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THE INFLUENCE OF CURRENCY EXCHANGE RATES ON STOCK MARKET

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ABSTRACT

In this we discuss about the factors influencing the currency fluctuation on global economy, Indian market and it also affect the stock market. We shift our focus to Indian rupees which causes the rupee fluctuation will be discussed. The exchange rate and stock market play a very important role in the world. The exchange rate and stock market is treated as the two fundamental financial markets in the world.

KEY WORDS: Stock market, Currency exchange, Principles of the financial market.

INTRODUCTION:

The market value of firms and the stock prices affected by the different factors in which exchange rate fluctuations can be compared. There is still no clarity about the relationship between stock market and exchange rates in the worldwide markets. Financial theory explains that the value of firms and it is been influenced by exchange rates and interest rates. The stock value will always increase and decreases the value of stocks in every market.

The exchange rate and stock market are the two fundamental financial markets in the world. These two markets are playing key role in an international business all over the world. It is necessary to understand the relationship between the both markets so that the investors may be able to invest in a better way by taking the minimum risk.

The stock market refers to the collection of markets and exchanges where regular activities of buying, selling and shares of publicly held companies take place. Such financial activities are conducted through institutionalized formal exchanges or over-the-counter.

.While both terms - stock market and stock exchange are used interchangeably. The latter term is generally a sub set of the former. If anyone says that she trades in stock market, it means that she buys and sells shares on one or more of stock exchanges. The leading stock exchanges in U.S. include the New York stock exchange (NY SE), Chicago Board Options Exchange.

In finance, an exchange rate between two currencies is the rate at which one currency will be exchanged for another. It is also regarded as the value of one country's currency in terms of another currency.

Exchange rates are determined in the foreign exchange rates, which is open to wide range of buyers and sellers where currency trading is continuous. In the retail currency exchange market, a different buying rate and selling rate will be quoted by money dealers. Most trades are to or from the local currency. The buying rate is the rate at which money dealers will buy foreign currency, and the selling rate is the rate at which they will sell the currency.

LITERATURE REVIEW:

Essentially inspected the influence of interchange rate on stock market earnings with co-ordination S&P500 (Strong and Poor's 500 Index). By means of proceeds on S&P 500 the index has the reliant flexible and deviations in the US dollar-Euro exchange rates as the self-regulating flexible, reversion talent has charity to normalise elements stock market proceeds depend on exchange rates.

Survey on the active networks between foreign exchange and stock market for India.Applied outcome show that normally proceeds in these two markets are not interrelated, though in current years, the return in stock market had essential inspiration on return in exchange rates.

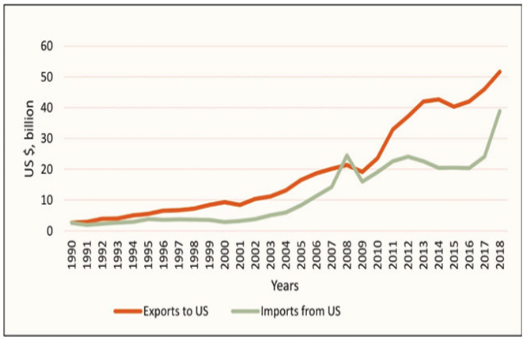
Exchange rate has oscillated a share from 1990-1991 Indian rupee had drop over by virtually 20% in the fiscal year. Results of break down basics of exports incomes and imports posters show the crucial role of change in exchange rate.

According to the study of Franck and Young (1972), the stock market and exchange rates are different. When compared to each other and interrelated in some cases. It has been examined in (2003) by Bhattacharya and Mukherjee about the stock prices and financial sector of currency in India and found no important integration.

Both has bidirectional relationship between the two variables. They also have little or more impact on each other. Yu (1997) conducted the study by using daily data for the period 1993-1994 on three Asian countries Hong Kong, Tokyo and Singapore.

The relationship between the exchange rate and stock market may vary and different. It depends up on the Geographical, Economic conditions relations with the international world.

The results between the different countries might be due to the trade volume, Equity economic relations and risk assessment. The impact of both variables may not be estimated because it may be unidirectional, bidirectional, multidirectional.



