Factors Affecting Indian Stock Market

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"FACTORS AFFECTING INDIAN STOCK MARKET"

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ABSTRACT

In current scenario of Indian stock market each investors are required to be alert enough about happenings in the market. For that purpose it is very important for each and every investor to be aware about major factors affecting stock market. In this paper it has been tried to find out major factors responsible for up-down movement in Indian stock market. From the study it has been found that factors like Flow of Foreign Institutional Investors, Political Stability, Growth of Gross Domestic Product, Inflation, Liquidity and different interest rate and Global level factors are major factors responsible to create movement in Indian stock market.

INVESTMENT: MEANING

Investment is the commitment of funds to one or more assets that will be held over some future time period. Investment sometimes refers as investment process. Investment process is the process of decision making about parking our fund in different investment avenues. Investment decision involves the process of selecting best alternative(s) with respect to risk averseness and expected return of investor. Investment avenues we can mainly divide in to two parts: 1. Investment in for of securities, which are marketable and 2. Non-securities form i.e. non-marketable.

MARKETABLE SECURITIES: TYPES

Following are marketable securities:

- **Equity shares**: These are shares of company and can be traded in Secondary market. Investors get benefit by change in price of share and dividend given by companies. Equity shares represent ownership capital. As an equity shareholder, a person has an ownership stake in the company. This essentially means that the person has a residual interest in income and wealth of the company. These can be classified into following broad categories as per stock market:
- **Bonds/Debentures**: Bonds/Debentures are the instruments that are considered as a relatively safer investment avenues. Bonds/Debentures are debt instrument issued by government or government authority, public sector, companies etc.
- **Money market instrument**: By convention, the term "Money Market" refers to the market for Short-term requirement and deployment of funds. Money market instruments are those instruments, which have a maturity period of less than one year. These instruments are also issued by government, public sectors, companies etc for their short-term requirement of finance.
- **Mutual Funds** - A Mutual fund is a trust that pools together the savings of a number of investors who share a common financial goal. The fund manager invests this pool of money in securities, ranging from shares, debentures to money market instruments or in a mixture of equity and debt, depending upon the objective of the scheme. The different types of schemes are: Balanced Funds, Index Funds, Sector Fund, Equity Oriented Funds

Factors affecting Indian Stock Market

- Mrunal Joshi[1]

Abstract

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Capital Market

The capital market is market for financial assets which have a long or indefinite maturity. Generally, it deals with long term securities which have a maturity period of above one year. Followings are the importance of capital market.

1. It is important source for the productive use of the economy's savings. It mobilizes the savings of the people for further investment and thus avoids their wastage in unproductive uses.

2. It provides incentives to saving and facilitates capital formation by offering suitable rates of interest as the price of capital.

3. It provides an avenue for investors, partially the household sector to invest in financial assets which are more productive than physical assets.

4. It facilitates increase in production and productivity in the economy and thus, enhances the economic welfare of the society. Thus, it facilitates "the movement of stream of command over capital to the point of highest yield" towards those who can apply them productively and profitably to enhance the national income in the aggregate.

5. The operations of different institutions in the capital market induce economic growth. They give quantitative and qualitative directions to the flow of funds and bring about rational income in the aggregate.

6. A healthy capital market consisting of expert intermediaries promotes stability in values of securities representing capital funds.

7. Moreover, it serves as an important source for technological up-gradation in the industrial sector by utilizing the funds invested by the public.

For better understanding of capital market we should also know its divisions. Capital market may be divided in to three segments. 1. Industrial security market; 2. Government security market and; 3. Long term loans market. But this paper is restricted to industrial security market; hence here only industrial security market is discussed below.

Industrial Securities Market

It is market for securities issued by different companies. Such securities are equity shares, preference shares and debentures. In this market investor invest their money by purchasing these securities and companies raise their fund from different issues. This market can be subdivided into Primary market and secondary market.

Primary Market

Primary market is the market where industrial securities are first time issued. This market is also known as new issue market. It deals with those securities which were previously not available to the public. Thus it deals with issue of fresh capital by companies either for cash or for consideration other than cash. This capital may in any of the form i.e. equity shares, preference shares, debentures etc.

