

BEHAVIOUR OF SECURITIES MARKET IN NEPAL

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RECOMMENDATION

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DECLARATION

I hereby declare that the work done in thesis entitled “**Behavior of Securities Market In Nepal**” has been submitted to Lumbini Banijaya Campus Faculty of Management, Tribhuvan University, is my own created work reported in the form of partial fulfillment of the requirement of Master's Degree in Business Studies (MBS) course under the guidance of respected teachers Rajendra Lamsal, Lumbini Banijaya Campus.

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ABBREVIATIONS

AGM	:	Annual General Meeting
AMEX	:	American Stock Exchange
B.S	:	Bikram Sambat
BODs	:	Board of Directors
BSE	:	Bombay Stock Exchange
CATS	:	Computer Assisted Trading System
CBS	:	Central Bureau of Statistics
Fig	:	Figure
FY	:	Fiscal Year
GDP	:	Gross Domestic Product
i.e	:	That is
Ltd	:	Limited
MBS	:	Master Business Studies
MOF	:	Ministry of Finance
NEPSE	:	Nepal Stock Exchange
NGO	:	Non Government Office
NIDC	:	Nepal Industrial Development Corporation
NO.	:	Number
NPC	:	National Planning Commission
N.G	:	Nepal Government

IPO	:	Initial Public Offering
NRB	:	Nepal Ratra Bank
NYSE	:	New York Stock Exchange
OE	:	Organized Securities Exchange
OTC	:	Over the Counter Market
P/E Ratio	:	Price Earning Ratio
Pvt	:	Private
Rs	:	Rupees
SEBON	:	Security Board of Nepal
SEC	:	Security Exchange Centre
TU	:	Tribhuvan University

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CHAPTER -I

INTRODUCTION

1.1 General Background

Each and every business enterprise requires short-term, intermediate and long-term capital funds for the smooth operation and expansion of the organization's activities. Among these types of funds, the long-term funds are highly significant for future growth and prosperity. Most of the business organizations generate long-term funds from the financial market & secondary market. The purpose of financial market in an economy is to allocate saving efficiently during the period of time, -a day, a week, or a quarter- to consumption (Van Horne, 2000).

The secondary stock market efficiently occupies an important place in financial management. If there are certain imperfections in the stock market, wise investors attempt to utilize them to achieve a better return. Stock market efficiency cannot be tested directly. However, by postulating some security price behaviors, one can have some ideas about market efficiency. History indicates that much time and effort have been devoted in the field of financial research to investigate the movement of share prices (Regmi, 2005).

As the Nepalese economy is in developing phase, so in order to speed up this pace of development, financial sectors have critical roles, as they can pool scattered saving for capital formation. The public investors are interested to invest their savings in the common stocks of the financial institutions. As a result, such institution's shares are being traded among the investors in the secondary market in larger volume every day.

Today, however as the part of a general trend towards liberalization, globalization, privatization and the diminution of the role of the state, and enhance of the market has become common feature of the economy in which various reasons in the world is sweeping the globe the north and the south, and remains the east as well an important feature of the development of the financial sector, many developing economies are having a very fast growth of markets. Only the capitalists and economist as well as those for the centrally planned economies do not favor the establishments and expansion of this market.

Therefore, stock markets have become global markets of fact and arising the scholar and practitioners to seek for more knowledge of the real place of the trading and tracking of the securities (Adhikari, 2004).

For efficient mobilization of financial resources, the financial market has an intermediately role to bridge funds from surplus units to deficit units secondary market provides a forum in which suppliers and demanders of funds can transact business funds directly. Especially, secondary market primarily refers to stock market and capital market. The stock market is created by a financial relationship between suppliers and demanders of short-term funds, which have maturities of one year or less. Most of the money market transactions are made in marketable securities, which are short-term debts instruments such as treasury bills, commercial papers and negotiable certificates of deposit issued by government, business and financial institution. The money market exist because certain individuals businesses, governments, financial institutions have temporary idle funds that they wish to place in some type of liquid assets or short-term, interest-earning instruments. At the same time, other individual's businesses, governments, financial institutions find themselves in need of seasonal or temporary financing.

Capital market also plays a very important role in the national economy. Capital market facilitates the allocation of the funds between the savers and borrowers. This allocation will be optimum if the capital market has efficient pricing mechanism. If the capital market is efficient, the current share prices of the companies fully reflect the available information and there will be no question of the share price being overpriced or under priced. Capital market is concerned with the source of long-term finance for businesses, governments, and financial institution. The funds collected in this market are arisen and traded by long-term financial instruments such as equities and bonds for more than one year.

1.1.1 Securities Markets

A security market of financial markets can be defined as a mechanism for bringing together buyers and sellers of financial assets in order to facilitate trading. One of its main function is “price discovery” that is, to cause security price to reflect correctly

available information. The more quickly and accurately price discovery is achieved, the more efficiently financial markets will direct capital to its most productive opportunities, there by trading to greater improvement in public welfare.

As far as securities market is concerned, it is an important constituent of capital market. It has a wide term embracing the buyers and sellers of securities and all the agencies and institutions that assist the sale and resale of corporate securities.

Securities are traded in a market called securities markets. Although securities markets are concentrated in a few locations, they refer more to Mechanism, rather than to place, designed to facilitate the exchange of securities by bringing buyers and sellers of securities together. In other words, people and organizations wanting to borrow money are brought together with those having surplus funds in the securities market.

Securities Such as equities, short and long-term debt instruments, derivatives etc are the products that are traded in the security markets, institutions such as investment bankers and securities firms, securities issuing institutor such as government and corporate bodies and the participants of the securities markets. Securities markets major function is to provide line between saving and investment there by facilitating the creation of new wealth.

The development of a sound securities market with its constituent financial institution is one of the mechanisms, which enables the efficient transformation of savings from the hands of surplus spending units to those of deficit spending ones who can use them more productivity and risk aversion.

The existence of markets for securities is of advantage to both issuers and investors. As to their benefit to issuers, securities maker assist business and Government in raising funds. In a society with private ownership of the means of production and distribution of goods and services, savings must be directed towards the investment in industries where capital is must productive. Government must also be able to borrow for public improvements. Market mechanism makes possible the transfer of funds from surplus to deficit sectors efficiently and at low cost.

According to wheeler, the securities market includes:

1. Activities relating to the organizational distribution and trading in of securities.
2. Organizations, which facilitate these securities.
3. Individuals and institutions, which buy and sell securities.
4. Rules, regulations, customers and practices that control the organization and conduct of business.

In the broadcast term, securities market can be classified into primary markets and secondary markets.

Primary market

The primary markets are media through which new financial assets are issued or generated. They are the media through which the demands and suppliers of today's funds, the creators and acceptors of financial claims, meet. In these primary markets, financial assets are created and exchanged, satisfying in the part of the financial needs of both demanders and suppliers of today's fund. At present concept, it is the market for direct issuance of government securities. The primary market of country is dominated by the government securities due to the existence of insignificant new issue market for industrial securities.

Securities available for the first time are offered through the primary securities markets. The issuer may be a brand new company or one that has been in business for many years. The securities offered might be a new type for the issuer or additional amounts of a security used frequently in the past. The key is these securities absorb new funds for the coffers of this issuer.

The primary securities market includes all transactions that result in the accumulation of financial capital by firms. Governments or individuals to be used in consumption or real capital investment. The participants in this process are many and varied but an important segment, includes the money brokers who acts as a middlemen in the process of exchanging securities for fund. These brokers provide invaluable services. Their principal role is to assist in the pooling of funds by the certain of security forms that will appeal to the ultimate investors.

Primary market transactions are normally effected through the issuance of short and long-term bonds and other debt instruments and through the issuance of common and preferred stocks.

All securities, whether in the money of capital markets, are initially issued in the primary market. This is the only market in which the company or government is directly involved in the transaction and receives direct benefit from the sale of securities. Once securities begin to trade among individual, business, government or financial institution, savers and investors, they become part of the secondary market.

Primary market is distinguished by the flow of funds between the market participants. Instead of trading between investors as in the secondary markets, participants in the primary market buy their assets directly from the source of the asset. Once the assets or securities are sold in the primary market, they begin trading in the secondary market.

Secondary Markets

Secondary markets are markets for existing assets, which are currently traded between investors. These markets create the piece and allow for liquidity. If secondary markets did not exist, investors would have no place to sell their assets. Without liquidity, many people would not invest at all.

Secondary (indirect) securities markets allow outstanding securities to be traded from old to new owners. The advantage of secondary market is to provide liquidity or cash and investment opportunities to investor and to make certain assets more attractive to buyers and sellers. Secondary market comprises the stock exchange, the over the counter market.

The function of the secondary markets is to provide liquidity for securities purchased in the primary markets. Once investors have purchased securities in the primary markets, they need a place to sell those securities. Without the liquidity of the secondary market, firms would have difficulty raising funds for productive purposes in the primary markets. (<http://www.nepalstock.com>)

1.2 Focus of the study

In Nepal, there has been a huge amount of unutilized saving funds with public due to the lack of wider investment opportunities that provide good return. Most of the public investors are not well knowledgeable about the real financial strength and weakness of the public companies and they cannot well analyze and interpret the real financial position of the company according to the available data and information. Hence, this study may provide a boon to the investors to think about restructuring their investment portfolio. Furthermore, the potential investors can take better decisions based on the findings of the study.

1.3 Statement of the Problem

Today, the capital market investment plays the key role in the economic development of the country. The economic, social, and political interference directly influences it. The phase of development of the capital market in any country and its effective growth is depended upon the collective economic condition, saving and investment opportunities etc.

Though there are various institutions in touch with capital market, they have not been able to display the better performance as expected by the investors. On the other hand, the investors themselves are not responsible for not having self-judgment and self-control in the choice of securities for investment. Hence, most of the investors are carelessly investing in shares.

The present political instability, economic imbalance, ineffective implementation of liberal economic policy of the country has arisen negative symbols in the economy of the country. The price of the securities, particularly, common stock has been randomly fluctuating and declining over the past years due to political causes. As a result, some companies were liquidated and some are working with hardship in the market. The policy makers are unable to make the proper policy for the development of the stock market. Most of the government level efforts for the development of the stock market have inadequately contributed.

Regarding the share price movement in the markets, one approach assumes that market is inefficient in pricing of shares. In which the technical analysis theory argues that the analysis of the historical prices and trading of stocks provides meaningful information, which provides a picture of future price movement to the investors. It attempts to explain and forecast in security price by studying the market data rather than information about a company or its prospects (Bhalla, 1997).

The second approach, the efficient market theory, which argues that market, is efficient in pricing the shares. In situation where stock price movement follows random walks and at every point in time actual prices represent good estimate of its intrinsic values, general investors tend to select any security randomly to from his/her optimum portfolio (Fama, 1965).

In the primary market, the price of common stock is par value but in secondary market the price may be equal to par value, more than or less than par value. Various factors affect the price of share in the secondary market. Thus; stock price in secondary market is the main issue of this study. The following are some question regarding stock price of listed company's determination of secondary market in Nepal.

This present study is carried out to answer the following research questions:

1. What are the problems of Nepalese stock market?
2. What are the prospects of Nepalese stock market?
3. Is growth rate of Nepalese stock market satisfactory?
4. Are people satisfied from the information provided by NEPSE and SEBON?

1.4 Objectives of the study

Objective of the study are guidelines by which the study can be conducted in a systematic manner. The main objective of the study is to study, examine and analyze the behavior of security price in the stock market. The specific objectives of this study are follows:

- 1 To analyze the behavior of stock price of secondary market in Nepal.
- 2 To examine the trend of securities market and volume of stock traded on the secondary market.
- 3 To measure composition of sector and their market capitalization of listed companies in NEPSE.
- 4 To analyze the investor's view regarding the decision on stock investment.

1.5 Significance of the study

Most of the people in our Nepalese society inhabit under the poverty line. They have low earning capacity. Thus, they cannot think of investing money due to risk and they have no blond and precise information about the financial strengths and limitations of the companies which they are going to invest. The investors cannot interpret the financial position of the company based on available data and information to take the correct decisions. Hence, this study is very beneficial to all the parties involved in the stock market. It provide the guidance to the investors of stock market

1. The study may draw the attention from every corner of entrepreneurs and investors and other academicians and other interested parties.
2. This study is very useful to potential investors who are interested to know the effect of price trend, volume of the stock traded, and impact of signaling factors on NEPSE index.
3. . This study will contribute literature to further researches in this area.

1.6 Limitations of the study

Time limitation, resource constraints, availability of materials and objectives of the study confine the study. Thus, following are the limitations of the study:

1. Most data and information are secondary and the findings and conclusions are strictly dependent on the reliability and accurateness of those data because most of the analysis and interpretation have been done based on the available secondary data and information.
2. Due to the lack of timely and easily available data, reporting errors might occur.
3. Only the common stocks have been taken into the account for the purpose of the study.

4. The study covers the past and present state of stock market in Nepal hence does not make any projection about the future.
5. This study is being conducted for the partial fulfillment of M.B.S. degree in management. Therefore, it is not a comprehensive study.

1.7 Organization of the study

The chapter schemes of this proposal comprise a total of five chapters which have been briefly described as follows:

Chapter One: Introduction

Introduction chapter is the first chapter which includes the Background of the study, Statement of problem, Objective of the study, Significance of study, and Limitation of study.

Chapter Two: Review of the Literatures

This part includes Theoretical reviews and Reviews of the previous studies This is also devoted to theoretical analysis and brief review of related literature available, Journal, article review etc.

Chapter Three: Research Methodology

Research design, Population and Sample, Nature and sources of data, data collection procedures, tools used for analysis and limitation of the methodology have been included in this chapter.

Chapter Four: Data Presentation and Analysis

It deals with presentation and analysis of relevant secondary data and information through a definite course of research methodology.

Chapter Five: Summary, Conclusion and Recommendation

The last or fifth chapter will contain summary, conclusion and recommendations of the thesis

CHAPTER- II

REVIEW OF LITERATURE

2.1 Introduction

This chapter gives the information on the literature that is available in the topic. Mostly, it includes those available relevant studies done inside the country and outside the country done by scholars and academicians.

The first section of this chapter describes the behavior of share prices theoretically. It comprises of technical analysis, fundamental analysis and efficient market theory. The second section is limited to the review of related literature carried out previously in the Nepalese as well as in the foreign context.

2.2 Historical Development

The Nepalese stock market is just coming of age. Therefore, it has been changed in various new forms. After the enactment of the Company Act in 1936 for the first time, various considerable events have been observed in the development of security market. The history of securities market began with the floatation of shares by Biratnagar jute Mills ltd. and Nepal Bank Ltd. in 1937. Introduction of the company Act in 1964, the first issuance of Government Bond in 1964 and the establishment of securities Exchange center Ltd. in 1976 were other significant development relating to capital markets

securities Exchange Center (SEC) was established in 1984 with an objective of facilitating and promoting the growth of capital markets. Before the conversion into stock exchange it was the only capital markets institution undertaking the job of brokering, underwriting, managing public issue, market making for government bonds and other financial services. His Majesty's Government, under a programmer initiated to reform capital markets converted securities Exchange Center into Nepal stock Exchange in 1993. Nepal Stock Exchange, in short NEPSE, is a non-profit organization, operating under Securities Exchange Act, 1983. The basic objective of NEPSE is to impart free marketability and liquidity to the government and corporate

securities by facilitating transaction in its trading floor through member, market intermediaries, such as broker, market makers and securities dealers. At the same time, the Securities Exchange Board of Nepal (SEBON) was constituted to oversee the regulatory provisions. Presently, in Nepal, NEPSE is the only one secondary market (organized stock exchange) of the country for security transactions. Other forms of secondary market such as OTC market, the third and fourth market are not initiated till date.

NEPSE appointed five market makers and twenty-five brokers to smooth daily transaction of buying and selling of securities under its restrictive programmed in 1993.

2.3 Introduction of Security Board of Nepal (SEBON)

Securities Board, Nepal was established in May 26, 1993 under the provision of Securities Exchange Act, 1983 (first amendment). Since its' establishment, SEBON has been concentrating its efforts to improve the legal and statutory frameworks which are the bases for the healthy development of the capital market. As a part of its' continuous effort to build a sound system, the Securities Exchange Act, 1983 was amended for the second time on Jan 30, 1997. This amendment paved the way for establishing SEBON as an apex regulatory body as it widened the horizon of SEBON by bringing market intermediaries directly under its' jurisdiction and also made it mandatory for the corporate bodies to report to SEBON annually as well as semi-annually regarding their performance. Although the second amendment in the act established direct relationship of SEBO with the market intermediaries and the listed companies, supremacy in its jurisdiction is yet to be established and clearly recognized.

2.4 Introduction of Nepal Stock Exchange (NEPSE) Ltd.

Nepal Stock Exchange was established on 1993 under Securities Exchange Act 1983. Nepal Stock Exchange was known as securities Exchange center earlier. Securities Exchange Centre was established with on objective of facilitating and promoting the growth of capital markets. The major tasks undertaken by Nepal stock Exchange are brokerage, undertaking, managing public issue, making market for government bonds

and other financial services. Nepal stock Exchange is a non profit organization operating under securities Exchange Act, 1983.

It was established with joint effort of Nepal industrial Development Corporation and Nepal Rastra Bank to mobilize the public saving for ensuring public ownership in the shares of public limited companies. In order to promote the stock exchange business, the center made a series of studies in the beginning regarding both the public limited companies and undertaking the business of buying and selling of securities. Recently, NEPSE has adopted the 'Circuit Breaker' system by which the speculation and fluctuation of share price is controlled. This has led the investors feel secured about their investment in certain extent.

