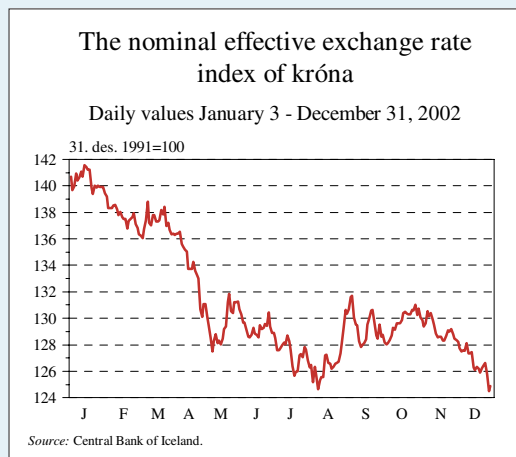


Foreign exchange market highlights 2002

Exchange rate developments

The exchange rate of the króna strengthened in 2002. The exchange rate index was registered at 141.7985 at the end of 2001 but 124.8994 on December 31, 2002. The index went down by 11.92%, which corresponds to a strengthening of the króna by 13.53%.



Turnover and trading

Total turnover in the forex market in 2002 was 834,444 m.kr. Of this figure, the Central Bank bought US dollars for 4,528 m.kr., giving it a 0.54% share of total market turnover. Market turnover in 2002 was somewhat lower than in 2001, down by 383 b.kr., but was 66 b.kr. greater than in 2000.

The highest monthly turnover was in September at almost 104 b.kr. Monthly turnover was lowest in June at just over 37 b.kr. On a single day, the most turnover was on April 24, at 16 b.kr. No trading took place in the forex market on six days during the year, once because of a breakdown in the submarine telephone cable.

Exchange rate volatility

The table below shows exchange rate volatility over the past three years, as the calculated standard deviation in day-on-day changes in the exchange rate index, US dollar and euro. As may be expected, the sharpest swings were in 2001, while last year was less volatile. Nonetheless, the exchange rate was more volatile than in 2000.

Table 1 Exchange rate volatility 2000-2002

<i>Standard deviation (%)</i>	<i>US dollar</i>	<i>Euro</i>	<i>Exchange rate index</i>
2000	0.57	0.50	0.35
2001	0.84	0.77	0.72
2002	0.56	0.54	0.46

Commission system

The Central Bank introduced a commission system for market makers on July 1, 2001 in response to pronounced volatility in the forex market. Although the swings died down, it is unlikely that this was solely thanks to the commission system. Under the initial agreement market makers received a 0.2% commission on their positive market making up to a total of 100 m.kr. per quarter. If the calculated total commission exceeded 100 m.kr. it was divided among the market makers on a proportional basis. The agreement was revised at the end of 2001 and again in March 2002. When the Central Bank introduced the commission arrangement it announced that it was an experiment and regarded it as a temporary measure. In June 2002 the Central Bank decided to discontinue commission payments¹ to market makers by phasing them down to zero on January 1, 2003. The Central Bank paid 200 m.kr. in commission to market makers in 2001 and 354 m.kr. for 2002, or a total of 554 m.kr.

Central Bank transactions with foreign exchange market makers

The Central Bank did not intervene directly in foreign exchange market trading during 2002, i.e. with the aim of influencing the exchange rate of the króna by buying currency from or selling it to all market makers. In *Monetary Bulletin* 2002/3 the Central Bank said that conditions were in place for moderate purchases of currency in order to boost its foreign position. These

1. A letter dated June 18 was sent to CEOs of bank and other companies involved in the forex market informing them of the Central Bank's unilateral decision.

remarks aroused interest among market makers, who interpreted the phrase “moderate purchases” in different ways. After considering a number of possibilities and talking to the market makers the Central Bank issued a press release on August 27 announcing its plans to purchase 1.5 m. US dollars 2-3 times a week for a total of 20 b.kr. from September 1 to the end of 2003. Regular purchases are made just before the market opens. The Bank also offered to buy higher amounts at the request of market makers on an ad hoc basis. Despite the Bank’s talks with market makers who were thereby aware of what was pending, the króna weakened on August 28. This weakening can be attributed to the press release, since there was a break-

down in the submarine telephone cable that day and no trading took place in the forex market. The Central Bank made its first purchase of 1.5 m. US dollars from market makers on the morning of September 2 and continued to do so every Monday and Wednesday until the end of the year. Once the Bank purchased from a market maker on a Friday, during the Christmas break when the market was closed on the Wednesday. The Central Bank bought 1.5 m. US dollars 35 times, making a total of 52.5 m. US dollars or the equivalent of 4.5 b.kr. During the year, on August 27, the Bank made its first forward sale of currency. The contract was made in four currencies and involved three different lengths of time.