The Impact of Monetary Policy on Stock Market Performance in Sri Lanka

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ABSTRACT

Introduction: An understanding of stock market volatility and its macroeconomic causes is important in assessing investment and leverage decisions of emerging economies especially where the market consists of risk-averse investors. Therefore, the objectives of the current study are to identify the volatility of stock return in Colombo Stock Exchange (CSE) and investigate the influence of monetary policy variables to stock market return.

Design/ Methodology/ Approach: This study incorporated stock returns generated through ASPI index as dependent variables and money supply, interest rate, inflation rate and exchange rate as explanatory variables on the monthly basis from 2008 January to 2018 December. When considering about the data analysis, Generalized Auto Regressive Conditional Heteroskedasticity (GARCH) Model was used to find the presence of the stock market volatility on CSE.

Findings: The finding of GARCH model discovered that interest rate has positive significant impact on ASPI return. Also, money supply has a negative significant impact on ASPI return. But exchange rate and inflation rate have insignificant impact on ASPI return.

Conclusion: The change of monetary policy is mostly impacted to the share returns of the companies which are highest market capitalization in Sri Lankan context.

Keywords: *All Share Price Index Return, Monetary Policy, GARCH, Volatility, CSE*