A Study on the Relationship between Monetary Policy and Stock Market Returns of Bank Nifty in India

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ABSTRACT

The monetary system is a formal mechanism accepted by, government as an issuer of currency and controllerof aneconomy. It is a reflection of theoverall change in the economic policy in a country. Hence, there arises a need to study the impact of monetary policies on stock market returns and the existence of a causal relationship between monetary policies and bank nifty returns. The study has been performed by using time series data from 2006 to 2016 for four monetary policy variables that is repo rate, reverse repo rate, cash reserve ratio (CRR) and statutory liquidity ratio (SLR). By applying augmented dickey fuller unit root test, granger causality test, correlation and regression, the study found that repo rate, reverse repo rate, CRR has negative correlation against returns of bank nifty whereas SLR showed a positive correlation against returns of bank nifty. The study concluded that there is no causal relationship between monetary policy variables and the returns of bank nifty. It was found that there exists a negative relationship between reverse repo rate and CRR with bank nifty returns whereas repo rate and SLR have a positive relationship with bank returns. Also, all other variables were considered insignificant except for CRR.

Keywords- monetary policy, bank nifty returns, repo rate, reverse repo rate, cash reserve ratio, statutory liquidity ratio.