2.5 Capital structure

Table 2.1
Ownership structure of NEPSE

S. No.	Shareholders	Rs. In million	Percentage (%)
1	NG	20.48	58.67
2	NRB	12.08	34.60
3	NIDC	2.14	6.13
4	Members	0.21	0.60
Total		34.91	100

(Source: NEPSE: Annual Trading Report, 2004/2005)

The authorized capital of the NEPSE is Rs. 50 million. Out of the Rs. 50 million issued capital, Rs. 20.48 millions (58.67%) is subscribed by N.G. Similarly, Rs. 12.08 million (34.60%) is subscribed by NRB, Rs. 2.14 million (6.13%) is subscribed by NIDC and Rs. 0.21million (0.60%) is subscribed by rest of the licensed members

2.6 Theoretical Review

In the present situation, more and more people are being interested in the investment sector as in other economic sectors. Most of the developing countries are enhancing their economy by the help of contribution in the investment sector. Hence, business cycle theorists thought of the need of tracing the evolution of various economic variables over the long run of time. Many steps are performed in the investment

process. Among them, security analysis is one. It includes the inspection of the various individual securities or groups of securities within the broad categories of financial assets. Mainly, there are two approaches in the case of behavior of stock market prices. They are as follows:

Classical approach

Efficient market theory approach

Classical or conventional approach includes fundamental Analysis theory and Technical Analysis Theory. Under efficient market theories, there are three forms of efficient market hypothesis. Classical approach assumes market inefficient whereas the efficient market theory argues that the market is efficient prior to the development of the efficient market Theory, investors were generally divided on to two groups, fundamentalists and technicians (Reily, 1986: 347).

2.6.1 Classical Approach

This approach comprises of fundamental analysis and technical analysis theories. Technical analysis talks about the stock prices on the basis of past price behavior of the company but the fundamental analysis talks about the stock prices on the basis of earning and dividends of the company.

2.6.1.1 Technical analysis

Technical analysis is probably the most controversial aspect of investment management. That technical analysis is a delusion, that it can never be any more useful in predicting the stock performance than examining the insides of a dead sheep in ancient Greek tradition. The term 'technical analysis' is used to mean fairly wide range of techniques, all based on the concept that past information on prices and trading volume of stock gives the enlightened investor a picture of what lies a head. It attempts to explain and forecast changes in security prices by studying only the market that is rather than information about company or its prospects as is done by fundamental analyst (Bhalla, 2001: 409).

In its simplest form, technical analysis involves the study of stock market prices in an attempt to predict future price movements. Past prices are examined to identify recurring trains or patterns in price movements. Then more recent stock prices are

analyzed to identify emerging trends or patterns that are similar to past ones. This analysis is done in the belief that these trends or patterns repeat themselves. By identifying an emerging trend or pattern, the analysts hope to predict the accurately future price movements for a particular stock (Alexander, Sharpe and Bailey, 2001: 12).

Technical analysis can be defined as the use of published market data for the analysis of both the aggregate stock market and individual stocks. It is some times called market or internal analysis (Jones, 1988: 396).

Hence, the technical analysis is based on the assumption that past information of prices and trading of stocks gives some picture of the future prices of stocks. Technicians try to predict security prices rather than security value, particularly trends in the price changes.

Technical analysis is based on the widely accepted premise that security prices are determined by the supply of, and the demand for, securities. The tools of technical analysis are therefore designed to measure certain aspects of supply and demand (Francis, 1991: 521-22).

Technical analysis involves the examination of past market data, such as price and the volume of trading, which lead to an estimate of future price trends and, therefore an investment decision. Whereas fundamental analysts use economic data that are usually separate from the stock or bond market, the technical analyst believes that using data from the market itself is a good idea because "the market is its own best predictor." Technical analysts base trading decisions on examinations of prior price and volume data to determine past market trends from which they predict future behaviour for the market as a whole and for individual securities (Reilly and Brown, 2000: 870).

Technical analysts maintain that the price of a share at any time (present price) is the balance struck by buyers and sellers at a point in time price movements take place on account of changes in buying and selling pressures. This occurs in account of diverse internal and external factors (profits, political environment, prediction and the likes). Prices stabilize when equilibrium between buyers and sellers is achieved. They believe that record of price movements over a period of time in the past, as the whole theory is based on the assumption that history repeats itself. That human nature does

not change and that man is likely to repeat his patterns of past moments will repeat themselves in the future (Palat, 1991: 172).

The technical analysis believe that the price of a stock depends on the supply and demand in the market place and has little relationship to value, if any such concept even exists. Price is governed by basic economic and psychological inputs so numerous and complex that no individual can hope to understand and measure them correctly. The technical thinks that the only important information to work from is the picture given by price and volume statistics.

The technical sees the market, disregarding minor change, moving in discernible trends, which continue for significant periods. A trend is believed to continue until there is definite information of the change. The past performance of a stock can then be harnessed to predict the future. The direction of price change is as important as the relative size of the change. With this various tools, the technical attempts to correctly catch changes in trend and take advantage of them (Bhalla, 2001: 409).

Technicians seek to forecast security prices rather than security value especially trends in the price changes. Price and volume are the primary tools of the technical analyst. Technicians believe that the forces of supply and demand show up in patterns of price and volume. Volume data are used to gauge the general condition in the market and to help assess its trend. The evidence seems to suggest that rising (falling) stock prices are usually associated with rising (falling) volume. If the stock prices but volume activity does not keep pace, technical analyst would be skeptical about the upward trend. A downside movement from some pattern or holding point, accomplished by heavy volume, would be taken as a bearish sign (Jones, 1988: 396).

Technical analysis however may be useful in timing a buy or sell order than may be implied by the forecast of return and risk. For example, the technical analysis may reveal that a drop in price is warranted. Postponement of purchase, then, if the technical analysis is correct, will raise the forecast holding period yield (HYP). Conversely, a sale order might be postponed because the charts reveal a raise in the price of the security in question (Fisher and Jordon, 1995: 510).

Typically, technical analyst records historical, financial data on charts; study these charts in search of patterns that they find meaningful and endeavor to use the patterns to predict future prices. Some charts are used to predict movements of market index and still others are used to predict the action of both individual assets and the market (Francis, 1991: 522).

The basic assumptions of technical analysis are listed below:

- 1 Market value is determined by interaction of supply and demand.
- 2 Supply and demand is governed by numerous factors, both rational and irrational.
- 3 Security prices tend to move in trends that persist for an appreciable length of time, despite minor fluctuations in the market.
- 4 Changes in trend are caused by the shifts in supply and demand.
- 5 Shifts in supply and demand, no matter why they occur, can be detected sooner or later in charts of market transactions.
- 6 Some charts patterns tend to repeat themselves (Francis, Edwards and Magee, 1958: 86).

Hence, the technical analyst suppose that changes in the pattern or trend of security prices occur on account of the changes in the demand and supply of the securities, and that crucial insight into these patterns can be obtained by keeping track of price chart. The technical analysts can predict whether the price of a share is on upswing or on the downswing in the days to come. Various studies proved that the technical analysis is helpful in enabling investors to beat the market. Technical analysis, on the other hand, attempts to forecast the future stock prices by analyzing past behavior of stock prices. In general, tomorrow's stock price is affected by the today's price. The direction of price change is important as the relevant size of change. The technicians attempt to catch changes in trend correctly and take benefit of them with the application of various tools.

Technical Tools

The Dow Theory

This tool originated by Charles Dow, founder of the Dow Jones Company is one of oldest and the most famous technical method of analyzing security prices. The aim of the Dow Theory is to identify long-term trends in stock market prices. "According to this theory, it is believed that the market is always considered as having three

movements, all going at the same time. The first is narrow movement from day to day. The second is the short swing, running from two weeks to a month or more; the third is the main movement, covering at least 4 years duration (Francis, Jr., 19 Dec. 1900).

The Dow Theory employs two indicators called Dow Jones Industrial Average (DJIA) and Dow Jones Transportation Average (DJTA). The DJIA is a key indicator of underlying trends, while the DJTA usually serves as check to confirm or reject that signal (Bodie, Kane and Marcus, 2002: 344).

Hence, the forecasting of Dow Theory is less precise. It might work only when a long, wide, upward movement is registered in the market. It is mostly unsteady as a market predictor when the market trend frequently reserves itself in the short or the intermediate term. This theory fails to explain a consistent pattern of the short price movements.

¶1 **Barron's Confidence Index**

The confidence index is usually, but not always, a leading indication. Like most of other technical indicators, the confidence index may sometimes issue erroneous signals and should therefore not be used without confirming evidence from other indicator (Francis, 1991: 531).

In the literal sense, the confidence index is defined as the ratio of high-grade bond yields divided by low-grade bond yields. The ratio is supposed to reveal how willing investors are to take investment risks. Barron's confidence index is constructed by using Barron's index of yields on the high-grade bonds to low-grade bonds (Giri, 2005: 20).

¶1 **Odd Lot Theory**

Odd lotters try to do the right thing most of the time; that is, tend to buy the stocks as the market retreats and sells stocks as the market advances. However, technicians feel that odd lotters are inclined to do the wrong thing at critical turns in the market (Fisher & Jordan, 1995: 515).

This theory deals with the purchase and sales of securities by small investors. These investors perform transaction of less than 100 shares. Some technicians take the ratio of these odd lot purchases to odd lot sales as an indicator of the direction of the future

prices. An increase in the index suggests relatively more buying, a decrease indicates relatively more selling. During most of the market cycle, odd lots are selling the advances and buying the declines.

2.6.1.2 Fundamental Analysis

Fundamental analysis, the second approach to security analysis, tries to identify the real or true value of financial assets. The real value of any kind of financial assets is the present value of the future cash flow given by the assets or expected by the holder. The fundamental analyst attempts to forecast the timing and size of this cash flow, and then converts them into their equivalent present value by using an appropriate discount rate. Once the real value is calculated, it is, thereby, compared to the current market price per share to identify where the security is under-priced or over-priced.

These unusual cases of mis-pricing will be corrected in the future. The price of an over-priced security declines to meet the real value and the under-priced security's price increases to meet the real price. The person utilizes the technique is called a fundamentalist or a fundamental analyst.

Fundamental analysis approach involves the working to analyze various Factors like economic influences, industry Factors, Firm's financial statement and pertinent company information such as product demand, earnings, dividends and management in order to calculate an intrinsic value for the firm's securities. The theory assumes that knowledge about the future of the companies is not perfect. Some stocks are under priced and other is over priced. The investor's task is to study certain fundamental factors that may enable them to select undervalued stock for purchase and sell overvalued stock. After extensive analysis, the investor derives an estimate of the 'intrinsic' value of the security, which is then compared to its market price. If the value exceeds the market price, the security should be acquired and vice versa (Reily, 1986 347).

Fundamental analysis theory claims that at any point of time an individual stock an intrinsic value, which is equal to the present value of the future cash flows from the security discounted at appropriate risk, adjusted discount rate. The value of the

common stock is simply the present value of all the future income, which the owner of the share will receive (Francis, 1991:398)

After estimating the true value of stock of a particular firm, it is compared with the current market price of the common stock to determine whether the stock is fairly priced. Stocks whose estimated value or true value is less than their current market price are known as overvalued and vice versa. Fundamental analysts believe that any notable cases of miss pricing will be corrected by the market in the near future, meaning that prices of overvalued stocks will show unusual appreciation and prices of under valued stocks will show unusual depreciation.

In its simplest form, fundamental analysis being with the assertion that the true value of any financial assets equals the present value of all cash flows the owner of the asset expects to forecast the timing and size of these cash flow and then converts the cash flows to their equivalent present value using an appropriate discount rate (Sharp and Bailey, 2001: 12).

Fundamental analysis use public information to calculate a fundamental value for a share and then offer investment advice by comparing the fundamental value with the current market price. Fundamental analysis is not possible if capital markets are semi-strong form efficient, since security prices will already fully and fairly reflect all publicly available information (Watson and Head, 1998: 31-32).

The objective of the fundamental analysis is to appraise the intrinsic value of the security. The intrinsic value is the true economic work of the financial assets. Therefore, fundamental analysts work to find new information before other investors, so they can get into the position to profit from the price changes they anticipate. Fundamental analysts use different models like Top- Down versus Bottom- Up forecasting, probabilistic forecasting, economic models, financial statement analysis etc. to estimate the value of security in an appropriate manner for making investment decision (Giri, 2005: 14-15).

Some limitations of the fundamental analysis approach are as follows:

- 1 The information and analysis may be itself incorrect.

- 2 Many companies with the help of the creative and innovative accounting and accounting cosmetics disguise the real earnings.
- 3 The entire fundamental approach is based on a rational scientific analysis of the data the market is rarely rational
- 4 The fundamentalist's estimate of intrinsic value may be incorrect. This is not only possible but also probable that he often forecast growth, profit and other factors without grasping all the facts.
- 5 The fundamentalists may not fully understand the economy or the industry, as there are several external factors.

Hence, fundamental analysis is ever-going process because values change in accordance with time. Ideally, revision in analysis should occur wherever new information affecting the future benefits to security holders becomes available.

2.6.2 Efficient Market Theory

An efficient market is defined as a market where there are large numbers of rational profit maximizers actively competing with each trying to predict future market values of individual securities, and where important current information is almost freely available to all participants. In an efficient market, competition among the many intelligent participants leads to a situation where at any point in the time, actual price of individual security already reflect the effects of information based on both on events that have already occurred and on events which as of now, the market expect to take place in the future. In other words, in an efficient market at any point in time the actual price of a security will be a good estimate of its intrinsic value (Fama, 1970 384-85).

In an efficient market, all the relevant information is reflected in the current stock price. Information cannot be used to obtain excess return: the information has already been taken into account and absorbed in the prices. In other words, all prices are correctly stated and there are no "bargains" in the stock market (Bhalla, 2001: 433).

In a competitive market, the equilibrium price of any good or service at a particular moment of time is such that the supply is equated with the aggregate demand. This is the true worth of the goods or services, based on all publicly available information.

The new equilibrium price will hold until another bit of information is available for analysis and interpretation.

In an efficient market, a security's price would correctly reflect the important variables for that security and would represent an unbiased estimate of its investment value (Cheney and Moses, 1992: 746).

An efficient market is one where shares are always correctly priced and where it is not possible to outperform the market consistently except by luck (Pike and Neal, 1996: 41).

Efficiency in this context means the ability of the capital markets to function so that prices of securities react rapidly to new information. Such efficiency will produce prices that are appropriate in terms of current knowledge, and investors will be less likely to market unwise investment. A corollary is that investors will also be less likely to discover great bargains and thereby earn extraordinary high rates of return (Lorie, 1974: 3).

In an efficient market, current market prices fully reflect available information (Fama, 1996: 133). Therefore, if the market is efficient, it uses all the available information to its in setting price.

If a market is efficient, then there is a very important implication for market participants: all investments in that market are zero NPV investments. The reason is not complicated. If prices are neither too low nor too high, then the difference between the market value of an investment and its cost is zero; hence, the NPV is zero. As a result, in an efficient market, investors get exactly what their stocks and bonds are worth when they sell them (Ross, Wethersfield and Jordon, 2003: 405).

The efficient market hypothesis advises that investors cannot expect to outperform the market repeatedly on a risk-adjusted basis over an extended period. This hypothesis is based on the premise that security prices reveal all available information concerning a firm and that security price change rapidly in response to new information. Market efficiency also implies that new information that becomes available, the market quickly analyzes it, and any necessary price adjustments occur rapidly.

The following are the necessities for a securities market to be efficient:

- 1 A large number of rational, Profit maximizing investors exist who actively participate in the market by analyzing, valuing, and trading stocks. These

investors are price takers; that is, one participant alone cannot affect the price of a security.

- 2 Information is free of cost and widely available to market participants at approximately the same time.
- 3 Information is generated in a random fashion such that announcements are independent of one another.
- 4 Investors react quickly and accurately to the new information, causing stock prices to adjust accordingly (Jones, 1988: 425).

The degree of market efficiency has important implications for the economy and for investment decision makers. In an economic sense, it is important that security prices provide accurate signals that can be used to allocate capital resources correctly. Incorrectly priced securities would result in incorrect allocation of capital (Cheney and Moses, 1992: 746). Although efficient market may be very important and pleasing from of a right investment policy.

In an efficient market, liquid capital will channel quickly and accurately where it will do the community the most good. Efficient market will provide ready financing for worth while business venture and drain capital away from corporations that are poorly managed or producing obsolete products. One of the main reasons that some under developed countries do not advance is that have inefficient capital markets, where prices may be fixed or manipulated rather than determined by supply and demand. An efficient market is assumed perfect market in which there are many small investors, each having the same information and expectations with respect to securities; there are no restriction on investment, no taxes, and no transaction costs and all investors are rational, view securities and are risk averse, preferring higher returns and lower risks (Gitman, 2000:265-66).

Although it may not literally be true that all relevant information will be uncovered, it is virtually certain that there are many investigators hot on the trail of most leads that seem likely to improve investment performance. Competition among these many well backed, highly paid, aggressive analysts ensures that, as a general rule, stock prices ought to reflect available information regarding their proper levels (Bodie, Kane and Marcus, 2002: 342).

There are three forms of the efficient market hypothesis

- 1 The "Weak" form asserts that all past market prices and data are fully reflected in securities prices. In other words, technical analysis is of no use.
- 2 The "Semi strong" form asserts that all publicly available information is fully reflected in securities prices. In other words, fundamental analysis is of no use.
- 3 The "Strong" form asserts that all information is fully reflected in securities prices. In other words, even insider information is of no use.
(www.investorhome.com/ehm.html.-17k)

Weak form efficiency, suggests that, at a minimum, the current price of a stock reflects the stocks own prices. In other words, studying past prices in an attempt to identify misplaced securities is futile if market is weak form efficient. Although this form of inefficiency might seem rather mild, it implies that searching for patterns in historical prices that will be useful in identifying mis- priced stock will not work (Ross, Westerfield and Jordon, 2003:407).

Under the semi strong form, all publicly available information is pre assumed to reflect in securities' prices. This includes information in the stock price series as well as information in the firm's accounting reports of competing forms announced information relating to the state of the economy and any other publicly available information relevant to the valuation of the firm (Haugen, 2001:575).

The strong form takes the nation of market efficiency to the ultimate extreme. This form includes private or inside information as well as that which is publicly available. Under this form, those acquire inside information act on it, buying or selling the stock. Their action affect the price of the stock and the price quickly adjusts to reflect the inside information (Haugen, 2001: 575).One obvious way to check the validity of the strongly efficient market hypothesis is to examine the profitability of traders in securities made by insiders to see if the insider's access to valuable information allows them to earn statistically significant trading profits (Francis, 1991: 558).

Therefore strong form of efficient market hypotheses is same to perfect market in which the market prices securities correctly by adjusting quickly to new information whether it is public or private.

