

Most Affected Stock Market Index from Macro Economic Shocks: Evidence from Sri Lanka

Gallage, I. U.¹, Wijesinghe, M. R. P.² and Dissanayake, D. M. U. H.³

The Colombo Stock Exchange (CSE) is the only share market that operates in the Sri Lankan economy. All Share Price Index (ASPI) and Standard and Poor Sri Lanka 20 (S&P SL20) are the two stock indices that operate in the CSE. Macroeconomic factors play a vital role in determining the share market performance in a country. The purpose of this research is to identify which stock market index primarily affects macroeconomic shocks. We incorporated stock returns generated through ASPI and S&P SL20 index as dependent variables and real GDP, real interest rate, inflation rate and exchange rate as explanatory variables. We employed quarterly data from 2008 Q1 to 2018 Q2 using Vector Error Correction Model (VECM) to analyze the data. Based on the results, it can be concluded that there is a significant negative long-run relationship between macroeconomic variables and S&P SL20 index return. Further, all the macroeconomic variables have a short-run relationship with S&P return and a unidirectional relationship between S&P return and real interest rate in the short run. The results also indicate that S&P SL20 index is the most affected stock market index from macroeconomic shocks in Sri Lanka.

Keywords: All Share Price Index, Macroeconomic shocks, S&P SL20 Index, Sri Lanka

¹ Department of Finance, Faculty of Commerce and Management Studies, University of Kelaniya, Sri Lanka [uvindugallage@gmail.com]

² Department of Finance, Faculty of Commerce and Management Studies, University of Kelaniya, Sri Lanka [ruwanmrp@kln.ac.lk]

³ Department of Finance, Faculty of Commerce and Management Studies, University of Kelaniya, Sri Lanka [uththar_2019@kln.ac.lk]