

DOES EXCHANGE RATE AFFECT THE KARACHI STOCK MARKET PRICES IN PAKISTAN?

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Abstract

The purposes of this study are to find the empirical relationship between Karachi Stock market (SP) and Exchange rate (EX). Daily data is used 2102 to

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2018. To find this relationship the ordinary least square technique is used. This is also being used many researchers in literature. The results of this study Exchange rate (EX) is positively significant at 1% level This study is help for domestic and foreigner investor and also policy maker for economy of Pakistan.

Keyword: stock prices, Exchange rate, OLS

Introduction

Investment is one foremost flourishing indicator for the sustainable escalation of a country. Countries having large volume of investment at hand retain vast span of business activities, eventually which contributes in making strengthen the basic economic fundamentals of a country (Cox, Ingersoll Jr et al. 1985). For instance, Gross Domestic Product (GDP), Foreign Reserve (FR), strengthen of Currency value in respect to dollar and Interest rate (IR) etc. Principally investment is the raped of funds over one or more assets with the intention of some return over a time. There are mainly two techniques by which investment can be made like say for instance investment in financial assets (i.e. stocks or debt instruments) or investment may be in real assets (i.e. gold, silver, diamond and real estate) (Rasheed, Baloch et al. 2014).

Stock exchange is the place where funds are invested in stocks under the regulatory body of security exchange commission (SEC). Further stocks are traded in two major markets i.e. Primary market and Secondary market, first place where shares are bought and sold for the first time for instance initial public offering (IPO) while the former is the place where stocks are traded on second time. Investors attempts to predict the performance of the stocks either

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by broker or by self in order to plan their investments that have a large cushion from risk and have a more tendency toward normal return. Keeping in mind these two factor i.e. (Risk and Return) and to maintain the investment at equilibrium investors buy and sale the particular stocks or shares. Sometimes such buying and selling is at peak or sometimes very low, this act of investors termed as turnover of shares in stock market/stock exchange (Bodart and Reding 1999).

Behavior of stocks doesn't merely dependent to their associated returns called dividend, there are also a large number of factors that may also influence the expected returns and share prices like say for instance political events, monetary policy, fiscal policy, discount rate, foreign reserve, company performance and exchange rate. Therefore every investor looks after the all factors and then finally decides that either to make investment in stocks or not (Naseem, Mohsin et al.).

Exchange rate means the proportion of one currency to switch in other currency at a given rate also known as Forex rate. Stock exchange provides a means to investors to scrutinize the business prototypes in a country. In the context of Pakistan there are three stock exchanges are in function i.e. Karachi Stock Exchange (KSE), Lahore Stock Exchange (LSE) and Islamabad Stock Exchange (ISE) in which shares of listed companies are traded. As U.S dollar is known as internationally trade currency therefore this research emphasizes on identifying the relationship between exchange rate (U.S dollar) and shares turnover of the Pakistan largest stock exchange i.e. Karachi Stock Exchange. there is any significant relation exist between these two variables it will be very

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useful for analyzing the expected behavior of market as a single unit change exists in exchange rate of a country it is because the strength of a currency can be predict carefully by knowing the proportion of converting one into another which is expressed as exchange rate.

Data

For this research secondary data is used. Daily data is used to find the relationship of both variables. The span of data is consists of 7 years from 2012 to 2018. The data is obtained from different site i.e. State bank of Pakistan, Business recorder and different other official websites

Methodology

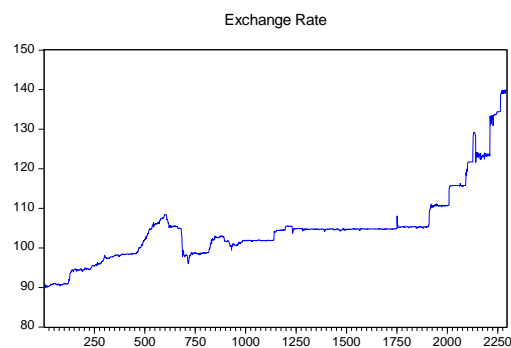
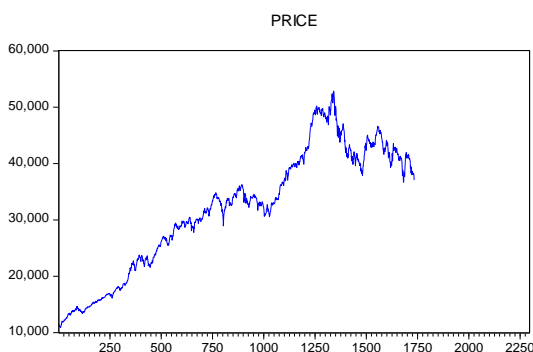
To find the impact of Exchange rate (EX) on Pakistan stock exchange prices (SP) the ordinary least square (OLS) method is used. This model is also used by Mohsin et .al,(2108)

$$SP_t = \beta_0 + \beta EX_t + e_t$$

SP= stock prices (dependent Variable)

EX= Exchange rate of Pakistan against dollar (independent Variable)

Descriptive statistics of Dependent and Independent Variables



	Stock Prices	Exchange Rate
Mean	31909.15	101.0993
Median	32957.87	101.925
Maximum	52876.46	108.5
Minimum	10909.12	89.87
Std. Dev.	10830.73	4.493943
Skewness	-0.239897	-0.874641
Kurtosis	2.01321	2.817973
Jarque-Bera	86.98582	223.4778
Probability	0	0
Observations	1734	1734

Table 1 shows that the result of descriptive statistics of both variables the average value of stock prices is 31909.15 and the average value of exchange rate 101.0993, the value of skewness of both variables negative and the value of kurtosis is below 3 of both variables. The Jarque-Bera test significant at 1% level which mean data is normally distributed as (Naseem, Mohsin et al. 2018).

Ordinary least Square (OLS)

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	-169600	3294.579	-51.4786	0.000
EXCHANGE_RATE	1993.184*	32.55543	61.22431	0.000
R-squared				0.683966

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In the above model the value of R² is 63.1% which means that 63.1% of dependent variable Stock price is explained through independent variables which are exchange rate. The exchange rate is significant at 1% level and the value of coefficient is positive which mean that show the positive relation with stock prices.

Conclusion

In Pakistan many factor is involved to determine the stock prices. In Pakistan the current account balance value is low and also having unemployment. In this study we find a relationship between stock prices and exchange rate. The result shows that exchange rate is significant at 1% level and the value of coefficient also positive which shows that positive relation between both variables means that when the exchange rate high the stock prices of Pakistan stock exchange also high. This study is important for researcher, policy maker and investor.

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