2.6.2.1 The Random Walk Theory

The third theory involves study of random walk or efficient market hypothesis. In 1900 a French mathematician, Louis Bachelier wrote a scientific paper suggesting, that day-to-day security price fluctuations were random. His idea is known as the random walk theory (Cootner, 1962: 24-45).

Random walk is a stock market theory that states the past movement or direction of the price of a stock or overall market cannot be used to predict its future movement. Originally examined by Maurice Kendall in 1953, the theory states that stock price fluctuations are independent of each other and have the same probability distribution, but that over a period of time, the prices maintain an upward trend. In short, random walk says that stocks take a random and unpredictable path. The chance of a stock's future price going up is the same as it going down. A follower of random walk believes it is impossible to outperform the market without assuming additional risk.

(www.investopedia.com/university/concepts/concepts5.asp-27k)

The weak form says that the current prices of stocks already fully reflect all the information that is contained in the historical sequence of prices. Therefore, there is no benefit-as far as forecasting the future is concerned- in examining the historical sequence of prices. This weak form of efficient market hypothesis is popularly known as the random-walk theory (Fisher and Jordan, 1995: 540).

The weakly efficient hypothesis stipulates that historical price and volume data for securities contain no information which can be used to earn a trading profit above what could be attained with a naïve buy-and-hold investment strategy (Francis, 1991: 543).

The random walk theory asserts that stock market's price movements will not follow any patterns or trends and that past price movements cannot be used to predict future price movements. In effect, efficient markets depend on market participants who believe the market is inefficient and trade securities in an attempt to outperform the market. (www.greekshares.com/emt.asp)

If the price changes could be used to predict future price changes, investors could make easy profits. But in competitive market easy profits don't last. As investors try to take advantage of the information in past prices, prices adjust immediately until the superior profits from studying past price will be reflected in today's stock price, not

tomorrow's. Patterns in prices will no longer exist and price changes in one period will be independent of changes in the next. In other words, the share price will follow a random walk (Brealey and Myres, 2000: 357-58).

Random walk theory describes whether past prices can predict future. "Random walk theory implies the future path of price level of a security is no more predictable than the path of series of cumulated random numbers. The series of price changes has no memory; that is, the past cannot be used to predict the future in any meaningful way." It means that the current size and direction of price changes is independent and unbiased outcome of previous price changes. The random walk model in share prices actually involves two main hypotheses 1) Successive price changes are independent and 2) the price changes conform to some probability distribution (Fama, 1965: 34-35).

More precisely, in algebraic term,

$$\Pr (X_t = X | X_{t-1}, X_{t-2}) = \Pr (X_t = X)$$

Where the term on the left side of equation is the conditional probability that the price change during time t will take the value X , conditional on the knowledge, the previous price changes the values X_{t-1} , X_{t-2} etc. But the term on the right of the equation is the unconditional probability that the price change during will take the value X . The expression means the conditional and marginal probability distribution of an independent random variable are identical (Gupta, 1989: 31).

Out of two hypothesis of random walk theory, independence of successive price changes is strong and most important one to make theory valid. The second one is price changes conforms to some probability distribution but its shape or form of the distribution need not be specified i.e. any distribution is consistent with the theory as long as it correctly characterizes the process generating the price changes. However shape or form of the distribution of price change knowledge is important to both investors and researchers for determining risky ness of investment in common stocks (Fama, 1965: 40-41).

But the model when stated in terms of predictability of price changes from earlier changes need not be specific about this distribution (Clive, Granger & Morgenstern, 1970: 72).

The random walk theory says nothing more than the successive price change are independent. This independence implies that prices at any time will on the average

reflect the intrinsic value of the security. If a stock's price deviates from its intrinsic value because, among other things, different investors evaluate the available information differently or have different insights into future prospects of the firm, professional investors and smart non professional will seize upon the short term or random deviations from the intrinsic value, and though their active buying and selling of the stock in question will force the price back to its equilibrium position (Fisher and Jordan, 1995: 553).

The fundamental ideas behind the efficient market theory are that in a stock market, the prices of financial assets should reflect all publicly available information and that these prices should adjust very rapidly to new information. In the uncertain world, however, one would expect differences of opinion among market participants as to the value of each share (Fama, 1965: 56).

As a result, the actual prices move randomly around the intrinsic value. If enough buyers and sellers have received and accurately measured all information on a stock and have acted rationally, prices always in line with intrinsic value (Dreman, 1977: 37).

If the random walk hypothesis holds, the weak form of efficient market hypothesis must hold (though not vice versa). Thus evidence supporting the random walk model is evidence supporting weak form of efficiency (Elton and Gruber, 1991: 404).

If prices follow a random walk, price changes overtime are random (independent). The prices change for today is unrelated to the price change on previous days. Any new information arrived randomly in the market results in the random changes in the prices. Random walk theory which involves random selection of securities is represented as the modern approach to investment decision (Mainali, 2003: 28).

2.7 Review of Previous Theses

In general the random walk literature is the foundation of weakly efficient market hypothesis. The progress of efficient market hypothesis could also be found out from the random walk theory of stock market price behaviours. Various scholars have been studying how the security prices rise and fall for over a century.

The empirical evidence in the random-walk literature existed before the theory was established. This is to say, empirical results were discovered first, and then an attempt was made to develop a theory that could possibly explain the results. After these initial occurrences, more results and more theory were uncovered. This has led then to a diversity of theories which are generically called the random-walk theory (Fisher and Ronald, 1995: 539).

2.7.1 Review from Foreign Previous Studies

The pioneer work in this field is due to French mathematician Louis Bachelier, (1900) who used the data of commodity price during the period of 1894-1898. He tested the model in the commodity priced and found that those prices followed a random walk. He concluded that commodity speculation in France was “fair game” that has no expected profit for buyers and sellers. He also concluded that the current price of the commodity was an unbiased estimate of its future price. Unfortunately, his insights were so far ahead time that was largely unnoticed for a long period until his paper was rediscovered and in the long run translated into English and was printed in 1964.

Slutsky, in 1927, proved that the randomly generated price changes look like stock price changes and they appear to exhibit cycles and other patterns. (Gupta, 1989: 33).

Cowles, in 1933, found little proof that market analysis could forecast future prices (Cowles, 1933: 309).

Halbrook Working, in 1934, found the more evidence that security prices followed a random walk. He analyzed the commodity prices in detail and found that speculative price patterns might be shown to be random comparing with artificially generated series of prices. “It has been noted that time series commodity possesses in many respect the characteristics of series of cumulated random numbers. The separate items in such time series are by no means random in character but the changes between successive items tend to be largely random (Working, 1934: 11-24).

Alfred Cowles and Herbert E. Jones, in 1937 found that stock prices moved with predictable trends. They provided a controversy to the random walk model as a valid share prices behaviours model in U.S.A. In facts, their finding remained a challenge against the random walk hypothesis more than two decades (Cowles, 1960: 916).

Kendall, in 1953 made important progress in the study of random walk model. He examined the behavior of weekly changes in 19 indices of British industrial share prices and spot price series of cotton (New York) and wheat (Chicago). He found no relationship between share price changes in the current week and previous week. He widely analyzed data by autocorrelation and found that successive price changes are statistically independent or stock price movement follows random walk. In summary, the review of literature suggests that share price; actually, follow a random walk, before 1959 (Kendall, 1953: 11-25).

Osborne, in 1959 conducted that, one of the distinguished physicists, ignorant about the stock market at that time watched the numbers representing stock prices to see whether they conformed to certain law governing the motion of physical objects. He found the movement of stock prices similar to that of the movement of small particles suspended in a chemical solution so called 'Brownian Motion'. Although, Osborne attempted to give the empirical reason for his theory, most of data were cross sectional and could not be provide a satisfactory test (Osborne, 1959: 145-173).

Alexander, in 1961 reported empirical result of the filter technique for filter ranging in size from 5 to 50 percent. He tests the filter rule technique on the closing prices of two indices, the Dow Jones Industrials Average from 1897-1959 and standard & poor's Industrial Average from 1929-1959 and reported that in general, filters of all different size and all different periods yield substantial profits, significantly grater than that of simple buy and hold policy. Finally he concluded that the independence assumption is not validated as a description of reality by his data. But later in 1964, he corrected the shortcomings on his previous study were the failure to realize that dividends were cot rather than benefit. Alexander found that his filter rules produced very large rates of return, particularly for small filters. However when transaction costs are considered, the abnormal returns disappear for all filter rules (Alexander, 1961: 1-26).

Granger and Morgenstern, in 1962, had adopted typical method of analysis to the weekly, monthly and volume series form the New York Stock Market which involved of Dow- Jones, standard and poor and various indices as well as price series of individual stocks. Particularly there exists no linear relationship of dependence between lagged price changes. They found that short run movement in stock prices followed a simple random walk model. However, they reported that this model does

not adequately explain the long run movements (Granger and Morgenstern, 1962: 24-45). Again, Godfrey, Granger and Morgenstern (1964) tested the some method widely and recommended that the random walk hypothesis appears to give a logical model for the logarithmic series from both New York and London.

A.B. Moore, in 1962 studied weekly priced changes of 29 randomly selected US stock for 1951-58 and found an average serial correlation coefficient -0.06. The value was extremely low and indicated that the weekly changes data were of no value in predicting future price changes. The explanation of his test is that a low co-efficient estimate suggests that previous price changes do not provide any reliable information in estimating future price changes. Cootner (1964) examined the randomness of the series of 45 companies stock from New York exchange by using serial correlation on the logarithms of daily price changes. In his study he found low correlation coefficient of - 0.046, which are inadequate to forecast the future price changes (Cootner, 1964: 412-474).

Fama, in 1965, analyzed the movement of stock market price changes of all the stock that make up the Dow Jones industrial index for the period end 1952-1962 and investigated the daily comparative price changes of those 30 industrial stocks and auto correlation were estimated for a variety of lags ranges from 1 to 10 days. In his study, he found that the auto correlation coefficients for daily average being 0.03, near to 0. Out of thirty, eleven auto correlation coefficient was significantly different from zero and lagged price changes show some degree of dependence. He further analyzed the data by run tests by total number of runs by sing and distribution of runs by length. He found slight tendency for this to occur, but again the result were sufficient to accept the random walk hypothesis (Fama, 1965: 34-105).

Samuelson, in 1965 concluded that the market will efficient and prices will fluctuate randomly if the market has zero transaction costs, if all available information are free to all interested parties and if all market participants either potential and existing have the same time horizons and expectations about the prices. His findings support the independence hypothesis of random walk theory in stock prices (Samuelson, 1966: 41-49).

Fama and Blume, in 1966, adopted the filter technique with the view to solve the limitations of Alexander's mechanical rules. They reported that none of the 30 Dow

Jones industrial average stocks that investigated outperformed the strategy. Therefore their study concluded that filter technique can not buy and hold policy (Fama and Blume, 1964).

King, in 1966, made a conclusion that there exists low degree of co-efficient estimates of serial correlation, i.e. 0.018 which is close to zero. He had tested the behavior of 63 securities from six industries of New York Exchange from 1927 to 1960. Therefore, his study also made the conclusion that stock market price follows the random walk model (King, 1966: 136-190).

Praetz, in 1969 made a study of the three sets of price data of Australian shares. He adopted the serial correlation and run tests and thus made the conclusion that random walk hypothesis is a useful first approximation as a description of series of price changes (Praetz, 1969: 123-139).

Dryden, in 1970, made a study of three London indices for about 4 years in Great Britain. He found that the first order serial correlation coefficients were statistically significant. He, thus, concluded that the share price movements were not random (Dryden, 1970: 369-389).

Brealy, in 1970, made a study of various stocks by applying similar methodology to that used by Fama in 1965 and also supported the random walk model. He, thus, drew the conclusion that the successive price changes in the stock market are independent (Brealy, 1970).

Niarchos, in 1971 made a study of price series of 15 individual stocks from Athens Stock Exchange from 1957-1968 and reported that the serial correlation coefficients for individual stock as 0.036, close to zero. He, therefore, drew the conclusion that the price fluctuations were random walk and past price had no meaningful information to show the prices of future (Niarchos, 1971).

Kemp and Remp, in 1971, studied the British stock market and reported that the share price movements were conspicuously non-random over the period considered. Thus their study was also against the random walk theory (Kemp and Remp, 1971: 28-51).

Gupta, in 1985 analyzed the equity share behavior in India during the period January 1971 to march 1976 and extensively tested the random walk hypothesis using daily and weekly price of 39 individual shares and two indices. (The economic time index and financial Express index) He employed the serial correlation analysis and run test and found proof in support of random walk hypothesis. He also concluded that the

random walk model appeared to be a suitable model even for the less developed country like India to explain share price behavior (Gupta, 1989: 53-54).

Sweeny, in 1988, made a filter rule which was able to earn modest profits. He found that the long position were often profitable. He also found that filter rule trading tended to be fairly and consistently profitable in some stocks while being fairly consistently unprofitable year after year in another stocks. These rules mechanically trade some stocks and earn a statistically significant rate of product after reducing small trading costs incurred. However the filter rule seems to be unprofitable if the higher commission rates that most investors pay were deducted (Sweeny, 1988: 285-300).

Rao, in 1988 employed the autocorrelation analysis, run test and filter rule to the weekend closing price of 10 blue chip stock over the period 1983 to 1987. The results from all his study support the random walk hypothesis (Rao, 1989: 203-218).

Hence, the reviews of above-mentioned studies held in foreign countries depict money interesting findings on the price behavior. According to the review of above research works, it can be concluded that the stock market prices depict a random movement and the security prices appear to be serially independent. Therefore the investors cannot develop any profitable trading strategy by using the information of the past series. However, the question arises as to what extent these are finding relevant in Nepal. They all may not be applicable in Nepalese context where the stock market is small and underdeveloped. Therefore studies conducted in India would be more relevant because Nepalese and Indian companies are running under similar condition.

2.7.2 Review of Previous Studies

In Nepal, the stock markets have been less subjected to investment research. The researches have been concerned with the investigation of effect of certain financial variables on the equity share prices. So, some of the available relevant studies have been reviewed in this section.

Bhattarai, (1990) has conducted a study on “Share market in Nepal.” He has emphasized the historical background and the analysis of various financial variables affecting the smooth operation of share market. The study was mainly based on

secondary data obtained from various sources. He has applied both financial and statistical tools in the study. He found that out of 12 sample companies, only 2 companies were useful to cross over the average price-earning ratio, as a result, market price of shares were highly skewed. Moreover, there was mismatch between calculated and quoted price. However, he concluded that the involvement of more and more institutions as well as individual investors in capital market through broker's network raised the transaction volume. Rumors spread by brokers, and create genuine speculation. Fair play of bulls and bears makes the market equilibrium resulting price stabilization. Speculation on the trading of shares is encouraged. Thus, the market starts to walk randomly reflecting true value of shares. Investors are facilitated by providing alternatives to make diversified portfolio.

Aryal, (1995) has conducted a study on "behaviour of stock market prices." The objective of his study was discussing the movement of stock market prices and to develop the empirical probability distribution of successive price change of an individual common stock and a stock market as a whole. This study was conducted on the basis of secondary information obtained from Nepal stock exchange. This study covers almost 8 month period and the sample was 21 listed stocks. He applied serial correlation and run test as statistical tools to analyze the data. Through the analysis he has concluded that the assumption of independence, as predicted by random walk model of security price behaviour has been refused at least for Nepalese context as the first approximation even in the rough way for early days of stock market operation. This rejection of hypothesis made clear that the knowledge of past and present becomes useful in predicting the future price movements of stock market prices. The investors, on the floor of exchange, can make higher expected profits in future on the basis of these historical price series. In other words, the dependence nature of price series produced by general market fluctuation statistically implied, today's change is positively depending upon yesterday's price change. This implied that there is an absence of financial and market analysts who are sophisticated and superior in analyzing the general market fluctuations, predicting the occurrence of future potential and economic events that their eventual effects on price series.

Gurung, (1999) has conducted a study on "Share price behaviour of listed companies." He applied statistical tools like percentage, correlation coefficient, bar

graphs, and line charts for analyzing the data. The object of his study were to provide the conceptual glimpses of capital markets, to evaluate the trend of trading turnover, to analyze the trends in paid value and market capitalization, and to recognize the market behaviour in Nepal. He has found that the correlation coefficient of 0.97 between the number of traded and listed companies is significant, where as it is negative in trading group and perfectly positive in the case of banking group. The market capitalization value is in irregular trend in every group in each year. The proportion of marker capitalization of banking group is the highest among six groups. During the study, the number of transaction in banking group is the highest, where it is long in other groups. Hence, the investment on banking group is highly attractive and liquid. The prices of share are fluctuating during the study period the capital in Nepal was bullish in the initial period but it turned bearish in the successive year. In the initial period, share prices, trading turnovers, market index as well as earnings have positively moved except market capitalization, but they have negatively moved in the following years. Therefore, now the capital market is passing through bearish trend in Nepal. There is lack of investor's opportunities and economy is passing through the recession year by year.

Paudel, (2001) has conducted a study on "Share price movement of joint venture commercial bank." He used various financial and statistical tools like standard deviation, correlation, beta, t-test etc. the major objective of the study was to examine Nepal stock exchange market and to judge whether the market shares of different banking indicators (book value per share and major financial ratio) explain the share price movement. With the application of above stated methodologies, he concluded that the market share and the growth rates of different banking indicators used are not captured by the market share of these banks. The ordinary least square equation of book value per share on market value per share reveals that the independent variable does not fully explain the dependent variable on the basis of above mentioned points. So, Nepal stock exchange operates in a weak form of efficient market hypothesis, indicating that the market prices move randomly. The market value per share does not accommodate all the available historical information. The beta coefficient which measures the risk ness of individual security in relative term, suggest that the stocks of joint venture commercial banks are less risky as compared to other average stock traded in the stock exchange.

