Relationship between macro-economic variables and stock market prices: With special reference to Colombo Stock Exchange

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Abstract

The relationship between macroeconomic variables a nd the stock prices has been tested by many researches with reference to different economies. Fluctuations in stock prices occur due to the supply and demand forces. But there is no pool proof or perfect system that indicates the exact movement of stock prices. The movement of stock prices is based on internal and external factors. Internal factors are dividend per share, earning per share, book value, leverage and size. External factors or macroeconomics variables are money supply, influence rate, gross domestic products, interest rate, government regulation and foreign exchange rate. Therefore, the present study focusses on the relationship between macroeconomic variables and the stock prices in Sri Lanka. All share price index was taken as the dependent variable and Exchange Rate, Interest Rate, Inflation Rate, Money Supply, were considered as independent variables. Monthly data of a ten years period from 2008 to 2017 relating to Sri Lankan economy were obtained from different sources such as Colombo Stock Exchange data library, Central Bank website and the Department of Census and Statistics. Data were analyzed using descriptive analysis, correlation analysis and regression analysis. As per the four regression models resulted, exchange rate and interest rate demonstrated inverse relationship, where money supply showed a positive relationship and inflation rate demonstrated a negative relationship but not significant on stock prices.

Keywords: *Macroeconomic variables, stock market prices*