ABSTRACT

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Stock market plays an important role in the economic development of a country. The relationship between stock market returns and macroeconomic variables is well documented for the US and other major economies. However, few studies focused on developing countries.

This paper examined the effects of the macroeconomic variables such as interest rate, exchange rate, inflation rate, and industrial production index on the returns of the stock market indices of Indonesia, Malaysia, Philippines and Thailand using multiple regression analysis. The study also described the trends of the variables from 1993 to 2009.

Data for stock market index and macroeconomic variables of the Philippines were obtained from Bangko Sentral ng Pilipinas. Data for other countries were gathered from the International Financial Statistics of the International Monetary Fund and Reuters database. The main objective of the study is to analyze the effects of the macroeconomic variables on stock market returns of selected ASEAN countries.

Results of Granger causality test showed that stock market could be used as a leading indicator of some macroeconomic variables such as exchange rate, inflation rate, and industrial production index which is in line with the theory. Other macroeconomic variables, such as the discount rate and inflation rate, were found to lead stock market returns.

On the other hand, multiple regression analysis provided evidence that the effect of these variables on stock market returns vary across countries except for the exchange rate which was found to have a significant and positive effect on stock market returns for all. Optimal lags and forward were also utilized in the study. Based on the empirical results, conclusions of the efficient market hypothesis (EMH) are thrown in doubt. This claim is based on the results that a relationship was found to exist between macroeconomic variables and stock prices. This means that the behavior of stock market may be predicted, contrary to the EMH conclusions. Test also showed that the hypothesis of the study is in line with the Arbitrage Pricing Theory which states that inflation has a negative effect on stock market returns and industrial production index turns out to have a positive effect. For this reason, policymakers may need to re-examine their economic policy because of its effect on stock market returns.