

IMPACT OF MACRO-ECONOMIC FACTORS ON STOCK PRICES

(With Special Reference to Hotel and Restaurant Sector in CSE)

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ABSTRACT

The Impact of Macro – Economic Factors on Stock Prices

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Keywords: Colombo Stock Exchange, Macro-economic factors

Security markets are one of the best ways to fulfill the capital requirements of companies. Security markets are the place where the secondary shares of the listed companies are issued. As well as stocks reflect how the economy performs at any given time. A stock market is a good tool for assessing the macro-economic environment which affects the stock prices. In this scenario the Colombo Stock Exchange is one of the most promising emerging markets in South Asian region.

Hence, there is lack of supporting materials regarding the impact of macro-economic factors on stock prices, little attention of the responsible parties and the lack of knowledge regarding this issue in the Sri Lankan context may cause to unavailability of information for investors, policy makers like parties. Therefore, they unable to take necessary decisions on the right time and ultimately suffer with losses. Therefore, research problem of this study is to find out whether there is any relationship between macro-economic factors and stock prices of Hotel and Restaurant sector in CSE.

Stock market plays the significant role for the industry and as well as for the investors who wants to invest in the stock market to gain maximum return on their

investment (Fama, 1981). The primary function of any stock market is to play the role of supporting the growth of the industry and economy of the country. The growth of the country is directly related to the economy which consists of the variables like GDP, FDI, Inflation rate, Interest rate, Exchange rate like many other variables. These variables are the backbone of any economy. The movements in the stock prices are affected by the changes in above mention macro-economic factors. Hence, the findings of this study will help investors to make better predictions regarding the movements of the stock prices when they take investment decisions. Therefore, it is essential to identify the impact of major micro-economic factors on stock prices for investors who keen to invest in stock market to take correct investment decisions when necessary.

Hotel and Restaurant sector is one of the emerging sectors in Sri Lanka after the post war situation which has the highest contribution to the GDP under the service sector in Sri Lanka after the 2009. Since 2010 the service sector has recorded the highest contribution in sector wise Gross Domestic Production growth. Therefore, Hotel and restaurant sector is one of the booming sectors in Sri Lanka. Through this sector high amount of foreign currency comes to Sri Lanka. When considering the Total tourist arrivals to Asian region it has been increased as well as accommodation providing also increased (Department of Census and Statistics).

Therefore, it is important to assess whether there is an impact of macro-economic factors on stock prices or not. Thus, the primary objective of this study was to identify the impact of macro-economic factors (Inflation rate, Exchange rate,

Money supply and Interest rate) on stock prices of Hotel and Restaurant sector of CSE. The secondary objective was to identify the relationship between macro-economic factors and stock prices.

Population of this study was listed companies under Hotel and Restaurant sector in CSE and there are 37 listed companies. The survey was conducted being based on a sample of all 37 companies under Hotel and Restaurant sector and omitted the companies which do not have the data for the period of 10 years from 2002 to 2011. Seven companies were omitted out of 37 which the ultimate sample size become 30 companies.

All the data in this study context were secondary in nature and the data related to the company stock prices were obtained from the CSE data library and macro-economic factors related data were obtained from the Central Bank Annual Reports and Central Bank monthly bulletins from the period of 2002 to 2011.

Both descriptive and inferential techniques were used to analyze data. Furthermore, multiple regression analysis was used to identify the impact of macro-economic factors on stock prices and correlation coefficient analysis was used to measure the relationship between macro-economic factors and stock prices. Independent variables are recognized as Interest rate, Inflation rate, Money supply and Exchange rate while Stock price has been used as dependent variable.

Accordingly, this study identified that selected macro-economic factors have significant impact on stock prices and the researcher found that, the interest rate and

money supply are the most important macro-economic factors when determining the stock prices of companies' of Hotel and Restaurant sector in CSE.

Further, this study identified that there is a linear relationship between interest rate, inflation rate, money supply, exchange rate and stock prices in order to achieving the secondary objective, which was to identify the relationship between macro-economic factors and stock prices. The results indicated that most of the companies reported a higher R^2 which implied that the employed regression model has the higher explanatory power of macro-economic factors in explaining stock prices.