A STUDY ON FACTORS AFFECTING THE EQUITY SHARE

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ABSTRACT

The Indian stock markets are long compared to other developing nations. The oldest stock exchange – Bombay Stock Exchange (BSE) is over hundred years old. But till 1970s, there was a limited volume of transactions in these markets. The markets grew fast during 1980s because at that time corporate sector was turning towards equity market increasingly. Though transactions volume rose, the markets were at primitive stage and faced several difficulties. Companies needed to have the prior permission from the government to access he capital market and government used to approve the price at which new equity could be raised. Government aimed to provide fair value to the investors and to control the flow of funds to the private sector. However, the practice affected negatively to the firms raising capital from the market: through Initial Public Offer (IPO) where initially equity were under-priced compared to their listing price and through new issues where equity were at substantial discount to the prevailing price. There was a scenario where primary market was over regulated and secondary market was under regulated. There was no global link for the domestic capital market and information disclosure as well as transparency was limited which resulted in higher transaction costs. Moreover, public sector financial institutions like Unit Trust of India (UTI), Development Finance Institutions (DFIs) and insurance companies were playing the prominent role in stock market.

Key Words: BSE, DFI, Equity,, IPO,UTI

INTRODUCTION

Equity market is an indispensable part of the economy of a country. The stock market demonstrates a crucial role in the growth of the industry and commerce of the country that eventually affects the economy of the country to a large extent. That is why the government, industry and even the central banks of the country keep an eye on the events of the stock market. The stock market is ineluctable from both the industry‘s point of view as well as the investor‘s point of view. When a company wants to raise funds for further expansion or setting up a new business venture, they have to either take a loan from a financial organization or they have to issue shares via the stock market. Mostly the stock market is the

fundamental source for any company to raise funds for business expansions. For raising capital for the business, the company can issue shares of the company that is primarily part ownership of the company. Firstly the company should be listed on a stock exchange so that the investors can invest into the stocks. There are few rules and regulations pertaining to the listing at a stock exchange and the companies must fulfill the basic criteria to issue stock and go public. The already listed company can issue more shares to the market for raising capital for business expansion. For the companies which are going public for the first time, they must begin with an Initial Public Offer (IPO). In either way, these companies have to go through the stock market. This is the primary function of the stock exchange and it plays a critical role of supporting the growth of the industry and commerce in the country. So it can be said that a rising stock market reflects the developing industrial sector and a growing economy of the country. Much of the required funds for stimulating the business and providing a common platform for stock trading are being provided by stock market. Stock market aids making liquid asset unlike the real estate investment. It provides a mean to sell the stocks at any time and to get the investment with considerable gain. Owing to all these facts, stock market has attracted many investors being more liquid in nature.

Literature Review

Petter (1970) studied the factors which influence and motivate the investors to invest in the stock market. He found out several reasons like investors want to have rapid growth, income from dividends, professional management. It has been observed that young are more risk averse than old, women are more risk averse than men, rich peoples‘ willingness to invest in equities is higher than poor.

Jack Clark Francis (1986). There is an uncertainty in market so investor cannot be sure about their returns for any investment they make. Francis suggested that investors can model a probability distribution of possible return rates. He argued on few noticeable warnings of company‘s failure for the precautions. He also stated that any investors investing into corporate securities must take bankruptcy and default into consideration.

Preethi Singh (1986) remarked in her studies that most investors are risk averse. But it is very important to understand that risk is an inseparable part of equity investment. Higher the risk, higher would be the returns. Therefore investors should carefully study and evaluate the financial statements and other reports of the companies before investing.

Jawahar Lal (1992) attempted to evaluate the investment decisions of Indian investors by looking at their profile. He also aimed to figure out their familiarity with the financial

information and the extent of which it is used. It is the general phenomenon that investors do not receive the annual reports and other statements and do not utilize them for investment decision making.

Gupta, L. C. (1992) in his study discovered the fact that there exists wild speculation in Indian stock market which could lead to _artificial price'. A term artificial price has been described here which means that it is not vindicated by prospect earnings, dividends, etc. and is considered to be brought upon by rumours and manipulations. These prices are confined to crash sometime

Regulatory framework of the Equity market:

Environment of market proceeding to reforms:

The history of Indian stock markets is long compared to other developing nations. The oldest stock exchange –Bombay Stock Exchange (BSE) is over hundred years old. But till 1970s, here was a limited volume of transactions in these markets. The markets grew fast during 1980s because at that time corporate sector was turning towards equity market increasingly. Though transactions volume rose, the markets were at primitive stage and faced several difficulties. Companies needed to have the prior permission from the government to access the capital market and government used to approve the price at which new equity could be raised. Government aimed to provide fair value to the investors and to control the flow of funds to the private sector. However, the practice affected negatively to the firms raising capital from the market: through Initial Public Offer (IPO) where initially equity were under-priced compared to their listing price and through new issues where equity were at substantial discount to the prevailing price. There was a scenario where primary market was over regulated and secondary market was under regulated. There was no global link for the domestic capital market and information disclosure as well as transparency was limited which resulted in higher transaction costs. Moreover, public sector financial institutions like Unit Trust of India (UTI), Development Finance Institutions (DFIs) and insurance companies were playing the prominent role in stock market.