Kharel (2002) has conducted his study on “Stock market efficiency and behaviour of share prices.” He used serial correlation test and runs tests as statistical tools, further he used technical trading rule named filter rule for analyzing the data. He found that standard deviations of each and every individual stock’s price changes are higher than the mean. Therefore, the general shape of empirical frequency distribution is flatter than normal distribution’s shape. Most of the results obtained from the serial correlation test for 30 stocks is absolutely large and significantly insulated from zero. The results obtained from the runs test are also consistent with the results of serial correlation tests. When the runs test analyzed by lengths; it was found that actual numbers of runs are not normally distributed. Therefore, there exists significant determination in the successive price changes series of Nepalese stock market. Similarly, the result obtained from the filter test showed that difficult mechanical trading rule can beat the average market return. As most of the filter’s trading returned higher than buy-and-hold strategy, it supports the result of serial correlation and runs test. Hence, he concluded that today’s price changes are not an unbiased outcome of yesterday’s price changes.

Dahal, (2002) has conducted a study on “Stock market behaviour” by taking 67 sample companies. To analyze the gathered data he used simple percentage and paired t-test as an analyzing tools. He found that most of the investors were attached with banking sector for investment. On analyzing primary data it was found that the stock market in Nepal is in developing stage as investors are not well aware about the investment process and its other factor like NEPSE index, price trend and investment facilitators are not doing their work in systematic way. It was also found that the investor’s motive for owning shares of company is to receive the dividend from the shares. On analyzing the price trend of two years NEPSE index in different months with the help of monthly trend, while that of year 2001 was in decreasing trend. Similarly, the result of paired t-test for signaling factors with reference to major seven events showed that signaling effects had played main role in fluctuation of stock prices.

Mainali, (2003) has also conducted the study on “Share price behaviour of listed commercial banks.” The prime objective of his study was to analyze the performance of stock market and the behaviour of share price of listed commercial banks. The

other specific objectives were to provide glimpse of NEPSE, examine the risk involved in the common stock investment of the sampled commercial banks and discuss the movements of stock market price. He used parametric and non- parametric test to explore the randomness of stock return. He used standard deviation coefficient of variation beta coefficient for individual stock to test the friskiness of share. The results of estimate serial correlation were found to have deviated significantly from the expected value zero i.e. serially correlated. So, that the results obtained from the serial correlation tests tend to invalidate the hypothesis of independence. The results of run tests also consistence with the results of serial correlation tests. He found that past and present price changes can screen out some valuable information in predicting future price changes. So, there exists sufficient amount of opportunity for sophisticated investors. The statistical analysis is regarding the risk and return of sampled stock showed that most of the stock seemed to be riskier than the average stock. But most of the banks are offering cash dividends every year, which may not be applicable to other non- banking firms.

Ban, (2004) also conducted the study on “valuation of stock in stock market” with reference to banking, finance and insurance companies listed in NEPSE. He applied statistical tools, financial tools and financial parameters. The objectives of his study were to predict trends and significant development of stock in NEPSE, analyze size and return of securities, and compare with market return, examine the relation between market capitalizations with other determinants variables. He found that banking sector occupy 62.18% whole transaction of NEPSE. So, the fate of stock market depends on performance of banking sector. The participation of people is encouraging in stock market due to higher return. The average return of financial and insurance is 13.86% and coefficient of variation is 290.03%. The risk associated with finance and insurance sector is higher then banking sector. Similarly, in the case of finance and insurance sectors, EPS has found significant relationship with market capitalization.

Dhakal, (2004) conducted a study on “contribution of the finance companies in the economic development of Nepal.” The objective of his study was to study the contribution of finance company in the economic development, analyze the growth of financial sector, and review the evaluation development of finance companies and

examine the prospects and problems of finance companies in Nepal. He found that the finance companies are exposed to greater degree of risk since they are still weak and deficient in credit analysis and appraisal. Finance companies are not going adequate public confidence because of fear that there is risk of depositing money in finance company. Many finance companies have not been able to prove professional competency and make selective investment. Finance companies are competing for funds in the market. Finance companies are the outcome of the government's economic liberalization policies. All together the finance companies are operating their business in the country.

Giri, (2005) has conducted a study on "Behavior of share prices of listed commercial Bank" by taking 10 sample commercial Banks. She used statistical tools, financial tools and financial parameters. The objectives of her study were to provide glimpse of Nepalese Stock market, analyze the share price behavior of listed commercial banks, to examine the risk involved in the common stock investment of those listed commercial banks. She found that weakly efficient market hypothesis does not offer a satisfactory explanation to these speculative price series. The information of the past price changes is helping in predicting future change. So, sufficient opportunities are available to institution and individual investors to make higher expected profit in future. Most of the stocks seemed to be risky than the average stock. She found that mot of the banks are offering cash dividends every year. According to her it is not applicable in the other type of non-banking industries.

Regmi, (2005) conducted his study on "Share price behavior in Nepal". His major object was to assess equity share price behavior in Nepal. The other specific objectives were to test random walk or weak from efficient market hypothesis, examine whether successive price changes are independent or not, conduct the opinion survey financial executives regarding the various aspects of the share price behavior in Nepal. He found that both the tests-serial correlation and run test analysis do not support the independence assumption of random walk model. Share price movements are caused by flow o several kinds of information in the market. The existence of work from efficient market hypothesis is slightly accepted by the financial executives in Nepal.

Sarada Mainali (2006) has conducted research on “ A Study on Share Price Behaviour of Listed Companies”. The main objectives of this study were:

- To analyze the behavior of stock price of Listed Companies.
- To examine the stock price trend and volume of stock traded on the secondary market.
- To identify the factors affecting stock price.
- To analyze the investors' view regarding the decision on stock investment.

In her study, Mainali concluded that Share trading system in share market is still uncivilized even in this IT age. Though the volume to trading has increased the number of brokers has not increased. Therefore, for the systematic operation of the share market, the number of brokers should be increased according to the volume of trading. Similarly, the automation system has to be put in to practice to make the share market effective and competitive.

- The public investors not direct their savings in shares haphazardly. They should at least analyze or get suggestions from experts about financial position and the level of risk prior to taking and investment decisions. Because of the persistence in the stock price movements professional traders either institutional or individual can beat the market. Thus it is suggestions that the investors should be alert to exploit the opportunities

Overall, the previous studies in stock market support the idea that Nepalese stock market is not efficient even in the weak form hypothesis. Nepalese investors are not efficient enough to recognize potential for excess return.

Rudra Hari Gyawali, (2007) has conducted research on "Rights share practice and its impact on share price movement" the main objective of the study were:

- To explain the price movement before and after the right offering.
- To analyse the relationship between share price movement and market movement.
- To identify the problem associated with the right practice.
- To study investors opinion regarding various aspect of right offering.

In his study he found impact of right offering on share price movement various from company to company in case of listed companies such differences are not only

between the companies of different sectors but also between the companies within the sector. Differences in share price movement before and after the offering are significant as well as in significant.

Sita Bhandari, (2008) has conducted research on "A study on investors' response to initial public offering in Nepal" the main objective of the study were:

- To assess the growth of initial public offering.
- To analyze the subscription pattern of securities in response to IPO.
- To analyze the sector-wise public response to IPO.

In this research she found that the capital market of Nepal is still in a developing stage. Most of the investors in the primary market are involved from Kathmandu valley; Most of the companies have issued only common stocks. The annual growth rate of IPO in the financial sector is greater than that of the non-financial sector.

2.4 Research Gap

There is a gap between the previous research and this research. Previous research was conducted only on the growth and size of the stock market. They were analyzed only on the basis of secondary data analysis. Few of the previous researches were concerned with problems of the stock market. However, they were not analyzed taking such variables like sufficiency of legal rules and regulations, availability of information, provision to attract institutional investors etc. To do this research, the researcher does not find any previous research on the topic of prospects of the Nepalese stock market. So to fulfill this gap, this present study is conducted both analyzing the secondary data and primary data. The growth of the stock market is analyzed using both secondary data and primary data analysis as well as analyzing over the 14 years data. Behaviors of the securities market in Nepal are analyzed on the basis of primary data analysis using the Likert scale method.

These researches are helpful in different areas. The findings of previous researches are equally important. The main focus of the research will be to analyze the performance, growth and downturns of the Stock Market. This will help to analyze whether the Stock Market is in an increasing trend or in a decreasing trend. By analyzing

these aspects, focuses can be set on the weakness. So, that in future these weaknesses can be turned into the strength of the Stock Market. This will help to make the existence of the Stock Market more robust. Further more, by being able to point out the weakness; more investors can be made to contribute for the growth of Stock Market

CHAPTER III

RESEARCH METHODOLOGY

3.1 Introduction

Research means to search or study about a phenomenon. Generally research is an effort to search new fact, knowledge and principle in scientific ways. Research is the process of a systematic in –depth study or search of any particular topic, subject or area of investigation backed by the collection, complication, presentation and interpretation of relevant details or data. Methodology refers to the various steps that are generally adopted by a researcher in studying his research problem along with the logic behind it. So that research methodology is a systematic way of conducting the research in an effective and practical so that it can explain how the research is done.

Therefore this chapter highlights the research methodology used for the study of “Behavior of Securities Market in Nepal”. In this regard, this chapter explains not only talk of the research methods but also consider the logic behind the methods, which are used in the context of our research. This chapter consists of the research design, population, sampling procedure and sources and analysis of data.

3.3 Research design

Research design is the conceptual structure within which research is conducted. In other words, a plan of study or blue- prints for study is called research design or research strategy. It facilitates the smooth sailing of the various research operations, thereby making research as efficient as possible. Research design is a plan, structure and strategy to obtain the objectives of the study.

According to the Kerlinger (1998), “Research design is the plan, structure and strategy of investigation conceived so as to obtain answer to research questions and to control variance”.

This research is based on secondary data and primary data analysis. Hence, the historical and descriptive research design has been used to conduct the study of "Behaviors of securities market in Nepal". It deals with the stock market on the basis of available information.

3.3 Population and Sample

The total variable is simply called population. The process of selecting the sample out of the population is called sampling. The analysis of behaviour of security market in Nepal depends on the number of company listed in the Nepal Stock Exchange and major economic indicator (GDP, Inflation, Turnover etc) are taken 141 listed sector wise companies as total population. Moreover, the companies that are in existence and doing share transactions in NEPSE and the factor that affects the present economic growth are considered as the sample of the study. The required data have been collected from the various sources; but mainly from the annual reports of securities exchange board, Nepal covering a period of 1993/94 to 2006/07. Therefore, all the companies listed in the stock exchange are taken as samples.

3.4 Sources of Data

The main place of data was the central office of Nepal Stock Exchange (NEPSE), Securities Boards office, Thapatali, Kathmandu and Economic Survey published by Ministry of Finance. The main source of data is annual report of the SEBON. Besides annual report, various bulletins available and useful to the study are also taken into consideration. The research is mainly based on the secondary data. The required data will be collected through the corporate office of the security Board of Nepal.

Primary Data

The primary data are collected through questionnaire and informal interview of concerned persons like officer of SEBON and NEPSE, share broker and investors. All together 50 copies of questionnaires were distributed to the persons and institution irrespective of their professions and nature of activities of which 80 percent of questionnaire have been collected during the study period.

Secondary Data

The secondary source of data are the annual report of the Security Board Nepal, different books from library, periodicals, newspaper cuttings, company's magazines etc. Guidelines and unpublished thesis, research work that directly related to the financial performance and stock market would form secondary data for the purpose of this study. Significant information's are also collected from Internet and various websites like www.nepalstock.com , www.sebonp.com etc.

3.5 Data Collection Technique

The research contains of both primary as well as secondary data. Since the nature of these two data is different, the data collection procedure also varies. To collect the secondary data, published materials are viewed in various spots such as books by different authors, unpublished thesis reports, journals, Internet web sites, online library, AGM reports of listed companies, NEPSE, SEBON etc. To collect these secondary data, the researchers visited campus library of NCC, TU central library, SEBON library. On the other hand, the primary data collected through scheduled questionnaire.

3.5 Data Processing

Data so obtained have no meaning unless they are arranged and presented in a systematic way. Data processing technique is one of the most important parts of the research study. The researcher should adopt that data processing technique to process the information and data which is suitable and feasible according to nature and objects of the research study. The available information and data should be present in different way, which can easily be understood by the general public. In this study, the required available data and information are shown in figures. The computation has been done with the help of calculator and computer.

3.6 Analysis of Data

Analysis is the careful study of available facts so that one can understand and draw conclusion from them on the basis of established principles and sound logic. This study is mostly based on the analysis of secondary and primary data with the help of different statistical tools like Diagrammatic presentation and mean. The empirical result has been extracted in this study by using annual data of listed companies from 1993/94 to 2005/06.

3.7 Data analysis Variables

Gross Domestic Product (GDP)

Issue Approval

Public Issue

Issue Manager

Stock Broker

Paid-up Value, Turnover and Market Capitalization

3.8 Tools of Data Analysis

On the basis of secondary and primary data collected from the trading report, published books, journal and questionnaire with different financial and non-financial expert and staff as well as officers of NEPSE and SEBON were done, so effective analysis of data could be done on effective manner. To draw the conclusion by analyzing the collected data simple statistical tool are used as follows:

3.8.1 Financial Tools

Percentage:-

Percentage is used to measure the changing position of different time period values or amount. The use of percentage can make the data much simpler to grasp.

we use the given formula to find out the percentage or percentage changed.

$$\text{Percentage} = \frac{\text{Number or Values or Amount of specific period}}{\text{Total Number or Values or Amount}}$$

$$\text{Annual Percentage change} = \frac{\text{Amount or Values of This year} - \text{Amount or Values of last year}}{\text{Amount of last year}}$$

3.8.2 Statistical Tools

Diagrams and Graphs

Diagrams and graphs are visual aids which give a bird's eye view of a set of numerical data which show the information in a way that enables us to make comparison between two or more than sets of data.

Pie charts

The pie chart is well known method of presenting data. The pie chart is named like a pie, it is a circle divided in to slices or section these charts are used to show how the

parts of a whole are distributed. The main advantage of this chart is that it permits of quick and easy understanding of relative percentages or divisions of the whole.

Bar charts

A very popular way in which research findings are presented is through the use of bar charts. The simple bar chart is perhaps the most effective graphic method for comparing quantities. A bar chart presents the data through a series of bars.

Line charts

Line charts show the changes in quantitative data over time and illustrate trends. A line chart is thus a two-dimensional chart that represents changes over time.

CHAPTER – IV

DATA PRESENTATION AND ANALYSIS

4.1 Background

This chapter is basically focused upon the analysis of data collected from different secondary sources. It will reveal the development of Nepalese stock market in terms of turnover, issued – capital, paid-up capital, contribution of market capitalization to GDP etc. comparing with different years. With reference to various readings and review of literature in the preceding chapters, effort is made to analyze and diagnose the recent Nepalese Stock Market Development. Different tables and diagrams are drawn to make the result more simple and understandable.

The relevant information and data are collected from Nepal Stock Exchange (NEPSE), Security Board (SEBON) and from different books and articles. All companies listed in stock market (NEPSE) are taken as a sample and appropriate statistical and financial tool have been used to perform the analysis.

Group-wise Description of Listed Companies

Table 4.1

GroupWise Description of Listed Companies

S.N.	Sector	No. of Listed Co. Group-wise	Percentage
1.	Commercial Banks	15	10.63
2.	Development Banks	20	14.18
3.	Finance Companies	55	39.0
4.	Insurance Companies	16	11.34
5.	Hotels	4	2.83
6.	Manufacturing & Processing	21	14.89
7.	Trading	5	3.54
8.	Others	5	3.54
Total		141	100.00

Source: Annual Report of NEPSE 2006/07

Group Wise Description of Listed Companies

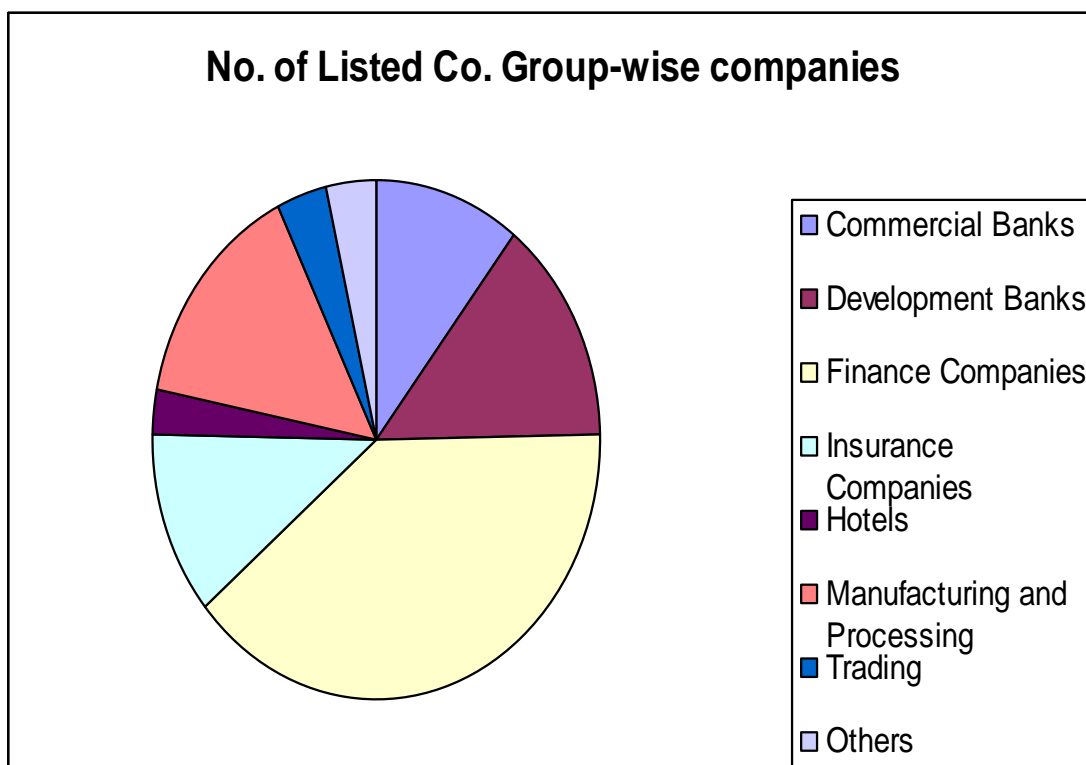


Figure No. 4.1

Table no. 4.1 and the Chart no. 4.1 represents that 141 companies listed in NEPSE in this fiscal year 2006/07, 39 Percent (55) finance company are listed out fo 141 listed companies and only 5 Hotels companies are listed in NEPSE. 15 new organized companies are listed in this fiscal year 2006/07.