OBJECTIVES:

- To analyze dependency of the stock market on exchange rates.
- To understand the currency market and the concept of exchange rate and currency fluctuation.
- To analysis the factor affecting the demand for a currency.
- To find the relationship between exchange and currencies like USD, Euro and Pounds.

METHODOLOGY:

In order to check interaction between stock price and exchange rates, firstly it is essential to determine whether the data is collected are stationary or not.

1. Source of data:

The present study depends up on the secondary data only. The daily data on NIFTY and varies currency values against the Indian rupee has been ,takes from the website of the national stock exchange, money control, Yahoo finance and investing.

2. Sample Size:

The study has considered 1998 trading days' data from Jan 2011 to Dec. 2015.

3. Tools and Techniques: Regression Analysis

a) Multi regression:

The regression analysis helps us to measure impact of the independent variable on Dependent variable. The R-square value in the regression analysis calculation measure the total impact of independent variable on dependent variable. The analysis also generates the co-efficient and corresponding probability values. If the probability value is less than 5 percent of a particular variable then we can consider that the independent variable has a significant impact on the dependent variable

b) R-Square:

Is the percent of the variable in the dependent variable explained by the independent variable? It also called the co-efficient of the multiple of determination.

Nifty=B0+B1*X1+B2*X2+B3*X3

C) Adjusted R square:

When there are large number of self-determining variable, it is conceivable R square may become artificially large, simply because some independent variable unplanned differences explains minor parts of the differences of the dependent variable. It is so fundamentals to adjust the value R square as the quantity independent variables growths. And normally adjusted R Square is less than the R square.

LIMITATIONS:

- Foreign currency effects are gains or losses on foreign investments due to changes in the relative value of assets denominated in a foreign currency.
- A rising domestic currency means foreign investments will have lower returns when converted back to the local currency.
- On the other hand, a declining home country currency will increase the domestic currency returns of foreign investments.
- An investor will gain the most when the value of their international investment goes up along with the currency.
- Foreign currencies can amplify losses as well as gains.
- Currency-hedged ETFs allow retail investors to take positions in foreign stocks and bonds without having to worry about foreign currency effects.
- Foreign investments are complicated by currency fluctuations and conversions between countries. A high-quality investment in another nation may lose money because that country's currency declined.
- When investing in foreign securities, returns are impacted by both the performance of the primary investment itself and the foreign currency.
- Foreign currencies can amplify losses as well as gains. Between 2010 and 2019, U.S. stocks and the U.S. dollar both tended to outperform in international markets.
- As a result, Americans investing in foreign markets often had to deal with lower returns from stocks and currency losses at the same time.
- International investors may choose to hedge against risks from undesired movements in foreign currencies.
- They may hedge because they are bullish on a foreign company stock index and bearish on the country's currency.

ANALYSIS:

We can analyse the stock market related to currency exchange rates by using the example of.

DEMONETIZATION:

On November 8, 2016, Prime Minister NarendraModi announced the demonetization of Rs. 500 and Rs. 1,000 currency notes. Furthermore, the government gave two months to deposit demonetized notes in any bank.

Demonetization is an economic process in which a country's currency unit is no longer legal tender.

A currency unit is what we would commonly refer to as physical money, such as banknotes and coins.

REASONS FOR DEMONETIZATION:

Although demonetization is rare, countries around the world have conducted demonetization measures for various reasons.

- Governments may choose to undergo demonetization if the currency gets out of control, due to problems like hyperinflation.
- Demonetization can also be used to prevent criminal actions, such as counterfeiting, terrorism or tax evasion

When demonetization occurs, the country's currency unit is essentially worthless, as it can no longer be used to purchase goods and services.

At times, countries may also decide to reinstate discontinued currency as legal tender through a process known as remonetisation.

Demonetization causes highly decreasing in the rates of stock market and it also affects the future market position.

Demonetization is a form of economic intervention, where a country moves to replace one form of currency with another. At the beginning of the demonetization process, the old currency is discontinued and pulled from circulation to be replaced with new forms of money.

In other cases, demonetization occurs to implement a new currency standard. For example, in 2002, the European Union introduced the euro, a central currency that would replace the existing currencies of several nations. In adopting the common currency, countries across Europe discontinued their currencies and introduced the euro as the standard across the European Union.