Equity market after proceeding of reforms:

As a result of various reforms, Securities Exchange Board of India (SEBI) was designated with the powers in 1992 to regulate and reform the capital market. Then after, equity market reforms can be classified into two broad categories: one which increases the competition level in the market and the other which is concerned with the problems of information and transaction cost. Free pricing of IPO and new regulation guidelines related to new issues increased the competition in the market. The new regulatory framework focused

on working out for greater investor protection by ensuring disclosure and transparency. National Stock Exchange (NSE) was set up and NSE came up with new automated screen based trading system known as National Exchange for Automated Trading (NEAT) system. With the introduction of NEAT, members across the country could simultaneously trade with greater ease and efficiency. Because of the competition, BSE had to adopt the similar technology. Foreign institutional investors were welcomed to trade and private mutual funds also came into existence. Various measures were taken to manage the market imperfection like information asymmetry and high transaction costs. At the trading level, transparency was enhanced with the NEAT system operated on a strict price/time priority. To increase the Transparency at the investor level there was a regulation requiring listed companies to increase the frequency of their account announcements. The Depositories Act was passed in 1996 to ascertain transferability of securities with speed, accuracy and security. This resulted in securities to be dematerialized. After that, India‘s first depository- National Securities Depository Limited was launched. Other initiatives for reducing transaction costs were electronic trading and settlement, and streamlining of procedures with respect to clearance of new issues.

Equity market reforms since 1992:

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FACTORS AFFECTING EQUITY MARKET:

Financial markets play a vital role in forming an efficient financial system of an economy. Various domestic as well as international factors affect stock market‘s performance. They are interest rate, inflation, exchange rate, index of industrial production, money supply, gold price, silver price, oil price, etc. money supply and inflation have two different effects on the market. As per the study of

Shanken and Weinstein (2006), only Index of Industrial Production is an influencing factor for stock markets.

Srivastava (2010) analysed the relevance of macroeconomic factors for the Indian stock market and found out that in long term, stock market is affected by domestic economic factors like industrial production and wholesale price index and interest rate than global factors.

Chen, Roll, and Ross (1986) examined the effect of various economic variables like

industrial production rate, inflation, risk premium, oil prices, etc. on stock market returns. They found out that there existed a positive relationship between industrial production rate and stock returns and there was a negative relationship between inflation and stock returns.

Jones & Kaul (1996) came to know that stock prices in US, UK, Canada and Japan respond to oil price shocks. As per the study of Papapetrou (2011), there exists a negative relationship between oil price shocks and stock prices because they have a negative impact on industrial production and employment. Bhattacharya et. al. (2001) used Granger non- casualty to test the relationship between there variables: exchange rate, foreign exchange, trade balance and stock returns. After the study, it was concluded that there was no casual linkage between these variables and stock prices. Debarata Mukhopadhyay and Nityananda Sarkar (2003)in their research paper addressed the influence of macroeconomic variables on stock returns. Effects of interest rate, exchange rate, oil prices, inflation, money supply, etc. were taken into consideration for the study.

Inflation:

Higher inflation rate turns up in increased cost of living. This would leave investors with little or no savings as they have to spend more money on their consumption needs. So in turn

it reduces the investment volume in the stock market. Higher inflation rate also results in higher cost of production which would curb corporate profit margins and likely to diminish the dividends. This would result in decreased share prices. Thus, it is expected to be a negative relationship between inflation rate and stock returns.

Crude oil price:

India is dependent on gulf countries for crude oil. India imports oil from the international market. Increased oil prices would result in increased cost of production and transportation that might decrease firms'profit margins and ultimately result in decreased share prices. Besides this, oil prices also have an impact on general public by affecting their transportation costs. Rise in oil prices might result in inflation and decreased consumer savings. This might cause decrease in investment flows.

Gold prices:

Gold is considered to be conventional investment type in India. Generally decrease in its price would increase in demand as people wish to invest their surplus money into gold. This may result in decreased investment in stock market as investors choose gold over share market investment. Since last many years, gold prices have gone high and stock market has also showed significant growth. To have an insight, here the gold prices and BSE Sensex points from march 2015 to march 2016 has been considered for reviewing the present prevailing relation between gold prices and stock market index. (For interpretation, amount as on starting of the month has been taken into consideration.)

Interest rate:

Interest rate that is decided by government institutions and banks affects stock market movements. Higher rate of interest means higher cost of borrowing. Companies need to pay higher for borrowed money which results in higher expenses. So in order to balance expense and earnings, it implies that companies cut down their borrowings compared to their previous regular borrowings. This could lead towards stock market slowdown.