4.1.1 Yearly Volume of Traded Stocks and NEPSE Index:

Table No. 4.2

(Rs. in million)

Year	No. of Companies	No. of transactions (Shares units) '000'	Market Capitalization	Traded Total Turnover Volume '000'	Turnover Values in Rs.	Yearly NEPSE index '000'
1996/97	95	12428	12698	9443.28	416.19	176.34
1997/98	101	15483	14289	1195.1	202.61	163.35
1998/99	107	15814	23508	4788	1500	216.92
1999/00	110	29136	43123.33	7674	1157	360.70
2000/01	115	46095	46349.4	4987	2344.20	348.43
2001/02	96	42028	34704	5791	1540.60	227.54
2002/03	108	69163	35240.40	2427.89	575.99	204.86
2003/04	114	85533	41424.77	6468.18	2144.27	222.04
2004/05	125	106246	61365.89	18433.55	4507.68	286.27
2005/06	135	97374	96813.74	12221.93	3451.43	386.83
2006/07	141	120510	186301.30	18147.25	8360.1	683.04

Source: Trading Report of NPESE 2006/07

Table 4.2 shows that the yearly volume and values of traded stocks are fluctuating. However, there is a sharp rise in the volume of traded stocks in fiscal year 2006/07. The major reason for the sharp rise in the trading volume in fiscal year 2006/07 may be attributed to heavy transaction of banking sectors. We can see that the significant increases in NEPSE Index in the fiscal year 2006/07 by 296.21 points. Here the lowest number of listed companies is 96 in fiscal year 2001/02 due to the case of financial performance of the companies, political effect, can not meet the rules and regulation of NEPSE. So, the Nepse de - listed the 19 companies in this fiscal year.

4.2 Analysis of Turnover

Annual Turnover:

Annual turnover constitutes an important indicator for measuring the nation's economic activity. It also reflects the stock market liquidity as higher the amount of trading of stock market size, the greater is the stock market liquidity.

Table No. 4.3
Monthly Turnover in 2006/07

S.N.	Month	Amount Traded (in million)
1.	July/August	3424.2
2.	August/September	3740.8
3.	September/October	2458.6
4.	October/November	7117.6
5.	November/December	9444.8
6.	December/January	10816.7
7.	January/February	6077.5
8.	February/March	7164.2
9.	March/April	5102.3
10.	April/May	4990.4
11.	May/June	8942.9
12.	June/July	14320.6

Monthly Turnover in 2006/07

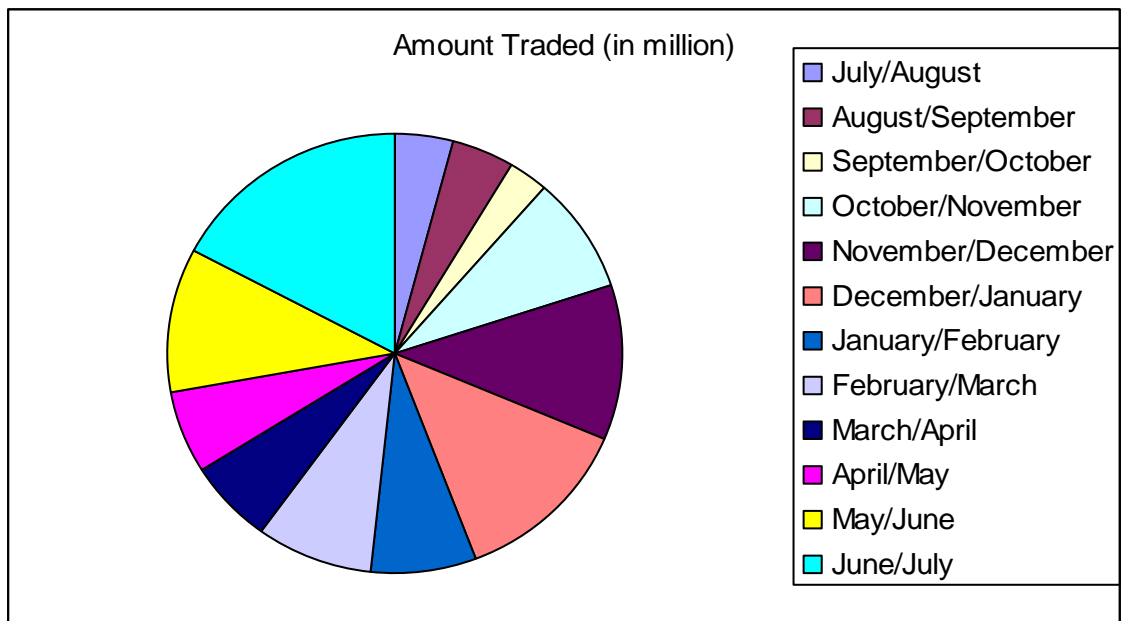


Figure No. 4.3

Table no 4.3 and figure no. 4.3 represents that the highest amount traded in June/ July Rs in 14320.6 million and the lowest is September /October Rs in 2458.6 million. The highest number of amount traded in month of December January due to the case of companies declaration their dividends, right share as well as bonus share.

4.2.1 Paid-up Value of Listed Securities:

The paid-up value of listed securities in the end of this fiscal year was Rs. 186301.3 million as compared to the paid-up value of Rs. 96813.74 million in the previous year 2005/06. The paid-up value of securities in the end of this fiscal year is given below:

Table No. 4.4
Paid-up Value of Listed Securities

S.N.	Sector	Paid-up Value (Rs. in million)	Percentage
1.	Commercial Banks	135584.40	72.78
2.	Development Banks	6010.60	3.23
3.	Finance Companies	9889.30	5.31
4.	Insurance Companies	8059.80	4.33
5.	Hotels	32611.0	1.75
6.	Manufacturing and Processing	796.40	0.43
7.	Trading	796.40	0.43
8.	Others	16495.70	8.85
Total		186301.30	100.00

Source: Trading Report NEPSE 2006/07

Paid –up Value of Listed Securities

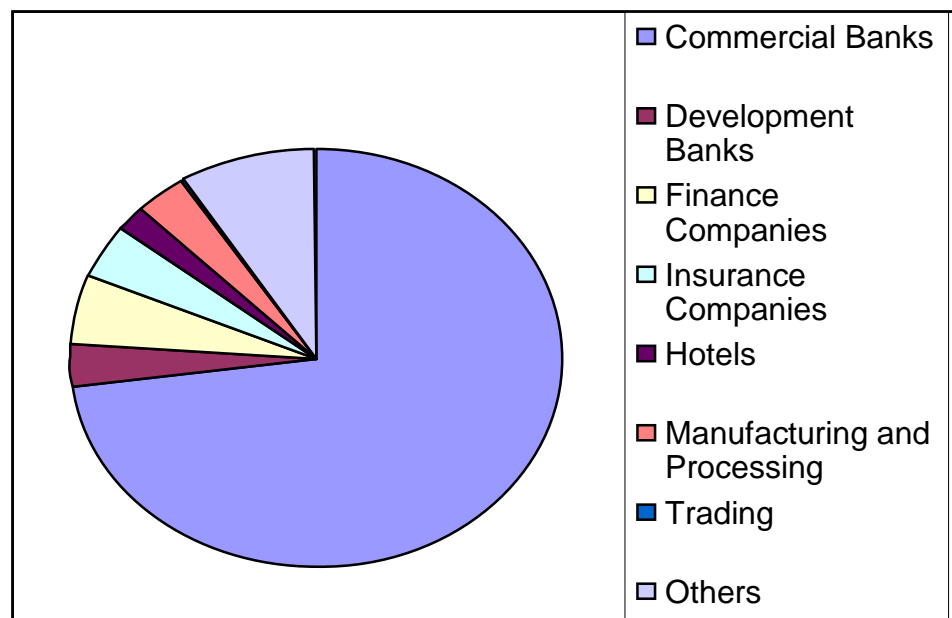


Figure No. 4.4

Table No. 4.4 and chart figure no. 4.4 shows that the huge amount of paid –up value covered by the commercial Banks. It's Cover 72.78 percent (Rs. 135584.40 million

out of Rs. 186301.30 million) and lowest paid – up values are equally Trading and manufacturing and processing companies only 0.43 percentage.

4.2.2 Paid up Value of Listed Securities for Different Years

Table No. 4.5

Paid-up Value of Listed Securities

Fiscal Year	Paid-up Value (Rs. in million)	% Increase in Paid-up Value	% of Turnover in Paid-up Capital
1993/94	2182.2	-	20.23
1994/95	2961.8	35.73	35.60
1995/96	3358.5	13.40	6.42
1996/97	4476.5	33.29	9.30
1997/98	4959.8	10.80	4.09
1998/99	6487.4	30.80	23.12
1999/00	7347.4	13.26	15.75
2000/01	8165.2	11.13	28.71
2001/02	9685.04	18.61	15.91
2002/03	12560.07	29.69	4.84
2003/04	13404.90	6.73	15.99
2004/05	16771.80	25.11	26.87
2005/06	19958.00	18.99	17.29
2006/07	21798.8	8.94	38.35

Source: Annual Report, SEBO 2006/07 Trading Report, NEPSE 2006/07.

Paid-up Value of Listed Securities

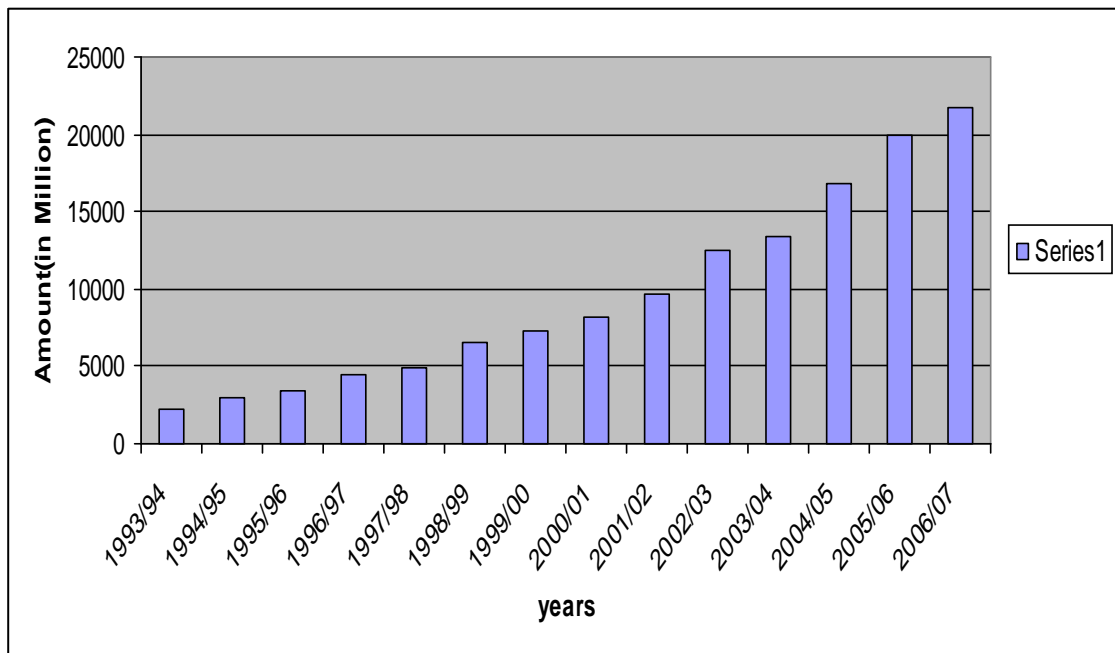
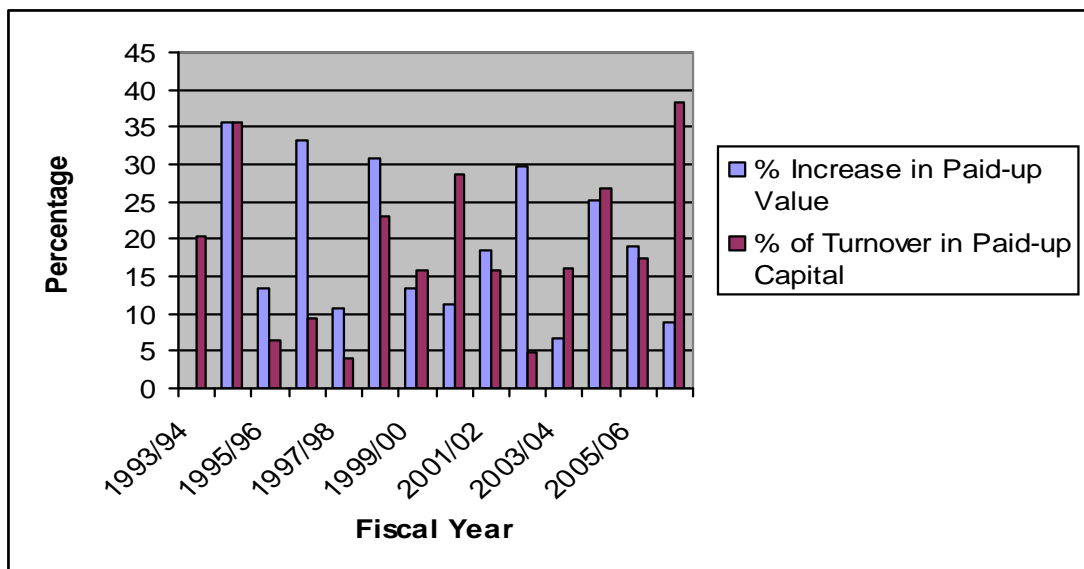


Figure No. 4.5



Percentage increase in paid-up Value & Percentage of turnover in paid-up capital

Figure No. 4.6

By the end of this fiscal year 2006/07, the paid-up value of listed securities increased by only 8.94 percent and reached to Rs. 21798.8 million as compared to the increase

rate of 29.69 percent of the fiscal year of 2002/03 which was Rs. 12560.07 million. The highest increase in percentage of paid-up value was in the year 1994/95 by 35.73 and lowest is in the year 2003/04 by only 6.73 percent.

The percentage of turnover on paid-up capital is highest in the fiscal year 2006/07 with 38.35 percent and lowest in the fiscal year 1997/98 with 4.09 percent. The percentage of turnover was 20.23 percent in the fiscal year 1993/94 and is 38.35 percent in the fiscal year 2006/07. It has been increased from 17.29 to 38.35 percent from the year 2005/06 to 2006/07.

4.2.3 Market Capitalization

The market capitalization value of listed securities in the end of this fiscal year 2006/07 is Rs. 186301.30 million. The market capitalization value was Rs. 96813.74 million in the last year.

Table No. 4.6
Market Capitalization

S.N.	Sector	Market Capitalization Value (Rs. in million)	Percentage
1.	Commercial Banks	135588.40	72.78
2.	Development Banks	6010.60	3.23
3.	Finance Companies	9889.30	5.31
4.	Insurance Companies	8059.80	4.33
5.	Hotels	3261.10	1.75
6.	Manufacturing and Processing	6200.0	3.33
7.	Trading	796.40	0.43
8.	Others	16495.70	8.85
Total		186301.30	100

Source: Trading Report NEPSE 2006/07

Market Capitalization of Listed Securities

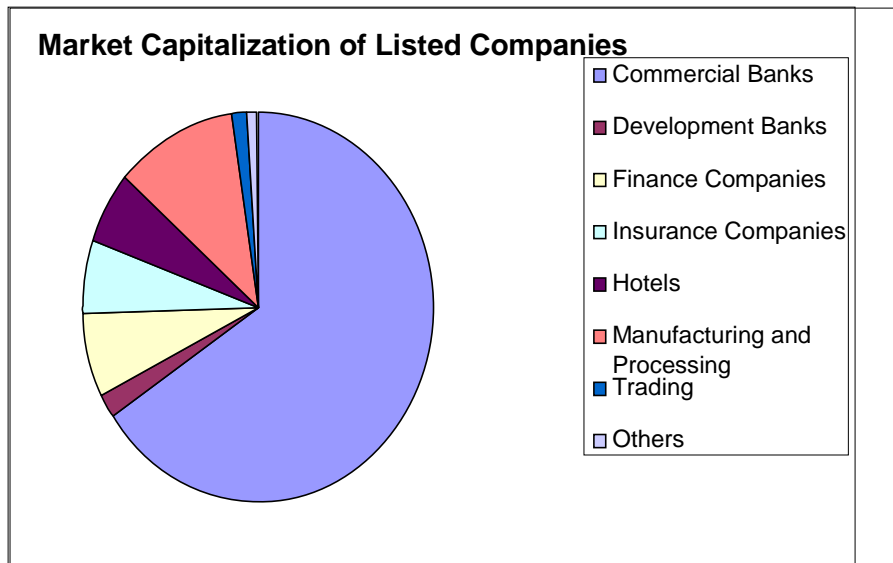


Figure No. 4.7

Table No. 4.6 and the Figure No. 4.7 represents that the highest market capitalization by commercial banks and it's covered the 72.78 percent (135588.40 million out of 186301.30 million) Here the lowest market capitalization by trading sector and it's covered only 0.43 percent.

4.2.4 Analysis of Market Capitalization

Table No. 4.7

Market Capitalization in NEPSE

Fiscal Year	Market Capitalization (Rs. in million)	% Increased in Market Capitalization	% of Turnover to Market Capitalization
1993/94	13872	-	3.18
1994/95	12963	-6.55	8.13
1995/96	12295	-5.15	-1.75
1996/97	12698	3.28	3.28
1997/98	14289	12.53	1.42
1998/99	23508	64.52	6.38
1999/00	43123.3	83.44	2.68
2000/01	46349.4	7.48	5.06
2001/02	34703.87	-25.12	4.44
2002/03	3520.40	1.55	1.63
2003/04	41424.77	17.55	5.18
2004/05	61365.89	48.13	7.34
2005/06	96813.74	57.76	3.56
2006/07	186301.3	92.43	4.48

Source: Annual Report, SEBO 2006/07 Trading Report, NEPSE 2006/07.

