

# INTERNATIONAL JOURNAL OF RESEARCH IN COMMERCE, ECONOMICS & MANAGEMENT

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**OBJECTIVES**

**HYPOTHESES**

**RESEARCH METHODOLOGY**

**RESULTS & DISCUSSION**

**FINDINGS**

**RECOMMENDATIONS/SUGGESTIONS**

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**A STUDY OF RELATIONSHIP BETWEEN S&P CNX NIFTY AND EXCHANGE RATE**

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**ABSTRACT**

*The relationship between stock prices and exchange rates has preoccupied the minds of economists since both play important roles in influencing the development of a country's economy. Many factors, such as enterprise performance, dividends, stock prices of other countries, gross domestic product, exchange rates, interest rates, current account, money supply, employment, their information etc. have an impact on daily stock prices (Kurihara, 2006: p.376). This paper investigates the nature of relationship between stock prices and exchange rates in India. For the purpose of determining relationship between the S & P CNX Nifty and Exchange Rate (USD/INR) the techniques of correlation and regression analysis has been applied. For using the above techniques SPSS tool has been used. The results suggest that there is causal relationship between stock prices and the exchange rate and fluctuations in exchange rate affect the movement of S&P CNX Nifty.*

**KEYWORDS**

Exchange Rate, Financial Market, Stock Exchange.

**INTRODUCTION**

Stock exchange and exchange rate fluctuations are the center of curiosity for researchers and businessman for a long time. Knowledge of exchange rate movement is of immense help for both exporter as well as importers, because it is directly related to company's transaction exposure. There are many concepts and theories regarding these two variables (stock exchange value and exchange rate value). This research is carried out by taking S&P CNX Nifty and exchange rate between USD and INR. The reason for selecting S&P CNX Nifty is that it tracks the behavior of a portfolio of blue chip companies, the largest and most liquid Indian securities. The reason for selecting USD and INR is that US dollar is the most readily available currency in the world and most of the trade settlement done in dollar. US dollar is called "vehicle currency" and its quote is easily available in foreign market.

**LITERATURE REVIEW**

Apte (2001) investigated the relationship between the volatility of the stock market and the nominal exchange rate of India by using the EGARCH specifications on the daily closing USD/INR exchange rate, BSE 30 (Sensex) and NIFTY-50 over the period 1991 to 2000. The study suggests that there appears to be a spillover from the foreign exchange market to the stock market but not the reverse.

Bhattacharya and Mukharjee (2002) studied the nature of causal relation between the stock market, exchange rate, foreign exchange reserves and value of trade balance in India from 1990 to 2001 by applying the co-integration and long-run Granger Non-causality tests. The study suggests that there is no causal linkage between stock prices and the three variables under consideration.

To examine the dynamic linkages between the foreign exchange and stock markets for India, Nath and Samanta (2003) employed the Granger causality test on daily data during the period March 1993 to December 2002. The empirical findings of the study suggest that these two markets did not have any causal relationship.

Yamini Karmarkar and G Kawadia tried to investigate the relationship between RS/\$ exchange rate and Indian stock markets. Five composite indices and five sectoral indices were studied over the period of one year: 2000. The results indicated that exchange rate has high correlation with the movement of stock markets.

**STATEMENT OF PROBLEM**

One question that always rotates in front of exporters and importers or an export or import dominated company is how exchange rate and stock prices of their company going to change in coming time. The various problems that they might have to face are as follows-

- How appreciation or depreciation of home currency will affect the share price of any particular company.
- How the inflow or outflow of money from home country affect exchange rate.
- Is there any relation between Indian market or stock market performance and exchange rate?
- Who will more affected because of currency fluctuations export oriented company or import oriented company
- How these two variables behave in long run and short run.

**OBJECTIVE OF THE STUDY**

- To find out relationship between S&P CNX Nifty and exchange rate between US Dollar and Indian Rupee.
- To find out that how much S&P CNX Nifty is dependent on US Dollar.

**HYPOTHESIS**

Hypothesis means pre-thoughts. It means the particular thoughts of researcher on a topic before conducting research/study is hypothesis. The hypothesis of this study is as follows:-

- There is a casual relationship between S&P CNX Nifty and USD/INR.
- S&P CNX Nifty is dependent on USD/INR.

## SCOPE OF THE STUDY

The various scope of the study is as follows-

- The finding and various concepts of this study are useful to the importer and exporter
- This study is helpful in currency trading
- Government and various financial institutes can use this concepts in making rules and regulations
- Helpful to RBI for setting monetary policies
- Helpful to figure out total demand and supply of money

## SIGNIFICANCE OF THE STUDY

The various significance of the study is as follows-

- This study focuses on two very important variables of the financial market- stock index value and exchange rate.
- Knowledge of fluctuation pattern of stock index and exchange rate will be helpful for people or brokers involved in stock as well as currency trading.
- This study can be used for the forecasting of appreciation or depreciation degree of domestic currency.
- This study will be helpful in generating basics theoretical concepts about stock index movement and exchange rate.