Secondary Market

The stock market is a market for old securities i.e. those which have been already issued and listed on a stock exchange. These securities are purchased and sold continuously among investors without the involvement of companies. Stock exchange provides not only free transferability of shares but also makes continuous evaluation of securities traded in the market.

Relevance for the Study

Stock market is one of the vital sources of investment to earn good return, which could be more than the real expected rate of return. (Real rate of return is = actual rate of return – inflation rate). To earn in stock market, knowledge related to it is very important. Performance of stock market is reflected by number of factors related to country's economy, industrial positions, companies' performance and factors related globe. If investor wants smart movement in stock market he is required to understand effect of major factors in stock market. Before understanding effect of major factors it is important to aware about these major factors.

Literature Review

Galbraith (1954) has found that the Great Crash of 1929 was followed by boom. Due to rapid **economic growth** of the 1920s created euphoria in investment. The Element of **loan from brokers** added fuel in it i.e. dangerous leverage. All these are due to **irrational investors**.

*DeLong and Summers (1989) show that the **variance of real GNP** was not much higher* during the financial panics from 1890-1913 than during non-panic periods.

Schwert (1988) shown that the standard deviation of both stock returns and **industrial production growth** are higher during recessions than during expansions.

Schwert (1989a, b) shown that volatility was higher during recessions and around the major banking panics in the nineteenth and early twentieth century. Negative returns lead to larger increases in volatility than do positive returns. The risk borne by investors in the stock market, and where stock volatility reflects uncertainty about more **fundamental economic aggregates**, they provide information about the health of the economy.

White Eugene N. (1990) found that the major reason for the crash of 1929 was the **irrational behavior of the investor**. The mania of the investor was also due to expansion of broker's loan. Fundamentals of certain companies were supported it. Many people who had never bought stock before entered the market. Women, new investor, supplied programs and articles in women's magazines. Including irrational behavior of the investors other factors were **Credit Policy, New stock Issue, Decision of Authorities for Big Corporate, Changes in Dividend/Earning of company, Changes in Tariff, Duties and charges, International Effect like Monitory policy of other countries, Interest Rate of home and other country**.

Chen, H., Lobo, B. J., & Wong, W.-K. (2006) had seen that the **U.S. stock plays dominant role** in the relation with Indian and Chines stock market, whereas there is an interactive relationship between Indian and chinese stock market.

Mukerjee D. (2007) has studied the competitive analysis of Indian market with international market. In his study he has studies BSE and NSE, Indian stock exchanges with New York Stock Exchange (NYSE), Hong Kong Stock exchange (HSE), Tokyo Stock exchange (TSE), Russian Stock exchange (RSE), Korean Stock exchange (KSE). In this study he has found that the markets do react to global cues and any happening in the **global scenario** be it macro-economic or country specific (foreign trade channel) affect the various markets.

Avadhani V.A. (2008) has noted that trading on May 5th 2000 was Teji (Bullish) while trading the next day May 8th, was Mandi (Bearish) both involving wide wings of 140 to 230 points in a day and both sawed by market rumors and sentiment. These days are classical example of role of sentiments on the market. The **fundamental of the economy** were good.

Avadhani V.A. (2008) had mention in his book, if **purchases of FIIs** are more than sales involving a net long position, the market may turn out to be Bullish and if net sales are more involving a short position, the market turn Bearish.

Ahmed Gauher and Syed Abdul Malik (2009) had shown that according to the Indian establishments, India is not going to be much touched by the crisis if growth rate of some 8 to 9 percent is going to hold good. But according to the first or preliminary symptoms, the Indian Economy is also going to be hit by the crisis, as already there is a **crisis of liquidity in the economy** and the estimates of the growth rates are also being lowered.

Kawai (2008) described **subprime story**: Bubble burst in 2008, collapse of the financial system of US, affected global level.

Sandeep Kumar and Sweta Bakshi (2009) observed that 1.3% **industrial growth** is the lowest IIP (Index of Industrial Production) data ever registered since last ten years. April-august growth is 4.9% which also lowest for the first five months of the financial year in 14 year period except 1998 and 2001. The Industrial growth in August of 2008 plummeted to mere 1.3% compared to same month in 2007. This industrial slow down affected transport service too. **Global recession** will also lead to less tourists coming to India. That will negatively affect tours and travels industry. The global recession affected IT, automobile industry and export oriented firms adversely.