Reduces various criminal activities

Prevents tax evasion

Promotes a cashless economy

- 2016 is not the first instance of demonetization in India. In fact, demonetization happened in India even before 2016.

- In 1946, the Reserve Bank of India had demonetized Rs. 1,000 and Rs. 10,000 currency notes which were then under circulation.

- In 1954, the Government introduced new currency notes of Rs. 1,000, Rs. 5,000 and Rs. 10,000.

- In 1978, the Moraji Desai Government demonetized Rs. 1,000, Rs. 5,000 and Rs. 10,000 to curb illegal transactions and anti-social activities.

DEMONETIZATION AFFECTS CURRENT EXCHANGE RATES AND STOCK MARKET:

Literature studies have taken different events to study variation in market behaviour, among which demonetization stands as a prime event where the whole economy is disrupted. The impact of this disruption has also affected the stock market and its return.

Modi's government has announced the demonetization of the high-value banknotes of Rs. 500 and Rs. 1000. The move has polarized the entire country between those who are in support of the idea and those who are not. This move has also shown its impact on the Indian stock markets. A number of investors have started to withdraw their capital from the share markets; while some did it due to lack of funds, there are others who are expecting a further fall and hence are looking for an opportunity to buy shares at a lower level.

The mutual funds are expected to get benefited from demonetization in the long term. With the banks to reduce the fixed deposit rates soon, more people would shift their investments towards mutual funds to earn more returns from inflation. As good equity mutual fund companies invest in strong stocks, one can expect to receive good results with a low price investment.

A negative correlation was found between the foreign exchange rate and sensex after demonetization. It was found that exchange rate has a significant impact on sensex.

Currency demonetisation, rather Demonetisation of Currency Notes, does not directly affect the foreign exchange rate of a country. However, it may have an indirect effect on the exchange rate since Demonetisation of currency notes could reduce the GDP growth for a few quarters.

- High deposits in the banking system
- Deposit rates slashed
- Attractive borrowing rates

FINDINGS:

It suggested that a positive relationship between stock prices and exchange rates exists when local currency depreciates and local firms become more competitive which leads to an increase in their exports. This will result in an ultimate increase in stock prices.

If the currency exchange rates decrease automatically the stock market value will be decreasing automatically and it also affects the market in the future.

1) Investments on the stock market will be decreased automatically when the currency value decreases.

2) During the Demonetization, the stock market and the currency rates is low, and it also affects the future.

3) Demonetization is one of the examples for the decreasing of Currency exchange rates and stock market.

4) Demonetization has become profitable and also problematic to for the Indian economy.

5) Stock market value will be increased when the investors invest the money in the market.

6) The stock market value will be decreased when the Currency value will be decreased

CONCLUSION:

How Currency Fluctuation will affect the Stock Market

The investors know that a part of their equity holdings will be exposed to currency fluctuations. When it comes to foreign currency movements, the company source and revenues is important because the company is based on them, and also in the United States. Here the currency fluctuation can affect stocks and also the stock market.

Strong Dollar: Always not good: The US dollar fluctuates in value against the world's wide currencies. For the investors, a strong dollar is not always good thing. An investor buys shares of ABC., which derives one- third of its revenue on Bangladesh; one -third of Euro zone and one -third of the United States, in a quarter, then the euro and taka are weak against the dollar. Upon converting the revenue earned in those areas into the dollar and calculating that quarter's profit.

Benefits: Weak Dollar

Just as a strong dollar can be a drag on a company's position, a weak dollar can be useful to the company and its shareholders. Using the example of ABC; assume that the euro and taka were strong against the dollar during the quarter. That means it takes less of those currencies to buy more socks in the market.

Volatility

One of the main reasons U.S. stocks often appears less volatile than their foreign counterparts is because some foreign currencies are themselves volatile. Studies have shown that increased currency risk can mean higher portfolio volatility and perhaps hinder an investor's overall return.

Rupee appreciate: which exports expensive and imports cheaper and it deals with industries of with high imported inputs engineering, drugs, Pharmacy,Gems and jewellery.

Rupee depreciate: which exports is cheaper and imports is expensive and it deals with industries of IT, textiles and automobiles, hotels, tourisms, etc.

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