation. Readers' comments are welcome at pm@pathfinderfoundation.org/www.pathfinderfoundation.org