## RESEARCH METHODOLOGY

The basic objective of the research is to establish relationship between Indian Stock Market and USD/INR. The representative variables used for the study are closing values of S&P CNX Nifty and USD/INR between the periods of 1<sup>st</sup> October 2011 to 31<sup>st</sup> December 2011.

➤ The first step of the research is to find out relationship between CNX Nifty and USD/INR, for that purpose **correlation** has been used.

### Formula

$$r = \frac{N\sum dxdy - \sum dx \cdot \sum dy}{\sqrt{N\sum dx^2 - (\sum dx)^2} \cdot \sqrt{N\sum dy^2 - (\sum dy)^2}}$$

- After this **Linear Regression** analysis has been used. It includes any techniques for modeling and analyzing several variables, when the focus is on the relationship between a dependent variable and one or more independent variables. It helps one to understand how the typical value of the dependent variable changes when any one of the independent variables is varied, while the other independent variables are held fixed. In this case USD/INR has been kept constant as it depends on the Macro Economic factors and value of CNX Nifty has been kept dependent on USD/Rs.

### Formula

Regression Equation  $y = a + bx$

$$\text{Slope (b)} = \frac{N\sum XY - (\sum X)(\sum Y)}{N\sum X^2 - (\sum X)^2}$$

$$\text{Intercept (a)} = \frac{\sum Y - b(\sum X)}{N}$$

where,

$x$  and  $y$  are the variables.

$b$  = The slope of the regression line

$a$  = The intercept point of the regression line and the  $y$  axis.

$N$  = Number of values or elements

$X$  = First Score

$Y$  = Second Score

$\sum XY$  = Sum of the product of first and Second Scores

$\sum X$  = Sum of First Scores

$\sum Y$  = Sum of Second Scores

$\sum X^2$  = Sum of square First Scores

## RESULTS AND DISCUSSIONS

### CORRELATIONS

		Exchange Rate	Nifty
Exchange Rate	Pearson Correlation	1	-.796**
	Sig. (2-tailed)		.000
	N	60	60
Nifty	Pearson Correlation	-.796**	1
	Sig. (2-tailed)	.000	
	N	60	60

\*\*. Correlation is significant at the 0.01 level (2-tailed).

**Interpretation:** As it can be seen that the Correlation is – **0.796** which indicates that there is a negative high correlation between S&P Nifty and USD/INR and it indicates that there is an inverse relationship between S&P Nifty and USD/INR, but the value is between moderate and high therefore it can be concluded that there is a casual relationship between S&P Nifty and USD/INR.

### REGRESSION

MODEL SUMMARY						
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate		
1	.796 <sup>a</sup>	.633	.627	130.4778045		
a. Predictors: (Constant), Exchange Rate						
ANOVA <sup>b</sup>						
Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	1705993.333	1	1705993.333	100.208	.000 <sup>a</sup>
	Residual	987418.533	58	17024.457		
	Total	2693411.866	59			
a. Predictors: (Constant), Exchange Rate						
b. Dependent Variable: Nifty						



COEFFICIENTS <sup>a</sup>					
Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
1 (Constant)	10268.277	532.115		19.297	.000
ExchangeRate	-104.486	10.438	-.796	-10.010	.000

a. Dependent Variable: Nifty

**Interpretation:** The above result indicates that on every single change in the value of Exchange Rate brings **0.633** changes in the value of S&P CNX Nifty, which shows that changes in the Exchange Rate affects the S&P CNX Nifty but not to a great deal, it is only about 63.3%.

## FINDINGS

1. After performing the correlation between the one year values of S&P CNX Nifty and Exchange Rate (USD/INR), final correlation (r) comes out is – 0.796.
2. It shows an inverse relationship between S&P CNX Nifty and movement of Exchange Rate, but the relationship is not very significant. It is kind of moderate relationship, and on the basis of the result we can conclude that there is a casual relationship.
3. After performing the Linear Regression between the one year values of S&P CNX Nifty and Exchange Rate (USD/INR) while keeping the Exchange Rate constant, value of  $r^2$  comes out is 0.633.
4. It shows that fluctuation in Exchange Rate does affect the movement of S&P CNX Nifty.
5. The relationship between S&P CNX Nifty and Exchange Rate (USD/INR) is only applicable in a considerable span of time.
6. It can also be explained by the demand and supply theory that as Nifty starts moving up there would be more demand of INR and consequently the value of INR will get appreciated.
7. In reverse case when Nifty drops down then demand of INR will get decreased and consequently INR got depreciated.