The market capitalization of listed securities in the fiscal year 2006/07 is Rs. 186301.3 million. It is increased by 34.67 percent from the fiscal year 2005/06 which was Rs. 96813.74 million. The market capitalization was decreased by -25.12 percent in the fiscal year 2001/02. The highest increase in market capitalization rate is 92.43 in the fiscal year 2006/07

%increased in Market Capitalization& % of Turnover to Market Capitalization

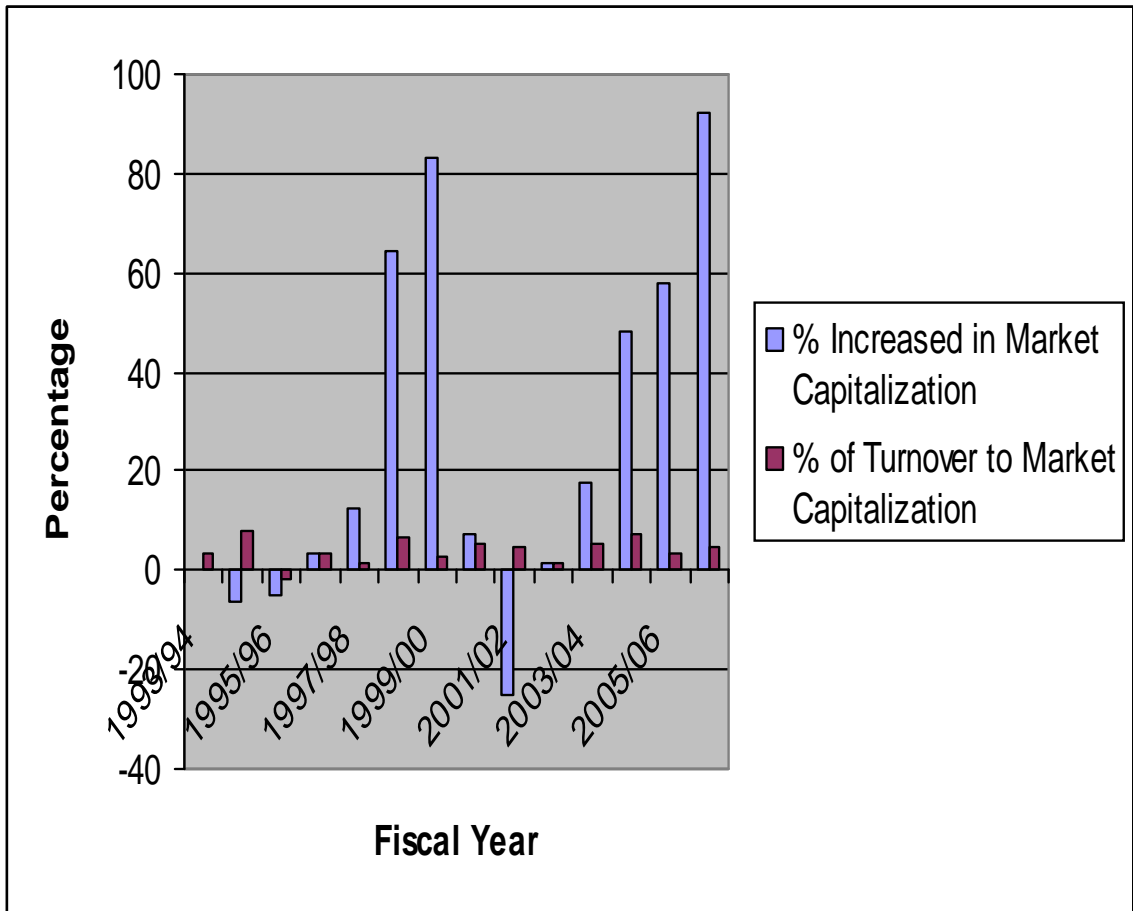


Figure No. 4.8

4.2.5 Analysis of the Growth Trend of Stock Market Indicator

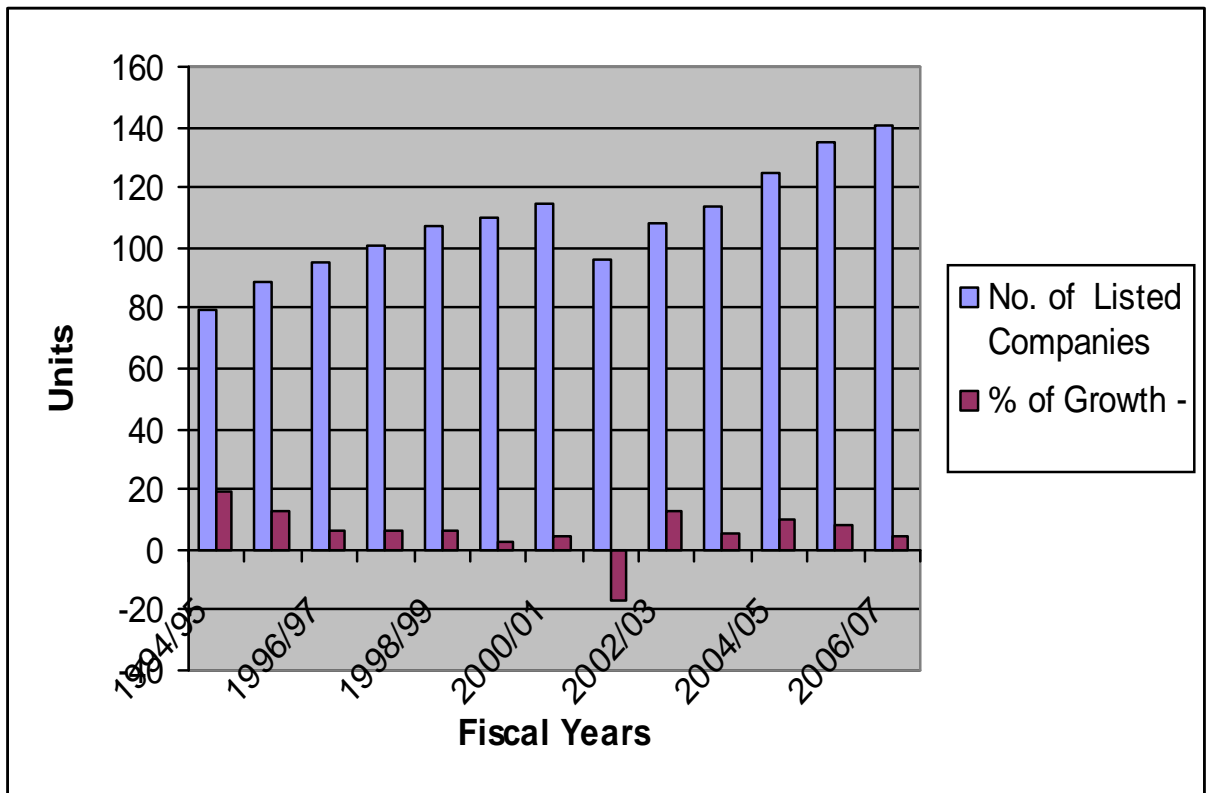
Table No. 4.8
Stock Market Indicator

Fiscal Year	No. of Listed Companies	% of Growth	No. of Traded Company	% of Growth	No. of Share Traded '000'	% of Growth
1993/94	66	-	38	-	993	-
1994/95	79	19.70	53	39.47	3901	292.85
1995/96	89	12.66	59	11.32	2954	-24.28
1996/97	95	6.74	67	13.56	9443	219.67
1997/98	101	6.32	68	1.49	1195	-87.35
1998/99	107	5.94	69	1.47	4857	306.44
1999/00	110	2.80	69	0	7674	58
2000/01	115	4.55	67	-2.90	4989	-34.99
2001/02	96	-16.52	69	3.00	6005	20.36
2002/03	108	12.5	80	15.94	2428	-59.57
2003/04	114	5.56	92	15	6468	166.39
2004/05	125	9.64	102	10.86	18433	184.98
2005/06	135	8.00	110	7.54	12221	-33.70
2006/07	141	4.25	116	5.45	18147	48.49

Source: Annual Report, SEBO 2006/07

Figure No. 4.9

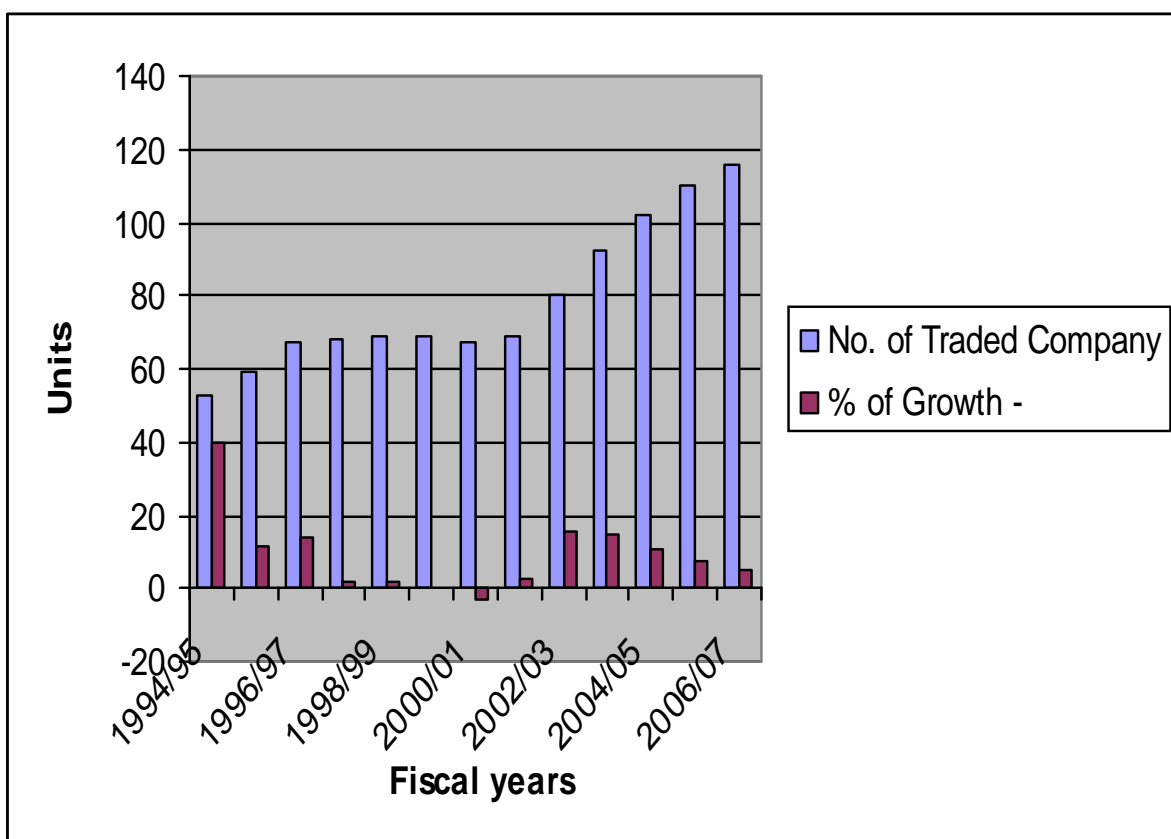
Number of Listed Companies in NEPSE & % of Growth



The number of listed companies was 66 in the base year 1993/94, 135 in 2003/04 and 141 in 2006/07. The growth rate of listed companies is positive in all these years except in the year 2001/02 with the negative growth rate of 16.52. In that year NEPSE de-listed some companies from its list because of non-disclosure of necessary information correctly and timely. The growth rate was highest in 1994/95 with 19.70 percent and lowest in 2001/02 with -16.52 percent.

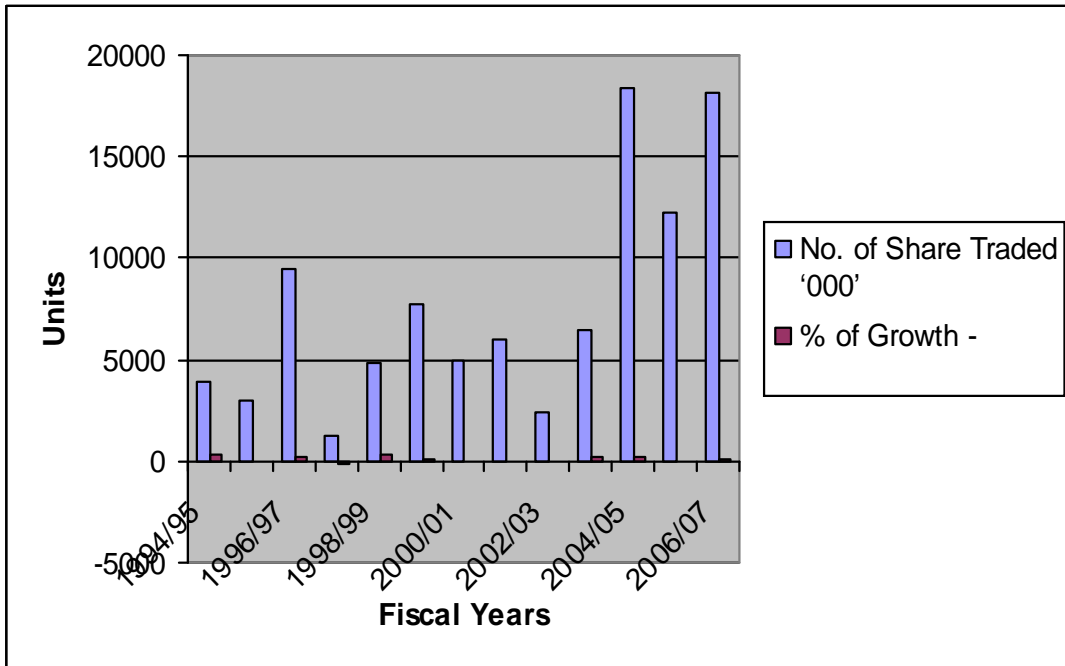
Figure No. 4.10

Number of Traded Company & its % growth Rate



The number of traded companies was 38 in the base year 1993/94 and, 110 and 116 in the year 2005/06 and 2006/07 respectively. Only 38 companies were traded in the trading floor and it rose up to 63 in the year 1998/1999 and 1999/2000. The number decreased to 67 in the year 2000/01 with the negative growth rate of -2.90 percent. However, the no. of trading companies is increasing after the year 2000/01, Then Continue to increase under the Study Period.

Figure No. 4.11
No. of Share traded & it's % of Growth



number of shares traded in different years, we conclude that it is very much fluctuating. The impact on growth rate is also affected. The number of shares traded in the year 1993/94 was only 993000 whereas it was 3901000 in the year 1994/95 with the growth rate of 292.85 percent. Again, in the year 1995/96 it was declined and came to 2954000 with the negative growth rate of 24.28 percent. This negative trend of growth rate was continued in the year 1997/98, 2000/01 and 2002/03 with -87.35, -34.99 and -59.57 respectively. But in the year 2003/04 the growth rate was significantly increased and became 166.39 percent with the shares traded 6468000 as compared to the preceding year of 2428000. then also decrease the fiscal year 2005/06 by 33.70% but it's recover in fiscal year 2006/07.

4.2.6 Number of Transaction and Listed Securities in NEPSE:

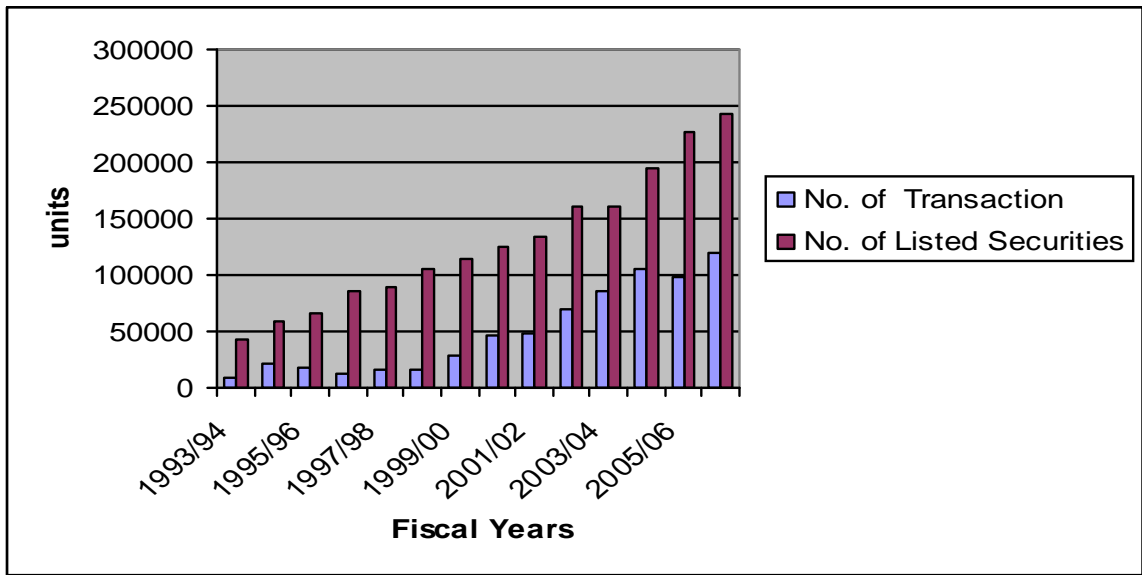
Table No. 4.9

Number of Transaction and Listed Securities in NEPSE

Fiscal Year	No. of Transaction	% of Growth	No. of Listed Securities	% of Growth
1993/94	9357	-	43424	-
1994/95	21472	129.48	58247	34.14
1995/96	17943	-16.44	65880	13.10
1996/97	12428	-30.74	85193	29.32
1997/98	15483	24.58	90107	5.77
1998/99	15814	2.14	105632	17.23
1999/00	29136	84.24	114057	7.98
2000/01	46095	58.21	124971	9.57
2001/02	48028	4.19	134150	7.34
2002/03	69163	44	159958	19.24
2003/04	85533	23.67	161141	0.74
2004/05	106246	24.21	194673	87.91
2005/06	97374	-8.35	226540	16.36
2006/07	120510	23.75	243504	6.96

Source: Annual Report, SEBO 2006/07/ NEPSE, Summary Sheet of Transaction 2006/07

Figure No. 4.12
Number of Transaction and Listed Securities in NEPSE



Number of transactions is very much varied comparing with different years. In the year, 1993/94 the number of transaction was 9357 while in 1994/95 it rose up by 129.48 percent with transaction of 21472. There was a negative growth rate in transaction in the year 1995/96 by 16.44 percent and it was continued by -30.74 percent in the year 1996/97. The significant growth rate can be traced in the year 1999/00 by 84.24 percent as compared to the growth rate of 2.14 of 1998/99. The negative growth rate in number of transactions in 2005/06 was by -8.35 percent as compared to the growth rate of 24.21 percent of 2004/05. The growth rate in 2006/07 was by 23.75 percent with 120510 No. of transactions.