Taylor (2009) studied the greater depression was marked by banking crisis, **unemployment rate** soared past 20 percent and 89 percent decline in stock prices.

Desai Jayesh N. (2009) depicted in his paper that world output rose at 5% in 2007, slowdown at 3.9% and 3% in 2008 and 2009 respectively. According to IMF world economic outlook; India grew at 9.3% in 2007 and 7.9% and 6.9% in year 2008 and 2009 respectively. He has also focus on measurement of effect on developing countries, which can be identify by **decrease in Export**.

Raj, J., & Dhal, S. (2008) have found in their study of period of April 1993 to January 2008, that impact of regional and global stock markets on the Indian market in the long run as well as the short run. The absolute size of coefficients in the long-run co-integration relation suggests that the Indian markets dependence on **global markets**, such as the **United States and the United Kingdom**, is substantially higher than on regional markets such as Singapore and Hong Kong. Within Asia, the Singapore and Hong Kong markets have significant influence, while the Japanese market has weak influence on the Indian market. The two global markets, the United States and the United Kingdom, could have a differential impact on the Indian market in the opposite direction.

Ravishankar B. and Mahesh Rajgopal (2009) have described several stages of financial crises in US and also observed that the BSE Sensex has continued to bleed more out of panic and **psychological reasons** than for others. In last few weeks (3-4) BSE Sensex fell by almost 15%. It is also due to shortage and **dries up of capital from FII and FDI**.

Bhalla V.K. (2011) has described in his book that the extent of stock price volatility is also influenced by the extent of **integration between the domestic and international capital markets as well as the regulatory framework** governing the stock market. In India, two most important factors which had significant bearing on the behaviour of stock prices during the 'nineties were net **investment by FII** and trend in the **international stock exchange, especially NASDAQ**.

Few of the articles from local daily news papers were also collected and analysed to identify major factors due to which stock market movements increase.

Objectives

Primary Objective for the study was **to identify major factors affecting Indian stock market**.

Research Design:

For this study the Descriptive Research design is used. Different factors are described on the basis of data analysis. In this study primary data about opinion of stock brokers, sub-brokers and their employees had been collected to identify major factors affecting Indian stock market. Population for the study was all the experienced and well positioned member stock brokers, sub-broker and employees of them, listed at stock exchanges at national level in India i.e. BSE and NSE, and having their branch or franchisee at Surat city.

Sampling

Initially efforts was made to collect the list of broker, as list was not available convenience sampling is used initially and then for further work snowball sampling is used. In survey 56 respondents were surveyed from 39 different offices of 25 different brokers. Out of them 38 were head or owner of the company, whereas 18 were employee of these companies. Sample structure is mention in following table.

Table 1. Sample Structure

Sr. No.	Name of Broker	Respondents are Promoter / Head or Employees		Total respondents	Total number of broker offices visited
		Promoter/Head	Employees		
1	Angle broking	3	0	3	3
2	Arham Share Consultant Pvt. Ltd	1	0	1	1
3	Concept Sec. Pvt. Ltd.	1	1	2	1
4	Dhwaja Shares and Sec. Pvt. Ltd.	1	0	1	1
5	Enam Securties Direct Pvt. Ltd.	2	0	2	2
6	FairWealth Sec. Ltd.	1	0	1	1
7	HDFC Securities Ltd.	2	0	2	1
8	ICICI Securities Ltd.	2	1	3	1
9	India Infoline Ltd.	3	5	8	3
10	ISE	0	3	3	1
11	Jainam Share Consultant Pvt. Ltd.	3	2	5	4
12	Karvey	1	0	1	1
13	KRChoksey	3	2	5	3
14	Marwadi Shares and Finance Ltd.	1	0	1	1
15	Monarch	1	1	2	1
16	Nirmal Bung	2	0	2	2
17	Prabhudas Lilladher Pvt. Ltd.	1	2	3	1
18	Religare Sec. Ltd.	1	0	1	1
19	Roongta Rising Stock Pvt. Ltd.	2	0	2	2
20	South Guj. Shares & Sec. Ltd.	0	1	1	1
21	Sherkhan Ltd.	2	0	2	2
22	SMC Global Sec. Ltd.	2	0	2	2
23	SSJ Finance	1	0	1	1