## SUGGESTIONS

1. Exchange rate is complex variable that depends on a number of macroeconomic variables.
2. We should also consider the aggregate influence of Interest rate, inflation, money supply, central government policies etc. on exchange rate.
3. We can look at the exchange rate by dividing it in to two part- spot exchange rate and forward/future exchange rate.
4. We can also include BSE (Bombay Stock Exchange) with Nifty
5. Since exchange rate is very active variables, we should take the data for analysis of more than 1 year
6. We can also directly link the inflow or outflow of FII and DII on the stock exchange value and consequently to exchange rate
7. We can also analyze the effect of major foreign stock exchange performances i.e. Dow Jones industrial average etc. on Indian stock exchange
8. We can also analyze the effect of market sentiments on stock performances and finally on exchange rate.
9. We can also extend this study up to forecasting part of either stock index or exchange rate movement
10. Relationship is more visible or transparent only after analyzing one year data.

## CONCLUSION

After conducting the research it can be concluded that, in the second last quarter of the financial year 2010-11 there is casual relationship between S&P Nifty and Exchange Rate and fluctuations in the Exchange Rate does affects the movements in S&P Nifty but not to a great deal. But it can be said that in a long run, there is a very significant relationship between stock index and exchange rate, and a bull market will attract more foreign investment and consequently there will more demand of domestic currency, more demand of local currency will cause it to appreciate and vice-versa.

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**ANNEXURES****DATA OF EXCHANGE RATE AND S&P CNX NIFTY****TABLE-1**

S.No.	Date	INR/USD	Nifty Value
1	3 October 2011	49.2493	4849.5
2	4 October 2011	49.3464	4772.15
3	5 October 2011	49.2985	4751.3
4	7 October 2011	49.1782	4888.05
5	10 October 2011	48.9088	4979.6
6	11 October 2011	49.1794	4974.35
7	12 October 2011	49.0164	5099.4
8	13 October 2011	49.0932	5077.85
9	14 October 2011	49.0049	5132.3
10	17 October 2011	48.8606	5118.25
11	18 October 2011	49.1894	5037.5
12	19 October 2011	49.0984	5139.15
13	20 October 2011	50.0527	5091.9
14	21 October 2011	49.9819	5049.95
15	24 October 2011	49.842	5098.35
16	25 October 2011	49.6041	5191.6
17	26 October 2011	49.3106	5201.8
18	28 October 2011	48.7384	5360.7
19	31 October 2011	48.774	5326.6
20	1 November 2011	49.3921	5257.95
21	2 November 2011	49.3103	5258.45
22	3 November 2011	48.8946	5265.75
23	4 November 2011	49.009	5284.2
24	8 November 2011	49.5115	5289.35
25	9 November 2011	49.9315	5221.05
26	11 November 2011	49.8074	5168.85
27	14 November 2011	50.2907	5148.35
28	15 November 2011	50.6721	5068.5
29	16 November 2011	50.9784	5030.45
30	17 November 2011	50.8817	4934.75
31	18 November 2011	51.3474	4905.8
32	21 November 2011	52.2236	4778.35
33	22 November 2011	52.4709	4812.35
34	23 November 2011	52.4036	4706.45
35	24 November 2011	52.0968	4756.45
36	25 November 2011	52.1262	4710.05
37	28 November 2011	51.8121	4851.3
38	29 November 2011	52.1323	4805.1
39	30 November 2011	51.9923	4832.05
40	1 December 2011	51.6106	4936.85
41	2 December 2011	51.1679	5050.15
42	5 December 2011	51.1465	5039.15
43	7 December 2011	51.8046	5062.6
44	8 December 2011	51.6447	4943.65
45	9 December 2011	51.874	4866.7
46	12 December 2011	52.7297	4764.6
47	13 December 2011	53.297	4800.6
48	14 December 2011	54.2244	4763.25
49	15 December 2011	53.6853	4746.35
50	16 December 2011	52.5142	4651.6
51	19 December 2011	53.0316	4613.1
52	20 December 2011	52.7023	4544.2
53	21 December 2011	52.5273	4693.15
54	22 December 2011	52.8349	4733.85
55	23 December 2011	52.8601	4714
56	26 December 2011	52.7552	4779
57	27 December 2011	53.164	4750.5
58	28 December 2011	52.9791	4705.8
59	29 December 2011	52.8607	4646.25
60	30 December 2011	52.8392	4624.3

Source: www.nseindia.com &amp; www.exchangerates.org.uk

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