The present system is that the securities issued to the public should be listed in stock exchange within 45 days after the allotment date. The growth rates of number of listed securities are all positive with lowest in the year 1993/94 and highest in the year 2006/07 and the numbers are 43424 and 243504 respectively. The highest growth rate is in the year 2004/05 by 87.91 percent with 194673 numbers of listed securities and the lowest growth rate is 0.74 percent with 161141 numbers of listed securities in the year 2003/04.

4.2.7 Market Day per Year and Daily Turnover:

Table No. 4.10

Market Day per Year and Percentage Growth Rate

Fiscal Year	Market Day Per Year	% of Growth
1993/94	121	-
1994/95	242	100
1995/96	240	-0.83
1996/97	239	-0.42
1997/98	237	-0.84
1998/99	231	-2.53
1999/00	240	3.9
2000/01	231	-3.75
2001/02	246	6.50
2002/03	238	-3.25
2003/04	243	2.10
2004/05	236	2.88
2005/06	228	3.38
2006/07	232	1.75

Source: Annual Report, SEBO

Figure No. 4.13
Market Day per Year and Percentage of Growth Rate

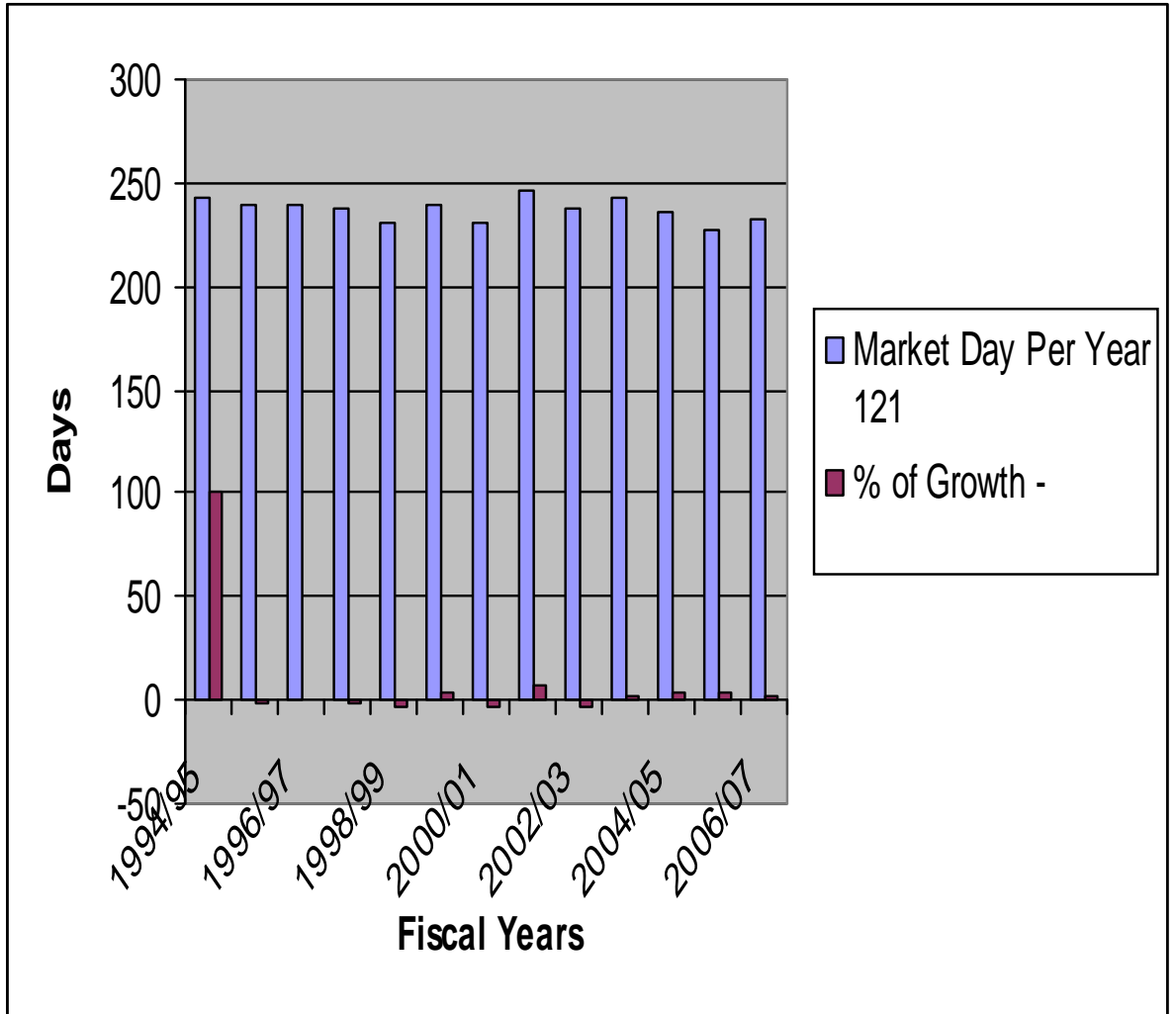


Table No. 4.11 and Figure No 4.13 represents that the highest turnover day was 246 days in 2001/02 and the lowest turnover year was 121 in fiscal year 1993/94. according to above figure market day per year percentage of growth rate is increasing and decreasing condition.

4.2.8 Market Turnover in Volume and Value:

Table No. 4.11
Annual Market Turnover in Volume and Value

Fiscal Year	Annual Turnover in Volume (00000)	Annual Turnover in Value (Rs. in million)
1993/94	9.93	441.60
1994/95	39.00	1054.30
1995/96	29.47	215.60
1996/97	91.43	416.20
1997/98	11.95	202.60
1998/99	47.88	1500.00
1999/2000	76.74	1157.00
2000/01	49.87	2344.20
2001/02	57.91	1540.60
2002/03	24.28	575.99
2003/04	64.68	2144.27
2004/05	184.33	4507.68
2005/06	122.21	3451.43
2006/07	181.47	8630.1

Source: Annual Report, SEBO 2006/07

Figure No. 4.13
Annual Market Turnover in Volume and Value

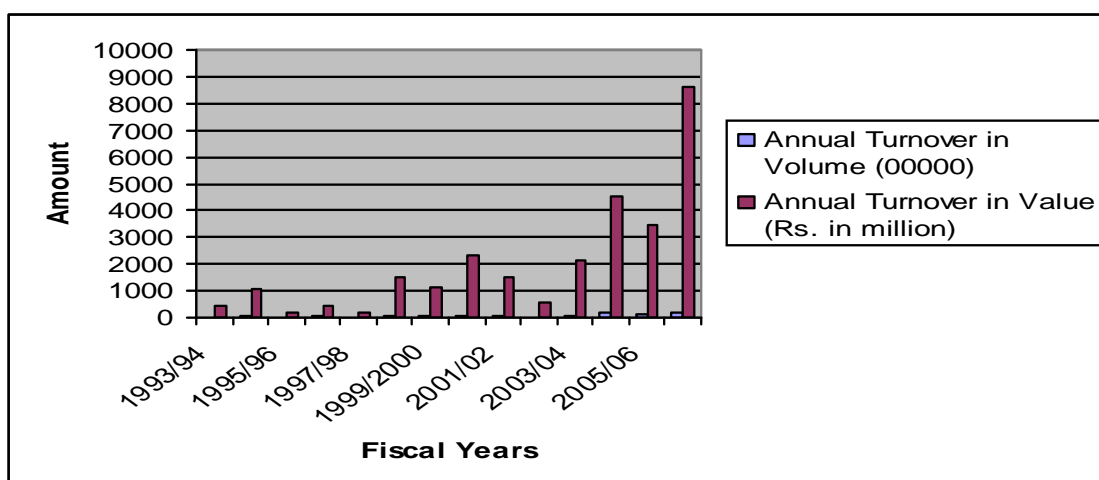


Table No. 4.12 and figure No. 4.12 Shows that the highest Annual Market Turnover value was Rs 8630.1 million in the fiscal year 2006/07 and lowest was Rs 202.60 million in fiscal year 1997/98. But the volume of Market Turnover was highest in the year 2004/05 and lowest in the year 1993/94.

4.2.9 NEPSE Index:

Market indexes are used to determine the relationship between historical price movements and economic variables and to determine the systematic risk for individual securities and portfolios.

The index is taken as a measuring tool whether the performance of stock market is good or not. This clearly focuses on the price of stocks that is increasing or decreasing in the market. Because the prices of stocks go up and down in a particular period compared to the previous period as disclosed by index. The highest index suggests the increase in market price of the stocks and implies the better performance of companies and vice-versa. Thus the NEPSE index shows the behaviour of stock prices in the capital market.

The computation formula for price index is as follows:

$$\text{Each day's index} = \frac{\text{Each day's total market value}}{\text{Base day's total market value}} \times 100$$

$$P_{01} = \frac{\sum P_1 \times Q_1}{\sum P_0 \times Q_0} \times 100$$

Where,

$$P_0 = \text{Base Market Price}$$

P_{01} = NEPSE Price Index

P_1 = Today's Stock Price

Q_1 = Listed Shares (i.e. no. of Shares outstanding)

Q_0 = Base Listed Shares.

Table No. 4.12

Year	NEPSE Index	% Change in Index
1993/94	226.03	-
1994/95	195.48	-13.52
1995/96	185.61	-5.05
1996/97	176.31	-5.01
1997/98	163.35	-7.35
1998/99	216.92	32.79
1999/00	360.70	66.28
2000/01	348.43	-3.40
2001/02	227.54	-34.70
2002/03	204.86	-9.97
2003/04	222.04	8.39
2004/05	286.67	29.10
2005/06	386.83	34.93
2006/07	683.95	76.80

Source: Trading Report NEPSE, 2006/07

Figure No. 4.14

NEPSE Index (Fiscal year 1993/094 to 2006/07)

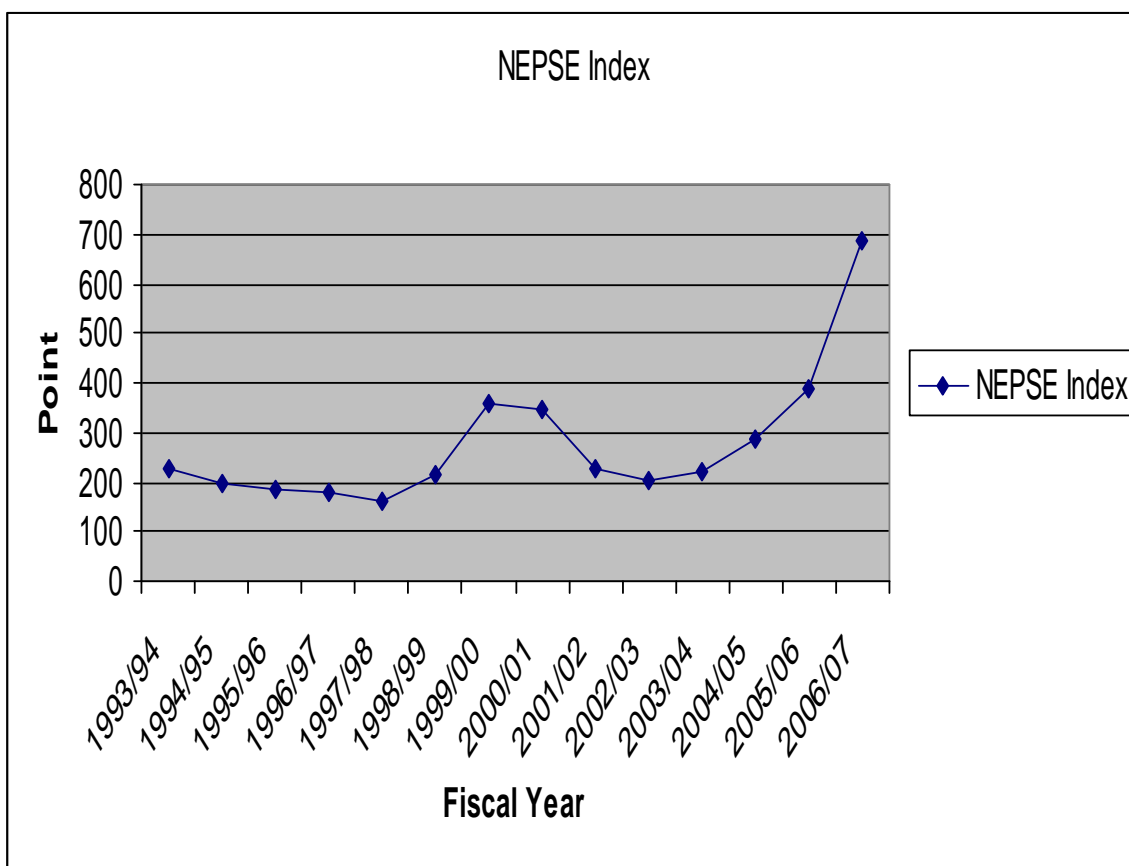


Table No. 4.12 and Figure No. 4.14 represents that the NEPSE Index is fluctuating trend before fiscal year 2003/04, But after that fiscal year NEPSE Index is increasing trend over the study period. The NEPSE index was highest in the fiscal year 2006/07 with 683.95 and it was lowest in the year 1997/98 by 163.35 points. The NEPSE index for this fiscal year 2006/07 is 683.95 which is somewhat high than 386.83 of the previous year 2005/06.

4.2.10 Market Capitalization Vs Nominal GDP:

Table 4.13

Fiscal Year	Market Capitalization (Rs. in Million)	GDP (Rs. in Million)	% Increased in Capitalization on Nominal GDP
1993/94	13872	191596	7.24
1994/95	12963	209974	6.17
1995/96	12295	239388	5.14
1996/97	12698	269570	4.71
1997/98	14289	289798	4.93
1998/99	23508	329960	7.12
1999/00	43123	365465	11.77
2000/01	46349	392532	11.78
2001/02	34703	405632	8.56
2002/03	35240	435531	8.09
2003/04	41424	472424	8.77
2004/05	61365	548484	11.18
2005/06	96813	603672	16.03
2006/07	186301	670588	27.78

Source: Annual Report, SEBO 2006 /07 Trading Report, NEPSE 2006/07.

The highest percentage of market capitalization on nominal GDP was 27.78 percent in the year 2006/07. Likewise the lowest was 4.71 in 1996/97. The contribution of market capitalization on GDP for the year 2003/04, 2004/05, 2005/06 and 2006/07 is 8.77, 11.18, 16.03, and 27.78 respectively.

4.3 Presentation and Analysis of Primary Data

The questionnaire survey method is used to analyse the “problems and prospects of stock market growth in Nepal.” Samples are taken from different sectors such as investors, offices of SEBO & NEPSE, Share brokers, students. The results are analysed carefully so that it could lead to real problems and prospects of stock market in Nepal

Questionnaire survey

1. Analysis of the problem faced by stock market

Table 4.14

S. N.	Problems	No of respondent	% of respondent
A	Shortcomings of rules and regulations	6	12
B	Lack of sufficient knowledge among investors	16	32
C	Lack of sufficient knowledge among stock market intermediaries	14	28
D	Lack of proper coordination between authoritative body	4	8
E	Restriction to foreign investors	8	16
F	All of the above	2	4
	Total	50	100

Source: Field Survey

Regarding this question, almost the same percentage of respondents agrees about the lack of sufficient knowledge among investors and stock market intermediaries. Actually Nepalese investors as well as stock market intermediaries do not have sufficient knowledge about the stock market.

2. Analysis of information provided by NEPSE and SEBO correctly and timely

Table 4.15

S. N.	Variables	No. of respondent	% of respondent
A	Yes	6	12
B	No	40	80
C	Do not know	4	8
	Total	50	100

Source: Field Survey

Regarding this question, 80 percent of the respondents are of the view that the information provided by NEPSE and SEBO are not correct and timely.

3. Analysis of the performance of Nepal Stock Exchange

Table 4.16

S. N.	Variables	No. of respondent	% of respondent
A	Yes	22	44
B	No	18	36
C	Do not know	10	20
	Total	50	100

Source: Field

Survey

Regarding this question, more than 40 percent (44) are satisfied about the performance of Nepal Stock Exchange. 36 percent are not satisfied and 20 percent do not know about the performance. In fact, despite of many rise and fall the work of NEPSE is satisfactory.

4. Analysis of the growth trend of Nepalese Stock Market

Table 4.17

S. N.	Variables	No. of respondent	% of respondent
A	Good	18	36
B	Bad	28	56
C	Do not know	4	8
	Total	50	100

Source: Field

Survey

Regarding this question, 36 percent agree the growth trend of Nepalese Stock Market is good, 56 percent feels it bad and other 8 percent are unknown about it. If I were put forward my opinion about growth trend of stock market, I am to some extent satisfied with the growth trend of Nepalese Stock Market.

4. Analysis of Motivating factors for investment

Responses about factors which motivate investment

Table 4.18

S. N.	Variables	No. of respondent	% of respondent
1	Marketability & Profitability	22	44
2	Limited opportunity to invest in other sector	8	16
3	Friends and Family	14	28
4	Share brokers consultation	4	8
5	If other, please specify	2	4
	Total	50	100

Source: Field

Survey

Regarding this question, 44 percent of the respondents invest in stock because of marketability and profitability, 28 percent invest with consultations from family and friends, 16 percent are of the view that they see limited opportunities of investment, 8 percent consult brokers and 4 percent say that they act on a whim of the market, political legal environment. We can clearly observe that Nepalese investors are more profit concerned, and a large number also invest taking suggestions with friends and family. We may conclude that a scenario for tendency of observation and analysis has been developed quite among Nepalese investors.