24	Sunidhi Sec. and Fin. Ltd.	1	0	1	1
25	VSE Stock Services Ltd.	1	0	1	1
Total		38	18	56	39

For primary data collection questionnaire is used with personal survey method. This questionnaire was prepared carefully with the consideration of important variables studied in literature review. From literature it has been found that there are more than 60 variables which may affect Indian stock market. These entire variables were evaluated with the use of likert scale. In data analysis simple tabulation and scores derived from respondents were considered, that much was enough to give the rank to different factors. For detailed study factor analysis were also applied with the use of SPSS, but results were not good enough to determine the groups of these factors.

Limitations of the Study

No research model or theory could be without a single limitation. In our study also we have faced following problems, which had restricted scope of our research work.

1. As my respondents where professionals like broker, sub-broker and their employees due to their busy schedule, lack of interest and fear to get exposed about their lacking in knowledge about their business, responding ratio was low.

2. Few of the owners were not found much knowledgeable, as they were ready to invest in broking firm business due to lucrative position of service sector, but practically they have less experience. Literature also supports that near about 6000 sub-brokers quit stock market during financial year 2011-12 that shows that people have started their business in stock market without proper planning and knowledge and due to that finally they have to stop their business of broking service in stock market.

3. As focus was only to identify major factors affecting Indian stock market, no specific test or special tools has been used. Even due to small sample size few of the techniques like factor analysis could not produce good result.

Data Analysis

Following table summarize major factors affecting trend of stock market. This list of factors is prepared after analyzing views of respondents about all related factors.

Table 2. Top seven factors affecting stock market

Factors	Actual Score	Maximum possible Score	Percentage Scored
Foreign Institutional Investors	249	285	87.37
GDP Growth	233	285	81.75
Political Stability	227	285	79.65
Oil Price	221	285	77.54
Liquidity Condition	219	285	76.84
Cash Reserve Ratio	217	285	76.14
Subprime Crises	217	285	76.14

Table 3. Other major factor affecting stock market

Factors	Actual Score	Maximum possible Score	Percentage Scored
No. of Follow up Issues in the period	141	285	49.47
No. of New Issues (IPO) in the period	141	285	49.47
Scams in Stock Market	128	285	44.91
Trade Volume in Commodity Market	125	285	43.86
Indian Government Debt (Including both Outside and inside India)	122	285	42.81
Dividend-Earnings Ratio	118	285	41.40
Astrology	103	285	36.14

In above two tables (Table 2 & Table 3) score for the factors are derived after summation of all respondents' response about that factors i.e. score marked for respective factor. Hence maximum possible score is 285 (5X56) i.e. maximum score of 5 by 56 number of respondents. Column of percentage shows percentage of score calculated using following formula.

$$\frac{\text{Actual Score X 100}}{\text{Maximum Possible Score}}$$

Respondents Views: Major five factors affecting stock market

From open-ended question it has been tried to found major factors responsible for bullish trend and bearish trend. There were separate questions asked for factors responsible for bullish and bearish trend, but all respondents (52 have responded to this question) have responded same factors responsible both phases. Out of responses we had found Companies' Performance, Political Stability, GDP Growth, Inflation, Govt. Policies, FII Flow and Global factors were the frequent answers. Following table shows the frequency of all those factors identified as frequent responses.

Table 4. Factors identified by respondents as part of major five factors

Factors identified	No. of Respondents	Total Responses	Percentage*
Flow of Foreign Institutional Investor (FII)	30	52	58
Political Stability	27	52	52
Inflation	26	52	50
Govt. Policies	24	52	46
GDP Growth	22	52	42
Performance of Companies	19	52	37
Global Level	10	52	19

* Due to multiple responses

In above table column of number of respondents explains number of respondents who have listed down respective factors in their response of major five factors affecting bullish or bearish trend. In Table 4 percentages are calculated in following way:

$$\frac{\text{Number of Respondents X 100}}{\text{Total Number of Respondents}}$$

Major Findings

We have found following major factors affecting stock market.