Exchange rate:

Exchange rate also affects the stock returns. Exchange rate is the value of one nation's currency in terms of another currency. Currency depreciation leads to decline in share prices as people think there will be inflationary situation in future. Import oriented companies benefit from stronger currency whereas export oriented companies benefit from weaker currency.

Index of industrial production:

The index of industrial production indicates industries' growth. Industrial production

reflects the state of overall economy of the nation. It affects the stock prices by affecting future cash flow expectations. Increased IIP means increased industrial production that leads to increased profit. Rise in profit results in rise in dividend which affect the share prices positively. Thus, it is expected to have positive relation between IIP and stock market returns.

Greek‘s debt crisis:

Greece was the epicenter of Europe‘s debt crisis after Wall Street collapse in 2008. In 2009, Greece alarmed about the soundness of Greek finances. In 2010, Greece was on the verge of bankruptcy which would set a new financial crisis. To revive Greece‘s economy, International Monetary Fund, European Commission and European Central Bank issued two international bailouts for Greece worth more than 240 billion euros. These bailouts were given with the conditions. Greece was required to have deep budget cuts, tax increment, etc. The bailout money majorly went towards payment of Greece‘s international loans instead of its inflow into economy. Greek GDP witnessed its worst decline in 2011 when it was -6.9%. Around 111,000 Greek companies went bankrupt. Youth unemployment rate was 54.9% during May 2012. The unemployment rate has risen considerably from 10% in 2005- 09 to around 27% in 2013-14. 44% (approx.) Greeks lived below poverty line in 2014. Interest rate in Greek long term debt has been found to be at 10% in 2015 as compared to 6% in 2014. Greece struggled to come out of the crisis all these years. On 29th June, 2015, Greece defaulted on $1.7 billion IMF payment. In 2015, International Monetary Fund threatened to withdraw support for Greece‘s bailout unless European leaders agree to substantial debt relief. Eurozone ministers agreed to provide Greece a € 7bn bridging loan from EU wide fund to keep its finances until a bailout is approved. On the other hand, the European Central Bank also agreed to increase emergency funding to Greece.

China‘s financial market fall:

China‘s stock market tumbled over in June, 2015. China‘s stock exchange is the second largest after the New York stock exchange. Shanghai Composite Index lost 30 percent in three weeks. It gave up $2 trillion in value. To compare this with debt troubled Greece, GDP of Greece is $200 billion. There are several reasons that explain China‘s market fall. In most major economies, professional money managers dominate the stock market trading. But in China around 80 to 90 percent investors were retail investors. Surprisingly 40 million new brokerage accounts were opened in the one year time period ending on May. And these accounts were added at a rate of three million per week. For the first time or less or inexperienced investors, entryprice was margin lending. Margin lending as a percentage of

total market cap rose to 20 percent which is very high. It's around 2.5 percent in US. The combination of millions of new accounts and unprecedented leveraging contributed to the selloff. In response to this market condition, Beijing banned huge institutional investors from selling until Shanghai Composite rises above 4500.

Foreign Institutional Investors (FIIs):

Foreign investments through investment in stock market in listed companies in India are allowed since 1991. They are called foreign institutional investors. FII investment flows into the secondary market and it results in increased capital availability in general. As per one research study, the growing participation of FII in Indian stock market had an impact on each other. But the timings of influence were different(Ambuja Gupta, 2011)8. According to another study of FIIs and Indian stock market, it was found that the net FII amount influence the stock prices in India.(Rao, 1999) Here past 10 years' closing index of NIFTY and Data of FII into India that is from 1993 to 2013 have been considered for analyzing the relation between them.

Conclusion and Suggestions

The study based on Secondary data of selected Articles and Related Projects and Some Websites done to gain a deeper understanding of the what are the factors affecting the equity share. The study established the fact that the investment strategies. Technical analysis before making an investment. The current financial literacy levels are not adequate. Financial literacy is to be promoted at a very early age in one's life and help the common man to make his financial plan profitable for himself. Investors do not have to speculate to achieve their desired. The investors need to be educated through appropriate publicity measures and short term courses. These programs should be sponsored by companies and institutions. Full-fledged continuous awareness campaign can help cure many ills of stock market. For this, required funds can be realized through large quantum of accumulated unclaimed dividends and interest accrual lying with the companies. Regular training programs should be organized for brokers and sub brokers to improve their professional competence. Investor education is very important factor for investors. Research and awareness programmers 'should be conducted for investors. Seminars, conferences and training programs should be arranged for this purpose. Adequate publicity through newspapers, T.V., radio, pamphlets and brochures should be done.

Government and SEBI should take appropriate measures to weed out the discouraging factors and help provide a conducive climate for growth of equity market in the country.

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