5. Analysis of Share Purchase decision

Response to share purchase decision

Table 4.19

S. N.	Variables	No. of respondent	% of respondent
1	Increasing Market price of the	20	40

	share		
2	Profit/Losstrend of the Company	18	36
3	Act of whim	8	16
4	Broker's consultation	3	6
5	If others, please specify	1	2
	Total	50	100

Source: Field

Survey

Answer to this question, about 40 percent purchase the share observing the trend of market price, other 36 percent observe Profit/Loss situation of the company, 16 percent act on the whim of market, 6 percent consults brokers and rest 2 percent analyze management team.

6. Analysis of disclosure requirements

Response to weakness of Players

Table 4.20

S. N.	Variables	No. of respondent	% of respondent
1	The office of the company registrar	25	50
2	Security Board Nepal (SEBO/N)	15	30
3	Nepal Stock Exchange (NEPSE)	5	10
4	Investors/ Brokers	2	4

5	Particular company	3	6
	Total	50	100

Source: Field

Survey

In response to this question, 50 percent of the respondents are of the opinion that company registrar office is responsible for not presenting the financial statement of particular company to SEBO and NEPSE. 30 percent blame it to SEBO, 10 percent to NEPSE and other 4 and 6 percent to Investors/Brokers and to the particular company respectively.

7. Analysis of interrelationship between Stock Market and Economy

Response to relationship between stock market

Table 4.21

S. N.	Variables	No. of respondent	% of respondent
1	High	30	60
2	Moderate	15	30
3	Low	5	10
	Total	50	100

Source: Field Survey

Regarding this question, 60 percent agree towards high relationship between stock market and economy, 15 percent say it moderate and other 10 percent rank it low correlated. Undoubtedly, we can say that stock market and economy is positively correlated i.e. highly related to each other.

8. Analysis of performance of stock market for the development of the economy

Response to performance of stock market for development of economy

Table 4.22

S.N.	Variables	No. of respondent	% of respondent
1	Yes	25	50
2	No	20	40
3	Do not know	5	10
	Total	50	100

Source: Field

Survey

In response to this question, 50 percent are satisfied with the performance of stock market, 40 are not and other 10 percent do not know about it.

9. Analysis of risky investment

Response of risk for investment

Table 4.23

S. N.	Variables	No. of respondent	% of respondent
A	Buying the share when first issued	12	24
B	Buying the share in secondary market	8	16
C	Both of them	30	60
D	None of them	-	-
	Total	50	100

Survey

Regarding this question, 60 percent feel both investments mentioned above in 1. and 2. are risky, 16 percent feel investment through buying from secondary market is risky, while the other 24 percent feel investment in primary issue is more risky. As an analyst, I feel both of them are risky as it is said profit is the consideration for risk.

10. Analysis of time to sell the share.

Response of time to sell the share

Table 4.24

S. N.	Variables	No. of respondent	% of respondent
A	When company's profit declines	15	30
B	When company fails to pay dividend	13	26
C	When market price of the share starts declines	12	24
D	When cash is needed	8	16
E	If other, please specify	2	4

	Total	50	100
--	-------	----	-----

Source: Field

Survey

Regarding to this questions, 30 percent sell their share when company's profit declines, 26 percent sell their share when it fails to pay dividend, 24 percent sell it when market price of the share starts declining, 16 percent sell it when cash is needed and other 4 percent sell it to maintain portfolio investment.

11. Analysis of the points that provide prospects to Nepalese stock market growth

Responses in prospect of stock market growth

Table 4.25

S. N.	Variables	No. of respondent	% of respondent
A	Stock market provides max returns	10	20
B	Limited opportunities for investment	8	16
C	Liquidity & Marketability of securities	12	24
D	Increasing concerns of generals and academicians in stock market	8	16
E	All of the above	12	24
	Total	50	100

Source: Field Survey

Regarding to the question, the highest 24 percent agree on liquidity & marketability in the prospect of stock market development, while the other 24 percent agree that all the points are equally important. Other 20 percent, 16 percents are divided into maximum returns, limited opportunities and growing concerns in this sector.

12. Experience about the problems in NEPSE

One question was asked to respondents to share the view regarding the problems of stock market in Nepal. 4 respondents have given many suggestions answering their views out of the 50 respondents. They are presented below:

- (1) The operation of NEPSE is not transparent.
- (2) There is not efficient information system and much delay in providing company's financial status.
- (3) Brokers do not provide proper advice and suggestions to the clients.
- (4) Brokers are commission oriented and have very little knowledge about stock market mechanism.
- (5) The stock market is trading with open out-cry system even in these computerized business days.
- (6) The process of transferring of ownership of shares is lousy and time consuming.

They provide many suggestions to solve these problems.

1. The securities board should monitor and regulate stock market by following strict controlling mechanism and appropriate penalty system. It should withdraw traditional operation by introducing modern International standards of trading.
2. The stock exchange should carry out periodic research and analysis and findings should be made public.

3. The open-out-cry system of trading should be replaced by e-trading mechanism.
4. Laws governing the stock market should be more liberal but strict to maintain stock market discipline.
5. Investors should be provided with investment guidelines.
6. The role of market player in the stock market should be made more effective.

4.4 Major findings of the study

The major findings of the study from the analysis of primary and secondary data are as follows:

1. It was found that the stock market in Nepal is in developing stage, however, majorities of the respondents are not fully satisfied with the growth trend of the market.
2. The major portions of Nepalese investors do not have sufficient knowledge about investment.
3. Majority of respondents are not satisfied with the performance of stock market for the development of the economy.
4. NEPSE and SEBO do not provide information accurate and timely. They further added that information provided is not sufficient.
5. Marketability and profitability are the major motivating factors of investment for investors. Majority of them make share purchasing decision without analysing the financial performance of the company and without consulting the experts.
6. Most of the respondents feel the company registrar's office should play vital role in providing the financial statement of particular company to SEBO and NEPSE. They further added that the government should play the important role to increase investment in stock.
7. Among the listed companies during the year 2006/07, majority are from the finance companies which is 39 % of the whole.
8. The numbers of listed securities are increasing gradually whereas the numbers of transactions in NEPSE are in fluctuating manner.

9. Growth of market day per year, average turnover in volume and value are in satisfactory level.
10. Paid-up value is increased by 8.94 percent in fiscal year 2006/07 and paid up capital is 38.35 percent increase in this fiscal year.
11. The highest increase in market capitalization rate was 92.43 percent in fiscal year 2006/07. Banking sector covered most of the market capitalization in NEPSE.
12. NEPSE index continuously declined from the year 1993/94 till 1997/98. It was highest in the year 1999/00 by 360.70 points. Because of weak law and order situation, industrial service and trading sector cannot perform well. But after fiscal year 2003/04 NEPSE index increasing trend to reach 683.95 points in fiscal year 2006/07.
13. Percent of market capitalization on nominal GDP is positive in all the years and is maximum in year 2006/07 with nearly 28 percent.
14. There are many problems by which stock market is suffering but the prospect of it is also equally strong.

CHAPTER –V

SUMMARY, CONCLUSION AND RECOMMENDATION

5.1 Summary

As stated earlier, the process of stock market development in the country actually started in 1976 when the government established Securities Exchange Centre to provide and develop market for securities, both the government bond and corporate securities. In 1993, Securities Board Nepal was established with the objectives to regulate, supervise and monitor the securities market. Similarly, the Securities Exchange Centre was converted into Nepal Stock Exchange Limited (NEPSE) with the objectives to provide secondary market for securities transaction. NEPSE, now, is adopting an open out-cry system, where the investors were allowed to deal in securities out through licensed brokers.

The equity market activities grow with the development and reform in the financial sector. Over the past 15 years the stock market of Nepal has made some progress. For example, between the fiscal year 1993/94 and 2006/07, the number of listed companies in NEPSE increased almost two-fold from 62 to 141 and the market capitalization value rose almost thirteen times from Rs. 13872 million to Rs. 186301 million. Likewise, during the same period the number of annual transactions increased more than ten times from around 12 thousands to 120 thousands. During this period NEPSE index jumped from its base value of 100 to 683.0

The paid-up value at the beginning of the fiscal year 1993/94 was Rs. 2182 million as compared to the paid-up value of Rs. 21798 million of the fiscal year 2006/07. But annual turnover has lot of fluctuations during this period. Average daily turnover and market day per year in 2006/07 are also in satisfactory level.

Despite the large volumes traded on stock exchanges many listed stocks trade infrequently; or their balance of trading is not sound. For example, in NEPSE mostly the commercial banks shares are transacted. The reason behind this might be traditionally guided investors return principle where most earnings of investors have been in the form of divided rather than capital gains. Though regular and high dividends are provided only by commercial banks in past day, it becomes the only potential investment destination comparing to the other stock market participants. Therefore, the serious problem facing by Nepali Stock market is among various sectors only the banking sector is doing well in terms of liquidity, but other sectors rarely do so.

Unfortunately, in Nepal, despite a history of about half a decade of planned economic activities to develop real sector of the country, little attention was paid to the development of financial sector. Over the past one and half decade, financial sector, despite many problems has developed significantly in Nepal. However, most of the developments were confined to the banking sector stock market has virtually remained stalled because of the low priority in the government's financial reform policies.

Various measures of stock market development indicate that the stock market in Nepal is underdeveloped and has failed to show impact on the overall national economy. Small market size has made it vulnerable to manipulation and price rigging. Low turnover rates and value-traded-rate to volatility, and high concentration ratio indicate that the stock market in Nepal is highly illiquid and risky. Investors tend to avoid stock market because they do not have options to invest in securities according to the risk-return preference. Similarly firms shun it because stock market is less reliable source of raising funds for them. Due to this financial system in Nepal has remained basically bank-dominated.

5.2 Conclusions

The development of stock market in Nepal so far cannot be considered satisfactory. This is evident from the facts and figure available in the stock market performance during the last 15 years. The diverse sector is coming up that need capital. The only requirement to fulfil the objectives of both parties is to create a conducive atmosphere where investors can avail the required capital from the market at low cost.

The dynamism of the stock market has been greatly reduced by the domination of the long-term shareholders, who prefer holding the shares with the hope of increasing their wealth. This can be justified by small number of shares that are traded on the stock market. Even though this reduces the dynamism of the stock market the investors have very few rather no alternative to holding shares.

There is almost no liquidity in the stock market for shares except that of banking and some finance and insurance sectors. Although, it has become late to take steps to overcome such problems of the Nepalese stock market in order to make it active and supportive, the stock market has a good prospect for the resource mobilization to finance the productive enterprises in the Nepalese economy.

Despite the increase in the number of companies and paid-up value of the securities listed with the exchange, Most of the companies that are listed with the exchange belong to banking, finance, and insurance sectors. While only few companies from the trading, hotel, manufacturing, and aviation sectors are listed with the exchange, not a single company from powers information technology and construction sectors has entered the organized stock exchange of the country. This indicates that firms tend to avoid stock market as an alternative source of long-term capital in Nepal. Significant increase in the number of companies registered as private limited during the last one and half decade also supports this view. This has adversely affected the liquidity and supply of securities in the stock market.

All Brokers agreed that there should be right code of conduct and monitoring for brokers operations. It was observed that the prescribed code of conduct is hardly enforced.

In the context of primary share issue, there should be strict time frame for allotment of share, refund of money, distribution of share certificate and history of shares. There should be strict punishment if the prospectus is misleading and investors are affected by misleading prospectus.

The brokers do not have problem with each other in share transaction and settlement. But they have experienced conflicts in buying and selling of shares, mostly in signature verifications, and cash payment. Investors do not pay when prices fall and do not accept share price when prices rise. Shouting system is not effective because sometimes the board marker (person who writes in the board placed on the wall) may not listen to the first broker's quote and writes another broker's number in the board. It creates conflicts in the floor.

Majority of brokers agree that certain requirement like minimum qualifications and experiences should be met. Some added the brokers should be allowed to operate according to volume of transaction.

Investor's confidence in Nepalese stock market is relatively low because of stock market volatility, low return in investment, inadequate information, lack of financial market instruments and investors not knowing about the risk of the stock market investment. The size of the market in terms of market capitalization and number of issue is relatively small. Market for corporate debt instrument is undeveloped. The retailers also dominate present stock market in the absence of foreign investors and local institutional investors. Only a small portion of shares is actively traded while others are traded either in small number or infrequently which leads to poor liquidity and small turnover in the market.

Transparency and openness of transaction, quality professional services, adequate corporate financial disclosures and improved legal and supervisory framework are the urgent needs of Nepalese stock market.

5.3 Recommendations

- ☞ The government should make policies only but not properly implement it.
- ☞ Securities Board Nepal (SEBO/N) should regulate NEPSE and other financial institutions adequately, appropriately and effectively.
- ☞ The Securities Board in co-ordination with the Ministry of Finance and NEPSE should develop research, public awareness and investor education programmes.
- ☞ Tax system should be reformed. It should encourage and stimulate capital formation.
- ☞ Manipulative practices like wash sales and churning should be strictly controlled.
- ☞ Investment in corporate sector should be encouraged.
- ☞ The listed firms whose shares are not traded should provide the financial status publicly in order to make the investors aware about their exact financial condition.
- ☞ The government should make appropriate policies and programs for the enhancement of the entrepreneurship development in the Nepalese economy.
- ☞ Large and ineffective government corporations should be privatized in order to develop the Nepalese stock market through the wide spread distribution of shares to public investors.

- ☞ The government should allow foreign investors to invest in Nepalese Capital Market.
- ☞ The procedure for offering public issue should be simplified and rationalized.
- ☞ The information and financial statements of the companies should be disseminated properly and timely.
- ☞ Different market intermediaries should be educated, trained and professionalized.

Besides it the most needed changes which are fundamental for stock market development are listed below:

- ⇒ The electronic system of trading.
- ⇒ The automation in the clearance system.
- ⇒ The de-mat system of securities.
- ⇒ The mutual saving schemes should be enhanced.
- ⇒ Stock Exchange should be privatized.

Besides these other factors which have slowed the stock market growth should be adjusted and improved. They are:

- ⇒ Unfavourable macroeconomic conditions.
 - ⇒ Political instability.
 - ⇒ Low investors confidence.
 - ⇒ Weak tax system.
 - ⇒ Slow privatization process.
- ☞ NEPSE is still following the old and outdated open out-cry system of trading. Such a system is neither efficient nor scientific. The online trading system or an advanced electronic system of trading should be introduced without any further delay.

THE END

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APPENDIX – I

Dear Sir/Madam,

I am preparing my research work on the topic “Behaviour of Securities market in Nepal.” for the partial fulfilment of the requirement for the degree of Master in Business Study. The questionnaire given below will be very helpful to collect primary data in respect of my research work. Therefore, I would like to request for your grateful opinions and correct information’s regarding these questions.

I hope forward for your kind cooperation.

Respondent	Researcher
Name: -----	Pramod Khanal
Education: ----- Campus	Lumbani Banijaya
Occupation: -----	T.U. Regd. No.
Position: -----	M.B.S
Date: -----	

Questions

1. Which of the following problem that the Nepalese stock market has been suffering from?
 - (a) Shortcomings of rules and regulations. []
 - (b) Lack of sufficient knowledge among investors. []
 - (c) Lack of sufficient knowledge among stock market intermediaries. []
 - (d) Lack of proper coordination between authoritative bodies. []
 - (e) Restriction to foreign investors. []
 - (f) All of the above. []

2. Do you think Nepal Stock Exchange and Security Board Nepal (NEPSE & SEBO) provides information correctly and timely?
 - (a) Yes []
 - (b) No []
 - (c) Do not Know []

3. Are you satisfied with the performance of Nepal Stock Exchange?
 - (a) Yes []
 - (b) No []
 - (c) Do not Know []

4. What do you think about the growth trend of Nepalese Stock Market?
 - (a) Good []
 - (b) Bad []
 - (c) Do not Know []

5. What factor motivates you to make investment in stock?
 - (a) Marketability and profitability. []
 - (b) Limited Opportunity to invest in other sector. []
 - (c) Friends and Family. []
 - (d) Share Brokers. []
 - (e) If other, please specify. []

6. Which of the following factor makes you decide to buy share of particular company?
 - (a) Increasing Market Price of the share. []
 - (b) Profit/Loss trend of the company. []
 - (c) Act of whim. []
 - (d) Brokers, consultation. []
 - (e) If other, please specify. []

7. Listed companies do not present financial statement in time to NEPSE & SEBO who is responsible for this?
 - (a) The office of the company registrar. []

- (b) Security Board Nepal (SEBO/N) []
 - (c) Nepal Stock Exchange (NEPSE) []
 - (d) Investors/Brokers. []
 - (e) Particular Company. []
8. To what extent Nepalese Stock Market and Nepalese economy are interrelated?
- (a) High []
 - (b) Moderate []
 - (c) Low []
9. Are you satisfied with the performance of stock market for the development of the economy?
- (a) Yes []
 - (b) No []
 - (c) Do not Know []
10. Which is risky to invest?
- (a) Buying the share when first issued. []
 - (b) Buying the share in secondary market. []
 - (c) Both of them. []
 - (d) None of them. []
11. When would you like to sell your share in secondary market?
- (a) When company's profit decline. []
 - (b) When company fails to pay dividend. []
 - (c) When Market Price of the share starts declining. []
 - (d) When cash is needed. []
 - (e) If other, Please Specify []
12. Which of the following is more relevant in the prospect of Nepalese Stock Market growth?
- (a) Stock market provides maximum return. []
 - (b) Limited opportunities of investment other than in stock. []

- (c) Liquidity and Marketability of securities. []
- (d) Increasing concerns of academicians and general public in stock market. []
- (e) All of the above. []

13. Express your views for the development of Nepalese Stock Market?

Problems:

Solutions:

Thank you, for your co-operation.

APPENDIX - II

List of Respondents

S. No.	Respondent Type	No. of Respondent	% of Respondent
1	Offices of SEBO	5	10 %
2	Offices of NEPSE	5	10 %
3	Listed Securities Brokers	4	8 %
4	General Investors	26	52 %
5	Lecturer of T.U.	4	8 %
6	University Students	6	12 %
	Total	50	100

BIO-DATA

NAME : **PRAMOD KHANAL**
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LANGUAGE : **HINDI, NEPALI, ENGLISH**