1. Firstly, **FII flow** is found most important factor affecting Indian stock market. This factor got score of 87.37% (**Error! Reference source not found.**) and got maximum favor of 30 respondent out of 52 (Table 4). We have also observed that in local news paper there were articles, pasted in appendix, about stock market explaining that increase in FII inflow leads raise in stock market and outflow leads to downfall in stock market. FII flow is one of the significant factors which may change the trend from bullish to bearish in case of negative flow and bearish to bullish trend in case of positive flow from outside the country. BSE sensex fell by almost 15% during subprime crises. It was due to shortage and dry up of capital from FII and FDI (Ravishankar and Mahesh Rajgopal, 2009). *Avadhani V.A. (2008)*, also wrote in his book that If purchases of FIIs are more than sales involving a net long position, the market may turn out to be bullish and if net sales are more involving a short position, the market turn bearish. Net investment of FII had significant bearing on the behaviour of stock prices of during 'nineties' in Indian stock market (Bhalla, 2011).

2. Second important factor identified by respondents is related to Political stat and Economical development in the country. This factor mainly includes **Political stability, Government Policy and GDP growth** (Table 2 & Table 4). GDP growth scored 81.75% and Political stability scored 79.65% in Table 2, whereas both factors got favored opinion of 22 and 27 out of 52 in Table 2. Political stability leads to stability in govt. policy as different political party have different philosophy and according to that they used to make certain changes in different policy. All these also directly or indirectly determine the economic growth of the country i.e. GDP growth rate. The Government policy also determines opportunity or threat for different business and industries. So performance of different industries and companies are also affected by them. There is high positive correlation between performance of economy and stock market especially in case of recession in economy and crash in stock market (*Barro Robert J., 2009*).

3. A further important factor is **Inflation**. We can find that 26 out of 52 respondents (Table 4) identified inflation as one of the factor among five most important factor affecting stock market. Effect of inflation may be direct or indirect on stock market. Inflation directly affects the profitability of the industries by affecting their cost of production. As government try to control inflation through changes in **interest rate** which affect **liquidity** position. The change in **liquidity** of cash in market leads to increase or decrease in volume in stock market. Thus inflation indirectly also affect stock market. The articles from local news paper (pasted in appendix) also support this interpretation. Thus, major factors like inflation, liquidity (scored 76.84% in Table 2), interest rates and volume are directly or indirectly related with each other and affect stock market all together.

4. Other important factors are related to **global financial circumstances**. From Table 2 we can find that oil prices (scored 77.54%) and subprime crises (score 76.14%) are major factors which can affect stock market. The same kinds of factors are grouped as global level factors in Table 4. As Liberalization, Privatization and Globalization (LPG) opened doors for Indian players at other countries and domestic market for foreign players in number of way. Even investors of different countries can also roam their investment through different instrument like Global depository receipt (GDR), American depository receipt (ADR) and other innovative financial instruments. International stock exchanges, especially NASDAQ had significant bearing on the behaviour of stock prices during 'nineties' in Indian stock market (Bhalla, 2011). Global recession will lead to less tourists coming to India, that will negatively affect tours and travels industry. The global recession affected IT, automobile industry and export oriented firms adversely (Sandeep Kumar and Sweta Bakshi, 2009). During the period of April 1993 to January 2008 regional and global stock markets affected the Indian market in the long run as well as short run (Raj & Dhal 2008). *Kawai (2008)* has mentioned in his study that subprime story: Bubble burst in 2008, collapse of the financial system of US, affected global level. The markets (stock market) do react to global cues and any happening in global scenario affect various market (Mukerjee D. 2007). Chen, H., Lobo, B. J., & Wong, W.K. (2006) has also observed that U.S. stock market dominates indian stock market and Chinese market also interact with Indian stock market. From all these supported literature and our study

we can surely say that suprime problem during the year 2008 has affected indian stock market advesly.

Conclusion

It has emerged from the research that the major factors that affect the Indian stock market are as under:

1. Flow of Foreign Institutional Investors
2. Political Stability
3. Growth of Gross Domestic Product
4. Inflation, Liquidity and different interest rate
5. Global level factors

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